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Handbook of OPEC and the Global Energy Order

Past, Present and Future Challenges

Edited by Dag Harald Claes and Giuliano Garavini



Handbook of OPEC and the Global Energy Order

The Organization of the Petroleum Exporting Countries (OPEC), celebrating its 60th anniversary in 2020, is one of the most recognizable acronyms in international politics. The organization has undergone decades of changing importance, from political irrelevance to the spotlight of world attention and back; and from economic boom for its members to deep political and financial crisis.

This handbook, with chapters provided by scholars and analysts from different backgrounds and specializations, discusses and analyzes the history and development of OPEC, its global importance, and the role it has played, and still plays, in the global energy market. Part I focuses on the relationship between OPEC and its member states. Part II examines the relationship between OPEC and its customers, the consuming countries and their governments, while Part III addresses the relationship between OPEC and its competitors and potential partners, the non-OPEC producers, and the international oil companies. The final section, Part IV, looks at OPEC and the governance of international energy.

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Preface

The chapters of this book derive from a conference, ‘OPEC and the Global Energy Order’, held at New York University / Abu Dhabi (NYUAD) in 2017. The idea of the conference was to bring together scholars and analysts from different backgrounds and specializations to discuss the importance of the organization and the role it has played, and still plays, in the global energy market. The three-day conference had about fifty participants, with thirty presentations. Most of the presentations have materialized as chapters in this book. In addition, we have invited other authors to join this collection of analyses of the many various aspects of one of the most prominent organizations in world economic and political relations. Unfortunately, the recordings of the very interesting final roundtable of the conference have been lost so we were unable to include a summary of that conversation in the book.

We have organized the chapters in this book primarily according to the various relations that influence the role and working of OPEC. The first section focuses on the relationship between OPEC and its member states. Then follows a section on the relationship between OPEC and its customers, the consuming countries and their governments. The third section addresses the relationship between OPEC and its competitors and potential partners, the non-OPEC producers, and the International Oil Companies. We find that the global energy order, at least in the oil sector, is constituted by the changing patterns in these relationships. However, we have a final section addressing the various more overarching historical and contemporary aspects of this order.

We would like to acknowledge the generous financial support we have received from the NYUAD Institute and the NYUAD Research Fellowships in the Humanities program as well as from the co-sponsor of both the conference in 2017 and the publication of this book, the University of Oslo, with its strategic research facility: UiO:Energy. In addition to the necessary financial support, the head of NYUAD Fellowships in the Humanities, Reindert Falkenburg, and the head of UiO:Energy, Vebjorn Bakken, have provided moral support enabling us to bring this project over the finish line.

The staff at Routledge have provided all necessary support to bring the pages you have in your hand from rough sketches to the final printable product. Our main contact and supporter has been our editor, Cathy Hartley, and her assistant, Lucy Pritchard. Many thanks to you both, for encouragement, support and grace, as the due date had to be extended yet another time. Gill Gairdner has meticulously copy-edited the entire manuscript, improving the text in both form and content. We are deeply grateful. Our two assistants, Solveig Bjorkholt and Giancarlo La Rocca, have both made a tremendous effort in bringing 28 chapters into coherence. A good research assistant is hard to come by; we were lucky enough to have two.

On a somewhat more personal note, although the two editors have different scholarly background, our disciplinary differences never caused any conflict or disagreement. The book covers OPEC both ‘then and now’. On the surface, the past seems more glorious than the present, not to mention the future. However, this book shows that OPEC still has a role to play for many years to come. OPEC is still too important to be left only in the hands of the historians.

OPEC and the global energy order

Past, present and future challenges

Dag Harald Claes and Giuliano Garavini

Myths about OPEC

OPEC has been considered both all-powerful and dead. During the ‘oil shocks’ of the 1970s OPEC was viewed as responsible for the decline of the West and the tensions in the Atlantic Alliance. OPEC was openly blamed for the oil embargo in October 1973 even though it was only partially responsible for the crude price increases of the 1970s and had nothing to do with the embargo itself. When the oil prices significantly increased once again in the 2000s, many considered these increases as a trigger for the economic and financial crisis of 2007/8. The British prime minister, Gordon Brown, told oil-exporting nations they had a responsibility to increase production to avoid ‘uncertainty and unpredictability for years ahead’.¹

On the other hand, the Vienna-based organization has been considered weak and ineffective when oil prices have fallen, as they did in the middle of the 1980s, during the so-called ‘counter-shock’ with crude oil trading from more than forty dollars a barrel in 1981 to less than ten dollars a barrel in 1986. Again, with the rapid decline in oil prices after 2014, when the organization decided to avoid production cuts and crude prices collapsed, numerous analysts, such as the head of commodities at Citigroup and former US deputy assistant of state for international energy policy Edward Morse, predicted the ‘end of the organization’ or its future irrelevance.²

A sticky myth concerning OPEC is that it is an Arab organization (see chapter 2 by Fuccaro). The embargo of 1973 is often referred to OPEC, even though OPEC never had a real role in it. The key role in the embargo was in fact played by the Organization of Arab Oil Exporting Countries (OAPEC, the A here is important), and by individual Arab oil exporters with the very notable exception of Iraq. The ensuing increase in oil prices in December 1973 (the two things are often conflated) was instead a policy chiefly advocated by the Shah of Iran and Iranian oil technocrats, and was motivated by the need to curb ‘overconsumption’ of oil by the industrialized countries as well as by the willingness of the ruling elites of petrostates to jumpstart the industrialization of their countries (Iran aimed at becoming the fifth most industrialized country in the world within a decade) (Garavini, 2019, pp. 2016–230). Taken together, the essays in this book clearly demonstrate that although Arab Gulf countries, with Saudi Arabia first among them, played and continue to play a key role, OPEC is a truly global organization, with a very diverse membership in terms of culture, language and geopolitical interests. The various member states are similar in their position as significant exporters of a key commodity and energy source (as collectors of an

international land rent), and in their crucial dependence on the income from these exports for both financing state budgets and vital imports. But there is a huge difference between OPEC countries with big production, huge reserves and a relatively small population, such as Saudi Arabia or Kuwait, and countries such as Nigeria (see chapter 7 by Olorunfemi) with smaller production and a huge population. During the Cold War there was contrast between the so-called ‘progressives’, such as Algeria (see chapter 5 by Malti) and Iraq, and ‘moderates’ such as Iran until the rule of the Shah (see chapter 4 by Atabaki), Saudi Arabia and other Gulf sheikdoms. Most of its members also changed their political outlook and oil policy over time, such as in the striking Venezuela (see chapter 6 by Rosales). These differences were often used against OPEC members by its enemies.

As petrostates became increasingly important, the pressure from outside grew, as is well manifested not only in media criticism and direct military interventions, as in the case of Iraq, but even, on one occasion, in direct attack when Carlos ‘The Jackal’ kidnapped OPEC delegates during an OPEC Conference in 1975 (see chapter 24 by Riegler). Not only do OPEC members have diverging interests but, as has been suggested, their role and policies within the organization have shifted very significantly. Venezuela – a founding member of OPEC and possibly the country that at the beginning pressed most strongly for a ‘global prorationing’ modelled on the experience of the Texas Railroad Commission in the United States (see chapter 21 by Wald) – eventually shifted in the early 1990s towards compromise with international oil companies, did not abide by the quotas assigned by OPEC and ‘overproduced’ by nearly one million barrels a day, coming very close to abandoning OPEC altogether. Saudi Arabia was at the forefront of the 1973 ‘oil embargo’ targeted against the United States and other key allies of Israel, defended OPEC and its quota system in the early 1980s, but eventually shifted its policy to one safeguarding its ‘market share’ both in the late 1985 and then again in 2014 (see chapter 3 by Al Moneef). These changes certainly reflect structural characteristics of each member such as population, productivity of the oil fields and geopolitics, but also point to the fact that internal ideological, political and social shifts affect the position and the willingness of petrostates to cooperate with one other and their ability to challenge consumers and international oil companies.

The petrostates’ organization has had many enemies. It has been declared dead numerous times by politicians, economists and industry leaders. Nobel prize winner Milton Friedman predicted the crisis of petrostates already when they were at the height of their power in 1974:

In order to keep prices up, the Arabs would have to curtail their output by even larger amounts. But even if they cut their output to zero they would not for long keep the world price of crude at \$10 a barrel. Well before that point the cartel would collapse.

(Garavini, 2019, p. 302)

Heads of states, especially US politicians such as more recently Donald Trump, have accused OPEC of unlawfully playing with oil prices, thus damaging the economy of key oil importing countries and making life difficult for consumers. Various legal initiatives have been put forward in the US Congress to remove the state immunity of the OPEC members in order to allow OPEC members and their national oil companies to be sued under US antitrust legislation. The last attempt was made in spring of 2019 as the US Congress deliberated another version of a Congressional bill known as the No Oil Producing and Exporting Cartels Act (NOPEC), initially put forward in 2000.³ The numerous previous attempts have stranded due to the uncertainties it creates in the market and the risk of some form of retaliation from OPEC members. Although US competition law might be suitable for curtailing antitrust behavior among international companies, it is harder to apply against other states. In this respect the World Trade Organization (WTO) could to be a more appropriate arena. In general, the governance of the oil market has been given surprisingly little attention by global trade institutions (Hughes, 2014, p. 17). After the Second World War, Western countries had no reason to create an international trade organization that would also

deal with raw materials because this would have potentially curtailed the power of their international companies. In the case of oil, the war had also shown its pivotal role in warfare. Controlling the flow of oil was at the top of the security agenda of Western powers at that time.

The wrong question: a cartel or not?

In academic circles, the most deliberated issue regarding OPEC since the early 1970s has been whether the organization is a cartel or not (Griffin 1982). The economic models applied have become increasingly sophisticated, but the literature remains inconclusive as to whether or not OPEC is a cartel (Kisswani, 2016, p. 172). There is no conclusive evidence of cartel behavior either in either price control or production behavior. The main reason is that OPEC's market behavior is not constant. 'Although some empirical models may fit the data quite well in specific time periods, they fail miserably in other time periods' (Fattouh and Mahadeva, 2013, p. 440). One 'external' reason for this is that the oil market has strong cyclical features. If OPEC cuts production in order to increase the oil price, the higher price will both curb demand and increase production from other oil producers, as more oil resources becomes profitable to extract, thus creating a supply surplus, which then reduces prices. Reduced prices increase demand and curb oil production as more oil fields become 'uneconomic'. Governing such a cyclical market is a tall order. No wonder OPEC has only occasionally been successful in this endeavor. The other challenge is the internal discipline, a challenge for any cartel. The more OPEC is successful in increasing the oil price, the stronger the incentive for individual members to defect from the cooperation, increase production, and reap the benefits of free-riding on the other members' cooperation. Johany (1980, p. 26) uses the concept of a 'centralized' cartel, where 'decision-making with regard to pricing, output, sales, and distribution of profits is accomplished by the central agency'. OPEC is far from being such an organization (as we will return to below).

The key feature of OPEC is the meetings (usually twice a year) of the oil ministers or any other delegate, setting common prices and/or production levels for the members to implement individually. Up until 1982 OPEC did not put any set limits on the oil production of its members. As the market conditions turned, OPEC introduced production quotas in March 1982. As pointed out by Al Moneef (chapter 3), OPEC then ignored the contradiction inherent in fixing both prices and volume. Colgan (2014, p. 606) finds that, calculated in months, between 1982 and 2009 the production of the OPEC countries exceeded the quotas 96 percent of the time. He also correlates production and quotas and finds that 'at most 1.8 percent of the variation in the month-to-month changes in [the members] oil production can be explained by changes in their OPEC quotas' (Colgan, 2014, p. 607, see also chapter 26 by Colgan). Claes (2001, p. 258) shows that OPEC members' production was consistently above quotas every month between April 1982 and April 2000, with very few exceptions. However, *changes* in production and quotas are strongly correlated. This, however, can imply causality either way. The quotas can constrain production, even though it is still above quotas. But it could also be the other way around – that the quotas are adjusted to changes in production. The fact that OPEC made 38 adjustments in the quotas between 1982 and 2003 could indicate the latter (OPEC, 2003). In 1999, the then secretary general of OPEC, Rilwanu Lukman, had the following reflection: 'OPEC is not the cartel that some of our friends outside like to portray us as; if we acted as a true cartel, prices wouldn't be where they are right now!'⁴ In a recent study, Aquilera and Radetzki (2016, p. 25) describe OPEC as 'a less than entirely coherent producer group able to extract prices somewhat above the competitive level for limited periods [...]. Whether this description warrants the label 'cartel' is a semantic and, for our purposes, not very important question'.

The right question: what difference has OPEC made?

Fattouh and Mahadeva (2013) provide a review of economic models of OPEC. They conclude that the role of OPEC varies over time, and no single economic model can explain all of OPEC's market behavior. Adding political, social, cultural, or other factors to the explanation of OPEC members' behavior, the picture becomes even more complicated, to say the least. Obviously, we cannot know with certainty how the OPEC members would have behaved domestically, or internationally, had they not been part of the organization. If we focus on the oil market, it is equally hard to determine what the oil price would have been without the existence of OPEC. At the end of 1985, when OPEC abandoned the strategy of defending the price level and began pursuing a strategy to protect its market share, i.e. a competitive strategy, the price fell to about \$10 per barrel. The same level was reached during the price fall of 1998/9. Since the price only stayed at that level for short periods of time, the actual effect on investments and replacement of reserves was not empirically tested. Adelman (1986) estimates the competitive price of oil – that is, the price without producer cooperation in any form – to be \$8 per barrel in the short run and \$5 per barrel in the longer run. He claimed that these prices would maintain investments in new reserves and production capacity.

The conclusion regarding the relationship between cooperation and the price is thus a mixed one: OPEC has not behaved as a true cartel, but the oil price has been above what it would have been in a true competitive market. Given the massive interest paid to the OPEC Conferences by economic pundits, industrial leaders, analysts of all kinds, politicians, and business journalists, one might conclude that OPEC has had something to do with the level of the oil price over the last sixty years. A fundamental reason for this is the concentration of oil reserves. Still today, the OPEC countries control nearly 72 percent of the world's proven oil reserves. Four major OPEC oil producers, Saudi Arabia, Iraq, Iran, and Venezuela, hold more than half of these reserves. OPEC's share of global oil production peaked in 1973 at just above 50 percent; in 1985 it was less than 30 percent. Since the early 1990s, OPEC's market share has been around 40 percent (Claes, 2018, p. 154). Several OPEC countries have proven reserves that can sustain their present level of production for decades, in some cases centuries (BP, 2019, p. 14). Perhaps more importantly, its share of global oil exports has decreased from more than 90 percent in 1960 to 54 percent in 2019 (OPEC, 2019, p. 60). Today's world of oil production is far more polycentric than when OPEC was born, but OPEC countries still control a significant share of global reserves, production, and trade, although most exploration for new reserves takes place outside OPEC. The very same petrostates that sixty years ago took the initiative to create OPEC are still the most productive oil regions in the world. Furthermore, the role of OPEC is not restricted to the oil price and the oil market. A narrow focus on its role in the oil market will overlook its importance for the wider economic and political development of its members – a point made by several authors in this book.

OPEC, its member states, and cooperation in petroleum policy

OPEC has had quite a few successes in its history since the 1960: mostly in areas other than governing the market price of oil. During its first decade of existence it managed to increase the producing countries' income per barrel of oil by collectively negotiating increases in royalties and taxes at a time when market prices for raw materials (including oil) were falling. The resulting increase in income per barrel was a terrific success under very difficult circumstances, unmatched by the other commodities' organizations and one that curtailed the profit margin of the seemingly unbeatable oil majors (or 'seven sisters' as Enrico Mattei, the head of the Italian ENI, used to call them). In the 1960s, the OPEC members could not influence the price at which their oil was sold. The international oil companies defended their concessions signed in the 1920s and 1930s. These concessions ruled out any role for local governments in oil production and pricing, except as tax collectors. By the Tehran and Tripoli agreements of 1971, and the events of

1973, after a momentous shift from a consumer to a producer market, OPEC managed to negotiate increases in posted prices (these ‘tax reference’ prices were for the first time increased unilaterally by OPEC in October 1973) and helped its members move toward direct control of oil production either through nationalization or through majority participation in the various consortiums. Although the member countries chose different strategies in this respect, the cooperation within OPEC was of paramount importance for strengthening the members’ ability to control and govern all aspects of their oil sectors.

From the end of 1973, OPEC countries were able to gain a significant degree of control over the oil price, but during the second oil shock of 1979/80 they were unable to stop an increase in prices that eventually got out of control and backfired. In 1982 they had fight to avoid a decline in oil prices by introducing production quotas for the members. The ‘cartel-like’ efforts failed. By the middle of the 1980s OPEC lost control over the market. As pointed out above, internal struggles and free-riding led to disrespect for the quotas. The national oil companies of the OPEC members ended up being more in competition than in cooperation in the low price market that followed the ‘countershock’ of 1986 (Basosi, Garavini and Trentin, 2018). The rise of China, and generally Asia, as the key consumer region helped OPEC countries in their exports by the end of the 1990s. China’s change from an oil exporting country in the 1980s to single largest oil importer after 2015 had not only economic but also political and ideological implications for its relations with OPEC (see chapter 12 by Bao). The OPEC members had enormous financial gains from the increase in oil prices during the 2000s. However, it is harder to assess the specific role that OPEC played in this increase in oil prices, as opposed to the 1970s, when OPEC was able to set a global reference price.

The hard reality is that, for all the efforts of OPEC countries and even their successes, what happens in the oil market is far more important for oil exporting countries than it is for the oil importing ones. Petrostates are in a structurally weaker position *vis-à-vis* their customers and have all the more to gain from cooperation than from competition: when prices decline, the economy of petrostates can be destroyed, potentially leading to regime change and social and economic collapse. On the other hand, when prices increase, consuming countries are forced to change and reform radically their energy policies, but crude oil prices only represent one of the factors at play for the wellbeing of the complex economies of industrialized countries.

The cooperation within OPEC has helped very ‘young’ nation states, such as Nigeria or the United Arab Emirates, to establish themselves as crucial members of the international community and strong regional players. At the beginning of the 1920s, Venezuela was probably the poorest region in Latin America with a nonexistent state. By the middle of the 1970s it had become the richest country in Latin America in terms of per capita income, with a weekly Concorde flight from Caracas to Paris that allowed Venezuelan ladies to shop for fashion in the French capital. If one pattern can be traced in OPEC member states it is that when their cooperation has been stronger, the wellbeing of their citizens has increased; while when competition and anarchy has prevailed, governments have been forced to apply austerity measures and citizens have suffered economic hardship and political instability.

The evolution of OPEC as an international organization

International organizations, as well as human beings, change over time. Both internal and external conditions produce changes. The North Atlantic Treaty Organization (NATO) was a child of the Cold War but survived the end of it, changed its modus operandi and persists as a vital organization for the military security of Europe and North America. The European Community (EC) was born out of the Second World War, with the aim to preventing war in Europe through cooperation in coal and steel sectors, establishing a common external tariff, and overcoming the loss of colonial empires. Today, the European Union (EU) focuses on building a single market and on competition policy, and has become the hub of politics and governance of 28 countries.

When OPEC was established in Baghdad in September 1960, by Iran, Iraq, Kuwait, Saudi Arabia, and Venezuela, none of its members, as we have seen, controlled their respective petroleum industry. OPEC was very important at the beginning for the support it offered its members' quest for sovereignty over natural resources and economic development. The petroleum sector was considered a key instrument, and OPEC was a device to get the petroleum sector under governmental control and allow increase oil rents that would help guarantee development goals (see chapter 4 by Atabaki). The international oil companies were at the beginning opposed to any role for OPEC and even to its very establishment as an international organization (see chapter 23 by Trinkler and chapter 15 by Kuiken) since this would have potentially limited their profits and their liberty to control the market by shifting production at will from one to the other areas. Their refusal to accept a real negotiation with OPEC, especially their refusal to abide by the clause of 'changing circumstances', their stubborn sticking to the colonial 'concession' contracts, may be one the worst mistakes the oil majors have made since the beginning of the oil industry (see chapter 22 by Boué).

A significant turning point came in 1973 when the oil price increases and nationalizations changed the respective role of international oil companies and sovereign governments: concession contracts became something of the past, while new contractual relations of a different nature were established (see chapter 14 by Nakhle and Petrini). After the middle of the 1970s, all OPEC countries were in charge of their oil sectors. Their newly created national oil companies were in competition for new costumers, even if at the expense of the national oil companies of other OPEC members. On the other hand, their governments still had an interest in cooperating with each other in order to guarantee stable prices and thus a reliable petroleum rent. In a nutshell: after 1973 the commercial interests of national oil companies were frequently misaligned with the interest of oil exporting governments as sovereign landlords.

The world today looks very different from what it was in 1973. Ramady and Mahdi (2015, p. 216) find that two of the three key instruments in the hands of the OPEC member states in the early 1970s are absent today. Obviously, they cannot nationalize one more time. The 'posted prices' are something of the past, and in a 24/7 trading marketplace for crude oil, increasingly linked to the financial markets, it is very hard to have stable prices (see chapter 25 by Claes and Moe). Today, the organization has 14 members.⁵ The criteria for membership states that any other country

with a substantial net export of crude petroleum, which has fundamentally similar interests to those of member countries, may become a full member of the Organization, if accepted by a majority of three-fourths of full members, including the concurrent vote of all founder members.

(Article 7 of the Statutes, OPEC 1990: 33)

The principal aim of OPEC is 'coordination and unification of the petroleum policies of member countries and the determination of the best means for safeguarding their interests, individually and collectively' (Article 2 of the Statutes, OPEC 1990: 32). OPEC has three main bodies: the Conference, the Board of Governors and the Secretariat. Although bureaucrats can make a difference in terms of effectiveness and background work, the key actors of OPEC remain its member states. The main authority and essential decision-making body of OPEC is the Conference. It consists of delegations representing the government of the member countries, usually headed by the countries' oil ministers. It meets in principle twice every year, but extraordinary conferences can be called. The Conference meetings are prepared by the Board of Governors composed of elected governors from the member states, leaving little autonomy or authority to the Secretariat:

The Secretariat shall carry out the executive functions of the Organization in accordance with the provisions of this Statute under the direction of the Board of Governors. The Secretariat of the

Organization shall consist of the Secretary General, the Deputy Secretary General and such staff as may be required. It shall function at the headquarters of the Organization.

(Articles 25 and 26, OPEC 1990: 37)

Decisions at the meeting of the Conference are taken by unanimity and are binding for all members. Formally, the member states are only committed by decisions they agree to and there are no sanction mechanisms against members that fail to abide by the agreements. Informally, powerful states can make weaker ones abide, by both sticks and carrots. As pointed out by Alnasrawi (1985, p. 3):

It must be recognized that the character and direction of OPEC is determined not by what OPEC has done or intended to do but failed to do, but by what each member government has done or proposed to do [...]. The moment the perception exists that an individual country's interests and goals are not served by an OPEC decision, [...] the interests of that country can be expected to supersede those of the organization's common objectives.

OPEC has none of the 'supranational' characteristics that can be found for instance in the European Union (EU) or the World Trade Organization (WTO). The Council of the EU makes many of its binding decisions by majority voting. An individual member country can thus vote against a proposal and still be obliged to abide by it. In the WTO, the dispute settlement system subjugates the member countries to decisions made by tribunals of selected independent experts. In OPEC, the Board of Governors and the Secretariat are far weaker than similar bodies of the EU; but also weaker than sectorial organizations such as the World Bank and the IMF that have been able, at times, to force recipients of their aid and interventions to abide by rules they have set. OPEC has from time to time created committees to monitor and control the respect of quotas, but ultimately only the member states can impose sanctions, although it is not clear how this could happen since any decision requires unanimity.

Nevertheless, OPEC is much more than a talking shop since many of its decisions have effectively been implemented, and since it is the only international organization that has some degree of theoretical control over the supply of a key raw material and energy source. There is nothing like it. Even though key members have been at war with one another, such as in the case of Iraq and Iran in the 1980s, they never considered abandoning an organization that, while weak at times, is certainly stronger than they would be if left alone facing the international oil companies and the governments of consuming countries. Thus, OPEC is in line with most international organizations, where the sovereign participating countries are only members as long as they find it to be in their own interest. This does not imply that the organization is trivial and without influence on the behavior of states. The liberal-institutional perspective in the study of relations between sovereign states suggests that international institutions can

affect the incentives facing states, even if those states' fundamental interests are defined autonomously [...] make it possible for states to take actions that would otherwise be inconceivable [...] affect the costs associated with alternatives and the understandings that leaders of states have of the roles they should play and their assumptions about others' motivations and perceived self-interests.

(Keohane, 1989, pp. 5–6)

OPEC certainly fulfills many of these roles and mechanisms of international cooperation among sovereign states. The cooperation among the member states of OPEC is in many ways a classic example of the challenges of collective action. Although all members have an interest in limiting oil production to ensure a high oil price, they simultaneously have an interest in sustaining or increasing their own production volume. In such a case, the actors can gain by cooperating (reducing production), but individually they can gain more by defecting while the others continue to cooperate. The presence of an international institution

can ensure that the member states trust each other's compliance, reduce the potential gains from defection, and thus facilitate cooperation. As discussed above, we cannot know what the oil price might be without OPEC, and thus not the net benefit from it to the individual member states. Nor has the collective action of the OPEC member states been anywhere near perfect, with consistent overproduction compared to the agreed production quotas. Therefore, the conclusion might be that OPEC has made a difference – to some extent, sometimes.

Present and future challenges

Today, oil is as important as ever, with global oil consumption reaching its highest historical levels at almost 100 million barrels per day. OPEC's member states produce 39.3 million barrels per day, more than ever.⁶

Nevertheless, OPEC faces a number of new challenges, both internally and externally. In terms of membership, even though this is not the first time, Qatar, the first non-founding member of the organization, joining in 1961, appears to have abandoned the organization for good, while Indonesia, also one of the first countries to join in the early 1960s, has recently become a net oil importer. On the other hand, Equatorial Guinea and Congo have joined the organization. Generally, one would assume that more members would strengthen an international organization. Oil producers come and go. Some countries find oil, others run out of it. Since the 1980s, OPEC has tried to strengthen its relations with oil producers outside the organization in order to have them join OPEC's market governing efforts. After the oil price fall in 1986, a handful of non-OPEC producers stated their intention to contribute by cutting production in order to increase the market price (Claes, 2001, pp. 289–291). In 2016, following the oil price fall in 2014, the 14 members of OPEC and ten non-OPEC producers initiated a joint-cooperation of production cuts, for shorthand known as OPEC+. This cooperation has been prolonged several times and is becoming institutionalized through regular meetings, joint declarations, and a formal pact (a draft Charter of Cooperation between OPEC and non-OPEC countries was presented during the 176th Meeting of the OPEC Conference in July 2019).⁷ The most important non-OPEC producer in this cooperation is Russia, with its 12 percent share of world production, trailing the Saudi Arabian market share of 13 percent. These two countries dominate their respective side of the OPEC-non-OPEC cooperation, making the real power in the producers' attempt to govern the oil market to some extent a Saudi-Russian bilateral affair. Nevertheless, the OPEC+ cooperation has definitely strengthened the producing countries influence in the market, notwithstanding, the importance of the rebound of US oil production over the last decade.

In 2008, the consistent decline in US oil and natural gas production since the early 1980s was abruptly turned around by the introduction of horizontal drilling in the exploration of oil and gas in rock formations together with more efficient fracking, creating the so-called shale gas and tight oil revolution (Aquilera and Radetzki, 2016, pp. 81–83).⁸ This technological revolution has made vast oil resources economically viable in the US, with potential for exploration in other countries like Australia, China and Russia. In many cases, the tight oil resources are costly to develop for various reasons. So far, the performance of the US tight oil industry stands out as an exception. The US oil supply shock has been phenomenal, with tight oil production rising from around 1 million bpd in 2010 to more than 8.5 million bpd in mid-2019. The technology of extracting tight oil is improving, so the potential for exploration worldwide can expand. Traditionally, the conventional wisdom has been that non-OPEC oil reserves would be exploited, leaving an increasing share of the market to the OPEC members with large untapped reserves of conventional oil. This prospect, of an increasingly bright future for the OPEC producers, have been clouded by the tight oil revolution, creating a sustained competition from producers outside of the organization, in particular the United States.

An even more fundamental challenge to OPEC is to be found on the demand side of the oil market. Based on the increasingly alarmist observations by scientists of an increasing global temperature caused by the emission of CO², mostly from the burning of fossil fuels, a shift in international public discourse against the use of fossil fuels is emerging. The issue of climate change and new environmental obligations of energy consumers and producer nations is an emotive one with significant long-term consequences for both in terms of the quality of life and impact on economic growth. After dragging its feet at the beginning of the Kyoto negotiations, OPEC countries will have to engage much more with the issue and possibly become partners in the search for solutions if they do not wish to be passive recipients of decisions taken by others, with devastating impact on their economies and societies (see chapter 28 by Muttitt). The Paris Agreement, also called the Convention, signed by the parties of the United Nations Framework Convention in 2015, aims at keeping the global temperature rise this century well below two degrees Celsius and to pursue efforts to limit the temperature increase even further to 1.5 degrees Celsius. The Convention does not set limits on individual countries' emissions. The ambitions of the signatory countries vary. Nevertheless, the Convention, and the public awareness of climate change, will affect energy policy-making processes both directly and indirectly in the future. Directly, in terms of putting pressure on governments to honor their promises of climate warming abatement action, and indirectly in the sense that the general public will be more inclined to accept changes in energy usage, while energy producers will get incentives to 'decarbonize' their energy products. In order to avoid global temperature rising above two degrees Celsius, the International Energy Agency assumes that the share of fossil fuels in the global energy mix will have to be reduced from over 80 percent to about 60 percent (IEA, 2018, p. 38). World oil consumption will come down from about 100 to about 70 million barrels per day (IEA, 2018, p. 136). This last challenge means that the fear of 'peak oil' production (see chapter 27 by Noreng) might transform itself into a fear of 'peak demand' for oil with stranded assets, potentially diminishing oil rents. The petrostates born in the middle of the 20th century will have to become something very different.

The role of OPEC

Most histories of OPEC agree that the organization played a role from time to time. According to the excellent history by former OPEC secretary general Francisco Parra, the first OPEC resolution in 1960 was so weak that 'the united needle-workers trade unions of greater Manchester would have produced something with more red blood in it' (Parra, 2009, p. 99). Also, former OPEC deputy secretary general Fadhil Al Chalabi sees the peak of OPEC power in 1973, but considers that later it undermined its role by accepting a price that was too high, which in turn led to 'diversification', conservation measures and the 'countershock' (Chalabi, 2010, pp. 5–8).

This volume points to the fact that OPEC has been important in the past, affecting the policies and choices of its members and used by its members as an instrument to reinforce their position. But the importance of OPEC is also indirectly confirmed by the fact that it generated significant reactions in consumer countries, forcing them to devise efforts at international cooperation and, in some cases, affecting their internal energy policy choices (see chapter 11 by McFarland). The Rambouillet Summit of the five largest economies (eventually morphing into the G-7) was launched in 1975 not only to quell the instability of monetary system and overcome the crisis of Bretton Woods but also as a way for the biggest industrialized countries to cooperate with one another in the face of the pressures stemming from raw materials producers – oil exporters in particular – that were battling for a new international economic order (see chapter 10 by Romero). The same can be argued for the International Energy Agency, which was created in 1974 as a reaction to the oil shock and as a way to foster energy cooperation among consumers that up to then mostly had to rely on international oil companies and emergency stockpiling (see chapter 9 by Turk and chapter 8 by Frøland and Ingulstadt). Also the relationship between the European

Community and OPEC points to the growing importance of petrostates in the 1970s (see chapter 13 by Bouvier and Beltran), even though a direct dialogue was never established. In the case of Norway and the UK the public governance of their petroleum sectors was partially inspired by the experience of the OPEC countries (see chapter 19 by Thomassen), although the subsequent models of state involvement became very different in Norway and the UK. Elisabetta Bini and Marta Musso (chapter 16), while speaking about the Italian national oil company ENI, explain the strategy of its founder Enrico Mattei of entering into a direct dialogue with OPEC countries, possibly bypassing international oil companies and favoring direct state-to-state dialogue. This strategy ended up being a failure, but for a short time in the 1970s state-to-state international oil deals seemed feasible and might have changed the global oil market. OPEC's policy affected the energy policies of consumers and the market strategies of non-OPEC producers. The latter ones such as Norway (see chapter 18 by Claes) and Mexico (see chapter 17 by Navarro) had to come to terms with their strong economic interdependence with the OPEC members, seeking cooperation but not membership. Another non-OPEC producer, Russia (see chapter 20 by Krutikhin and Overland), is today a vital partner in OPEC's market-governing strategy.

It is not easy to define OPEC and its role. Al Nasrawi (1985, p. 89) succinctly argues that 'OPEC is simply OPEC, and to attempt to force it into any of the frameworks of conventional economic analysis is a futile exercise.' Ramady and Mahdi (2015, p. 233) point out that

when OPEC came to life, production, marketing, and prices were controlled unilaterally by the International Oil Companies (IOCs), and there was little or no concern for the environmental and the social impacts of the industry such as global warming and ozone depletion. Today things have fundamentally changed, and at their peril, neither OPEC nor the IOCs can ignore these issues.

It is certainly true that OPEC needs to find a role. There are numerous proposals for reform that could render the organization meaningful once again, although obviously not on setting prices, something it has not been able to do since the middle of the 1980s. OPEC remains central in the petroleum sector, which itself is a key global energy source. It is the only international organization with some power to control the supply of oil and has been reinforced by the new link with non-OEPC producers such as Russia. But, while oil will remain a key primary source for petrochemical industry, its future importance as an energy source will necessarily have to decline together with the reduction in the use of fossil fuels.

OPEC secretary general Barkindo has declared that the biggest challenges OPEC has to face today is coming from 'environmental activism' that is present even within the families of OPEC officials when their children 'are asking us about their future because [...] they see their peers on the streets campaigning against this industry'.⁹

OPEC is an organization of sovereign landlords that have an interest in both preserving an international land rent and preventing a fast depletion of their natural resources. In the face of the challenge of climate change, can the OPEC member states take a long-term view and ensure the interests of their citizens by smoothening the unavoidable transition of their economies and societies? And, might OPEC actually become a partner and contribute to international cooperation in managing a reduction of fossil fuels production and CO² emission?

This can only be done if there is willingness to cooperate between oil consumers and oil producers. Today, the oil market is a 24/7 global free trade market for crude oil, refined products and, not least, oil-related financial assets and instruments. OPEC and its new partners (OPEC+) are trying to influence the price of crude oil set in this free trade market by adjusting their production to changing market conditions, with the aim of securing substantial revenues for the oil producers. Crude oil producers outside OPEC+ are in fierce competition for market share and the development of oil resources, illustrated by heavy investment in unconventional oil such as the one extracted from tar sands in Canada, low taxation in the UK to extract marginal fields in the North Sea and US tight oil production that is marginally profitable if at all.

In this situation, there are no incentives at all for the producers to reduce oil production due to the aim of reducing CO² emissions. If climate change considerations significantly reduce oil consumption, one can assume that the market will end the production of high cost oil first. This will benefit many OPEC producers, for a while. However, rather than intensifying competition in a falling market, the oil producers could accept a more orderly decline in their oil production and allow for some sort of international cooperation on the global quantities of oil that are produced and consumed each year, for instance by an international organization with the mandate to allocate production rights. Let us call it the Organization of Oil Producing Countries (OPPC).

Although the future of OPEC looks challenging, the organization is still a vital actor in any global attempt to face the coming energy transition, whether implemented by market mechanisms or by international political cooperation.

Notes

- 1 *The Times*. Sam Coates, Chief Political Correspondent, in Jeddah, 23 June 2008. www.thetimes.co.uk/article/gordon-brown-visits-saudi-arabia-to-plead-for-win-win-deal-on-oil-m7q69zg6q06.
- 2 *CNN Business*, 10 February 2015.
- 3 Anjali Raval and Ed Crooks: 'Opec faces fresh threat from US legislation', *Financial Times*, February 7, 2019. www.ft.com/content/047e222c-2af6-11e9-a5ab-ff8ef2b976c7; and Stephen Cunningham: 'Retaliation Risks From NOPEC Bill Exaggerated, Proponents Say', *Bloomberg*, April 11, 2019.
- 4 OPEC's secretary general, Rilwanu Lukman, interviewed in *Petroleum Economist*, March 1999, p. 8.
- 5 The five founding members were later joined by ten other members: Qatar (1961) – terminated its membership in January 2019; Indonesia (1962) – suspended its membership in January 2009, reactivated it in January 2016, but decided to suspend it again in November 2016; Libya (1962); United Arab Emirates (1967); Algeria (1969); Nigeria (1971); Ecuador (1973) – suspended its membership in December 1992, but reactivated it in October 2007; Angola (2007); Gabon (1975) – terminated its membership in January 1995 but rejoined in July 2016; Equatorial Guinea (2017); and Congo (2018). OPEC had its headquarters in Geneva, Switzerland, in the first five years of its existence. This was moved to Vienna, Austria, on 1 September 1965. www.opec.org/opec_web/en/about_us/24.htm.
- 6 All figures from BP (2019).
- 7 The formal declarations of the OPEC–non-OPEC cooperation is found here: www.opec.org/opec_web/static_files_project/media/downloads/publications/Declaration%20of%20Cooperation.pdf.
- 8 Tight oil is oil that has not yet migrated to a conventional trap but instead remains in the porosity of the source rock unit in which it was generated. Shale oil is also used to describe this type of oil.
- 9 'Biggest compliment yet: Greta Thunberg welcomes oil chief's 'greatest threat' label', *The Guardian*, 5 July 2019.

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Part I

OPEC and the member countries



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Oilmen, Petroleum Arabism and OPEC

New political and public cultures of oil in the Arab world, 1959–1964

Nelida Fuccaro

The birth of OPEC as an international community of oil producers and exporters was part of an institutional, economic and ideological setting that contributed to eradicate Western hegemony in the name of anti-imperialism, nationalism and, crucially, the global quest for sovereign rights of former colonized nations (Dietrich, 2015 and 2017). Among the five largest oil exporters that formed OPEC in September 1960, three were Arab countries (Iraq, Saudi Arabia and Kuwait), with the addition of Iran – whose oil fields and installations bordered Iraq – and the Arab states of the Persian Gulf. It is widely recognized that Venezuela played a paramount role in the establishment of OPEC. Yet the question of ‘Arab Oil’ and the tensions between Arab states – particularly what Malcolm Kerr has defined as the ‘Arab Cold War’ between Iraq and Egypt – profoundly influenced the early years of this organization, culminating with the 1973 oil embargo. The idea of ‘Arab Oil for the Arabs’ started to gather momentum in the 1950s following the nationalization of the oil industry in Iran and that of the Suez Canal by the Egyptian president Jamal ‘Abd al-Naser.

It is tempting to adopt a unidimensional view of the relationship between OPEC and Arab nationalism/pan-Arabism as one characterized by a lingering tension between a global vision and parochial national/regional concerns. Nathan Citino for instance sees the establishment of OPEC as a ‘drastic retreat from Arab Nationalism’. He contends that the organization dealt a fatal blow to ‘Arab Oil’ by detaching large oil producers such as Saudi Arabia and Kuwait from the radical nationalism of al-Naser, effectively preventing any transfer of petroleum wealth to poorer Arab countries (Citino, 2002, pp. 145–160).¹ Moreover, literature on oil has tended to look at the production of politics – particularly at the level of the rentier state – as the result of compartmentalized structural forces, such as the economy, ideology, market logics and state building.

This article adopts an approach that is historically and agency grounded. It shifts attention to Arab oil technocrats as indigenous actors and promoters of petroleum Arabism in the context of a new knowledge-based political and public culture of oil that they fostered as members of both OPEC and the Arab League.² The focus is not so much on the achievements of their oil politics and diplomacy in the regional and international arena, as skillfully discussed by Citino. Instead, attention is devoted to the novel ideological and policy-oriented sphere of public engagement they were able to create in the period between 1959 and 1964 when they deployed their technical expertise and the popularization of knowledge about the oil industry as powerful weapons against multinational corporations and Arab governments. This article

covers the early years of OPEC. It begins with the formulation of an Arab oil policy that consolidated these technocrats as a cohesive and self-conscious group, and runs through the establishment of OPEC in Baghdad in 1960 and the first four Arab Petroleum congresses organized by the Arab League.

Baghdad, September 1960: establishing OPEC

The involvement of Saudi Arabia, Iraq and Kuwait in the establishment of OPEC, and the choice of revolutionary Baghdad as the venue of the first meeting in September 1960 unmistakably placed this organization in the orbit of Arab Oil and in a regional setting fraught with political tensions. An intelligence report produced by the Iraq Petroleum Company (IPC) a few months before the meeting anticipated the explosive political implications of plans for the control of the international oil market by oil producers, outlining potential regional repercussions in terms of strikes, withdrawal of working permits for staff and the import of spare parts for the machinery necessary to oil extraction. The report also summarized political tensions very succinctly as ‘UAR (United Arab Republic) versus Iraq’, the two revolutionary regimes vying with each other to establish their regional anti-imperialist credentials.

The timing of OPEC’s birth was quite momentous in regional terms. On the one side stood Egypt, President Jamal ‘Abd al-Naser, and the country’s recent political reincarnation, the United Arab Republic (UAR), which had come to life in 1958 as a union with Syria. In spite of being a minor oil producer, Egypt for some time had taken up the cause of Arab oil through the Cairo-based Arab League. In 1954, the League established a Petroleum Department following the creation of a committee of Arab oil experts in 1951. By 1960, as the UAR had become the flagship of pan-Arabism, Egypt took on the mantle of key promoter of the idea of oil as an inalienable Arab right, a pillar of Naserist anti-imperialist propaganda. This idea played into the foundation of OPEC through the First Arab Petroleum Congress sponsored by the League and held in Cairo in 1959, as explained below. Yet the regime’s attitude vis-à-vis Arab oil was ambivalent. It was shaped by propaganda campaigns against conservative oil producers (Saudi Arabia, Iraq until 1958, and Kuwait) but did not materialize in concrete policies. The absence of such policies prevented the Egyptian government from giving the impression of trying to take advantage of the oil royalties accrued by regimes that in the eyes of Egyptian radical ideologues practiced ‘the deplorable squandering of oil revenue by the privileged classes’ (Hirst, 1966, p. 109).

The exclusion of Egypt from the Baghdad meeting and from OPEC – because the UAR was not a petroleum-exporting country – elicited fierce reactions in the Egyptian press. According to the Cairo daily *al-Jumhuriyyah*, the resolutions of the meeting were ‘weak and conciliatory, lacking any indication that the Arab producers will actually challenge the decision of the foreign states exploiting *Arab oil* [my emphasis] to cut posted prices’.³ Yet the pivotal role of Egypt and the Arab League in shaping and popularizing debates – if not implementing policies on the ground – on the future of petroleum in the Arab world was in the mind of oil companies and the Western press. Both viewed with some apprehension what they called ‘The Baghdad Petroleum Conference’ as the curtain raiser for the Second Arab Petroleum Congress to be held in Beirut under the patronage of the Arab League and closely identified with al-Naser’s oil initiative.⁴

On the other side of the contest stood Iraq’s young and unstable military regime, which triumphantly hosted the Baghdad meeting in September 1960 in the middle of stalled oil negotiations with the IPC, one of the hated symbols of the ancient regime. Since the 1958, the revolutionary government – well known for its lambasting propaganda machine – construed the question of the control of petroleum resources as a domestic issue against British imperialism and the lynchpin of the definition of Iraqi nationhood. According to the Iraqi oil economist Fadhil al-Chalabi, who served as acting secretary general of OPEC from 1983 to 1988, in the period immediately following the 1958 Revolution ‘oil became a political commodity by politicians to outbid each other, and the criteria for ‘national interest’ involved necessarily confronting the companies and their concession system, that legacy of colonial rule’ (Chalabi, 2010, p. 25).

It is no surprise that the British Embassy in Baghdad portrayed the fierce anti-imperialist stance of the Iraqi delegation led by Tala't al-Shaybani, the Acting Iraqi Oil Minister and chairman of the meeting, in unequivocally disparaging terms: 'The Iraqis, ignorant men of low caliber, were approaching the problem (of oil) from a political and doctrinal point of view' (Burdett, 2004e, p. 93). State rhetoric in early revolutionary Iraq deployed internationalist propaganda to substantiate claims of solidarity with colonized countries and the Soviet Bloc. It was decisively anti-Nasserist, to a large extent anti-Arabist and left leaning given that Iraq's revolutionary leader Colonel 'Abd al-Karim Qasim was able to keep power with the support of the Iraqi Communist Party. This mood was captured by the Communist newspapers *al-Mabda'* and *Ittihad al-Sha'b* when they claimed that the resolution of the Baghdad meeting translated the principle of Arab solidarity into a concrete form but crucially bolstered worldwide efforts to contain imperialism and world monopolies.^{5 6}

In fact, following the public announcement of the formation of OPEC, the Iraqi press and the regime drew much attention on the negotiations with the IPC. In both radio communiqués and press interviews, Iraq's revolutionary leader 'Abd al-Karim Qasim declared Iraq's wealth and resources limitless, demanding that the public be patient, hold firm and be prepared to endure hardship for the sake of upholding the rights of the Iraqi people.^{7 8} The birth of OPEC served to widen the horizons of public expectation regarding the government's prospect of quickly increasing ownership of Iraqi oil, naturally bringing into sharper focus the regime's claims of petroleum sovereignty and its anti-Arabist position.⁹ More specifically, while the government was trying to redefine the terms and territorial extension of the original oil concession, the creation of an organization that brought together major oil producers served to focus public attention on oil as an irreplaceable and unlimited national resource. This was not only for the extraordinary wealth it could generate but also as an inalienable national and natural right that cemented an indissoluble bond between people, territory and geology.¹⁰ It is significant that during the meeting the newspaper of Iraq's National Democratic Party demanded in a leading article that oil companies relinquish unexploited areas, and that the nation take charge of this unexplored land as the new Eldorado replete with inexhaustible natural wealth. This focus on petroleum geology and the need to control exploration echoes ideas popularized the previous year by the Saudi oil consultant Omar Kamil Haliq, who urged Arabs to take over the largely untapped oil regions of the Persian Gulf and Arabian Peninsula. Evidence provided by 'geological oil intelligence' produced by companies suggested that large oil reserves of these areas had been only 'scratched'.¹¹ The IPC's reaction to the meeting's resolutions was somewhat optimistic. The company's Baghdad office concluded that OPEC might have a curbing influence on the negotiations, as the Iraqi government would be unlikely to jeopardize its position with the newly established organization by taking extreme measures with the Company. The reasoning was also that by alienating OPEC the Iraqis would also undermine the position of prestige that the organization granted them vis-à-vis Egypt.¹²

Arab oil technocrats and the radical age of Petroleum Arabism, 1959–1963

Let us be grateful for this [God's] gift [oil] and show our gratitude by creating a new generation of Arab Oil men capable of developing what is today our national wealth and what will be tomorrow the mainspring of our industrial greatness. Let this generation be the nucleus of future generations, the sturdy oak whose branches will spread beyond the confines of oil into other fields of industrial endeavour.

(Lutfi, 1960)

In 1959, a year or so before the establishment of OPEC, Ashraf Lutfi was writing about the future of oil in the Arab world as the voice of the very same Arab oil men he celebrated as the dawn of a new industrial era. A Palestinian transplanted to Kuwait, by 1959 holding an important position as assistant to the state secretary, Lutfi was part of a new transnational network of Arab oil technocrats that had a

profound impact on the establishment and development of OPEC, which Lutfi led between 1964 and 1965. Crucially, these individuals represented the ideological and operational link that connected OPEC to the Arab League, the sponsor of the First Arab Petroleum Congress held in Cairo in April 1959. In the words of Omar Kamil Haliq – one of the early ideologues of the group and like Lutfi a Palestinian transplanted to Saudi Arabia – this Congress was the ‘mental product and purposeful scheme’ of this group, who succeeded to bring it about by ‘sheer dedication’¹³ (Dietrich, 2017, pp. 70–77). Shortly before the birth of OPEC this Congress was the single most important event that established this new group of oil technocrats as the talk of the town. They started to feature prominently in the intelligence reports of oil companies, concerned at the prospect of having to lose face and revenues confronted with their demands. They also elicited extraordinary interest in the Arab and Western press and captured the attention of oil consultants and academics writing about the industry. In April 1959 during the First Arab Petroleum Congress, *Time* magazine called Abdullah Tariki ‘The unquestioned spokesman of the new generation of Arab experts on oil’.¹⁴

This network of exceptionally gifted individuals formed the first generation of Arab Petroleum elites that emerged on the trail blaze of the industry’s development throughout the region after the Second World War. They were the bearers of a new culture of oil modernization, technical and legal experts who shared a regional, global and internationalist outlook alongside a Western education, in some cases acquired through government scholarships.¹⁵ To name a few: Abdullah Tariki, one of the standard-bearers of the group, since 1954 director-general of Petroleum and Mineral Affairs, and between 1960 and 1962 minister of oil and mineral resources of the Kingdom; Anis Qasim, a prominent Palestinian lawyer and head of the Libyan Petroleum Commission; Muhammad Salman, the Iraqi-born head of the Arab League Petroleum Bureau and since December 1961 Iraqi minister of oil; Omar Kamil Haliq, the Palestinian-born counsellor for research at the UN Saudi Arabia mission; Hassan Kamel, an Egyptian lawyer who since 1960 was employed as advisor to the Qatari government and also acted as the main liaison officer with the Qatar Petroleum Company; Nadhim Pachachi, a very prominent Iraqi politician who served as minister of oil under the Hashemite monarchy and became advisor to the Libyan government after the 1958 Revolution. Tariki and Salman were the architects of both OPEC and the First Petroleum Congress. An IPC memo called ‘Abdullah Tariki’s Plan for the Control of the International Oil Market’ written on the eve of the Baghdad meeting and shared with all major companies operating in the Middle East is testimony to Tariki’s influence in facilitating the establishment of the organization and in providing an earlier programmatic agenda.^{16 17 18} Qasim and Haliq provided important ideological foreground to the development of new ideas of Arab oil sovereignty that nurtured the development of both OPEC and the Arab League.¹⁹ Lutfi and Pachachi served as OPEC secretaries after having started their careers as oil advisors and bureaucrats for the Kuwaiti and Iraqi governments respectively, positions that allowed them to contribute substantially to the oil policies of the Arab League.

As Lutfi makes clear in the opening quote to this section, this group of Arab oilmen – the self-professed *Rijal al-Bitrul al-‘Arabi* – were central to the development of new thinking about the future of the petroleum industry in the Arab world. Their vision promoted struggles in the name of ‘Arab Oil for the Arabs’ that came to fruition with the progressive nationalization of the industry throughout the region in the 1970s and 1980s. As perceptively discussed by Dietrich, these Arab oil technocrats belonged to a new global anti-colonial elite that operated in an age of decolonization profoundly influenced by Iran’s oil crisis and the nationalization of the Suez Canal. Their thoughts and actions fed into international struggles for political and economic emancipation from Western domination that focused on petroleum, by the 1950s the most precious mineral resource in the hands of old and new powers, most notably colonial Great Britain and corporate America (Dietrich, 2017 and 2015, pp. 63–78). The role of these individuals and petroleum in the new politics and cultures that emerged in local, national and regional arenas has been so far largely underestimated, particularly in relational to the twilight of colonial empires, modernization and vexed question of Arab nationalism and pan-Arabism. Literature on oilmen in the Middle

East has tended to be celebratory and focus on groups other than the *Rijal al-Bitrul al-'Arabi*. In the first instance, much attention has focused on the so-called 'pioneers', an early generation of Western explorers and adventurers that unveiled to the world the petroleum riches of the Arabs.²⁰ The underlying tone of much of the oil literature has celebrated the expertise of oil companies and in particular the European and American executives, engineers and administrators on their payroll as the wealth creators par excellence. In most accounts, foreign companies and their staff also appear as the benevolent protagonists towards the path of nationalization. As aptly summed up by Boué, indigenous governments appear as:

incompetent entities ... only adept at placing obstacles in the path of oil companies, so as to hinder productivity and thereby avail themselves of economic surpluses that by rights ought to go either to consumers (in the form of lower prices) or else to company profits.

(Boué, 2017)

Mutually reinforcing connections rather than divisions shaped the personal histories and professional trajectories of these Arab oilmen. For instance, in 1960 Qasim – then in charge of the Libyan Petroleum Authority – hired Pachachi to scrutinise Libya's petroleum laws (Dietrich, 2017, pp. 94, 97–98). Typically, their working lives crossed paths with several Arab governments, which they served as both citizens and expatriates. Their legal and technical education in European and American universities, often in petroleum-related fields, allowed them a meteoric rise in government departments as public officials and oil consultants. They also represented Arab states in major international organizations, such as OPEC, the UN and the Arab League. It is no coincidence that after September 1960, association with OPEC was influential in shaping this group. Yet, in spite of representing (or having represented) governments, the thoughts and actions of this first generation of Arab Oilmen often antagonized kings, presidents and public officials, often obfuscating state policies.²¹ Described by *The Economist* in 1959 as 'Highly intelligent, technically competent, nationally and personally ambitious ... (their) desire to be inside (the oil industry) is both personal and nationalist.'²² Essentially, they were regionally and globally connected, politically conscious but often detached from the turbulence of national and ordinary politics. With often eventful and highly dynamic careers, their political influence depended on their success in dealing with oil companies, often having started their careers working for them. Company executives did not necessarily view the emergence of this new class as bad news. According to a telling memo produced in early 1960 by the American Gulf Oil (which had interests in the Kuwait concession), these Arab technocrats were considered 'misinformed' but 'able'. Crucially, they were not judged fanatics like Musaddiq and were known to be aware that the companies are the best of necessary evil, as colorfully put in the memo, 'the only geese who know how to lay golden eggs'.²³

As perceptively noted by Hirst, not having firm political commitments to the countries they ostensibly served – or, as in the case of Tariki and Pachachi, having severed such commitments – contributed to strengthen horizontal solidarities with peers and develop ambitions centering on unified Arab oil policies (Hirst, 1966, p. 105). One notable exception seems to have been the Egyptians. In the al-Naser era oil technocrats were bound to the regime by tight political and ideological protocols and less likely to develop independent profiles as both consultants and government representatives. The group's ambitions to voice unified Arab oil policies that crossed state boundaries converged into what can be termed Petroleum Arabism, an expression of resource nationalism that construed oil in the same way as language and history, an important bond that united Arab peoples and transcended political realities and national boundaries. In their vision, the cultural and historical intimacy that characterized the relationship between Arabs and oil as an industry, substance and commodity underpinned future political and social struggles. In essence, while appealing to Arab nationalism, they rejected political parties and government positions and went beyond the political conventions of the 'Arab Cold War'.

By the end of 1959, this group had acquired a manifesto, a paper by Omar Kamil Haliq called 'A Statement of Arab Oil Objectives'. Written for publication in a leading New York newspaper while Haliq was working for the UN, most likely in 1958, it remained unpublished but circulated widely. For instance, it formed the centerpiece of a meeting of public relations officers working for major oil multinationals convened at Oxford University in late 1958. As Haliq clearly states at the beginning of the paper:

The purpose of this article is to spell out in frank terms certain aspects of the thinking and planning of those purposeful Arab Technocrats who form the decisive *second front* in the raging battle for a unified and independently viable Arab national existence [my emphasis].

This paper provides plenty of evidence of Haliq's self-identification with the group as well as the extent to which this new class had developed a coherent political, sociological and ideological worldview, a *second front* that was distinct from the Arabist, pan-Arabist and leftist lines promoted by Arab governments.²⁴ The paper is also witness to the *Rijal al-Bitrul al-'Arabi's* conviction that they were indispensable to the governments they served, a belief that led them to develop a sense of purposeful self-assurance. Haliq places himself and the group as an alternative to demagogues (that is, Arab elites and by extension governments), street mobs (a clear reference to the revolutionary crowds of both Egypt and Iraq) and Western oilmen. Haliq's resource nationalism is summed up by the motto that Arab technocrats should transform oil into a 'national occupation' to stop it from being a mere 'income-producing lease'.²⁵ In other words, for Haliq petroleum was to be used as an alternative political currency to Arab insurgency, a currency much needed to address an image deficit that beset the region, which in the eyes of the West was identified exclusively with bloody upheavals. Haliq was very unappreciative of Arab revolutionary movements, whereas Tariki celebrated the Egyptian revolution as a world revolution.²⁶

By the time OPEC was born in September 1960, Tariki, Lutfi and Haliq had already proposed concrete plans for the Arabization of the oil industry. These included the establishment of an Arab Petroleum Authority as a central organization to coordinate unified Arab oil policies, the construction of an Arab pipeline and tanker fleet with a view to eventually controlling the transport of crude, and the development of an Arab-controlled petrochemical industry²⁷ (Lutfi, 1960, p. 82). Tariki presented a paper entitled 'Middle East Pipelines and Their Economic Future' at the First Petroleum Congress, bringing the issue to the attention of the foreign and Arab press. Oil companies also closely scrutinized the paper as Tariki called them directly into question as partners in the project²⁸ (G. and H. S., 1959, p. 249, 251). The Arab League Economic Council had already discussed an all-Arab pipeline proposal in 1957, and after the First Petroleum Congress Tariki presented the project at the meeting of the Arab League Oil Experts Committee held in Jiddah in November 1959. Tariki's idea was to connect pipelines carrying crude from the oil fields of Saudi Arabia, Kuwait, Qatar and Syria to a line running from the Eastern Province of Saudi Arabia through Iraq and then parallel to the Kirkuk-Tripoli pipeline that carried Kirkuk oil to the Mediterranean.^{29 30} When the Arab Economic Council took up the project in 1961, southern Iraq had become the convergence point of the pipeline, effectively bypassing the IPC-controlled Kirkuk-Tripoli line. This reflected the growing importance of Basra oil as well as the intensification of the ongoing negotiations between the IPC and the Iraqi government, by then a cause that was taken up in the context of the project of Arab oil. The main line was to run from Basra to one or two terminals in an unspecified coastal area of the Eastern Mediterranean³¹. This specific vision of an Arab petro-future centering on the pipeline and tanker fleet clashed with that of the Lebanese tycoon Emile Bustani. Discussing how best to invest income derived from oil royalties during the First Petroleum Congress he called for the creation of an Arab development fund, an idea that Abdallah al-Tariki opposed vehemently on the grounds that such fund would eventually favor foreign oil companies, reproducing relations of economic and political subordination (Bustani, 2004).

In spite of sharing similar worldviews, the oil technocrats that took center stage in the late 1950s were different in temperament: some were more radical and vociferous than others, few changed positions and style throughout their career. In spite of distancing himself from Arab revolutionary regimes, Haliq often used a left-leaning anti-imperialist language that was not too different from that employed by the pro-communist press in Qasim's Iraq. He construed oil areas under concessionary regimes as 'pieces of personal real estate' in the hands of oil companies and accused the companies of acting like 'absentee landlords'. His sociological analysis of the impact of oil on Arab societies is class determined. Haliq for instance regrets the formation of a small middle class of local contractors lacking any socio-political consciousness.³² By the mid-1960s, Tariki's political and personal style had grown increasingly radical. Various referred to by Western oil executives and unsympathetic journalists as 'a demagogue' and 'the scoundrel of Arab Oil' since the beginning of his career, he developed an apolitical Arab nationalist style, which he accentuated after he left Saudi Arabia to relocate to Beirut. He became a veritable oil populist, a self-styled social reformer that linked petroleum to the welfare of ordinary people and used the *Arab Oil and Gas Journal* (*Majallat al-Bitrul wa-l Ghaz al-'Arabi*), which he established in 1965, to popularize his views (Al-Sayf, 2007a, pp. 311–408; Duguid 1970).³³

The degree of institutionalization of oil development in Arab producing nations also determined the ideological position of this generation of technocrats, their attitude vis-à-vis the governments they served and their ability to enforce their personal petro-visions. It is easy to grasp why a conservative country like Saudi Arabia became the hotbed of oil radical thinking in the late 1950s as technocrats such as Haliq and Tariki were quite free from established institutional protocols. The Saudi Ministry of Oil and Mineral Resources was created only in December 1960 under Tariki. It was previously in existence only as a directorate, part of the Ministry of Finance. In Kuwait, a department of General Oil Affairs was established at independence in 1961 as part of the Ministry of Finance and Industry. Only in 1975 was a separate oil ministry formed.³⁴ This is in contrast with Iraq, an early petroleum developer, which by the 1950s had an established and relatively well-staffed oil ministry that witnessed frequent reshuffles of personnel. The dramatic change of regime in 1958 forced Nadhim al-Pachachi out of Iraq and brought back in Muhammad Salman who returned as minister of oil in December 1960 after an illustrious career at the Arab League. Both Pachachi and Salman were oil diplomats rather than propagandists, and their politically shrewd and pragmatic style contrasted with Tariki's often bombastic and very direct manner of engaging his interlocutors.³⁵ The Iraqi delegation to the first OPEC meeting was staffed exclusively with government officials, in contrast to other Arab delegations that also included company employees and consultants. Only four months after the Baghdad meeting, the composition of the Iraqi delegation to the second OPEC meeting in Venezuela changed dramatically because of intensifying purges in the administration and army and the appointment of Mohammad Salman as head of the oil ministry.^{36 37 38}

A change of guard among oil technocrats started to become apparent by the Fourth Arab Petroleum Congress held in Beirut in November 1963. Partly because of a generational shift, individuals with more moderate views took over. It is what Stephen Duguid forty years ago in his perceptive study of Arab Oil technocrats called the forging of a 'rational' oil policy (Duguid, 1976, pp. 12–13). The Petroleum Press Service labelled them 'The New Professionals' because they behaved less militantly and radically than their predecessors and looked at companies as partners rather than enemies. Representatives of this new age of compromise were Tariki and Salman's successors: Ahmad Zaki Yamani, who joined OPEC after he became Saudi oil minister in March 1962, and 'Abd al-Rahman Bazzaz, a seasoned Iraqi politician who became secretary general of OPEC in May 1964. In the eyes of Western observers, the 'professionalization' of oil affairs in the Arab world was linked to the more conciliatory stance assumed by oil technocrats towards the companies. These observers tended to interpret this stance as a rational choice determined by economic considerations rather than by the emotional responses identified with the 'irrational' sentiments associated with Petroleum Arabism, and with the behavior of individuals like Tariki and Haliq³⁹. Soon

after his appointment as Saudi oil minister, Yamani – diplomatic and softly spoken – entered a collision course with Tariki. During the Beirut Congress he dissociated the Saudi government from Tariki's declarations. In a later issue of the *Arab Oil and Gas Journal*, Tariki attacked Yamani in an opening editorial accusing him of claiming to have invented the concept of *al-musharakah* joint ownership of oil resources. In a very didactic tone, Tariki reminded Yamani that the Saudis were the first to raise the flag of joint control from the well to the pump in the late 1950s (Al-Sayf, 2007a, pp. 321–322; on Yamani, see Robinson, 1988). Bazzaz established for himself a reputation as moderate as member of the OPEC delegation that entered negotiations with the IPC in March 1964, two months before his appointment as the organization's secretary general. At the opening of the meeting he expounded the principle of moderation versus extremeness, called for a realist approach against the purely legalistic arguments put forward in the past by the company and the Iraqi government, and advocated a forward-looking attitude oblivious of past recriminations, particularly against IPC as an agent of British imperialism.⁴⁰

OPEC in the Arab Petroleum congresses

After September 1960, the Petroleum Congress became the venue where Arab oil technocrats played out their relationship with each other and OPEC. Until the late 1960s these congresses remained identified with the more emotional nationalist discourse championed by al-Naser's Egypt and supporters of Tariki-style Petroleum Arabism.⁴¹ In this respect, while sharing a new broader anti-imperialist culture of the periphery, congresses provided a counterpoint to the internationalist rhetoric of OPEC. A BP observer noted that the Second Congress aimed at establishing an 'emotional and intellectual background against which Tariki could pursue his course of diplomacy, negotiation and legislation.' The same observer remarked that the Beirut event was 'in the direct line of Cairo [i.e. the First Petroleum Congress] and not of the OPEC meeting in Baghdad.' Ultimately, as an Arab initiative the Second Congress showed a higher degree of confidence compared to the First and appeared to many observers as the continuation of the establishment of OPEC, but also presented the Baghdad meeting as one of the latest steps in Arab activities.⁴²

During the second and third congresses Tariki claimed that OPEC owed its existence to these gatherings and that the congresses and OPEC had complementary profiles. He maintained that the congresses were the rostrum of the people and the venue for the creation of an informed public opinion about the industry, regionally and internationally. In fact, oil technocrats like Tariki used these events to appeal to a variety of publics, in parallel with the Arab League's propaganda machine that engineered and financed them. Crucially, congresses also became the primary settings where companies could engage with the concerns of Arab oil producers. In fact, the companies continued to debate vigorously with each other the desirability and extent of their participation to these events. One cause of persistent disagreement was the technical versus political content of the papers presented by their representatives. In October 1961 Frank Stoakes of BP, in a candid assessment of the Third Congress, noted that the companies should produce 'reasoned and coherent arguments' in these papers to uphold their position for consideration by the new Arab intelligentsia, increasingly powerful with governments and keen to absorb as much information as possible on the oil industry.⁴³

In contrast to the populist and public relations nature of the congresses, many technocrats like Tariki viewed OPEC as representing the aspirations of governments, the forum for the setting of oil prices and a powerful instrument for the gathering and discussions of scientific information on the industry.⁴⁴ Egyptian delegates often used the congresses to criticize OPEC, posing the UAR as the statist model for the national management of the industry. Some OPEC delegates – particularly the Venezuelans, who continued to be baffled by relentless inter-Arab rivalry – tended to emphasize the common ground of the two organizations trying to overcome rifts among Arab oil producers. When questioned about the credibility of an Arab policy that did not include countries such as the United Arab Republic and Libya, Tariki took for granted

that eventually all Arab countries were bound to enter OPEC's orbit⁴⁵ (Lutfi, 1960, p. 82; Hirst, 1966, pp. 111–112). The Fourth Congress held in Cairo in late 1963 witnessed the escalation of rhetorical tension between Tariki, OPEC delegates and Egypt, effectively provoking a rift between OPEC and the Congress. After the collapse of the UAR, Egypt was vying to establish its credentials as a petroleum superpower, entering into fierce competition with Tariki who still acted as the superstar of the event. The Saudi maverick cut such a towering presence as oil's political entrepreneur that he lent himself for comparison with al-Naser. As put by Stoakes of BP:

Nasser's influence is that of an Egyptian and Arab political leader and the only oil he can hope to control is that of other Arab countries. Tariki's reputation is that of an international oil figure who was mainly responsible for associating the major Arab producers with the other great producing areas; he at one time spoke for a great producing country himself [Saudi Arabia] and hopes, from a position of much greater power, to do so again. Tariki's interests lie with a strong, aggressive OPEC in which he can some day hope to have a predominating voice, whereas Nasser can view OPEC favorably only if he controls a major source of Arab oil, an end to which Tariki is perhaps closer than himself.⁴⁶

While Tariki had an obvious interest in a strong OPEC, he was no longer part of it. During the Congress he criticized it harshly, particularly for its ineffective shuttle diplomacy that was emerging in the new age of the Yamanis and al-Bazzazs. Declaring that he always had a 'soft spot' for OPEC, he accused OPEC governments of having 'degraded themselves by sending their men ... chasing after the oil companies from capital to capital to knock at the companies' door... the companies should be called to Geneva and be dictated conditions.'⁴⁷ Two years later Tariki passed hard judgement on OPEC's achievements in an article published in the *Arab Oil and Gas Journal*. Providing an assessment of the first five years of OPEC, he conceded that the organization had managed to become established but also lamented that it had wasted so much time in studies and negotiations while oil companies continued to accumulate profits (Majallah al-Bitru' wa al-Ghaz al-'Arabi, 1965). During the Fourth Congress, OPEC was also attacked by the late Emile Bustani, the Lebanese entrepreneur who during the First Congress had competed with Tariki in his developmental vision for the Arab world. His paper, delivered by Bustani's daughter after his unexpected death, was highly critical of OPEC's policy to raise oil prices urging producers to capture quickly as high as possible a share in oil production. In essence, Bustani urged Middle East producers to take advantage of their huge reserves of low-cost oil and put the emphasis on volume of sales rather than price.^{48 49}

The open confrontation between Tariki and the Egyptian delegates and the public rift with OPEC prompted large oil corporations to start arguing against sending delegates to the congresses, which they had done since 1959. By 1963 these events had become burdensome for the companies as they were subject to 'public verbal whipping' and 'methods of public prosecution', according to alarmed oil executives.^{50 51} The increasingly uncomfortable position of oil corporations and the unmistakably powerful propaganda emanating from the congresses prompted Stoakes of BP to comment:

Blessed are the meek; by sitting quiet on their uncomfortable chairs and letting division take its course they were pelted with little but token dirt.... They should not, however, believe that the Arabs will ever regard them as other than a convenient evil, or that any patriotic Arab can collaborate with them without a feeling of guilt.⁵²

Making the invisible visible: a new knowledge-based petroleum culture

In January 1962 Sharif Yusuf, the Iraqi director of OPEC's Personnel Department, arrived on an official mission in Umm Sa'id, the headquarters of the Qatar Petroleum Company (QPC). By then an oil town, Umm Sa'id had originally developed on the Qatari coast as the tanker terminal of the rich oil fields of Jabal

Dukhan. It was little over six months since Dr Yusuf, an academic engineer and a training and labor consultant, had left Baghdad to take up a new position at the OPEC General Secretariat in Geneva. Dr Yusuf arrived in Qatar from Saudi Arabia after a visit to Aramco in Dhahran and was on his way to Iran where he was going to inspect oil facilities. He was on a very special official assignment, visiting all OPEC member countries to obtain information on the working and social conditions of the local labor force and on the training methods used in the technical schools run by the companies. During his fleeting visit to Umm Sa'id's hospital, training center and company accommodation, Dr Yusuf enquired about workers' pay, food, transport and recreational facilities. His fact-finding tour of QPC installations involved the exchange of paperwork that was central to OPEC's new mission, the gathering of information and statistics in order to compare the treatment of the indigenous workforce in OPEC member states. Dr Yusuf dished out to QPC's head of personnel a long OPEC questionnaire on labor conditions and duly received copies of the handbook detailing the company's salary structure with pay rates for monthly staff and daily laborers, the two groups that absorbed the majority of non-white oil workers.^{53 54 55}

Dr Yusuf's mission was part of OPEC's policy to gather information on the oil industry in order to challenge the monopoly of technical, legal and statistical knowledge by large corporations, and the exclusive and secretive information order that supported their operations. Besides fact-finding missions such as that of Dr Yusuf's, since 1962 OPEC's Public Relations Department started to collect data on company operations by requesting their official publications and annual reports⁵⁶. Once in OPEC's hands these materials served as a blunt instrument to dissect global patterns of exploitation and fight oil companies on their own turf and break their conspiracy of silence, perceived culture of back-deals and dark machinations. OPEC was trailing the path of other bodies such as the International Labour Organisation, since 1946 a specialized agency of the UN in charge of investigating labor issues and standards, and the Arab League, which in 1956 conducted extensive tours and surveys of oil producers in the Arab world under the aegis of its Petroleum Office. Proposals for the creation of an Arab Petroleum Authority before 1960 also envisaged the creation of a repository of information on the industry that could help governments to negotiate deals and train Arab experts (Burdett, 2004a, pp. 162–163; Lutfi, 1960, p. 82ff).

Tackling the knowledge deficit that marred the industry was an important aspect of OPEC's contribution to the process of decolonization in the first years of the organization's existence. It was one of the strategies used to pursue sovereign rights over petroleum resources, which led to the adoption of the UN Resolution on Permanent Sovereignty over Natural Resources in 1963. The opening speech to the Baghdad meeting by Iraq's acting oil minister Tal'at al-Shaybani already set the tone of OPEC as an organization devoted to scientific research. He declared that the meeting was convened 'to study' the reduction of posted prices in the international markets, the unilateral decision by the companies that triggered the creation of OPEC. Before September 1960 intelligence on plans to create a new forum for oil producers already warned companies that in the future they would be forced to provide detailed 'facts and figures' on their activities. In fact, once established, OPEC was often likened to a petroleum bureau devoted to the study and dissemination of information on the global oil industry. By 1963 its strong profile in this area, and the lack of tangible achievements on the negotiating table so bitterly criticized by Tariki, prompted observers to wonder whether the organization was bound to become only 'a clearing house for research and information.'^{57 58} (Hirst, 1966, p. 144).

The establishment of OPEC's technical department during the second conference of the organization held in Caracas in January 1961 shaped the scientific ethos of the organization. During a press conference held in Baghdad after his return from Caracas, Muhammad Salman declared that the success of OPEC depended on the efficiency of this department. In charge of gathering data, preparing reports and devising practical plans on petroleum prices, marketing, producing, transportation and export it was created in Salman's own words in a manner that ensured 'the rights' of OPEC member states.⁵⁹ Entrusted with submitting recommendations to the OPEC conferences, the technical department was created to feed evidence directly into the setting of OPEC's policies rather than to use this evidence to justify policy

decisions. As stated by Tariki a month after the Caracas conference, the aim was to place oil producers with no qualified expertise ‘in a better position to understand the problems of the oil industry to confront the oil companies with the combined expert knowledge of the OPEC members and to justify or defend their point of view’⁶⁰ (Hirst, 1966, p. 108).

The technical department had quite a broad mandate that covered research on geology, new oil deposits and energy supplies, marketing, concessions, capital investment, and ongoing costs of production, transport and refinement. Legal and academic literature, reports by consultants and firms, and information collected on the ground backed the reports and decisions produced by the OPEC Secretariat.⁶¹ As practitioners, academics and members of special study groups and UN and Arab League’s committees, Arab and Iranian technocrats working for OPEC produced a large number of academic publications, newspapers articles and official reports. Ultimately, the legal sphere was central to OPEC’s dealings with the companies in order to claim back the ‘natural’ petroleum rights of oil-producing nations. To this end, the organization relentlessly promoted the study and comparison of legal regimes that regulated oil concessions in member states.⁶²

The standard of well-informed objectivity, rigor and the desire for centralization of information that animated OPEC was the brainchild of the international elites of the oil world who practiced a new scientific spirit and used horizontal transnational perspectives to pursue their cause (as also discussed in Dietrich, 2017, p. 87). From the perspective of first-generation Arab oil technocrats such as Tariki and Lutfi, OPEC was the practical application of some of the ideas that had animated public debate on oil in the 1950s and culminated with the efforts of the Arab League to spread information about the oil industry, Haliq’s writings and the First Petroleum Congress (Duguid, 1976, pp. 62–90). This age also ushered in the notion that the Arab world needed enlightened public opinion about oil. In order to create this opinion, the industry needed to be made visible and known to Arab governments, elites and populations so that they could eventually shape its future direction. Besides information-gathering, this objective also required the popularization of technical and statistical knowledge about the industry, an endeavor that characterized Arab Petroleum congresses as venues where Arab governments and peoples came in close contact with the industry, eventually – at least this was the hope – shaping their aspirations and strategies.

Both the Arab League as a regional organization and oil technocrats as members of OPEC, representatives of Arab governments or independent oil consultants used the congresses as propaganda events to further the agenda of Petroleum Arabism. The technical and scientific papers on oil-related topics delivered by government officials, technocrats, oil consultants and representatives of operating companies offered experts and the public new ammunition against oil companies. Before the Second Congress, a representative of Aramco presciently forecast that the event was going to provide ‘a corpus of literature on oil subjects which would be found in every Middle East reference library’. Commenting on the outcome of the same congress a BP executive remarked that ‘nothing which was said on the Arab side was new but had not before been presented in such a comprehensive and compelling form either to the public or to the companies.’^{63 64} In the eyes of many Western observers, the ‘emotional’ discourses of exploitation of rights and resources that transpired from many of the papers and debates run against the moderate and measured approach that was expected by technocrats and consultants with technical expertise and Western education.

In reality, some Arab oil technocrats managed quite well to reconcile the passionate undertones of Petroleum Arabism with the technical spirit of the new age by drawing attention to the knowledge and information deficit as one of the main culprits behind the sorry state of the oil industry in the Arab world. In a postmodern anti-Orientalist twist, Haliq bitterly criticized petroleum literature as reflecting the ‘subjective value judgement by outsiders on Arab life and thought’, particularly by so-called Western oilmen. Discussing publications on petroleum trade, Haliq underlined how in the absence of hard data on pricing and marketing the speculative statistical deductions by Arab technocrats and European and Asian

consumers had inevitably favored the disproportionate profits of oil companies. According to him, oil technocrats have a duty to make up for this shortfall by making use of their own skills and the services of foreign oil consultants.⁶⁵ Tariki first initiated this practice very successfully during the First Petroleum Congress. As head of the Saudi delegation, he commissioned a very controversial paper on oil sovereignty from Frank Clifton Hendryx, an American attorney and oil consultant (Dietrich, 2017, pp. 71–72). Tariki's activities were grounded in his core belief that intimate knowledge of the industry, the history of oil companies, their operations and their relationship with markets represented a key weapon in the battle to restore 'Arab Oil for the Arabs'. While remembered for his fiery language, his colleagues at the Centre for Arab Unity Studies in Beirut credited him as having established a school of oil thought (*madrasah fikriyyah naftiyyah*) that helped to popularize oil as a public cause through lectures, oil diplomacy, newspaper and academic articles, and the editorship of the *Arab Oil and Gas Journal* (Mustaqbal al-'Arabi, 1997). Celebrating Tariki's life and achievements in the Lebanese newspaper *al-Safir*, 'Abd al-Rahman Munif, the famous author of the internationally renowned petroleum trilogy *Cities of Salt* and himself an oil technocrat, called him a repository of Arab oil expertise (*bayt al-khibrah al-'arabiyyah al-naftiyyah*). Munif's obituary of Tariki emphasizes the centrality of technical knowledge (*al-ma'rifah al-fanniyyah*) to his activities as oil propagandist who popularized a new oil consciousness (*al-wa'i al-nafti*) (Munif, 1997).

As propaganda occasions engineered by the Arab League, Arab Petroleum congresses were central to the formation of this consciousness and to the display of a new knowledge-based petroleum culture. Al-Naser's political ambitions as a pan-Arab leader unmistakably shaped the First Congress as clearly suggested by the wide circulation throughout the Arab world of official Arab petroleum envelopes and stamps issued by the UAR government to celebrate the event.

Yet during the congress, the technocrats took center stage. They molded claims of ownership of Arab oil that emphasized the need to make the young aware of petroleum benefits, and of the importance of technical and scientific education. Various papers presented at the meeting focused on different political, legal and managerial aspects of the oil industry foreseeing an increasing future role for oil experts from Arab countries. Proposals were also made to include oil resources as a standard subject in school curricula and to standardize the Arabic terminology for oil technical terms (Burdett, 2004b; Stevens, 1959; G. and H. S., 1959). Crucially, the event itself became a forum for public education through a petroleum exhibition, a large event set up at Gezira and covering an area of over five thousand square meters. Taking part in the exhibition were Saudi Arabia, the UAR, Libya, Kuwait and Qatar, with the pavilions of Aramco, Shell, QPC, KOC and several Egyptian oil companies taking the largest share of visitors. Models, posters, photographs and movies narrated to the public the technical world of the oil industry, from extraction and production to marketing. The much publicized visit of President al-Naser took over three hours. Large numbers of primary and secondary schools and technical colleges attended the exhibition and it received considerable coverage in the Arab and Western press and the reports of oil companies⁶⁶ (Risalah al-Naft, 1959; Burdett, 2004c; Burdett, 2004d).

The opening up of oil knowledge to the Arab elites and the disclosure of the multi-faceted world of petroleum to a wider public was one of the successes of both OPEC and the congresses between 1959 and 1964. Yet in spite of evident achievement for its time and the future, some of the protagonists of this remarkable story were made invisible, erased from the public and political memory of oil. The American consultants Hendryx disappeared from the scene soon after he delivered his controversial paper on petroleum sovereignty at the First Congress. In the following years, the text of the paper was hidden from public gaze in a sort of conspiracy of silence that involved companies, oil magazines, journalists and scholars (Hirst, 1966; Boué, 2017). The same kind of deafening silence seems to have descended upon Tariki, whose legacy was forgotten until recently. The opening line of Munif's obituary published in the Lebanese newspaper *al-Safir* reads, 'In silence ... Abdallah al-Tariki has left us.' Munif's piece intimates that Tariki's vision and actions have been erased from public memory because of the challenge he posed to oil interests, both Western and Arab. He credits him with having initiated an Arab political, economic and moral

renaissance by breaking the thick layer of secrecy (*al-takattum al-shadid*) that surrounded the industry (Munif, 1997). With Munif's tribute in mind, the American academic Robert Vitalis also treats Tariki as one of oil's casualties. He laments, 'In a better world we would find statues of him in public parks, if not in Dhahran, then in Algiers, Beirut, Cairo and Kuwait City. Streets and schools in the Arab world would be named after him.' (For Vitalis' article, see Al-Sayf, 2007, p. 456).

Conclusion

In spite of the tensions between Egypt and Iraq, the period 1959–1964 should not be remembered as a time of confrontation and conflict in the Arab world. In petroleum terms, this was a period of rapprochement and dialogue between oil technocrats, governments and foreign companies. The interplay between OPEC and the Arab League, and the agency of those Arab oilmen who shared common platform in these organizations, was instrumental in the creation of new political and public cultures of oil throughout the region, mediated by the new international climate of decolonization. These cultures evolved around a discourse of petroleum rights that coalesced into Petroleum Arabism, an expression of resource nationalism that on the one hand advocated new policies for the management of the oil industry and on the other promoted the formation of a new oil consciousness shaped by a knowledge-based petroleum public sphere. This process of consciousness formation was the result of the vision and efforts of Arab Oil technocrats who used a variety of mediums: from diplomacy and the written word, to public oration and exhibition display. They endeavored to penetrate the thick layer of secrecy that until the early 1950s had surrounded petroleum expertise and to divulge the facts and figures of the industry to a wider public in order to overcome the doubt and mistrust that for decades had surrounded oil extraction. As voiced by the moderate Bazzaz in 1964 at the opening of OPEC negotiations with IPC, this doubt and mistrust was partly the result of the secrecy and unpredictability with which the oil industry was associated and created a 'fear for the future' that could only be countered by efforts to restore confidence on both sides.⁶⁷ While al-Bazzaz's clearly had in mind the example of Iraq, his words had broader resonance for the region as a whole.

Notes

- 1 Although from a different viewpoint, Duguid fundamentally agrees with Citino by arguing that the formation of OPEC accentuated the political divisions between Arab Oil Technocrats and represented a victory for governments (Duguid, 1976, p. 107).
- 2 This is in line with Hertog's arguments about rentier state formation, which he formulated over a decade ago (Hertog, 2007). For an earlier critique of the rentier state approach in relation to urbanism and urbanization in the Arab states of the Persian Gulf, see Fuccaro (2001).
- 3 Middle East Economic Survey, 16.09.1960.
- 4 *British Petroleum (BP) 163727* (1960b). Baghdad Petroleum Conference. Memo IPC Baghdad to London, 10.09.1960.
- 5 *Al-Mabda'*, 15.09.1960.
- 6 *Ittihad al Sha'ab*, 15.09.1960.
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Saudi Arabia's role in OPEC's evolution

OPEC and the global energy order from its origins to the present time

Majid Al-Moneef

The relationship between the Organization of Petroleum Exporting Countries, OPEC, and Saudi Arabia and their respective roles in the international oil market have dominated the literature on OPEC's behavior since 1974 until today. Commentators and market watchers continued for decades to emphasize the dominant position of Saudi Arabia in OPEC since its inception. This role is derived from its weight in OPEC's reserves and overall production and exports, the relative stability of its supplies throughout and its readily available excess production capacity to mitigate supply interruptions. The relative political stability of Saudi Arabia was reflected among other things in the consistency of its oil policy and the longevity in office of its oil ministers, which contributed to the effective utilization of its role in OPEC and the market.¹

A whole line of economic literature used the dominant firm hypothesis to model OPEC behavior, postulating that Saudi Arabia either alone or in association with its Gulf partners dominated OPEC's pricing and production decisions. Another line of research used the game theory approach to model Saudi Arabia's relations with the other members in devising the latter's role in the market. Others sought to emphasize the political factors contributing to Saudi Arabia's decision-making process within the Organization.²

Needless to say, as the market evolved over the decades, so did the Saudi position and role within OPEC, the effectiveness of the organization and the Saudi policy approach to it. However, such a role was also influenced by its political relations with the other members, the market environment, the international political scene and Saudi Arabia's internal politics. At different critical market junctures, Saudi Arabia's role was critical, beginning with the events contributing to the birth of OPEC and the process of building the organization during its early years, its assumption of market management role in the seventies, its declining market power in the eighties and its re-established market role since the beginning of the 21st century.

The events leading to the creation of OPEC

It has long been established that OPEC's creation resulted from the interplay of different political, economic and energy relations. On the political side these were the struggle for independence after WWII, the Cold War polarizations, the creation of Israel in 1948, the Suez Canal crisis of 1956, the overthrow of the Egyptian and Iraqi monarchies in 1952 and 1958, the spread of Arab nationalism and the struggle for

democracy in Venezuela. On the economic side, these were the relations of the post-WWII reconstruction of Europe and Japan and the economic boom that followed, the spreading of a government-led growth model resting on Keynesian economics and the growing appeal of the 'Unequal Exchange' theory of the Latin American school of development, which also influenced the establishment of UNCTAD. There were also many oil-related factors that contributed to the environment that brought birth to OPEC. These were the Iranian oil nationalization and its subsequent foiling after the companies boycott of that oil and the US/British-sponsored coup that reversed the nationalization 1951–1953, the resentment in the Middle East and Venezuela towards the old concession arrangements, the growing oil nationalism and the debate over the sovereignty over natural resources in the fifties and sixties, the growing importance of oil in energy, economic growth and geopolitical relations, the increasing importance of the independent oil companies, undermining the market domination of the big majors of the so-called 'Seven Sisters' and the changing patterns of global oil supply.³

After WWII, the Middle East and Venezuelan oil came to dominate global supply. Their combined production jumping from 1.4 million barrels per day (mb/d) right after the war to 8 mb/d in 1960 accounting for half of the growth of world oil production over the 15-year period. As Table 3.1 shows, Venezuela's production increased threefold and that of the Middle East tenfold, to contribute to the total increase in global world production estimated at 13.8 mb/d between 1945 and 1960. The concession systems in both regions, which were devised when the host countries were disadvantaged politically and economically, were so generous to the concessionaires that it allowed many independent oil companies outside the international cartel to enter the business, offering more attractive terms to governments and as a result competing with the majors for markets. The governments of the region, realizing the demand and supply patterns, the post-WWII economic, political and oil relations and their dire need for revenues to implement their ambitious development and modernization programs, pressured the operating international oil companies to modify the original concession agreements to account for the changing political environment. Their demands concentrated on changing the unfavorable fiscal terms of the concession agreements, the free-hand concessionaires' operations and the conditions of the local workforce and communities. Such demands soon become rallying points for the people, the technocrats and the opposition in these countries.

The socioeconomic and political development of Saudi Arabia after WWII was influenced by the underlying global and regional political, economic and oil-related factors mentioned above. However, there were Saudi-specific factors that shaped its political and economic orientation as well as its oil policy. First, unlike all the other oil-producing countries of the region, it was united through long internal struggles and not subjected to colonial or semi-colonial rule. This was reflected in the government-concessionaire relationship, which was not as politicized or tied to the relationship with the colonial power as other countries of the region. Second, the exclusivity of the American interests exemplified in granting

Table 3.1 Historical evolution of world oil production (million barrels per day mb/d)

	<i>ME & Venezuela %</i>	<i>World</i>	<i>United States</i>	<i>Russia</i>	<i>Venezuela</i>	<i>Middle East</i>
1940	13	5.9	4.11	0.596	0.508	0.260
1945	20	7.1	4.69	0.408	0.885	0.512
1950	31	10.4	5.41	0.729	1.500	1.723
1955	35	15.4	6.81	1.400	2.160	3.210
1960	38	20.9	7.04	2.940	2.760	5.220
1970	37	48.0	11.30	7.100	3.700	13.900

Source: Jenkins, 1989.

the concession in 1932 to the American Standard oil of California (SOCAL and currently Chevron) and its evolution to a consortium of four 'Major' oil companies in the concession. The granting of the concession, without the United States government involvement or even diplomatic presence in the Kingdom, gave it strength after WWII when the latter became the world's superpower sidelining the old colonial powers, Britain and France. This was evident when the U.S government debated during the war the option to acquire a controlling interest in the concession, which the companies foiled at the time. It was also evident when those companies, with U.S government approval, were the first to agree to the profit-sharing amendment to the concession with Saudi Arabia in 1950 that resulted in revenue gains to the Saudi treasury, allowing others in the region to follow. Third, the realization of the great potential of the Saudi oil especially after the discovery of super-giant oil fields and the construction of the pipeline (TAPLINE) to transport Saudi oil to the Mediterranean.

The international, regional and county-specific dynamics were all signaling that the old relations with the great powers as well as the oil concessions were in a state of flux. They also signal the emergence of new technocrats who came to influence the development and oil policies of their countries considerably. They saw their countries further integrating into the international economy through oil and recognized that the development potential of their countries will have depended on the conduct of the oil relations. In Saudi Arabia, Abdullah Al Tariki came to symbolize those technocrats during the years leading to the establishment of OPEC.⁴

The Arab Petroleum Congress organized by the Arab League and first convening in Cairo in 1959 witnessed the manifestation and reflections of such political developments and sentiments into the oil relations. Nasserist Egypt, assuming then its leadership role in the Arab World and the Arab League, used the Congress to promote its pan-Arabism and nationalist agendas, including calls for the nationalization of the oil interests in the region. At that time, the governments of the oil-producing countries of the region had different agendas to Egypt. Their focus was mainly on engaging the concessionaires to modify the fiscal terms of the oil concessions, change the mechanisms oil price setting and adjust the government-concessionaire relation taking account of the sovereign rights of the state.

In adopting the negotiated approach to modify the concession terms rather than the confrontational one promoted by Egypt, the oil-producing governments and its technocrats were influenced by the ill-fated Iranian oil nationalization of 1951 and the struggling Mexican nationalization of 1938, as both faced concerted boycott from the then dominating international oil companies, reversing the first and constraining the other. They also had made few fiscal gains and better control over the companies' operations and relations with the communities and workers in the early fifties through negotiations. The technocrats and nationalists in those countries, mostly educated in European, Egyptian and U.S universities or coming from the ranks of the operating oil companies, aligned themselves with the governments and used the power of the state and of local cadres in the oil industry to advance such an agenda locally and in the international and regional arenas.

The first Congress was particularly important for OPEC's birth and Saudi Arabia's role. The event was attended by Venezuela and Iran as observers and saw the first meeting between the minister of mines and hydrocarbons of Venezuela in a newly elected government, Perez Alfonzo, and Abdullah Al Tariki, then head of the Directorate of Oil and Mining Affairs of the Ministry of Finance of Saudi Arabia, and in charge of government/oil company relations as well as international and regional relations. Both Perez and Al Tariki headed their respective countries' delegation to the Congress. The Congress was chaired by Mohammad Salman, an Iraqi then director of the Petroleum Bureau of the Arab League, with Al Tariki as co-chair. On the sidelines of the Congress and initiated by Venezuela a secret meeting was held involving Salman, Tariki and Perez as well as the representatives from Iran and Kuwait. The meeting agreed to what came to be known as the 'Maadi Pact' in reference to the yacht club hosting the meeting. The parties to the pact identified five common issues proposed mainly by Venezuela that their countries had with the operating international oil companies and set up an 'Oil Consultative Committee' to follow up on these issues⁵:

- 1 Improvement of contractual terms and the requirement for consultation on price changes
- 2 An integrated approach to oil industry operations
- 3 Increasing refining capacities in the host countries
- 4 Establishment of national oil companies
- 5 National coordination of the conservation, production and exploitation of oil resources.

The Congress also witnessed an articulate critique that initiated intense debate on the oil concessions from the American lawyer Frank Hendryx, then advisor to Al Tariki and legal councilor to the Saudi Directorate of Oil, in which he invoked the sovereign rights of nations to modify the oil concessions under the principle of changing circumstances, arguing that ‘An oil producing nation, by the law of civilized nations may clearly, in a proper case, modify or eliminate provision of an existing petroleum concession which have become substantially contrary to the best interests of its citizens.’ The overall event and what transpired afterwards put Saudi Arabia and Al Tariki center stage in the oil relations that followed.⁶

The Saudi role in the developments leading to the creation of OPEC

The events leading to the creation of OPEC in 1960, and the role of Al Tariki in building the momentum towards that, relying on the outcome of the Maadi Pact and on his shared views with Perez Alfonzo, are all well documented in the literature. The posted price cuts (of less than 10 percent) through which the government’s share from the revenues is calculated, first announced by Esso (now Exxon) on 9 August 1960 and followed by other companies, was identified in the literature as the trigger that prompted Al Tariki to lead the coordination to invite the founding members of the organization to Baghdad the next month. The literature also documents the intense negotiation during the founding meeting in Baghdad to secure Iranian approval for establishing OPEC, against its preference at the time for a loose coordination mechanism. The idea of forming a united front of producing governments vis-à-vis the international oil companies was ultimately shared by all the founding members. However, production rationing, which was central to Alfonzo’s thinking and shared by Al Tariki, emulating the US production rationing experience of the ‘Texas Railroad Commission’, was not preferred by Iran at that time.⁷

One of the other issues that influenced the process was the dynamics of the ‘Arab Cold War’ of the fifties and sixties. Although OPEC’s roots go back to the Maadi Pact, the Saudi preference to hold the founding meeting outside Egypt, and not under the auspices of the Arab League, aimed to distance the process from complex inter-Arab politics. Al Tariki, known to be an Arab nationalist and supporter of Egypt’s Nasser, negotiated the convening of the foundation meeting of OPEC in Baghdad, then a political rival to Cairo. By doing so he seemed to be more influenced by his technical background in government/company relations than his political ideology. He also seemed to be in line with the shifting political alliances of his country and eager to deliver to its leadership some tangible results on the oil front. Years later, Saudi Arabia would again bypass the Arab League and Egypt when orchestrating the establishment of the Organization of Arab Petroleum Exporting Countries (OAPEC) in 1968, with Kuwait and the monarchical Libya as co-founding members.

The enactment of the profit-sharing agreement with Aramco in the early fifties increased the government’s oil revenues, but the absence of credible fiscal institutions and budgetary procedures for the disposal of such revenues led to uncontrolled spending, mounting debt, devalued Riyal and the denial of credit to the Saudi state. This coincided with the spread of Arab nationalism and the complexities of the Cold War, to which King Saud aligned temporarily with Egypt’s Nasser due to concern over Hashemite’s Iraq and the controversial security arrangements of the Cold War era, known then as the ‘Eisenhower Doctrine’ and the ‘Baghdad Pact’. This alignment lasted until 1958 and started to crumble, straining relations between Saudi Arabia and Egypt for more than a decade. These all worked in the background of the rivalry between King Saud and the crown prince and later King Faisal throughout the former’s reign. This shifting

political alignments, the different rivalries within the ruling family, the fiscal crisis of the state and the spread of Arab nationalism provided opportunities for young technocrats like Al Tariki to pursue their reform and modernizing agenda which each faction of the royal family aligned itself with. For example, he negotiated different changes to the fiscal and operational terms of Aramco's concession, and a favorable concession agreement with a Japanese concern in the offshore Neutral Zone.⁸

In this context, one can understand how Al Tariki, being only a director of division within the Finance Ministry, was able to maneuver – whether in signing the Maadi Pact or his immediate response to the unilateral oil price cut in 1960 and his shuttle travel between Baghdad, Beirut and Kuwait ending in the establishment of OPEC. He must have had the blessing of the king or/and crown prince or might have benefitted from the decision vacuum created by internal rivalry, or both. But in either case, his response ascertained Saudi Arabia's leading role in the creation of OPEC.

Saudi role during the early years of OPEC

Right after the creation of OPEC in September 1960, the internal struggles in Saudi Arabia culminated in King Saud assuming full control, heading a new cabinet in December of that year that included some technocrats known for their nationalist leaning, including Al Tariki as the first minister of the newly created Ministry of Petroleum and Mineral Resources. While this seemed to have given Al Tariki room to pursue his domestic agenda vis-à-vis Aramco and his international agenda through OPEC, the political situation in Saudi Arabia and the region was far from stable. Growing public concern about the impact of the royal division on the country's stability and security, the inability of the new government to deal with mounting internal and external challenges and the deteriorating health of King Saud weakened his power grip and forced him to hand over the government to Faisal, who headed a new cabinet, dismissing Al Tariki after 13 months as minister and appointing instead a lawyer and close associate, Zaki Yamani.⁹

Al Tariki, attending as minister the first and second conferences of the organization he helped create, departed from the political scene of Saudi Arabia forever and chose self-exile and oil consulting services in Beirut, giving advice to many governments except his own. The transfer of power in Saudi Arabia also signaled a distancing from Nasserist Egypt and an end to the tense relations with Aramco, toning down the nationalist fervor and redesigning the relation with OPEC. The first sign of the latter was the reversal of Saudi Arabia's support for Alfonzo's production programming within OPEC, citing sovereignty and its impracticality.¹⁰

Yamani proved that the departure of Al Tariki did not impact on Saudi Arabia's leading role in the organization. His negotiating and communication skills and the trust of King Faisal enabled him to pursue his predecessor's objectives differently. Internally he went on to build a national oil industry by creating Petromin to be the petroleum and industrial arm of the state and the College of Petroleum and Minerals (CPM) as the higher education vehicle to develop national talent for the oil and industrial sectors; he also continued negotiations with Aramco to clear some outstanding fiscal and operational issues. Internationally he preferred a negotiated rather than confrontational approach to the oil companies. During the period 1961–1973 when OPEC acted as a collective bargaining instrument to counterbalance the collective power of the companies, Yamani asserted the Saudi position of negotiating with the companies on three issues that OPEC came to deal with: royalty expensing and marketing allowance, oil nationalization vs. participation, and oil pricing.

The royalty expensing issue was raised by OPEC right after its creation, noting that the companies operating in the Gulf, unlike in Venezuela, credited royalty payments to the governments against their obligated income taxes. The demand to end such a practice implied an increase in the revenues to the Middle East members of OPEC, as would ending the marketing allowance. While from a legal perspective this issue is more country specific, OPEC chose it as its first encounter with the companies. This also signaled a dilemma that would face OPEC throughout, to harmonize the collective negotiating position with

the national objectives of members. After six years of collective and bilateral negotiations with the companies and differences among the members on the matter, royalty expensing was achieved resulting in a modest increase in the revenues of the concerned members. Saudi Arabia's role in the royalty expensing process was marginal since the first secretary general of OPEC, the Iranian Fuad Rouhani, led the negotiations on behalf of the members.

The other issue that divided OPEC in its early days was putting the nationalization of the international oil interests in member countries on the organization's agenda. The issue was put forward by Iraq but objected to by all other members. It was for Yamani to take the lead in opposing it and articulating in a lecture in Beirut in June 1968 the more gradual form of 'Participation'. A principle adopted by OPEC later that month in a resolution that came to be known as the 'Declaratory Statement of Petroleum Policy in Member Countries', incorporating nine principles, stated that 'the governments may acquire a reasonable participation in the ownership of the concession-holding company on the grounds of the principle of changing circumstances'. But the process was not put into force until 1971 when OPEC set up a ministerial committee headed by Yamani to draw up the basis for the 'effective participation' with the Middle East members of OPEC (Abu Dhabi, Kuwait, Qatar, Iran and Iraq), empowering Yamani to negotiate on their behalf, since the other members had different plans then. While one understands why the first three countries delegated Yamani to negotiate on their behalf on such a sovereign issue since they shared the same perspective, the decision of Iran and Iraq, considering their disagreement with Saudi Arabia on many oil issues, was problematic. The only explanation is that they perceived that any concession that Yamani could get from the four powerful American companies comprising Aramco would be better what they might get from other approaches they were contemplating. Ultimately, after realizing the position of the companies in the early rounds of negotiations, the two countries withdrew from the process, limiting it to the four Gulf countries, which after arduous negotiation and positioning concluded the 'General Agreement on Participation' towards the end of 1972, whereby the four governments would start owning 25 percent of the oil assets in each, escalating to 51 percent in 1981.¹¹

The agreement included different complex and controversial issues such as the valuation of the assets, the marketing of the participation crude and its pricing, as well as the degree of control. But the agreement was criticized on different grounds, the strongest of which was that the agreement came too late, with too little and with high compensation. The first blow was its rejection in July 1973 by the Kuwaiti parliament, which renegotiated and in May 1974 got 60 percent initial participation from its concessionaire companies, followed by Qatar, Abu Dhabi and then Saudi Arabia. Although Saudi Arabia championed and led the participation negotiation, the outcome embarrassed Yamani personally and undermined Saudi Arabia's leadership role in OPEC and among its Gulf allies. The oil market dynamics, the political developments regionally, and the options before the countries and the companies all seemed to have changed dramatically during the negotiation, which Saudi Arabia seemed to brush aside. Other non-Gulf member countries such as Libya and Algeria nationalized their oil interests without the dire consequences feared by Yamani, while others such as Nigeria and Indonesia got better participation terms and lower compensation than the ones suggested in the participation agreement.

The third issue dividing OPEC and which continued for decades was oil price determination. During 1970–1973 there was a fundamental difference among members as to how to achieve higher revenues from oil, with Venezuela pushing for production programming as a means to maintain or increase oil prices, while all the others preferred a negotiated approach with the companies to increase the companies' set 'posted price'. Capitalizing on its location near the European market, the quality of its crude and the weakness of the independent oil companies operating in Libya, the new military regime that overthrew the monarchy in September 1969 initiated negotiations with the companies and by end 1970 had achieved an oil price increase for Libyan oil as well as an increase in the tax rate to 55 percent. Such price and tax increases were possible due to the above factors and to Libya's cutting production as means to pressure the companies. The Libyan gains soon initiated collective negotiation between the oil exporters of the Gulf

and the Mediterranean on the one hand and the companies on the other to adjust the prices of their crude in line with this. Both came to be known in the annals of OPEC as the 'Tehran and Tripoli' agreements, concluded in February and April 1971 respectively. Soon after that the U.S unilaterally abandoned the convertibility of the dollar to gold, reducing the value of the latter vis-à-vis other currencies and subsequently reducing the purchasing power of the negotiated oil price in Tehran and Tripoli. This led to other rounds of negotiation between OPEC and the companies to compensate for the dollar's decline and inflation rise, indexing the oil price to a basket of currencies known in the annals of OPEC as the 'Geneva I and Geneva II' baskets.¹²

Although Saudi Arabia was party to both agreements since it exported from the Mediterranean and the Gulf, it did not lead the negotiations resulting in the price increase. That was left to Iran and Libya in the two respective agreements. Aside from its role in the participation process, which had its setbacks, Saudi Arabia did not exercise a leadership role in OPEC during the 1962–1973 years. This was due to its pre-occupation with regional issues such as the Yemen war and the polarization of the Arab Cold War. Its influence over the organization during this period was limited to directing it to pursue a negotiating and conciliatory rather than confrontational approach towards the companies. Its leadership of the participation process, besides being consistent with its political and economic ideology, could also be looked upon as its response to the ideology of Arab nationalism, manifesting itself in the calls for nationalization of the oil interests. Its contribution to OPEC during those years was its ability (through Yamani) to pursue a consensus-building approach and distance OPEC from the inter-Arab conflicts.¹³

OPEC ascendance and Saudi prominence

The events leading to OPEC's ascendance in 1974 could be traced to its ability in the early seventies to wrestle control from the companies through the privatization process, the nationalizations as well as the Tehran/Tripoli agreements. They could also be traced to the almost doubling of world oil demand and to OPEC's production increasing three times between 1961 and 1973. The entry of new independent oil companies and the proliferation of new forms of company/government oil arrangements, different from the old concession agreements, further weakened the bargaining position of the major international oil companies vis-à-vis the governments and undermined their market dominance. When hostilities erupted in the Middle East following the Arab-Israeli war of October 1973 and spot oil prices surged, OPEC and the companies met to negotiate new prices. When they could not agree, OPEC decided that the selling price of oil was a sovereign matter and it assumed its determination irrespective of the consent of the international oil companies. Within a few months in late 1973 and early 1974, official selling prices followed the spot prices, increasing more than fourfold in response to the imbalance created by the production cuts exercised by the Arab members of OPEC and the panic resulting from the Arab oil embargo against the US for its support for Israel in the war. From then on, OPEC controlled production and price setting and a new era of its dominance started. This brought in new sets of contradictions in its market management role and conflicts within its ranks or with the major importing governments, since the international oil companies were either sidelined or struggled to secure supplies mainly from OPEC sources.¹⁴

The dramatic change in Saudi Arabia's oil policy during the war by leading the boycott and the production cutback warrants an explanation. Its long-held position of resisting the Arab nationalists' slogan of using the oil as a political weapon was well known. So, taking the leadership role was problematic. First, the Egyptian-Syrian war against Israel to liberate their occupied lands since 1967 was popular throughout the Arab world and calls for the use of the oil 'weapon' to force Israel to cede occupied territories and find a solution to the Palestinian problem intensified. Saudi Arabia could not ignore that sentiment. Second, after decades of confrontation with Egypt during the Arab Cold War, Saudi Arabia forged an alliance with the post-Nasser regime in Egypt and was keen to strengthen this.

Once OPEC took control of price setting, it inherited the fixed price regime from the international major oil companies. These were able to administer it for some forty years because the crude oil was sold to their affiliates with little left for sales to third parties, the posted price being just a reference price to pay taxes and royalties to the producing governments. Surprised and seemingly unprepared for the task of managing the market as a cartel of sorts, OPEC chose to fix and periodically adjust the price of the 'OPEC marker', which was then Saudi Arabia's Arab light crude, being the mostly traded crude in the three main markets – Europe, the US and Japan. After agreeing to the price level of the marker, the prices of the other crudes were determined through agreed differentials to the marker, reflecting gravity, sulfur content and freight. The production needed from each member under that price and its differentials was left to the market to determine. Needless to say, determining the price level of the marker and its differentials turned out to be contentious.

OPEC behavior and dynamics were put into the international political, economic, and media spotlights after it took the price administration role. Saudi Arabia by virtue that its main export crude became OPEC's marker, and its production weighted within OPEC, averaging one third of the group's production between 1973 and 1982, became the de facto leader of the newly emerging OPEC. The economic literature modeling OPEC behavior during that period considered it either operating in an oligopolistic market along with a competitive fringe (non-OPEC) or a monolithic price setting, two blocks or a Saudi-dominated cartel. Other strand of the literature focused on the political, institutional and negotiating strengths of its members in explaining the different junctures of OPEC pricing decisions during its ascendancy.

The price regime under which OPEC operated, as well as Saudi Arabia's production and export potential, gave the latter a leadership role with all its attributes. First, OPEC could not set or adjust the level of its marker price without Saudi consent, and that price could not be maintained without proper Saudi production enforcing it. Second, the level of the marker price and its differentials would result in world demand and supply responses, with most of OPEC's gains or burdens borne by its dominant producer. Third, although differentials to the marker were agreed upon based on detailed models, the selling prices of the other crudes oftentimes did not follow the agreed differentials, contributing to the under- or overpriced Arab light, with all the consequential export adjustment needed by Saudi Arabia, making it the 'swing producer' of the group, years before that term came to characterize Saudi behavior. For example, when OPEC's production declined by 3.5 mb/d in 1975 due to the world recession and non-OPEC production increase, Saudi Arabia's share of such decline was 40 percent, and when OPEC production recovered by 3.8 mb/d in 1977, Saudi Arabia's share of which was 58 percent. During 1978–1980, its production increased by 1.7 mb/d to compensate 63 percent of the production decline of Iran and Iraq of 2.7 mb/d resulting from the revolution in the first in 1979 and the war between the two in 1980.¹⁵

The agreement on the level of the price of the marker turned out to be a contentious issue all through. Saudi Arabia, realizing that supply-demand responses to the price would be felt in the longer term, particularly on its production potential, stood against the demands of the other producers for further price increases. Such showdowns led at one point to two-tier OPEC prices: when OPEC's December 1976 conference ended up with Saudi Arabia and the UAE increasing their official prices by 5 percent and the others by 10 percent, this price split lasted six months before being unified. The other contentious issue was the agreement on and adherence to the price differentials, which often appeared during oil gluts when other members were able to undercut the marker price.

The price of OPEC marker that stood at three dollars when the October 1973 war broke out, jumped to \$5.12 late that month and \$11.65 at the end of the year. It changed marginally, reaching \$14 in 1978, in the midst of continued split within OPEC ranks on the level of prices between what came to be known then as the price moderates led by Saudi Arabia (sometimes aligned with other members) and the price hawks (led by Iran often aligned with Libya, Iraq and Algeria). That period was characterized by widespread predictions of impending oil supply crisis and rising world dependence on OPEC oil, more so from

Saudi Arabia. The interruption of Iranian production in early 1979 and of the Iranian and Iraqi supplies in the fall of 1980, following the Iranian revolution and the outbreak of the Iran-Iraq war, reinforced such dire predictions. Following the two crises and the removal of some 2.3 mb/d from the market, panic oil buying led to escalating prices in the spot market, in which many OPEC members were active, which started thin but gradually expanded. Saudi Arabia's production adjustments to fill the supply gap resulting from the two crises did not seem to arrest the price escalation. OPEC incorporated these crises driven by spot-determined prices into its official prices, increasing the marker price ten times in successive meetings during 1978–1981, reaching \$34 in October 1981.¹⁶

The predictions of rising global demand, limited non-OPEC supply and increasing requirements from OPEC, which contributed to the panic buying largely for commercial and strategic stockpiling in OECD, turned out to be exaggerated. Demand declined by 3 mb/d between 1979 and 1980 and a further one million mb/d decline the next year; OPEC production declined by 4 mb/d in each of the two years as a result of declining demand and increasing non-OPEC supply. It was clear that the price increase of 1973/4 and even more that of 1979/80, as well as the energy programs of the OECD countries grouped after the first oil crisis under the International Energy Agency (IEA), had worked their way through and caused the changes in oil consumption and non-OPEC supply. Although part of the demand response was due to the price increases and the resulting economic slowdown, most of the other changes were of long-term duration. Enacting policies to promote energy efficiency, diversifying energy sources and oil supplies and building strategic petroleum stocks were all structural factors. This ultimately led to a declining OECD oil intensity, measured as oil consumption per unit of GDP, from an average two barrels during the seventies to 1.3 barrel per 1000-dollar GDP (in constant terms) in 1985. Globally, oil demand was declining by an annual average of 0.8 percent, and while OECD economies grew by an average 2 percent annually, their oil demand declined by an average 3 percent annually between 1979 and 1985. On the supply side, non-OPEC supply increased by 6 mb/d, half of which was from Mexico and the UK. This ultimately resulted in a decline of OPEC production by more than 10 mb/d, absorbing the demand drop and non-OPEC production increases during the period, with Saudi production decline accounting for 70 percent of that.¹⁷

What was known as the 'OPEC golden era' came to an end in 1981 with the declining world oil demand and OPEC production and the pressure on OPEC's price structure. The role of Saudi Arabia during this eight-year period of OPEC ascendance was instrumental, whether through leading the Arab oil production cuts until late 1973 that triggered the price rise and OPEC's assuming the price administration role, or through its price preferences and advocacy in OPEC and its production policies the following years. Its leadership in OPEC was manifested in the emergence of its minister Yamani as the de facto spokesman and defender of the organization during the years of mounting political and media campaign directed against it, especially in the US.

The role of Saudi Arabia during OPEC's declining power

While it was clear that the demand and supply responses starting in the mid-seventies and accelerating in the early eighties were structural in nature and long in duration, OPEC seemed over-confident of its market power. Either not realizing the impact of the high prices on demand and supply or not being able to separate the economic and the political needs for high prices on the one hand and the sustainability of such prices and the market responses to them on the other. In such an environment, OPEC continued to defend the crisis-driven prices in the face of fierce competition from new production in the North Sea, Mexico and elsewhere that was not bound by OPEC-set price levels or differentials. The early eighties saw increasing spot sales at favorable prices for crude closer to the consuming markets versus predominantly term sales at higher official prices from the Gulf. In this 'buyer's market', spot sales were estimated to have grown from less than 2 percent of globally traded oil to more than 30 percent in the mid-eighties,

involving not only non-OPEC producers but also OPEC members, the former responding to competition from the North Sea in Europe and the latter to competition from Mexico in the US as well as spot sales from Iran.

Faced with the glut in the market, OPEC adjusted its fixed pricing policy by adopting ceiling and quotas to defend the higher price, acting for the first time according to a textbook cartel. However, in doing so, it ignored the contradiction inherent in fixing both prices and volume. This happened in theory anyway, since countries seldom abided by their agreed quotas or sold under the set official prices. Although by definition OPEC was the 'residual oil producer' providing the difference between world oil demand and non-OPEC supply, Saudi Arabia acted over 1982–1985 as the 'swing producer' of the group – that is providing the difference between world oil demand on the one hand and non-OPEC supply as well as the rest of OPEC supply on the other. In a period of declining production needed from OPEC, the swing producer would have absorbed the brunt of OPEC's supply adjustment. While OPEC's production declined by 42 percent (32 percent excluding the production from Iraq and Iran, which were then at war) from 26 mb/d in 1980 to 15 mb/d in 1985, Saudi Arabia's production declined by 68 percent, from 10 mb/d to 3.2 mb/d during the period, reaching a low of 2.2 mb/d in July 1985. The decline in oil revenues was asymmetrical: OPEC's declining by 48 percent while Saudi Arabia's by 75 percent between the two years. The contribution of Saudi Arabia to OPEC's production and revenue decline were 70 and 60 percent respectively. The Saudi production decline was due to the adherence to the fixed official prices, prompting buyers to turn to discounted crudes from elsewhere.

It is unclear why Saudi Arabia willingly accepted shouldering such a burden and consequently losing market share and leverage in OPEC. When OPEC was forced in 1982 to consider pro-rationing amid the market glut, it adopted during its extraordinary meeting on 20 March that year for the first time a 17.5 mb/d ceiling and production quotas, maintaining the fixed official price of \$34 per barrel. Saudi Arabia refused to be assigned a quota in the overall ceiling in line with its long-standing opposition to production programming. It announced a self-imposed production of 7 mb/d, lower than the calculated 'quota' of 7.5 mb/d. It reiterated this further at the March 1983 OPEC meeting, when no quota was assigned to it under the same ceiling (but a lower market price at \$29 per barrel), implicitly agreeing to balance the 'market requirements' for OPEC crude. However, such requirements were then lower than the ceiling, leading its production to settle below the self-imposed production of 7 mb/d as well as its later quota of 5 mb/d. Its actual production ended up even lower at 4.5, 4.1 and 3.2 mb/d respectively in the 1983–1985 period.

Further aggravating its position, Saudi Arabia's pronouncements seem to suggest that demand, non-OPEC production changes and pressures on the fixed price regime might have been reversed in the medium to long term. However, the pressure on oil prices continued despite lower production from OPEC, forcing it to adjust its market price downward by six dollars during the period. This price decline did not impact on either the pattern of declining demand, especially in OECD, or the increasing non-OPEC supply, the first actually declining by 1.7 percent annually and the second increasing by 2.5 percent annually 1980–1985. The ongoing Iran-Iraq war of the time, tense political relations between Saudi Arabia and Iran and the intensity of the competition between North Sea and Nigerian oil made the prospect of changing the price structure or reaching any meaningful compromise within OPEC even more difficult.

The market pressures were immense: OPEC had lost its commanding share in the market, its obituaries in the international media were common and Saudi Arabia's balancing act could not effectively maintain the organization's role nor its influence within it. By August 1985, Saudi Arabia's production at 2.2 mb/d and exports at 1.4 mb/d had reached their 1960s levels. Declining Saudi production impacted its leverage within OPEC as well as its revenues and growth potential. The situation was so critical that the future of the petrochemical sector, considered then the backbone of the Saudi industrialization strategy and relying then on the associated gaps arising from the production of crude, became questionable. All this brought

home the consequences of an otherwise international aspect of the petroleum policy of Saudi Arabia that remained uncontested locally for some 25 years under the leadership of a technocrat who had enjoyed the political backing of three successive kings.

Mounting domestic pressures and the seemingly ineffective official pricing policies prompted Saudi Arabia to change its market strategy and relationship with OPEC. It chose to regain market share from fellow OPEC members as well as non-OPEC producers through 'netback' pricing, to induce buyers to prefer Saudi crude by linking the FOB prices of its crude types to their CIF product price realization. The arm's length netback pricing contracts, between the agency (or company) of the producing country and the buyer, tied the price of a barrel of its crude exports of different qualities to the gross product worth of the refined products from each crude weighted by its refining yield in the refinery minus the transportation cost to the refining center, as well as the costs of refining it and an agreed margin to the refinery. As such, each contract would include agreement to each parameter mentioned above, inherent in which are many tradeoffs for both buyer and seller.¹⁸

Because it was the first to initiate this approach, Saudi Arabia was able to regain its market share and almost double its production in a few months, getting a \$27.7 price for its Arabian light crude in the second half of 1985, which was slightly lower than the \$28 official price at the time. When other OPEC producers entered into the competitive foray using similar netback pricing methods, the buyers had the upper hand when negotiating such deals, thus undermining the competitive edge of netback pricing. And when OPEC, upon Saudi urging and earlier market positioning, took a decision at its December 1985 meeting to 'secure and defend for OPEC a fair share in the world oil market consistent with the necessary income for Member Countries' development', the market took that as sign of free-for-all production within OPEC. While the decision of Saudi Arabia was intended to discipline other members and ultimately get the ceiling, production quotas and marker price at more sustainable and equitable levels, OPEC's decision in December 1985 meant an abandonment of its role as a residual supplier – in short, ending its market management role. The competition for market share led to a continued decline in the price of the marker crude from \$27.8 per barrel in December 1985, to its monthly lowest at \$8.5 per barrel in July of 1986, averaging \$13.7 per barrel for the full year, around half of its 1985 average, even reaching \$3.25 per barrel for one Saudi cargo of two million barrels destined for Brazil that month.¹⁹

Judging from the price outcome of the early netback contracts in mid-1985 and in the aftermath of OPEC's decision in December 1985, it seemed that overproduction contributed more to the price collapse, while netback pricing was a result or the reason for the extent of the fall. It also seemed from subsequent events that Saudi Arabia did not foresee such price collapse. The disarray in Saudi Arabia's marketing policies was manifested in the continued use of an already discredited netback pricing, especially when it was forced to modify the terms of its earlier netback contracts to keep the volume gains in competition with other producers who adopted a similar approach. This state of affairs led ultimately to the dismissal of Yamani in October 1986. OPEC's disarray was evident in its inability to come together during the year and arrest the price decline due to the mistrust between its members which had been building up since 1981 and the inability of Saudi Arabia to exercise effectively its leadership in time of crisis.

Although the above analysis considers the abandonment of the fixed price regime and Saudi Arabia's swing role and the competition for market share as natural outcomes of a non-sustainable price and production regime, others saw political motives behind the price collapse and Saudi actions. According to those, Saudi Arabia in collusion with the US government intentionally sought a price collapse to deny two other producers, Iran and the Soviet Union, the financial means that had enabled the first to continue its war with Iraq and the second its war in Afghanistan. Although the subsequent Saudi response to the price collapse within OPEC invalidates this 'conspiracy' theory, it had its adherents, especially in the international media. The fact of the matter is that while Saudi Arabia regained volume during the course of the price decline, it suffered 52 percent oil revenue losses, prompting it to impose austerity measures

detrimental to its very security and stability. Needless to say, political factors did play a role in the price collapse, but not in the framework suggested above. The polarization resulting from the Iran-Iraq war made it difficult for OPEC to reach meaningful consensus to deal with the market impasse resulting from the structural changes. The lack of trust among its members aggravated the situation that led ultimately to each country seeking its self-interest independent of the common objective of the group.²⁰

When OPEC finally came together in late 1986, it agreed to a new ceiling, a new \$18 price for an OPEC basket of crudes instead of the marker crude, Arab light, and an end to netback pricing. The agreement signaled Saudi Arabia's official abandonment of its swing role in OPEC but delayed for a short while the eventual end of the fixed price regime that lasted for some five decades, administered first by the international oil companies for four decades and then by OPEC.

The current role of OPEC and Saudi Arabia

The counter-shock was coincidentally followed by a change in demand patterns, the most notable of which was the emergence of new demand growth centers in Asia and Latin America, outside the OECD, which had traditionally dominated world oil demand. While demand had grown by less than 0.5 percent annually in the OECD since 1987, it was growing by close to 3 percent in those emerging economies led by China, fueled by rapid industrialization and urbanization. The developing countries' share of global oil consumption increased from 37 to 52 percent between 1987 and 2015, accounting for 80 percent of the growth in global oil demand. This, along with the slowdown in the growth of non-OPEC production and even the decline in the production of the North Sea and the US, led to an increase of 17 mb/d in OPEC production, commanding some 64 percent of the increase in global crude oil production over the period.

The oil market is currently characterized by the presence of many OPEC and non-OPEC producers with 40 and 60 percent average market shares respectively since 1987. The oil market is also characterized by the interaction between its fiscal and financial aspects and the interplay of economic and political factors to determine prices. Since mid-1987, the fixed price regime was abandoned altogether in favor of flexible market-determined pricing. The latter was introduced by Saudi Arabia through the sale of its diverse crude types to the different markets via announced monthly price formulas, linking the sale prices of its crudes to the prices of other traded crudes either in established commodity exchanges in London (Brent) and New York (WTI) – for sales in Europe and North America respectively – or the spot quotations of Dubai and Oman crudes for sales to Asia, with adjustments accounting for crude quality, transportation and seasonality variations. This approach was soon adopted by most OPEC members and survives until today. The reference crudes for the formulas changed over the years reflecting changes in their liquidity and the characteristics of each market. The price formula announced by Saudi Aramco each month became in one way or another, and irrespective of OPEC, the reference to pricing all other crudes due to the size of Saudi exports, its presence in the three main markets and the consistency of its formula and its dynamism.

The role of Saudi Arabia during this stage of OPEC's development was more characterized by the part played by its excess production capacity. It became clear in the thirty years since 1987 that the excess production capacity in Saudi Arabia, constituting around 70–80 percent of the peacetime excess capacity of OPEC, was the main factor in ensuring market stability and supply continuity, thus re-establishing OPEC's role and its ceiling/quota systems. The use of that excess production capacity during supply interruptions, within the OPEC framework or otherwise, contributed to easing their price impact (Table 3.2).

It should be pointed out, however, that despite the imperfections of the formula pricing and the loose production management, they have contributed to the continuity of OPEC's role and its market relevance. The lessons of the oil price collapse of 1986 came to the fore thirty years later when OPEC, led by Saudi Arabia, decided not to cut production in response to the growth of US shale oil, effectively abandoning its

Table 3.2 Supply interruptions and Saudi Arabia (excess crude oil production capacity – mb/d)

<i>The crisis</i>	<i>Production impacted</i>	<i>Duration (months)</i>	<i>Saudi excess capacity</i>
Invasion of Kuwait (August 1990)	5.0	12	3.0
Venezuela strikes (November 2002)	2.2	2	2.7
Invasion of Iraq (February 2003)	2.3	2	2.0
Gulf of Mexico hurricanes (Sep. 2005)	1.3	1	1.5
Libya's production interruptions (2011–)	1.5	–	2.7–1.3

Source: Calculated from BP (2016), SAMA (2016).

production management role. This ultimately led to a price collapse of 58 percent, to be arrested in late 2016 when OPEC and non-OPEC producers came together to agree to restrain production to rebalance the market. Saudi Arabia's insistence not to respond in 2014 and its oil diplomacy forging the alliance in 2016 were key to the two price episodes.

The current global environment in which OPEC operates is distinctively different to the old epochs when it was at loggerheads with the companies, or when it was in full control under a fixed oil price regime, or when it switched to market-determined prices. Today's world oil demand and supply patterns and trajectories are different, and OPEC's ability to influence the market outcome significantly has been eroded. Growth in demand has been – and is projected to be – modest, non-OPEC production from conventional and non-conventional sources have increased and this trend is projected to continue albeit at slow rates, and the physical/financial market integration is here to stay. Furthermore, the global climate change process has reached maturity and action and the world's transportation and mobility systems are undergoing rapid change, both of which will impact the options before the oil producers, especially OPEC as a residual producer.

The different market junctures referred to above point also to the vulnerability of OPEC countries to the price shocks due to the continued dependence of their economies on oil income. This has been a long-time concern and needs to be addressed in each country both for its own sake and in order to give them more room when dealing with the inherent market volatility and uncertainty. It is worth noting that the consuming countries faced with higher oil prices embarked on a concerted effort to diversify away from oil, and succeeded in doing so. Within this context, OPEC's success hinges more on lessening its countries' dependence on oil, which depends on policies and initiatives from within, than on seeing oil prices rebounding, which depends on many factors, some out of its domain of influence.

Conclusions

Saudi Arabia was instrumental in shaping OPEC's role during each of the different stages of its development into a global economic and energy player. It took the lead in the creation of the organization through the vision and energy of its then lead official, Al Tariki, relying on the support of his government and the political backdrop at the time. In the early years up to 1970, its role in OPEC was marginal except for its early association with the members opposed to production programming advocated by Venezuela, thus delaying using the mechanism until the early eighties. Its active role in the early seventies in the participation vs. nationalization debate contributed to launching the 'negotiation' framework with the companies to own increasing shares in their concession assets and adjust the price levels and fiscal terms. Its leadership in the events leading to OPEC's assuming the price administration role, especially the production cutbacks and the Arab oil embargo against the US of 1973, ensured it a leadership role in the organization during its ascendance.

OPEC's gradual loss of power in the eighties followed Saudi Arabia's losing leverage in the organization due to its swing role, the unfavorable political climate and declining OPEC production and influence. Its inability to introduce an alternative to the unsustainable fixed oil price regime amid the structural changes in demand and supply, under which it lost market influence, led ultimately to the oil price collapse of 1986. However, its adoption of a market-determined pricing mechanism in 1987, through formula prices and widespread use, contributed to the organization's viability and re-emerging role especially during crisis times. Maintaining excess production capacity throughout the period since 1987 has ensured it a dominant role in OPEC and strengthened the organization's production management role.

Notes

- 1 For example, Yamani remained minister of petroleum and mineral resources for 24 years (1962–1986) during the reigns of three kings (and prime ministers) Faisal, Khalid and Fahad. Nazer held the post for nine years (1986–1995) and Al Naimi held it for 21 years (1995–2016). When the Ministry was first established in March 1961, Abdullah Al Tariki headed it for only 18 months before being sacked in September 1962.
- 2 On the models on OPEC market behavior, see the review articles of Cremer and Salehi-Isfahani (1991) and Fischer, Gately and Kyle (1975), Griffin and Teece, (1982), Griffin (1985); on modeling Saudi role in OPEC see Johany (1980), Al-Yousef (1998) and Stevens (1982).
- 3 On the history of such developments between the two wars see (Yergin 2009) and on the international oil cartel see Sampson (1976), Jacoby (1974) and Blair (1976).
- 4 Duguid (1970) analyzed thoroughly the role of technocrats in the formation of states, taking Al Tariki as an example.
- 5 See Terzian (1985, pp. 18–30) for an account of the first Arab Petroleum Congress and Skeet (1988, pp. 15–16) on the Maadi Pact.
- 6 Hendryx submitted two papers to the first and second congresses emphasizing the concept of the sovereign rights of nations to modify unilaterally the concession terms. On the debate on the permanent sovereignty over oil resources and the Middle East oil concessions, see the review of Fatouros (1968) available in www.repository.law.indiana.edu/ilj/vol43/iss4/8
- 7 The posted price cut of August 1960 was the industry's response to the market imbalance following the U.S government's decision to impose import quotas in March 1959 to protect its oil industry and increasing Russia's oil exports, leading to increased competition for other markets. This, as well as Alfonso's and Al Tariki's fascination with the experience of oil production programming of the Texas Railroad Commission, led some to credit the establishment of OPEC to the 'misguided' US policy of controls and rationing. The main proponents of this view are Morse (1995) and Adelman (1993)
- 8 On the shifting alliances in the region during the Cold War, see Safran (1985, pp. 77–103) and on Saud-Faisal rivalry see Vassiliev (2000, pp. 354–362).
- 9 Faisal's return to head the cabinet in March 1962 did not end the power struggle with Saud, which was finally resolved with Saud's abdication and Faisal becoming the king and prime minister in March 1964.
- 10 In his attempt to shore up his rule amid splits in the royal rank and mounting internal pressure, Saud aligned with Egypt on regional matters and distanced himself from US, but Faisal reversed this brief cozy relationship and hostility between the two countries then lasted for a decade.
- 11 On the participation vs. nationalization see Yamani (1968) and Terzian (1985, pp. 150–162). And on the participation negotiations and outcome, see Parra (2004, pp. 154–160) and Skeet (1988, pp. 105–116).
- 12 See the chapters on the Tehran and Tripoli agreements in Terzian (1985, pp. 112–146) and Parra (2004, pp. 110–145).
- 13 Besides, Yamani (Parra, 2004, pp. 107) cites the personalities of Ali Al-Sabah, Jamshid Amuzegar and Perez Guerrero, the respective ministers of Kuwait, Iran and Venezuela during these early and disturbing years, as instrumental in forging the 'sense of commonality' among OPEC members.
- 14 The events leading to the price increase of 1973/4 is well covered in the energy and oil literature as the first 'energy crisis' and the beginning of the 'OPEC era'. See Yergin (2009), Maugeri (2006) and Vernon (1976)
- 15 For a survey of the economic literature on OPEC behavior, see Cremer and Salehi-Isfahani (1991) and Griffin and Teece (1982); on Saudi behavior within OPEC see Johany (1980), Stevens (1981) and Quandt (1982)
- 16 For a critique of the pessimistic demand and supply predictions during that period, see Lynch (1992),
- 17 These and subsequent figures were derived from OPEC data bank and BP (2016)
- 18 On netback pricing see Mabro (1986) and PIW (1986).

19 See Al-Naimi (2016) and Ait-Laoussine and Gault (1986).

20 On a critique of this political conspiracy theory behind the oil price collapse of 1986, see McFarland (2017)

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Trade not aid

OPEC and its contribution towards restructuring the Iranian economy in the 1960s

Touraj Atabaki

Introduction

The world coming out of the Second World War was characterized as the world of Cold War, new political realignment, economic and social reconstruction chiefly through the agency of developmental states (for a historical review of the formation and practices of the developmental states, see Woo-Cumings, 1999 and Ludden, 2005). The United Nations called the post-war period and explicitly the 1960s as the decade of global and massive economic and political reform. In a language turn, the underdeveloped countries became members of the developing world, poised to leap over decades of economic stagnation and poverty. In Iran, following labor militancy and vigorous anti-British social protest by the urban middle class in the 1940s, the Iranian oil was nationalized in 1951. However, the jubilation surrounding the nationalization did not last long and in the 1950s the country experienced one of its most arduous periods of economic decline and political repression. Both the coup d'état of 1953 and the denationalization of the management of the oil industry in 1954 were major architects of this repression and stagnation.

One immediate outcome of the August 1953 coup was the wide-ranging repression affecting every corner of the political sphere in Iran. The return of autocratic rule brought the 12 years of participatory politics to a sudden end. The years 1953–1960 were a barren period and the labor movement hit rock bottom. Compared to the national-scale labor movement in the 1940s, in the post-1953 coup period we see fragmented provincial labor activity in some labor-intensive complexes and industries – for example, the strikes of the brick workers of southern Tehran in 1957 and 1959 and workers' protests in the Vatan Textile Factory of Isfahan in 1959. Labor activism even reached the Iranian oil industry in 1957 and 1959, ending the period of labor semi-placidity since the coup d'état of 1953. The rise of the labor movement in the late 1950s was substantial, the number of strikes per year leaping to over twenty (Abrahamian, 1982, p. 422).

Surprisingly, in contrast to the 1940s, there was no cooperation between the labor movement and other guild or political movements. Each of these movements followed their own path, independent from and indifferent to others. The political movement's aim was to protest against both the government that had seized power in the aftermath of the coup and the repression that ensued. Their goal was to open the window of opportunity just wide enough to let in a ray of light, allowing supporters of the anti-government

movement to breathe easier and carry out their activities more freely. The labor movement, in contrast, was indifferent to the turbulent political situation and remained focused on issues connected to ensuring the workers had money to put bread on the table.

The drastic fall in the Iranian oil revenue by 55 percent at the end of the 1950s paved the way for a widespread economic crisis, causing social grievances among industrial workers as well as the laboring poor. Moreover, the 13 percent fall in the Iranian oil price in 1960 brought the country to the edge of total economic collapse. Meanwhile the Iranian government was warily engaged in negotiations with the Consortium of Oil Companies – known as Iranian Oil Participants Ltd (IOP)¹ – to increase or at least sustain the country's oil revenue.

In the late 1950s, the reliance of the government on loans in order to meet the country's deficit triggered a rapid increase in the rate of inflation and the cost of living. In 1961, the Ministry of Labor conducted a survey of prices in Tehran for workers' market basket commodities. This revealed that

a worker with wife and two children had to take home a minimum of 178 Rials (\$2.37) a day in order to feed and clothe his family at a minimum standard of decency and health. This compared to minimum wage of 50 Rials (\$ 0.66) a day in Tehran. The minimum wage for the rest of the country remained the same in 1947, 35 Rials (\$ 0.46) a day.

(Lajevardi, 1985, p. 205)

The immediate outcome of the economic recession was social and political instability – social grievances and protest at the 'bottom' and political disarray amongst the ruling elites. The country was dominated by days of social and political unrest. A number of political organizations that had been silenced after the 1953 coup, when martial law led to widespread repression, were now able to organize themselves and once again come to the fore. The formation of the second pro-Mosaddeq Iran National Front (Jebheh Melli) and the commencement of strikes and political and union protests are the hallmarks of these years and led to a deep political crisis. In May 1961, teachers organized a nationwide strike demanding a pay rise, and nine months later, on 21 January 1962, the students of the University of Tehran went on strike, with the support of the National Front.

Following almost eight dark years of severe political despotism, in May 1961 a rally was organized by the opposition – the National Front – in Jalaleyeh, north of Tehran, calling for economic reform and an end to political exclusion and repression. Meanwhile, the socio-political consequences of economic recession and the resurgence of political activism worried some reformist statesmen in government circles. Statesmen such as Ali Amini, who enjoyed the support of Democrats in the United States, launched their own campaign, calling for change and reform in both the country's economy and its political establishment.

Along with some elements within the Iranian political establishment who were anxious about the country's deteriorating economy and its social consequences, the United States, despite its major role in bringing about the prevailing political impasse and economic recession by leading the coup of 1953, now joined the Iranian reformist political elites and did not conceal its deep concern about social and political unrest in Iran that potentially paved the way for 'communist agitprop' in the midst of the Cold War.

The post-Second World War period was the pinnacle of anti-colonial and national liberation movements worldwide, with their substantial ingredient of anti-imperialism and anti-Americanism. These movements became embedded in the ever-increasing tensions of global refashioning known as the Cold War. The need for authoritarian reforms, albeit within the boundaries of economic and social development, dated back to the United States Democrat Harry Truman's 'Four Points', launched in 1949. A concern that could be traced back even earlier to before the Democrats resumed power in United States in 1961 and pursued economic and liberal reforms in Iran (Amanat, 2017, p. 584). The Democrats' concern

was about delays in the implementation of what they already proposed. The Kennedy administration's call to their allies in the Global South was crystal clear: either you opt for top-down reform or the bottom-up revolt will wrap up your rule!

Three months after the National Front rally in Jalaleh, in August 1961 the Shah held his own rally in Doushan-Tapeh, east of Tehran, where he announced the introduction of a series of widespread economic reforms.² Following some two years of scrutinizing all possible reform paths, finally on 26 January 1963 an outline of authoritarian development was announced by the Shah and put to a referendum. The core of the reforms was a series of far-reaching socioeconomic plans, later to be known as the White Revolution.

However, the economic growth which occurred together with notable economic and social change was not accompanied by political development. Exclusive and coercive political practices prevailed as before. While in the social sphere, changes in the urban and rural relationship were becoming conspicuous, the political space was still suffering from the post-1953 coup repression. A strong female presence in all professions, including an increase in the total number of female workers, widespread literacy programs, increased higher education opportunities and improved healthcare and communication networks, were some of the direct outcomes of this development regime. The population mobility that was the outcome of these reforms led to increased rights for citizens, whom the Shah, using leftist terminology, referred to as 'free-liberated men' and 'free-liberated women'. Enforced top-down reforms together with greater forces from below resulted in demands from citizens for their rights. The political activists of this period could not ignore these developments.

With the commencement of governmental reforms there was great confusion among the various political parties and organizations that opposed the government. They were unsure how to react, whether to support the reforms, oppose them or a combination of both. The protest slogans of the students from the University of Tehran at that time, 'Yes to reforms, no to dictatorship', were soon adopted by many political organizations, including the National Front. The reaction of the Communist Tudeh Party to the reforms was influenced by the diplomatic relationship between the Soviet Union and Iran; it changed from rejection at the beginning of 1942 to welcome at the end of the year.³

Iran in 1960s: the inauguration of the developmental state

At the heart of the White Revolution was land reform. It was hoped that this reform would eradicate the old land ownership, upsetting the existing pre-capitalist relations in rural areas and bringing about rapid capitalist economic growth. Through this rapid growth it was hoped that the pre-industrial stages of societal development could be skipped so that a society that was largely dependent on agricultural economy might develop into a capitalist society capable of joining the global economy. Industrialization of the economy was fundamental for this process.

Prior to the referendum for the White Revolution, it was the introduction of the Third Five-Year Development Plan (1962–1967) that provided the roadmap for the extended reform, although the Shah, in order to register the reforms in his own name, insisted that the outline and outcome of reform should be detached from the Third Development Plan. The Third Development Plan followed two consecutive development plans, both of which ended with relatively poor results. The First Seven-Year Development Plan (1949–1955) coincided with the nationalization of Iranian oil in 1951 and the coup of 1953, and although it failed to achieve any tangible results, it nevertheless constituted the development planning in Iran, coordinated by a new institution, the Plan Organization, founded in 1948 (for the history of development planning in Iran, see Gudarzi et al., 1999). The Second Seven-Year Development Plan (1956–1962) was inaugurated by the allocation of 60 percent of the oil revenue to development planning, chiefly regional planning, coordinated by the Plan Organisation.⁴ Furthermore, the share of the oil in the development planning was programmed to be increased by 5 percent per year with the maximum input of 80 percent (Gudarzi et al., 1999, pp. 219–220). However, the Second Seven-Year Development Plan was

faced with a bad harvest in 1959/60 compounded by deficit financing as a result of a drop in the posted price of Persian Gulf oil from \$2.04 per barrel to \$1.78, a fall of 26 percent per barrel during the period 1957–1960 (Fesharaki. 1976, p. 97). As a result, the cost of living went up by 35 percent, further adding to social grievances among the working class and laboring poor.⁵

The Third Five-Year Development Plan managed to secure GDP growth of 8.8; within this, the average annual growth share of industrial and mining sectors was 7.12 percent (The Plan Organization, 1968). During this period the migration of labor from rural to urban areas resulted in a decrease of the labor force in the agricultural sector and an increase in urban industrial sectors. This led in turn to an increase in urban unemployment. Hundreds of thousands of villagers surged towards the cities. Between 1956 and 1966, of the total 950,000 newly created jobs, 623,000 were in the industrial and mining sectors. Those employed in these sectors were predominantly from the excess labor force from rural areas. Between 1962 and 1967, from within the total active labor force of the country (6.6 million in 1962 and 7.8 million in 1967), the share of the agricultural sector shrank by 6.1 percent. This was despite the fact that the number of employees in industrial sectors grew by 4.2 percent to more than two million. In real terms, the purchasing power of workers in certain large industries improved by 40 percent between 1962 to 1967, an indication of uneven development in waging policy endorsed by the government (The Plan Organization, 1968).

Iran's oil revenue had certainly made a major contribution to the effectiveness of the Third Five-Year Development Plan. With an estimated increase of 13.6 percent, oil represented the main input into the country's economic reconstruction. As Fesharaki correctly argues,

the fiscal influence of the oil revenues [had] twofold effect on the Iranian economy: first it provided a source of income for the government to supplement its budgetary expenditures, and second, the oil revenues [were] channeled through the Plan Organisation for investment in various developments projects.

(Fesharaki, 1976, p. 130)

Alinaghi Alikhani, the Iranian minister of economy (1963–1969), claims that in 1960s the oil revenue allocated an average of 81.5 percent to Iran's development plans.⁶ In the Third Five-Year Development Plan, with an annual 13.6 percent increase, the share of oil revenue inputs was boosted from 38 to 71.7 billion rials. Such an escalation not only doubled the value added by the oil revenue but also increased the oil share in the country's gross national product (GNP) from 11.6 percent in 1962 to 14.5 percent in 1967 (Plan Organization, 1968).

The foundation of the Organization of Petroleum-Exporting Countries (OPEC) in 1960 opened a window of opportunity, helping Iran to bargain with the Consortium of Oil Companies. There was an optimism in the air that the increase in the oil revenues would ultimately expedite economic and social development.

OPEC and its contribution to restructuring the Iranian economy in the 1960s

On 29 May 1963, Fuad Rouhani,⁷ the first secretary general of OPEC who was also deputy chairman of the Board of National Iranian Oil Company (NIOC), presented a lecture at the Society for the Advancement of Management in Tehran under the title 'OPEC and Economic Development of its Member Countries'.⁸ On the objectives that brought OPEC into existence, Rouhani referred to the preamble to the Resolutions of the First OPEC Conference by saying:

The desperate need for accelerated economic development among the so-called underdeveloped countries of the world is self-evident. Mankind has at its disposal today technical knowledge sufficient

to ensure for all of us the material comfort and security which we need. We must put this knowledge to work, and employ all our resources, both human and material, in order to combat the evils of hunger, sickness and lack of adequate shelter which still plague the majority of countries throughout the world. As a nation, we have the will power to do so. What we need now is to create a larger body of people familiar with already known techniques in agriculture, industry and commerce and to make the enormous investment required in each sector. The formation of these professional bodies and the investment of the huge sums required, will tax our financial resources to the utmost.

[...]

In the face of these difficulties, the responsibility for channeling the resources of a nation towards economic development must lie with the government. Nowhere is this truer than in the great oil exporting nations, most of whom are members of OPEC, and earn almost all of their foreign exchange from payments by the oil companies exports of the nation's production of crude oil and refined petroleum products.⁹

The establishment of OPEC in 1960 paved the way for the growing prosperity of oil-producing countries through increased oil revenues and smoother industrialization of their economies was on the horizon.

In Iran, the country's presence and performance in negotiation with the Consortium of Oil Companies and later with OPEC was largely based on annual guidelines prepared by the biannual economic direction extended by the Assembly of Shareholders of the National Iranian Oil Company (ASNIOC), an institution bringing together the Iranian prime minister, the minister of finance, minister of economy, minister of energy, director of the Central Bank of Iran, chairman of the Board of NIOC and the head of the Plan Organization.¹⁰ Although the foundation of ASNIOC dated back to the nationalization of Iranian oil in 1951, it was only in the late 1950s that it became more functional, coordinating Iranian short- and long-term oil policies.¹¹ The ASNIOC met biannually in March and in December. In the March meeting, which corresponded with the Persian New Year, the ASNIOC outlined the country's annual policy, associated with the expected oil revenue, while the December meeting was more for assessing the annual accomplishments and failures. Between the biannual meetings of ASNIOC, a triangle committee (called the Directorial of Oil) in the Ministry of Finance, comprising representatives of the NIOC, Plan Organization and the Ministry of Finance, was in charge of observing and acting on all ASNIOC's decrees. With the foundation of OPEC, Iran's presence and performance in OPEC was added to the tasks of first the ASNIOC and later the Office of OPEC, the latter founded in 1974 in NIOC as an office of the International Department.¹²

While the decisive status of ASNIOC, the Directorial of Oil and later the Office of OPEC has been confirmed in all newly disclosed documents and witness accounts, what should not be underestimated in

Table 4.1 Iranian oil production: World, Middle East, OPEC production (1,000 barrels/day)

Year	World	Middle East	OPEC	Iran	Iranian share (percentage)		
					World	Middle East	OPEC
1955	16,190	3,220	-	329	2.0	10.2	-
1960	21,046	5,269	7,876	1,052	5.0	20.0	3.3
1965	30,530	8,333	13,172	1,885	6.2	22.6	14.3
1967	35,580	9,970	15,624	2,596	7.3	26.0	16.6
1968	38,835	11,170	17,652	2,848	7.3	25.5	16.1
1970	46,130	13,725	21,131	3,829	8.3	27.9	18.1

Source: Compiled from NIOC publications, OPEC Annual Statistical Bulletin, and Fesharaki (1976, p. 203).

the historiography of OPEC in Iran is the pivotal position of the Shah in meddling in and leading the country's bargaining and conferring with both the Consortium and OPEC.¹³ According to Fuad Rouhani, during the early days of OPEC there was some degree of apprehension in NIOC regarding possible cooperation with other oil-producing countries. The roots for such mistrust were laid in 1951 following the nationalization of Iranian oil, when the country's oil export was blocked by the all world's major oil companies. Following the sanction, the other Arab oil-producing countries adopted a non-cooperative policy towards Iran and increased their production, compensating for the loss of the Iranian share in the world oil market (Tadjbakhsh and Najmabadi, 2012, pp. 35–37).

Harmony or disarray in the OPEC's in and out

Although the period 1965–1969 in the history of OPEC is recognized as the period of consolidation (Skeet, 1988, pp. 35–57), the Arab–Israeli conflict that exploded in 1967 into the Six Days War was one of a series of disarrays, chiefly political, that threatened the unity and harmony of OPEC. In March 1967 the Fifth Arab Petroleum Congress was inaugurated in Cairo. In contrast to OPEC's assemblies, the Arab Petroleum Congress adopted a radical stance, against the international oil companies and those countries eroding Arab interests. In the process of the congress, the Saudi 'Red Sheikh', Abdullah Tariki, not only called for the nationalization of all oil in Arab countries but added that 'oil prices are [a] political matter, entirely unrelated to supply and demand' (Skeet, 1988, p. 43). Surely Iran was not endorsing these radical stances, as Fuad Rouhani argued in his account of OPEC history (Rouhani, 1974, pp. 216–222). The alliance between some OPEC member states weakened further following the Six Days War in June 1967. To varying degrees, an oil embargo, though not lasting long, was adhered to by Algeria, Kuwait, Iraq and Libya against countries supporting Israel. The impartiality of Iran during the Six Days War Iran not only resulted in the continuation of Iran's oil export but allowed it to increase its rate of production from 2,603,000 barrels per day in 1967 to 2,840,000 in 1968 (OPEC, 1969).

For the Iranian government, still recalling the bitter memory of 1951, when, as was mentioned earlier, the Arab oil-producing countries adopted a non-cooperative policy towards Iran and increased their production when the purchase of Iran's oil was sanctioned, Iran's stance in OPEC in 1967 was justifiable. But this Iranian policy was not limited to its neighboring Arab oil producers. The executive of NIOC and its chairman of the board, Abdollah Entezam, were convinced that Venezuela, as the other non-Arab member of OPEC, was seeking its own profit through obstructing the flow of Middle Eastern oil to the world market by pursuing an egalitarian policy in OPEC (Tadjbakhsh and Najmabadi, 2012, p. 171).

In addition to such views in NIOC, there was another faction in the Iranian political establishment that was not happy with any alignment with OPEC, but for different reasons. For example, Asadollah Alam, then the prime minister and later minister of court, and Manucher Eqqbal, who followed Abdollah Entezam as the chairman of the board of NIOC, were very anxious not to join OPEC, which according to them was nothing more than a 'radical club', jeopardizing Iran's relations with the Consortium. Although the anti-OPEC bloc during the period 1960–1963 endeavored to persuade the Shah to adopt a more skeptical approach towards OPEC, nevertheless, according to all accounts, the Shah – who was very eager not to miss any opportunity or platform that might increase Iranian oil revenue – opted to stay actively in OPEC, but not to lead it.¹⁴

For example, on the eve of the Baghdad Conference in September 1960, Manucher Farmanfarmaian, who was then one of the leading directors in NIOC and was due to present the Iranian government at the Conference, referred in his diary to a hotfoot meeting he had with the Shah, two days ahead of departing for Baghdad:

Shah was standing on the stairs of the Sa'dabad Palace when I arrived. He told me: 'you will be representing of Iran in Baghdad. I want you to put asides all past disputes and find a common stand

with the Arab states. Oil is the soil [sic] revenue for us and we need money to feed our growing population'. Then he added 'the shameless oil companies are steeling [sic] our poor people's wealth and keeping us at their mercy. I want to cooperate with the Arab states to end this'.

(Farmanfarmaian, 1999, p. 632)

To Manucher Farmanfarmaian's surprise, he was not appointed as the head of the Iranian delegation to the Baghdad Conference. In order to be confident that Iran would be favorably and conspicuously presented in Baghdad, NIOC decided to appoint Fuad Rouhani instead. The appointment of Rouhani, then a 53-year-old jurist with a long and loyal record working in the Iranian oil industry and promoting Iran in negotiations with the Consortium, was not only an indication of changes in the NIOC leadership's attitude towards cooperation with the oil producers in the region and beyond, it was also nominating an expert who was already engaged with the Consortium, bargaining on Iran's share of its oil.

In Fuad Rouhani's diary there are references to Consortium putting pressure on the Iranian government to disassociate itself from OPEC. In one of the meetings between Abdollah Entezam, the general director of NIOC, and Bridgeman, the representative of British Petroleum, which took place in Tehran in October 1962, British Petroleum offered a loan to Iran if Iran would leave OPEC (Farmanfarmaian, 1999, p. 318). Although the British Petroleum offer was rejected at once by NIOC and the Iranian government clearly decided to stay in OPEC, nevertheless the radical stance often adopted by some OPEC members such as Venezuela or Iraq prompted the Iranian government to embrace a more moderate stance in the organization (Farmanfarmaian, 1999).

According to Parviz Mina, the Iranian performance in OPEC during the early life of the organization was uneven. The major obstacle for the Iranian government observing a more coherent policy in relation to OPEC in the 1960s was not solely uninterrupted pressure from the Consortium, as largely believed by oil experts and historians. It was also the government's commitment to the ambitious development plans initiated and refashioned since the early 1960s that made it fluctuate its stand in OPEC in pursuit of a better share.¹⁵

Regarding the Iranian government's commitment to development planning, the high dependency of Iran's economy on oil revenue essentially guided the country to on the one hand demand the Consortium for increased revenue through higher production and on the other to adopt a more competitive stand in OPEC. Within the context of comparative outputs, Iran with 65 million metric tons in 1962 provided about 13 percent of total OPEC production, and it occupied the fourth exporting rank after Venezuela, Kuwait and Saudi Arabia. Over Over a 15-year period (1953–1968) the leading Middle Eastern oil producers, apart from Iraq, had almost equal outputs.

Asadollah Alam, minister of court, highlighted in his diary Iran's need for oil revenue in 1966, when the future of ongoing development plans was in serious jeopardy (Alikhani, 1998, p. 146). Alam refers to a meeting the Shah had with some members of the Directorial of Oil where he furiously accused the Consortium of not meeting Iran's development's need. He went so far as to ask the Directorial of Oil to issue an ultimatum to the Consortium that unless an agreement was reached within a month, Iran would take unilateral action against it (Alikhani, 1998, p. 126).

In 1967, sponsored by the Iranian government, David Missen, a British financial consultant, published a booklet in which he explicitly presented Iran's oil demands, including an increase in oil revenues sufficient to permit Iranian policymakers to execute their impressive economic and social development plans. Accentuating that what developing countries need is trade, not aid, in order to carry out sustainable development programs, Missen argued that

Iran is one of the few countries which have freed themselves from dependence on aid. But in the process Iran's dependence on increasing earnings from the export of her own produce has been enhanced. The internationally accepted case for justified economic development, and where possible

for development through trade rather than aid, strongly emphasize Iran's essential need for export opportunities. Inevitably at the present stage of Iran's economic development this means increased opportunities for export of Iranian oil.

(Missen, 1969, pp. 12–13)

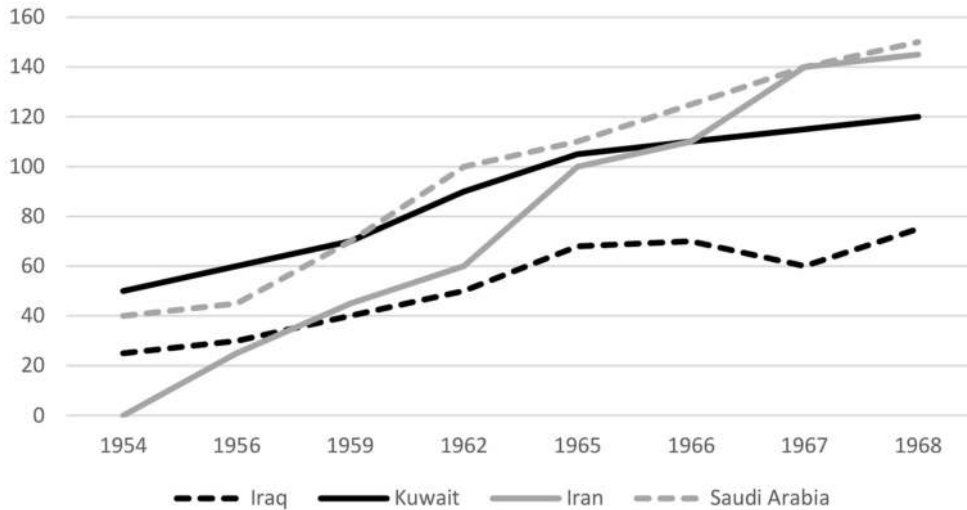


Figure 4.1 Leading Middle East Oil producers 1945–1968 (millions of metric tons)
Source: Missen (1969, p. 8). Cross-checked against British Petroleum (2011).

David Missen's argument for the increase in oil income corresponded with the inauguration of Iran's Fourth Five-Year Development Plan (1968–1972). In order to meet the goals put forward in the development plan, Iranian oil revenue with an average increase of 17 percent, needed to climb from 865 million dollars to 1,555 million dollars in 1972, contributing 80 percent of planned development expenditure. To achieve such a large input of foreign exchange for the country's economic development, Iran needed to increase its share of Middle East oil production from 25 to 35 percent. Such an increase was in contrast to the oil output of the other major Middle Eastern oil producers of the time, Iraq, Saudi Arabia, Kuwait, Qatar and Abu Dhabi. In his survey Missen examined the geostrategic status of these countries compared to Iran.

In 1967, the NIOC published a chart, lobbying for the increase of Iran's oil production. By comparing the population per capita revenues from oil and the share of total Middle East oil production, Iran argued that

in contrast to its neighbors, Kuwait, Abu Dhabi, Qatar, Saudi Arabia and Iraq, Iran has a substantial population, totaling more than 28 million. This is around twice the total for the other Middle East oil exporters put together. Although Iran is a substantial producer and exporter of oil, in relation to her population, the current level of output is modest, and amounts to less than 10 British pounds per head each year – far short of the fantastic totals of 519 and 2,187 British pounds respectively attained by Kuwait and Abu Dhabi.

(Missen, 1969, pp. 2–3)

Iran continued to press both OPEC and the Consortium for an increase of her oil revenue. In 1968, Iran insisted that the rate of its oil production within OPEC should correspond to its relatively high population compared to other OPEC members, as well as its need to pursue the development plans projected in Iran's

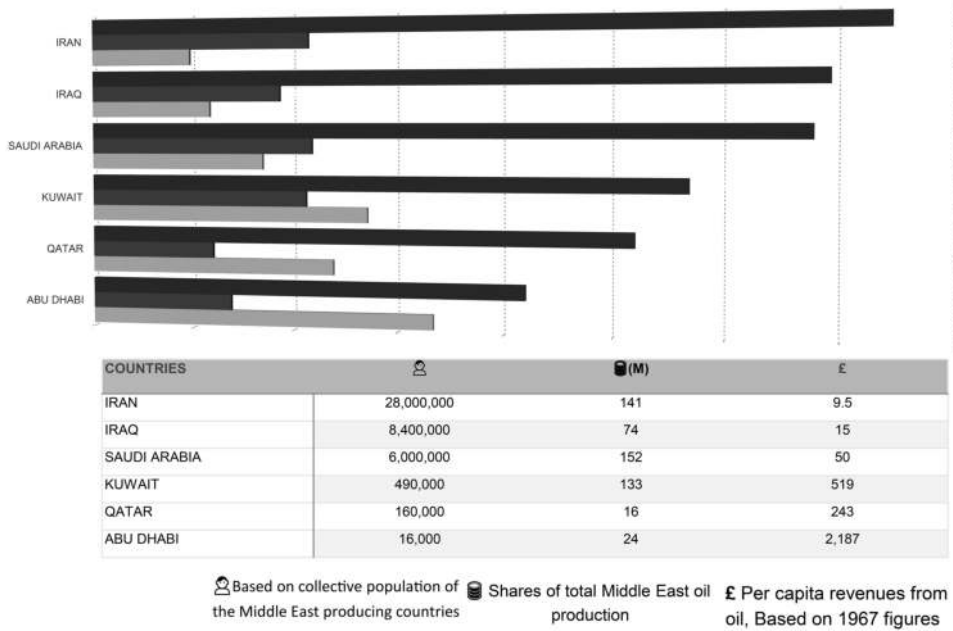


Figure 4.2 Population and income in relation to oil in the Middle East (1968)

Source: Adapted from Missen (1969, p. 6).

Fourth Five-Year Development Plan (1968–1972). In March 1968, Prime Minister Hoveida, in a speech to the Iranian Parliament, announced that his government intended to gear oil output to Iran’s needs, as envisaged in its development program:

The oil income figures contained in the 1968 budget reflect neither Iran’s true needs nor her demands. They merely represent the bare minimum required by Iran during the five-year period of the Fourth Five-Year Development Plan. We cannot stand by idly while our own oil resources are kept unexploited underground and not utilized for the country’s development.¹⁶

Meanwhile, with more than 63 percent of its development expenditure coming from expected oil revenue, the Directorial of Oil in the Ministry of Finance presented the Consortium with a complete list of Iran’s development expenditure for the Fourth Five-Year Development Plan (Fesharaki, 1976, p. 105). A development plan that aimed to boost the annual national gross domestic product by 9 percent (Majles Shora-ye Melli, 1968, p. 3).

Conclusion

Iran of the 1960s was one of the major developing countries, characterized by a certain of authoritarian development initiated and implemented by the state. According to all accessible social and economic indices, in 1960s the material standard of living of the Iranians, including the growing middle class and some parts of the working class, increased. This improvement predated the oil price boom in 1970s and was chiefly made possible by the more than 3.5-fold increase in the country’s oil export, enabling Iran’s added value of the oil revenue to be doubled and the country’s GDP experiencing nearly a 3 percent increase during the period 1962–1967.

The early years of OPEC history corresponds with the implementation of the Third Five-Year Development Plan (1962–1967) in Iran. For the Iranian government, OPEC opened a window of opportunity, enabling Iran to practice economic development that the country after a decade of social and economic austerity very badly needed.

As an alternative to the conventional historiography of OPEC, which confines its study to surveying the state–state and state–oil companies’ interactions, this paper aimed to examine the status of OPEC through the prism of the social and economic development of one of its member states. Furthermore, instead of locating the early history of OPEC within the boundaries of formal functional meeting of the representative of its member states, it aimed to place the history of OPEC within the larger context of social and political history of one of its founding members.

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Notes

- 1 Iranian Oil Participants Ltd (IOP) was a consortium of oil companies founded in 1954 with the task of extracting, refining and exporting the Iranian oil. However, in practice, the denationalization of the management in the Iranian oil industry became one of its major tasks. The founding members of the IOP included British Petroleum (40%), Gulf Oil (8%), Royal Dutch Shell (14%), and Compagnie Française des Pétroles (later Total S.A., 6%). The four Aramco partners – Standard Oil of California (SoCal, later Chevron), Standard Oil of New Jersey (later Exxon), Standard Oil Co. of New York (later Mobil, then ExxonMobil), and Texaco – each held an 8% stake in the holding company.
- 2 The program of widespread economic reforms that the Shah promised was in fact the brainchild of Hassan Arsanjani. Arsanjani was a longstanding advocate of land reform and also a renowned expert in agriculture who had prepared this plan at the request of the prime minister, Ali Amini (Afkhami, 1999, pp. 167–170) (Amini, 2009, p. 171 and p. 385) (Afkhami, 2001, p. 37).
- 3 In order to refashion its relationship with the Soviet Union, in July 1962 the new Iranian government announced that Iran never let any country install a military base for long-range missiles. A stand welcomed by the Soviet Union and one that opened a new chapter in diplomatic relations between two countries.
- 4 Along with the mega-national planning, the Second Development Plan introduced the regional development schemes, by implementing new hydroelectric and irrigation projects in north-west, south-west and south-east Iran (Ebtehaj, 1991, pp. 353–452).
- 5 The author’s interview with Alinaghi Alikhani (minister of economy in Iran, 1963–1969), Washington, 21 November 2016. According to Ervand Abrahamian, ‘The number of major strikes, which had totalled no more than three in 1955–1957, jumped to over twenty in 1957–1961’ (1982, p. 422).
- 6 The author’s interview with Alinaghi Alikhani, Washington, 21 November 2016.
- 7 Fuad Rouhani, an advisor to Mohammad Mosaddeq and a historian of Nationalization of Iranian oil was born in 1907 in Tehran and died in 2004 in exile in London. Rouhani graduated in law from the University of London in 1937 and received his PhD from the University of Paris in 1968. With lengthy employment in the Anglo-Iranian Oil Company and, later, the National Iranian Oil Company, Rouhani was elected as the first secretary of OPEC, following its foundation in 1961.
- 8 *NIOC Newsletter*, No. 60, July 1963
- 9 *NIOC Newsletter*, no. 60, July 1963.
- 10 Unlike most of the oil-producing countries, prior to the revolution of 1978/9, Iran never had a ministry of oil. The Ministry of Petroleum of Islamic Republic of Iran (*Vezerat-e Naft*) was established in September 1979.

- 11 The author's interview with Parviz Mina, Paris, March 24, 2017. Parviz Mina joined the Iranian oil industry in 1947. Following the nationalisation of Iranian oil, he worked at the NIOC Department of Exploration and Production and later in 1974 he became the Director of the International Department of NIOC.
- 12 The author's interview with Parviz Mina, Paris, 24 March 2017.
- 13 The author's interview with Alinaghi Alikhani, Washington, 21 November 2016.
- 14 The author's interview with Alinaghi Alikhani, Washington, 21 November 2016; The author interview with Parviz Mina, Paris, 24 March 2017.
- 15 The author interview with Parviz Mina, Paris, March 31, 2017.
- 16 *Middle East Economic Survey*, 8 March 1968.

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Algeria and OPEC

Hocine Malti

Algeria has been independent since 5 July 1962. After conducting a war of liberation lasting seven and half years, it gained its independence following negotiations between the independence movement – the FLN (National Liberation Front) – and the French government. The war lasted so long partly because oil was discovered in the Sahara in January 1956. Immediately afterwards, the French government put in place the legal provisions regulating oil exploration and exploitation. Following the example of Great Britain and the United States, which had seized oil deposits in the Middle East after the First World War, the new French law allowed access to Saharan deposits to French companies only or, eventually, to foreign companies in partnership with a majority French partner.

July 1969, Algeria becomes a member of OPEC: why so late?

At independence, some fifteen French companies, operating nearly fifty oil and gas deposits, were present on Algerian territory. The only exception was that of the Sinclair Mediterranean Petroleum Company, a small independent American firm that held less than a 15 percent stake in the Rhourde El Baguel field. The French government was aware from the outbreak of the war of liberation that the conflict would lead to the independence of Algeria. That is why, when oil was discovered, it began to envisage the break-up of the country into two entities –the Sahara to the south, which would become ‘Saharan zones of the French Republic’, and the northern part of the country, which would gain independence. These two actions, the Saharan oil reserved for French companies and the break-up of the country into two separate parts, demonstrate that in the eyes of the French government, even if Algeria ceased to be a French territory, its hydrocarbons should continue to belong to France. But it was necessary to convince the Algerians to accept such an antinomy. It took six years before the French head of state, General De Gaulle, officially recognized that the Sahara was an integral part of Algeria. He did not, however, renounce the principle that Algerian oil belonged to France, a principle rejected by the Algerians. The compromise reached in Evian during negotiations between the FLN and the French government was to establish, in independent Algeria, a kind of Algerian-French co-sovereignty over its oil wealth. A joint body, responsible for ‘the development of the wealth of the Saharan subsoil’, was created, administered by a board comprising an equal number of representatives of the two founding states, each of them having one vote. This body, with extensive powers, was responsible for supervising the exploitation of oil and gas deposits; it was the representative of the Algerian state in its relations with the companies. Two of the principles adopted at

Evian show very clearly how the French negotiators had pre-empted in advance any attempt by the future Algerian government to make any change to the established order. The fact of freezing in the Evian agreements 'the right of the concessionary and his associates to sell and manage freely their production' guaranteed the supply to France of Algerian oil and did not allow Algeria to create commercial links with other partners. Another clause required the Algerian authorities to grant, for the next six years, in case of equal offers, priority to French companies regarding exploration and exploitation permits, which effectively increased the number of French companies active in the Sahara.

These examples show to what extent the ties between the two countries would be entangled even if Algeria ceased to be a French colony. Algeria found itself bound hand and foot, unable to take any initiative in the oil field without French consent. It could not exclusively take into account its national interests while using such a strategic product (oil) even if this use allowed it to achieve vital political, economic or social objectives. In such a situation, joining OPEC was of no interest to Algeria since it had no means of implementing any decision that the organization might take, given that the treatment of oil matters did not fall directly under its authority. The hydrocarbons component of the Evian agreements had been renegotiated in 1965; a new Algerian-French agreement regulated hydrocarbon and industrial development issues in Algeria. The concept of co-sovereignty was again present throughout the text of this agreement, which created an equal partnership between Algerian and French national companies for the exploitation of Algerian hydrocarbons. The huge area reserved for joint exploitation meant that companies other than French companies were de facto excluded from oil exploration in the Sahara. Algeria was again in an exclusive tête-à-tête with the French oil companies and beyond them the French government. Again, adhering to OPEC was of no use since the organization could not in any way interfere in relations between two sovereign states. This agreement had to be renegotiated in 1970. After months of discussion that yielded no results, the Algerian government decided to implement the objectives it had established during the negotiations. On 24 February 1971 it proclaimed the nationalization of its oil industry (i.e. up to 51 percent for oil fields and 100 percent for gas fields and oil and gas pipelines). It is only from this date that Algeria had any freedom of movement, in a position to diversify its partners and attract other than French oil companies. Membership in OPEC could thus be considered. Algeria became a member of the organization in July 1969, since it was already clear by that date that the 'divorce' from French firms was about to be consummated.

Algeria in OPEC

The duration of the liberation war, led by men with very few, often dilapidated weapons and ammunition in limited quantities but with an iron will, facing one of the best armies in the world, and the enormous sacrifices made by the Algerian people earned the country the admiration of the whole world, in particular other Third World countries. Once independence was gained, the Algerians continued to defend the rights of 'the damned of the Earth', as Frantz Fanon called them, welcoming onto their territory and helping all movements that fought for the liberation of their countries, the defense of their rights or greater justice and equality between men. Its commitment in all these areas and the great fervor it showed when leading this fight earned Algeria the title of 'Mecca of the revolutionaries'. When it became a member of OPEC, Algeria continued to advocate the defense of these same values in the highly strategic sector of the oil industry and sought to inject OPEC with this revolutionary spirit. OPEC itself had begun to change. A few months after Algeria joined the organization, Colonel Muammar Gaddafi came to power in Libya. One of the first steps he took was to start negotiations with the oil companies operating in the country in order to review the price of Libyan oil. He solicited the assistance of Algeria for the implementation of the strategy that would allow him to win the price battle. In 1968 the Algerians had engaged in some arm-wrestling with the French state enterprise CREPS on the conditions of exploitation of the Zarzaitine oil field. Considering that the high rate of production of

the deposit had resulted in a waste of national resources and caused significant damage to the country's oil economy, the Algerian administration had imposed on the French firm a significant reduction in the quantities produced by closing some twenty wells. After studying the operating conditions of a number of deposits, including that of Intissar (Occidental Petroleum) and Zelten (Esso), the Algerian experts dispatched to Tripoli found that both these fields were exploited at very high rates and suggested that Libya insist on a significant decrease in production, just as was done for the Zarzaitine field. Colonel Gaddafi then required the companies present in his country decrease their production levels, promising to revise these quotas if they accepted changes in price and taxation. After nine months of give and take the Libyans won their arm wrestling. The strategy suggested by Algeria proved a winning one. Just a few months after its accession to OPEC, Algeria had participated indirectly in change in the balance of power that had prevailed so far in the oil companies' relations with the host countries. This first victory of a member country of OPEC was the origin of the enormous upheavals that took place later on the world oil scene. In 1970, Algeria continued to be active within OPEC. At the organization's twentieth conference in Algiers in June, it recommended to the ministers' meeting the adoption as a model of relations between producing countries and oil companies the contract it had made with the American company Getty Oil. It had proposed this same scheme a month earlier, during the meeting of what was called the 'refusal front', namely Algeria/Libya/Iraq, aimed at harmonizing the policies of the three countries. It is true that this contract was innovative in many areas. Getty Oil held a 5 percent stake in the Rhourde El Baguel oil field. During discussions with the Algerian government, the company sold 51 percent of this participation to SONATRACH and entered into partnership with it. Getty Oil agreed to raise the posted price by 20 percent and revise the tax rate. It also undertook to place 75 percent of its sales income in Algeria. The most important provision, however, was not financial: the partners agreed that the role of operator would be delegated to SONATRACH in any future joint work. This was a precedent for OPEC countries: for the first time an oil company, an American one, awarded the national company of a producing country the label of reliable and respectable partner, entrusting to it the conduct of operations within the company they had just founded. Another important step for Algeria's policy within OPEC was the oil nationalization. Twenty years after the Iranian attempt to nationalize hydrocarbons, that of Algeria had gone well. In September 1971, the OPEC Ministerial Conference endorsed what was called the 'qualitative request' of Algeria, a proposed resolution that would commit member states to take stakes in oil companies present on their territories. In December that year, Colonel Gaddafi ordered the nationalization of British Petroleum's activities in Libya. In January 1972, the Gulf States (Iran, Iraq, Saudi Arabia, Kuwait) engaged in negotiations in New York with the companies operating on their territories regarding the acquisition of majority stakes in their operations. Saudi Arabia took a 25 percent stake in Aramco on January 1973, Iraq nationalized IPC in June 1972, Kuwait increased its stake in companies operating on its territory to 60 percent, while Iran obtained the transfer of all oil activities – from well to refinery – to the national company NIOC.

Although not responsible for the event, OPEC found itself in the midst of the storm caused by the war unleashed by Egypt against Israel on 10 October 1973; this was called the first oil shock. Algeria played an important role in this turmoil. In solidarity with Egypt and in order to put pressure on Western countries and thus lead them to exert pressure on their Israeli ally, the Council of Ministers of the Organization of Arab Petroleum-Exporting Countries (OAPEC) decided on 17 October 1973 a program of progressive reduction of the oil production of its member countries. The resolution indicated that an immediate retention of 5 percent would be implemented, that it would be increased by the same amount each month, and that a total and immediate embargo was imposed on exports to the United States, the Netherlands, Portugal, South Africa and Rhodesia. The measure had the effect of an earthquake, the consequences of which are felt even today, including considerable repercussions for the development of competitive petroleum energy sources, on North-South relations, on the energy policy and energy economy of Western countries as well as on US policy in the Middle East. Among the decisions adopted by the

OAPEC Council of Ministers was one that charged two ministers, the Saudi Ahmed Zaki Yamani and the Algerian Belaid Abdesselam, to undertake a tour of Western capitals in order to clarify the point of view of Arab countries. The two ministers were received, during their visits to Paris, London, Washington, Madrid, Rome, Bonn, Brussels and Tokyo, by the heads of state or prime ministers of the countries visited, by the president of the European Commission and by the emperor of Japan. In order to closely follow the evolution of the situation, the Council constituted a commission of control of the embargo comprising Saudi Arabia, Kuwait, Libya and Algeria; Algeria was also designated as supply coordinator for African countries.

The permanent presence of Algeria on all key fronts for oil producers, as well the success of the nationalization of hydrocarbons, pushed its prestige to the zenith within OPEC. Among the Gulf countries, the small emirate of Abu Dhabi did not have the human resources to take in hand the 25 percent of interest that oil company members of the cartel had agreed to transfer to it in conformity with the 1972 New York agreement. The Emir, Sheikh Zayed Ibn Sultan Al Nahyan, asked Houari Boumediene, during a stopover made by the latter in Abu Dhabi in March 1974, for assistance with the implementation of the New York resolution. SONATRACH then detached to the emirate a team composed of more than twenty oil executives. This mission lasted 13 years; it helped negotiate partnership agreements with multinationals, create a major oil industry and set up a national oil company, the Abu Dhabi National Oil Company (ADNOC), which later became one of the most dynamic in the Middle East. As can be seen, Algeria played a pivotal role in many events following its accession to OPEC. It was to weigh even more in later years. It would be seen as a defender of the economic interests of Third World countries and would therefore face, live in various international fora, the world's leading power – the United States.

Algeria and the New World Order

In January 1974, as Arab countries ended their program to cut oil production, US president Richard Nixon proposed a conference of OECD countries in order to create a front of consumer countries that would meet the producers within three months. At the same time, the instructions of State Secretary Henry Kissinger were that American diplomats should lobby representatives of the Third World countries and convince them that the tool the Americans were planning to create would serve to defend their interests as well. Such language was likely to be well received by these countries since the retention measures imposed by the oil multinationals following the actions of OPEC member countries had mainly affected them. The American initiative came to fruition at a conference in Washington, 11–13 February 1974, during which the International Energy Agency (IEA) was created; the war machine desired by Henry Kissinger was born. A few days before the conference, the American secretary of state threatened the producing countries with total war should they seek to 'strangle' the industrialized world. This conference and the warlike atmosphere in which it took place provoked an uproar on the part of the producing countries, which had understood that the goal sought by the United States was not to find a solution to the problems of oil shortage but to enter into conflict with OPEC, wrongly accused of all ills. On the other hand, Algerian president Houari Boumediene, acting as president of the Non-Aligned Movement, wrote a letter in January 1974 to the secretary general of the United Nations proposing a special session of the General Assembly be held on commodities and development. To the tendency of Americans to make non-oil-producing Third World countries allies in the battle they were going to wage against OPEC, Houari Boumediene answered with the obvious: oil was only one of the many natural resources the Third World was so rich in and thus the fight against the plundering of these resources did not only concern oil, it was global. By mid-February, all members of the United Nations had endorsed the proposal and on 9 April 1974, the work of this extraordinary General Assembly in New York began. It ended with the adoption of two resolutions; the first one admitted the urgency of the establishment of a New International

Economic Order (NIEO), while the second highlighted the need for aid to poor countries. Despite the decisions taken by the United Nations, the United States persisted in saying that the conference that would deal with the NIEO, which had been scheduled in Paris for the first quarter of 1975, should have focused only on energy and energy issues and therefore only representatives of the IEA and OPEC should have participated. Facing powerful America, Houari Boumediene called on all countries of the south of the planet. First, at the initiative of Algiers, there was the meeting of the 'Group of 77' in Dakar in February 1975. In the communiqué adopted at the end of this meeting, the participants recalled the right of Third World countries to control their natural resources and stated that members of the group would not participate in the Paris conference if the prices of raw materials other than the oil were not on the agenda. Then, in March 1975 the first summit of the OPEC countries took place in Algiers and was a big success for the organization, for Algeria and for its president. The recommendations of the summit, which later constituted OPEC's demands at the Paris conference, fully echoed the points made by Houari Boumediene in his inaugural address – namely, the establishment of a more equitable international monetary system, the stability of the principal currencies necessary for the development of all the countries of the planet, the dollar in particular, and a fall in oil prices in return for a similar effort on the part of the industrialized countries regarding the prices of manufactured products. Boumediene managed another coup at the summit; he succeeded in reconciling the two enemy brothers, Iran and Iraq, both OPEC members, in relation to a dispute over the course of their common border at the level of Shatt-El-Arab. The intense discussions between the two sides of the NIEO negotiations, led by Algeria on the one hand and the United States on the other, which took then place actually reflected the agenda. The conference began on 16 December 1975 and an agreement was reached to create commissions dealing with four key topics: energy, raw materials, development and financial issues. The work of the conference lasted two years from 1976 but did not have any notable results. Much later, the fall of the Berlin Wall and the advent of a unipolar world, resulting in unbridled free trade and the creation in 1995 of the World Trade Organization (WTO), showed that the very principles underlying the notion of a new international economic order were obsolete.

The first step taken by the new Tehran regime in the aftermath of Imam Khomeini's rise to power in January 1979 was to stop crude oil exports. The traders who sold the quantities made available to them by the majors resold them on the spot market at more than twice the official price. This speculation was to be at the origin of the second oil shock, the consequences of which on the economy of developed countries were however less than those recorded during the 1973/4 shock, mainly because of OPEC's commitment to limiting soaring oil prices. In September 1980 the Iran-Iraq war began, which led to a further rise in prices. Five years after the reconciliation between the two countries following the efforts of President Houari Boumediene, who had died in the meantime, Algeria launched a new mission of good intent to put an end to this fratricidal confrontation. His foreign minister, Mohamed Benyahia, made a series of trips between Baghdad and Tehran in order to bring the points of view closer. He died during one of these trips when his plane was shot down by an Iraqi missile as he headed for Tehran.

When it was first established in 1974, it was said that the main objective of the international energy agency was to defend the interests of its members, and in particular to fight against the rise in prices that was systematically attributed to OPEC. This was not exactly reflected in what happened through the 1980s and 1990s when OPEC lost a lot of its power in the oil market, which was taken over by the IEA. This transfer was symbolically formalized in 1984 when Brent from the North Sea replaced Arabian light as the crude benchmark on the market.

Boumediene died in December 1978. The struggle for power in Algeria that followed meant that its role as a pivotal state within OPEC declined sharply. The new teams that took the country's destiny into their own hands were then committed, first and foremost, to sacking all the leaders they had succeeded and strengthening their own power. The deleterious atmosphere in the Algerian energy sector, in addition to disorder in the ranks of OPEC, ended the active participation of Algeria within the organization.

Texas oilmen at the White House facing OPEC and Algeria

George W. Bush's presidency was a major blow for OPEC countries. The first task he tackled upon his arrival at the White House in January 2001 was to establish a new American doctrine in the energy sector. The main purpose of this doctrine was to ensure that US oil companies take possession of maximum reserves in the world's major oil regions. With regard to MENA (Middle East North Africa), the working group that had worked on the issue recommended encouraging attempts to open foreign investment in the oil sectors of several countries, including Algeria, the goal being to eventually achieve the total privatization of their oil industries. That meant a return to the concession system of the 1950s and the disappearance of OPEC. At that time, Algeria was in a special situation. Because of his devouring thirst for power but also because he was looking for support to face the military nomenclatura that had brought him to power, Abdelaziz Bouteflika, who had just been elected president, planned to establish a very close political and economic relationship with the United States and to secure, in a personal capacity, the confidence, even friendship, of the American president. He named his childhood friend, Chakib Khelil, minister of energy. Khelil was an American citizen and had lived for thirty years in the United States. He post-graduated at an American university and worked in several oil companies, as well as at the World Bank. He thus had the connections that would allow Bouteflika to establish the relationship he wanted with George W. Bush and his administration. Of course, getting access to and the support of the president of the United States has a cost. George W. Bush asked the Algerian president to hand over control of Algerian hydrocarbons to American oil companies, which he agreed to. Chakib Khelil's task was to prepare a new petroleum law that would be fully in line with the new US energy policy. This law allowed any foreign company wishing to explore for oil in Algeria to do so either alone or in partnership with the national oil company, which could hold a stake of up to 30 percent. The consequence of such conditions would be that all Algerian oil and gas reserves would have been transferred to foreign companies after a few years. The other great danger was that it set a precedent in the ranks of OPEC. Other countries would certainly adopt the same approach; some because they were predisposed to take such a step and now there was a precedent; other countries might well be pressured to emulate the Algerians. A wave of protest arose across Algeria. The saga lasted five years (from 2001 to 2006). Opposition was so strong that Bouteflika, fearing that he would not be re-elected for a second term, froze the law in 2003. Once re-elected, he adopted it by ordinance, before deleting, in 2006, the most disputed provisions of the law. Algeria and OPEC must pay tribute to Venezuelan president Hugo Chavez, whose intervention was decisive. During a visit to Algiers specifically scheduled for this purpose in May 2006, he convinced his Algerian counterpart to change his mind, given the immense damage his initiative would cause in all oil-producing countries. Algeria – once the great defender of Third World peoples' interests, ready to sell off its own natural wealth to satisfy the ambitions of one man. The soaring price of oil since the beginning of the 21st century accelerated the decline of OPEC. The producing countries have ceased to be a major partner in the world oil scene. The market on the one hand and American oil and shale gas producers on the other hand 'did the job' for them since high prices were needed for shale oil to become profitable. The price of a barrel of oil rising to more than \$100, even close to \$150, made the OPEC countries happy, but they did not see the danger that awaited them. When they realized that American shale oil producers had nibbled their market share, it was too late. Despite the efforts and sacrifices of the last three years, they could not recover the market share they once controlled, nor have they been able to raise the price of a barrel of oil to a more desirable level.

Algeria has never been as rich as it was at the beginning of the 2000s, when shop fronts and displays in Algiers and elsewhere in the country were full of goods and products of all kinds even if people didn't always have the necessary income to meet their needs. The oil rent of the country has caused a certain laxity in the government and amongst its citizens: why create another source of wealth if oil can make life easy for the Algerian population? However, oil sales represent 98 percent of the country's foreign exchange

earnings, which pays for the import of almost everything that Algerians consume. The sharp fall in prices from the ceiling reached in 2008 has dug a huge hole in the budget of the state and of its citizens. This pushed the Algerian energy minister to demonstrate an activism within OPEC seldom seen in the last twenty years. He has been touring the capitals of the member countries of the organization; he went to Moscow and tried to convince the Russians to participate in a joint action with other producers hoping to raise the oil price again. The government sought to develop the production of shale gas and faced the anger of the population of the small town of In Salah throughout 2015. However, none of these initiatives produced the desired results.

However, regardless of Algeria's role in OPEC, the big question concerns the organization as a whole: will OPEC survive the great crisis it is going through now?

From norm entrepreneur to reluctant overachiever

Venezuela in the history of OPEC

Antulio Rosales

Venezuela is often cited as an important factor in the global oil market of the twentieth century (Colgan, Keohane, and Van de Graaf, 2012; Yergin, 1993; Karl, 1997). From the late 1920s to the late 1960s, Venezuela was the world's largest oil exporter and among the top producers. Together with the largest oil producers in the Middle East, Venezuela holds the largest world reserves. Most importantly, over time Venezuelan state officials developed the confidence and capacity to regulate foreign companies that operated in the country, progressively exerting regulatory measures that became important benchmarks for other producers elsewhere. The country developed a strong identity as a 'landlord state' and promoted multilateral coordination among oil nations to intervene in the global oil market and protect their own interests.

The rise of the Organization of the Petroleum Exporting Countries (OPEC) and the different crude producers' benchmarks throughout the second half of the 20th century are institutional innovations that emerged from the Global South. These innovations may be viewed in line with recent scholarship in international relations that has sought to highlight the significance of peripheral states in the formation and diffusion of global institutions, norms and behavior (Acharya 2016; Helleiner 2014; Helleiner and Rosales 2017; Sikkink 2014). In this case, Venezuela, through its well-known minister of development, Juan Pablo Pérez Alfonzo, became an important player in the formation of OPEC. The role of Pérez Alfonzo as well as Venezuela's notions of the 'petroleum pentagon' were pivotal in the organization's development (Garavini 2011; Prasad 2008). These principles were forms of 'localizations', as Acharya explains (2004, p. 241), through building 'congruence' between existing norms – in this case among major producers in the United States, most notably the Texas Railroad Commission (TRC) – and local beliefs and practices.

OPEC's success as a cartel, however, has been questioned (Radetzki, 2012; Colgan, 2014; Fattouh and Sen, 2016). The history of the organization is plagued with cheating relating to production quotas and with contentious moments among its members, between member states and non-OPEC producers, and with major consumers (Colgan, Keohane and Van de Graaf, 2012; Van de Graaf et al. 2016). Regardless of the importance of OPEC as a cartel, the organization holds fundamental reputational value for its members (Colgan, 2014), and it represents an arena for multilateral cooperation, information sharing, monitoring and the establishment of rules. Of course, it is also subject to contentious politics (Claes, 2001).

Despite Venezuela's initial protagonism in OPEC, the country progressively became a follower as its share in the oil market declined over time. The reasons for this decline lay in the country's domestic disputes around the desire to control the oil industry and the evolution of its identity as an oil nation. In the 1980s and 1990s, a productivist logic around the oil industry became hegemonic, encouraging an increased production above OPEC quotas. The government pursued this production-maximizing logic as Venezuela's national oil company (NOC), *Petróleos de Venezuela (PDVSA)*, captured important decision-making nodes and effectively controlled the nation's oil policy (Mommer 2003; Hults 2012; Rosales 2018a), undermining the traditional principles of rent maximization and conservation. The expansion of production came as a result of a liberal policy of opening up to foreign investment in the upstream of the industry, known as *apertura* (Manzano and Monaldi, 2010).

In the 2000s, a dramatic transformation of Venezuela's political system took place with the rise to power of Hugo Chávez and his Bolivarian Revolution. Among the main pillars of his movement, dubbed *chavismo*, was the goal of eliminating this oil opening, the return to the traditional logic of a rentier landlord state and the strengthening of OPEC around price-protecting principles (Lander, 2002; Mommer, 2002b). The government sought to control the industry and especially PDVSA in order to promote social spending and political stability. The rise of resource nationalism under Chávez coincided with the rise of the oil price as a consequence of increased demand by China and other emerging powers. The high price juncture also contributed to a relatively cordial intra-OPEC dynamic.

This dynamic changed after the 2014 oil price drop. Between 2014 until 2016, the leading strategy by Saudi Arabia was to protect market share rather than prices (Ramady and Mahdi 2015; Almonneef, this volume). The plan was to put pressure on marginal producers, such as those in the US shale and tar sand industry, by maintaining production levels and not resisting low prices. This upset the Venezuelan position, which was heavily dependent on a high price due to its inefficient model of price controls and social spending. During this time, the government of Nicolás Maduro unsuccessfully attempted to push for a production cut among OPEC countries. Simultaneously, Maduro's regime also engaged in a fierce battle to control PDVSA, pursuing a purge of its managerial staff. Nevertheless, through its own industry's collapse, Venezuela contributed the most by involuntarily reducing its own production by over 1 million bpd. This massive industry collapse is one of the factors that have contributed to the more recent increase in oil prices.

This chapter explores the evolution of Venezuela in the OPEC and the role that OPEC has played for Venezuela as a major oil producer and landlord state. The chapter explains the paradoxical shift of Venezuela from a founding member of the organization to follower and reluctant overachiever. The explanation for these shifts lies in conflicting views within Venezuela between notions of sovereignty and the role of the petro-state and global oil producer.

The concessionary era: a preamble

There is a wealth of literature centering on the evolution of the concessionary system that largely organized oil production from the early 20th century until roughly the 1960s and 1970s (Parra, 2004; McBeth, 1983; Tugwell, 1975; Coronil, 1997). States, as landlords or proprietors of subsoil resources in much of the developing world, set up concession agreements for companies to explore and extract minerals and hydrocarbons. State control and nationalizations eventually superseded the era of concessions. In the Venezuelan case, the era of concessions is intimately linked to the dictatorial regime of General Juan Vicente Gómez, who ruled the country between 1907 until 1935. Through this regime, foreign corporations obtained large plots of land and extracted crude oil under a liberal framework that allowed companies to extract large profits.

In 1943, Venezuela was gradually transitioning to a more open political system. General Isaías Medina Angarita, taking advantage of a positive international environment marked by the war effort and the allies'

need for a continuous supply of oil, attempted to increase state participation in the business and increase rent intake. A new hydrocarbons law was negotiated with companies, the US State Department and Medina's regime. The most important provision of the law was a complete renegotiation of concessions, which aimed to solve all legal breaches in the previous contracts. This renegotiation included drafting new concessions to the same companies in exchange for their commitment to follow the new regulations. The new royalty would be one-sixth (16.33%) of output, the income tax imposed on companies would be 12 percent, and customs fees were to be applied for company exports and imports. The law also obliged companies to build refineries in Venezuelan territory, enabling for the first time the development of downstream linkages in the industry.

The emerging left-leaning anti-imperialist party *Acción Democrática* (AD) heavily criticized Medina Angarita's reforms. Juan Pablo Pérez Alfonzo, AD congressional representative and oil nationalist expert, opposed the new law because it meant relinquishing any claims against the legality of the concessions from the Gómez era. Unsurprisingly, once AD rose to power in 1945 (after a military coup overthrew Medina Angarita), the law was reformed once again. The reform brought an additional tax on profits to bring state rent intake to 50 percent. According to Parra (2004), these provisions faced little to no resistance from corporations, mainly because companies credited these increased taxes against US income taxes. With time, the 50/50 arrangement spread among major producing nations, beginning with Saudi Arabia and later including Kuwait and Iraq (Yergin, 1993; Parra, 2004).

In the 1950s, oil-producing nations in the Middle East and Venezuela increasingly coalesced around their identity as landlord states and faced rising motivations to cooperate in terms of policies and prices. In 1958, after a civil-military rebellion overthrew General Marcos Pérez Jiménez, AD returned to power, now with the intention to consolidate a multi-party democracy with the cooperation of other centrist parties and a developmentalist agenda (Urbaneja, 2013). During Venezuela's first democratic government led by Rómulo Betancourt after the military dictatorship, Pérez Alfonzo was in charge of the Ministry of Mines and Hydrocarbons. Pérez Alfonzo promoted five clear policy lines, which became reference points for Venezuela's oil policy for the next two decades and influenced other producers. The 'petroleum pentagon' included a commitment to cease granting any more concessions to foreign companies. Further, it sought the creation of a NOC to give Venezuelans managerial capacity in petroleum, aiming at gradually replacing the concessionary system with a national monopoly. Third, it sought the improvement of state revenue intake from the oil industry. Fourth, the government developed a conservation policy for the resource by protecting reserves, reducing production and defending prices. Lastly, and tied to the former goals, the government fostered coordination with other oil-producing countries to exert their power in defence of the resource, its market price and business conditions vis-à-vis concessionaires (Garavini, 2011; Darwich Osorio, 2015).

OPEC and Venezuela's norm entrepreneurship

In the late 1950s, the IOCs' strategy to influence production levels in Venezuela and the Middle East in order to improve their market conditions was challenged. After previous and failed attempts at direct diplomatic cooperation, a cooperative proposal was seen with better eyes as a reformer in Saudi Arabia, Abdulla al-Tariqi, director of mines in the Saudi government, advocated nationalist ideas that resembled those perused by the Venezuelans in 1936–1948. Venezuela and Iran were invited as observers in 1959 to the first Arab Petroleum Congress in Nasser's Cairo. Pérez Alfonzo engineered a stealth meeting with Tariqi, and the two agreed with an Iranian representative in an unwritten pact, known as the Maadi Pact, to keep prices stable. The rest of the agreement resembled Pérez Alfonzo's Petroleum Pentagon. Specifically, it centered on the creation of NOCs, the advancement of refining in producers' territories, the protection of state profits following the Venezuelan threshold of 60–40 profit share, the need to reach

agreement among all parties before changing prices, and the enhancement of cooperation on conservation, production and exploitation.

As the literature on norm diffusion points out, there are different mechanisms through which norms ‘travel’. Similarly, norms have different points of origin and can emerge from the periphery of the international system (Finnemore and Sikkink, 1998). Scholars in international relations and other social sciences have noted the often-complicated directions of policy diffusion (Sikkink, 2014; Acharya, 2014; Helleiner and Rosales, 2017; Helleiner, 2014). The borrowing and adaptation of policy ideas from different contexts has been noted in reference to Latin American free-traders of the 19th century as well as by its protectionist counterparts as ‘alternative localizations’, as they included policies and ideas that did not conform with the hegemonic doctrines emerging from the core of the international system (Helleiner and Rosales, 2017). In similar ways, the TRC served as an example to resource nationalists in the Global South that sought to defend the interests of oil-producing nations and uphold resource conservation (Parra, 2004). The TRC model of price protection was ‘localized’ and adapted to the national context in Venezuela’s nascent democracy through Pérez Alfonzo’s Petroleum Pentagon. Starting with the Fifty-Fifty Agreement, the values of cooperation and resource conservationism tied to the Petroleum Pentagon became ‘transnational’ norms that flowed from Venezuela to other oil-producing nations.

In 1960, OPEC was created in Baghdad after the Seven Sisters unilaterally decided to drop prices to 1950 levels in reaction to increasing competition from Italy’s oil company Ente Nazionale Idrocarburi (known as ENI) and from the USSR. At the time, the five founding members of OPEC represented 83 percent of total world output. Thus, this was among the boldest moves made by Third World nations in the global economy. OPEC was indeed an action by producers to impact prices, but it was also a crystallization of emerging notions about the role of natural resources in the pursuit of development (Prashad, 2008; Garavini, 2011; Mora Contreras, 2009). This initiative served as a precursor—more than a decade before the launching of the New International Economic Order (NIEO)—of Third World stances on the governance of the global economy as ‘oil producers anticipated the creation of UNCTAD [United Nations Conference on Trade and Development] by giving birth to their own co-operative structure in 1960, to deal with the declining price of commodities’ (Garavini, 2011, 476). It also represented a stance held by Third World countries aiming to take part in multilateral cooperation from their position as sovereign states. Betancourt defended this move as a nationalist position in consonance with multilateral behavior. Recalling the creation of OPEC, he argued in a speech years later: ‘we are in an interrelated world; nobody can aspire to make exclusively national decisions, nationalism is not incompatible with internationalism’ (Betancourt, 1978, p. 27).

OPEC initiated a gradual shift in the balance of power away from IOCs to producer states. This shift was not by any means a process of absolute power change; rather, it was a negotiated process that enhanced states’ control over operations while the Seven Sisters remained important cooperation entities and exerted pressure in local as well as global markets (Parra, 2004). The footprints of these changes can be found in Venezuela’s historical process of acquiring knowledge and exerting its power as a landlord state through state regulation. Other partners in the Middle East and North Africa effectively adopted Venezuelan benchmarks of rent appropriation as acceptable norms, beginning with the Fifty-Fifty Agreement. As Pérez Alfonzo put it, ‘the example-demonstration of Venezuela’s measures and government policies ... transcended to other exporter countries with whom we had initiated contact’ (Pérez Alfonzo, 2011, p. 288). A delegation from Venezuela had traveled to the Middle East attempting to convince other producers of the Fifty-Fifty Agreement (Yergin, 1993). The goal was to prevent Venezuela’s losing market share by favoring more flexible markets. In addition, these cooperation ideas appealed to an identity of oil producers with the ‘right’ to extract royalties and benefits from the fruits of the earth. Pérez Alfonzo described it as follows: ‘for the first time in the international history of oil an concessionary country exercised its sovereign right to change unilaterally the tax and royalty rates’ (Pérez Alfonzo, 2011, p. 288). Second, such measures responded to a sense of international justice toward the owners of natural resources (Betancourt, 1978).

During the 1960s, low prices remained the norm, but producer states had initiated different mechanisms to exert further control on rents and price, while seemingly unrelated events also contributed to a subsequent upturn of prices. Muhammad al-Qaddafi's increasing tax revenues from concessionaires in 1961 was an important innovation. Later, Venezuela increased corporate taxes on companies to 60 percent. In the OPEC conference held in Caracas in December of 1970, member states reached a consensus to declare a minimum 55 percent income tax on companies and gradually increase prices (Alnasrawi, 1973). Moreover, at the end of the decade, what was considered the 'peak of oil' had been reached in both the United States and Venezuela (Garavini, 2011). The peak oil notion contributed to Venezuela's position in favor of conservationism and price protection at the Caracas meeting. Lastly, US president Richard Nixon's unilateral abandonment of the gold standard put an upward pressure on prices. The devaluation of the dollar prompted intense negotiations between companies and producing states, which agreed to an increase of 8.75 percent in oil prices (Alnasrawi 1973).

In 1973, a concerted move by Arab countries, known as the 'oil embargo' on western powers in political response to the Yom Kippur War, provoked a dramatic price increase. This price hike was concomitant to a radicalization of Third-Worldism. Third World nations advanced a code of economic rights for developing countries and sought to strengthen the Non-Aligned Movement (NAM). The NAM sought 'the extension to the international economic system of the redistributive framework that had been consolidated in the social democracies of Western Europe after World War II' (Berger 2004, 24). A largely symbolic outcome of this movement was the approval of UNCTAD's NIEO document in the United Nations' General Assembly in 1974. Indeed, 'the call for a NIEO followed on the heels of the 1973 oil crisis and the demonstration by the OPEC of its ability to set the price of oil' (Berger, 2004, p. 24).

While the NIEO was never implemented and the implications of the oil price increase actually generated the basis for crises both in developed and developing countries that precipitated neoliberal restructuring, it consolidated the final steps for nationalization in major oil-producing nation states. It also meant an important ideational mobilizer for Third World nations that sought to attain more control over their natural resources. In Ecuador, for example, the ideas of Pérez Alfonzo were well known, and influenced the policies of resource nationalism pursued by the military regime of Guillermo Rodríguez Lara in the 1970s (Philip, 1982). In this case, the role of nationalist-conservationist Gustavo Jarrín Ampudia, minister of oil at the outset of the regime, was crucial. Ecuador's desire to enter OPEC was notably guided by its desire to boost its international reputation and join the club of other landlord states with nationalist goals (Jarrín Ampudia, 1976; Rosales 2017). In the mid-1970s, an optimistic Pérez Alfonzo argued that the history of OPEC 'has shaken the world and feeds hopes to build a new economic order' (Pérez Alfonzo, 2011, p. 288).

An inevitable nationalization

During Pérez Alfonzo's tenure in the ministry, the government created Venezuela's *Corporación Venezolana de Petróleos (CVP)*, an NOC with the goal of gaining expertise at all levels of the oil industry from extraction to commercialization, transport and management. The CVP remained a small enterprise during the 1960s, which worked well under AD's conservationist paradigm, as concessionaires continued to extract oil and the government did not wish to contribute with meaningful production of its own, which might drive prices down further (Tugwell, 1975). Pérez Alfonzo's conservationist policy derived from his understanding, mistaken as it was, that proven oil reserves had reached their limit and Venezuela's crude was close to exhaustion. But most importantly, Pérez Alonzo was at the core a nationalist who wished to limit concessionaires' extraction because of his belief that the remaining crude should be under the absolute control of the state. Lastly, he heralded a notion that non-oil-related revenue was required to increase faster than oil revenues to enable diversification (Pérez Alfonzo, 2011).

Throughout the 1960s, the major oil companies had no incentives to invest as there was a general consensus that once concessions expired in 1983 and in 1996, they would not be renegotiated. The companies defended their positions in the political arena, opposing the government's attempts to expand its claim on oil rents. Companies decided to make their presence in the country as inexpensive as possible (Tugwell, 1975). As a result, underinvestment ensued, which led to aging infrastructure and equipment, lower exploration and stagnant reserves. Concessionaires increased production to the highest possible capacity in search of the last possible drop of oil; production reached 3.7 million bpd in 1967 (Urbaneja, 2013).

The gradual shift in power toward the landlord state culminated with the nationalization of the industry in 1975. The state–corporations' relations in the country pointed to the eventual reversion of all concessions to the state in 1983 and 1996 (Silva Calderón, n.d.; Philip, 1982). Advancing a nationalization process was largely uncontroversial. Other OPEC nations had previously followed this process. In 1975, President Carlos Andrés Pérez introduced a law of nationalization, which at this point was a matter of broad consensus across the political spectrum. That is, returning state control over the oil industry was largely consensual in the political establishment. Nevertheless, the kind of nationalization that took place, with important compromises given to IOCs, was still a matter of controversy. After broad discussions, the nationalization law protected the autonomy of the industry, making the national managers of the IOC concessionaires in charge of the newly nationalized company, PDVSA. The nationalization law ended all concessions starting in January 1976. It also meant the creation of a holding company, PDVSA, with the state as the sole shareholder, while it protected workers in the industry during the transition to state ownership. Nationalization also contemplated the compensation of foreign concessionaires, despite criticism from the left. Lastly, the law allowed for the possible association of the state with foreign companies in operations where technical assistance would be required (Article 5) (Congreso de la República, 1975).

For the nationalist left, the terms of nationalization must have reflected the spirit of the reversion law (approved by Congress in 1971), centering on confiscation and a complete rupture of ties with foreign corporations (Mommer, 1999; Mendoza Potellá, 2010). Regardless, concerns around the complexity and interdependence of the oil business justified the terms of Article 5, according to which the state could 'enter into agreements of association with private entities, but with participation such that [it would] guarantee state control, and for a limited duration' (Congreso de la República, 1975). Nationalists from the left, with the support of Pérez Alfonzo, fiercely opposed Article 5, arguing that this was in fact an obstacle to true nationalization; it meant a 'truncated nationalization' (Pérez Alfonzo, 2011, p. 234).

Market dominance and the counter-shock

After the 1970s oil price shocks, major oil consumers decided to shift away from OPEC producers' supply. The result was increased cooperation among consumers and a relative increase in the importance of non-OPEC suppliers. In turn, OPEC tried to restrict the oil supply twice in the 1980s to protect prices, mainly with Saudi Arabia taking the burden of export cuts (Van de Graaf et al., 2016; Claes, 2001). The dramatic loss in Saudi market share without successfully helping to increase prices demonstrated the failure of OPEC's quota system (Fattouh and Sen, 2016). Furthermore, OECD developed conservation strategies that resulted in a sustained decrease in demand from approximately 44 million to 36 million bpd (Ramady and Mahdi, 2015). Sustained investments in new reserves and exploration brought about an oil glut and the collapse of prices in 1986.

Broadly speaking, market-oriented governance mechanisms were becoming the rule at the time and the logic of increased production quickly spread among oil countries. Private actors and principles took the lead in the global energy market. As Fattouh and Sen (2016, p. 78) pointed out:

this period consequently laid the ground for the development of the current structure of oil markets, with physical, forward, futures, options, and other derivatives' markets flourishing and with oil benchmarks namely Brent, West Texas Intermediate, and Dubai playing a key role in the new international pricing system.

Furthermore, 'the move towards market-based pricing opened a new history in the chapter of the oil market, which saw OPEC lose control of the administered pricing system and its price-setting power' (Fattouh and Sen 2016, p. 78).

What is more, NOCs around the world incorporated private actor logics and behavior. Venezuela's NOC, *Petróleos de Venezuela*, developed an ambitious strategy in the 1980s to vertically integrate and internationalize its operations (Urbaneja, 2013; Giusti, 1999; Hellinger 2017). The goal was to become closer to its buyers' markets by setting up refineries and gas stations in the Caribbean, Europe and the United States. The internationalization plan was coupled with a broad project of opening to upstream and downstream investments in the Orinoco River belt (Giusti, 1999). As it has been argued elsewhere, this logic contradicted the traditional identity of the landlord state that sought to maximize rents over production (Rosales 2018a). In fact, nationalist observers highlight that the internationalization plan sought to divert rents away from the state and into the company itself (Rodríguez, 1997; Mommer, 2002a).

After successfully lobbying the Supreme Court to allow new contracts under the guise of Article 5 of the nationalization law, PDVSA introduced production sharing agreements and operation contracts, allowing new investments in extraction (Giusti, 1999; Manzano and Monaldi, 2010). These contracts reduced royalty rates and income tax to historical low levels while shielding investments with PDVSA's assets as guarantees (Rosales, 2018a; Hellinger, 2017). By 1998, Venezuela had increased its output by 800,000 bpd. PDVSA argued that heavy and extra-heavy oil was not oil but bitumen, and that this move justified breaking the OPEC quotas, as conventional field production remained stable (Hellinger, 2007; Mommer, 2003).

For Philip,

it was possible to argue in 1994, when PDVSA was only modestly in breach of its OPEC quota, that Venezuela was simply becoming a more individualistic, less team-spirited, member of OPEC in recognition of the fact that its good behavior in the past had not been recognized'

(Philip, 1999, p. 372)

Even so, he argued:

this argument was clearly unsustainable by early 1998. There can be little doubt that 800,000 b/d is a high enough to influence the world price of oil. This means that [...] Venezuela is increasing its oil income by less than it is increasing production.

(Philip, 1999, p. 373)

Mommer also blamed PDVSA for low oil prices: 'world petroleum prices broke down again, and this time it was PDVSA to blame, not the ministry or OPEC' (Mommer, 2002a, p. 209). Fattouh and Sen (2016) argued, in turn, that this increase in production prompted Saudi Arabia's increased output of 300,000 bpd in 1998 as a way to discipline Venezuela's defiant behavior.

For Luis Giusti, PDVSA's top executive at the time, the policy of *apertura* represented a bold move to challenge the traditional notions of the Venezuelan oil state. PDVSA and Giusti challenged the authority of the Ministry of Mines, and in turn, that of OPEC (Rosales, 2018a). The broader ideational inspiration in this change of orientation was a move away from rent-maximizing logics to productivist principles (Urbaneja, 2013). For Giusti (1999, p. 121), these new principles had become commonplace for producers:

the specific needs and circumstances of producers, technological processes that greatly reduced production costs and growing demand have made the owners of the low-cost barrels increasingly reluctant to curtail their production, since limits entail the loss of market-share to non-OPEC competitors.

The loss in revenues from the state would be compensated for by new forward linkages and increased interdependence at the level of the downstream global energy market, bringing about a dramatic change in the outlook of producers as emerging outward entrepreneurs (Giusti, 1999; Hellinger, 2007; Urbaneja, 2013). PDVSA eventually became a global corporation, lauded for its increased capacity and vertical integration while at the same time criticized by nationalists at home for decoupling from the interests of the state (Hults, 2012; Urbaneja, 2013; Mommer, 2003).

PDVSA's take-over of oil policy formulation in Venezuela has been noted as a case of increased autonomy and principal-agent problem, commonly depicted as a 'state within the state' (Mommer, 1999, 2003; Hults, 2012). The underlying state-company struggle reveals the contention between the principles of a landlord state and a global oil producer (Rosales, 2018a). Nevertheless, this contention also had international reverberations, as OPEC sought to protect market share and, in light of its failures as an apparent cartel, abandon the promise of protecting prices. The general energy market saw an increase in private dominance, and deregulation that eventually stimulated marginal producers and new technologies (Vivoda, 2016; Ramady and Mahdi, 2015).

The return of the rentier state

The objectives of the new oil policy promoted by Chávez centered around the following main issues: strengthening OPEC and bringing Venezuela back to its traditional landlord position of defending prices, restoring the regulatory capacity of the Ministry of Energy and Mines over the industry in general and over PDVSA in particular, and in doing so maximizing rent acquisition via royalties (Lander, 2002; Mommer, 2002b). Chávez's oil policy resembled the 'petroleum pentagon' of the mid-20th century and promoted increased cooperation among producers. As Ellner (2007) argues, Chávez's OPEC policy was illustrative of two fundamental aspects of his foreign policy. First, Chávez believed that strengthening OPEC through bilateral diplomacy was a strategic move that would promote higher prices. Second, and perhaps more importantly, OPEC and oil diplomacy more generally gave Chávez an important platform to enhance a new Third Worldist alliance and accomplish his goals of pursuing a multi-polar world. Hence, Chávez also used oil to develop cooperation agreements in Latin America and the Caribbean that attempted to internationalized social policies based on oil revenues and which ultimately served to gather international solidarity for the Bolivarian Revolution (Muhr, 2012; Benzi, 2016; Burges, 2007).

For these reasons, Chávez traveled to all OPEC member countries to invite heads of state to the second-ever heads of state summit of the organization. Chávez's active diplomacy paid off, contributing to his successful reactivation of OPEC quotas and unifying objectives and coordination from the main producers. Venezuela's proposed price band was approved in the meeting. Soon after the summit, Chávez's minister of energy and mines and well-known oil nationalist Ali Rodríguez Araque was named secretary general of the organization (Rodríguez, 2012; Ellner, 2007). More importantly, Chávez initiated a battle for control over PDVSA that included the company's respect of OPEC quotas (Mommer, 2011).

Later, in 2001, the government approved a controversial new hydrocarbons law. The new law returned the power of oversight and policy design to the Ministry rather than the company. Foreign investment was to be protected under the framework of joint-ventures with majority shares for the state, while royalty payments and income tax were adjusted, increasing the former and lowering the latter (República Bolivariana de Venezuela, 2001). The principles of sovereign control over natural resources were mentioned in the law and reiterated in speeches by Chávez and other top officials (Mommer, 2011; Rodríguez, 2012).

Control over underground resources became the epitome of Chávez's resource nationalism and translated into a fierce struggle with PDVSA (Rosales, 2018a).

PDVSA's managers resisted Chávez's policies, especially the new hydrocarbons law. Later, they openly opposed the president's appointment of new managers that were loyal to his political project because such appointments were seen as breaching the company's meritocratic culture. PDVSA's managers called for a strike twice between 2002 and 2003, first leading to a coup attempt in April 2002, and later to a complete standstill of the industry's operations (Hults, 2012; Philip and Panizza, 2013; Rodríguez, 2012; Mommer, 2011). The goal of the strike was to force Chávez's resignation and the withdrawal of all laws approved by the executive in 2001. Instead, the government controlled the rebellion with a military takeover of the company, ensuring control. The government fired more than half of the company's payroll staff for joining the strike, effectively purging the company of dissenting voices and ensuring staff loyalty (Philip and Panizza, 2013; Luong and Sierra, 2015; Manzano and Monaldi, 2010; Hellinger, 2017).

During a legal process of forced migration from operating contracts in the Orinoco River Belt to joint ventures, the Venezuelan government assured increased control and higher oil revenues. Between 2003 and 2008, the sustained increase in oil prices was due to the increase in demand from China and other emerging economies rather than to OPEC action (Colgan 2014; Ramady and Mahdi, 2015). Regardless, as Colgan (2014) suggested, the idea of OPEC membership, and particularly of Venezuela's leadership, has been used domestically to attribute the price increase to Chávez's intellect. In 2008, a new progressive tax was applied for extraordinary profits at times of high prices (Manzano and Monaldi, 2010). The government used PDVSA as a bankroll agency, dedicated to providing surplus funds for social programs and, in some cases, directly executing them. According to the company's 2016 business report, in the past 15 years, it contributed over 265 billion USD to social programs and development funds with negligible institutional oversight (Petróleos de Venezuela, 2017).

The government devised several mechanisms to centralize the use of oil rents. Most notably, the government set up a policy of capital and exchange controls that overvalued the legal tender and centralized the distribution of foreign currency (Dachevsky and Kornblihtt, 2017; Saboin García, 2017; Palma, 2013). Moreover, through a series of changes in the Central Bank law, the executive created dollar-denominated funds from 'surplus' oil rents (above the level of the national budget) for discretionary use of the presidency (Rosales, 2016; Balza Guanipa, 2017). This model allowed the government to pursue active social policies that lowered poverty rates for a few years and secured a remarkable electoral performance for Chávez and his movement (Urbaneja, 2013; Corrales and Penfold, 2011).

A reluctant overachiever

The policies enacted under *chavismo* led to the underinvestment of the oil sector and the weakening of PDVSA. Under high oil prices, however, Venezuelan production was sustained between 2.7 million to 3.3 million bpd. This changed with the drop in the oil prices of 2014. Until this point, the country had accumulated huge debts to China and private investors but was increasingly unable to find new sources of financing. The government opted to print inorganic money to fill the gap between revenues and expenditures, producing an unprecedented inflationary crisis. Hyperinflation was coupled with severe scarcity due to the sustained controls on prices on most productive chains, provoking a deep social and economic crisis that has since led to double-digit recessions, a migratory wave and increasing poverty rates¹ (UCAB, 2018; Rosales, 2018b). In this context, the Venezuela oil industry was brought to the verge of collapse. Today, much of its production is used to pay off debts and satisfy the increasingly inefficient internal market, which is highly subsidized (Monaldi, 2018).

The shale revolution and the increase in oil output coming from the United States and other countries has been seen by Venezuelan officials as a 'political weapon' to weaken critical emerging powers such as Russia, Iran and Venezuela. Since late 2014 and throughout 2015, the government of Nicolás Maduro

attempted, largely unsuccessfully, to gather support within OPEC to make production cuts that could support a price increase. This international campaign was led by Rafael Ramírez, first as minister of foreign affairs and later as ambassador to the United Nations. Ramírez was a long-lasting minister of oil and was president of PDVSA during most of Chávez's administrations. Ramírez led several delegations and meetings in OPEC as well as with Russia, Mexico and other producer allies to convince them to join a major agreement to curb production.^{2 3 4}

This time around, Saudi Arabia did not wish to bear the burden of a major production cut—which it had experienced in the 1980s—and chose to protect its market share. The argument was that low prices would drive out of business the high-cost crudes coming from US shale and Canada's tar sands, among other unconventional yields, giving prevalence to lighter and conventional crudes⁵ (Ramady and Mahdi, 2015). Furthermore, there was doubt as to the willingness of other producers such as Iran and Russia to follow through with a production cut. As Ansari (2017, p. 174) argues: 'OPEC attempted to defend its market share and to test for the elasticity of supply and survivability of shale in an uncertain environment'. Nevertheless, a change in attitude from Saudi Arabia came late in 2016 when it was able to strike a deal with Russia, Iran and other OPEC allies to cut production.

Paradoxically, while Ramírez tried to gather international support within and outside of OPEC to protect prices, President Maduro waged another battle with PDVSA. This renewed struggle has been largely overlooked and its similarity with the state–company dispute of 2002 has been ignored. This time, the aim was to purge the company of Ramírez's inner circle and to replace top managers with *maduristas*.⁶ Ramírez had become a dissenting voice within *chavismo*, initially calling for sensible reforms to the foreign exchange regime, gradual reductions in the domestic petrol subsidy and other market-oriented policies that would allow the refinancing of Venezuela's debt.⁷ Later, he denounced Maduro's increasing authoritarianism within the ruling party and questioned his true commitment to the legacy of Hugo Chávez.

Ramírez attempted to gather support as the true heir of Chávez's legacy, but Maduro had the upper hand, with increasing repressive power and complete control over state institutions. Over 60 top PDVSA officials were dismissed and persecuted for corruption charges from 2016 onward. In addition, former PDVSA president and former minister of oil Eulogio del Pino was arrested together with former Citgo CEO Nelson Martínez, in late 2017⁸ (Monaldi, 2018). This precipitated the resignation of Ramírez from his post as ambassador to the UN. In January 2018, the government-appointed attorney general, Tarek William Saab, issued an international arrest warrant against Ramírez, who remains in exile.

The power struggle in the Maduro administration had the oil company at the centre. While the establishment of PDVSA did not openly contradict Maduro's authority as it had in 2002 under Chávez's rule, Maduro still considered the company's managers a threat to the stability of his increasingly authoritarian regime. Military official Manuel Quevedo was appointed the company's CEO and minister of oil with a mandate to increase oil production. In addition to this radical change in leadership, PDVSA and the oil industry more generally had suffered from workers fleeing the country's economic hardships. The nation's output has declined systematically since 2016, in addition to the collapse in prices. The largest share of production decline came from PDVSA-operated fields, while joint ventures followed the decline. According to OPEC's monthly report, in August 2018, PDVSA's production was 1,235 million bpd, more than 1 million bpd less than in 2015. That same month, there were 69 active rigs, down from 110 in 2015 (OPEC, 2018). Beginning in 2015, Venezuela has single-handedly achieved a major cutback in oil output that has, in part, contributed to the increase in oil prices. Venezuela reluctantly surrendered oil exports, making OPEC's 2016 production cuts easy to achieve.

The dramatic collapse of the Venezuelan oil industry is in part a result of the country's broader economic crisis but is also a consequence of its incompetence and paralysis following the managerial swap. External factors have also impacted the fate of the industry. US-imposed financial sanctions that ban US banks from engaging in debt renegotiation have affected the company's ability to obtain new credits.⁹ Recent rulings from arbitration tribunals that demand PDVSA's retribution of over US\$ 2 billion to

ConocoPhillips for the nationalization of its assets in 2007 reduced the company's possibility of meeting its export commitments. Following this rule, a dispute over the use of Caribbean terminals hampered the country's ability to export.^{10 11} US-Venezuela relations worsened at the outset of 2019 when Nicolás Maduro was sworn in for a second six-year term after questionable elections were held in May 2018. The administration of Donald Trump backed up the claim of Juan Guaidó, speaker of the National Assembly, to be the legitimate interim president of the country until new elections can be held. The US followed with tougher sanctions on PDVSA, banning oil trade between the company and US buyers.¹² Similarly, China's bet on Venezuela's stability has been seriously challenged in the past few years, with loans and investments stagnating. Whereas at the outset of Venezuela's economic crisis China was flexible regarding delays in oil shipments, it has become increasingly evident that Venezuela is unable to meet its commitments given the current state of the oil industry. Chinese state-owned enterprises have therefore only committed funds to Venezuela's joint ventures with the stipulation that these funds are used to increase oil production. Russia has been a more solid supporter of the Maduro government, offering some loans and investments in the oil industry while allowing potential payments to be made through Rosneft to Venezuelan oil sales to avoid US-imposed sanctions.¹³ Venezuela's production and exports shrunk in 2019 and the country has drastically changed its destination for exports to Asian partners, especially India.

The desire to control PDVSA and its use as a political tool during the governments of Chávez and Maduro led to undermining the company's capacity to extract oil. During Chávez's administration, the government sacrificed the expertise of managers who opposed it. The administration increasingly relied on foreign investors, especially in the joint ventures of the Orinoco River Belt. In the current government, a new struggle for control ensued since 2017, this time to replace the circle of traditional *chavistas*, led by Rafael Ramírez, for *maduristas*. Nevertheless, this strategy proved disastrous due to the decline in oil prices and the international environment of 'debt toxification' that has closed avenues for financing the company.¹⁴ In a desperate attempt to cope with the crisis, the Maduro government has opted for a fire sale of assets, both domestically and abroad, this time receiving less enthusiasm from China, and instead increasing the stake of Russian state capital in Venezuela's oil industry (Kahn, 2017; Monaldi, 2018). In sum, the dramatic decline in oil production has hindered Venezuela's importance in OPEC, transforming the country from a strong advocate of price protection to a reluctant overachiever.

Final remarks

This chapter summarized the trajectory of Venezuela as a founding member of OPEC. Drawing on literature on norm diffusion and the spread of ideas as well as the historiography of the organization, it highlighted the role of Venezuela as a norm entrepreneur that helped constitute the principles that underpin OPEC. Despite these origins, Venezuela became a follower. The reason for this change is rooted in disputes around sovereignty over natural resources, the struggle for control and autonomy over the industry and, overall, the notion of the rentier state in Venezuela's political economy.

In the 1980s, PDVSA's autonomy translated into bold programs to internationalize its operations and open the industry for broad investments in exploration and extraction. As a result, PDVSA hijacked the role of the Ministry in the formulation of oil policy as well as the authority to regulate joint ventures. This principal-agent problem translated into intense struggles between state and company where the latter ultimately prevailed, increasing oil output significantly above OPEC quotas.

After a period of increased production and rejection of OPEC mandates and quotas in the 1990s, Venezuela returned to its traditional position of price-defender and resource conservationist in the 2000s, under the leadership of Hugo Chávez. At this time, Chávez actively engaged with OPEC in attempts to revive its reputation. Further, he used this activism to galvanize support for his policies at home. These policies included attempts to bring PDVSA back under state control and to increase the state's oil revenues.

The policies of resource nationalism and the battle for control over PDVSA ultimately diminished the country's productive capacity.

In recent years, Venezuela's political regime has turned into a predatory regime with increased motivations to make the oil industry subservient to the ruling elite. In this context, the Venezuelan oil industry has collapsed, with a high debt burden, increased workers' absenteeism and long-term disinvestment. Despite its calls during 2014 and 2015 to defend prices through a production cut, the country has contributed the most in a supply contraction among OPEC members. The disastrous consequences of Venezuela's mismanagement have rendered the country's role within OPEC notably inconsequential. In a context of heightened hostilities with the US and other western powers, Venezuela's oil industry has been hindered further. More importantly, the country's leadership has put at risk the essence of the long-defended identity of a petro-state.

Notes

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Nigeria and the uncertain future of the oil market

Michael Olorunfemi

Introduction

The abundance of oil and gas placed Nigeria at a considerable advantage for rapid economic development. Joining the Organization of Petroleum Exporting Countries (OPEC) in 1971, Nigeria gained the benefits of a stable oil market, yielding enormous levels of foreign exchange. It was said that money was no longer Nigeria's problem, only how to spend it. Unfortunately, Nigeria became a consuming nation, with the absolute neglect of agriculture that had been the mainstay of the economy. In addition, the enormity of the oil revenue emboldened government to widen their involvement in almost all areas of economic activity. The political structure grew from three autonomous regions at independence in 1960 to 12 states on 27 May 1967, and finally 36 states on 1 October 1996. Recurrent expenditure became excessively high with little or nothing for capital expenditure, thereby depriving the country of necessary infrastructure for economic development. Nigeria's continued dependence on oil and gas as a mono-product commodity economy has made the country extremely vulnerable to visible volatility in the oil market. As OPEC's influence gradually declines in the oil market, Nigeria faces an uncertain future.

Resource endowment

Nigeria is blessed with a major hydrocarbon resource endowment both in absolute terms and relative to other oil-producing countries, particularly within the Organization of Petroleum Exporting Countries (OPEC). As at the end of year 2017, the country's proven crude oil reserves stood at 37 billion barrels representing about 2.5 percent of the world proven crude oil reserves, which stood at 1,483 billion barrels as at the end of year 2017 and 3 percent of the total crude oil reserves within the OPEC members, which stood at 1,208 billion barrels as at the end of year 2017.

With crude oil production per day that stood at 1.53 million barrels at the end of 2017, Nigeria represents 2 percent of the global crude oil production, which stood at 92,650,000 barrels per day, and 5 percent of OPEC crude oil production, which stood at 32,076,000 barrels per day at the end of 2017. Saudi Arabia had an average daily production output of almost ten million while Nigeria – which used to be the leading oil producer in Africa – came behind Angola due to challenges of insecurity in the oil-producing areas and uncertainty in the fiscal regime, particularly, as it relates to the pending Petroleum Industry Governance Bill (PIGB) awaiting approval by the president of the Federal Republic of Nigeria.

Nigeria oil and gas policy development/regulations

According to Olorunfemi et al. (2014), the early policy formulation in Nigeria oil and gas started with institutional safeguards to protect national interest. To achieve this, the government established a procedure through which they could predetermine and maintain a level of production that conserved the resources. Thereafter, there was the need to get more benefits and more revenue to the country, which led to the development of a fiscal system that allowed the investor to bring in capital. The Ministry of Mines and Power, which later became the Ministry of Petroleum Resources, together with the Nigerian National Oil Corporation (NNOC) were responsible for recommending policy decisions to government. The major policy developments in the upstream industry include concession policies, petroleum conservation policy, manpower development policies, indigenous participation policy and local content policy.

Concession policies

In pre-independence Nigeria, the power and authority for mining was vested in the governor general. The concession policy, marking the nation's status as a British colony, vested the whole country as a single acreage to a company called Shell D'Arcy. However, during the post-independence period the policy changed by demarcating the petroleum basins in the country into various acreages for allotment to various companies. The policy subsisted till the early seventies when no more acreage was allotted to private companies. The remaining un-awarded acreages were vested in the Nigerian National Oil Corporation (NNOC). However, in the early nineties when it was observed that the NNOC lacked the required capacity to explore the acreages vested in it, this was reversed. During this period, private companies with required capacity to explore the acreages were allowed to bid for and get acreages again.

When it dawned on the government that all the operators of the post-commercial discovered oil fields in 1956 were foreign companies and that they were largely profit-driven and also in a hurry to maximize their returns on investment before the expiration of the terms of their acreages, a set of petroleum conservative policies such as gas conservation and operating efficiency policies in order to regulate oil field production rates was introduced. In the mid-sixties, when oil activities began to increase and the government recognized the dearth of local experts to participate in and supervise these activities, it introduced a series of manpower development schemes in the Ministry of Mines and Power. This subsequently led to the launching of the Petroleum Technology Development Fund for high-level manpower training, establishment of the Petroleum Engineering Department in the University of Ibadan and the setting up of the Petroleum Training Institute in Warri for the development of middle-level manpower for the industry.

Still in the 1960s, when the oil and gas industry started to occupy the commanding height of the country's economy and the government felt that such a critical sector should not be left exclusively in the hands of foreign oil companies, an indigenous participation policy was introduced. The government started to give oil blocs to some prominent Nigerian businessmen. It should be noted that this crop of businessmen did not succeed due to lack of required investment capital and technical know-how. The later block awardees were engaged in more marginal fields than had been previously discovered by the international oil companies. In 2010, after fifty years of oil and gas exploration in the country, all the raw materials used in the exploration and production activities were being imported without considering the abundance locally of some these raw materials. In order to address the problem of the importation of raw materials that could be sourced locally, a local content policy was introduced. The policy recognizes that in addition to the use of locally produced raw materials and manpower, the oil and gas industry should be mandated to utilize the services of the country's financial institutions and its insurance, health care, advertising and catering sectors. The oil companies are therefore obliged to indicate the level of local content that every contract they engaged in will attain without compromising on quality and safety standard.

Nigeria oil and gas regulatory bodies

According to the publications of the Nigerian National Petroleum Corporation (2001), the Ministry of Petroleum Resources in Nigeria has primary oversight function over the oil and gas industry activities. Thus, it is the responsibility of the ministry to formulate, implement and coordinate all government policies for the upstream industry. Shortly before Nigeria joined the Organization of Petroleum Exporting Countries (OPEC), the Nigerian National Oil Corporation (NNOC) was established in 1971 to be an organ to wrestle control of the upstream industry from the hands of the multinationals. The corporation also provided a platform for the government to take up participating interest in the operations of the multinational oil companies (MNOCs).

Furthermore, in 1977, the Nigerian National Petroleum Corporation (NNPC) was formed through the merger of the then NNOC and the Ministry of Petroleum Resources. The formation of the NNPC was to put an end to the rivalry between the ministry and NNOC and also utilize the scarce manpower requirements in the oil and gas industry. The NNPC, in addition to its exploration and production activities mainly offshore, was given powers and operational interests in refining, petrochemicals and products transportation as well as marketing. For regulatory functions, the Department of Petroleum Resources (DPR) was created in 1985. The department is basically responsible for routine monitoring of the petroleum industry activities carried out under licenses and leases in the country as well as carrying out a supervisory role with a view to ensure compliance with the applicable laws and regulations. The department is also responsible for collecting royalties due to the government from both onshore and offshore production.

In 1988, the Nigerian Petroleum Development Company Limited (NPDC) was established under the Exploration and Production Directorate of the NNPC. The objectives of the company include producing and marketing hydrocarbons with a mission to profitably operate a medium-size petroleum exploration and production business locally and internationally taking full advantage of local expertise in upstream operations. Thereafter, for the purpose of acquiring engineering technology through direct involvement in all aspects of engineering in the oil and gas industry, the National Engineering and Technical Company (NETCO) was established under the Engineering and Technology Directorates of the NNPC in 1989. The company is responsible for providing basic engineering, procurement, construction supervision and project management using state-of-the-art technology. It is one of the most successful subsidiaries of NNPC today.

Finally, for effective monitoring and supervision of government investments in the Joint Venture, Production Sharing Contract and other contract agreements in the upstream sector of the industry, the National Petroleum Investment Management Services (NAPIMS) was established in the Exploration and Production Directorate of the Nigerian National Petroleum Corporation in 1993. NAPIMS, in addition to its monitoring and supervision of government investments, is also responsible for marketing the Federation's crude and engages in direct exploration services, especially in the frontier areas of the Chad basin.

Nigerian petroleum fiscal regime

Taxation and state participation

It is generally believed that exploration and production activities in the upstream industry are highly likely to generate economic rent. Economic rent for non-renewable energy is defined as the returns in excess of the supply price of investment required to sustain oil production, new oil field development and exploration. The need for the government to enhance the efficient recovery of the hydrocarbon resource, improve its revenues from oil and benefit maximally from the exploitation of the hydrocarbon resource led to the designing of a fiscal regime aimed at encouraging investors to invest in the upstream activities.

Taxation and state participation are both designed to deliver benefits from the petroleum sector to the government. Under the Oil Taxation Scheme, the fiscal tools employed by the Nigerian government to extract economic rent from hydrocarbon activities are corporate income tax and royalties. Corporate income tax is levied on oil companies. While being more sensitive to profitability than royalties, its implication on investments is not merely a function of the nominal rate but also on the depreciation provisions. The royalty rates are variable in nature as well as sensitive to oil field area whether onshore or offshore. The royalty rate ranges between 20 percent for onshore locations to 0 percent for deep-water project with depth above 1,000 meters.

The government of Nigeria participates in the exploitation of hydrocarbon resources in Nigeria through joint venture contracts (JVCs) and production sharing contracts (PSCs). Under JVCs, the Nigerian National Petroleum Corporation (NNPC) participates in upstream oil and gas projects through equity contribution. The NNPC's equity contribution is perceived as providing Nigeria with a number of non-financial benefits such as greater control in a strategic sector and development of local capacity, among others. It is also seen as providing an attractive equity return superior to that which might be earned in other sectors where public funds have been squandered. Nevertheless, equity participation generates only a relatively small financial benefit relative to what would be collected through taxes with effective tax administration. Furthermore, those incremental benefits could easily be eroded by delays in cash call obligations by the NNPC to fund projects in a timely manner. Moreover, the sums required to maintain NNPC financial participation at the current level of 60 percent with major operators like ExxonMobil and Chevron is substantial. Such financial obligation is well in excess of funding going to other critical infrastructure and social sectors and such could expose the government to significant budget deficit.

Another form of government participation in hydrocarbon resource exploitation in Nigeria is the production sharing contract (PSC), which is targeted at developing offshore petroleum resources. The PSC is mainly regulated by the Deep Offshore and Inland Basin Production Sharing Contract Acts 1999. The applicable fiscal elements comprise 50 percent petroleum profit tax. The royalty rates depend on water depth with rates ranging between 12 percent for water depth within the range of 200 meters, and 0 percent for water depth up to 1,000 meters and above. There is an investment allowance of 50 percent coupled with special charges such as an education tax of 2 percent of assessable profit and 3 percent charge for the Niger Delta Development Commission. Depreciation is charged at 25 percent on a straight-line basis. The combined effect of the fiscal regime for deep-water operations is a tax rate of 55 percent. Cost oil limit is 100 percent after royalty and the profit oil split for government is set at minimum of 20 percent for a production volume of up to 350 m/bl, 35 percent for production volume of 750 m/bl, 45 percent for production volume of 1,000 m/bl, 50 percent for production volume of 1500mmbbls and gradually rising to 60 percent for production volume of above 2 m/bl.

International competitiveness of Nigerian petroleum fiscal regime

In recent years, many international oil companies have divested their interests in Nigeria oil assets. According to the Nigerian Economic Summit Group (2013, p. 5), between 2008 and 2013, oil majors such as Royal Dutch Shell, Petrobras, Total, Conoco Phillips and ENI concluded plans to divest US\$5 billion's worth of onshore oilfields and other assets. Such divestment has been attributed to increasing local insecurity, oil theft, unfavorable profit-sharing agreements, high taxes and royalties as well as the fact that there are better opportunities in new discoveries outside Nigeria. Rolake Akinkugbe¹ considered another reason for the recent divestment of oil asset interest by the international oil companies in Nigeria to be global capital re-allocation in the upstream industry and the rebalancing of international oil companies' Nigerian portfolio towards the offshore.

In 2009, according to Akinkugbe, the British Gas Group kick-started the divestment program among the international oil companies operating in Nigeria when it announced a pull-back in financing for the

Olokola LNG export development. The British Gas Group was in partnership with Chevron Nigeria Limited, the Shell Petroleum and Development Company and the Nigerian National Petroleum Corporation on the project but later sold its right in the three oil prospecting licenses 284, 286 and 332.

In 2010, the Shell Petroleum Development Company of Nigeria also launched a divestment program that eventually resulted in the sale of eight oil mining licenses (OMLs) worth US\$2.7 billion to indigenous Nigerian companies. Chevron Nigeria Limited followed suit in 2012 by embarking on a divestment program with an offer of five shallow water blocks estimated to hold as much as 250 million barrels of oil reserves. The value of the blocks, which include OMLs 52, 53, 55, 83 and 85, was estimated to be in the region of \$1.5 billion. In the same year 2012, Conoco Phillips, a United States oil firm operating in Nigeria also sold its stake in the Brass LNG project for \$1.79 billion.

The offshore assets were not spared by the divestment program. In November 2012, Total Nigeria Exploration and Production Company sold its 20 percent in OML 138 block in the offshore Usan field for approximately US\$2.5 billion. In 2013, Petrobras, Brazil's National Oil Company operating in Nigeria stated that it would sell off its Nigerian interest which is mostly offshore for \$5 billion. In the same year 2013, Shell Petroleum further sold its interest in additional four assets in Nigeria which include two of its offshore oil blocks OML 71 and OML 72 as well as two of its onshore oil blocks OMLs 13 and 16.

According to Ecobank Research (2013), the ongoing divestment program majorly from the onshore operations by the international oil companies operating in Nigeria could possibly see Nigeria losing the whopping sum of US\$11.5 billion. The beneficiaries of the loss in investment from the Nigeria upstream would be any other oil provinces with a more economically efficient and competitive fiscal system. More worrisome is the fact that the local operators of the divested assets lack the required expertise and funding capacity to sustain the momentum of operations of the international oil companies. Consequently, Nigeria oil production volume has once again been on a downward trend in recent years, with attendant loss of revenue, and the country is currently facing a huge fiscal deficit challenge.

In view of the above, concerns have been heightened as to whether the current Nigeria petroleum fiscal regime is achieving its main aim of attracting investment for efficient recovery of hydrocarbon resource in the upstream sector. Given the mission of the international oil companies, which is to find, develop, refine and market these resources in a fashion that achieves the highest economic return to the owners, it follows that if the Nigerian business environment is becoming too difficult for the operators to achieve their mission, they could shift base.

Nevertheless, Akinkugbe is of the opinion that given the international oil companies' commercial shift towards offshore operations, the Nigerian deep-water could be considered for possible investment opportunities. However, for Nigerian offshore to be considered a viable investment opportunity as against other deep-water projects in oil provinces outside Nigeria, the fiscal terms for offshore exploration could be critical in this regard. The Nigeria fiscal regime for deep-water oil projects should be economically efficient and competitive enough to guarantee investors at least the opportunity cost of investing \$1 in Nigeria offshore rather than investing the same amount in another oil province – particularly the non-OPEC members such as Norway and United Kingdom in the North Sea or United States of America in the Gulf of Mexico deep-water operations.

According to Omoniyi (2017), in his empirical analysis of the economic impact of the Nigerian petroleum fiscal regime on deep-water oil projects in comparison with the United States, the United Kingdom and Norway concluded that the Nigerian petroleum fiscal regime provides investors with fair post-tax margin per dollar investment from field sizes with minimum recoverable reserves of 40 million barrels. However, it was discovered that the fiscal regime has optimality issue. For a fiscal regime to be considered optimal, not only should it procure some early revenues to the government but should also be targeted on economic rent. The royalty element of the fiscal regime though procures early revenue to the government but fails to target the project's economic rents because it is not profit related.

In addition to the above, the margin provided by the Nigerian petroleum fiscal regime, though, may be less competitive to the investment opportunity cost per dollar investment particularly for large and medium oil fields in the United States (GOM), such margins are still fair enough to attract investment in Nigeria. For the small-volume fields, the investment returns from Nigeria are the least competitive. Thus, domestic upstream industry in Nigeria may find it challenging to compete favorably for investment capital internationally with such oil provinces with more attractive and competitive investment returns for small oil field development.

Economic relevance of the Nigerian petroleum industry

Undoubtedly, crude oil production is central to the Nigeria economy. Nigeria's total revenue from crude oil rose by 29 percent to NGN7.3 trillion in 2017 from NGN5.68 trillion in 2016, reflecting the impact of increase in production volume and increase in crude oil price per barrel. In 2017, the revenue from oil represented 69 percent of the total federation revenue, which gained an increase of 22 percent to hit NGN10.6 trillion from NGN8.26 trillion achieved in 2016. However, according to the Central Bank of Nigeria Economic Report (2017), the deficit spending by the federal government equally rose by 22 percent to NGN2.7 trillion during the year, thus showing the possibility of a lack of financial prudence on the part of the government. In 2017, the average spot price of Nigeria reference crude oil, the Bonny Light (37°API), rose from \$52.92 per barrel in the third quarter of 2017 to \$62.48 per barrel in the fourth quarter of 2017. This represents an increase of 18.1 percent, which was attributed to the production-cut agreement, demand growth from China and increased refining activity in the United States.

Despite the efforts of the government to diversify the economy away from oil, the receipts from oil and gas still account for a huge chunk of the country's total export earnings, standing at 78 percent of Nigeria's export earnings. An analysis of the foreign trade statistics obtained from the National Bureau of Statistics (NBS) showed that of the total export earnings of NGN3.1 trillion in the second quarter of 2018, oil and gas receipts accounted for NGN2.43 trillion while non-oil sector accounted for the balance of NGN670 billion

Figure 7.1 shows the revenue from oil in Nigeria between 2008 and 2017, a period of ten years which is well over NGN50 trillion.

The projected revenue from crude oil in 2017 was estimated at NGN1.985 trillion representing about 40 percent of the total projected expected revenue of NGN4.94 trillion. However, the actual receipts from crude oil in 2017 was put at NGN7.3 trillion, more than triple the budgeted revenue. The budgeted revenues from crude oil are capable of funding critical social program in Nigeria at well above the current levels. In spite of the huge yearly revenue from crude oil, the government of Nigeria has woefully failed to transform the national economy to an expected level commensurate with the earnings from oil and gas due to gross mismanagement and unprecedented level of corruption. For instance, Norway has been able to build up assets worth \$960 billion from oil proceeds as a Sovereign Wealth Fund to take care of their future generations. The Sovereign Wealth Fund is so large that it is twice the size of the gross domestic product (GDP) of the country; it is large enough to increase the wealth of each Norwegian; young or old by \$185,000. The country only spends the interest from the Fund while the principal Fund is kept for future generations. But, in Nigeria, debt is being accumulated for the present and future generations.

In spite of the enormous wealth the Nigerian petroleum sector has generated over the years, all the three tiers of government in the country have not been able to improve on the standard of living of the Nigeria citizens and the economic performance is the lowest relative to other members of the oil producing export countries as shown in Table 7.1.

The gross domestic product per capita in Nigeria of \$1,994 is the lowest among the OPEC members. While countries like Kuwait, Qatar and Saudi Arabia have 100 percent access to electricity, only about 59 percent of the Nigerian population has access to electricity in spite of the country's huge energy resources.

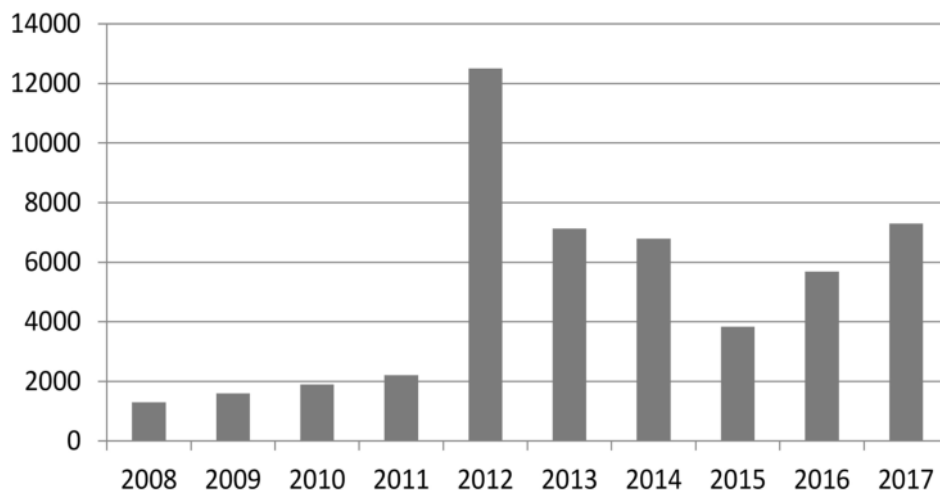


Figure 7.1 Revenue from crude oil between 2008 and 2017 in Nigeria (billion Naira)
Source: Central Bank of Nigeria (CBN).

The infant mortality rate in Nigeria is 65 in every 1,000 births, while the infant mortality rates for even war-ravaged countries like Libya and Iraq is 11 and 25 respectively. The unemployment rate of 33 percent in Nigeria is the highest among oil-producing exporting countries. The statistics indicates that the government of Nigeria has not been able to translate its enormous wealth from crude oil and gas into programs of economic and social development that could improve the standard of living of her citizenry above average.

The future of the Nigerian petroleum industry

It is pertinent to state here that according to Sheikh Ahmed Zaki Yamani, the former oil minister of Saudi Arabia, the Stone Age did not end because of lack of stones; similarly, fossil fuels would still be available should the world move to a new world of energy source. Thus, it is high time Nigeria began to diversify away from oil and gas as the future of the hydrocarbon resource is likely to be shaped globally by climate change and environmental concerns that require a transition from fossil fuel to cleaner, renewable and more efficient energy sources.

Table 7.1 Economic performance indicators relative to OPEC members, 2017

OPEC	GDP per capita (US\$)	Access to electricity	Infant mortality/1000	Unemployment rate
Nigeria	1,994	59%	65	33%
Algeria	4,292	99%	21	29%
Libya	4,859	98%	11	17%
Iraq	5,088	100%	25	14%
Gabon	7,972	91%	35	19%
Saudi Arabia	21,120	100%	6	6%
Kuwait	27,319	100%	7	2%
Qatar	60,804	100%	7	1%

Like many other oil-rich developing nations, Nigeria depends hugely on fossil fuels such as crude oil and natural gas to provide energy for economic activities and household energy needs. However, fossil fuels are not being newly formed at any significant rate, thus, current stocks are ultimately finite. Coupled with the finite nature of fossil fuels is the issue of climate change, which has become a global concern and a serious threat to human existence. Undoubtedly, fossil fuels cannot sustain future energy needs because of depletion of the reserves and concerns for global environmental impacts. Consequently, renewable energies are currently receiving global attention and have begun to form part of the essential components of every nation's energy strategy for economic development sustainability. According to Twidell and Weir (2015), the remedy for air pollution and climate change is to replace fossil fuels by renewable energy and improve the efficiency of energy use.

Unfortunately, while the Nigeria federating units and the central government are fighting over how fairly to share the revenues from the hydrocarbon resource, the rest of the world is thinking how to move away from hydrocarbon resources as a way of preserving human existence, threatened by environmental hazards resulting from the consequences of the production and utilization of fossil fuels as an energy source. The economic relevance of fossil fuel is enhanced by the automobile industry that produces vehicles that run on fossil fuels such as petrol and diesel. Currently, efforts are being made toward the production of electric vehicles that are capable of performing similarly to petroleum-powered vehicles. Countries like Norway, China, the United Kingdom, Germany and Sweden have already set a target date of 2040 to replace gasoline-powered vehicles with electric vehicles. When the electric vehicle policy in those countries becomes fully operational, the implication for Nigeria hydrocarbon resource is that fewer investors would be willing to invest in its exploration and production because there would be fewer buyers for the product.

Another threat to the future of Nigerian oil is the development of shale oil in the United States. With America's resolution to fully develop and produce her shale oil, Nigeria would not only lose one of her biggest crude oil buyers but also lose substantial revenue from crude oil sales due to the fact that the availability of shale oil would crash the crude oil price and could even result in Nigerian crude oil being sold at high discounts in order to attract new buyers.

According to Akhigbe,² Nigeria could still have time to restructure her economy to be less dependent on oil by shifting the emphasis to mining, agriculture and manufacturing. For this to be possible, however, the government would have to give deserved attention to the problematic power sector. The power sector must be fixed to aid rapid economic development through the manufacturing and agricultural value chains. The security challenge must also be addressed, while the business environment made conducive to attract foreign investment.

In conclusion, with the finite nature of hydrocarbon resource coupled with the global climate change concerns, environmental pollution, threat to crude oil by America shale oil and the world quest for a cleaner efficient energy source like renewable energy, the future of Nigeria oil is uncertain. Like the Stone Age, Nigeria will be compelled by global demands to move away from her crude oil while the crude oil may still be flowing under the ground.

Notes

- 1 Akinkugbe, R. (2014). IOC divestment in Nigeria: Opportunities, challenges and outlook. www.nigeriadevelopmentandfinanceforum.org/PolicyDialogue.aspx?Edition=159.
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Part II

OPEC and consuming countries



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Emergency stockpiles of oil among Western consumer countries prior to the International Energy Agency system

Hans Otto Frøland and Mats Ingulstad

Introduction

Dependency on imports constitutes a fact of life in the modern global economy. It is inescapable; no advanced industrialized state has ready access to all the resources it needs domestically. Even so, import dependence seldom commands political attention in times of stable supply and absence of price volatility. But whenever the availability of key resources appears threatened, it is put front and center on the political agenda. A prospective failure in the raw materials supply conjures up the spectacle of debilitating shortages with disastrous consequences for economic growth and military capabilities. The political severity of oil supply crises become particularly acute since oil is often considered to be even more important than other critical, high-demand resources, constituting the very lifeblood of modern society (Huber, 2013; LeMenager, 2014; Beaubouef, 2006). Loss of oil imports invokes horror as an existential threat to a modern consumerist culture that praises individual mobility and malleability in industrial products. The stakes are high for all affected parties if external oil supplies are severed and the government may react by putting conservation measures in place, such as rationing and ‘car-free Sundays’. Meanwhile the oil companies are exposed to critical scrutiny and harsh censure for padding their profits in times of crisis (Norsk Esso, 1974). So how does an industrialized state seek to protect itself against that eventuality? Already prior to the First World War oil supply security was recognized as a problem for reasons that would ring familiar today. A critical shortfall of physical stocks could be brought about by deliberate action or market failure, substitution was costly, and any shortages would have knock-on effects on the wider industrial economy (Royal Commission, 1905, pp. 194–197). But while oil consumption grew relentlessly in the following half century, oil supply security only started receiving serious academic scrutiny in the 1960s (Lubell, 1960). The oil crises of the 1970s generated both a great demand for and a robust supply of, academic research on energy security (Cherp and Jewell, 2014). The oil shocks also gave birth to the current system tasked with handling major supply disruptions of oil, coordinated through the International Energy Agency (IEA), established in 1974. Its core mechanism was a network of oil stockpiles for emergency sharing among IEA members, among which the US Strategic Petroleum Reserve was and remains the most significant (Yergin, 2006; Toner, 1987; International Energy Agency, 2014).

Our understanding of the history of oil supply security, as much as the current international oil security system itself, is in many ways shaped by the oil shocks of the 1970s (LaCasse and Plourde, 1995). The well-established view is that Western countries, having relied for decades on the major oil companies for cheap oil, were unprepared, unequipped or even unable to comprehend their potential vulnerability to supply disruptions (Yergin, 1991; Priest, 2016, p. 121). The belated and painful realization of their own failures then led these governments to embark on a new and untried course of multilateral cooperation to deal with future oil crises (Scott, 2004). The fact that the US petroleum reserve was only established after the first oil shock has also reinforced the notion that there had been failure to provide for stockpiling of oil prior to the oil shocks (Weyant, 1984). This narrative, embedded in the term oil shock itself, serves as a cautionary tale of how failure to prepare is to prepare for failure. But while it might teach policymakers a valuable lesson about the need to take supply security seriously, it also obscures the history of previous attempts to engage critically with Western import dependency in the years before the first oil shock.

This chapter will complicate the narrative about a lack of preparation for loss of oil imports. The long string of postwar crises in the Middle East had in fact forced the Western industrialized countries to face the fact that their supply of cheap oil also entailed an increased risk of supply difficulties. Several scholars have pointed to various strategies that were adopted to deal with this problem by different states, such as contingency planning for oil tanker logistics or diplomacy directed at the producing states in the Middle East (Bini, 2014; Kuiken, 2014). This chapter will show that many states also had national stockpiling schemes in place prior to the oil shock. Oil stockpiles are stocks held above the buffers maintained in the course of normal commercial operations. They are set aside to mitigate the grave consequences for the national economy inherent in case of serious disruptions in the oil supply. Stockpiling can also provide additional security gains through collective action, but coordination problems have been seen to act as a significant barrier. This is hardly surprising as concerns about energy autonomy as a matter of national survival and sovereignty can act to restrain international cooperation in energy policy in general (Strunz et al., 2014; Hubbard and Weiner, 1986). However, Henning Türk (2014) has noted that there were attempts at multilateral cooperation that predate the founding of the IEA, particularly through the OECD itself. NATO and the emerging European communities have as well sought to bolster stockpiling to reduce the vulnerability to supply disruptions, in addition to a series of bilateral arrangements for oil storage on foreign soil. The last part of this chapter identifies several such forms of cross-border cooperation on stockpiling schemes prior to the oil shock.

Stockpiling oil: the national approaches

The US has been among the foremost exponents of stockpiling for more than a century. President Theodore Roosevelt warned in 1906 that the available coal and oil resources might run out within a generation, which would threaten the ‘civilized progress’ of the US as well as its claim to international leadership. Between 1909 and 1924 Roosevelt’s successors set aside tracts of land with known oil reservoirs to cover the requirements of the US Navy. The growing oil consumption also raised concerns about supply for domestic civilian industries (Nash, 1968, pp. 17–18; Tyrell, 2015, pp. 79–97). During World War II the US government, having recently introduced legislation for stockpiling of other raw materials, considered various means to establish a stockpile of crude oil (Fanning, 1950, p. 373). Such suggestions were forcefully opposed by the Petroleum Industry War Council, an industry advisory group set up by the Department of the Interior. The council argued that government involvement in stockpiling ‘would not in fact promote true national security’ but would be harmful to ‘this most individualistic of all economic activities’ (Petroleum Administration for War, 1946, p. 395). In the face of industry lobbying, no stockpiling program stood a chance of passing Congress, a lesson learned successively by the Roosevelt, Truman and Eisenhower administrations (Krasner, 1978, p. 189).

Despite its vaunted self-sufficiency, close observation of US trade patterns revealed that the its postwar supply position was becoming more vulnerable to developments in foreign markets.¹ By the time the Nixon White House started working on stockpiling, even the National Petroleum Council acknowledged the dependence on foreign oil and its grave security implications. Although this influential industry group preferred to reduce imports through deregulation, domestic exploration and exploitation, it conceded that the problem only could be handled by stockpiling (NPC, 1973; NPC, 1974). Nixon's Project Independence did not initially provide for stockpiling, but the new Federal Energy Administration (FEA), drawing heavily on the NPC's recommendations, strongly suggested that it would be better to stockpile oil than face the socioeconomic costs of cutting oil consumption (NPC, 1975). The *Energy and Conservation Act of 1975* gave the government the power to require each importer and refiner to acquire and store readily up to 3 percent of the amount imported or refined as available inventories, designated as an Industrial Petroleum Reserve. The industry mustered strong opposition to the idea of saddling importers with minimum inventory requirements and subjecting domestic producers to prorating. The FEA eventually refrained from exercising this discretionary authority from fear of its legal, administrative and economic consequences.² On the other hand, the traditionally market-oriented industry representatives agreed to place the responsibility with the federal authorities, despite their abiding distrust of government intervention. The result left US with a completely government-run stockpiling program, unique among Western industrialized countries (Pratt et al., 2002). Once enacted, the Strategic Petroleum Reserve was planned to cover crude oil imports for 90 days, with 500 million barrels to be placed in salt caverns in Texas and Louisiana. The targets were shortly after raised to 750 million barrels and later to one billion barrels (Beaubouef, 2007).

Several European countries also have long histories of government involvement to reduce supply risks in the oil sector, including the mandatory creation of stockpiles. But in marked contrast to the US, the burden of holding emergency stocks has fallen to a much greater extent on private industry. During the First World War French policymakers had become acutely aware of the strategic value of oil, the 'blood of battles' that saturated its fields. In 1925 the government introduced requirements for import licenses subject to state control. License holders were obligated under law to set aside stocks of oil. In the following decades French oil policy involved careful balancing between domestic and foreign supplies, with supply security a crucial consideration (Demagny, 2010; Philippon, 2010). The 1951 Iran crisis caused the government to issue a special decree that required all oil importers to maintain a stock of crude oil equivalent to 1/9 of all imports in the preceding quarter. Following the Suez crisis this was tightened further, as a new decree required all holders of special import authorizations for petroleum products to maintain stocks equivalent to one quarter of preceding 12 months of inland sales. Domestically produced oil was exempted. The 1973 oil crisis pushed France even further in the direction of establishing a large stockpile of 10 million barrels of to be in place by 1975. France did not join the IEA until many years after the oil crisis, but generally complied with its recommendations and was known to favor a large stockpile.

West Germany, traditionally a coal-based economy, also had to cope with its growing dependence on oil. In 1965, the federal government introduced the Minimum Storage of Mineral Oil Products Law, which designated firms engaged in the petroleum business as *vorratspflichtige* (obliged to keep stocks) and required them to hold stocks of oil above a certain threshold. This entailed heavy costs for the firms, and the law was almost immediately challenged on constitutional grounds. The German Supreme court ruled that energy security was an 'interest of most urgent public concern', and consequently the oil importers would have to accept the additional burdens imposed by the law (Kühne, 2004). In the early 1970s the German government also developed plans to create an additional strategic stock of 25–30 days oil consumption (10 million tons) to be placed in North German salt caverns.³ After the oil crisis, a law on the storage of mineral oil products was passed in 1978. This law established a public corporation, the Erdölbevorratungsverband, in Hamburg.⁴ German companies producing or importing oil products had to

contribute funds and support the work of the corporation, which was charged with storing oil products equivalent to a 90-day period of imports and production based on the last three years. Releases from the stocks were to be determined by the government in consultation with oil industry.

Interwar Italy was a clear example of a state almost completely dependent on oil imports, and it established AGIP in the mid-1920s in a conscious effort to overcome this problem (Bini, 2014). During the Ethiopian crisis it was threatened with an embargo on oil with potentially crippling effects (Ristuccia, 1997). To guard against such eventualities the government had already introduced minimum storage obligations on the domestic oil industry through a decree in late 1933, followed by a law in early 1934. The *Legge Petrolifera* no. 367 of February 1934 required stockpiles to be maintained in accordance with government guidelines when licenses were issued for the construction of refinery or storage depots. Postwar Italy's more measured aspirations for energy autonomy were undermined by the rapidly growing role of oil in Italian energy consumption. The share of crude oil to total energy consumption increased from 22 percent in 1950 to 75.3 percent in 1973, and in the meantime the build-up of stocks did not keep up with the increase in consumption (Toninelli, 2010). To address these shortages the government issued a number of decrees between 1961 and 1976 that established storage targets equivalent to 60 days of consumption in the previous year, later raised to 90 days. The costs had to be borne by the companies without subsidies. There was also a particular requirement for owners of storage facilities to keep a minimum fill of 20 percent in their tanks. Failure to keep the stocks could result in the import licenses being revoked.⁵

Sweden was in a strategically disadvantaged position as a heavily industrialized country dependent on oil imports. After several years of investigations and discussions, a stockpiling requirement for importers was introduced in 1938. Importers and oil refiners designated as *lagringskskuldiga* (obliged to keep stocks) had to bear the costs, but oil consumers could also be subjected to the same requirement (SOU, 1957). As a neutral country susceptible to pressure from the Soviet Union, the Swedes also tried to reduce their vulnerability. While the mandatory stockpiles had to be kept on Swedish soil, the government looked to Norway as a potential 'breathing hole in the West' (*andningshål västerut*) in the event of war. Discussions began in 1954, during one of the periodic bouts of enthusiasm for Nordic regional cooperation. A secret deal provided for cisterns to be blasted into the mountains around the Trondheim fjord. They would hold oil that could be supplied by a pipeline to Sweden to cover military supplies and potential shortfalls in difficult winters. The facilities were completed in 1962 but quickly proved cumbersome and costly. The strategic value was greatly reduced when the nearby airport was slated for expansion as a NATO installation, which made the prospective pipeline a likely casualty of collateral damage (SOU, 1994). Rather than relying on storage on foreign soil, the Swedish government in 1957 initiated a series of programs to expand stockpiling. As in the US there were arguments that since stockpiling was a matter of national security, the burden should not be placed on an industry already hampered by capital shortages (Teknisk Tidsskrift, 1957). In 1962 the Swedish parliament, the Riksdag, introduced legislation that provided government subsidies for the creation of stocks over a seven-year period. The arrangement was based on interest-free loans that depreciated as the storage obligations were fulfilled, while ownership of stocks and storage facilities remained in private hands.⁶ After 1969 the costs of further building up the stocks were supposed to fall on the companies alone. But in that year the government decided to continue to provide some economic support for continued expansion of stockpiling for the 1970–1976 period (Carlsnaes, 1988; SOU 1970).

Denmark is almost completely devoid of fossil energy resources. After many years of unsuccessful prospecting of gas under Danish soil, a consortium led by A.P. Møller turned its attention to the sea after 1960, inspired by the large discoveries off the coast of the Netherlands (Hahn-Pedersen, 1999, p. 49). Even so, Mogen Rüdiger has concluded that Denmark lacked a national energy policy and for a long time was content to rely on international markets for its oil (Rüdiger, 2014). Nevertheless, oil security cropped up on the agenda after the passage of an emergency preparedness act shortly before Christmas Eve in 1959.

The act empowered the government to set minimum stock requirements of necessary items for both private companies and public institutions.⁷ A proposal for a gasoline tax to pay for emergency stockpiles of oil stranded on resistance from the Ministry of Finance. Instead, the Ministry of Commerce and the Danish subsidiaries of international oil companies created the Foreningen Danske Olieberedskapslagre (Association for Danish Emergency Stocks) (FDO) in 1964. The Ministry made annual declarations on the legally required stock sizes of the different products. The firms built the protected storage facilities and maintained the compulsory stocks, the Ministry supervised compliance through its representation on the board. It worked reasonably well and enabled Denmark to comply with the recommendations on minimum stock levels issued by both NATO and OECD.⁸ After the Danish entry into EEC in 1973, a new act demanded that Danish oil companies should maintain at least 25 percent of their turnover from last year as a reserve. This stockpiling requirement entailed that Denmark could meet the 65-day threshold set by the OECD recommendations after it joined IEA in 1974 (Dahlberg and Ankjærgaard, 2014).

For the UK the transition from coal to oil not only entailed the technical and strategic question of fuel for Navy ships in the first decade of the 20th century but also touched upon broader social questions related to the need to maintain employment in the domestic coal industries. The weakening of British power, on full display during the 1956 Suez crisis, coupled with its imperial presence in conflict-ridden areas, ensured that the UK was likely to suffer threats to its supply lines. Rather than legislating a stockpiling requirement or curb consumption, the British government established a policy in 1958 that stocks were to cover four months' supply. Private companies should hold stocks equivalent to 16 weeks and the government would cover the remaining 10 days. As Richard Marsh, the minister of power, explained in 1967, restrictions on the use of oil would hinder technological advances and increase costs. Instead, 'it is our policy to mitigate the security disadvantages of oil imports by diversifying sources of supply, by stockpiling and other measures, including the encouragement of oil and natural gas exploration in the North Sea'.⁹ The stockpiling objective was not achieved. British stocks fell from a high point of 14.3 weeks in 1961 to 10.4 weeks in March 1966. The government itself held 1.1 million tons against supply interruption, but relative to the increase in consumption it declined from 10 to 6 days. The government did consider introducing formal legislation for stockpiling requirements but held back due to its perennial fears about the British balance of payments.¹⁰ That left the government at the mercy of the oil companies, as it discovered during an unsuccessful attempt to persuade them to increase the emergency stocks before the oil crisis. As there was no legal basis for the enforcement of stock levels, nor any financial assistance scheme, the oil companies could not be induced to build up emergency stockpiles against their will.¹¹ Nevertheless, on the eve of the first oil shock, the UK did have substantial stocks on hand, and as Table 8.1 shows, it was well aware that so did many other countries (Chick, 2007, pp. 20–26).

Stockpiling oil: multilateral approaches

Despite the various attempts by individual states to improve their own supply security through stockpiling, the rapidly growing oil dependence of the postwar era made it difficult for any single state to handle the problem on their own. The US Paley Commission in 1952 forecast that oil consumption would double in the US, triple in Europe, and quadruple elsewhere over the next 25 years. The Commission simultaneously labeled the European dependence on Middle Eastern oil the gravest threat to 'the wartime security of the free world' (Paley Commission, 1952). As the US emerged as the dominant player within the Western bloc, the US Petroleum Administrator for Defense warned that the US could not merely ensure its own supply security through rationing, production increases and stockpiling. Crucially, it also had secure adequate supplies for its allies.¹³ Accordingly, the US pushed for the establishment of an oil-planning group within NATO. The initial concern was to supply armed forces in Europe with oil, but civilian requirements quickly became an issue. As the military planners recognized, it would be

Table 8.1 Western European countries' oil stocks and stockpiling requirements (number of days of consumption, as per 1970)¹²

	<i>Stocks, 1969</i>	<i>Requirement</i>	<i>Legislation</i>
EEC	82	65	Directive 68/414
Belgium	82	65	Decree of 14.11.59
Denmark	82	46 (gasoline importers) 13 for oil importers, 90 for power stations and 120 for state railways	Laws of 23.12.1959, and 10.3.1966
France	99	90	Laws of 1925 and decrees 19.9.1951 and 10.3.1958
Italy	82	60	Law of 8.2.1934 Legge Petrolifera n. 367.
Netherlands	57	–	Gentleman's agreement replaced by law.
Norway	77	–	N/A
Sweden	74	Considered to be 75 days	Law of 1963. State paid 55% of cost until 1969, then nothing.
Switzerland	103	n.a. (4–6 months)	Law of 30.9.1955, Ordinance 15.7.1958
W. Germany	68	45 for importers/65 for refiners	Law of 9.9.1965

complicated and costly to cover the European requirements of oil. Storage capacity was simply inadequate. The NATO Petroleum Committee therefore concluded that it was unfeasible to build up stocks in Europe for the time being.¹⁴ NATO instead made the case for more clarity on the need for stocks, expressed either in terms of days of consumption or as the ratio between storage capacity and requirements.¹⁵ Only in 1957, in the wake of the Suez crisis, did NATO establish a common target for oil: 'Nations should as an initial objective establish secure oil stocks sufficient to meet all essential requirements for the first 30 days of a conflict.'¹⁶ A survey revealed that only four countries had stocks to 'cover essential requirements at bare survival rates for more than 30 days'. While eight countries did not meet the 30-day threshold, practically every member was working to improve their stock positions.¹⁷

The transatlantic alliance's economic counterpart, the OEEC, also started working on the European oil supply. While the OEEC oil committee in early 1956 discussed technical issues relating to tariffs on oil products and their effects on intra-European trade, the Suez crisis dramatically shifted the attention to supply shortages and stockpiling of oil.¹⁸ The organization developed an emergency protocol that required the OEEC secretary-general and the oil committee chairman to declare a state of emergency for the OEEC area (including Spain, only an associated state at the time). Emergency procedures would then be put in operation in conformity with plans made by the oil committee, and the US government was to be informed of their actions. The oil committee was also instructed to prepare measures to coordinate the oil industry and develop methods for ensuring fair and equitable distribution of supplies between the member countries. These measures had to take into account the availability of oil and the supply situation of each member country, which would naturally be an immense political challenge.¹⁹ The OEEC envisioned an apportionment scheme that divided the supply between European members, largely in proportion to their share of the supply in normal times. In 1964 the OEEC, now reconstituted as the OECD, issued a recommendation for minimum levels of stocks equivalent to 65 days of consumption of crude oil and oil products (Beer, 2016; OEEC, 1958, p. 46).

European integration provided new opportunities for collective action. The European dependence on oil imports had been fostered by the Marshall planners, who believed that although Europe would remain a coal economy, ‘without petroleum the Marshall Plan could not function’ (Economic Cooperation Administration, 1949, pp. 1–2, p. 16). From the very outset of the integration process, energy supply security was enshrined as a guiding principle in community law (Maltby, 2013). The Treaty establishing the European Coal and Steel Community charged the High Authority with seeing ‘that the common market is regularly supplied’.²⁰ Likewise, the EURATOM treaty established supply security as a key objective and provided as well for the possibility of establishing of joint emergency stockpiles subject to qualified majority votes.²¹ However, in those early days economic efficiency trumped security. Oil was not initially part of these supranational deliberations on supply security. Rather, the High Authority (HA) favored energy imports in the form of petroleum because it was deemed more economical. The Suez crisis made the HA reconsider its preference for oil imports. It also stimulated fanciful ideas of an integrated community energy policy under the auspices of EURATOM or converting the ECSC into a ministry of fuel and power for a federated Europe. The Suez crisis also underlined how divided the European countries were regarding their willingness to utilize their existing stocks, as well as the need for a common understanding of how stockpiled oil could be used, and to what extent (US Senate, 1957, p. 2380).

Between 1950 and 1965 petroleum displaced coal as the primary source of energy for the countries that would form the European Community. A special committee working on behalf of all three communities peered into the future in 1962 and predicted: ‘growing energy requirements, growing proportional consumption of oil, growing dependence on imports, hard times for much of the Community’s coal industry’ (European Commission, 1964). The ECSC did not become the nexus of an integrated energy policy; instead it was the EEC that emerged as an arena for formulating common goals relating to oil security. To address the problem of import dependency, the EEC Council of Ministers in 1964 adopted a protocol that charged the member states to strive for a common policy on energy. The common objectives were a cheap, stable and secure supply of energy, development of substitute products, while working for fair competition and freedom of choice in line with the general economic policies of the community. The protocol also advocated a common policy on oil stocks.²² The European Commission subsequently drafted its first directive on stockpiling in November 1964. The draft would require the member states to hold stocks equivalent to at least 65 days average domestic consumption. However, the share met from domestic oil production received a 15 percent rebate on storage requirements. Quarterly reporting of stocks would be required, and the stocks must be built up within six months. This caused disagreement between member states. Italy held that its own stocks (56 days) were sufficient. Italy also wanted to include oil in the pipeline, while France, the Netherlands and Belgium wanted to exclude oil in barges, tank wagons and coasters.²³ The Commission’s draft was not adopted by the Council.

The objectives outlined in the Council protocol of 1964 were again seized upon by the Commission in 1968. Noting that member states were becoming dependent on imports for a larger share of their energy requirements, this dangerous trend was to be mitigated through the adoption a coherent community energy policy. The 1968 Communication reiterated its support for the aims of the 1964 protocol, and explicitly suggested the ‘[a]pplication of a stockpiling policy for crude oil, oil products and nuclear fuels as part of the supply policy’.²⁴ In line with the 1968 Communication and the 1964 draft directive, the Council issued its decision 68/414/EEC two days later, which imposed an obligation on member states of the EEC to maintain minimum stocks of crude oil and/or petroleum products. These had to be enshrined in domestic laws or regulations, and stocks of petroleum products had to be kept at a level corresponding to least 65 days’ average daily internal consumption in the preceding calendar year, with a deduction for up to 15 percent for consumption of domestically produced petroleum. Beyond the discussion of emergency stockpiling levels, the Council and the member states generally spurned the Commission’s

recommendations to address supply risks through a joint framework, such as a Common Raw Materials Policy covering both oil production in the 'EC seas' and imports of externally sourced oil²⁵ (Krämer, 1977; Maltby, 2013). There were limits to multilateralism.

Even without the emergence of a full-fledged community-level energy security policy, there was an increasing integration process occurring for stockpiling. The 1964 protocol gave impetus to legislation for cross-border stockpiling arrangements for oil. The German 1965 act on minimum stocks of oil specified (Art.4) that the legally required minimum stocks had to be held under the jurisdiction of German law, but there was an exception. The government could declare that the duty to hold stocks was fulfilled by stocks held within the boundaries of the European community if they were certain to be available in times of crisis.²⁶ The law was complemented by specific ordinances that made the arrangements for storage of oil in other countries, i.e. with France in October 1966, followed by Italy in 1969. To avoid double counting of the strategic stocks, these ordinances specified that the stocks had to be owned or co-owned by the *Vorratspflichtige*. Furthermore, the storage facility in the other country also had to meet the national requirement of minimum stocks in that country, and naturally the German emergency stocks could not be reported to other national authorities as representing imposed minimum stock requirements in those nations.²⁷ Similar agreements were subsequently concluded with Belgium and the Netherlands.²⁸

Cross-border stockpiling agreements were subsequently provided for in the EEC 1968 directive. But it carefully specified the intergovernmental rather than the supranational nature of the undertaking: 'stocks may be established, under individual agreements between Governments, within the territory of a Member State for the account of undertakings established in another Member State'.²⁹ The stocks were still nationally owned and controlled, they were just stored on the soil of another EEC member state. The Commission's more ambitious proposals for a 120-day stockpile stored in salt caverns in Germany and France, excluding the day-to-day stocks of companies, was less successful. As the proposal would give the Commission the power to allocate in times of crisis, this met with strong opposition among member states and oil companies alike. The words of a contemporary observer aptly confirm the limits of the European willingness to engage in burden-sharing before the 1973 oil shock: 'The time is not quite yet ripe when one country would be willing to trust its supply of vital oil to the care of a neighbor'.³⁰

Concluding remarks

In its most basic form, a stockpile can be designed to cover the shortfall of supply due to complete loss of imports for a limited time period. However, stockpiling raises complex questions that need to be addressed at both the domestic and the international level. They include the size and type of oil stocks, ownership and rules for release, burden-sharing between states but also between business and national governments, as well as the linkages between national and international allocation mechanisms during a crisis. While the oil shocks of the 1970s occupy a privileged space in ongoing discussions about oil supply security, we should not neglect the longer history of stockpiling of oil among Western industrialized countries. European states had already imposed storage obligations on businesses in the oil industry prior to the oil shock, despite protests that they were unfair, costly or unconstitutional. In this respect, the Europeans were ahead of the US, even though the latter had a long tradition of reserving oil lands for military requirements. While the US also introduced similar provisions for private stockpiling obligations in the wake of the oil crisis, they were quickly abandoned as the massive federal stockpiling program got underway. Beyond the national stockpiling programs, multilateral discussions of stockpiling targets occurred in NATO, OEEC/OECD and the European communities. This cooperation ranged from the storage of resources on foreign soil to the establishment of common norms for stock levels and allocation schemes under crisis conditions. There were also instances of trans-border

stockpiling projects, such as between Norway and Sweden, or a series of German arrangements pursuant to the EEC's 1964 recommendation. In the latter case the bilateral arrangements were themselves the outcome of a multilateral endeavor, but also the Swedish–Norwegian project was established during discussions of Nordic regional integration. So although oil security might cut to the heart of national security and sovereignty, it did not take an oil shock to make Western industrial states realize that 'national oil supply security is a function of international factors' (Krapels, 1980).

Notes

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Talking about OPEC without talking to OPEC?

The (non-)relationship between the International Energy Agency and OPEC 1974–1990

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Introduction

2014 was an important year for the International Energy Agency (IEA): the organization of oil-consuming countries celebrated its 40th anniversary. For this reason, it acclaimed itself with a special issue of its magazine *IEA Energy*. Prominently placed, the first article in the magazine was an official message of congratulations by the secretary-general of OPEC, Abdalla Salem El-Badri. Under the headline ‘Dialogue replaces OPEC-IEA mistrust’ (El-Badri, 2014, p. 7), he emphasized the importance of OPEC’s close collaboration with the IEA for the stability of global energy markets.

When the industrialized countries founded the IEA in 1974 under US leadership, such a development was not foreseeable. The provision of the International Energy Programme (IEP), the basic founding document of the IEA, to ‘promote co-operative relations with oil producing countries [...] through a purposeful dialogue, as well as through other forms of co-operation, to further the opportunities for a better understanding between consumer and producer countries’ (Scott, 1994a, p. 143), was not worth the paper it was written on. Therefore, the first IEA executive-director Ulf Lantzke conceded when he resigned in 1984: ‘The one area where the IEA has made little progress during the last 10 years is in its relations with OPEC’ (Scott, 1994b, p. 341).

So, in this chapter I would like to discuss why there were no formal contacts between the most prominent oil producer and oil consumer organizations in the 1970s and 1980s. Why was it impossible to talk directly with each other, although both had the aim of stabilizing the oil market? By trying to answer these questions the article will shed light on the (non)relationship between the IEA and OPEC in the first 15 years that has not yet been in the focus of research.²

Of course, we have to bear in mind that the IEA represented only one of many possibilities for the member countries to communicate with OPEC and the oil-producing countries. The government representatives talked directly on a bilateral basis with the oil producers. The most important bilateral relations were the US-Saudi-Arabian contacts.³ Additionally, the large multinational oil companies were important purveyors and transmitters of information, at least for their home countries, the United States, the United Kingdom and the Netherlands. Representatives of member states, international organizations and business

also met at international conferences or events organized by institutions like the Ditchley Park Foundation, the Oxford Institute for Energy Studies or the Bergedorfer Gesprächskreis. Nevertheless, the member states discussed time and again an activation of the IEA to start an inter-organizational dialogue. And, above all, it was in the genuine interest of the organization itself, the secretariat with its executive-director at the top, to play a prominent role in a potential global energy dialogue to underscore the IEA's relevance. The view I present on the following pages is therefore based mainly on sources of the IEA, its member countries and its first executive-director Ulf Lantzke.

To answer the opening questions, the chapter is divided into four sections. In the first part I will describe how the relationship with the oil producers influenced the founding negotiations of the IEA and the first contact during the Conference on International Economic Cooperation (CIEC). The following part deals with the poor relations throughout the second oil crisis. Subsequently, the possible rapprochement during the deliberation on OPEC's long-term strategy at the beginning of the 1980s comes into focus. The final section analyzes the influence of the changing market conditions and economic doctrines of the 1980s on the discussions about an energy dialogue between oil consumers and producers.

Undermining OPEC's dominance without deliberate provocation: the founding period of the IEA

The IEA was not the first organization of oil-consuming countries, but it changed the established patterns of cooperation considerably. Before its founding the developments of the oil market and possible interruptions of oil supplies were discussed in the oil committee of the Organization of Economic Cooperation and Development (OECD). This Paris-based organization of the industrialized countries had the advantage of being able to assemble the economically most important countries of Europe, North America and the Pacific region (Graf, 2018, pp. 52–62; Türk, 2014, pp. 209–230; Beers, 2016, pp. 143–171). At the beginning of the 1970s the oil committee established an oil crisis mechanism for its European members and made specifications for the strategic petroleum reserves of the OECD countries. It regularly checked whether its recommendations were being implemented (Scott, 1995, pp. 163–164; Kapstein, 1990, pp. 159–160).

But the oil committee was ill equipped for quickly deciding in crises situations. It was composed of bureaucrats from the governments and mainly discussed ongoing and future trends of the oil market. Above all, its decisions had to be adopted unanimously. The defects of the oil committee structure became obvious during the first oil crisis in 1973/4.

Shortly after the outbreak of the Yom-Kippur-War between Israel and its Arabian neighbors Syria and Egypt on 6 October 1973, the Organization of Arab Oil Exporting Countries (OAPEC) decided to embargo Israel-friendly countries like the USA and the Netherlands. Other countries, like the UK and France, were classified as friendly and were thus treated preferentially. The remaining countries were considered to be neutral. They were hit by a monthly 5 percent reduction of oil production. In parallel, the broader OPEC increased the posted price of oil until it quadrupled at the beginning of 1974 (Hohensee, 1996, pp. 80–82; Graf, 2012, pp. 185–208; Yergin, 1991, pp. 735–773).

The clever breakdown of consumer countries into preferential and non-preferential categories was effective. It was not possible for the OECD's oil committee to reconcile the different positions of the member states. France and Britain, in particular, tried to maintain their preferential status, fearing disadvantages should they increase cooperation with the embargoed countries. Therefore, the oil committee was incapable of bringing about a decision and finally had to leave the allocation of oil to the oil companies. The US government was particularly disappointed by the oil committee's performance and dismissed the OECD as a mere 'talk group',⁴ which was not able to counter the assumed new power of the oil-producing countries.

Consequently, it was mainly the State Department with Secretary of State Henry Kissinger that started to look for new ways of organizing consumer cooperation. Kissinger saw a possibility of increasing the US profile with regard to OPEC by taking over the leadership of consumer cooperation (Türk, 2014, pp. 217–226). Additionally, he tried to exploit the energy vulnerability of the Western European countries and Japan, which had become more self-confident in the realm of foreign policy in the preceding years. With US offers in energy cooperation he could potentially tie these countries closer to the US and reinstall its leading role in the Western camp. The strong position of the US regarding questions of energy, which Kissinger wanted to bring into the equation, brought no advantage to the OECD. Due to the unanimity rule, any small country could hold up a vote. The question was therefore how to find new forms of cooperation whereby the US could make better use of its strong role on energy policy.

Kissinger took the initiative and proposed an ‘Energy Action Group’ of oil-consuming countries in December 1973. This proposal was discussed during the Washington Energy Conference, 11–13 February 1974. Finally, the conference participants, with the exception of France, authorized a group of leading energy bureaucrats to explore how a close cooperation of the energy-consuming countries was to be formed. During these founding negotiations of the IEA between February and November 1974, the officials of the participating governments discussed controversially how strictly or loosely the cooperation of the oil-consuming countries should be organized (Graf, 2018, pp. 287–307; Türk, 2014, pp. 209–230). The discussion ranged between founding a strong organization as a sort of anti-OPEC or just to broaden the tasks of the OECD’s oil committee. This decision would of course imply different signals to OPEC. It was especially the US government that favored a strong new organization that would counter the power of OPEC; whereas the more energy import-dependent Europeans argued for the OECD option. Such a solution would also enable the participation of France, whose government refused to take part in a new organization led by the US (Gfeller, 2012, pp. 114–141). The main source of conflict was therefore the question of what message the industrialized countries wanted to send to OPEC and the oil-producing countries. The negotiating countries finally found a compromise. They established a new organization, the IEA, but under the umbrella of the OECD, an organization not known for its aggressive policies. Besides, the officials took the technical name ‘agency’. This sounds neutral, without any political impetus; at first glance it looked like a technical organization of energy experts. The officials also agreed that the founding act was to be organized ‘business-like’ and ‘low-profile’⁵ and not even TV cameras were allowed. This underlines the effort that was made not to provoke OPEC by saber-rattling.

Of course, this sort of sober and technical atmosphere surrounding the IEA was to cover up the fact that the IEA’s founding was eminently political. It was a tool for the consuming countries to influence the evolving global energy order. Thus, the IEA did not just establish a crisis mechanism for the sharing of oil in future oil crises, it also developed a long-term strategy away from insecure Middle Eastern oil. The so-called Long-term Cooperation Program was based on the substitution of oil by coal, gas and atomic energy, a diversification of oil imports and the conservation of oil (Scott, 1995, pp. 171–204). Additionally, it comprised a minimum safeguard price for crude oil of 7\$ per barrel. This floor price was to protect the investments of the oil consumers in the development of their own resources against a feared dumping strategy of OPEC. Of course, the IEA’s cooperation program was not overtly aggressive. It was, as the IEA’s executive-director, the West German Ulf Lantzke emphasized, a ‘defensive’⁶ strategy that even corresponded to the demand of OPEC. In the solemn declaration of OPEC’s summit meeting in March 1975 the heads of state proclaimed:

While recognizing the vital role of oil supplies to the world economy, they believe that the conservation of petroleum resources is a fundamental requirement for the well-being of future generations and, therefore, urge the adoption of policies aimed at optimizing the use of this essential, depletable and non-renewable resource.

(Skeet, 1988, p. 126)

But, mainly from the US perspective, the IEA's inward-looking approach was ultimately designed 'to break the political and economic power of OPEC'.⁷ Even after the adoption of the Long-Term Cooperation Program on 30 January 1976, the US particularly pushed for further decisions to maintain the impression of the IEA being an 'action-oriented organization'.⁸ Secretary of State Henry Kissinger emphasized in a conversation with the CEOs of the major US oil firms that the 'IEA must be strong and, more importantly, must look strong'⁹ to achieve its aims.

This is also reflected in the communiqués the IEA released after its ministerial meetings during that period which always used strong wording. For example, the consuming countries pledged 'to strengthen their energy policies and measures' (Scott, 1995, p. 355). They were determined to reduce the future risks by 'a strong, concerted and sustained policy response' (Scott, 1995, p. 356). They 'expressed their firm political determination to reinforce their national policies' (Scott, 1995, p. 354).

So, in the first years of the IEA's existence the oil-consuming countries perceived themselves to be in a weak position vis-à-vis the oil-producing countries. The IEA therefore served as a tool to boost the position of the oil-consuming countries. This also influenced the only direct contact of OPEC and IEA in the 1970s during the CIEC.¹⁰ The conference took place in Paris between 1975 and 1977 and was attended by 19 developing countries, seven industrialized countries and the EC delegation. OPEC and IEA were allowed as observers with the right to speak. The conference discussed the economic relationship between the developing and industrialized countries. For most of the industrialized countries the conference basically centered on energy. Before the official meetings they determined their position in an ad-hoc IEA committee, the so-called Burrows Group that was headed by the British assistant under-secretary for transport and energy in the Foreign and Commonwealth Office, Reginald Burrows (Roggen, 1979, pp. 175–188). The Burrows group met on an informal basis and was more flexible in its work than the formally responsible Standing Group on Producer–Consumer Relations.¹¹

In contrast to the narrow approach of many industrialized countries, OPEC and other participating developing countries wanted to use the CIEC for the establishment of a New International Economic Order that would improve the position of the developing countries in the world economy. The CIEC therefore provided an opportunity for OPEC to present itself as the vanguard of developing countries. At the conference, the gap between the different approaches could not be bridged. It ended with only meager results and above all, it proved impossible to install a mechanism for consultations between oil-consuming and oil-producing countries that was put forward by the industrialized countries. Some OPEC countries viewed this proposal with suspicion. They feared discussions about oil pricing where they would face a phalanx of industrialized and developing oil-consumer countries (Stabreit, 1977). OPEC and IEA thus passed up a chance of rapprochement.

Based on its positive experiences during preparations of the conference meetings, the IEA now decided to continue the work of the 'Burrows Group' that became the Ad Hoc Group on International Energy Relations in June 1977. The IEA's decision-making body, the Governing Board, instructed the Ad Hoc Group to regularly 'report to the Governing Board on international energy relations' (Scott, 1994a, p. 148). When Reginald Burrows resigned in May 1978, his female successor in the Foreign and Commonwealth Office, Gillian Brown, took over the chairmanship of the Ad Hoc Group – a change that underscored the continuous interest of the British government in this topic.¹²

In 1978 and 1979 the Ad Hoc Group discussed the various UN conferences and initiatives on energy and the members informed each other about their bilateral contacts with oil producers and OPEC. Proposals to re-open a formal dialogue, advocated by British and Dutch representatives, were opposed by American and German delegates that feared the role of supplicant and warned about re-establishing a common front of OPEC and the developing countries.¹³ In this way, the IEA maintained a 'low profile'¹⁴ on the issue. The difficult relationship between the consumer and the producer organization was further strained by the second oil crisis.

Strained relations: the second oil crisis

Despite the precautions for another oil crisis, the IEA and its member countries were ill prepared for the second oil crisis in 1979 (Martin and Harje, 2005, pp. 101–103; Keohane, 1982, pp. 469–481). The drop out of Iran as the second largest oil exporter from the oil market was caused by violent regime change from the Shah to Ayatollah Khomeini in January/February 1979. This event caused panic in the oil market, with the result that many oil companies bought their oil on the narrow market for short-term contracts, the so-called spot market. The price for crude oil exploded, and the OPEC countries adapted their price policy to the spot market trends (Kohl, 1982, pp. 214–239; Yergin, 1991, pp. 830–883).

The developments intensified the IEA's impression that OPEC and its members were not interested in a stable development of the oil market but rather in short-sighted maximizing of the revenues. The IEA therefore tightened its internal measures to reduce oil consumption and the monitoring of the implementation (Scott, 1994b, pp. 114–120). The fact that the activity of the IEA directly aimed at influencing OPEC's and its members' production and pricing policy can be illustrated by looking at the IEA's ministerial meeting in December 1979. Primarily it was scheduled for January 1980 but the US proposed in November to bring the meeting of ministers forward to December, shortly before OPEC's meeting in Caracas on 17 December. During the preparation of the meeting, the US State Department pleaded for strict oil import targets of the IEA's member countries for 1980 to release pressure on the market. It explicated that the targets 'must be credible if they are to have any effect on the oil market and on other nations, particularly members of OPEC'.¹⁵

During the IEA ministerial meeting the ministers decided to introduce so-called oil import ceilings for every member country that were to be revised quarterly¹⁶ (Scott, 1995, pp. 364–367). The results of the IEA ministerial were transmitted by the US government to the Venezuelan Government and the delegations of OPEC countries in Caracas. The US State Department assessed the IEA meeting in its aide-mémoire for the OPEC member countries:

The IEA nations agreed that a solution to the world's serious energy problems requires a common approach by producing and consuming countries, both developed and developing. They expressed their confidence that oil producers will recognize their important role in pursuing policies which contribute to the stabilization of conditions in the world oil market and in the world economy.¹⁷

By this, the IEA members appealed to OPEC to decide on setting moderate prices and adequate production levels. The IEA therefore served as a sort of signal transmitter to OPEC. The IEA members tried to show OPEC that they were determined to reduce oil consumption heavily and thus change market conditions by internal measures. Additionally, countries like the US tried to exploit the coordinated IEA and G7 meetings¹⁸ in subsequent bilateral talks with OPEC members like Saudi Arabia. The US government thus underscored with the help of the IEA its leading role with regard to the energy policies of the Western industrialized countries.¹⁹

But all the signals of the IEA and its member countries were in vain. Even when the demand was starting to decline, the OPEC ministerial meeting in Algiers on 9–11 June 1980 increased the range of prices for crude oil (Skeet, 1988, pp. 170–171). The fact that OPEC disregarded the signs of the IEA disappointed the member governments. A direct reaction was the tough wording during the G7 summit in Venice on 22–23 June 1980. It adopted a communiqué that sharply condemned OPEC's behavior:

Successive large increases in the price of oil, bearing no relation to market conditions and culminating in the recent decisions by some members of the Organization of Petroleum Exporting Countries (OPEC) at Algiers, have produced the reality of even higher inflation and the imminent threat of severe recession and unemployment in the industrialized countries. At the same time they have

undermined and in some cases virtually destroyed the prospects for growth in the developing countries.

(G7, 2007a)

Against this background, the summit countries pledged in a chapter on energy issues to reinforce the measures for a transition of their economies away from insecure oil supplies (G7, 2007b). In parallel to this more confrontationist rhetoric first signs appeared that heralded a rapprochement between the oil-producing and consuming countries.

A chance for rapprochement: OPEC's long-term strategy and its discussion by the IEA in 1980

Since May 1980, in the final phase of the second oil crisis, the IEA members discussed the possibility of approaching OPEC directly.²⁰ During a ministerial meeting of the IEA in May 1980, the European Community (EC) delegation headed by Commissioner Guido Brunner advocated talking with OPEC and the oil-producing countries. Brunner proposed political arrangements about production levels and pricing.²¹ The IEA's executive-director Ulf Lantzke mentioned in an interview with the West German newspaper *Saarbrücker Zeitung* that arrangements with OPEC could be possible at the end of the year. Both saw a reliable development of oil prices as more beneficial to the world economy than the sharp jumps in prices during the first and second oil crises.

These voices were a direct reaction to OPEC's search for a long-term strategy that had already started two years earlier. During a meeting in Taif on 6–7 May 1978, OPEC countries had decided to set up a ministerial committee that was to prepare a future strategy concerning supply and prices and the relationship towards the less developed countries. The committee was composed of the oil ministers of Algeria, Iran, Iraq, Venezuela, Saudi Arabia and Kuwait and established an expert group under the chairmanship of the Saudi Arabian oil minister, Ahmed Zaki Yamani (Skeet, 1988, p. 147; Parra, 2009, pp. 216–217). The committee and the expert group had numerous meetings in the following turbulent years but in 1980 the end of the process was eventually on the horizon. An extraordinary ministerial conference discussed a draft of the final report in May 1980 and planned to solemnly introduce the long-term strategy during the celebrations of OPEC's 20th anniversary in autumn 1980.

For the oil-consuming countries the report was the starting point for intensive discussions. The report fixed a formula for indexing the oil price and comprised some paragraphs on producer–consumer relations. The draft assumed a new dialogue in the near future and advocated the participation of OPEC countries 'as a bloc' (CIA Report, 11 September 1980). Expecting the adoption of the report on the planned OPEC summit in Bagdad in November, the IEA and its member states started to discuss possible reactions to OPEC's long-term strategy and the dialogue proposal. In parallel to the summit meeting, OPEC wanted to hold an expert seminar in Vienna and invited the IEA secretariat and some member states to participate.

Thereupon, IEA executive-director Ulf Lantzke convened the representatives of the most important member countries for two brainstorming sessions in October 1980 to prepare a common position. During these discussions the secretariat championed a replacement of the 'present unorganized development of producer/consumer relations through the North/South-Dialogue' by 'an attempt to organize coherent exchanges about energy alone'.²² All the other delegations expressed their doubts about the usefulness of this idea. The British representative recommended further studying OPEC's proposals before starting a dialogue. The head of the energy department in West Germany's economics ministry, Ulrich Engelmann, warned that a direct talk with OPEC could offend the other developing countries. Other delegations preferred bilateral talks to a multilateral dialogue. The US representative, Leslie J. Goldman, saw the Vienna expert seminar as a kick-off for further talks and advised meeting again before the seminar. Rossoni, the Italian delegate, favored starting the discussion with OPEC on the basis of an IEA paper and not

with the OPEC long-term strategy as a starting point. Lantzke summarized that ‘existing bilateral contacts should continue’, but that ‘broader contacts while avoiding ‘institutionalization’²³ were needed.

In the following weeks these plans failed to come to fruition because OPEC was deeply divided. The war between its members Iran and Iraq that had begun in September 1980 particularly strained the internal work of the producers’ organization. OPEC therefore cancelled the meeting of heads of state and the scheduled seminar in Vienna. The work on the long-term strategy was suspended. Instead of pushing forward its own agenda, the IEA and its members now also stopped their discussions about OPEC’s long-term program. The topic of an intensified exchange between OPEC and IEA disappeared from the agenda and the IEA switched to business as usual. The Ad Hoc Group on International Energy Relation, now headed by the Dutch ambassador H. C. Posthumus Meyjes, reported on bi- and multilateral contacts, for example in the framework of the UN, and the IEA’s Standing Group on the Oil Market observed OPEC’s economic decisions and the effects on the oil market. Above all, the urgency of a dialogue diminished from the perspective of the IEA’s member states as the market became more and more relaxed.

From asymmetries to a more balanced relationship: the buyers’ market of the 1980s and the developments of the 1990s

In the first years of the 1980s, three developments influenced the oil market: the global economic recession after the second oil crisis, the diversification and conservation measures of the industrialized countries and the extraction of more oil by non-OPEC oil producers like the UK, Norway or the Soviet Union. This led to an excessive supply and consequently to falling prices.²⁴ In this situation, where the industrialized countries’ strategy since the first oil crisis finally seemed to be bearing fruit, there was no need for the IEA countries to start direct talks with OPEC.²⁵

Additionally, the now prevailing economic approach of the industrialized countries was not favorable for common talks between IEA and OPEC. The more state-centric Keynesian view of the economy during the 1960s and 1970s now gave way to a so-called neoliberal approach that tried to roll back the state’s interference in the market (Rodgers, 2012). The new thinking was mainly promoted by the new US administration of President Ronald Reagan, who won the elections in November 1980 and the British prime minister Margaret Thatcher, who held office from May 1979 to November 1990. From a neoliberal perspective it was unthinkable that oil consumers and oil producers would sit at the same table discussing the development of the oil market. This was made plain by the US representative to an informal meeting of oil consumers in April 1981. The deputy assistant secretary of energy for international resources, Peter Borre, told the participants, that ‘[a]n agreement with OPEC countries on prices was not compatible with the economic attitudes of the new US Administration which favored laissez faire, budget cuts, and putting domestic economy in order before negotiating abroad [...]’ (Garavini, 2014, p. 159). As a result, dialogue was prevented by the prevailing economic doctrine.

The unbalanced relationship between the two parties was equally important. During the 1970s, the consumers seemed to be in an inferior position towards the producing countries. This relationship changed in the 1980s. Now, in the atmosphere of a buyer’s market OPEC seemed to be in a relatively weak position. For OPEC it thus would have been unwise to get closer to IEA from the inferior position of supplicant, and for the consuming countries there was a danger of giving up their favorable position (Mabro, 1991, p. 2).

The new initiatives that were launched by Lantzke’s successor Helga Steeg were therefore only supported in a lukewarm way by most of the member states. She took the opportunity of an intensified exchange between the EC and the Gulf Cooperation Council (GCC) to propose closer contacts between the IEA and Middle Eastern oil producers in October 1984. But it was mainly the US government, supported by the Germans, which opposed any installation of a structured dialogue and warned of talking about prices and production levels.²⁶ In the following months every cautious step to convert the bilateral

and informal contacts into a more structured dialogue was declined by Allan Wendt, Borre's successor as deputy assistant secretary of state for energy and US representative in the Governing Board of the IEA. He emphasized that the agency was not designed for a structured dialogue and that bilateral talks were essential.²⁷ Obviously, besides neoliberal doctrine that did not provide for interference in the market, it was the fear of the US government of losing its privilege of preferential contacts with the oil producers that influenced the US position.

The intransigent US attitude and the prevailing 'asymmetry' (Mabro, 1991, p. 2) between a weak and a strong group of countries only changed at the beginning of the 1990s. During the Gulf War, close collaboration of the IEA and some OPEC countries, especially Saudi Arabia, which increased production, helped to calm the oil market (see Van de Graaf, 2016, pp. 595–600). The communiqué of the IEA ministerial meeting on 3 June 1991 therefore 'commended the cooperative spirit shown by oil producing countries which had increased their oil production during the crisis to compensate for lost Iraqi and Kuwaiti supply' (Scott, 1995, p. 444). Additionally, with the collapse of the Soviet Union and the Eastern European communist states, the oil market changed rapidly. In this situation of common interests of OPEC and IEA in stabilizing the market, the IEA executive-director Helga Steeg took the initiative and organized informal meetings of IEA and OPEC officials in her apartment in Paris, as she told the author in an interview. The contacts developed into official meetings on ministerial and expert levels. The meetings were not meant as a means to influence the markets but as an exchange of views, discussions on common problems and a closer collaboration in the collection of data about the oil market. These common talks were finally institutionalized as the so-called International Energy Forum (IEF) with its secretariat in Riyadh that mainly organizes the contacts between the IEA and OPEC today (Fattouh and van der Linde, 2011).

Conclusion

A closer look at the relations between the IEA as the main energy consumer organization and the OPEC as the main producer organization during the 1970s and 1980s reveals that it was impossible to develop official and formalized contacts. The exchange between the two organizations therefore remained informal. The staff met at private conferences or at sessions on the international level, as in the UN framework. Additionally, the IEA member states had their bilateral channels to communicate with the oil-producing countries and exchanged views with the multinational oil companies.

Although a formal dialogue between IEA and OPEC was not possible in these decades, the IEA closely observed and discussed the decisions of OPEC and the development of bilateral relations between consumer and producer countries. The IEA thus served as a forum for the exchange of the member states' perception of OPEC and the producer countries. The main bodies that dealt with this topic were the Standing Group on the Oil Market and the Ad Hoc Group on International Energy Relations.

As we have seen, it was mainly the executive-directors Ulf Lantzke and Helga Steeg that tried to change this *low profile*-policy of the IEA with the aim of increasing IEA's importance for the global energy order. They initiated discussions about formalizing a dialogue during the negotiations of OPEC's long-term strategy in 1980 and during the extension of the EC relations with the Gulf Cooperation Council in the midst of the 1980s. Both initiatives were thwarted by the reactions of the IEA member countries that feared a formal dialogue for a number of reasons.

One point was the unbalanced relationship between the two organizations. During and after the first oil crisis, with prices going up, the IEA members perceived the OPEC to be in the ascendancy. Thus, a direct contact was a dangerous game and especially the US representatives always warned of going into direct talks without carving out a common and strong position before the meetings. Additionally, the main interest of the IEA and its member states was energy. This approach led to a cautious reaction from OPEC. It perceived possible talks about energy alone as dangerous, because they could lead to an isolated position

of OPEC among the developing countries. This was something the oil producers wanted to avoid at any costs, because they saw themselves as the vanguard of the developing countries in the carving out of a New International Economic Order based on fair prices for the resources of the developing countries.

With the oil price decline and the drop of OPEC's share in the oil market in the 1980s, the oil consumers seemed to be in a better position. Now, it seemed unwise for OPEC to search for common talks from a weak starting base. Besides, the 1980s, with the 'neoliberal agenda' coming into vogue, were not suited for a formal dialogue. It was above all the US government that now opposed any strengthening of contacts between the two organizations, which it denounced as an unnecessary interference in the market. By this, the US with its special relations to producer countries like Saudi Arabia also defended its predominant position with regard to consumer–producer contacts.

All in all, the IEA was not able during the 1970s and 1980s to establish a global energy order in cooperation with OPEC. It remained a more or less inward-looking organization that laid the focus on the development of a coherent energy policy of its member states. By pushing the use of nuclear energy and coal and the advancement of energy conservation the IEA tried to change the global energy order with defensive measures that were even in line with OPEC's demand of a canny use of crude oil resources. In this respect the IEA also served as a signal transmitter to OPEC. The consumer organization and its member states kept OPEC informed about their internal measures. They tried to influence OPEC's decisions by demonstrating their determination to restructure the energy basis away from OPEC's oil.

This inward-looking approach changed at the beginning of the 1990s. Now, international developments like the Gulf War and the fall of communism in Eastern Europe had drastic impacts on the global energy order and led to a rapprochement between producer and consumer countries and their respective organizations. In this period both OPEC and IEA built the groundwork for the formal exchanges of today.

Notes

- 1 I would like to thank Giuliano Garavini and Dag Harald Claes for their comments on a first draft of this article.
- 2 The research on the relationship between OPEC and IEA mainly concentrates on the developments since 1990. See, above all, Van de Graaf (2016, pp. 591–609).
- 3 On this topic see the contribution by Anne Viden to this volume.
- 4 *Foreign Relations of the United States* (1969–1974), volume XXXVI, document 247, pp. 697–701. 'Memorandum of Conversations', Washington, DC: Government Printing Office, 26 November, p. 699.
- 5 *International Energy Agency Archive*. Folder ECG 11600 7, I General, 'Memorandum from Ulf Lantzke to the Secretary General of the OECD, Emile van Lennep, Paris, 10 November 1974, concerning ECG–Meeting held in Brussels on 8th November'; *Politisches Archiv des Auswärtigen Amts*. Bestand B71, vol. 113894. 'Aufzeichnung des Referatsleiters Kruse betr. Folgearbeiten der Washingtoner Energiekonferenz, hier Sitzung der Energiekoordinierungsgruppe (ECG) am 8.11.74, Bonn, 11 November 1974'.
- 6 *Bundesarchiv Koblenz (BaK)*, Bestand N1360 (Nachlass Lantzke), vol. 154, 'Lecture series of Ulf Lantzke at the University Cologne 'Problems of the international cooperation on energy', 1977/78', p. 6.
- 7 *Foreign Relations of the United States* (1974–1980). Volume XXXVII, document 40, pp. 135–139. 'Paper Prepared in the Department of State, undated [presumably February 1975]'. Washington, DC: Government Printing Office, p. 137.
- 8 *Foreign Relations of the United States* (1974–1980). Volume XXXVII, document 100, pp. 357–360. 'Briefing Memorandum from the Acting Assistant Secretary of State for Economic and Business Affairs (Katz) to Secretary of State Kissinger'. Washington, DC: Government Printing Office, 16 July 1976, p. 359.
- 9 *Foreign Relations of the United States* (1974–1980). Volume XXXVII, document 75, pp. 255–262. 'Memorandum of Conversation, Washington, 7 August 1975'. Washington, DC: Government Printing Office, pp. 255–256.
- 10 The following sketch is very rough. For a more nuanced view on the CIEC, see Garavini (2009, pp. 153–168), Graf (2018, pp. 315–319) and Garavini (2012, pp. 215–230).
- 11 The IEA was organized on the basis of so-called Standing Groups where government representatives and members of the secretariat met to discuss the various topics of IEA's work. On the structure of the IEA, see, for example, Willrich and Conant (1977, pp. 199–223), Scott (1977, pp. 1–56), and Roggen (1979).

- 12 *Politisches Archiv des Auswärtigen Amt*. Zwischenarchiv, vol. 121293. 'Vermerk Betr. OECD/IEA, hier: Vorsitz in der ad-hoc-Arbeitsgruppe für Internationale Energie-Beziehungen der IEA (Burrows-Gruppe)'. Bonn, 24 February 1978.
- 13 *Politisches Archiv des Auswärtigen Amt*. Zwischenarchiv, vol. 121293. 'Aufzeichnung der Abteilung III D1 betr. International Energy Relations'. Bonn, 17 January 1978.
- 14 *Politisches Archiv des Auswärtigen Amt*. Zwischenarchiv, vol. 121293. 'Vermerk betr. Sitzung der Burrows-Gruppe am 18.1./Verwaltungsrat am 19.1.1978, hier: Zukünftige Ausgestaltung der Arbeiten der Burrows-Gruppe'. Bonn, 23 January 1978.
- 15 *Foreign Relations of the United States (1974–1980)*. Volume XXXVII, document 244, p. 770–772. 'Telegram from the Mission to the Organization of Economic Cooperation and Development to the Department of State, Paris, 16 November 1979'. Washington, DC: Government Printing Office.
- 16 *Foreign Relations of the United States (1974–1980)*. Volume XXXVII, document 251, p. 787–788. 'Memorandum from Secretary of Energy Duncan and Henry Owen from the National Security Council Staff to President Carter, Washington, 12 December 1979'. Washington, DC: Government Printing Office, p. 788.
- 17 The communiqué of the next meeting was sent by the German chair to OPEC and its members. See *Bundesarchiv Koblenz (BaK)*, Bestand B102, vol. 309210, 'Aufzeichnung des Auswärtigen Amtes der Bundesrepublik Deutschland betr. Ministerkonferenz der Internationalen Energieagentur (IEA) am 21./22. Mai 1980
- 18 The meetings of the heads of states of the economically most important industrialized countries mainly centered on energy until the beginning of the 1980s. See the contribution by Federico Romero to this volume.
- 19 *Foreign Relations of the United States (1974–1980)*. Volume XXXVII, document 274, pp. 861–863. 'Telegram from the Department of State to the Embassy in Saudi-Arabia, Subject: Text of Letter from the President to Prince Fahd, Washington, 31 May 1980'. Washington, DC: Government Printing Office.
- 20 *Bundesarchiv Koblenz (BaK)*, Bestand B102, vol. 309211. 'Aufzeichnung des Wirtschaftsministeriums betr. IEA Governing Board 21./22.5. 1980, here: International Energy Relations, Bonn, 19.5.1980'.
- 21 *Bundesarchiv Koblenz (BaK)*, Bestand B102, vol. 309210, 'Energie-Agentur: Ölverbrauch einschränken', *Süddeutsche Zeitung*, Mai 23, 1980.
- 22 *National Archives of the United Kingdom*. Foreign and Commonwealth Office (FCO), vol. 96/1029, 'IEA Members Informal Lunch'. Paris, 20 October 1980.
- 23 *National Archives of the United Kingdom*. Foreign and Commonwealth Office (FCO), vol. 96/1029, 'IEA Members Informal Lunch'. Paris, 20 October 1980.
- 24 A lowpoint was reached in 1986. On the oil market in the 1980s, see Basosi et al. (2018).
- 25 *Akten zur Auswärtigen Politik der Bundesrepublik Deutschland 1984* (2015). Document 215, pp. 983–989. Berlin: De Gruyter, 'Aufzeichnung des Ministerialdirigenten Sulimma, 14.8.1984, betr. gegenwärtige Rolle und zukünftige Entwicklung der OPEC zehn Jahre nach der ersten Ölkrise 1973/74', p. 985.
- 26 *Historical Archives of the European Union*. Christopher Audland Papers, vol. CA-1. 'Christopher Audland, Directorate-General for Energy, Commission of the European Communities, Note for the Attention of Vice President Davignon, Subject: Contacts between industrialized countries and oil producing countries'. Brussels, 26 October 1984.
- 27 *Historical Archives of the European Union*. Christopher Audland Papers, vol. CA-2, 'Christopher Audland Directorate-General for Energy, Commission of the European Communities, Note for the Record, Subject: Informal IEA lunch on Producer/Consumer Relations'. Brussels, 5 February 1985.

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How OPEC made the G7

Western coordination in the wake of the 'oil shock'

Federico Romero

Western powers experienced, and to a certain extent steered, profound economic policy changes in the aftermath of OPEC's oil price rise of 1973. They reframed their perception of the international trade and finance system, with a strong emphasis on an unprecedented interdependence. They transformed their own mode of coordination and governance. They ushered in a new, market-driven financial and monetary regime that eventually shaped the more recent stage of globalization. The G7 summits, which came about in direct response to OPEC's challenge, were the most visible aspect of these intertwined changes, the emblematic tip of the iceberg. By looking at their debates, I argue that OPEC and the broader Global South had a considerable impact on the refashioning of Western economic governance along the emerging neo-liberal paradigm. The latter triumphed also because it functioned as a tool to rebut and divide the Global South, while channeling OPEC's increased revenues in liberalized financial markets. At the origins of modern globalization sits a complex, mobile triangular relationship that reframed financial dominance in the post-colonial world as well as the West's own system of governance.

A divided West gets 'shocked'

The key term used by contemporaries to label the industrialized countries' reaction to the oil crisis of 1973–74 was *shock*. The notion of an *oil shock* still echoes in public memory and many historical accounts. Its immediate connotations are of surprise and disbelief, but its more meaningful implications spell disarray and muddled responses. The latter descended, at least in part, from poor predictions and therefore unpreparedness. The consequences of a steep oil price rise were not really anticipated, except by a few specialists, and its public impact was therefore more disruptive and bewildering (Madureira, 2014). However, at the core of the *shock* interpretation advanced by subsequent analysts sits also a negative assessment of the policy responses devised by the West. Historians pointed out that different degrees of vulnerability dictated divergent national reactions; that most European countries scrambled to secure their supplies unilaterally; and that early attempts at coordination by the Organization for Economic Cooperation and Development (OECD) failed (Chakarova, 2013; Lieber, 1983). As one of the most authoritative scholars, Fiona Venn, wrote, 'dynamics of conflicting interests' appeared to have prevailed within Europe and across the Atlantic, and they doomed to failure any 'attempts to create an international regime' (Venn, 1999, p. 71 and p. 91). This assessment makes sense if referred to failed plans for energy resources' pooling or large-scale conservation. Yet, the West's own transformations in reaction to the oil crisis were so profound that such a

belittling reading appears misleading. Far from failing to respond, the West embarked on a profound, momentous redefinition and restructuring of its international economic regime.

The failed response thesis rests on two premises that need to be reconsidered in order to situate this story in context. The first one concerns the assumption that the *oil shock* pulled Western countries apart. It rests on a misapprehension. When the oil embargo and price rise struck, Japan was a substantial but still distant trade partner, with a very limited voice or role in intra-Western coordination. More importantly, Western Europe and the United States were more divided than they had ever been throughout the whole post-war period. The rise of détente, with the widely held notion that the Cold War was fading into the past, had considerably loosened the trans-Atlantic discipline of bipolarity. The Vietnam War had cast serious doubts on United States leadership, and Nixon's attempts at restoring it further exacerbated trans-Atlantic frictions. The European Community (EC), strengthened by the accession of the United Kingdom, was striving for a foreign policy identity of its own that entailed an explicit distancing from US guardianship. Its policy on the Middle Eastern conflict, albeit largely declaratory, put it on a collision course with Washington. In short, the solidity of the Western compact was at a historical low point (Möckli, 2015; Schulz, 2010; Sargent, 2015, pp. 101–130).

A second, related premise concerns international monetary disorder, the policy area around which Euro-American estrangement was most acute and seemingly insoluble. Trans-Atlantic concerns around monetary instability had grown in fits and spasms for quite some time, and then exploded when the Nixon administration decoupled the dollar from gold in August 1971. With the dollar sliding down and inflation inching up, the breakdown of Bretton Woods set the premises for a rising dollar price of oil (Hammes and Wills, 2005). Even more problematically, it opened up a period of convulsive, unsuccessful trans-Atlantic attempts at negotiating a new systemic solution based on fixed rates and shared rules. Europeans were either opposed to, or wary of, floating exchange rates. By and large they maintained a preference, shared also by the OECD, for capital controls and other measures to assure a negotiated governance of international finance. The United States government was far less resolute on the matter and inherently divided. However, it became increasingly prone to experimenting with floating exchange rates and an unencumbered integration of international financial markets, as advocated in particular by US secretary of the treasury George P. Shultz. By spring 1973, the impossibility to find a compromise solution gave way to a hopeful or (for many Europeans) reluctant acceptance of a market solution. In March the Bundesbank ceased to intervene in defense of a stable D-Mark rate, soon thereafter the G10 agreed to floating exchange rates, and in January 1974 the United States would abolish capital controls. In Western Europe, and particularly in France, there was considerable angst directed at the United States' decisions – or non-decisions – that appeared to negate the very notion of monetary stability, made Europe's defensive attempts at joint floating virtually impossible, and opened up to the new market-driven paradigm that would eventually come to be known as neo-liberal.

Trans-Atlantic relations were, as a consequence, colored by recriminations and adversarial mistrust. Perhaps even more relevant was the emerging belief that increasing international capital mobility defied predictability and undermined the very possibility of coordination. Divided on policy recipes, Western governments ultimately accepted the impossibility to agree on a rule-based systemic solution because they had grown convinced – with varying degrees of confidence or wariness – that financial flows had grown so large as to overwhelm states' ability to regulate them, that markets were increasingly empowered at the expense of governments (Eichengreen, 2008, p. 134; James, 1996, pp. 234–259; Sargent, 2015, pp. 118–130).

Thus, the oil embargo and price rise of late 1973 landed on an already unsettled terrain, further heightening the mystified anxiety with which Western governments – and now also public opinion at large – were contemplating the end of the long post-war boom. In the convulsive attempts at making sense of the multiple crises Western societies were suddenly facing (and at structuring some material and discursive management of their effects), the *oil shock* concept rose beyond its actual impact on trade and financial

markets to epitomize a bewildering reshaping of international power relations. More than any other single factor, it came to embody, in Western eyes, the end of the previous era of progressive optimism (Graf, 2012; Gray, 2016; Bösch and Graf, 2014). ‘We have entered the era of uncertainty’, said French president Georges Pompidou at the beginning of 1974, and he certainly reflected a widespread sentiment (Möckli, 2015, p. 249).

Crisis and responses

Western Europe’s immediate reaction to the oil crisis was dictated by its more pronounced vulnerability to import shortages, which sparked a scramble to secure oil supplies along separate, national lines. Yet, the emergency also hastened the ongoing effort at presenting the European Community as an actor with a new, heightened profile in international affairs. The *European Community Declaration on the Middle East* (November 1973) and the subsequent *Declaration on European Identity* (December 1973) embodied an attempt at maintaining a dialogue with the Arab world rather than precipitating a confrontation with it. It corresponded to the EC’s own self-perception as a *civilian power*, but it also entailed a partial, prudent distancing from the United States and a less belligerent view of North–South relations. If France was specifically pursuing ‘the Europeanization of [its] Middle East and Arab policy’ (Gfeller, 2012, p. 104; on the European Union as an international actor, see Krotz et al., 2019), its more cautious partners were far less desirous to mark a sharp divergence with the United States. However, they shared a desire for some degree of engagement with the push by Less Developed Countries (LDCs) to gain control over natural resources and develop their national economies. This attitude of vague benevolence towards the emerging demand of a New International Economic Order (NIEO) also reflected the Europeans’ residual desire to reform rather than dismantle the Bretton Wood regime (see Garavini, 2012; on the NIEO, see Gilman, 2015).

All these threads played out in a complex way in the following months, highlighting differences and divergences with the United States. Washington saw the oil exporters’ push under a much harsher light, primarily for reasons related to the geopolitical balance of the Middle East and its own conception of hegemonic dominance. Henry Kissinger prioritized a reassertion of Western power, often couched in a language of civilizational superiority. ‘It is ridiculous that the civilized world is held up by eight million savages,’ he grumbled. ‘We are now living in a never-never land ... in which tiny, poor, and weak nations can hold up for ransom some of the industrialized world.’¹ However, he was also persuaded that the NIEO challenge could not simply be rebutted. It had to be engaged with, at least rhetorically, in order to defuse it. On both fronts – OPEC and the G77 – he aimed first and foremost at uniting the West and reassert US leadership in it. ‘Our basic strategy must be to hold the industrialized powers behind us and to split the Third World’² (for recent scholarly reconstructions of Henry Kissinger’s strategy, see Dietrich, 2017, pp. 281–289; Sargent, 2015, pp. 140–361).

The oil emergency gave the United States the leverage with which it could try and rebuild its hegemony upon the West. The deeper vulnerability suffered by its allies, in Europe and elsewhere, challenged the political authority and sovereignty of their governments. It also undermined their attempts at a common response. In January 1974, the French government abandoned the European monetary ‘snake’ in order to regain some room for *maneuver* in its economic policy. The United Kingdom and Italy were also badly affected by the sudden swing in their trade balance. West Germany (FRG) enjoyed a higher degree of stability and resilience in view of its large trade surplus and huge currency reserves, but Bonn was shocked by Europe’s fragmenting crisis. Like the United Kingdom, it started to believe that a serious rapprochement with Washington was advisable (Möckli, 2015, pp. 250–252; Graf, 2014, pp. 43–69).

The United States government took the initiative, convening the Washington Energy Conference in February 1974. Its primary aim was to form a united front of the main consumer countries in order to negotiate with the oil producers from a position of strength (in Kissinger’s own lexicon, to break the ‘intolerable’ use of the ‘oil weapon’ by ‘backward people’ in order to dictate conditions to the world’s

richest societies).³ Inherent to the attempt to coalesce the West was also the goal of weakening the European Community's efforts at foreign policy coordination and reassert US hegemony over its allies. France saw through this ploy and went to the conference to insist on a different approach, based not on the consumers' front but on a multilateral dialogue between producers and consumers. But the pressure from Washington was very firm. Kissinger warned of a 'vicious cycle of competition, autarky, rivalry, and depression such as it led to the collapse of world order in the Thirties', while President Nixon hinted that disunity could have potential consequences for the US security commitment to its allies (Möckli, 2015, p. 272). With the FRG now firmly convinced that cooperation with the United States was central to any response to the oil crisis, and most other Europeans wary of a trans-Atlantic break and potential isolation, the Europeans' previous unity gave way to an acceptance of the US call for consumers' cooperation. Only France refused to sign the final communiqué establishing an energy coordinating group that would lead, in a few months, to the founding of the International Energy Agency (IEA) (Türk, 2014, pp. 209–230; Gfeller, 2012, pp. 125–130; Möckli, 2015, pp. 254–273; Beers, 2016).

The conference did not put an end to the national supply policies that Washington wanted to replace with a united, hard-nosed Western bargaining. Nor did it pave the way for truly coordinated energy policies except for the limited, technical tasks later entrusted to the IEA. In many other less tangible respects, though, it marked a turning point. First, it generalized and solidified a Western discourse of vilification of OPEC as an existential threat to the stability of the international system. Second, it constructed a 'theology' of interdependence that posited not only the need for intra-Western cooperation but in particular the necessity to wean the Global South away from a strategy of confrontation with the industrial economies, in favour of market-based solutions (Dietrich, 2016). Finally, it reset trans-Atlantic relations away from confrontation and towards consultations that would grow increasingly pivoted not so much on energy per se, but on overall monetary and financial policies.

By early 1974 it was becoming apparent that the most far-reaching, complex consequence of the oil price rise was the expansion of international capital flows. In the new monetary context in which everyone was just starting to grasp all the implications of floating exchange rates, the management of the so-called 'petro-dollars' took center stage. As the growing dollar surplus in the hands of oil-exporting countries went into Eurodollars and other offshore money markets, the amount of privately controlled liquidity outside publicly regulated channels expanded exponentially. Most Europeans, wary of such increased financial volatility's impact upon inflation and exchange parities, would have liked an International Monetary Fund (IMF) facility to collect deposits from oil exporters and lend to importing countries, or an OECD solidarity fund to channel capital to its weakest members. The United States, though, was now fully in favour of a dollar-based market mechanism. It rejected plans for official international facilities – which it feared would have entrenched OPEC international status and power – removed its own capital controls to allow private banks to accumulate and recycle international liquidity, and reached a specific, crucial agreement to that end with the Saudis. This market-oriented shift by the United States was also helped by the reluctance of most oil-exporting states to invest their growing revenues in less secure LDCs, and by the FRG's own decision to liberalize capital movements (on the assumption that an inflow of investments and a strong D-Mark would contain inflation). The burden of adjustment was shifted almost entirely on the oil-importing LDCs and, as far as the industrialized economies were concerned, on deficit countries like Italy and the United Kingdom, which were only partially supported by EC (and later IMF) credits conditional on policies of fiscal prudence (Basosi, 2016; Gray, 2016; Sargent, 2015).

Thus, the seeds were planted for some of the key transformations that would soon come to define the late 20th-century global economy. The redistributionist thrust inherent to the NIEO was side-lined, and eventually crushed, by the exponential growth of international debt in the non-oil-producing countries of the Global South, whose pursuit of sovereign rights had to give way to a stern market discipline (Dietrich, 2015, pp. 299–313). Larger, more internationalized private Western banks and financial corporations became key actors in a regulatory and legal environment that favored the mobility of

international capital investments. In the new regime of floating exchange rates, the stronger, more stable currencies became the keystone of a monetary system exerting tough pressures on the deficit countries. Consequently, the established Keynesian strategies of reflation by public spending were not only intellectually delegitimized but, perhaps even more crucially, materially undermined by a more open and fluid financial environment. ‘The recycling of petrodollars represents one of the pillars on which the modern monetary and financial system has been built’ (Altamura, 2016, p. 277; Frieden, 2006, pp. 366–370; Maier, 2010; Oliveiro, 2010).

The process was far from smooth, though, and eventually required new instruments of intra-Western coordination. The initial recycling of petrodollars did not mitigate the inflationary effects of the oil price rise; public spending programs could not thwart the severe recession that hit most Western countries in 1974/5; and the costs inherent in attempts to defend parities – including the risk of capital flight – were now too high. In the midst of the first serious post-war recession, with the danger of a protectionist fragmentation suddenly looming high, the West seemed gripped by ‘a crisis in ideas and intellectual authority’ (Rodgers, 2011, p. 49). As Western statesmen seriously discussed the danger of ‘the moral and political disintegration of the West’, the emerging concept of interdependence acquired a new relevance and a more urgent meaning⁴ (on the shift to ‘management of interdependence’ by the US administration, see Sargent (2015, pp. 167–190); on concepts of interdependence in the social sciences, see Cooper (1968) and Keohane and Nye (1977).

Interdependence and coordination: the G7

In 1974, as the recession set in, new leaders who shared a propensity for closer intra-Western cooperation came to power. French president Valéry Giscard d’Estaing and German chancellor Helmut Schmidt conceived of European consolidation only in conjunction with strong trans-Atlantic cooperation. They were also convinced that both processes required a direct dialogue among the top leaders. British prime minister Harold Wilson and US president Gerald Ford were no less keen on Western coordination at the highest level. With the deepening of the crisis, and unemployment rising, the main tensions that had set the United States and France at loggerheads began to be toned down, with a de facto acceptance of floating currencies by Paris. The prospect of top-level, ‘highly personalized financial diplomacy’ (James, 1996, p. 264) acquired momentum. Schmidt considered the crisis ‘la plus grave depuis 1929’, requiring ‘une action commune des grandes puissances industrielles’, Giscard bemoaned ‘l’absence total de concertation’⁵ and Ford saw the need to accept some coordination in order to project the image of a united West capable, under US leadership, of tackling its predicaments. Thus, a French proposal for a summit to be held at Rambouillet on 15–17 November 1975 rapidly gathered consensus.

The meeting saw the heads of the four most powerful Western governments (now joined also by Italy and Japan) putting up a very public show of unity and confidence as the key tool of crisis management. Behind closed doors, their debate focused on economic policy options, with a stalemate between advocates of fiscal austerity and reflation, and on relations with OPEC and the NIEO front. Kissinger once again called for ‘cohesion among the oil importers’ to put pressure on OPEC, while France and Italy argued for a softer approach. Schmidt, however, made clear that Western unity was predicated upon its confrontation with the Global South, as he stressed the need to ‘find a way to break up the unholy alliance between the LDCs and OPEC’.⁶ The summit did not reach any significant operational agreement, but its true significance was symbolical and cultural. It signaled that the West was not going to fragment in protectionist acrimony, nor yield to external pressure. Its key purpose was, as Gerald Ford put it, to ‘ensure that the current world economic situation is not seen as a crisis in the democratic or capitalist system’⁷ (Romero, 2014).

The following year at Puerto Rico, with Canada also joining in, the modern G7 was born around the mantra of ‘the interdependence of our destinies’ (Declaration of the International Conference, 28 June

1976, in Hajnal, 1989, pp. 15–20). As the crisis was easing, energy appeared less central a topic. However, Kissinger repeated that as the ‘engine of the world economy’ the industrialized countries ought to impress upon the LDCs that ‘they have no other place to go’.⁸ The meeting focused on inflation, with the United States and Germany pushing an agenda of fiscal restraint. The deficit countries were the direct target of the emerging consensus on austerity nurtured by the expanding international capital flows. In a few months, Italy and the United Kingdom had to accept IMF conditional loans predicated on anti-inflationary measures, a pivotal moment in the intellectual and operational shift away from the Keynesian priority for employment. In tune with the increasingly influential Washington neo-liberals, it was once again Helmut Schmidt who spelled out the ascending paradigm: ‘the root of all current evils [is] the failure to get a grip on inflation; in these circumstances traditional Keynesian economics [are] irrelevant’⁹ (Burk and Cairncross, 1992).

In the next two years, the G7 process revolved around attempts at coordinating fiscal restraint in the deficit countries with stimulus policies in the surplus ones, with limited success. In London in 1977 the leaders appeared concerned that the power of OPEC, while temporarily checked, was still such that oil prices had not dwindled. Giscard suggested an articulated strategy aimed at courting the moderate governments, like the Saudis, and isolating the radical ones, with a trade-off between a commodity agreement targeted at the poorest among the LDCs and an assurance of stable oil prices and protection for Western investments. The meeting, though, revolved on the new Carter administration’s plea for Germany to reflate in order to sustain growth.¹⁰ No concrete results were achieved, but the issue did not die. Growing US oil imports and a declining dollar actually renewed trans-Atlantic tensions in early 1978. Schmidt and Giscard accused the Carter administration of exporting inflation, and they promoted a European Monetary System (EMS) to shelter the EC economies from excessive volatility (Mourlon-Druol, 2012).

Increasing global capital flows were the key rationale for the G7 existence, but they were also exacerbating its tensions and hampering cooperation. Wary of further disruption, the OECD advanced the notion of the ‘convoy’ to emphasize a shared responsibility for growth. UK prime minister Callaghan suggested a package deal: Germany and Japan would reflate, the United States would commit to limit oil imports and contain inflation, while the deficit countries would stick to their anti-inflationary posture and further liberalize trade.¹¹ This became the basis for an agreement at the G7 meeting of July 1978 in Bonn. Schmidt symptomatically presented it not so much as a deal for growth but rather as a measure for monetary stability and payments’ balance. Once again, the focus was on the stabilization of Western economies, with no opening to the LDCs’ demands.¹²

It was the first and – more importantly – the last instance of (partially effective) international coordination still based on Keynesian notions of demand management. By early 1979, with anti-inflationary tightening in the United States and a new, sharp oil price rise as a consequence of the Iranian revolution, inflation returned to being an anxious concern. The largest states focused on conditions for domestic stability, coordination took a backseat, and recriminations on oil imports burst out (Japan and the Europeans had reduced them since 1973, while the United States – now plagued by lines at the gas stations – had actually increased them).

Thus, the 1979 G7 in Tokyo focused on energy, but it also witnessed the funeral of Keynesianism. The meeting tabled strong criticism against OPEC and agreed to set country-specific ceilings to oil imports together with goals for the development of alternative sources of energy, in what appeared as the first concerted response to the oil crisis (Chakarova, 2013, pp. 75–91). The discussion, though, revolved around the emerging paradigm of productive efficiency, flexibility and mobility, with the newly elected British prime minister leading the charge. Margaret Thatcher stressed the need ‘to revise all our previous ideas about growth’. ‘People have come to expect living standards to rise,’ she said, and as a consequence, ‘difficulties stemmed from the emphasis on Keynesian policies.’ It was time to abandon the practice of ‘deficit financing and printing money’. Giscard warned instead against a deflationary spiral, and Giulio Andreotti joined him with a plea for a ‘coordinated policy to reduce unemployment’. Schmidt, however, ‘concurred

with the [British] Prime Minister' against 'the temptation to increase nominal incomes to compensate for higher oil prices The last 5 years have shown the futility of this.'¹³ The final declaration stressed the need to 'improve long-term productive efficiency and flexibility' by reducing regulations and public spending, while stimulating labor and capital mobility. Unemployment went simply unmentioned. A few months later, the US Federal Reserve's turn to a high interest rates strategy to crush inflation sanctioned the turn to a new regime of tight money-supply focused on anti-inflationary fiscal discipline.¹⁴

As the US economy led the downward slide into recession, the G7 started to be riven also by foreign policy issues. The *European Community Declaration on Palestinian self-determination* (June 1980) resurrected the Euro-American dispute on the Middle East (Möckli and Mauer, 2010), fueled also by divergences on sanctions to Iran, and their tensions extended to the maintenance of détente in view of the Soviet invasion of Afghanistan and the Polish crisis. These disputes, though, did not hamper the joint refocusing on the anti-inflationary squeeze.

The 22–23 June 1980 G7 Summit in Venice was symptomatically preceded by a meeting of business and financial leaders who urged Western governments to free capital movements, reduce indexations and regulations, and continue to fight inflation, 'a disintegrating force throughout the world economy'.¹⁵ In Venice, the discussion focused once again on the reduction of inflation, defined in the final communiqué as 'our immediate top priority' to be pursued by 'determined fiscal and monetary restraint'. In what appears as a manifesto of the emerging neo-liberal paradigm, the declaration went on to advocate the 'shifting [of] resources from government spending to the private sector', and it praised 'the international capital market' as the primary tool for 'rechannelling the substantial oil surplus funds' (Hajnal, 1989, pp. 80–90).

The closed-door debate among the heads of government made clear that relations with OPEC and the LDCs remained paramount. The recent Brandt Report on North–South relations was briefly mentioned and rapidly shelved, since no one would contemplate the expansion of aid, on grounds of free market attitudes no less than fiscal austerity. President Carter urged a public criticism of OPEC and was joined by several leaders, on different but converging grounds. Giscard emphasized the need to convince public opinion that the Western nations could, by means of a concerted action, 'break the link between oil imports and growth'. He was joined by Japanese prime minister Okita in blasting OPEC for the limited aid it provided to the LDCs. Thatcher went further, seeing OPEC as the source of a 'fundamental shift in the structure of power' for which its moderate members (as opposed to the 'hawks') had to assume responsibility, by funding the LDCs and helping the West to stabilize the world economy.¹⁶ For Helmut Schmidt, oil prices were the key source of recessionary pressures, and had to be contained by 'a cartel of oil consumers and gas importers', although he feared that it might be too late for that. As for 'the people who are asking for a NIEO', they 'had no idea what they meant by that', and he bemoaned the West for not having had a strong 'concept to suggest in its place'.¹⁷

Conclusion

Today, historians largely concur in seeing the 1970s transition as the 'origine de notre modernité' (Chassaingne, 2008; Wirsching, 2011; Ferguson, 2010). The complex relationship between OPEC and the Western industrialized countries, against the background of the G77 claim for a New International Economic Order, was one of the key factors – in many ways the pre-eminent one – that drove late 20th-century globalization. The latter cannot really be reconstructed, much less understood, if we ignore this key triangle of shifting power relations and changing financial flows.

In the first place, the new, expanding flows of international capital strengthened the paradigmatic shift to a market-based monetary and financial system in decisive ways. The demise of Keynesian management was engineered by many factors – economic, socio-political and intellectual in nature. Among them, the recycling of 'petrodollars' in the Western financial system had a key role because it 'financed U.S. current

account deficits, stimulated the global circulation of capital, and guaranteed the continued pre-eminence of the U.S. dollar as the world's reserve currency' (Priest, 2012, p. 244; Ogle, 2014).

Second, the reshaping of international power relations that the West feared as a result of OPEC action was conflated with the G77 challenge and overblown into an existential threat. A threat – it was claimed – not only to Western international dominance, but to the very stability, cohesion, legitimacy and security of Western democracies, now beset by anxieties about the end of the age of (their) affluence (Rüdiger, 2010). This expansive perception (and public hyping) of connected threats originating in the Global South drove Western statesmen to embrace a double notion of interdependence. At an outer level it spelled the interconnectedness of an increasingly global economy that conveyed not only opportunities but palpable dangers as well. At an inner level, the need for intra-Western concertation was seen as a key tool to manage interdependence, and particularly to minimize its adverse consequences. The NIEO and especially OPEC were thus seen as inimical, demanding actors, and simultaneously constructed as bogeymen whose threat – epitomized by inflation – required new levels of Western coordination and unity around the emerging free-market paradigm. This 'us vs. them' binary simplified the real loss of control that most nation-states were experiencing. It abetted a reunification of the West around new governance practices and institutions. It helped to conceptualize and elevate inflation to an externally induced phenomenon that necessitated radically different responses, to be found in neo-liberal, free-market recipes.

The G7 was not so much the direct engine of these transformations as the crossroads where they intersected and got sorted out, the traffic junction that selected and rerouted policy recipes. It was also the symbolic locus of a refashioned West whose unity rested on a new degree of European actorness *and* a re-engineered United States leadership. Its relevance and effectiveness, therefore, should be gauged not so much by its operational efficacy – which was scarce – but by its figurative role as an emblem of Western coordination under a new economic paradigm (Bonhomme, 2012; Putnam and Bayne, 1987; Ludlow, 2013). In terms of pure energy policy, the IEA efforts at promoting conservation and diversification were no doubt far more effective. Yet, the G7 epitomized and publicized the ascendancy of market prescriptions to cope with expanding world trade and financial flows and perpetuate Western pre-eminence, albeit in a refashioned manner.

Without the new, far more active role played by OPEC in the 1970s, and without the redistributionist prospect promoted by the NIEO, none of these transformations could be envisioned. At the end of the day they had deeply disruptive consequences for most of the 'Third World' nations, whose economies became mired in debt and were subsequently forced to make painful adjustments. In the process, the post-colonial assertion of sovereign rights was dealt a terrible blow, further magnified by the global ascendance of individualized notions of human rights and capital 'freedom'. Whether and how those transformations satisfied, qualified or denied OPEC's own expectations are questions that other analysts in this volume are far better placed to answer. What becomes crystal clear when examining the West's own perspective, though, is that way before it acquired its current name, the Global South exercised an indirect but very influential agency in reshaping the global economic system and the West's own system of governance. Not always to its own advantage, though.

Notes

- 1 *Foreign Relations of the United States (1969–1976)*, volume XXXVI, document 251. 'Memorandum of Conversation' (Washington, November 29, 1973); *FRUS (1969–1976)*, volume XXXV, document 29. 'Minutes of the Secretary of State's Staff Meeting' (Washington, January 7, 1974).
- 2 *Foreign Relations of the United States (1969–1976)*, volume XXXI, document 295. 'Memorandum from the President's Special Assistant (Rostow) to President Johnson' (Washington, 27 June 1967).
- 3 *The National Archives of the United Kingdom*. CAC 164/1255. 'Record of conversation between Hunt and Kissinger, Washington 30 January 1974'.

- 4 *Foreign Relations of the United States* (1969–1976), volume XXXVII, document 24. ‘Memorandum of Conversation’ (Martinique, 15 December 1974).
- 5 *Archives Nationales, site de Fontainebleau*. CAC 19900568 art. 398. ‘Compte-Rendu du Conseil Europeen de Bruxelles’, 16–17 July 1975.
- 6 *The National Archives of the United Kingdom*. PREM 16/838. ‘Notes of the Third Session of the Heads of Government Conference at Rambouillet, 16 November 1975’.
- 7 *Foreign Relations of the United States* (1973–1976), volume XXXI, document 122. ‘Memorandum of Conversation’ (Rambouillet, 15 November 1975).
- 8 *Foreign Relations of the United States* (1969–1976), volume XXXI, document 144. ‘Economic Summit at Puerto Rico, Memorandum of Conversation’ (Washington, 14 June 1976).
- 9 *The National Archives of the United Kingdom*. PREM 16/851. ‘Record of a Meeting of the European Council held at Binnenhof, The Hague on Monday 29 November 1976 at 15:00’.
- 10 *The National Archives of the United Kingdom*. PREM 16/1223. ‘Note of the Third Session of the Downing Street Summit Conference at 10 Downing Street on Sunday, 8 May 1977 at 10.45’.
- 11 *The National Archives of the United Kingdom*. PREM 16/1656. ‘Draft message to President Carter, no date but 12 or 13 March 1978’.
- 12 *The National Archives of the United Kingdom*. PREM 16/1618. ‘Bonn Economic Summit, 16/17 July 1978: Record of First Plenary Session on Sunday 16’.
- 13 *The National Archives of the United Kingdom*. PREM 19/0028. ‘Record of the economic Summit Meeting Held in Tokio on 28/29 June, First Session’.
- 14 *The National Archives of the United Kingdom*. PREM 19/0028. ‘Declaration: Tokyo Summit Conference’.
- 15 *The National Archives of the United Kingdom*. PREM 19/188. ‘Informal pre-summit Meeting in London, 26–27 March 1980’.
- 16 *The National Archives of the United Kingdom*. PREM 19/189. ‘Record of the First Session of the Venice Economic Summit, Sunday 22 June 1980’.
- 17 *The National Archives of the United Kingdom*. PREM 19/189. ‘Third Session of Economic Summit on 23 June 1980 at 10:00 hours’.

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The US response to OPEC

Victor McFarland

As the world's leading oil consumer, the United States has played a central role in the international response to the Organization of Petroleum Exporting Countries (OPEC). During OPEC's first decade, US leaders paid little attention to the new organization. They did not see it as major threat, and in some cases they hoped that it might even serve American interests. Starting in the early 1970s, however, US attitudes toward OPEC hardened. Americans blamed OPEC for raising oil prices and destabilizing the global economy. The US government tried various strategies for dealing with OPEC, including energy conservation, alliances with other oil consumers, and building ties with key OPEC members like Saudi Arabia. With the decline of oil prices after 1980, US fears of OPEC receded. They never disappeared completely, however, and they have continued to influence US energy politics and foreign policy into the 21st century.

Oil nationalism and the origins of OPEC

When OPEC was founded in September 1960, the international oil industry was dominated by a handful of giant Anglo-American corporations known as the 'Seven Sisters' that included the predecessors of today's ExxonMobil, Chevron, BP, and Shell. The Seven Sisters were vertically integrated, with operations extending from crude oil production to transportation, refining, and retailing. They coordinated their policies with each other to limit competition and prop up prices, prompting their critics to accuse them of illegal collusion (Sampson, 1976; Blair, 1976; McFarland and Colgan, 2018). The Seven Sisters faced many rivals, including nationalists in the oil-producing countries who sought to take more control over their own natural resources. Foreign oil interests were nationalized in Russia after the Bolshevik Revolution, in Bolivia and Mexico in the 1930s, and in Iran in 1951 (White, 1992; Spencer, 1996; Brown, 1992; Santiago, 2006).

The companies relied on their home governments – especially Britain and the United States – to help protect their investments abroad. The most notable example came after Iranian prime minister Mohammed Mossadegh nationalized the Iranian oil industry in 1951. The Seven Sisters responded with a boycott of Iranian oil, which weakened the Iranian economy and undermined Mossadegh's political position. Spare production capacity in the United States, as well as in Saudi Arabia, Kuwait, and other Middle Eastern countries, let the Seven Sisters temporarily replace the lost oil from Iran. Mossadegh was then removed in a military coup supported by the US and British intelligence services in 1953 (Abrahamian, 2013;

Gasiorowski and Byrne, 2004; Rahnama, 2014). The companies demonstrated their power again at the end of the 1950s when they imposed a series of price cuts despite active opposition from the producers.

OPEC was organized to strengthen the oil producers' bargaining position against the companies and their parent governments. By coordinating their oil policies, OPEC's founders hoped to prevent the Seven Sisters from dividing the producers and playing them against each other. The companies were alarmed. The chairman of Standard Oil of New Jersey (today's Exxon) privately told US State Department officials in 1960 that OPEC's founding left him 'greatly concerned about the implications for the oil industry and the security position of the West'. He worried about the loss of corporate control over oil policy, 'since the governments would take over the determination of oil prices, the amounts of oil to be produced, and the destination of oil shipments'. One State Department official reported: 'The companies are scared of OPEC because they don't think the people running it have a sufficient understanding of the economies of oil. They are frightened that the OPEC Governments will put international prorationing into effect'. The Seven Sisters were not, on principle, opposed to international prorationing (coordinated production quotas). It was essentially what they were already doing themselves, holding large volumes of oil off the market to prop up prices. The companies feared not prorationing itself but their loss of control over the process.^{1 2}

Compared with the companies, US government officials were less concerned about OPEC. They doubted that the new organization would be able to impose production limits on its members, given each country's incentive to maximize its own production at the expense of its rivals. One State Department report concluded that an OPEC-administered prorationing system 'seems almost impossible to realize'. When President Dwight D. Eisenhower was informed about OPEC's founding, he remarked dismissively: 'Anyone could break up the Organization by offering five cents more per barrel for the oil of one of the countries.' This confidence was bolstered by a persistent surplus of oil on the market, as global oil production (especially in the Middle East) grew rapidly during the 1950s and 1960s. The companies did not believe that shortages were likely in the near future, regardless of OPEC's actions. Standard Oil of New Jersey executives told the State Department in 1960 that they expected 'a large surplus crude oil producing capacity for quite a number of years'.^{3 4 5}

Some US officials even hoped that OPEC might serve American interests. At the time, the United States was worried about the entry of Soviet oil onto the world market, which raised concerns about European economic dependence on the USSR. Soviet exports also threatened the American oil industry by driving prices down, necessitating controversial import quotas to keep foreign oil out of the American market. Eisenhower's undersecretary of state Douglas Dillon suggested that OPEC could help restrain Soviet oil price cuts, since the Soviets might be 'responsive to protests from underdeveloped countries'. OPEC could also serve as an alternative to more radical plans offered by Arab nationalists and leftists in the Middle East. In 1966, Howard Cottam, the US ambassador to Kuwait, argued that OPEC moderated the demands of the oil producers, since within OPEC, 'the producing countries have to reduce their collective objectives to the lowest common denominator'. In fact, Cottam claimed, 'if there were no OPEC, perhaps the companies would have to create one'.^{6 7 8}

In any event, American policymakers believed that it would be difficult to oppose OPEC. In 1960, the State Department's top Near East policy officer argued that because the United States practiced prorationing at home (most significantly, by the Texas Railroad Commission, or TRC, which had been setting production limits since the 1930s), Washington could hardly condemn OPEC for trying something similar on an international scale. OPEC was also part of a broader shift in control over oil toward the producer governments, which many US officials believed the United States could do little to stop over the long run. A joint report by the US intelligence community concluded that major changes in the present concessionary model were likely, since the belief that 'the national sovereignty and national interests of the contracting states should override the legal rights and commercial interests of the private companies' was widespread in the Middle East. Companies might need to share more profits with their host governments,

allow more government participation in management of the oil industry, and eventually, perhaps even accept a role in which they 'act at most only as agents of the producing countries'. Such an arrangement would disrupt the world oil market and be a blow to Western prestige, but the intelligence agencies concluded that it could still assure 'the supply of sufficient oil for Western Europe and of sufficient revenue for the Middle East', while improving Western relations with Middle Eastern countries by separating the oil companies (widely disliked in the region) from their home governments in the United States and Western Europe.^{9 10 11}

US officials remained relatively unconcerned about OPEC through the late 1960s. During that period, OPEC's members secured more revenue through a variety of changes to their tax codes and treatment of royalty expensing in the 1960s¹². American policymakers expected that trend to continue as the oil companies came under increasing pressure to share more control and revenue with the producer governments. The US government did not, however, expect OPEC to implement an effective prorationing system, cut oil production, or act collectively against the oil consumers. As the CIA noted in 1969, OPEC members 'have cooperated to improve their own share in oil income, but they have shown little ability to agree on more controversial subjects'.¹³

The oil crisis of the 1970s

American attitudes toward OPEC changed dramatically as the global oil market was transformed during the 1970s. During that decade, producer governments gained more control over the industry, while fears of shortages and a series of huge price increases magnified the apparent threat posed by OPEC. The crisis was preceded by a major shift in global patterns of oil production. During the 1950s and 1960s, domestic American oil production had grown steadily, and the TRC maintained a substantial cushion of spare capacity that helped compensate for overseas supply disruptions like the 1951 Iranian oil nationalization, the 1956 Suez Crisis, and the 1967 Arab-Israeli war. In 1970, however, American production peaked and began to decline, and the spare capacity in Texas disappeared. Meanwhile, increases in global demand for petroleum were met mainly by new production in the Middle East, giving producers in that region more power to dictate prices.¹⁴

Political events also contributed to the beginning of the oil crisis. The closure of the Suez Canal during the 1967 Arab-Israeli war and the shutdown of TAPLINE, a key pipeline that carried Saudi oil to the Mediterranean, forced Persian Gulf oil to be carried on a much longer route around Africa to reach Europe. That put upward pressure on prices and increased demand for Libyan oil, which was easier to transport via the Mediterranean. Libya's monarchy was overthrown in 1969, and the revolutionary regime that replaced it was determined to secure more revenue from the oil industry. Production in Libya was dispersed among many companies, including smaller, independent firms that, unlike the Seven Sisters, could not easily replace their Libyan oil in the event of a shutdown. In 1970, the Libyan government forced the companies to significantly increase their tax payments. Other oil producers followed Libya's example, and soon the companies were under pressure to revise their concessions around the world.

After Libya's victory, US policymakers and oil company leaders agreed that the balance of power had shifted toward the producers. Some officials concluded that OPEC had become a major force in the global political economy. In December 1970, the US ambassador to Libya warned that the 'lessons now being learned by oil producing countries may cause them to assert, through OPEC, [the] economic influence which is theirs through control over oil supplies'. In the short run, he concluded, consumers might simply have to 'pay whatever producers demand'. A month later, John J. McCloy, the companies' attorney, said that the 'cartel of producing countries' was now in a 'very strong bargaining position', while a State Department official agreed that the 'producers may now have [an] effective cartel'.¹⁵ US officials feared that if the companies and the consumer governments put pressure on any one country, like Libya, the rest of OPEC could rally to its defense and curtail production to punish the consumers.

Other observers agreed that the oil producers had become more powerful, but they believed that the producers continued to act as individual countries rather than as a united cartel. A November 1970 US National Intelligence Estimate concluded that individual OPEC members had consistently been 'willing, in fact anxious, to take advantage of one another's difficulty in order to gain more total revenue by expanding output'. A year later, a State Department memorandum argued that not only was OPEC not yet a cartel, it was not even in a position to become one any time soon, since it was hindered by the stubborn divide between 'militant and moderate' OPEC members.^{16 17}

Some of this apparent disagreement stemmed from imprecision in the use of terms like 'OPEC' and 'cartel'. Did OPEC mean its member states, which were clearly becoming wealthier and more influential, or the organization itself, which had a tiny budget and no coercive power, depending entirely on voluntary cooperation by its members to enforce its decisions?¹⁸ And was a cartel an agreement to limit production according to a formal prorationing system (a condition that OPEC did not meet) or simply a group of producers who consulted with each other and sought to raise prices? Oil policy specialists tended to be more precise with their terminology, while higher-level policymakers, politicians, and the general public used looser definitions – often creating the impression that different parts of the US government were talking past one another.

The US government struggled to organize a coherent response to OPEC at the beginning of the 1970s. Few US foreign policy officials were very knowledgeable about the oil industry; expertise in the subject was concentrated in other branches of the government, like the Department of the Interior.¹⁹ The US government had long been accustomed to leaving the details of oil negotiations to the companies, and oil prices had been so stable for the previous quarter-century that US policymakers failed to appreciate the danger of major price increases. In any case, the price increases of 1970/1 were relatively small and did not have a major impact on the United States, which imported relatively little oil and already tolerated domestic prices that were higher than the world average. During that period, US officials prioritized security of supply over price, urging the companies to concede larger payments to the producers rather than risk outright nationalization or a halt to exports that would endanger the world economy.²⁰

Company and government officials could not initially agree on their stance toward OPEC. The companies thought OPEC might be an asset instead of a threat, since were concerned about the 'leapfrogging' process in which individual oil producers tried to outdo one another in raising prices. They hoped that OPEC might help them stop the spiraling escalation of producer demands, as OPEC moderates like Saudi Arabia would restrain radicals like Libya and settle on a more reasonable common bargaining position. At the beginning of 1971 the companies formed a united negotiating front and signaled that they would only negotiate with OPEC as a whole.²¹ The State Department disagreed, encouraging the companies to negotiate separately with producers in the Mediterranean and the Persian Gulf. With US government approval, the companies signed the Tehran and Tripoli agreements of 1971 with the Gulf and Mediterranean producers, respectively. The agreements brought some temporary stability but did not stop the upward pressure on prices. The US government also encouraged the companies to compromise with the OPEC states on the question of 'participation', in which the producer governments took a partial ownership stake in the companies' local operations.

By 1973, the US government was beginning to adopt a more adversarial stance toward OPEC. US imports were rapidly increasing and talk of an 'energy crisis' was becoming common even before the Arab embargo. In that context, OPEC's ambition to keep raising prices appeared more threatening. One official reported to National Security Advisor Henry Kissinger that the US goal should be to encourage the 'break down' of OPEC 'with competition leading towards lower world oil prices'.²² Kissinger became increasingly enamored with the idea of a consumer organization to counterbalance OPEC. In August 1973, he asked: 'If the producer countries can develop a cartel and confront the consumers, why not vice versa?'²³

OPEC and US energy policy after 1973

Between October 1973 and March 1974, the Arab oil producers imposed an embargo on the United States in response to US support for Israel. The embargo coincided with a massive increase in the price of oil from around \$3 per barrel to almost \$12 per barrel, with the new price made official at a December 1973 OPEC meeting in Tehran. In the popular American imagination, the Arab cutoff and the price increase often blurred together into an imaginary ‘OPEC embargo’.²⁴ Both the embargo and the increase in world oil prices exacerbated a variety of problems in the domestic American energy economy that had been developing for years. They included a growing natural gas shortage, financial problems in the coal and electric utility industries, and a cumbersome system of price controls (Lifset, 2014; Jacobs, 2016, pp. 24–48). The result was a temporary but highly disruptive shortage of petroleum products in the United States, long lines at gasoline stations, and a blow to the US economy that contributed to persistent ‘stagflation’ – slow economic growth and high inflation – during the 1970s.

At first, Americans tended to see the crisis as a domestic event caused by the policy failures of their own government and the greed of the oil companies, which were widely suspected of rigging prices and even concocting the embargo as cover for their activities. Consumer advocates like Ralph Nader claimed that the crisis was artificial, and a Gallup poll taken at the height of the embargo revealed that most Americans blamed the companies or the federal government rather than OPEC or the Arab producers.^{25 26} The American public was sharply divided on energy policy. The left and oil-importing states like Massachusetts wanted closer government supervision of the oil industry and tighter price controls, while conservatives and oil-exporting states like Texas criticized federal regulations and wanted to lift price controls.²⁷ In this context, redirecting public anger toward OPEC, the Arab producers, or both, was a way for US elites to call for national unity. It was particularly useful for oil companies and their political allies who wanted to shield themselves from public anger.

As a result, OPEC became the target of regular criticism by American politicians from across the political spectrum. After the embargo began, Richard Nixon announced ‘Project Independence’, a massive effort to free the United States from reliance on foreign oil involving energy conservation, more domestic production, and the increasing use of alternatives like coal. His successor Gerald Ford advocated the same goal. He also called for the politically contentious steps of deregulating domestic oil prices and imposing a fee on foreign oil imports, which would reduce US dependence but raise costs for consumers. Ford argued that in the long run, his plan would ensure that the United States retake ‘control of its energy destiny’ from OPEC and the Arab producers while ensuring that Americans ‘never again be forced to pay the cartel-manipulated, inflated prices of foreign oil’²⁸ (for more information on Ford’s energy policies, see Mieczkowski, 2005, pp. 197–271).

Ford’s Democratic critics in Congress argued that he was in fact ratifying OPEC’s power by lifting price controls and forcing American consumers to pay world prices set by the cartel. Representative Henry Gonzalez (D-TX) complained that Ford seemed reconciled to the oil cartel and was ‘far too weak in the face of a price gouging, international monopoly which is clearly harmful to American interests’.²⁹ Senator Henry ‘Scoop’ Jackson (D-WA) introduced an alternative bill strengthening price controls on oil. Jackson argued that Ford was ‘giving OPEC authority to fix the price of American oil’, while one of Jackson’s allies proudly announced that, by contrast, ‘our bill doesn’t kneel down to OPEC nations’.³⁰

Congress eventually produced a compromise bill, the Energy Policy and Conservation Act (EPCA) of 1975. It included conservation measures like new fuel economy standards for automobiles, along with a plan for the gradual decontrol of oil prices, but in the short term it strengthened price controls even further. Conservatives denounced the bill, arguing that it would increase US reliance on imported oil. The American Petroleum Institute (API), which represented the oil industry, wrote that high energy prices were only a symptom of the real problem, ‘the market power of OPEC’. US energy policy measures, the API argued, ‘must be judged by their effect on OPEC’, and by that measure, the EPCA failed.³¹ In a

meeting with the president, one Republican congressman scathingly mocked the EPCA as ‘the OPEC subsidy bill of 1975’.³² Ultimately, Ford decided to sign the bill, but he was sharply criticized by conservatives for doing so.

The foreign policy response to OPEC

In the long run, the US government hoped to limit American demand for imported oil through conservation measures, increased domestic production of fossil fuels, and the development of alternative energy sources. In the short run, though, US officials believed that the United States needed to challenge OPEC’s price increases. In June 1974, the CIA warned that the previous year’s price hikes had caused ‘sharply higher rates of inflation’ and ‘a slump in industrial output’ for the United States, Western Europe, and Japan. Policymakers believed that further price increases would pose a serious economic threat to the United States and its allies. The United States also feared that OPEC could become a model for other commodity cartels associated with the ‘New International Economic Order’ (NIEO), a set of proposals by developing countries at the United Nations that sought to raise commodity prices and revise the terms of trade between the industrialized world and the Global South. Henry Kissinger (now secretary of state) described the NIEO as ‘a super OPEC’ and argued that the West needed to separate the non-oil developing countries from the oil producers ‘and prevent a lot of other “pecs”’.^{33 34 35}

Some US policymakers still insisted that OPEC was not as dangerous as it appeared. CIA and National Security Council (NSC) officials argued that while OPEC was often described as a cartel, it had not proven that it could act like one since it had never successfully cut production to raise prices. At most, OPEC had taken advantage of production cuts that had been made for other reasons, like the Arab embargo. The State Department predicted that with the end of the embargo, ‘a mounting surplus production capacity – unsold oil’ could ‘compel OPEC states to compete amongst themselves’. Because OPEC members had ‘different circumstances and needs, the resultant divisions will bring their house down’. In 1975 Secretary of the Treasury William Simon told Kissinger: ‘I’m personally convinced, though I don’t go around saying this, that prices will come down soon, if we just let the market work’.³⁶ Simon argued that the United States could accelerate the process by convincing Saudi Arabia to auction off a substantial quantity of oil, which he hoped would demonstrate that the natural market price was below the artificial OPEC price.^{37 38 39 40 41}

Kissinger, though, argued that OPEC was a dangerous adversary that could only be stopped by being confronted politically. He told Gerald Ford: ‘We have to find a way to break the cartel.’ Kissinger’s anti-OPEC strategy consisted of two main parts. The first was to organize a consumers’ alliance against the oil producers. It was necessary, Kissinger explained, to show ‘what the West can do when it wants to get together and how it cannot be pushed around’. Such an alliance would improve the consumers’ bargaining position by presenting a united front against OPEC. It would also stop the producers from extracting political concessions and dividing the United States from its allies. During the 1973 war, some European countries had distanced themselves from the United States and refused to support the US airlift to Israel, a rift that Kissinger blamed partly on pressure from the Arab oil producers. Hoping to avoid similar problems in the future, Kissinger supported the creation of the International Energy Agency (IEA) in 1974 and the ‘Group of Six’ industrialized nations (later the G7 and G8, as other members were added), which first met in 1975.^{42 43 44}

The second part of Kissinger’s strategy was to divide OPEC’s members from each other and from their allies in the developing world. The United States emphasized the damage that high oil prices were doing to non-OPEC developing countries and sought to convince them that their interests lay with their fellow oil consumers and not with OPEC and the NIEO. The US government cultivated closer ties with certain OPEC members, selling them arms and encouraging their economic integration with the United States. US officials believed that Saudi Arabia was the most important member of OPEC since its small

population, limited revenue needs, and huge oil reserves gave the kingdom more freedom than other exporters to adjust production levels up or down. As NSC official Robert Hormats wrote in 1975: 'No international agreement on oil pricing or on use of OPEC reserves can have any meaning without Saudi support.'⁴⁵ The United States urged Saudi Arabia to keep prices down, regularly lobbying the Saudi government before every OPEC meeting. Kissinger also sought a special oil deal with Iran, which he argued would mean 'a first major break in OPEC solidarity' and 'almost kill a price increase—maybe even crack OPEC'.^{46 47}

Although the deal with Iran was never completed, US officials believed that Saudi Arabia tried to limit OPEC price increases. The Ford administration was particularly pleased after the 1976 OPEC meeting in Doha produced a split in the organization, with Saudi Arabia selling oil for a lower price than most other OPEC members. The US government believed the Doha outcome proved the wisdom of relying on Saudi Arabia to keep oil prices down. A State Department official told Kissinger that 'our intensive diplomatic efforts prior to the Doha meeting favorably influenced the final OPEC price decision', while Ford thanked King Khalid of Saudi Arabia for his kingdom's 'demonstration of responsible leadership at the OPEC Ministerial Conference'.⁴⁸

The second price shock and beyond

The Carter administration continued the general outlines of US energy policy set under Nixon and Ford. Carter sought to limit US reliance on foreign oil by reducing consumption and developing other energy sources. Like his predecessors, he was only partly successful. Carter decontrolled domestic oil prices, established the Department of Energy, and increased research and development funding for new energy technologies, but Congress blocked other important parts of his program. Continued US vulnerability to international supply shocks was demonstrated in 1978/9, when the Islamic Revolution shut down most Iranian exports and sent prices skyrocketing. As with the previous crisis in 1973–1974, gasoline lines were the most visible symptom and caused widespread public anger in the United States.

Carter and many of his advisors were convinced that the crisis was ultimately caused by a growing physical shortage of oil in the world. Shortly after taking office, Carter told the American people that both the United States and the rest of the world were 'running out of gas and oil,' and that the country had no choice but to 'balance our demand for energy with our rapidly shrinking resources'.⁴⁹ Privately, some advisors told Carter that even Saudi production capacity was smaller than previously estimated. In 1978 the CIA argued that Saudi production might reach a limit around 8.5 mb/d, far less than many observers had expected. National Security Advisor Zbigniew Brzezinski told Carter that 'the policy implications of the Agency's findings are ominous' since 'Saudi Arabia may not, in fact, have the capacity to prevent upward price movements; its influence within OPEC will decline accordingly.' The CIA predicted a dramatic round of price increases as oil demand outstripped the available supply by 1980. Brzezinski suggested with such dangers on the horizon, perhaps the United States should not seek an OPEC price freeze – instead, gradual upward adjustments of the price might be preferable.⁵⁰ In May 1979, during the second supply shock, an NSC report argued that the recent price increases could not be blamed on cartel manipulation, since 'OPEC decisions are shaped largely by judgments of what the world oil market will bear,' and in fact, 'market forces' were, 'if anything, pushing upward instead of downward on the Saudi market price'.⁵¹

US officials, however, concluded that in the short run they still needed to keep urging the OPEC nations, and particularly Saudi Arabia, to increase production and reduce prices. The Carter administration had been publicly criticizing price increases and privately lobbying Saudi Arabia since 1977. In November of that year, Secretary of State Cyrus Vance wrote that 'the highest objective of American international economic policy must be to obtain a freeze on oil prices at least through 1978'.⁵² The sharp increase in oil prices in 1978/9 reinforced the administration's fear that price increases could devastate the US economy.

In June 1979, one NSC study predicted that there could be 800,000 Americans unemployed by the next year 'as a result of 1979 OPEC actions'.⁵³ Carter's chief domestic policy advisor Stuart Eizenstat told Brzezinski that 'the economic stability and strength of this country is now dependent in good measure on OPEC oil pricing decisions' since higher OPEC prices could 'break the back of our anti-inflation program and jeopardize prospects for continued economic growth and high employment'.⁵⁴

Carter also had important political reasons for challenging OPEC price increases. Eizenstat warned Carter that the American people were blaming him for the oil crisis. He told the president that 'nothing else' besides the energy crisis 'has so frustrated, confused, angered the American people – or so targeted their distress at you personally'. As a result, Carter needed to 'mobilize the nation around a real crisis and with a clear enemy – OPEC'.⁵⁵ In Carter's notorious 'crisis of confidence' speech in July 1979, he followed Eizenstat's advice. 'Our excessive dependence on OPEC,' Carter proclaimed, 'has already taken a tremendous toll on our economy and our people,' threatening 'our economic independence and the very security of our Nation'. In a television interview he reiterated the point, stressing that a dramatic reduction in oil imports was the only way 'for us to have an independent foreign policy free of unwarranted control or influence by the OPEC nations who might try to use the oil weapon as blackmail as they did in '73 and '74'.^{56 57} In the short run, though, Carter had few good policy options. His administration continued to plead with Saudi Arabia and the rest of OPEC for lower prices while working with the other industrialized nations to set demand reduction targets. Carter expanded the US military presence in the Persian Gulf region and proclaimed the 'Carter Doctrine', promising US support for the Gulf nations against external aggression. Carter's domestic price decontrol also, over time, helped reduce US reliance on oil imports. The full impact of that adjustment, however, was not seen until well into the 1980s – too late to save Carter's presidency.

Partly because of the political toll that the energy crisis had taken on Carter, Ronald Reagan won a landslide victory in the 1980 election. He advocated deregulation, including the elimination of the last remaining price controls on domestic oil. Reagan justified that move with the usual anti-OPEC arguments, claiming that price controls had made the United States 'more energy-dependent on the OPEC nations, a development that has jeopardized our economic security and undermined price stability at home'.⁵⁸ Once prices began declining in the 1980s, conservatives declared victory. The 1984 Republican Party platform boasted that 'oil price decontrol crippled the OPEC cartel', while Reagan in 1985 suggested that the 'OPEC cartel' was 'ailing' and would remain that way as long as Americans supported his free-market energy policies.^{59 60}

Oil prices collapsed in the mid-1980s, but the specter of a powerful OPEC still haunted the US government.⁶¹ Policymakers worried that if any country besides Saudi Arabia attained a dominant role in OPEC, it could raise prices and trigger a new oil crisis. In 1986, during the Iran-Iraq War, the CIA warned that if Iran won it could gain 'a strong say in how Iraqi oil is marketed'. Such an outcome could give Iran great influence within OPEC. As a result, 'oil prices could increase sharply and quickly', which would 'clearly weaken US security interests in the region'.⁶² Over the next two years, the Reagan administration put increasing pressure on Iran, culminating in direct clashes between US and Iranian naval forces and the downing of an Iranian civilian airliner in 1988. Similar fears resurfaced at the time of the Persian Gulf War in 1990/1. In July 1990, even before Iraq's invasion of Kuwait, the CIA argued that OPEC had been reinvigorated 'with the help of Iraqi intimidation'. Even 'more ominous for Western oil consumers' was 'the prospect of continued Iraqi pressure on OPEC to raise oil prices substantially' and of the more moderate OPEC members having 'a difficult time resisting further efforts to raise oil prices' in the face of Iraqi military power. For the first time, the CIA concluded, 'OPEC now has a tacit quota-enforcement mechanism – the threat of Iraqi aggression'.⁶³ After the Iraqi conquest of Kuwait and a build-up of Iraqi forces on the Saudi border, American fears that Iraq might control much of the world's oil reserves helped convince the Bush administration to intervene in the Gulf War.

The US energy situation changed dramatically after the mid-2000s, when improved hydraulic fracturing techniques enabled huge increases in the production of oil and natural gas from shale and other low-permeability source rocks that were formerly too difficult to drill. The United States became less dependent on oil imports than at any point since the early 1970s. Even so, resentment against OPEC remained an important part of US politics. After Donald Trump took office in 2017, his administration announced that ‘President Trump is committed to achieving energy independence from the OPEC cartel.’ Trump repeatedly denounced OPEC on Twitter, declaring in 2018 that ‘oil prices are too high, OPEC is at it again’ and ‘the OPEC monopoly must get prices down now!’^{64 65}. Trump’s rhetoric is a reminder that the legacy of the 1970s continues to shape US policy. The oil crisis helped convince the United States to expand its military involvement in the Middle East, laying the groundwork for the contemporary American presence in the region. It also led to the expanded use of domestic energy sources like coal, which promised independence from foreign oil but now contribute to the greatest energy policy challenge of our own day: the fight against climate change.

Notes

- 1 *Foreign Relations of the United States (FRUS)* (1958–1960), volume IV, Foreign Economic Policy. ‘Memorandum of Conversation’, 19 October 1960, document 310.
- 2 *Foreign Relations of the United States (FRUS)* (1961–1963), volume IX, Foreign Economic Policy. ‘Summary of Minutes of Meeting of the Interdepartmental Committee of Under Secretaries on Foreign Economic Policy’ (Washington, 13 December 1961), document 345.
- 3 *Foreign Relations of the United States (FRUS)* (1958–1960), volume IV, Foreign Economic Policy. ‘Memorandum of Conversation’, 19 October 1960, document 310.
- 4 *Foreign Relations of the United States (FRUS)* (1958–1960), volume IV, Foreign Economic Policy. Memorandum of Discussion at the 460th Meeting of the National Security Council (21 September 1960), document 309.
- 5 *Foreign Relations of the United States (FRUS)* (1958–1960), volume IV, Foreign Economic Policy. ‘Memorandum from the Director of the Office of Near Eastern Affairs (Meyer) to the Assistant Secretary of State for Near Eastern and South Asian Affairs (Jones)’ (21 November 1960), document 314.
- 6 *Foreign Relations of the United States (FRUS)* (1958–1960), volume IV, Foreign Economic Policy. ‘Memorandum of Discussion at the 460th Meeting of the National Security Council’ (21 September 1960), document 309.
- 7 *Foreign Relations of the United States (FRUS)* (1964–1968), volume XXXIV, Energy Diplomacy and Global Issues. ‘Airgram From the Embassy in Kuwait to the Department of State’ (Kuwait, 14 March 1966), document 189.
- 8 Citino (2002) argues that OPEC served as an alternative to more radical Pan-Arabist visions of oil nationalization).
- 9 *Foreign Relations of the United States (FRUS)* (1958–1960), volume IV, Foreign Economic Policy. ‘Memorandum from the Director of the Office of Near Eastern Affairs (Meyer) to the Assistant Secretary of State for Near Eastern and South Asian Affairs (Jones)’ (21 November 1960), document 314.
- 10 *Foreign Relations of the United States (FRUS)* (1958–1960), volume IV, Foreign Economic Policy. ‘National Intelligence Estimate’ (13 December 1960), document 317.
- 11 Dietrich (2017) explores the history of oil nationalism during the decades surrounding OPEC’s founding in 1960.
- 12 On OPEC’s successes in the 1960s, see Jeff Colgan’s contribution to this volume.
- 13 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Memorandum Prepared in the Central Intelligence Agency’ (Washington, 8 August 1969), document 8.
- 14 For introductions to the transformation of the oil market in the 1970s, see Venn (2002), Schneider (1983) and Yergin (2008, pp. 543–680).
- 15 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Telegram from the Embassy in Libya to the Department of State’ (Tripoli, 5 December 1970), document 64.
Foreign Relations of the United States (FRUS) (1969–1976), volume XXXVI, Energy Crisis. ‘Telegram from the Department of State to Certain Diplomatic Posts’ (Washington, 8 January 1971), document 65.
Foreign Relations of the United States (FRUS) (1969–1976), volume XXXVI, Energy Crisis. ‘Telegram from the Department of State to Certain Diplomatic Posts’ (Washington, 8 January 1971), document 66.
- 16 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘National Intelligence Estimate’ (Washington, 14 November 1970), document 60.
- 17 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Memorandum from Robert Hormats of the National Security Council Staff to the President’s Assistant for National Security Affairs (Kissinger)’ (Washington, 20 October 1971), document 94.

- 18 On the weaknesses of OPEC as a formal institution, see Colgan (2014) and Epstein (1983).
- 19 The Department of the Interior *was* involved in natural resource development abroad; see Black (2018). Its primary responsibilities, however, were domestic.
- 20 On this pattern in US advice to the companies on the 1970 Libyan negotiations, see: *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis, ‘Telegram from the Department of State to the Embassy in Libya’ (Washington, 17 July 1970), document 50; see also:
Foreign Relations of the United States (FRUS) (1969–1976), volume XXXVI, Energy Crisis. ‘Action Memorandum from the Deputy Assistant Secretary of State for International Resources and Food Policy (Katz) to the Assistant Secretary of State for Economic Affairs (Trezise)’ (Washington, 28 July 1970), document 51; see also: *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Telegram from the Embassy of Libya to the Department of State’ (Tripoli, 23 September 1970), document 55; see also: *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Memorandum for the Files by the President’s Assistant for International Economic Affairs (Flanigan)’ (Washington, 29 September 1970), document 57.
- 21 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Memorandum from the President’s Assistant for National Security Affairs (Kissinger) to President Nixon’ (Washington, 18 January 1971), document 73.
- 22 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Action Memorandum of the Assistant of the State for Economic and Business Affairs (Armstrong) to the Under Secretary of State for Economic Affairs (Casey)’ (Washington, 20 April 1973), document 179.
- 23 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Memorandum of Conversation’ (Washington, 10 August 1973), document 191.
- 24 That mistake has proven remarkably persistent. For example, the 40th anniversary of the embargo in October 2013 saw a wave of news articles that sought to explain the historical legacy of the supposed “OPEC embargo.” Among others, see Koch, W. (19.10.2013). U.S. Oil Supply Looks Vulnerable 40 Years after Embargo. *USA Today*; Bryce, R. (11.10.2013). Forty Years after OPEC Embargo, U.S. Is Energy Giant. *Bloomberg View*; Strobel, W. (17.10.2013). Awash in Oil, U.S. Reshapes Mideast Role 40 years after OPEC Embargo. *Reuters*.
- 25 Gallup Poll (04.12.1973). No. 885.
- 26 *Los Angeles Times* (17.12.1973). Nader Calls Energy Crisis Phoniest Yet.
- 27 For the domestic political debate on energy policy in the 1970s, see Jacobs (2016).
- 28 Ford, G. (10.02.1975). ‘Address Before the House Chamber of Commerce Conference on Energy and the Economy’. University of California at Santa Barbara, American Presidency Project (APP). Available from: www.presidency.ucsb.edu/ws/?pid=5471
- 29 Henry Gonzalez to Arthur Burns (29.05.1974). Arthur Burns Papers Box B86. Folder: Oil, May–Dec 1974. Gerald R. Ford Presidential Library, Ann Arbor, MI.
- 30 Merna to Nipp (01.08.1975). John Marsh Files Box 15. Folder: Energy: Oil Decontrol, 8/1–6/75. Ford Library.
- 31 American Petroleum Institute (01.12.1975). Comments on the Pricing Provision of the Energy Policy and Conservation Act. Marsh Files Box 13. Folder: Energy – Energy Policy and Conservation Act: General 9/75–12/75. Ford Library.
- 32 Ford meeting with Republican members of Congress (10.12.1975). Robert Wolthuis Files Box 2. Ford Library.
- 33 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Minutes of the Rambouillet Economic Summit Meeting’ (Rambouillet, 16 November 1975), document 88.
- 34 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Paper Prepared in the Office of Economic Research, Central Intelligence Agency’ (Washington, 28 June 1974), document 356.
- 35 On the NIEO, see Ogle (2014) and Gilman and Moyn (2015).
- 36 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Memorandum From from C. Fred Bergsten of the National Security Council Staff to the President’s Assistant for National Security Affairs (Kissinger)’ (Washington, 21 January 1970), document 39.
- 37 John Bushnell to Charles Cooper (21.01.1974). NSC Subject Files Box 321, Folder 1. Richard Nixon Library, Yorba Linda, CA.
- 38 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Memorandum from Charles A. Cooper of the National Security Council Staff to Secretary of State Kissinger’ (Washington, 21 January 1974), document 286.
- 39 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Paper Prepared in the Office of Economic Research, Central Intelligence Agency’ (Washington, 5 March 1974), document 333.
- 40 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Memorandum of Conversation’ (Washington, 13 August 1974), document 1.

- 41 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Paper Prepared in the Department of State’ (Washington, undated), document 40.
- 42 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVI, Energy Crisis. ‘Memorandum of Conversation’ (Washington, 10 February 1974), document 315.
- 43 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Memorandum of Conversation’ (Washington, 17 August 1974), document 2.
- 44 For the founding of the IEA, see Scott (1994) and Türk (2014). Anti-OPEC or a Neutral Consumer Organisation? The Founding of the International Energy Agency in 1973/1974, *H-Energy*. For the early meetings of the G7, see Putnam and Bayne (1987). On Kissinger’s response to the oil crisis, see Sargent (2015), especially pp. 131–164.
- 45 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Memorandum from Robert Hormats of the National Security Council Staff to Secretary of State Kissinger’ (Washington, 4 March 1975), document 47.
- 46 Kissinger and Ford (12.06.1975). From National Security Advisor Memoranda of Conversation, Box 11. Ford Library.
- 47 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Memorandum from the President’s Assistant for National Security Affairs (Kissinger) to President Ford’ (Washington, 15 August 1975), document 77.
- 48 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Letter from President Ford to Saudi King Khalid’ (Washington, 29 December 1976), document 114.
Foreign Relations of the United States (FRUS) (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Briefing Memorandum from the Assistant Secretary of State for Economic and Business Affairs (Katz) to Secretary of State Kissinger’ (Washington, 3 January 1977), document 115.
- 49 Jimmy Carter (18.04.1977). Address to the Nation on Energy. APP.
- 50 Weekly report (27.01.1978). Zbigniew Brzezinski Papers Box 41, Folder: Weekly Reports, 10/77–1/78. Jimmy Carter Presidential Library, Atlanta, GA.
- 51 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Note From Henry Owen to the National Security Council Staff to the President’s Assistant for National Security Affairs (Brzezinski)’ (Washington, 15 May 1979), document 204.
- 52 *Foreign Relations of the United States (FRUS)* (1969–1976), volume XXXVII, Energy Crisis, 1974–1980. ‘Memorandum of Conversation’ (Washington, 16 November 1977), document 136.
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China and OPEC

From ideological support to economic cooperation

Bao Maohong

Energy is the blood in economic development, and oil is its most crucial form. In order to deal with the discrimination arising from the monopoly on sale and production of oil by international oil companies, newly independent oil-producing nations such as Iran, Iraq, Saudi Arabia, Kuwait and Venezuela coordinated to found the Organization of the Petroleum Exporting Countries (OPEC) on 14 September 1960, in an attempt to gain the initiative in the international oil market. After several oil disputes, OPEC has become an important figure playing an active role in the international oil market and international political economy. In an 11th-century Song dynasty (960–1279) text on natural philosophy¹, the first known use of the term *shiyou* (oil) appeared in China. As the largest developing country in the world, China shifted from oil-importing country (before 1963) to oil self-sufficient country with the development of the Daqing and Shengli oilfields, and to a net oil-importing one (since 2003). With its rapid economic growth, China surpassed the USA and in 2013 became the largest oil-importing country in the world. The relationship of China and OPEC is therefore an interesting field to explore. Regrettably, little research on it had been done, especially from an environmental history perspective. Using articles from the *People's Daily*, the official newspaper of the CPC Central Committee and Chinese national government, this paper will address what the relationship was, how it has changed, and why.

The ideologized relation of China and OPEC (1960–1978)

Before the reform and Open Door policy period started in 1978, China's foreign relations were highly ideologized. Before the breaking of Sino-Soviet relations in 1966, China mainly fought against colonialism and imperialism. After that, China mainly fought against imperialism and revisionism in its foreign affairs. However, from 1960 to 1978, China ideologically supported national liberation movements and economic nationalism in the Third World, even as Sino-Soviet relations and Sino-US relations changed dramatically. In this special context, China politicized and ideologized its relations with OPEC.

The period 1960–1966 was one in which China supported OPEC from the perspective of proletarian ideology. On 20 September 1960, the *People's Daily* reported the establishment of OPEC and pointed out that OPEC aimed at safeguarding the benefits of oil-producing countries by fighting against the multinational oil companies that unilaterally reduced oil prices. Hereafter, the reports and commentaries in the *People's Daily* mainly focused on the following five aspects.

First, it exposed the unjust activities that imperialist oil companies used to exploit oil-producing countries. The *People's Daily* reported that oil companies of some imperialist countries, such as the USA, UK and the Netherlands, caused the shortage of oil and high oil prices in oil-producing countries by plundering oil resources and cornering huge monopoly profits. For example, in total oil sales revenue, Iraq just got 6.7 percent while the rest was taken by wealthy countries and their oil cartels. American oil companies earned \$40,000 per Kuwaiti oil worker a year and \$21,800 per Venezuelan oil worker each year.² Among all the imperialist countries, the USA was the largest investor in oil-producing countries. Relying on its national power, American private capital entered the oil sector in Middle East countries and achieved net profit margins of 49 percent. Therefore, the USA became the largest exploiter, the main fortress of reactionary forces and the military policeman of the world. Of course, the USA also became the enemy of the people of the world.³

Second, it exposed the contradictions among imperialist oil companies. The increasingly worldwide expansion of American capital resulted in conflicts with its counterparts in the UK, Italy, France and the Netherlands. The so-called 'Seven Sisters', five of them headquartered in the US, competed severely with the rising national oil company of Italy. American oil companies robbed the oilfields in former British or French colonies while investing in the petroleum and chemical industries of the UK and France.^{4 5} The level of competition, in the name of economic cooperation or joint venture, was so high that NATO and its common market and free trade zone suffered.⁶

Third, it called on oil workers from all over the world to fight against colonialism and imperialism. Due to the evils of colonialism and imperialism described above, China, as the representative of the world proletariat, had a duty to encourage industrial workers in imperialist countries and the Third World to fight. Because the true aim of the British invasion of Kuwait was to monopolize oil profits rather than secure Britain's oil supply or the independence of the Kuwaiti people, its military adventure needed to be stopped.⁷ Because they worked 12–18 hours a day and earned just 1/7th–1/5th of an American oil worker's salary, oil workers in Arabian countries instigated massive struggles that attacked imperialist invaders directly and pushed forward the national liberation movement.⁸ The Chinese government supported these struggles against colonialism, imperialism and monopoly capital clearly and firmly.

Fourth, it supported the struggle of oil-producing countries for national sovereignty over oil resources. Between 1961 and 1962, the Iraqi national government directed three measures at foreign monopoly capital: Iraq took back unexploited oilfields from international oil companies; Iraqi investors' input made up 51 percent of the total capital of international oil companies in Iraq within six months; and benefit to Iraq was prioritized in the import and export trade while following the principle of mutual benefit. In the comments published in the *People's Daily*, Iraq's policy was appraised as a just action aimed at eliminating the remnants of colonialism, upheld state sovereignty and developed the national economy. Believing in the final failure of all imperialist schemes, China strongly supported the nationalization of oil in Iraq and was satisfied with its achievements.⁹

Fifth, it praised oil 'friendship' with the former Soviet Union and oil self-sufficiency in China. In contrast to its criticism of the monopoly capital of imperialist countries, the *People's Daily* warmly celebrated the Soviet Union's increasing oil production and export. In 1962, oil production in the Soviet Union surpassed that of Venezuela and ranked second in the world. Although the Soviet Union was behind the USA in oil production, the *People's Daily* praised the Soviet Union for shrinking the gap.¹⁰ With regard to the Soviet Union's oil exports to other communist states in Europe, the *People's Daily* gave prominence to its 'friendship' as fundamentally based on the spirit of proletarian internationalism.¹¹ In 1963, China could supply its own needs in petroleum and petroleum products. This was praised as a great achievement that changed China significantly. It meant that China was no longer a country short of petroleum. It was undoubtedly exciting for all Chinese.^{12 13}

1966 – when Sino-Soviet relations were broken and the Cultural Revolution was launched – was a key year. Paralleling these developments, China's foreign policy was further ideologized. Concretely speaking,

appraisal of the Soviet Union's oil production and petroleum diplomacy became negative; Mao Zedong thought appeared in ideological support for OPEC; and China exported oil and petroleum products to Japan and the Philippines according to its own political and diplomatic needs.

From 1971 on, OPEC as an independent organization was reported frequently in the *People's Daily*, portrayed as a key representative against the superpowers, especially after the oil shock of 1973. First, OPEC was seen as a 'united front' organization against imperialism. If the petroleum-exporting countries in Asia, Africa and Latin America could coordinate their actions, they would definitely be able to resist imperialist pressure and finally defeat these great imperialist monsters.¹⁴ The energy crisis was not seen as energy depletion but reflected fundamentally the crisis of the capitalist system and resulted from its various contradictions, such as the cruel exploitation of people at home and abroad by monopoly capital. At the same time, the energy crisis resulted directly from the crazy external expansion and scramble for hegemony of two superpower forces: American imperialism and Soviet Union revisionism.¹⁵ Third, OPEC resisted the exploitation and predation of international oil companies by coordinating its member countries' policies and allowing oil-producing countries to benefit from oil production and sale.¹⁶ The essence of the oil struggles of oil-exporting countries was to challenge the 'theory of limited sovereignty', to safeguard national independence, sovereignty and the right to subsistence, and to further its impact on the unequal international economic order.¹⁷ Fourth, it supported OPEC's struggle clearly and firmly. At the plenary meeting of the 30th UN General Assembly, the Chinese delegate criticized the accusations and threats the two superpowers directed at oil-exporting countries and supported their efforts to change the old international economic order and develop national economies through self-reliance.¹⁸ Fifth, oil as a weapon was powerful. Oil struggles aimed to not only change oil prices and the control of oil resources but also hit hard at both the economic and political hegemony of two superpowers and prompt the unity and awakening of the Third World. The oil struggle was a significant strategic action that caused international class power to change profoundly in favor of fighting against the two superpowers.¹⁹

To better understand the oil struggles of OPEC, we can use Mao Zedong's thought as a framework. In Mao's Three Worlds theory, imperialism depended on the Third World – and the superpowers were afraid of the Third World. Therefore, although oil-exporting countries were small, they could defeat the invasion of superpowers through their bravery, their willingness to fight with weapons and become masters of their own the destiny.²⁰ In Mao's world revolution theory, it was thus the new epoch for world revolution. As an integral part of the revolutionary storm in Asia, Africa and Latin America, the struggle for oil would decisively bring down the old world.²¹ Furthermore, in accordance with the observations of the Afro-Asian Journalist Association delegation, more and more Arabs, guided by Maoism, observed and analyzed what was happening around them, and realized that, armed with Maoism, they could make 'political power grow out of the barrel of a gun' and finally defeat their enemies, which included colonialism, American imperialism and Soviet Union revisionism.²²

The Soviet Union's oil activities were unrestrainedly attacked by the *People's Daily* after the breaking of Sino-Soviet relations. When Arabian oil-exporting countries placed an oil embargo on the USA and Britain, the Soviet Union seized the opportunity to export oil to Western European countries. This sale was criticized as activity that sabotaged the Arabian oil embargo and served only to further the Soviet Union's national egoism.²³ The oil exploitation and assistance agreement signed by the Soviet Union and Iran was criticized as Soviet revisionism controlling and plundering Arabian oil and intended to turn the Middle East into a Soviet colony. The so-called 'assistance' was definitely not friendship or cooperation. And finally, Soviet revisionism's collaboration with American imperialism in the Middle East would be bound to stir up a broader and more violent revolution among Arabs.²⁴ The Soviet Union's suggestion of a new oil export agency was criticized as designed to undermine relations between oil-exporting countries and further weaken OPEC. Essentially, the relationship between Soviet revisionism and OPEC was to be seen as hegemony vs. anti-hegemony, control vs. anti-control, plunder vs. anti-plunder. Therefore, the

Soviet social imperialist's suggestion was simply a negative that impelled OPEC member countries to unite more closely and further strengthen the anti-colonial struggle against imperialism and hegemony.²⁵

China exported oil to Japan and the Philippines. In order to deal with the common enemy (the Soviet Union), China improved its relations with the US. As allies of the US, Japan and the Philippines followed the US in improving their relations with China and obtained oil from China to relieve the negative impact of the 1973 oil crisis. Following a joint government statement by China and Japan, the first batch of sweet crude oil from the Daqing oilfield was shipped to Japan. This was reported as trade underpinned by the principle of equality and mutual benefit and the mutual exchange of necessary products. On 14 October 1974, the first batch of oil from China was shipped to Manila. President Marcos and his first lady attended the welcoming ceremony and praised the Chinese oil as a symbol of China's cooperation and friendship toward the Philippines.²⁶ On 14 November 1975, President Marcos personally presided over the signing ceremony of the Sino-Philippine Oil Trade Agreement, and accordingly China began to export oil to the Philippines at a discounted rate below world market prices. In contrast to how OPEC used oil as a weapon against imperialism and revisionism, China to some extent used oil as a weapon to improve its relations with neighboring capitalist countries and break through its isolation. Additionally, unlike Soviet revisionism trying to destroy OPEC's oil embargo, China just exported a small amount of oil.

Let me conclude by describing the character of this period. Without economic cooperation or oil trade, the relations of China and OPEC, from the establishment of OPEC to China's Open Door policy, was so highly ideologized in line with China's contemporary worldview that China understood and supported OPEC politically. This was modified in 1966 when Sino-Soviet relations changed dramatically. After this, China continued to criticize American imperialism but paid more attention to attacking Soviet revisionism and exported even more oil to US allies. This meant that relations between China and OPEC began to be depoliticized.

The relationship of China and OPEC in international oil trade (1978–2013)

It was in 1978 that China shifted its focus to economic construction, reform and its Open Door policy. Since 1978, China has created the 'economic miracle' characterized by its extraordinarily high-speed economic growth. In 2010, China surpassed Japan to become the second largest economy in the world. Paralleling the change in economic ranking, China depoliticized its 'OPEC narrative' and regarded OPEC as an oil trade partner. In the *People's Daily*, the literal English pronunciation of OPEC replaced the originally more meaningful translation of the term. After cooperating with OPEC to cut oil exports, China began to significantly import oil from OPEC countries while diversifying its oil supply and cooperation models. At this stage (1978–2013), relations between China and OPEC were underpinned by economic rationality rather than rigid ideology.

The frequent appearance of the term 'OPEC' in the *People's Daily* symbolized the normalization of relations between China and OPEC. During the first stage, China regarded OPEC as a weapon against imperialism from the perspective of ideology. Since the Open Door policy began in 1978, China has developed its economy by utilizing resources, investment, technology, management experience and markets (from) all over the world. In the world oil market, OPEC was just one of its trade partners. In line with this economic rationality, the *People's Daily* used the international term 'OPEC' in its reports. On 26 March 1986, Liu Kaichen and Mu Ni were first to use the English abbreviation when they reviewed the failure to reach agreement on the shift of policy from 'increase in production and share in world oil market' to 'limit output and boost prices' at the 77th special ministerial meeting of OPEC. This meant that China began to participate in the international oil market and deal with OPEC in accordance with the laws of the market.

In order to stabilize the oil price, China supported OPEC by decreasing oil exports. In early 1986, the world oil market fluctuated and became chaotic with the collapse in prices. Instead of the former

imperialist plundering vs. anti-imperialism perspective, articles in the *People's Daily* explored the oil price collapse from the perspective of supply and demand and the world economy as a whole, suggesting that a possible route to solving the problem could be stabilizing world economic development.²⁷ Although China's oil production mainly met domestic consumption, the National Chemical Import and Export Corporation decided not to increase the amount of oil export in 1986. On 21 February 1986, the *People's Daily* again published an article that argued that price collapse could result in global harm, from oil shock to financial crisis, and clearly hoped that OPEC countries and non-OPEC oil-producing countries should join together, on the basis of mutual benefit, to discuss how to keep oil prices at a reasonable level to stabilize and develop the world economy.²⁸ Since 1986, China has actually decreased the amount of oil exported every year, from 32 million tons in 1985 to 23 million tons in 1991. This shift reflected China's deepening dependence on the world market and world economy and its transformation from a closed domestic economy to an open export-oriented economy.

China contacted OPEC directly and promoted common development. On 2 April 1981, the vice premier of the State Council and director of the National Energy Board, Yu Qiuli, met the secretary general of OPEC, who was the first OPEC delegate to visit China. Yu said that China hoped to strengthen ties, increase contacts and exchange experiences with OPEC and its member countries and also promote the economic development of all parties. On 21 March 1985, Vice Premier of the State Council Gu Mu clearly stated that China supported OPEC's efforts to stabilize oil prices and emphasized that China was open to not only the developed countries but also the developing countries that would further cooperation among the developing countries within the framework of South-South Cooperation.²⁹ On 28 September 1990, the minister of foreign affairs Qian Qichen said at the 45th UN General Assembly that China affirmed and supported the efforts of OPEC from the perspective of strengthening South-South Cooperation and promoting South-North Dialogue.³⁰ In the eyes of China, economic hardship should be understood and solved in the world economy from a holistic perspective. The drop in oil prices superficially damaged the interests of oil-exporting countries, but the economic difficulties resulting from it would drag down the recovery of developed economies. Therefore, to prevent oil prices from dropping, the South and the North should cooperate to benefit the world economically and safeguard peace politically. In contrast to analyses of the role of OPEC within the framework of Three Worlds theory and world revolution, during this period its role was analyzed within the framework of Deng Xiaoping's theory and his 'peace and development are the trend of the world'. In Deng's theory, the world was divided into two parts: developed countries and developing countries. In this system, some developing countries have sought development and peace through reform and an Open Door policy rather than revolution, and tackled the unequal international order through cooperation and negotiation instead of armed struggle.

China imported oil from OPEC while diversifying its oil imports. Since the end of the 1980s, when economic development sped up and domestic oil production stabilized, China has imported petroleum and petroleum products from OPEC member countries. The amount of oil imports reached 120 million tons in 1992. Different understandings appeared in China regarding oil imports. First, China had once been proud of ending imports of 'foreign oil', so it had to come to terms with having to import such oil again. Second, as a strategic resource, importing too much oil would harm national economic security. In response to this, the *People's Daily* interviewed the general managers of the China National Petroleum Corporation and China Petrochemical Corporation to offer an official explanation: that importing oil to meet the large domestic demand was an economic endeavor based on the principle of cost-benefit accounting and the international economic cycle. So, oil imports could not be judged according to the percentage of nationalization of oil production and supply.³¹ This explanation showed how far China had moved its view of OPEC from a ideological and simple nationalist perspective to a market economy perspective. In accordance with market economy thinking, the rationale behind China's oil imports was ensuring reasonable prices and safeguarding energy security. The necessary and feasible approach lay in diversifying import sources and the ways of obtaining oil. China imported oil not only from OPEC-

member countries but also from non-OPEC oil-producing countries, especially Russia and Central Asian countries. Besides buying in the international oil market, China constructed oilfields and set up refineries in oil-producing countries. For example, China helped Sudan build a complete oil industry system and changed Sudan from an oil import country to a net oil export country. However, China's oil imports from Sudan, based on equality and mutual benefit, were definitely not similar to 'plundering resources from Africa' like the former colonialists and imperialists.^{32 33} Responding to the frequent fluctuation of prices in the international oil market, China came to form its own flexible price mechanism for petroleum and petroleum products. Since becoming a net oil-importing country in 1993, China has imported more and more oil. After becoming a member of the World Trade Organization, China reduced tariffs on crude oil and petroleum products, opened its wholesale and retail markets of refined products and allowed multinational oil companies to do business in China.³⁴ Due to China's oil prices integrating with the world market, the increasing rise of oil prices put pressure on China's economic development. Generally speaking, a rise of \$10 in oil prices maintained for a year would decrease China's GDP growth by 0.5 percent. It is difficult to argue that the rise in oil prices did not result from the lowering of production by oil suppliers³⁵ in accordance with OPEC's 'no ceiling but lower limit' policy of oil production.³⁶ This illustrates further how China, following the laws of market economy, was already relating to OPEC from the perspective of buyer.

As a developing country, China welcomed and utilized OPEC funds for international development. On 28 January 1976, thanks to the voluntary contribution of OPEC countries, the OPEC Special Fund was formally established for supporting developing countries with financial difficulties and backward agriculture overcome underdevelopment. From 1976 to 1980, OPEC gave 76 developing countries 232 loans, including some grants. By 1977, the amount of aid reached \$1.909 billion, of which \$1.405 billion was given on favorable terms to countries with less than \$400 per capita income.³⁷ China undoubtedly appreciated this OPEC fund. Additionally, OPEC donated to the International Fund for Agricultural Development (IFAD) to assist developing countries develop their agriculture. Since becoming a member country of IFAD in 1980 and until 1988, China has applied for \$13 million in concessionary loans for projects concerning grassland construction, improvement of saline/alkaline land and the development of animal husbandry, fisheries and agriculture.³⁸

In short, with the focus moving to economic construction, reform and an Open Door policy, China's understanding of OPEC changed dramatically from that of an organization fighting against colonialism and imperialism to one safeguarding the economic interests of oil-exporting countries. China's relationship with OPEC changed from the ideological, in which OPEC was regarded as anti-imperialist ally of China, to the pragmatic, in which OPEC was mainly regarded as an oil seller and China's economic partner. With the increase of oil imports, OPEC became a trade partner that China could bargain with in accordance with economic rationality and the laws of the market, a responsible organization that had an important impact on China and world economic development from the point of view of stabilizing global economic growth.

Brief conclusion

Relations between China and OPEC experienced two stages of development. Before 1978, their relationship was highly ideologized and China understood OPEC from the perspective of anti-colonialism, imperialism and revisionism. After 1978, their relations were almost completely depoliticized and OPEC became a normal trade partner for China.

The main driving forces for this change were the shift in China's dominant theory and its focus. During the Mao period, China ideologically and morally supported OPEC as a force against colonialism, imperialism and revisionism based on his theory of Three Worlds and world revolution. In Deng's era, China focused on economic development by practicing reform and an Open Door policy. In order to meet the

practical needs of economic development, China imported oil from OPEC countries and saw OPEC's policy from the viewpoint of meeting its increasing need to push forward economic development. During this time China regarded OPEC as a pragmatic economic cooperator.

What was the image of China in OPEC's eyes? Did this image change? These are the subjects that need to be studied further. Only then can the relationship between China and OPEC fully emerge. Studying this relationship will advance understanding of OPEC's past and present and the world energy order and with forecasting the future trends of the world oil market and world economy.

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The European communities and OPEC

From entangled international organizations to liberalism (1960s–1980s)

Alain Beltran and Yves Bouvier

Established in the same period, the European Economic Community (EEC, Treaty of Rome, 1957) and the Organization of Petroleum Exporting Countries (OPEC, Baghdad, 1960) were both part of the reconfiguration of regional organizations that took place during the Cold War but were motivated by radically different goals. Although it may seem like an invitation to force a comparison or draw systematic parallels between the two organizations, chronological proximity is actually deceptive here. Their purpose was indeed to coordinate an economic activity, namely oil production in the case of OPEC and the creation of a common market for the EEC, so as to carry more weight in the broader global economic order outside of the Cold War struggle. But these two bodies differed in their medium- and long-term objectives.

We will not go into a presentation of OPEC here (see e.g. Claes, 2001), but it is worth noting some key points about the European communities between the 1950s and 1980s (Dumoulin et al., 2014). The signing of the Treaty of Rome on 25 March 1957 created a European Economic Community of six countries (Federal Republic of Germany, France, Italy, Belgium, the Netherlands and Luxembourg). These countries were already associated through the European Coal and Steel Community (ECSC), created in 1951. On the same day in March 1957, a European Atomic Energy Community (Euratom) was also created. The growing importance of oil in the economy was a cause for concern among European leaders, as reflected in Louis Armand's 1955 report highlighting Europe's structural weaknesses and strategic impasses (Dumoulin et al., 1994). In this report, commissioned by the OEEC in December 1954 and published in June 1955, the French engineer and senior civil servant delivered a scathing indictment of Europe's oil and coal dependence. Stressing European States' structural weaknesses surrounding oil supply, the report mentioned nuclear energy as a possibility for the future, provided that European States pooled their investments. The Suez crisis in October 1956 finally convinced part of Europe's elites that nuclear power was a credible solution to limit dependence on oil from the Middle East. Whether it was coal in the early 1950s, oil in the middle of the decade or nuclear power in the latter half of the decade, energy was central to the European institutions created in the 1950s.

The significance of energy within European institutions can be seen from two different perspectives. Pragmatically, coal was traded within Europe and had created market solidarity (Hassan and Duncan, 1994; Maltby, 2013), and it was tempting to try to strengthen these ties through both electricity grids and the joint development of nuclear power, seen as the energy of the future. At that point, energy was the main

cement holding Europe together, giving concrete form to economic relations between states. On a political level, energy was a sector where agreements were possible without clashing head-on with industrial interests, thus making it an acceptable vector to support a project of political union, particularly with federalist designs. By contrast, the Baghdad conference that gave rise to OPEC in 1960 involved no such political unity project.

There are various ways to study the relationship between the EC (European communities) and OPEC. First, mutual economic dependence might have suggested that the two organizations would inevitably grow closer together. Second, these relations unfolded within an already very dense landscape of economic diplomacy. Finally, and this is well known, neither the EC nor OPEC were able to build a united front that stood the test of time. In our study, we look at the period from the late 1950s to the mid-1980s, from the creation of OPEC to the oil glut, focusing specifically on the history of relationships between international organizations (Saunier, 2004; Mechi et al., 2014). We show that, during this period, relations between the EC and OPEC depended more on intertwined relations between international organizations than on oil producer/consumer relations. While the chronological framework studied is deliberately broad, it must be noted that most of the documents consulted in the European archives relate to the 1973–1979 period.

Reciprocal ignorance: EC-OPEC relations entangled in the relations between international organizations, 1957–1970

There are many reasons why the EEC and OPEC did not establish direct relations from 1960, even though the economic and commercial stakes were already very real for both organizations. The European continent saw the proliferation of organizations in the energy sector. In addition to the European Coal and Steel Community, which remained even after the creation of the EEC, and the European Atomic Energy Community, it is worth mentioning the European Nuclear Energy Agency created within the OEEC in 1958, the European Petrochemical Association (1967), the International Union of Producers and Distributors of Electrical Energy (1928), and so on.

Two defining aspects of the EEC's situation were present as early as the 1960s: the absence of a global vision of energy, with instead an approach based on energy sources (coal, oil, nuclear, etc.); and the delegation of energy forecasting to the OECD. Even though energy was at the heart of the European project, neither the European Commission nor the EEC Council of Ministers took any significant initiatives in this respect. Expertise and projects developed within the specialized committees of the OEEC and then the OECD, particularly those dedicated to coal, electricity and oil (Schmelzer, 2016, p. 201). It seemed logical to entrust energy projects to an organization representing a large part of Western Europe, beyond the six countries of 'little Europe', for when the convention creating the OECD was signed in December 1960, no fewer than 18 European countries (as well as the United States and Canada) committed to cooperating in the different economic fields. The OECD was better suited to tackling the challenges of the energy sector. Issues surrounding oil, both in the context of expertise and within projects, were mainly addressed within the OECD which, since the Marshall Plan, was the most competent intergovernmental organization to coordinate investment. Launching energy projects in an international organization representing most of Western Europe, with 18 countries in December 1960 rather than the six of the European communities, made perfect sense. Many experts, such as Louis Armand, worked or had worked for both the OECD and the EEC. The delegation of energy issues to the OECD was illustrated by the presence of director generals in the commissions and committees set up by the OECD. Thus, Georges Brondel (DG II of the EEC) was a member of the OECD oil committee in 1962.¹ It was from this committee, and the High-Level Group in particular, that the first attempts were made at organizing consumer countries after the Tehran and Tripoli agreements, with notably consultation between the majors, European governments and the European Commission, from 1971 (Beers, 2016).

Also contributing to the lack of direct relations between the EEC and OPEC were the links established by oil companies with the different OPEC countries. There is little evidence to support this hypothesis, but the oil market was largely in the hands of the companies, particularly US companies, which were somewhat concerned about the emergence of nationalizations and agreed to give producer States a role in the global oil economy (New York Declaration, 16 January 1971). The European Commission was informed of the negotiations between the companies and OPEC by Angus Beckett, Chairman of the OECD Oil Committee.² In a way, consumer states, and in particular European states, had entrusted the security of their supply to these companies in their national interest.

However, issues surrounding oil were not absent from the debates, or even from the seeds of Community policies (Ranieri, 2016). The reduction of coal usage, particularly in countries like France with the ‘coal decline’ policy introduced in the early 1960s and then rolled out to ECSC countries from 1966 (Carbonnell, 2006), was justified by low-cost oil imports. However, the growth of these imports put European countries in such a state of dependence on oil that it had become a political issue for the EC. Contrary to what Timothy Mitchell argues, the centrality of oil was explained not so much by a desire to cripple trade unions (which had been engaging in compromise for several decades already) as by the prospect of cheaper energy. Oil dependence had become evident at geopolitical level with the nationalization of the Suez Canal, and in public opinion with the fuel shortage following the Franco-British military intervention.

A first decisive step was taken with the Memorandum of Understanding of 21 April 1964, which identified securing a cheap oil supply as a priority. Four years later, the publication of the ‘First Guidelines for a Community energy policy’ on 18 December 1968 once again focused on security of supply and consumer welfare. The guidelines saw competition as essential, even if some markets involved more regulation. The first measures taken in the energy sector related to the creation of 65-day oil stocks (1968), with the possibility of increasing the minimum limit to 90 days from 1975 (a number of countries had already adopted this policy).

The Communication to the Council of December 1968 was quite clear.³

Disparities between the costs of use of energy, resulting primarily from divergences between the energy policies of the individual Member States, are increasingly distorting competition in industries with high energy consumption, and penalizing certain regions of the Community when important investment decisions are to be taken. The attempts made to remedy this state of things by measures at national level are leading to a gradual disintegration of the Community’s energy economy (...). This dangerous trend can only be changed by a Community energy policy which fully integrates the energy sector into the common market. A Community energy policy is also necessary in order to counterbalance within the Community the risks arising from the great dependence of the Member States on imports and from insufficient diversification of the sources of supply.

The early 1970s saw yet another call for European solidarity when tensions first began to emerge on the oil market. The nationalization of Algerian oil, as well as OPEC decisions – with Resolution XVI.90 of June 1968, the famous Resolution XXI.120 adopted in Caracas in December 1970, and the Tehran and Tripoli agreements – were indeed perceived as establishing a new balance of power, and thus pushing for a coherent European policy. European oil companies also advocated such a policy. Speaking to ambassadors in Paris on 15 June 1971, Jean Chenevier, CEO of the Société française des pétroles British Petroleum, stressed that ‘profound solidarity de facto unites our old continent in the face of energy challenges. There is reason to believe that this community of interest will only grow stronger’ (Chenevier, 1971, p. 4). In the previous decade, oil had risen from 31.1 percent to 54.8 percent of the energy consumed by European OECD countries, but forecasts put it at nearly 70 percent by 1985. Thus, Chenevier considered that ‘real de facto solidarity therefore unites the consumer peoples of Western Europe and the peoples of the

producer countries of the Middle East and Africa.’ The interdependence created by oil relations had become central to European actors’ discourse in the decade preceding the oil crisis.

There was no pressure, strictly speaking, to explain this lack of direct relations between OPEC and the European communities. The situation stemmed far more from the existence of an already complex network of international organizations in the energy sector. Rather than establishing specific relationships with OPEC, the European Commission preferred to continue its work with the OECD and, by extension, with the United States, knowing that the majors were providing the necessary supplies.

No direct relations, no new international system: the failures of European initiatives, 1973–1979

The relationship between the EC and OPEC, embedded in a complex configuration of international organizations, was profoundly altered by the first oil crisis. The Arab-Israeli war and the rise in oil prices, given the intertwining of diplomatic and economic issues they raised, were an opportunity for the EC to establish direct relations with OPEC. But it ultimately proved impossible to break free of the relations established through the OECD and the patronage of the United States, even by politicizing the trade relationship.

In 1972, the Commission was aware that security of supply was more fragile for the Six, which soon became the Nine. Securing oil supplies required a long-term policy and, above all, stronger, more authoritative official bodies. In parallel, the Community also took environmental measures, promoting a more reasoned use of energy and seeking to improve relations and cooperation with energy exporting countries. A total of 46 actions were to lay the foundations for future energy policy (May 1973 resolution). In June 1973, Fernand Spaak – who was director general for energy and in particular Euratom – (Spaak, 1973) attempted to define what a European Community energy policy could look like. He noted that the division of responsibilities between the ECSC, Euratom and various other European bodies did not make the task any easier, that the different countries’ energy organizations often varied widely, and that the energy market had changed considerably since the late 1950s. While reasserting that energy should be prioritized in the European communities’ internal and external equilibrium, Spaak argued that, given the political deadlock, a political solution was first needed at European level before Europe could assert itself as an international actor. But this long-term structural strategy did not get a chance to be implemented.

Sectoral aid for oil (N3/71) appeared in the early 1970s. The 18 May 1972 rules on reporting information on oil imports and investment programmes (oil, gas and electricity) to the Commission demonstrated new concern about energy. Also in 1972, several important measures were taken, including a measure providing for the coordination of Community resources in the event of oil supply shortages. In order to gain a more comprehensive perspective, the Community made forecasts up to 1985. These showed oil providing for two thirds of future needs, with the Community’s dependence on outside countries peaking at around 1980 but hopefully decreasing in the following years thanks to nuclear power stations and the North Sea oilfields.

Needless to say, the EEC was directly affected by the first oil crisis. It is nevertheless important to remember that the decision to reduce oil production by 5 percent per month, made at the ad hoc conference of Arab oil ministers, held at the OAPEC headquarters (Evans and Brown, 1990; Graf, 2012), was coupled with an embargo on a single European country (the Netherlands). Generally speaking, OAPEC distinguished between three types of countries: friendly countries (France, United Kingdom), neutral countries (Italy, Federal Republic of Germany, Belgium, Luxembourg, Denmark, Ireland) and hostile countries (the Netherlands). The meeting in Kuwait on 4–5 November 1973 confirmed this decision by imposing a total embargo on the Netherlands and a 25 percent reduction of the quantities supplied to ‘neutral countries’, maintaining current quantities for ‘friendly countries’. But from 18 November 1973,

the EEC countries (except the Netherlands) were exempted from a further 5 percent reduction, scheduled for December. In March 1974, the embargo was lifted on the United States, while Italy and the FRG, previously considered 'neutral countries', became 'friendly countries'. It was not until 10 July 1974 that OAPEC, meeting in Cairo, decided to lift the embargo against the Netherlands.

But the temporary restrictions and embargo were of little bearing compared to the sustained and general increase of oil prices for all EEC countries, which relied on Arab States for over 50 percent of imported oil supplies.

European states' main response was to join the US in creating the International Energy Agency. Building on the work of the OECD, this new agency was first proposed by Henry Kissinger on 23 April 1973 to bring oil-consuming countries together. In the wake of the oil crisis, President Richard Nixon put the initiative back on the agenda (letter of 9 January 1974), and 13 countries came together for the Washington conference on 11 and 12 February 1974. The group of experts, which met for the first time in Washington on 25 February 1974, envisioned multilateral cooperation for energy saving, shortage management and expediting the development of new energy sources. But the real goal was to prepare a meeting between oil-producing and oil-consuming countries (Türk, 2014). With the exception of France, all the countries agreed to sign the final charter and take part in the creation of the International Energy Agency. The European Commission did not join as an entity, since not all EEC countries were members. By 18 November 1974, the International Energy Programme finally counted 16 member countries. The IEA was an autonomous body within the OECD framework (Carroll and Kellow, 2011, pp. 76–79). France had refused to join, despite direct discussions between Henry Kissinger and Michel Jobert, then French minister of foreign affairs. The French position was to limit American interventionism in European affairs, and France had proposed the creation of a European Energy Agency, which never materialized. The other eight EEC states became members of the IEA, prioritizing direct relations with the United States over hypothetical regional coordination. It is worth noting that the main body of the IEA was its governing board and that the first executive director of the new agency was Etienne Davignon from Belgium, future vice-president of the European Commission (Gfeller, 2012, p. 232).

At the initiative of France and Michel Jobert in particular, the EEC engaged in another type of relationship with OPEC: Euro-Arab dialogue, officially launched in June 1975. The aim was to create a broad framework of discussion where all relevant topics could be addressed, including oil trade, of course. Above all, this dialogue was part of the European political cooperation strategy, revived in 1970, to make the EEC a unified actor in international diplomacy. This ambition could but frustrate the United States, especially when the talks took place in the Middle East. However, the EEC was engaging in dialogue not with OPEC but with the Arab League. While France spearheaded the effort on the European side, on OPEC's side, the approach was strongly supported by Algeria. On 13 May 1971, the Political Committee for European Political Cooperation decided that the Six should adopt a common position on the Middle East. However, the initiative was halted when the decision, which was classified, was leaked, and it was revived only with the 1973 Arab-Israeli conflict (Găinar, 2009). In addition to the oil-related measures adopted in October and November 1973, the joint official declarations by the Nine on the one hand (Copenhagen Declaration, 20 November 1973) and the Arab League on the other ('Declaration for Western Europe', Algiers, 28 November 1973) laid the foundations for future meetings. As early as 14–15 December 1973, four Arab ministers (the delegation was comprised of the foreign ministers of Algeria, Sudan, Tunisia and the United Arab Emirates) approached the EEC at the Copenhagen Summit to propose a partnership around technological assistance. In January 1974, the Commission sent a communication to the Council about fostering discussions with producer countries, but in the form of cooperation to ensure stable supplies and reasonable prices in exchange. This Euro-Arab dialogue upset Washington, with Henry Kissinger openly opposing it, particularly at the Washington Energy Conference in February 1974. Consequent US pressure on Germany and the United Kingdom caused them to adopt a very cautious stance. President Richard Nixon cancelled his

visit to Europe in April 1974, and in Brussels the United Kingdom asserted that it would prioritize transatlantic relations over Euro-Arab dialogue. In June 1974, despite the presence of a European delegation in Egypt to meet Mahmoud Riad, secretary general of the League of Arab States, it was Saudi Arabia which, again under pressure from the United States, sought to interrupt these negotiations. Finally, a decision was made on 31 July 1974 when François-Xavier Ortoli, president of the European Commission, met with Mahmoud Riad. The European objectives were clear: 'to ensure the supply of oil and oil products on acceptable terms; to persuade the Arabs to invest their funds more usefully from our point of view; and to create and develop the Arab market for EEC companies' products and services'. But the institution of real dialogue was hampered by discussions⁴ surrounding the recognition of the PLO by the EEC. As the months passed with no significant progress, despite the Euro-Arab dialogue having officially launched on 10 June 1975, the frame of the discussion changed: energy issues were withdrawn from the dialogue at Arab countries' request in November 1975. The meeting in Abu Dhabi from 22 to 27 November 1975 thus marked the real start of the dialogue with, from that date, regular meetings of a Euro-Arab commission that had been partially stripped of its initial objectives. In 1979, French president Valéry Giscard d'Estaing sought nevertheless to revive this Euro-Arab dialogue, though no longer involving the United States, which until then had been present.

To establish direct relations between the EEC and OPEC, the Europeans had to contend with the United States, either by keeping them informed or by maintaining a certain discretion (the word 'dialogue' was considered 'diabolical') and limiting discussions to technical issues. A visit on 7 October 1974 by Aly Attiga, secretary general of OAPEC, to Henri Simonet, European commissioner for energy, was to lead to six-monthly technical meetings.⁵ These were not confidential, as a *New York Times* article published on 9 October 1974, titled 'OAPEC and EEC set regular talks after 2-Day Parley', illustrates. Guido Brunner also visited Kuwait in 1978 and, from 1982, annual OAPEC-EEC meetings were held alternately in Brussels and Kuwait City. Certainly, the meeting in Martinique in December 1974 between French president Valéry Giscard d'Estaing and US president Gerald Ford had opened up the possibility of a conference between oil-importing and exporting countries, but OPEC's wish from an early stage to extend the scope of the conference to all raw materials, sparked reluctance and resistance.

In parallel with these attempts at direct relations with OPEC and OAPEC, the EC sought to distance itself from international organizations too close to the United States (OECD) by initiating new multilateral meetings. With a view to integrating the oil trade into a broader diplomatic framework, North-South relations were the focus of the Paris conference (McFarland, 2015; Garavini, 2015; Gilman, 2015) on international economic cooperation. From 1975 to 1977, this conference was a focus of opposition between industrialized and developing countries, including OPEC. Discussions on a new international economic order, the theme of the conference, had been approved by the United Nations General Assembly in its Resolution 3201 of 1 May 1974. For Europe, these discussions were also very clearly about restructuring North-South cooperation (Migani, 2014). While energy and raw materials were central to the discussions, this included agricultural products as much as oil. Moreover, contrary to France's wishes, no distinction was made between OPEC countries and developing countries. During the discussions, the EEC spoke with one voice, which required prior consultation between the nine member states (Garavini, 2012). This slowed down the negotiation process, ultimately eroding it and resulting in no tangible outcome.

When the oil crisis struck, the EEC's stance, in accordance with the Treaty of Rome, was solidarity between member states. But in practice this solidarity was undermined as early as 1973. OPEC fully exploited the differences between EEC states' situations (for example, imposing a total embargo on the Netherlands), and these differences were moreover so wide that no common energy policy could emerge. The agreements concluded by the Compagnie française des pétroles (CFP) with Iraq, by Elf Aquitaine and the CFP with Saudi Arabia (three-year agreements of 1973, renewed in 1976), by the Belgian Distrigas with Saudi Arabia, by ENI with Iraq and Saudi Arabia, and by the modest Irish National Petroleum

Company with Iraq and the Danish State Oil Company with Saudi Arabia, were all signed within the framework of bilateral state-to-state relations. Above all, no European Commission department was notified of these agreements. Oil exports from producing countries using these direct contracts increased from 8 percent of total exports in 1973 to 42 percent in 1979,⁶ and oil companies confirmed their position as major actors on the oil market. With the exception of discussions surrounding refining issues from 1978 onwards,⁷ direct contact between the European Commission and oil companies was rare. The oil industry was clearly divided between European-owned companies, which supported the Commission's intervention on the oil market, and US companies that were reluctant (Chevron, Exxon) or even hostile (Texaco, which dealt directly with the IEA) with regard to it.

Finally, the oil crisis fostered the emergence of a new institutional actor within the EEC: the European Council, defined as the meeting of heads of state and governments. Decided on in Copenhagen in December 1973, this European Council was officially established one year later. Its creation was hardly insignificant: it was informed by the desire not only to give European decisions more clout by entrusting them to the executive heads of each member country, but also to be able to respond to crisis situations. Alongside this new intergovernmental body, the European Commission remained at Community level, creating a distinction, in a sense, between short-term and crisis management policies (European Council), on the one hand, and long-term structural policies (European Commission), on the other. The many communications from the Commission to the European Council thus focused not on how to deal with the crisis but on long-term policies to reduce oil dependency, particularly by promoting renewable energy. In the wake of the oil crisis, it was thus the European Council that liaised with the IEA and handled the Euro-Arab dialogue. As an intergovernmental body, the European Council also provided a forum for member states to voice their differences. The United Kingdom, for example, had no desire to make its North Sea reserves available (Leboutte, 2006). Likewise, France was committed to the nuclear programme, and encouraged other European countries to follow suit when public opinion began to make itself heard through movements protesting against nuclear energy. At the 14 June 1977 European Council meeting in Luxembourg, France had also considered proposing a cap on oil imports (06.05.1977). In May 1979, the European Council on Energy again pushed for establishing 'certain contacts between the Community and the OPEC countries' Strategy Group' chaired by Sheikh Yamani,⁸ in keeping with the French ambition expressed in March 1979. At Sheikh Yamani's request, technical contact was approved, devoid of formalities or publicity. A meeting between European experts, led by Guido Brunner and André Giraud, and OPEC experts took place on 30 June 1979 in London, in the presence of Sheikh Ahmed Zaki Yamani. Confidentiality had not been preserved; the *New York Times* reported on the meeting ten days prior to it, and the *International Herald Tribune* published a detailed report on 4 July 1979. The internal minutes noted:

The meeting was not unfriendly, but there was (as expected) no constructive reaction from the OPEC side. Without appearing as 'demanders', we should seek to follow up with a similar meeting later in the year, perhaps more explicitly 'technical', and perhaps without any Ministers present. We cannot be sure that such a meeting will be productive, but it might grow into arrangements for a continuing exchange of views, and form part of a wider pattern of contacts with the oil producers.⁹

Aid to developing countries became a common issue on which Europe and the OPEC countries could agree. From 1976, OPEC countries used available funds to carry out their own development aid programmes (Shihata, 1982, 1983), partly competing with European countries in Africa and the Middle East. In fact, the Algiers Declaration of March 1975 had entrusted OPEC with consolidating solidarity within the Third World, and the financial commitments of countries such as Saudi Arabia, the United Arab Emirates, Qatar and Kuwait to fund projects in the Third World were increased to between 7 percent and 15 percent of GNP. The EC also took a stance on the matter, launching cooperation programmes in the

energy sector for developing countries from 1979. Some of the countries targeted were actually members of OPEC (Venezuela, Nigeria) and were looking for the energy diversification that the EC could provide.¹⁰

The first oil crisis therefore boosted initiatives by European countries to build ties with OPEC countries, either through direct contact or through the implementation of a global multilateralism. Both attitudes involved a form of politicization of oil trade, with the EC supporting UN Resolution 242 as well as new North–South relations. But both approaches ended in failure. Once again, oil companies were the main actors in this period, handling the supply of oil through commercial transactions, with the help of a few bilateral actors.

Economic diplomacy outside international organizations, 1979–1986

From 1979, attempts to conduct oil diplomacy through direct negotiations, be they political or economic, turned into diplomacy outside of interstate negotiations. The failure of the New International Economic Order was glaring, divergences between EEC member states' energy policies were growing, and internal political tensions had surfaced within OPEC following the Iranian revolution and within the Arab League following the Camp David agreements. Against this backdrop, the market and oil companies – both Western companies and those of producer countries – became preferred intermediaries for establishing the framework of a *modus vivendi* to ensure the stability of supply to European countries, and the commercial revenues of OPEC countries. Within the IEA, cooperation between European countries gradually prevailed. At the December 1979 meeting, the EEC even forced the United States to adopt an energy policy based on both controlling consumption and price liberalization.

The second half of the 1970s, and even more so the 1980s, also corresponded to the period of full exploitation of the North Sea oilfields, which rapidly and substantially changed European countries' dependence on OPEC countries. Beyond purely economic considerations (in terms of both quantities and prices), the North Sea oil and gas fields offered European countries unprecedented security of supply, thus loosening OPEC's grip. In addition to this new local energy order, national strategies developed to foster diversification, either of the origin of imported oil (e.g. Africa and the USSR for France) or of the energy sources themselves (rapid growth of gas in the United Kingdom and the Federal Republic of Germany). As a result, relations between the EC and OPEC were no longer as crucial, though they remained important.

The creation of the Gulf Cooperation Council (GCC) in May 1981 in Abu Dhabi could have afforded an opportunity for the EEC to establish an oil diplomacy with some of the largest producer states, especially since Iran had naturally been excluded from this organization. The outbreak of the war between Iran and Iraq in the autumn of 1980 cut EEC supplies by 12 percent. But this was managed by the IEA Steering Committee¹¹ and not the European Council: to 'complete the EC's network of contractual relations'¹² with the Arab world, its policy was to conclude bilateral agreements with the Gulf states on a strictly economic level. Political references were deliberately removed. Yet initiatives had been taken since the autumn of 1979, with an informal meeting of foreign ministers on European–Gulf relations.¹³ During a technical mission to Oman in June 1980, positive contacts were also established with Bahrain and the United Arab Emirates. But Saudi Arabia, Iraq, Qatar and Kuwait refused these technical cooperation agreements, preferring to revive the Euro–Arab dialogue, which was limited to general political issues.¹⁴ The GCC prioritized strategic and political issues over economic negotiations, particularly with a view to securing stability in the region (Colombo, 2014). Moreover, the influence of the United States and Saudi Arabia led to the exclusion of oil negotiations from dialogue with the European institutions, regarding both quantities and prices. The Euro–Arab dialogue, relaunched in 1979, continued even though when it came to energy, European representatives had to stick to 'general terms'¹⁵ and focus on the issue of renewable energy in the run-up to the United Nations conference in Nairobi.

In some respects, the 1980s were a successful decade for Europe, despite the absence of a coordinated energy policy. A few days before the June 1980 G7 summit in Venice, the European Council had proposed a fund to ensure the stability of commodity prices, particularly oil prices, but the initiative failed. The endeavour to achieve energy savings by reducing oil imports placed the European Community in good stead, even though this reduction of dependency resulted from diverging national policies. The impact on OPEC was not negligible: between 1973 and 1980, EC oil imports dropped from 600 to 450 million tonnes. Yet despite efforts to devise an energy strategy for the European Community,¹⁶ the decade was once again marked by the absence of a common front in the EEC's external relations. Christopher Audland, British EC director general for energy (DG XVII) from 1981 to 1986, was the main architect of the twofold liberalization of the energy sector: internal competition and external trade liberalism. The idea of a common energy policy within the Single Market soon prevailed, though implementation was slow and primarily focused on opening up renewable energy to competition and boosting its development, rather than on the difficult convergence of the structures of energy production. By making energy an internal challenge and less and less a matter of external dependence, the European authorities promoted the most liberal trade negotiations in relations with OPEC member states. In the early 1980s the EC imported 91 percent of oil consumed, which still accounted for just over 50 percent of the European total energy consumption.

Eventually, most relations with oil-producing countries fell outside of the framework of the EC. Unlike the 1973–1979 period, when the EC's aim was to achieve European coordination, the following decade saw a return to national strategies and especially oil companies being reinstated as negotiation intermediaries to ensure EC countries' supply. The EEC no longer paid much attention to oil policy, seeking rather to engage in trade relations. With the rise in oil prices, most countries' trade deficit rapidly increased to the point of becoming a major concern. Several solutions existed to limit this trade deficit. The argument of global economic instability was regularly made:

We need to convince the OPEC countries – or at least those of them who are prepared to listen to logical argument – that they will not in the long run gain if their price policies generate inflation, economic instability, and above all unmanageable balance of payments problems for developing countries without oil. They must understand the interdependence of all our economies, and the need for the world to have stable supplies of oil at reasonable prices during the long period of transition to other forms of energy.¹⁷

Another way to recover part of the sums spent on oil was to promote direct investment by OPEC countries in Europe. Germany proposed the creation of an international 50–50 direct investment fund with oil-producing countries so that part of the petrodollars could be invested in industrialized countries. Likewise, the EC endeavoured to boost trade: studying the market shares and products exported by the EEC to OPEC countries in precise detail, its strategy was to recover part of the sums paid through industrial exports and to adopt a trade partnership approach¹⁸ (Gray, 2016). On the eve of the oil crisis, Europe accounted for 42 percent of OPEC countries' imports, in other words more than the United States (Table 13.1).

With the many indirect forms of contact made during this period, some academic organizations were able to serve as forums for discussion. This was the case of the Oxford Institute for Energy Studies, created in 1982, which rapidly established itself as one of the leading centres of expertise on energy issues. The seminars organized in this institute provided a space for dialogue (Mabro, 1986, p. 270), especially since the official members of the institute included OAPEC, the EEC and the UK Department of Energy.

Conclusion

In a diplomatic landscape characterized by a proliferation of institutions and organizations, the EEC and OPEC were not able to establish direct relations, neither regarding oil nor within a broader framework

Table 13.1 Distribution of OPEC imports across supplier countries in 1972

	<i>Algeria</i>	<i>Libya</i>	<i>Nigeria</i>	<i>Iran</i>	<i>Kuwait</i>	<i>Saudi Arabia</i>	<i>Iraq</i>	<i>Venezuela</i>	<i>Indonesia</i>	<i>OPEC</i>
EC (9)	65	62	56	44	33	32	32	31	18	42,5
USA	6	7	8	16	16	25	3	46	20	18,5
Japan	1	5	9	13	17	21	4	9	39	13,5
Rest of the World	28	26	27	26	34	22	61	14	23	25,5

Source: OECD. HAEC, BAC 250/ 1980–305.

(Euro-Arab dialogue, the New International Economic Order, aid to developing countries, etc.). The oil crisis disrupted the European institutions, leading to their partial reconfiguration with the creation of the European Council. This could also be read as a return to the primacy of the intergovernmental political dimension, with the European Commission proving unable to drive a Community policy in the oil sector. Economic and political differences emerged, to the point of paralysing any concerted initiative and confirming, if there were ever any doubt, that the EEC was a 'political dwarf'. But the same was also true of OPEC, and the relations that developed from 1977–1978, once its ambitious political objectives had been side-lined, were based on traditional economic diplomacy: that of contracts, investments and bilateral partnerships.

What conclusion can be drawn from these relations over a quarter of a century? The EEC, although it brought together consumer countries, did not position itself from the outset as a coherent entity to negotiate oil imports. To be sure, Europe was 'weakened and humiliated' by the failure to coordinate consumer countries under the aegis of the OECD (Chakarova, 2013, p. 149), but pre-existing perceptions also undermined efforts at direct political dialogue. The rhetoric of cooperation between consumer and producer countries was never without ulterior motives, throughout the 1970s. Europe sought to create a new set of multilateral initiatives to its advantage (New International Economic Order, Euro-Arab Dialogue, G7, etc.), but failed to untangle itself from the web of international organizations established by the United States since the Second World War. Ultimately, by dissociating trade relations from political issues, contrary to what the 1973 oil crisis might have suggested, European countries were better able to negotiate with oil-exporting countries. As advocates of a liberal approach in the energy sector, European countries could thus negotiate their oil supply within a stable framework (Garavini, 2014), deliberately autonomous – though that is not to say independent – of international organizations. As Laurent Warlouzet has shown (Warlouzet, 2018, p. 274), this neoliberal approach gradually prevailed within the EEC in the 1980s, without ever being cut off from social concerns or from a neo-mercantilist approach.

Since the mid-1990s, while the internal market has been reprioritized within European energy policy,¹⁹ a new impetus for multilateralism has driven the energy field, particularly with the 1994 European Energy Charter and its extension, the International Energy Charter. Likewise, the World Energy Conference, created in 1924, regained legitimacy in the 1990s by establishing itself as a forum for dialogue between producer and consumer countries. Yet these international organizations remained linked to state policies. The special relations between the United States and Saudi Arabia, at least until the mid-2010s, clearly hindered the establishment of direct relations between OPEC and the European Union, as well as any form of multilateral dialogue relating to oil.

Notes

1 *Historical Archives of the European Union*. BAC 3/ 1978–775. 'Letter'. 11 January 1962.

2 *Historical Archives of the European Union*. BAC 3/ 1978–775. 'Telex'. 2 February 1971.

- 3 COM (68) 1040. *First guidelines for a Community energy policy. Memorandum presented by the Commission to the Council*, 18 December 1968.
- 4 *Historical Archives of the European Union*. BAC 205/1980–302. ‘Note on the Euro–Arab dialogue’. 17 September 1974.
- 5 *Historical Archives of the European Union*. BAC 205/1980–302. ‘Note of 16 October 1974’; HAEC. BAC 16/1979–75. ‘Note of 10 January 1975’.
- 6 *Historical Archives of the European Union*. BAC 39/1986–572. ‘Note from Michel Vanden Abeele to Crispin Tickell’. 27 June 1980.
- 7 *Historical Archives of the European Union*. BAC 144/1987–312. ‘Meeting of 10 March 1978 between the Commission and the companies BP, CFP, Chevron, Elf-Erap, Exxon, Petrofina and Texaco’. 10 March 1978.
- 8 *Historical Archives of the European Union*. BAC 39/1986–568. ‘Energy Council meeting’. 17 May 1979.
- 9 *Historical Archives of the European Union*. BAC 39/1986–568. ‘Note for the attention of the members of the Commission’. 6 July 1979.
- 10 COM (79) 155 final, *First actions of cooperation with certain developing countries in the field of energy. Communication from the Commission to the Council*, 21 March 1979.
- 11 *Historical Archives of the European Union*. BAC 144/1987–281.
- 12 *Historical Archives of the European Union*. BAC 327/1993–32. ‘Council Secretary General. Internal memorandum on relations with the Gulf States’. 24 September 1981.
- 13 *Historical Archives of the European Union*. BAC 39/1986–568. 20–21 October 1979.
- 14 *Historical Archives of the European Union*. BAC 39/1986–568.
- 15 *Historical Archives of the European Union*. BAC 144/1987–275– ‘Note to G. Brunner. Preparations for the Energy Council’. 6. May 1977; HAEC. BAC 327/1993–32. ‘Council Secretary General, Memo for the attention of the heads of delegations of the *ad hoc* “Euro–Arab Dialogue” group’. 6 May 1981.
- 16 COM (81) 540 final, *The Development of an Energy Strategy for the Community. Communication from the Commission to the Council. Communication from the Commission to the Council*, 2 October 1981.
- 17 *Historical Archives of the European Union*. BAC 39/1989–527. ‘Note from DG XVII in preparation for the G7 Summit in Venice’. 16 June 1980.
- 18 *Historical Archives of the European Union*. BAC 250/1980–305; HAEC. BAC 130/1983–322. ‘Report by a United Kingdom Interdepartmental Working Party on the vast surpluses of the oil producers’. February 1975, p. 64.
- 19 COM (94) 659 final, *For a European Union Energy Policy – Green Paper*, 23 February 1995.

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Part III

OPEC, non-OPEC and the international oil companies



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The changing relationship between OPEC countries and international oil companies

The dynamics of bargaining power in an evolving market

Carole Nakhle and Francesco Petrini

Introduction

The formation of OPEC in 1960 marked the beginning of a new era in the structure of the oil market and in the relationship between host governments (HGs) and international oil companies (IOCs). In subsequent decades, the relationship has known many transformations as market conditions continued to evolve.

The overriding objective of this chapter is to analyze the evolution of the relationship between OPEC and IOCs between 1960 and 2018, with a special focus on market power and the fiscal and contractual changes that have accompanied that evolution. The paper also investigates the domestic and global factors that have triggered major changes in that relationship and in the bargaining power of the respective parties, and how these are likely to evolve in the light of growing competitive forces and challenges shaping global energy markets.

The paper proceeds as follows. Section 2 provides an overview of the main fiscal arrangements in the oil and gas sector. Section 3 tracks the relationship between OPEC and IOCs from 1960 to 2018 and their power over oil markets. Section 4 includes the concluding remarks.

Petroleum fiscal arrangements

Before elaborating on the evolution of the relationship between OPEC governments and IOCs, it is worth explaining the basic differences between the major petroleum fiscal arrangements and the factors residing at the center of that evolution.

In the case of minerals in the ground, and petroleum in particular, governments and state authorities in most countries are the legal owners of these resources and are therefore fully entitled to collect a revenue stream from what they own. This ownership status can be translated into policy in a variety of ways. The oil-producing nations can opt for complete state ownership (or monopoly) at one extreme (such is the case in Saudi Arabia and Kuwait) or permit total private enterprise operations at the other (as in the USA and

the UK). Between the two extremes of pure state and pure private ownership, a combination of the two is often found. Most oil-producing countries fall within that spectrum, the norm being a pattern of involvement by the IOCs, in cooperation with the host country's national oil company (NOC) and within a clear framework of national control.

Such a spectrum was inconceivable in the early days of the oil industry, which was marked by the dominance of the Western private oil companies, operating under generous concessionary agreements. During the 1950s and 1960s, the industry saw the development of new contractual arrangements that gradually replaced the then prevailing concessionary system in many developing countries and remain prevalent to date. No new such 'grand' regimes have appeared since, but the terms of existing contracts continue to evolve to accommodate changes in conditions particularly the oil price.

Main types of fiscal regime

In the spread of varying relationships between governments and the oil industry, one can identify two basic, broad categories of agreement that have developed over the years –concessionary systems and contractual agreements.

The concessionary system originated at the very beginning of the petroleum industry (mid-1800s) and still predominates in OECD countries. The contractual system emerged a century later (mid-1950s) and has been typically favored by developing countries. The UK, Australia, Canada, the US and Norway, for example, operate a concessionary regime, companies being entitled to the ownership of the oil extracted. By contrast, countries like Azerbaijan, Nigeria, Angola and Iraq apply a contractual regime, whereby the government retains the ownership of the petroleum produced.

A concession provides an oil company with the exclusive right to explore, develop and export oil. It also gives the company title to the oil produced, along with the requirement to pay the appropriate royalties and taxes. Because modern concessionary regimes include various combinations of a royalty, an income tax and a resource rent tax, they are also known as 'royalty and tax systems (R&T)'. It has also become common for the state or its NOC to participate in an oil and gas concessionary venture. The basic features of the oil and gas concessions are similar, but the fiscal terms or ingredients vary considerably and are likely to evolve over time as the fields and basins mature.

According to typical contractual systems, the oil company is appointed by the government as a contractor for operations in a certain license area. The title to the hydrocarbons remains with the state and all production belongs to the government unless it is explicitly shared. The IOC carries out petroleum operations in accordance with the terms of the contract and operates at its own risk and expense, providing all the financing and technology required for the operation. The parties agree that the contractor will meet the exploration and development costs in return for a share of production, or a cash fee for this service, if production is successful. If the company receives a share of production (after deduction of the government's share), the system is known as a PSC – also called a production sharing agreement (PSA) – which is a binding commercial contract between an investor – the IOC – and a state (or NOC). A PSC defines the conditions for the exploration and development of hydrocarbon resources in a specific area over a specific period. Under a PSC, since the company is rewarded in physical barrels, it takes title to that share of petroleum extracted at the delivery point (export point from the contract area). Under service contracts, the HG hires the services of an IOC and, in the case of commercial production, the company is paid a fee (often subject to taxes) for its services without taking title to any petroleum extracted. A distinction is sometimes made between a service contract and risk service contract. The former is based on a defined compensation for a specific task, while the latter may involve additional risk being taken by the contractor for which a variable fee may be applicable (Nakhle, 2008).

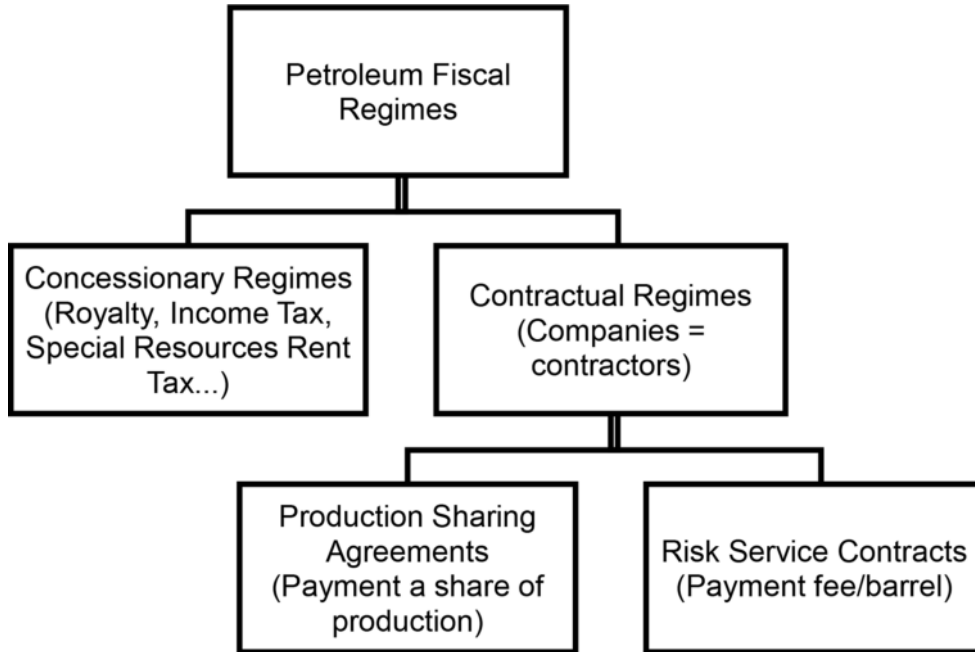


Figure 14.1 Petroleum fiscal arrangements

Diverging interests

Over time, concessionary regimes have lost their appeal in many developing countries. Most probably this goes back to the first half of the 20th century, when oil-producing countries' interests were heavily penalized by a system tilted in favor of the oil majors.

The early concessions signed in the Middle East were very generous to the oil companies. The concession granted to W. K. D'Arcy by the Persian monarchy in 1901, for instance, covered nearly the entire national territory and lasted a long time, up to 60 years (Ferrier, 1982). In return for the concession, the Persian monarchy received an up-front payment of 40,000 British pounds, the right to a yearly 16 percent share of net profits, and a royalty of four gold shillings for every ton of oil sold (Maugeri, 2006, p. 23). The D'Arcy concession became the model for subsequent agreements in the Middle East until after the Second World War. In particular, the production of those that were to become the other two main oil-producing countries of the region, Iraq and Saudi Arabia, was organized along similar lines, as far as the relation with the HG was concerned (Shwadran, 1973). The financial benefits accruing to the host government under such arrangements were limited, consisting primarily of royalties imposed at a flat rate as a percentage of the oil produced. The concessionaire retained control over virtually all aspects of the operations, including the rate of exploration, the decision to develop new fields and the determination of production levels, among others, leaving the government with a relatively passive role.¹

Those arrangements were bound to be called into question as the balance of power changed in favour of the ruling authorities and governments.

After the first wave of nationalizations (Bolivia 1937, Mexico 1938) and the weakening of colonial relations brought about by the Second World War, a second generation of concession agreements emerged. They provided for a more equitable sharing of the oil wealth between the HG and the IOCs and a greater degree of contractual stability, which was crucial in the eyes of the IOCs management that

foresaw those revisions as a necessity to prevent the eventuality of a clash with nationalistic forces (Painter, 1986; Qaimmaqami, 1995, pp. 3–6). As indicated by the US State Department: ‘the companies would have to sweeten the financial terms of their contracts with the Middle Eastern governments in order to keep their concessions’ (United States Senate, 1975, p. 82).

The 50–50 profit sharing principle was first introduced in Venezuela in 1948 and Saudi Arabia followed suit in 1950, quickly quadrupling its petroleum revenues (Duval et al., 2009). In 1949, the US Treasury collected \$43 million in taxes from Saudi Aramco, the US concessionary company in Saudi Arabia – four million more than the Saudi government received. Two years later that equation was more than reversed: the Saudi government collected \$110 million while only \$6 million went to the US Treasury (Yergin, 1991, p. 447). The tax payments made by Aramco to the US Treasury turned negative amount from 1953 onwards, since the payments to the Saudi government was considered entirely deductible under the foreign tax credit provision of the US internal Revenue Code (93rd US Congress, 1975, p. 85).

By 1952, the 50–50 profit sharing principle spread across most Middle Eastern producers except in Iran, where the industry was nationalized in 1951.

Additional notable changes were also made. The concession areas were delineated as blocks, while the awarding of concessions was restricted to a limited number of blocks. The agreements also contained provisions for the relinquishment of most of the original area (where a commitment to develop the area is not made within an agreed timescale). The duration of the concession became much more closely regulated.² From the 1960s onwards, many concessions have included provisions for HG equity participation, mainly through its NOC.

During the second half of the century, governments in many developing countries increasingly regarded the concessionary regime as incompatible with their sovereignty. Contractual regimes were therefore devised as an alternative to grant the HG more control over both petroleum operations and the ownership of production. The concept of the PSC was introduced as early as the 1950s in Latin America, but the first PSC model in its current form was applied in Indonesia in 1960 and has since become increasingly popular in the developing countries. Risk service contracts first came into use in the 1950s in Latin America and in the Middle East in the late 1960s. The main feature of the Indonesian PSC (and contractual regimes in general) is that it elevated the role of the HG to management and authority whereby the ownership and control of national resources became entrusted to the state, whereas the IOCs’ role was changed to risk-taking contractors entitled to reimburse their costs in case of commercial discovery and to a share of production to remunerate their efforts (the latter in the case of a PSC) (Duval et al., 2009).

OPEC and IOCs: evolution

This section identifies four key episodes in the evolution of the relationship between OPEC HG and IOCs. Interestingly, those episodes tend to have similar duration.

1960–1973: the cartel is dead, long live the cartel

The period 1960–1973 denoted the last hurrah of the private cartel system set up in the late 1940s on the foundation of the 1928 Achnacarry Agreement and solidified by the ‘postwar petroleum order’ (Yergin, 1991, p. 409) after 1945. The cartel of the Seven Sisters began to crumble from the beginning of the 1960s for various interrelated reasons. First, the evolution of the market with the entry into the international oil business of new actors – companies external to the circle of the big multinationals – as well as the return of Soviet oil in the West European markets. The increasing competition undermined the IOCs grip on the oil trade and brought about an inflection in the market price of crude and products. Second, a radical change of attitude of producing governments towards a more assertive stance in

defense of their interests. The clearest expression of this new attitude was the creation of an organization of producer states – OPEC.

The creation of OPEC was precipitated by the oil companies' unilateral cut in the posted price of oil, which was the reference price for tax assessment. The IOCs paid their taxes to HGs on the basis of a publicly posted price, while selling their oil and refined products to third customers at market prices.³ The latter tended to fall from the mid-1950s to the late 1960s as the entry into the oil business of new actors and the limits on oil imports imposed by the US government produced a situation of oversupply in oil markets.⁴ To relieve the pressure on its profit structure, in September 1959, Standard Oil of New Jersey (later Exxon), without consulting the producing countries, reduced its posted prices by about 5 percent, bringing the price of benchmark Arabian light to \$1.91 per barrel, closer to the market price. The move was reluctantly followed by other oil companies. In August 1960, posted prices were unilaterally lowered by 10 percent. As a result, millions of dollars of producing countries' expected revenues vaporized. One month later, OPEC was formed (Sampson, 1975).

Contrary to the common opinion, OPEC was quite effective in its first decade of its existence: the posted price remained steady and the government take – that is, the total share of government revenues from a project's net cash flows – increased at the expense of companies, rendering the 50–50 system more similar to a 60–40 and then even a 70–30 to the HG's advantage. In 1964, after lengthy negotiations, OPEC and the IOCs agreed on the 'Royalty Expensing' system, which abolished the deduction of the royalties paid by companies from the calculation of the 50 percent taxation of profits (Mabro, 1984, pp. 7–8; Bamberg, 2000, pp. 151–161). This brought about a significant increase in the fiscal revenue the producing governments received from the concessionaires. It is significant that – as pointed out by Bamberg in his history of BP (Bamberg, 2000, p. 178), the periodical meetings in New York of the representatives of the 'Seven Sisters', organized on the initiative of the influential business lawyer John J. McCloy, by the mid-1960s changed their focus from the danger posed by Soviet oil exports to the political situation in the Middle East and OPEC.

Overall, throughout this period the private international oil cartel managed to contain the tendency to overproduction, at the expense of some producing countries (mainly Iraq that had nationalized most of its oil industry in 1961), limiting market volatility to a 'gently declining price' (Parra, 2004, p. 73). However, the widening gap between the fixed posted price and the declining market price reduced the IOCs' profit margins and increased their fiscal burden to the benefit of the HGs. According to Shell, between 1960 and 1970, the government take in the Eastern Hemisphere grew from \$0.708 per barrel (/b) to \$0.860/b.⁵ As reported by Adelman, in the 1960s the profits of the oil industry in the Persian Gulf fell by some 24 percent, while the payments to HGs grew by 15 percent; so, in 1970, the government take came to count for nearly 70 percent of profits: out of a profit of \$1.334/b, defined as the posted price minus the royalty, various discounts and accounting cost, the government take – that is, the royalty plus the income tax at 50 percent – amounted to \$0.892/b, or 66.8 percent (Adelman, 1990, p. 5).

The phase of ascendancy of the postwar petroleum order in the 1950s can best be described as the calm that preceded the storm, as high oil price volatility characterized the following decades (Figure 14.2). Since the early 1960s, the IOCs increasingly found themselves in a difficult position, caught in a pincer between a declining market price and a rising government take. The rise in prices of the early 1970s, however, somehow solved their profitability problem.

At the end of the 1960s, after the rise to power of a radical government in Libya, a country that had become the new oil El Dorado,⁶ the movement towards the dismantlement of the concessionary system – seen by many as a relic of the colonial past – acquired momentum. After a few months of tough negotiations with the companies, at the end of 1970 the new Libyan government obtained a substantial increase in the posted price and a new profit tax rate ranging from 54 percent to 58 percent, depending on the company, compared to the previously prevalent 50 percent. That marked the first time a producing country snatched the price-setting power from the hands of the oil multinationals. OPEC was quick to

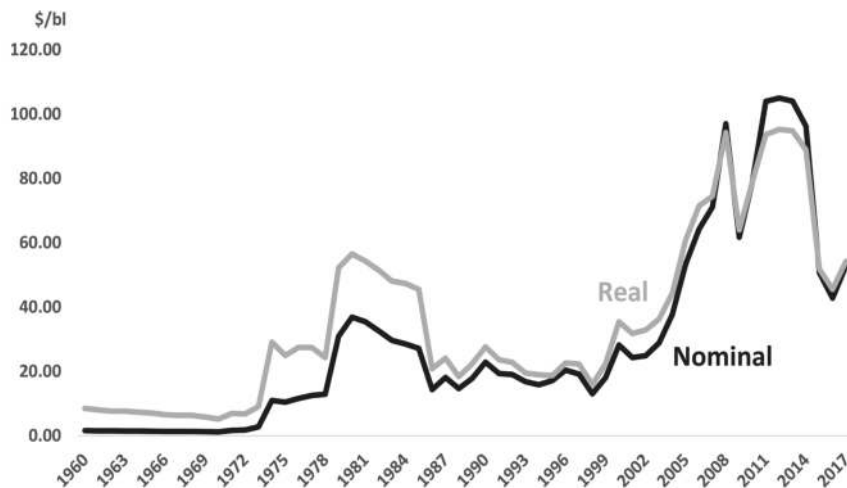


Figure 14.2 Historical oil prices, 1960–2017 (real and nominal)

Note: *Annual data for equally weighted average of WTI, Brent and Dubai oil prices.

Source: World Bank, Commodity Markets (September 2018).

demand an extension of Libyan concessions to other countries. The OPEC Caracas meeting of December 1970 demanded the generalization of the 55 percent tax rate and the establishment of ‘uniform general increases’ of the posted prices in all member countries (Skeet, 1988, pp. 63–64).

In the conferences held at Tehran and Tripoli in 1971, the unified front the companies created to negotiate with OPEC capitulated to the latter requests, provided that the rise in HGs’ take could be off-loaded onto the consumers’ shoulders (Schneider, 1983, pp. 135–166). The attitude of the consuming governments of the US and Europe also made it clear that the latter was the case.⁷ The script was then repeated in the subsequent rounds of price increases that led to the 1973 ‘oil shock’ (Petrini, 2016).

By progressively increasing the taxation and state participation in oil and gas activities throughout the 1970s, the largest oil producers attained a share of +/- 85 percent of the profits from production – a trend that was to continue in the following years (Duval et al., 2009).

The OPEC governments also wanted more voice in the management of their resources. This was first addressed by the idea of producing state participation to ownership as partners of the IOCs. This gradual approach was sponsored by the Saudi oil minister Ahmad Zaki Yamani, who was aware of the tensions that a direct step-in of the producing governments into the oil business would have created among them. Soon, the radicalization of the developing countries and of some major oil producers (Libya, Algeria) pushed aside the proposal and nationalization became the norm (Sampson, 1975).

1973–86: the era of OPEC dominance

The 1973 fourfold increase in the oil price, decreed unilaterally by OPEC, marked a momentous change, reflecting the shift in market power from the IOCs to HGs. This period effectively closed the era of dominance of the oil majors, which lost their role of price-setters and had to renegotiate their connection with both consuming and producing governments. But it was a question of time before OPEC felt the burdensome responsibilities that come with power.

The period witnessed several events that resulted in production cuts particularly among OPEC producers. First, the 1973/4 Arab oil embargo led to a 5 percent production cut by the Organisation of

Arab Petroleum Exporting Countries (OAPEC) on 16 October 1973 against selected Western countries viewed as supporting Israel in the Yom Kippur War. A firmer oil demand amplified the outcome of such a cut. At least 75 percent of that oil price increase could be attributed to shifts in the oil demand, especially that in the early 1970s, when a global demand boom was noted in all industrial commodity markets (Barsky and Kilian, 2004). Second, the 1979/80 Iranian Revolution and the geopolitical tensions between the US and Iran as well as between Iran and its neighbors, which in turn fueled increased inventory demand in anticipation of future oil shortages, contributed to an increase in crude oil prices from less than \$15/b in 1978 to almost \$40/b in 1980 (Kilian and Murphy, 2014). The outbreak in 1980 of the Iran-Iraq War resulted in a combined loss of production amounting to about 6 percent of world production at the time.

The higher oil prices translated into higher profits for oil majors, which led many HGs to further tighten their contractual and fiscal arrangements. This applied to all fiscal regimes with PSCs and service agreements increasingly popular in the developing world. The share of state participation among OPEC members increased from an average of 25 percent in 1973 to 51 percent by 1982. The UAE and Oman increased it to 60 percent in 1974 and 1980 respectively, while in Kuwait and Qatar (1975), Venezuela (1976), and Saudi Arabia (1980), it increased to 100 percent, which simply meant nationalizing the industry. In these latter cases, the governments offered short-term contracts, entitled technical service agreements, which limited the oil companies to the provision of technical services but without any access to production (Duval et al., 2009). By replacing the concessionaires upstream, the NOCs completely changed the structure of the international oil trade. The net effect of the advent of the NOCs⁸ and the loss of reserve ownership by the majors was the ‘de-integration’ of what had previously been an internal oil trade carried out mainly within the integrated oil companies or between them (Marcel, 2006, p. 34; Ross, 1987).

During this period, the oil companies saw OPEC both as an indispensable partner to maintain access to crude and govern the market, and as an adversary whose power had to be reduced. They tried to make the best of a bad situation while at the same time acting to redress the balance of power, mainly by investing outside the OPEC domain and fostering a new, wholly unprecedented (at least for international oil) way of determining the price of crude and products: the market (spot and futures).

The spot market increasingly became a major source of supply for IOCs that had lost direct access to crude ownership. According to *Petroleum Economist* in November 1983, between 20 per cent and 50 per cent of the crude oil supplies of the larger companies came from the spot markets, compared to 5–15 percent prior to the Iranian revolution and perhaps only 1–2 percent (if that) during the days of IOCs’ dominance. As the price of international oil became more volatile and the US authorities removed price controls on the US market,⁹ futures trading became increasingly important. The New York Mercantile Exchange (NYMEX) officially opened its doors to oil trading in 1983, although some transactions started a few years earlier. John Treat, the president of NYMEX, declared that the crude contracts would become a major pricing indicator for world oil markets, replacing OPEC as the ultimate price setter: ‘The true value of crude oil will increasingly be determined by ‘open outcry’ rather than behind OPEC’s closed doors’ (*Petroleum Economist*, June 1983, p. 226).

As far as the spatial restructuring of production went, since the early 1960s a significant wave of investments, driven mainly by the majors, had opened up new sources of supply in politically safe areas and largely private investment friendly like the North Sea and Alaska. These investments became productive during the 1970s, especially after the middle of the decade and, though at the time accounting for only around 10 per cent of world oil reserves, Western Europe and the US soon supplied 27 per cent of total oil output (Renner, 1984). The United Kingdom (UK) alone became the fifth producer in the world (*Petroleum Intelligence Weekly*, 1985).

Despite the high costs of development, the companies operating fields in those ‘new’ areas achieved higher profitability, thanks to the prevailing high prices, high quality of crude and more lenient fiscal terms. As a result, non-OPEC production soared and OPEC’s share of total production decreased (tables 14.1 and 14.2).

Table 14.1 Crude oil production by world's ten leading producers in 1984, in million barrels per day

	1973	1979	1984	Change
	(mb/d)			1979–1984
Soviet Union	8,7	11,9	12,4	+4%
United States	11,0	10,1	10,4	+3%
Saudi Arabia	7,4	9,6	4,7	-51%
Mexico	0,6	1,6	3,0	+88%
Iran	5,9	3,2	2,5	-22%
UK	0,0	1,7	2,6	+53%
China	1,1	2,1	2,3	+10%
Venezuela	3,5	2,4	1,9	-21%
Canada	2,1	1,8	1,6	-11%
Indonesia	1,3	1,6	1,4	-13%
<i>OPEC</i>	30,8	26,9 ^a	17,9	-33%

Source: Flavin, C. (1985) World Oil: Coping with the Dangers of Success. Worldwatch Paper no. 66, pp. 5–66, p. 14, p. 17.

Note: ^a Data from 1980.

Table 14.2 OPEC and non-OPEC crude oil production (% of world oil)

	1973	1976	1979	1980	1981	1982
US	19.9	17.8	17.4	18.8	20.5	24.7
North Sea	0.1	1.1	3.9	4.5	5.3	6.3
Mexico	1.0	1.8	3.0	4.2	5.5	7.3
Total non-OPEC	33.0	32.6	37.1	41.0	45.9	55.4
OPEC	67.0	67.4	62.9	59.0	54.1	44.6
<i>Total (mbd)</i>	48.3	47.5	51.3	48.0	44.4	41.3

Source: Renner, M. (1984). Restructuring the World Energy Industry. Merip Reports (January), pp. 12–17, p. 25, p. 15.

In all evidence, the period ended with OPEC losing control over production levels as its share of the world oil production was shrinking to the benefit of producing regions controlled by Western companies. OPEC was also losing the power of setting prices because new market-based mechanisms were taking hold (for more details see Petrini, 2018).

1986 to 2001: the erosion of OPEC price-setting power

In subsequent years, the erosion of OPEC's price setting power – set in motion by the dynamics outlined in the preceding section – continued (also helped by OPEC's fiery internal rivalries). The counter-shock of the 1980s marked the end of the period of OPEC ascendance and the organization ceased to be a meaningful actor on the oil scene as a unitary subject. The oil price was set by forces outside OPEC's grip and OPEC could act only in a reaction mode.

The 1983–86 price slump was a result of decreasing global oil demand – a combination of improvements in energy efficiency particularly in advanced economies and a reaction to higher oil prices, in tandem with increasing non-OPEC crude oil production particularly from Mexico and the North Sea

(Maugeri, 2006). The private oil companies and the majors among them acted as the independents did in the 1950s and 1960s, playing as free riders and leaving the task of balancing the market conditions to OPEC. The outcome was a paradoxical situation, as former OPEC secretary general Fadhil Chalabi described it, in which OPEC low-cost producers were forced to cut their output while the high-cost producers in the North increased theirs.¹⁰

OPEC attempted to respond to the price decline. However, a lack of cooperation between OPEC members resulted in Saudi Arabia being the only one to take the burden and reduce its production. This approach proved soon unsustainable as the losses in Saudi oil revenues proved so large that by the end of 1985 Saudi Arabia was forced to reverse its policy, causing the oil price to collapse from \$27/b in 1985 to \$14/b in 1986. Iraq's invasion of Kuwait in August 1990 led to supply disruptions in both countries, when together they accounted for nearly 9 percent of world production. The price spike, however, was short lived because the Saudis used their substantial excess capacity, which is the largest within OPEC. In the late 1990s, following the East Asian crisis in 1997/8, crude oil prices tumbled to as low as \$13/b, largely driven by reduced demand.

All in all, the period especially the 1990s is described as the 'lost decade' for producing governments that competed fiercely for private capital. The period exhibits a significant shift in the bargaining power from the cash-strapped HGs to the IOCs – almost a U-turn away from the trend in the previous three decades.

Globally, the privatization of several NOCs in the Western world (e.g. BNO in the UK, Elf and Total in France) as well as in the former Soviet Union was notable. Fiscal arrangements were also revisited and renegotiated to reverse previous tightening. Countries like Venezuela and Iran reopened their doors to private investment, albeit to varying degrees. In the 1990s, Venezuela signed 32 risk service agreements (Duval et al., 2009). As the Iran-Iraq war in the 1980s left the Iranian oil industry in dire need of rehabilitation and the low oil price was not helping, the Iranian government introduced a new type of contractual arrangement called buyback – a sub-category of the service agreement. Under such an arrangement, the IOC was able to invest in the country's closely controlled oil sector for a limited period (five to ten years) and deliver a specific work program. Once the program was completed (for instance when production started or reached a certain target), the company handed over the project to the national Iranian oil company (NIOC) and received, in return, an agreed fixed fee in addition to recovering some of its expenses. Along similar lines, Saudi Arabia, which remains closed to private investment in its oil sector, turned to foreign investment in 1997/8 to explore its gas potential, even offering a concessionary agreement, marking the first involvement of foreign investment in the Kingdom's upstream sector since the industry was nationalized.

2001–2018: fundamental changes

The final period analyzed can be considered the compact version of the developments throughout the 1960s until 1999 in terms of changes in government take but over a much shorter period. The period also experienced fundamental changes in oil markets that may have significantly altered the traditional OPEC model and its influence over markets with implications on the IOCs. In this respect, two sub-periods can be identified here with the collapse in the oil price in summer 2014 marking the dividing line.

2001–2014: the swinging pendulum

This period was first marked by talks about the return, then the decline, of 'resource nationalism', albeit with a significantly modified characteristic compared to what the industry faced in the 1970s and 1980s. In the more 'modern' definition, resource nationalism is described as 'an umbrella term which is frequently applied to acts by host states to expropriate or change the terms on which resources are extracted, and monetized, in order to obtain greater benefits for the host state' (Clarke and Cummins, 2012). In this

respect, resource nationalism encompasses more than the nationalization of assets that marked previous periods. Revisions of fiscal and contractual arrangements that result in increases in existing tax rates, application of new taxes and increasing the share of NOCs, and expropriation of assets, have all been placed under the concept of resource nationalism since their aim is to increase the HG take. Their impact, however, is considerably different. Furthermore, while in the previous periods identified in this paper the revision of contractual arrangements focused on increasing state control over its oil resources in addition to obtaining a bigger share of the proceeds, in the later period such revisions were more focused on increasing the government take, partly because many HGs felt their control over their natural wealth was a mission accomplished.

Several factors can lead HGs to change their contractual arrangements, which define their relationship with the IOCs (for a detailed review of the factors see Mansour and Nakhle, 2016). The most obvious determinant of this pattern has been the oil price, which plays a significant role in determining the degree of bargaining power each party has at the negotiating table. As argued by Duval et al. (2009, p. 7),

The history of the oil and gas industry is characterized by the constant struggle of host countries to assert control over petroleum operations by foreign investors and to maximize their share of the economic petroleum rents from such operations without killing the golden goose that discovered and developed the gold of crude oil. As a result, contract and fiscal terms between host countries and IOCs are subject to large variations as oil and gas prices rise and fall.

The 21st century started with a recovery in oil prices, following the increase in global demand supported by a firm global economic growth and expectations of tightening oil markets (Kilian and Murphy, 2014). Between 2002 and 2008, oil prices were on an upward trend, rising from \$26/b to \$100/b over that period. Once again the surge in prices helped to shift the global balance of power away from companies in favor of the HGs. In many countries across the world – both OPEC and non-OPEC, including Angola, Argentina, China, Ecuador, India, Kazakhstan, Libya, Nigeria, and the United States (Alaska) – HGs tightened their fiscal terms to increase their take, on the grounds that they were not receiving their fair share of the increasing profitability from the oil and gas sector,¹¹ a trend described as the ‘fiscal storm’ (Wood Mackenzie, 2008). In 2006, Algeria introduced a new hydrocarbons law that imposed a new windfall tax of up to 50 percent on profits when oil prices top \$30/b and fixed the rate of participation of its NOC, Sonatrach, to a minimum rate of 51 percent. Algeria also enacted additional foreign investment rules in 2009 and 2010, further restricting foreign investment. In 2007, the government in Venezuela replaced all the then-existing terms with new contracts and imposed a majority equity share of 60 percent for its NOC, PDVSA. The late Venezuelan president, Hugo Chavez, then confronted the industry with an ‘accept it or leave it’ offer – a *déjà vu* of Libya’s ultimatum 40 years ago.

The subsequent dramatic fall in oil prices following the financial crisis in 2008, combined with funding restrictions, generated different reactions in some oil-producing countries and raised companies’ hopes for a regain of bargaining power. The former CEO of British Gas (BG), Frank Chapman, stated in 2009 that resource nationalism was on the decline, arguing that

governments the world over now need investment more than ever [...]. They know capital is in short supply the world over, they know they are competing with other countries for capital, and they know the value investors place on stability and sanctity of contracts.

(Ward, 2009, p. 33)

Indeed, some countries relaxed their fiscal terms. Even in Venezuela, officials began to solicit bids from Western oil companies, promising them access to some of the world’s largest petroleum reserves.

The industry's hope for better terms was, however, short lived. As oil prices recovered in 2010 and continued to increase, the pendulum swung again in favor of HGs. The *Financial Times* published an article in 2012 entitled '2012: The Year of Resource Nationalism?', questioning whether 2012 would be the year HGs move toward securing greater rewards from their oil sector.¹² This was triggered by the decision of then Argentinian president Cristina Fernández de Kirchner to nationalize YPF, an oil company owned by Spain's Repsol, justifying her actions as a victory for 'energy sovereignty'.¹³

The fall in oil prices in mid-2014 pushed some governments to go in the opposite direction. This however, was most notable in countries which were struggling to increase production and attract investment, and/or that rushed to significantly tighten their fiscal terms and limit foreign oil companies' access to their oil reserves during periods of high oil prices. Low oil prices exacerbate an already dire situation and prompt anxious governments to implement drastic measures to stop conditions from worsening further, especially in oil-dependent economies.

Such continuous changes in the relationship between HGs and the IOCs led some experts to describe resource nationalism as cyclical, with the oil price seen as the driving force behind the cyclicity (Clarke and Cummins, 2012). The relationship, however, is more universal than just within OPEC's arena, as the examples above show.

For a major producer such as OPEC, behind what has become shorter cyclicity reside two important developments that have affected and will continue to affect the organization's influence on oil markets and its relationship with the IOCs. The changing importance of oil in the global economy and the advent of a new and more flexible competitor – that is, tight oil in North America – have diminished OPEC's power over the market compared to the early years of its formation

In 1965, oil dominated the world primary energy mix meeting 42 percent of energy needs (Figure 14.3). Then, both oil demand and supply were very inelastic so a small change in the oil price would send a rapidly rippling effect throughout world economies. Fast forward nearly half a century later, oil's share in the global energy mix declined to 34 percent as other competing fuels, primarily natural gas, increase in popularity. Also, improvements in oil intensity – that is, the unit of oil to produce one unit of Gross Domestic Product (GDP) – have been remarkable; after peaking in 1979, oil intensity declined by half by 2015 in the world, and in the developed economies by more than 60 percent (Christof, 2016), thereby weakening the impact of oil prices on global economies.

Meanwhile, on the supply side, major changes were also notable. First, OPEC's share of world oil supply has declined significantly, from a peak of nearly 52 percent in 1972 to around 42 percent in 2017 (BP, 2018). Second, some traditional importers have become major producers. The US, which is the world's largest oil consumer, is expected to become the world's top oil producer and a net exporter by the mid/late 2020s, for the first time since the 1950s (EIA, 2018). Such a drastic turn in fortunes has been made possible thanks to the shale revolution that has swept North America since 2008, with paramount implications on global oil markets, OPEC power and IOC strategy. After reaching a peak of 9.6 mb/d in 1970, US oil production shrank steadily for four decades. This inexorable decline was only broken in 2009, when shale oil began to reach the US domestic market in large quantities and US oil exports started to reach global markets a few years later, challenging existing exporters, particularly OPEC. The first victims that the US tight oil acclaimed were OPEC's light oil producers such as Angola and Nigeria and to a lesser extent Libya, which suffered production loss following its civil war in 2010. When the first shipload of crude oil from the US to Asia left the Gulf Coast on 18 February 2018, it was hailed as the beginning of a new oil-trading era, starting a war for Asian market share between US producers and conventional exporters, especially from OPEC's Middle Eastern members.

The new challenge that the shale revolution has brought to traditional oil producers such as OPEC is not just in terms of increasing competition but also with respect to tight oil's ability to respond much more rapidly to changes in oil prices compared to conventional oil supplies. For a conventional oil project, it normally takes 7–10 years to convert investment into production, resulting in an inelastic supply that is not

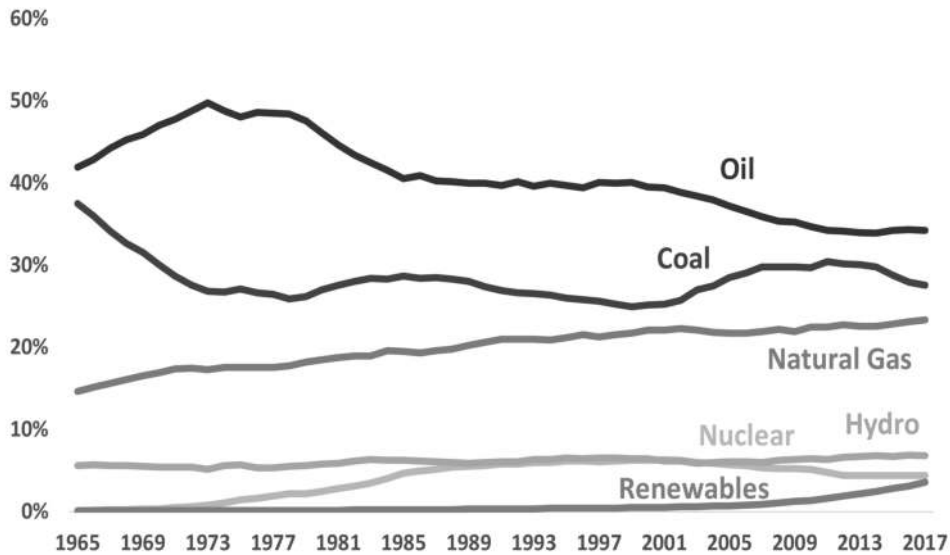


Figure 14.3 World primary energy mix (1965–2017)
 Source: BP Statistical Review of World Energy, 2018.

responsive to price changes in the short term. Tight oil is different; the lead time from investment to production has shrunk to months and output is more visibly responsive to short-term changes in prices. Not surprisingly, tight oil is capturing an increasing share of IOCs’ capital spending, primarily because it generates a much shorter payback period. Originally, investment in tight oil was primarily limited to the small independent companies in North America, but the oil majors soon followed suit and have significantly increased the share of shale in their portfolio. In addition to a rapid payback, shale has given the IOCs an attractive alternative to allocate their capital, and equally important, the option is provided in an investment-friendly environment that is primarily the US, which has some of the lowest government takes on the petroleum industry in the world. As a result, the global competition between HGs for private capital has increased and more lenient contractual terms have been offered consequently, especially following the collapse in prices in summer 2014.

2014–2018: structural changes

The shale revolution was the main driver behind the collapse in oil prices in summer 2014 and the subsequent increased competition for capital among major oil producers. Furthermore, the flexibility of shale’s production has fundamentally altered the global energy markets and challenged the existing order especially the effectiveness of OPEC in influencing oil prices. For the first time in its history, OPEC did not react to the collapse in prices, partly because it hoped the shale impact would be short lived and partly because it was dealing with a completely new situation. For two years, the oil market was entirely driven by competitive market forces with OPEC members producing at maximum capacity. However, lower oil prices proved to be too painful to handle for OPEC’s oil dependent economies especially in the light of ambitious economic reforms launched, such as Vision 2030 (in 2016) in Saudi Arabia.

In December 2016, OPEC announced a historical deal, assembling the biggest alliance in the history of the oil industry – what became known as OPEC+ – in which some non-OPEC countries joined forces with OPEC to limit production and halt prices from declining any further.¹⁴ Prior to the deal, some

commentators described OPEC as dead. The deal, however, has been successful not only in putting a floor to oil prices but also in increasing them to the region of \$70/bl. Despite this success, the challenge was so big that the OPEC+ was maintained much longer than the original plan of six months. Also, the deal received a helping hand from other unforeseen forces such as the involuntary record declines in Venezuela's oil production because of domestic political, economic and social problems.

At their June 2018 meeting, OPEC announced it would pursue a more formal relationship with non-OPEC countries, particularly Russia. If successful, such an alliance will mark the beginning of a new era for OPEC, which is likely to look very different from its past.

Meanwhile, the IOCs seem to be benefiting from the existing situation. On the one hand, the upwards pressure on oil prices courtesy of the OPEC+ deal has improved their financial situation. On the other hand, they are spoiled for choice as from the Americas to Europe and the Middle East, Africa and Asia, governments have announced and implemented reforms designed to make their country a more attractive investment proposition than elsewhere. Many HGs are offering more acreage for companies to explore and are holding more licensing rounds to optimize the chances of awarding contracts to a larger number of players. In 2018, Algeria announced new plans for tax incentives to boost investment in the oil and gas sector, while the Abu Dhabi National Oil Company (ADNOC) launched its first competitive oil and gas licensing round, offering several blocks to international bidders. Furthermore, some OPEC governments have announced the privatization of a part of their NOC's assets. In 2017, ADNOC announced it was privatizing some of its downstream assets, a strategy also contemplated by the Kuwait Petroleum Company (KPC). However, it is Saudi Aramco's initial public offering (IPO) that has captured international attention. The IPO is perhaps the most striking aspect of Saudi Arabia's major reform agenda, as postulated in Vision 2030. Saudi Aramco is the world's largest oil producer and most influential oil company in the world, supplying more than 12 percent of global demand (BP, 2018). It is also the cornerstone of the Saudi economy. The share sale of Saudi Aramco's would give investors a stake in the world's largest oil fields.

In the longer term, both OPEC and the IOCs will face the same existential threat – that is, climate change – which may bring these two players closer than ever as they share the same interest in extending the longevity of their core asset for as long as possible. The Oil and Gas Climate Initiative (OGCI) is one example. Launched in 2014, the initiative is CEO led, composed of 13 global oil and gas companies, private and state-owned alike, including: BP, Chevron, CNPC, Equinor, Eni, ExxonMobil, Oxxo, Pemex, Petrobras, Repsol, Saudi Aramco, Shell and Total, with the aim to reducing greenhouse gas (GHG) emissions through collaboration and technology.

Conclusion

The primary aim of this paper was to analyze the evolution of the relationship between OPEC and the IOCs between 1960 and 2018, with a special focus on market power and the fiscal changes that have accompanied that evolution. The paper also investigated the main factors that have triggered major changes in that relationship and in the bargaining power of the respective parties and how these are likely to evolve in the light of growing competitive forces and challenges shaping global energy markets. Although some basic features that initially triggered the changes in that relationship remain prominent to date, the relationship has come a long way since.

Looking back, two long-run dynamics that shaped the relationship between OPEC and IOCs, especially in the early years, can be identified: first, the basic nature of the oil trade is the extreme volatility demonstrated at various reprises in the history of the industry. Cycle of booms and busts are the norm: high demand, high profits, and heavy investments leading to over-production, falling profits and divestment. The industry's history can therefore be read as an attempt to find a solution to this recurring cycle through monopolistic or oligopolistic regimes. The era of the 'Seven Sisters' offered the most effective

solution in terms of price stability and profitability. However, it had a substantial cost for the producing countries in terms of dependency and loss of sovereignty over their natural resources. Some of these countries (especially Iraq and Iran) were heavily penalized to reduce the perils of overproduction.

Second, the intermeshing of politics and business in the oil industry, particularly in OPEC countries – what one could call the imperialist character of the multinational oil business. In this respect, the positions of the IOCs especially in the 1950s through to the 1970s cannot be read exclusively in economic terms; one must also consider that, to enjoy the support and protection of their parent governments, they had up to a point to act, or appear to act, as though taking into account the national interest (whatever this latter means).

Within this frame the IOCs developed a dialectical relationship with OPEC, which mixed conflict and cooperation. Undoubtedly OPEC was born to counterbalance IOCs' power in determining price and production in the international oil market. At the same time a degree of cooperation, its intensity varying in time, has always been necessary to assure the smooth working of the industry.

The formation of OPEC was part of a global trend towards giving HGs more control over their natural resources, at a time when the strategic importance of oil became more visible – a feature that remains predominant today. The first step in exercising that control was a revision in the fiscal terms. Even more than fifty years later, many developing countries reject the concessionary fiscal regime because of the early experience of HGs with arrangements that were significantly tilted in favor of the oil companies. In countries like Iraq and Iran, these arrangement contracts remain prohibited. Today, however, fiscal regimes have significantly changed and the fiscal and contractual arrangements are so sophisticated, and so often borrow features from each other, that judging on their effectiveness from their type would lead to simplistic conclusions.

While the earlier emphasis was on control and management of the sector, in addition to capturing a greater share of the value of the oil produced, the emphasis moved to the latter in more recent years. The concept of resource nationalism, which was pronounced in the 1970s, has taken a more comprehensive meaning, where expropriation of assets is only one manifestation.

The influence of OPEC on oil markets and prices, which in turn have played a major role in shaping the relationship between HGs and the IOCs, has also changed drastically, with OPEC being most influential in the early decade of its formation. The relationship between OPEC governments and companies has rarely been static. It has gone from deep asymmetry and complete openness to foreign companies' investment pre-OPEC in the 1940s and 1950s, when the IOCs dominated oil supplies under very generous concessionary terms, to the emergence of more assertive governments and their NOCs after OPEC's foundation. Some low-cost OPEC producers with giant oil and gas reserves completely nationalized their industry, though a few remain closed to IOCs' direct investment to date. Other OPEC members have allowed IOC investment but under new arrangements that secured stronger government control. Furthermore, over time the boundary between the producer countries and IOCs have become increasingly blurred, as NOCs increasingly internationalized their activities, often in partnership with the majors.

Looking ahead, changes in global energy markets, as well as political, economic and social domestic developments in major oil-producing countries, will continue to dictate the dynamics of the HG–IOC relationship and affect the bargaining power of each party and their influence over the market. The two key players are also facing a common challenge; the intensifying global fight against climate change is threatening the longevity of the oil industry and can render the value of physical oil in the ground, its ownership and control of much less significance than has been witnessed by the world through the decades of the last century and the early part of this one. Irrespective of what the future holds for the two key players – HGs and IOCs – the formation of OPEC provided HGs in the developing world with a vehicle for collective bargaining and action which in turn has shaped their relationship with the oil industry and their influence on oil markets – something that remains with us.

Notes

- 1 As an introduction to the characters of the concessionary system in the Middle East in those years, see Penrose (1971), ch. IX. On the levels of profitability of the Middle Eastern activities of the IOCs, see Issawi and Yeganeh (1962).
- 2 Early concessions granted in Kuwait were for up to 99 years. In the UAE a single onshore concession, granted in the 1930s, covered the whole of Abu Dhabi.
- 3 On the adoption of the posted price system for international oil in the early 1950s, see Penrose (1968, p. 69). The 'posted price', was determined quite arbitrarily by the companies and it was used mainly to establish the level of tax payments to producers and to transfer the crude within the vertically integrated structure of the majors. Each company had its own source of crude supply as well as the capacity to refine it. Only a tiny fraction of crude was sold outside the majors' circuit. The matter was different for product trade, where there was greater scope for market prices. On the structure of the oil industry at the middle of the 20th century remains unsurpassed, see Hartshorn (1962; on the crude pricing see pp. 130–151).
- 4 Between 1955 and 1959, the US government applied voluntary oil imports quota, which were replaced by the Mandatory Oil Import Program from 1959 to 1973. The latter was more effective at restricting oil imports, see United States Tariff Commission (1973).
- 5 Shell Briefing Service (April, 1971). Financial Needs of the Oil Industry in the 1970s.
- 6 Libya produced a low-sulphur, high-quality oil and, especially after the closure of the Suez Canal in the aftermath of the 1967 Arab-Israeli war, enjoyed a positional advantage to supply the European markets. In the early 1970s some 25% of Europe's oil supply came from Libya.
- 7 As explained by Peter Flanigan, the president's assistant in international economic affairs, the increased cost deriving from a settlement on Libya's terms 'would be passed on to consumers in Europe and Japan and, to the extent the US imports oil of and from Canada to US consumers. Since this increase would affect 100% of European and Japanese petroleum supplies and only a small per cent of US petroleum supplies, the result would be a competitive benefit to the United States' (*Foreign Relations of the United States (FRUS)*, (1969–1976), volume XXXVI, Energy Crisis, 'Memorandum for the Files by the President's Assistant for International Economic Affairs (Flanigan), RE Libyan Oil' (Washington, 29 September 1970), document 57, p. 131). As for the Europeans, they were resigned to accepting higher prices in exchange for stability of supply.
- 8 Many OPEC countries established a NOC well before the 1970s: Iran in 1948, Iraq and Algeria in 1963, but NOCs became more powerful in the 1970s.
- 9 In 1976, 40 US states removed price regulation of fuel oil; in February 1981 the Reagan administration completely liberalized petroleum pricing.
- 10 According to Chalabi, OPEC never acted as a cartel in the proper sense. In fact, a cartel, and especially one like OPEC enjoying the lowest cost of production in the industry, would have operated with a view of defending its market share, crowding out the most dangerous competitors from the market through an aggressive price policy. OPEC never did so, at least not in a systematic and coherent way. This was for a variety of reasons, not least because OPEC was born with the precise task of defending the price level and was thus consubstantially averse to price reductions (Chalabi, 2010, p. 242).
- 11 *The Economist* (2007). Barking Louder, Biting Less. *The Economist*, 8 March.
- 12 Minto, R. (2012). The Year of Resource Nationalism? *The Financial Times*, 18 January.
- 13 *The Economist* (2013). Flogging a Dead Cow. *The Economist*, 27 July.
- 14 On 30 November 2016, OPEC announced a coordinated production cut of approximately 1.2 Mbl/d, limiting its production to around 32 Mbl/d. A week later, ten non-OPEC members, led by Russia, also committed to reducing their combined output by an additional 600,000 bl per day, bringing the total cuts to 1.8 Mbl/d, effective as of January 2017.

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Ignoring, countering and undercutting OPEC

Britain, BP, Shell and the shifting global energy order (1960–1986)

Jonathan Kuiken

In the wake of the 1973 oil crisis, the Organization of Petroleum Exporting Countries (OPEC) became a favorite villain for British political cartoonists. Cartoon representatives of OPEC, almost invariably portrayed as stereotypically orientalist caricatures, were shown as greedy, devious and, most importantly, powerful. Western leaders, in contrast, were depicted as weak, groveling and in many cases literally bowing to the all-powerful might of OPEC.¹ Yet some cartoons of British leaders in the mid-to-late 1970s showed a slightly different image. Prime ministers Harold Wilson and James Callaghan were represented in a similar fashion to the OPEC leaders, wearing keffiyehs and other garb meant to mark them out as ‘Middle Eastern’. Still another cartoon used a similar motif, although this time it was a group of Scots combining keffiyehs with kilts.²

These British characters dressed in orientalist garb were meant to mock the pretensions of various leaders regarding the potential wealth and power represented by the production of North Sea oil. Although these crude caricatures were in no way meant to flatter the leaders of OPEC or of Britain, they do inadvertently represent a changing balance in the relationship between the two sides. When North Sea oil began to flow in 1975, Britain’s association with OPEC started to shift and become more complex. While this new oil province would not make the UK or its companies completely independent of OPEC oil, it did help to slow Britain’s declining influence in international oil matters and gave the country a relatively small but still significant voice in matters of international oil – a fact that would be demonstrated by Britain’s refusal to cut production during the 1986 oil counter-shock against the wishes of OPEC.

This turning of the tables was a far cry from 26 years earlier when OPEC was founded in response to the unilateral cut to the posted price of oil initiated by the major Western oil companies. Britain, along with its two domestically based oil companies BP and Shell, had resolved then to ignore the organization and let it collapse due to what they assumed would be intractable differences of opinion between the various member states. This early approach set off the first of three stages in Britain’s approach to OPEC during the crucial period from the founding of OPEC in 1960 until the oil counter-shock of 1986. During this period of transition in the international oil industry, British policy quickly evolved from a strategy of ignoring OPEC to one of actively countering the organization before finally settling into a position of antagonistic accommodation.

Key to this evolution in British policy were two parallel developments. The first was the changing position of BP, Shell and the other international oil majors as they gradually conceded control over pricing and production to the oil-producing states. The second was the discovery and eventual production of oil in the North Sea. Equally important, however, is the fact that the transitions between these policy stages were not clear-cut or smooth. British oil policy was shaped by a complex interaction of interests between businesses, bureaucrats and politicians with extremely different views on the future of the British economy. These various groups were as likely to work against one another as they were to cooperate. This chapter will therefore explore the evolution of British policy through these three stages with a focus on how broader transitions in the international oil industry coupled with the development of North Sea oil turned Britain from a haughty to a fearful opponent before finally transforming into an unfriendly fellow-traveler with OPEC.

Multipolar policy-making

The complex nature of oil policy decision-making in Britain stems from the equally complex relationship that it maintained with its two primary oil companies, BP and Shell. Prior to the late 1950s, Britain relied nearly entirely on these two businesses to manage the nation's oil supply, and the nature of the government's connection with the firms was somewhat unique compared with its dealings with other, mainly American, international oil companies.

In the case of BP, the British Treasury had owned roughly 51 percent of the firm since 1914, giving rise to the common perception that BP was a 'nationalized' company. Yet when the purchase was made, the Treasury and the company came to a mutual understanding which was laid out in a document known as the Bradbury Letter, stating that the government would not interfere in the day-to-day operations of the firm (Ferrier, 1982).

While not as formal as the connections between BP and Whitehall, Shell's relationship with the British Government was still significant. Although Shell was part of the larger company, Royal-Dutch Shell, which was 60 percent Dutch-owned, the company had taken refuge in Britain during the Second World War and after the struggle had signed the Shell-Treasury Agreement of 1946. This agreement gave Shell access to Britain's foreign exchange services in exchange for keeping its accounts in pounds sterling and giving British Treasury oversight of Shell's foreign investments.³

Interaction between the two companies and the British Government was not limited to the Treasury however. For domestic oil and energy concerns, the two firms dealt with the Ministry of Power (MoP), while the international nature of the industry meant that the Foreign Office (the Foreign and Commonwealth Office post-1967) also played a large role in oil matters. To ensure the smooth and stable flow of oil that the MoP desired, the FO encouraged the companies to maintain good relations with the oil-producing states, particularly in the Middle East. The Treasury, for its part, saw these concerns as being subjugated to the overwhelming priority of most post-war British governments, the maintenance of a healthy balance of payments. While these three priorities were not always mutually exclusive, they translated into Whitehall's advice to BP and Shell being sometimes weak and contradictory.

Ignoring OPEC

It was precisely this lack of coordination that began to concern some members of the British civil service in the late 1950s. In the wake of the Suez Crisis of 1956 and the Iraqi Revolution of 1958, a potent and volatile mixture of nationalism and oil politics in the Middle East led the FO to urge BP and Shell to moderate their activities in the region. These warnings were ignored, however. On 13 February 1959 BP announced a unilateral cut in the posted price of their oil. In a press release, BP stated that the move

'reflects the downward trend internationally in the market for Crude Oil under the pressure of very plentiful supplies'.⁴ The other major companies followed suit shortly thereafter.

This was precisely the type of act that the Foreign Office had warned against. Realizing that the determination of the companies to act according to purely commercial considerations ran the risk of doing further political damage, civil servants in Whitehall convinced BP, along with Shell, to begin holding regular monthly meetings with officials to discuss the coordination of activities in the Middle East. They code-named these secret meetings 'tea parties' and their plan was to create a more coherent approach towards oil matters – a goal that quickly proved overly ambitious. Despite their initial price cuts, the companies were still being forced to sell their oil at a discount. On 9 August 1960 Standard Oil of New Jersey (Exxon) initiated further reductions in the posted price. Anger at this second round of cuts galvanized the oil-producing states into action leading to the creation of OPEC on 14 September 1960.

The initial response by both the British Government and its oil companies to the creation of OPEC was muted. Writing in January of 1961, JE Lucas, a Treasury oil specialist, spelled out what was to become Britain's policy towards OPEC by stating: 'the general policy of the oil companies and the Governments of consuming countries should be to refrain from comment and, in particular, not to express any opposition'.⁵ Maurice Bridgeman, the chairman of BP, echoed this sentiment, noting that 'the quieter the oil companies kept about OPEC the better,' before adding, 'there was a reasonable chance that OPEC might become ineffective as a result of internal stresses'.⁶

OPEC seemed to oblige the oil companies' lack of concern in the first two years of its existence, choosing to focus on structural and organizational matters (Bamberg, 2000). Internal divisions were also acute. The prospective invasion of Kuwait by Iraq in 1961 even threatened to destroy the organization before it had fully formed. Yet the very existence of OPEC gave the producing states a better negotiating position when it came to discussions of prices and the 50/50 principle of profit-sharing.

Growing concern

The blasé attitude taken by the British during OPEC's formative years began to shift in 1962 when the organization's two-yearly conferences resulted in resolutions seeking to redress some of the revenue imbalance brought about by the price cuts of 1959 and 1960. A Whitehall report on the issue, however, stated optimistically that 'dissensions between members or success by the oil companies in dealing separately with some of them could lead to a weakening of the organization'.⁷

Despite this skepticism there was enough concern to prompt a new strategy to encourage a split between the moderate and radical members of OPEC. To do this, the companies proposed striking better deals with moderate states, such as Iran, to show that cooperation with the oil industry would bring more tangible benefits than taking a radical course (Bamberg, 2000).

In late October 1962, Maurice Bridgeman, representing the Iranian Consortium, visited Iran in order to work towards a deal. Bridgeman had known the Shah for years and, through talks with the Iranian prime minister Asadollah Alam, did all he could to guarantee Iran special treatment if the country led the resistance against the radical elements within OPEC. The vague assurances given by Bridgeman were taken at face value by the Iranians, so much so that the Shah let it be known that he was not averse to the idea of Iran leaving OPEC altogether.⁸ The FO was alarmed by this idea, but generally pleased with the brake that it had put on the country's willingness to be OPEC's 'spearhead'.⁹

But the Shah's inclination to cooperate did not mean that negotiations with Iran regarding changes to the concessionary agreement would be easy. Fuad Rouhani, the chief Iranian negotiator and head of OPEC, forced the companies to cross the line regarding the 50/50 profit-sharing scheme. When negotiations picked up steam in late 1963, the companies also agreed in principle to the concept of royalty expensing with the Iranians. In return, the Consortium won a largely symbolic victory by convincing the

Shah to give up a return of the posted price to its pre-1959 level as well as encouraging the Iranians to oppose the idea of a pro-rationing scheme (Parra, 2004, pp. 100–105; Rubino, 2008, p. 236).

As had been hoped, the Iranians encouraged the other moderate OPEC members, Libya, Saudi Arabia, Kuwait and Qatar, to agree to similar deals as well.¹⁰ The companies thus came out of the 1962–1965 negotiations feeling that they had made the best of a bad situation. Even so, there was a deep concern that these negotiations marked only the beginning of a new era of OPEC strength. During a meeting with US officials, John Kelly of the US Department of the Interior conceded that ‘We can no longer brush OPEC under the rug.’¹¹

This growing importance and the inherent instability of OPEC were both demonstrated in 1967 during the Six Day War. During the conflict Arab oil ministers agreed to an embargo against the United States, Britain and West Germany, cutting back production by 60 percent (Yergin, 2008). This desperate situation caused temporary panic in Whitehall. But unlike during the Suez Crisis, Britain did not end up facing oil shortages (Thorpe, 2007). Thanks to a combination of increased supplies from non-Arab OPEC members along with ramped-up US production, Britain was able to escape any serious disruption. But it was a Pyrrhic victory. The Arab embargo coupled with the civil war in Nigeria had knocked out much of the world’s ‘sterling’ oil (Galpern, 2009). This financial hit contributed to the decision of the Labour Government of Harold Wilson to devalue the British pound in November 1967. This devaluation was a huge blow for BP and Shell as well as for the Gulf states who kept a large portion of their reserves in sterling. A further shock to these countries came when Prime Minister Harold Wilson announced on 16 January 1968 that British forces would be withdrawing from their bases east of Suez by 1971.

Countering OPEC

The strategic retreat from the Gulf also marked a key transition in how Britain viewed OPEC and the means by which further changes to the oil industry could be resisted. Despite being a failure, the 1967 embargo gave British policy-makers a chilling taste of the power of the oil producers. It also, however, reflected the potential differences within OPEC that could be exploited. The goal therefore became one of creating a system by which Britain, its companies and its allies could resist pressure from OPEC regarding concessionary terms, price increases or participation in production for long enough that differences within the organization would weaken their negotiating position.

Proponents of this vision were initially optimistic that the humiliation of the Arab members of OPEC caused by the failure of the embargo might break the organization apart. But as OPEC recovered from the incident, it began to reconsolidate around a new set of objectives focused on taking sovereign control over their oil as well as the ability to set its price. More aggressive thinkers advocated for direct nationalization of the international oil companies’ holdings in OPEC territory, while more cautious strategists such as the Saudi oil minister Zaki Yamani began to push the idea of gradual ‘participation’ in oil production in partnership with the Western firms (Yamani 1969, p. 4).

All of this was deeply concerning to the British. The thought of ceding control over production to the oil producers was both strategically and financially worrying. This alarm only grew when Algeria joined OPEC in 1969, the same year that pro-Western King Idris of Libya was toppled by the decidedly anti-Western Muammar Gaddafi. These developments seemed to swing the entire organization closer towards the aggressive positions advocated by those in favor of nationalization.

Adding to the concern was that demand for oil throughout the Organization for Economic Cooperation and Development (OECD) was increasing to such an extent that the previously existing oil surplus was gone. This created a situation by the early 1970s where even a single oil producer could exercise out-sized influence over the industry. Just such a thing occurred when Gaddafi unilaterally forced the renegotiation of several oil concessions in 1970 (Skeet, 1988). This was followed by a more extensive series of negotiations as other members of OPEC sought to gain better terms, resulting in the Tehran and Tripoli

agreements in 1971. These deals were acknowledged as being defeats for the international oil companies as they not only increased the price of oil, but crucially gave the producers the right to ‘participate’ in the production of oil in their own territory (Skeet, 1988, pp. 66–88).

During a Whitehall post-mortem on these defeats, Anthony Fish, a government oil specialist, voiced a growing concern about the position of BP, Shell and the other international oil companies, writing,

what we should recognize about the position of the majors is the difference between increasing OPEC ‘take’ and OPEC participation demands. Demands along the former lines leave the majors very much in the same camp as the consumers, but participation would make the majors’ position more ambiguous.¹²

With the reliability of the major oil companies in doubt, government officials wrestled with ways in which to support the firms in the hopes of keeping them on side. To do this, they solicited requests from the companies. The chairman of BP, Sir Eric Drake, suggested in a memorandum to the Department of Trade and Industry that BP’s international position would be greatly aided by a safe, low-tax, foundational operation in the North Sea where BP had made a major oil discovery in 1969 followed in 1970 by another discovery by Shell.¹³ The Foreign and Commonwealth Office (FCO) even suggested that North Sea oil would be a major ‘positive negotiating factor available to the Europeans in negotiations with the Middle East producers on oil supplies and prices’.¹⁴

Even with this bolstered position, some officials continued to doubt that BP and Shell would fight for Britain if it meant jeopardizing their Middle East concessions. Therefore, other approaches to countering OPEC were floated. One such idea involved direct communication with OPEC on the part of the British Government with Lord Victor Rothschild noting to the Prime Minister’s office that ‘sooner or later, we, Western Europe and the USA will find it impossible entirely to leave negotiations with the oil producing countries to the oil companies’.¹⁵ The idea of government involvement had several different forms, but most revolved around some sort of negotiated framework between consumers and producers that would dictate acceptable price increases and guarantee contracts.

But even this idea was resisted both by the companies and in some corners of Whitehall. In a speech to an industry group, Sir David Barran of Shell argued that ‘If heat is generated in company/government negotiations it is ostensibly commercial heat, a less explosive commodity than the political heat of government-to-government confrontation.’¹⁶ Some groups in the government agreed with this sentiment, feeling that any move on the part of Britain would be doomed to failure if it was not backed by all the other major consumers. Out of this emerged the idea that the government could ensure the stability and price of their supplies by encouraging the development of a united front of consuming nations.

But constructing such a front presented its own difficulties. For example, existing OECD oil-sharing arrangements would actually bring Britain less oil when North Sea oil came online than going it alone would supply. The same could be said for ongoing discussions within the European Community, which Britain was due to join in January 1973, regarding a joint-EC approach to oil sharing. Entry into any EC arrangement carried with it the additional risk of losing complete control over North Sea oil.¹⁷

This inconvenient reality renewed the idea that the best way to protect against an oil shortage was to prevent one in the first place by moving consumer cooperation beyond simple oil-sharing agreements and towards the creation of a consumer bloc. The Central Policy Review Staff (CPRS), an organization set up by Prime Minister Edward Heath after his electoral victory in 1970, had perhaps the most visionary approach to this problem, arguing for a plan that would ‘bring importing States and the oil companies together in a single, two-tier organization (OPIC – the Organisation of Petroleum Importing Countries), for the purpose of coordinating State and company action’.¹⁸ The CPRS argued that the main flaw with the other proposals was that the oil companies were unable to coordinate more closely with one another on account of US anti-trust laws, a problem that an OPIC which could coordinate state and company

strategy would solve. The FCO, however, was not so sure. In a letter to Cabinet Secretary Burke Trend discussing the idea, the FCO's John Hunt commented that 'this is an interesting idea but completely unnegotiable'.¹⁹

The struggles to come up with concrete solutions did not mitigate growing concern within Whitehall. On a visit to Britain in June 1973 the oil analyst Walter J. Levy met privately with Heath, encouraging him that it was 'high time that the governments of consuming countries took a much more active and concerted interest in negotiations with the oil-producing countries'.²⁰ But Levy's advice also came with a warning when he admitted that Yamani had cautioned him that 'if the governments of the consuming countries formed a united organization to deal with OPEC, that would mean war'.²¹

The threat of OPEC retaliation was one that Heath took seriously. Britain's position between Europe and the US put the country in a strong position to coordinate the creation of a consumer bloc, but the fear of being too far out at the head of such a movement worried Heath. The British therefore sought to build a broader movement towards cooperation, first within the EC, which, it was hoped, would form a kernel that a broader OECD group could be built around. Heath wanted to widen this process since he feared 'that the Arab oil producing states would come to learn of the suggestion we have made,' and 'that the British Government would appear to the Arabs as advocating a hard line in relations with them'.²²

The problem with including the other major EC powers into the process of consumer cooperation was that it slowed the entire effort. A Nixon administration official, Peter G. Peterson, reported that he 'had detected very different attitudes depending on the way in which oil affairs were organized in each country'.²³ Even in areas where compromise was possible, the process was still tortuous and glacially slow. The summer of 1973 was therefore a period of fruitless talks and meetings. This led one exasperated official to write to his colleagues that 'much effort has been expended in Whitehall with remarkably little to show for it'.²⁴ Heath himself made this clear in a letter to BP's Drake, writing: 'I very much share your views on the need for urgent action by the EEC, the USA and Japan.' But he added that 'we must proceed circumspectly if we are to avoid the risks and consequences of exposing ourselves as the instigators of a common anti-OPEC front, or of moving too far in directions which could jeopardize our control of the North Sea'.²⁵

Heath, for his part, made one last attempt to prepare British oil policy for an eventual showdown with members of OPEC. In June, he ordered the creation of a new Oil Supply Task Force which was commissioned 'to keep under review any developments threatening to interrupt supplies of oil' and 'to consider measures to be taken to anticipate, or to deal with, such interruptions'.²⁶ Unfortunately for Heath and for Britain, the task force barely had time to organize itself before the serious crisis that had been forecast erupted.

Antagonistic accommodation

When the OPEC states dramatically seized control of oil pricing at their October 1973 meeting, Britain's position began to fundamentally change. While the initial response to the price increase, combined with an embargo of the United States and the Netherlands put in place by the Arab oil producers, could be charitably characterized as complete panic, the events also clarified for Whitehall the fact that going to war with OPEC producers would be counterproductive. The disruptions of the 1973 oil crisis and growing producer participation convinced British officials of two major points. First, Whitehall began to see the oil companies as truly international entities operating between the interests of Britain and those of OPEC. And second, officials grew more determined that North Sea oil, produced by those companies, would be an essential and reliable safeguard against future shortages. These beliefs weighed heavily on the minds of British diplomats at the Copenhagen Summit of the EC, held in December 1973 and the Washington Conference of 1974, where Britain continued to push for consumer cooperation but also remained deeply mindful of the need to do everything possible to protect their ability to control their developing North Sea oil assets.

At Washington, this meant arguing for stronger consumer cooperation while resisting arrangements that would have bound Britain to any strict resource pooling.²⁷ These negotiations mostly went Britain's way, but Heath's Conservatives had little time to celebrate this success. Shortly after the conference, a general election resulted in a Labour government, once again led by Harold Wilson. Despite this change in leadership, Britain remained committed to the consumer cooperation outlined at the Washington Conference. When a final agreement was struck in November 1974 for an International Energy Program (IEP) that would result in the creation of an International Energy Agency (IEA), British officials and BP and Shell were satisfied.²⁸ The IEP document envisioned the IEA working in concert with the international oil industry to regulate the allocation of supply and to keep track of price and supply trends.

By making the oil companies facilitators of the IEA sharing plan, the agreement effectively preserved much of the companies' traditional role. Although the foundation of the old integrated system, the long-term concessions in the Middle East, was crumbling, the companies were in a position to readjust. But that repositioning was challenged by political changes in Britain. The Labour Government which had come to power in 1974 had cooperated with the United States in the creation of the IEA but, even while officials worked to secure BP and Shell's role as international companies, Wilson's Cabinet was simultaneously laying plans to take greater control over Britain's North Sea oil resources.²⁹

OPEC's moves to seize a participation stake in their own oil industries appeared on the surface to have a common cause with the statist ideology of the Labour Government. But despite sharing similar rhetoric to some OPEC oil ministers, Labour's plans were complicated by the same split between moderate and radical factions within the party that many of their other economic goals would fall prey to. This is epitomized most clearly by the two Secretaries of Energy who occupied the post during this government's term in office, the moderate Eric Varley and the decidedly radical Tony Benn (Boué, 2016, p. 237).

In 1974, Varley was tasked with the mission of determining the best way to maximize government control over the oil found in British territory. His officials drew up a plan for a profits tax on North Sea production and recommended that the government should 'as a rule seek at least 51 per cent participation in all commercial oil fields under both new and existing licenses in the North Sea'.³⁰ How to achieve these goals brought OPEC back into the picture. OPEC's success against the international oil industry provided an inspiration but was also a caution. The oil analyst Levy warned the government that acting too aggressively in the North Sea 'might provoke the OPEC countries (even if they are going to do this in the long run anyway) to make an early move against the very large profits the companies still earn there'.³¹ Likewise, unilaterally changing the terms of licenses could be 'represented as close to nationalization', making the British Government look hypocritical for resisting similar moves by OPEC states against BP and Shell's concessions elsewhere.³²

Therefore, how exactly the British Government would 'participate' in the North Sea oil industry was a major question. Britain's traditional liberal approach to oil dictated a light touch, but the gains made by the national companies in the OPEC states seemed to offer an alternative model. After briefly considering using BP as an agent to handle Britain's participation oil, Varley proposed a middle course in between the liberal and interventionist approach. This was a plan to create a new body 'to be called the British National Oil Corporation (BNOC) – whose functions and constitution we can tailor to meet our needs'.³³

What the end result of this tailoring would be was a matter of debate. The division within Whitehall and the Cabinet was between those who wanted BNOC to serve as something closer to a holding company and those that wanted to create a truly national operating company. During a Cabinet shake-up in 1975, Wilson shifted a thinker of the latter bent into the post of energy secretary – the inveterate left-winger Tony Benn. Benn was determined to make BNOC a fully functioning oil company that would compete with internationals such as BP and Shell for the benefit of Britain. This even included a plan that would merge BP's UK assets including oil fields, pipelines, refineries and distribution networks with BNOC. In return, the government would sell its shares in the remaining aspects of BP – effectively asking the company to sacrifice its British holdings in order to become a truly independent international

company. Benn was of course very supportive of the idea, but Wilson was non-committal. For his part, Monty Pennell of BP argued that the plan ‘would amount to a “disemboweling” of the company’.³⁴

The radical idea of creating a BNOc that could stand alongside the ranks of the NIOC or Aramco met its end when Britain was forced to seek a bailout from the International Monetary Fund in 1976.³⁵ Regardless of this shift, the creation of BNOc and the fact that multiple wells were now producing in the North Sea meant that Britain’s relationship to oil prices were shifting. While officials still wanted stable prices, Britain perhaps more than most other members of the OECD was now more favorably disposed to OPEC’s ability to maintain that stability at a higher price point.

This came into play most dramatically in late 1978 during the early stages of the Iranian Revolution. The weakening position of the Shah in Iran had destabilized the oil markets and Iranian production had dropped.³⁶ The jittery spot market soon recorded huge increases in prices for oil. BNOc exacerbated this trend by increasing the price of North Sea oil by 11 percent in December 1978 to bring posted prices more in line with the spot market. This removed all restraint from OPEC and soon led to an unorganized increase of prices across the board (Parra, 2012, p. 221). The second oil shock would eventually send prices from around \$13 to \$34 a barrel.

Turning the tables

The crisis surrounding the price increases and supply fears had profound consequences for Britain’s North Sea oil production – and, in the long run, for OPEC itself. In the midst of the crisis the 1979 general election in Britain saw Margaret Thatcher’s Conservative Party returned to power. Thatcher sought to increase private investment in the North Sea at a time when high prices were already stimulating increased exploration and production efforts in the area. The combined effect of this would be to see a boost in North Sea oil production in the early-to-mid 1980s at exactly the time that OPEC was attempting to rein in overproduction.

Thatcher’s moves to reconfigure the British Government’s relationship to North Sea oil began in her first few weeks in power when she ordered that a thorough review of BNOc and its activities.³⁷ Thatcher made her own views crystal clear to the new secretary for energy, David Howell. During their first meeting, Thatcher informed Howell that she saw no value in BNOc. She recognized that for contractual reasons she could not abolish the organization outright, but she also ‘would prefer to dismember it’.³⁸ This sentiment was strengthened by the fact that during the second oil shock, Britain experienced gasoline shortages despite the high levels of production from the North Sea and the large amounts of oil being handled by BNOc (Hoopes, 1997, p. 34).

The result of the review process therefore sought ways of winding down BNOc’s operations in a way that would not give the appearance of selling off Britain’s important national asset. Thatcher, Howell and Chancellor of the Exchequer Nigel Lawson favored splitting BNOc into its production wing and trading and advising wing. The thought process behind this was that the production wing was not only the most profitable and therefore the most attractive for privatization, but that the retention of a rump BNOc would keep some government interest in the North Sea and would leave the government in control of the participation oil from existing licenses. The task of completing this split was complex, however, and it was not until 1982 that the production wing of BNOc, renamed Britoil, was partially sold off to investors – a process that was completed with a second sale in 1985.³⁹

The initial sale of Britoil shares in 1982 was a bit disappointing in large part because the period from 1979 until 1982 had already seen large investments made in expanding North Sea production to take advantage of the OPEC-driven price increases. That Britain could benefit from OPEC’s price increases was reflected in the Thatcher government’s initial mildly cooperative attitude towards the organization. Howell reflected this potential relationship in an interview with *The Christian Science Monitor* in August 1980 where he stated that ‘the old idea of OPEC-bashing has proved an absolutely fruitless course,’ going on to add

that the most important thing in regard to prices was ‘to see that their evolution is stable and not erratic’.⁴⁰ Ironically, it would be Britain and the companies operating in the North Sea that would significantly contribute to unstable and erratic price decreases over the next five years.

That prices could fall, and fall quickly, came as a surprise to many. However, the fact of the matter was that the price spikes in the 1970s were a result of political circumstances and the perception rather than the reality of shortage. In fact, production had continued to increase with OPEC reaching a new peak in 1979. The problem for OPEC was that non-OPEC production was also growing – a sector in which North Sea oil would play a prominent role. By early 1980 Britain had reached near self-sufficiency in oil from their domestic sources and had begun to contribute increasing production output to the international spot market. This was part of a spectacular reversal in fortunes for the OECD states as efforts to reduce consumption, boost alternative fuels and encourage new sources of supply such as Alaska and the North Sea all began to bear fruit.

Prices remained relatively high during the first years of the 1980s, due in part to the production decreases caused by the Iran-Iraq War, but the underlying trends were moving against OPEC. By 1982, weakening demand and overproduction put unsustainable pressure on prices. After a series of producers began cutting their prices, BNOC was pressured by the firms operating in the North Sea to similarly reduce prices in early 1982. This gave rise to an unofficial policy within Whitehall that North Sea oil prices should be one of ‘following, not leading, the market’.⁴¹ Attempts, led mainly by Saudi Arabia, throughout 1982 to encourage production levels consistent with a desire to maintain prices at roughly \$34 a barrel were undercut by some other OPEC members selling their oil at discounted prices.

The Saudis and other proponents of higher prices were forced to give way due to this pressure as well as another large BNOC price cut in March 1983. Efforts at stabilizing the situation through the London Agreement of 1983 worked for a short while but proved fruitless as internal pressures, a rapidly changing market and competition all militated against a united OPEC line. North Sea oil played a large part in this, not only because of its role in the spot market but also due to the fact that it was a major competitor to Nigeria’s light crude making it difficult for Nigeria to abide by any strict OPEC plan (Parra, 2012, pp. 280–281). The British Government actually did attempt to restrain price competition between North Sea oil and OPEC sources in an effort to allow the London Agreement to take root, but this effort collapsed by October 1983 when Norway’s Statoil announced that its prices would be fixed to the spot market, forcing BNOC to cut prices again (Skeet, 1988, pp. 198–199).

This situation revealed an awkward fact for both Whitehall and BNOC. Using BNOC to support higher oil prices meant that the government was simply perpetuating a growing problem for the organization, which was that it was being forced to sell oil at a loss in order to move the large quantities of participation oil it was acquiring at fixed posted prices.⁴² The increasing losses for BNOC were not only an embarrassment for the Thatcher government but was also demonstrative of the reality that keeping prices artificially high was doomed to failure. As such, the British began to play an increasingly antagonistic role to OPEC’s efforts to fight the price collapse.

The most obvious signal in this regard came in 1985 when the government announced that BNOC itself was to be abolished. This process was formalized in March 1986 when BNOC was replaced with a regulatory agency known as the Oil and Pipelines Agency.⁴³ From the time of the announcement of BNOC’s imminent demise in 1985, Britain gave up pricing its oil according to any artificial point and instead began relying solely on the market to determine value. This left only production levels as a tool to support OPEC’s efforts to bolster higher prices, but here too the British turned the tables on their previous tacit support for their oil-producing brethren.

As Britain began the process of dismantling BNOC, OPEC was also undergoing a major struggle. When Saudi Arabia announced in mid-1985 that it would be abandoning its role as a swing producer and would seek to regain market share, prices began to sink even faster. The growing crisis placed Britain and its fellow North Sea producer, Norway, in an interesting position. When OPEC representatives asked

Britain's secretary of energy, Peter Walker, to order production cutbacks in the North Sea to support OPEC's new policy, the British minister politely declined.⁴⁴ Rampant production in the North Sea combined with increased Saudi production turned the declining prices into a collapse, sometimes called the counter-shock, by 1986. The bottoming out of prices at nearly \$8 a barrel forced OPEC to turn back to a rough quota system to stave off disaster and severely traumatized the organization.

Conclusion

The evolution of the international oil industry from 1960 to 1986 was a story of rising and falling fortunes in terms of wealth, prestige and power for the oil companies, their parent governments and the oil-producing states. The long struggle on the part of Western states such as Britain and its companies to resist the loss of concessions, pricing control and other key perks of the oil industry had led to confrontation and consternation, periods of cooperation and ultimately adjustment to a new international system for oil production, transportation and sale. The transformation of BP and Shell as well as the other oil majors, combined with the emergence of the North Sea as a major oil province, eased this transition for Britain, bringing about a situation where the country's relationship with OPEC could reach a point of wary coexistence. While jokes made in the early 1980s of Britain being a secret member of the organization were off the mark, they do represent the fact that the United Kingdom played a crucial part in the existence of OPEC from its earliest days to its darkest hour.

Notes

- 1 Numerous examples can be found at the University of Kent's British Cartoon Archive. Available from: <https://archive.cartoons.ac.uk>.
- 2 See for example Cummings, M. (1977). Oh dear! Bad news – there's some good news. *Daily Express*, 5 July.
- 3 *The National Archives of the United Kingdom*. T 236/6129. 'Shell-Treasury Agreement'. Treasury: Overseas Finance Division.
- 4 *National Archives of the United Kingdom*. FO 371/141194. 'Note to Editor, 12 February 1959'.
- 5 *National Archives of the United Kingdom*. T 236/6443. 'OPEC, 3 March 1961'.
- 6 *National Archives of the United Kingdom*. T 236/6443. 'Organisation of Petroleum Exporting Countries, 5 April 1961'.
- 7 *National Archives of the United Kingdom*. FO 371/164605. 'Middle East Oil Report 1962'.
- 8 While Bridgeman made few concrete promises, he did imply that BP and other members of the Consortium would help Iran establish the lines of credit necessary to finance several major infrastructure projects. He also promised to boost production by 10% annually if the Shah's government continued to cooperate (TNA, FO 371/164604).
- 9 *National Archives of the United Kingdom*. FO 371/164604. 'Record of a Meeting with Shell and B.P. held in the Foreign Office 13 December 1962'.
- 10 *National Archives of the United Kingdom*. FO 371/183512. 'O.P.E.C, 15 January 1965' and 'Shell Paper on O.P.E.C. Negotiations, 26 January 1965'.
- 11 *Foreign Relations of the United States (1964–1968)*, volume XXXIV, document 176. Energy Diplomacy and Global Issues, 'Memorandum of Conversation, 29 January 1964'.
- 12 *National Archives of the United Kingdom*. CAB 184/10. 'Letter Fish to Mayne, 4 November 1971'.
- 13 For a detailed account of the early steps towards North Sea oil and gas exploration see Kemp (2012a). *National Archives of the United Kingdom*. T 317/2004. 'The Drake Memorandum, 20 October 1972'.
- 14 *National Archives of the United Kingdom*. FCO 67/751. 'Oil from the UK Continental Shelf: International aspects, 12 April 1972'.
- 15 *National Archives of the United Kingdom*. PREM 15/595. 'Minute Rothschild to Armstrong, 1 December 1971'.
- 16 *National Archives of the United Kingdom*. PREM 15/595. 'The Need for a National Fuel Policy? 1 October 1971'.
- 17 *National Archives of the United Kingdom*. CAB 130/610. 'The OECD and EEC Sharing Out Arrangements, 25 September 1972'.
- 18 *National Archives of the United Kingdom*. CAB 130/610. 'Collective Defence Against Collective Attack (OPIC), 28 September 1972'.

- 19 *National Archives of the United Kingdom*. CAB 164/1196. 'Letter from Hunt to Trend, 19 September 1972'.
- 20 *National Archives of the United Kingdom*. PREM 15/1837. 'Meeting between Walter Levy and Prime Minister, 19 June 1973'.
- 21 *National Archives of the United Kingdom*. PREM 15/1837. 'Meeting between Walter Levy and Prime Minister, 19 June 1973'.
- 22 *National Archives of the United Kingdom*. CAB 164/1197. 'Letter From Bridges to Alexander, 10 May 1973'.
- 23 *National Archives of the United Kingdom*. CAB 164/1197. 'Secretary of State's Meeting with Ambassador Peter G Peterson, 24 February 1973'.
- 24 *National Archives of the United Kingdom*. PREM 15/1837. 'Letter from Marshall to Greenhill, 31 August 1973'.
- 25 *National Archives of the United Kingdom*. PREM 15/1837. 'Letter from Heath to Drake, 10 August 1973'.
- 26 *National Archives of the United Kingdom*. CAB 164/1197. 'Letter from Trend to Heath, 6 June 1973'.
- 27 *National Archives of the United Kingdom*. FCO 96/86. 'Report from Sykes to Douglas-Home, 27 February 1974'.
- 28 BP and Shell were cautiously supportive of the goals of the IEA (*National Archives of the United Kingdom*. FCO 96/3. 'Record of a Meeting Held at the FCO on 20 May, May 1974').
- 29 For the impact of the 1973 oil crisis on Britain's fiscal policies in regards to North Sea oil, see Boué (2016) and Kemp (2012b).
- 30 *National Archives of the United Kingdom*. CAB 134/3748. 'FNO (74) 5th Meeting: Minutes of a Meeting on Friday 17 May 1974'.
- 31 *National Archives of the United Kingdom*. PREM 15/1467. 'North Sea Oil: Note by Officials, 31 August 1973'.
- 32 *National Archives of the United Kingdom*. PREM 15/1467. 'North Sea Oil: Note by Officials, 31 August 1973'.
- 33 *National Archives of the United Kingdom*. PREM 15/1467. 'North Sea Oil: Note by Officials, 31 August 1973'.
- 34 *National Archives of the United Kingdom*. T 370/58. 'BNOC and BP, 7 October 1975'.
- 35 As part of the effort to get their Public Sector Borrowing Requirement under control, the British even sold off some of their shares in BP in 1977 (Hoopes, 1997, p. 63).
- 36 Exports dropped from 4.5 million bpd to less than 1 million bpd by November (Yergin, 2008, p. 660).
- 37 *National Archives of the United Kingdom*. PREM 19/42. 'Letter from Hunt to Thatcher: Energy Issues, 4 May 1979'.
- 38 *National Archives of the United Kingdom*. PREM 19/42. 'Principle points made by the Prime Minister on her visit to the Department of Energy: 18 May 1979, 31 May 1979'.
- 39 For the earlier discussions on this issue, see *National Archives of the United Kingdom*. T 465/28. 'British national Oil Corporation Privatisation, 1982'.
- 40 Kidder, R. K. (1980). Britain turns to oil diplomacy with OPEC. *Christian Science Monitor*, 5 August.
- 41 *National Archives of the United Kingdom*. T 450/355. 'North Sea Oil Prices, 1 February 1983'.
- 42 *National Archives of the United Kingdom*. T 450/355. 'Meeting between Cassel and Townshend, 22 April 1983'.
- 43 *National Archives of the United Kingdom*. PREM 19/1474. 'Establishment of Oil and Pipelines Agency, 12 November 1985'.
- 44 *National Archives of the United Kingdom*. PREM 19/2137. 'Energy, 4 February, 1986–28 February 1987'.

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Consumer countries, producer countries, and the oil industry

Italy's role in the evolution of oil contracts (1955–1975)

Elisabetta Bini and Marta Musso

Introduction

Enrico Mattei, founder and first CEO of the Italian state-owned company Ente Nazionale Idrocarburi (National Hydrocarbon Agency, ENI), is one of those historical figures who can enjoy his own mythology, particularly in Italy – but not only. He has been defined as a hero, a revolutionary, a dictator, a Communist, a Fascist, the inventor of Italian-style corruption, a flamboyant character, and a new Napoleon (Buccianti, 2005; Frankel, 1966; Votaw, 1964; Pietra, 1987; Galli, 1976; Perrone, 2001). The most interesting and accurate definition is perhaps ‘il petroliere senza petrolio’ (the oilman without oil) coined by Indro Montanelli, one of the most important Italian journalists of the 20th century. Montanelli, a right-wing liberal, gave a negative connotation to the expression, suggesting that Mattei’s actions, focused on obtaining direct access to oil resources through state investments rather than relying on the supply system offered by what he called the ‘Seven Sisters’, were an exercise in megalomania, as well as a waste of public money.¹

During the 1950s and early 1960s, Mattei based his whole entrepreneurial and political strategy on the idea that building a state oil industry that could be independent from multinational oil corporations – which controlled the vast majority of the European market, as well as the production fields in producer countries – would guarantee Italy’s energy security and economic growth and boost the country’s international prestige. An effective communicator, Mattei promoted forms of economic cooperation between Italy and developing countries. By signing independent contracts with oil producers on terms different from those offered by the companies of the cartel, Mattei became known as a revolutionary; his death in a terrorist attack that still has no culprit fed into the myth. In many ways, Mattei was a forerunner of the politics later adopted by independent companies such as Occidental Petroleum, as well as of many OPEC countries’ requests for nationalization and control over their oil resources. While his power in changing the oil industry was largely overstated, Mattei had a crucial role in developing a large corporation in a country like Italy that lacked domestic oil resources and access to oil fields. Most importantly, his legacy remains in many producing countries, where he is still considered a symbol of anti-colonialism and a supporter of early efforts to challenge the power of the cartel.

This article examines the impact that ENI, through Mattei, had on international oil policies, in order to evaluate the effective degree of novelty and the long-term changes the Italian firm brought to the oil industry. Through a study of primary documents from the historical archives of ENI, OPEC, and the European Union, and through an analysis of oil industry journals such as the *Petroleum Intelligence Weekly* and the *Middle East Economic Survey*, this article highlights the changes introduced by ENI and Mattei during the 1950s and the limits and successes of this small ‘revolution’. In particular, it looks at the relations ENI established with leaders in the oil-producing world, the impact the ‘Mattei formula’ had on early OPEC policies, and the legacy ENI’s activities had on the subsequent development of the oil industry during the 1960s and early 1970s.

The oil industry in the 1950s

The oil concession system that governed international oil politics during the 1950s was in many ways reminiscent of imperial policies. The notorious ‘As-Is’ and ‘Red Line’ agreements of 1928 had established a de facto international cartel made of the seven largest companies in the world, of which five were US-based (Standard Oil of New Jersey-SONJ, Gulf Oil, Texaco, Standard Oil of California, Standard Oil of New York), one British (British Petroleum), and one Anglo-Dutch (Royal Dutch Shell). Plus the French Compagnie Française de Pétrole (CFP), which was much smaller than the other companies, did not influence price formation, and had significant market quotas only in France (Faure, 1939). By controlling Middle Eastern oil – the easiest to extract and cheapest to produce in the world – until the 1960s the cartel was able to control most of the markets outside the US and the Soviet bloc (Yergin, 2008; Maugeri, 2006; Odell, 1974; Ferrier and British Petroleum Company, 2009; Bamberg, 2000). These large companies recognized each other’s quota in both the downstream (refining and marketing) and upstream (research and extraction) sectors (Frankel, 1966). By doing so, the cartel was able to guarantee the stability of supply through an integrated production/distribution system, and the stability of prices through a series of price agreements, which left little space to the market. Many economists of the postwar period recognized that there was an ‘assurance element’ in the horizontal concentration of the oil business in a handful of corporations. Paul Frankel, one of the most important experts on the oil industry at the time,² wrote that ‘the opportunity for concentrated but diversified and internationally integrated oil companies to draw their oil from a substantial number of supply sources and to sell it virtually everywhere, provides a degree of security-with-flexibility which renders it shockproof’ (Frankel, 1966).

Companies belonging to the cartel took high risks in investing in the research of new oil fields and in the development of technology and know-how, acting effectively as investment banks to ensure the necessary funding needed to ensure the necessary funding needed to develop an oil economy (Penrose and Odell, 1968). The ability on the part of oil companies to self-finance fed the cartel and allowed firms to increase their size and profits as the industry developed. Firms retained and used more and more capital market, eating out a growing amount of resources as the market kept expanding because of the increase in demand; to the point that in the 1950s, economists such as Frankel warned about the damage they were provoking to the principle of a free-flowing capital market (Frankel, 1966). Oil companies’ role as ‘middlemen’ was also considered an important ‘social function’ in international relations between producer and consumer countries (Hartshorn, 1962). The first contractual models were very simple, and very convenient for the companies. Concessions for exploration and production were mostly based on fixed royalties, a rent tax that was independent from the companies’ profits on the oil they exported – very low compared to the profits made by selling the oil extracted (Cattan, 1967). The terms of the contracts were very long, as they were to last up to 75 and even 90 years.³ Some of the earlier concession agreements also gave oil companies sovereignty over territories. If firms found oil resources in the ground, they then had the right to determine unilaterally whether to exploit them or not, and the extent to which they would do so.⁴ These contracts were standardized internationally, with few variations.

With the expansion of the oil industry, producing countries started demanding greater control over the oil industry, over the quantities of crude to be exported and the price of crude. Their requests for higher government revenues became part and parcel of their political discourse and intersected in important ways with anti-colonialism (Garavini, 2012). One of the first countries to challenge the oil concession system was Venezuela, a crucial source of oil for the US, especially after Mexico's oil industry was nationalized in 1938. In order to retain access to Venezuelan crude and stabilize the concession system in the country, in the early 1940s the US government convinced American companies to accept what came to be known as the '50:50 formula'. According to the new principle, producers retained 50 percent of the profits made by companies from the oil sale (Frankel, 1966; Painter, 1986). In 1950, the same formula was applied to Saudi Arabia, which by the late 1940s had become the center of the world's oil production. While the 50:50 agreement effectively stabilized the concession system, according to Henry Cattani, a Palestinian-born lawyer specialized in oil contracts in the Middle East, it also marked a turning point in the evolution of the oil industry, not only because producers started influencing petroleum legislation but also because producers started to be paid on the basis of sales, linking their revenues to oil companies' profits. Oil companies, for their part, did not have any problem paying higher revenues, as long as they could offload higher costs to consumers or through tax rebates. Indeed, according to the 50:50 formula the revenues US oil companies paid to producer countries were considered a tax and could thus be deducted from the taxes owed to the US Treasury (Maugeri, 2006; Yergin, 2008).

Western European countries, which at the time were the largest consumers in the world, expressed increased worries about their dependence on oil imports controlled by American and British companies. In the late 1940s, oil was an important component of the Marshall Plan: the US gave Western European countries more than \$1.2 billion to buy oil, which accounted for 10 percent of the total aid provided under the European Recovery Plan. By doing so, it assured Western Europe's recovery, but also made it dependent on an energy resource controlled by the US (Painter, 2009). Furthermore, after 1948, the oil Western Europeans received came primarily from the Middle East, as the US government imposed restrictions on imports from the Middle East, which it considered to be less defensible in the case of a Soviet attack, and privileged oil from Latin America (Maugeri, 2006). Western Europe thus found itself not only dependent on energy supplies coming from an unstable area (Europe produced barely 3.5 percent of its total consumption)⁵ but also without any control over the industry managing oil supplies (Painter, 2009). Several countries began expressing their concern for the cartel's power and wealth. Indeed, in 1960 two of the most powerful companies, SONJ and Shell, had an annual turnover of 8.9 and 7.5 billion dollars respectively – around half that of France or, as *Le Monde* wrote in 1959, 'the budget of a medium-sized industrialized nation'.⁶ SONJ alone controlled 11 percent of the world's production, plus 150 million tons in refining and marketing. Shell had a tanker fleet of ten million tons, twice the size of the French commercial fleet (Durand, 1960).

Outside the cartel, only a few independent American companies were able to carve out niche pockets in the extraction and marketing of oil. These firms were powerful and important in the domestic market, on a state or federal basis, but they were not present outside the US. Frankel described them as the cartel's 'walking alibis': while they provided some elements of competition, at least in the US, they were usually acquired by one of the majors at a very high price when they started to be too successful, thus allowing the cartel to expand its control over the oil market (Frankel, 1966). As Frankel (1966) noted, 'The only truly independent oil company [was] the Esso organization [Standard Oil of New Jersey], the biggest of them all [...] it is more balanced and self-sufficient than any other, depending on no one for either supply or disposal.' Apart from US independents, the third type of oil companies outside the cartel was that of the European state-owned enterprises (SOEs), which usually only conducted research inside national borders or in the colonies. Their power was limited compared to both the cartel and American independents: in 1956 a company such as SONJ could count on a capital of 900 billion francs, the American independent Sinclair had a capital of 100 billion, while CFP, the eighth largest company in the world, had a capital of

barely 34 billion francs.⁷ CFP was considered an SOE because the government owned 40 percent of the shares; however, its strategy followed that of the cartel rather than the French government. As Frankel (1966) noted, ‘the idea that [the cartel’s] co-operation is an unspeakable crime for which there can be neither excuse nor remission penetrated Europe only after the last war in the wake of overall American influence’. This was the situation of the world oil market in which Mattei’s ENI came to operate.

ENI and the redefinition of international oil politics

During the 1950s, ENI rose to prominence in the international oil market mainly because of two features. First, under Mattei’s presidency the company implemented an aggressive policy to expand its upstream sector by promoting direct negotiations with oil-producing countries against multinational firms. Founded in 1953 as a state-owned oil company, ENI aimed at providing Italy with enough energy to meet its needs. Its affiliates discovered important gas reserves in the North of the country in the last months of World War II and started to extract them as a state monopoly. Before becoming president of ENI, Mattei engaged in a battle with the newly constituted Italian parliament to keep those reserves as a state monopoly rather than allowing companies (particularly SONJ) to be granted concessions (Pozzi, 2009). While gas reserves gave a first bust to the Italian hydrocarbon industry, oil was a fundamental source for economic expansion, and the country’s energy policy was developed on the central problem of oil supplies.

As the representative of a country that, with the exception of several gas reserves, lacked energy resources, ENI tried to establish an autonomous position, both domestically and internationally, by searching for different sources of oil than those provided by the cartel. It did so by redefining the rules of the international oil market and, in particular, the 50:50 formula. The company signed a series of contracts with oil producers, which assigned them wider control over their resources. What came to be known as the ‘Mattei formula’ recognized producers as partners in the exploration and production of hydrocarbons. According to the treaties, the Italian company would be responsible – financially and technologically – for searching for crude. Only in the case of success, oil-producing states would work side by side with ENI in developing their energy resources by participating in the management of mixed companies established between the Italian firm and oil-producing states, and having workers trained by ENI in Italy. Furthermore, in 1960 ENI signed an important deal to buy crude from the Soviet Union, against US efforts to avoid Western Europe’s dependence on Russian energy imports; a move that put Italy in a difficult position inside the North Atlantic Treaty Organization (NATO) (Cantoni, 2017b; Bini, 2017). Both actions challenged the position of the US majors in Western Europe and the Middle East, decreased the price of oil products sold on the international market, and contributed to the weakening of the cartel (Pozzi, 2009; Cottino, Pressenda and Sarale, 1978; Colitti, 1979; Sapelli and Carnevali, 1991; Galli, 1976).

An important aspect of Mattei’s approach to the oil industry, in his negotiations with producer countries, was to highlight the fact that ENI’s oil agreements were never just about oil. Although the actual negotiations only focused on oil, in all his speeches Mattei stressed the importance of using oil as the starting point of larger development projects that could enable producers to close the industrialization gap with the developed world. Most importantly, Mattei advocated the establishment of strong state oil industries that could operate alongside the private sector in order to negotiate supplies and prices among states and counteract the ‘predatory’ system put in place by the cartel, which damaged consumers and producers alike. Through a complex communication strategy, Mattei highlighted how both the British and the French empires, as well as the oil cartel (and thus the US), represented colonial powers, preventing free trade among nations and the development of oil producers’ economic resources. According to him, the achievement of national independence should be economic as well as political and decolonization should include the end of the policies carried out by the cartel. Mattei portrayed Italy as an anticolonial power

(since the country had lost its colonies after World War II), with a crucial role to play in guiding the process of decolonization, and argued that ENI's policies would allow oil producers 'not be passive recipients of foreign aid, but subjects, rather than objects, of the economy'⁸ (Bini, 2013).

ENI started investing in upstream production in 1953, the year the company was founded. At first it tried to enter into some of the consortia that had been created in the Middle East, with the aim of placing ENI in a position similar to the French CFP, a 'junior partner' of the cartel. During the 1951 Iranian crisis, ENI participated in the boycott of Iranian oil, which contributed to the downfall of Mohammed Mossadeq, in the hope that it would be granted concessions in the area. When, following the 1953 coup, the main international oil companies (namely British Petroleum, Gulf Oil, Shell, CFP, Aramco, SONJ, Standard Oil of New York, and Texaco) established a consortium in charge of operating and managing Iran's oil resources on behalf of the national Iranian oil company (NIOC), ENI immediately applied to join. However, the British intervened to block its agreement with NIOC, arguing that only companies with 'a tradition' of presence in the Middle East could enter, while the cartel refused ENI participation in the Consortium. The rejection was made worse by the fact that American independent firms were allowed in, even though they had not previously operated in the area (Bucarelli, 2010; Tremolada, 2011; Rosario, 2013; Marsh, 2003; Abrahamian, 2013).

The Iranian case was considered a slap in the face against ENI's international position and pushed Mattei to look for other ways to acquire autonomous sources of energy while at the same time pursuing a more aggressive oil policy. It was in the wake of the Suez crisis that Mattei realized that instead of trying to be the last of the aristocrats, in the shadow of dying imperial powers, ENI could seize the opportunities offered by the process of decolonization to become the first of the bourgeois. During and after the crisis, Mattei pointed out that oil producers represented both a threat and an opportunity for the countries that relied on their products. He argued that oil-consumer countries, by which he meant particularly Western Europe, should have a larger role in determining oil policies and prices, by challenging the forms of monopolistic power pursued by the cartel, and assuring a constant and relatively cheap flow of oil across the Mediterranean. Mattei advanced the idea that an international pool agency should be created, involving producers and consumers in a shared energy policy. A study prepared by ENI's Research Bureau and sent to Jean Monnet in 1956 pointed out that 'in the framework of the project to create a common market, it is necessary to find a solution that meets the oil needs of the six countries' by establishing international forms of control over the oil market.⁹ Some members of the British government initially supported this idea (they talked about a Schuman Plan for the Middle East, similar to the European Coal and Steel Community – ECSC). However, Mattei's proposal did not find enough support and, as a result, ENI started establishing agreements directly with producing countries.

In March 1957, Mattei signed an agreement with the Shah of Iran. According to the agreement between ENI and NIOC, the Italian firm was assigned exploration permits for free, instead of paying a cash bonus. AGIP Mineraria – ENI's affiliate in charge of exploring for oil and natural gas – would cover all the costs necessary to search for oil, while the joint company Italo-Iranian Petrol Company (SIRIP) would participate in the expenses only in the case of success. If ENI found commercial quantities of oil, SIRIP would control the development of the field and the production levels and ENI would pay taxes to the Iranian government on its oil revenues. However, ENI would only have ownership on 50 percent of the oil extracted; the second half of crude went to the Iranian government, which could then sell it independently. This formula, soon known as the 'Mattei formula', was innovative for three reasons. First, producer countries were recognized as partners in the oil industry through their participation in a joint company. They thus entered into the oil business as active entrepreneurs, had direct control over the oil extracted, and had their own quantities of crude to sell. Second, by promoting state-state agreements and asking producers to become entrepreneurs, the 'Mattei formula' undermined the principle of the cartel's self-financing. Finally, by lowering the capital required for exploration and extraction (given that producer countries invested part of their oil revenues in a joint venture), the formula opened the doors to new operators outside the cartel (Tremolada, 2011).

The ‘Mattei formula’ was considered a revolution in the oil industry. Shortly after the agreement, *The New York Times* wrote that ‘any future agreement will have to follow new schemes’ and ‘the companies holding concessions, whose existence depends on an efficient diplomacy, will have to consider it as a Sputnik [...] that orbits around them’.¹⁰ The Petroleum Press Service attacked ENI for abandoning the 50:50 agreements ‘for the sake of the other country [the producer country]’, and thus lowering the company’s profits, which in 1960 were only 4.6 billion liras (£2.6 billion), the same as the previous year. British Petroleum executives discarded Mattei as being a ‘para-communist’, while Shell accused him of accepting a bad deal with producers just to be able to step in, leading to a rise in the price of concessions while decreasing profits for the companies (Howarth et al., 2007). The American and British governments took issue with Mattei’s action in Iran, and pointed out that the agreement between ENI and NIOC might lead to a transformation of the relationship between ‘an industrial country and an under-developed country’ to the destabilization of the Middle East. They even argued that, in the long term, it would affect US-Italian relations inside the Atlantic bloc. The Eisenhower administration advanced different interpretations of how the US should respond to ENI’s activities in the Middle East. While the Operations Coordinating Board pointed out that the Italian-Iranian agreement challenged American oil interests, and increased Italy’s instability, Secretary of State John Foster Dulles and President Eisenhower took a more cautious stance. They highlighted the economic rather than political nature of Mattei’s approach, while at the same time pointing out that one of the consequences of ENI’s treaty might be to push oil producers to pursue a more autonomous policy and view ENI as a tool to promote the exploitation of their oil resources, especially in countries with good potential for oil and gas reserves, such as those of the Maghreb.

The importance of the ‘Mattei formula’ was indeed not economic but political and psychological: it encouraged producer countries to intervene directly in the decisions over oil production, and to claim ownership over crude. Mattei’s main goal was to re-shape the oil industry in a way where producers and consumers discussed directly the problem of oil prices and supplies via their national companies. This view was strongly welcomed by several OPEC countries. In a 1963 report written by OPEC on the changes of the oil industry in the previous ten years, the ENI-NIOC agreement was quoted as one of the milestones that had transformed the oil industry, along with the 1950 treaty that introduced the 50:50 formula in Saudi Arabia. According to the report, it was the first time that a contract gave an oil producer control over 75 percent of its revenues and set the duration of the agreement to 40 years, a much shorter period than usual. The OPEC report concluded that ENI’s agreement with Iran was of crucial political importance but was not so groundbreaking from a financial point of view, given that the 75:25 profit division was mostly on paper and that producer countries committed to heavy investments alongside ENI and thus reduced their profit margins. In OPEC’s view, it was the oil law introduced by the Indonesian government in 1963 that was more radical, as it stated that the government would be entitled to 60 percent of the revenues, breaking once again with the 50:50 formula, as Venezuela had already done in 1958. What ENI and Mattei did was to redefine the terms of the relationship between producing and consuming countries and between producers, independent companies, and the cartel.¹¹ As a result, a range of private and state-owned independent companies established similar contracts with producer countries, with the aim of entering into the upstream market. In December 1957, the Saudi Arabia-Japan Petroleum Trading Company Agreement was signed, followed by the NIOC-Pan-American contract in April 1958, and the Kuwait-Shell agreement in January 1961, in which for the first time a major oil company accepted this new type of agreement (Yergin, 2008).

After Iran, Mattei proceeded to sign deals with several other countries. In late 1957, ENI established a similar agreement with Nasser. In Algeria, the Italian company openly supported the National Liberation Front during the independence war, causing a serious diplomatic strain between Italy and France. When the Italian ambassador complained about the diplomatic incident Mattei caused between the two countries, ENI’s president replied that it was more convenient to deal directly with the future owners of the oil

concessions rather than with the old colonial power (Bagnato, 2012). ENI's activities in Algeria allowed Mattei to sign deals for the construction of a refinery and obtain research permits in Morocco and Tunisia, challenging France. In Libya, where the newly found oil resources were mostly controlled by SONJ, the cartel was able to bloc Mattei's attempts to enter the area thanks to a careful lobbying of King Idris, who denied ENI access to important concessions (Tremolada, 2015). In 1961, when Iraq passed a law to expropriate 99.5 percent of the concessions assigned to the international IPC consortium and created the Iraq national oil company (INOC), ENI offered to help the country by replacing the British technicians operating in the area with Italian personnel; a move that was allegedly blocked by the Italian government in order to avoid a diplomatic incident.¹² As part of the anti-cartel strategy, ENI regularly enquired about the competency level of producer countries, asking if local engineers could substitute Western ones; and through its Graduate School for the Study of Hydrocarbons in Milan, it offered professional training as part of its oil negotiations. By doing so, it built long-lasting relations with the new ruling classes and cadres in charge of defining the future of their countries' oil policies (Bini, 2013).

OPEC and ENI: an early and complicated friendship

Given Mattei's and ENI's activities in the oil-producing world, it should come as no surprise that when OPEC was founded the new organization took interest in ENI's policies. Already in 1959, during the first Arab Petroleum Congress ENI sent a delegation, represented by Enrico Bonomi, a prominent member of ENI's Ufficio Studi (Research Bureau), a division in charge of defining the company's policies in Italy and internationally (Lavista, 2017). In 1961, during the Third Petroleum Congress in Alexandria of Egypt, ENI presented a report on the company's guiding principles and its policies toward oil producers. It argued that since oil was crucial in assuring economic growth, in countries without reserves (such as Italy and developing countries) the state should intervene directly to ensure supplies – it should not be left to private companies only. The report went on to point out that ENI promoted the idea that producers should control the exploitation of their own resources and also support their economic development by guaranteeing a more adequate share in the benefits from oil production and promoting local industrialization and thus oil consumption. Finally, the report critiqued the conventional concession system and argued that this system went against the interests of both producer and consumer countries. It concluded that while the international oil industry attacked or ignored the creation of OPEC, ENI welcomed it and considered it a tool to bring justice to the market. It pointed out that producer and consumer countries should run joint companies, in which both interests were represented at all stages, while contracts for hydrocarbon extraction should be inserted into wider contracts that promoted forms of economic cooperation between countries.¹³

These instances were particularly welcomed by those countries in OPEC that promoted a more critical (and anti-American) view of the oil industry and took a more radical stance on the issue of oil nationalism. In 1963, Abdullah Tariki, one of the founders of OPEC (by then exiled in Lebanon by the strongly anti-communist King Faisal), hailed ENI's pro-nationalization stance as the future of the international oil industry. He argues that France was now doing the same with the national UGP distribution network (the result of a series of nationalizations in the downstream sector operating in France), and that in Great Britain the Labour Party was endorsing a similar project. Tariki concluded that 'The activities of ENI in Italy are beyond description. So, it is natural to put the Middle East oil industry in the hands of the governments of the area. It is an evolution that is dictated by the facts of life.'¹⁴

In 1963, during the Fourth Arab Petroleum Congress, OPEC's secretary general Fuad Rouhani highlighted the fact that the agreement between ENI and NIOC paved the way for a series of deals between oil producers and independent companies that assigned producers higher profits and more control over their oil resources. According to him, ENI had been the first to pursue a policy that revolutionized the international oil market and had quickly been followed by other firms.¹⁵ Overall, OPEC seemed to trust

ENI more than any other oil company. In 1962, for instance, Rouhani asked the company's Ufficio Studi to conduct a study about the structure of the international oil market. Titled 'The Profitability of Integrated Operations of International Oil Companies', the study argued that the cartel had established a quasi-monopolistic market undermining any attempt on the part of other oil companies to carry out their activities in the Middle East, and pointed out that its profits were much higher than those declared to producer countries¹⁶ (see Colitti, 2008). Furthermore, OPEC considered ENI, and Mattei in particular, as the most important interlocutor in Western Europe, and viewed the company as a bridge with the EEC. Since the establishment of the organization, the EEC had a delegate representing consumer countries at OPEC conferences and Arab Petroleum Congresses, although European-level energy policies were discussed entirely within the OECD. OPEC tried reaching the OECD for a mutual agreement on energy information sharing, but the OECD never invited OPEC to discuss its views on energy, as it periodically did with European and American oil companies.¹⁷

Early relations with the new organization, however, were not as smooth as expected. The fact that in 1960 ENI made a deal with the Soviet Union, a strong competitor of OPEC's oil, caused discontent among many producing countries, just as it did inside NATO and among Western oil companies. In October 1960, Mattei signed an agreement for the supply of 12 million tons of crude oil over a period of four years, at the price of \$0.06 per barrel, compared with the standard prices of \$1.59. This allowed ENI to lower the cost of gasoline to consumers by two liras, creating an internal market for which ENI's competitors – Shell, BP and SONJ – barely had any margin. At the same time, Russian shares of Italian oil imports jumped to 20 percent, more than three times those of any other Western European country (West Germany, the second most exposed, did not go above 6 percent of imports from Russia) (Bagnato, 2003; Cantoni, 2017a; Bini, 2013). The decision to become dependent on Soviet oil imports created strong tensions with NATO, the US government, and the cartel, and Mattei's name ended up on a CIA list of special surveillance (Castagnoli, 2015). OPEC was among the most vocal critics of ENI's decision to open the Italian market to Soviet oil. In February 1961, Rouhani visited the company's headquarters in order to 'clarify the positions of ENI with regards to the international oil problems and Soviet imports in particular'.¹⁸ Two years later, during the Fourth Arab Petroleum Congress, held in Beirut, Bonomi had to defend ENI's activities, arguing that the contracts with the Soviet Union were only in favor of Italian energy prices and against oil multinationals, and that the increase in world demand would not damage Arab producers. However, several delegates attacked Bonomi by arguing that, as a neighbor and a friend of the Arab world, Italy had a responsibility to buy oil from them rather than from the Soviet Union.¹⁹ Emile Boustani – chairman of the Lebanese committee – critiqued ENI's policies and argued: 'I am an Arab in the Arab world, I want my oil to be at the highest price. For heaven's sake, you Italians, as our friends, the friends of the Arabs, do not hurt your interests and ours together.'²⁰ Bonomi replied by pointing out that ENI's contracts provided an answer to oil producers' concerns.²¹ While Bonomi and the Ufficio Studi dismissed Boustani as someone who was paid by the cartel, it is true that during the 1960s oil prices did decline, and the arrival of Russian oil on the international market – of which Italy was one of the main promoters – was certainly one of the causes.²²

While Mattei and ENI dealt with OPEC, they also tried to promote a shared European oil policy. In 1961, the company presented a project to the OECD that proposed a state-directed framework under which crude oil supply agreements would be negotiated directly between consumer and producer governments. OPEC representatives reacted by defining ENI's idea as 'unrealistic', given that 'the oil companies could not be eliminated from the picture as easily as suggested by ENI' and that 'oil producing nations were not in a position to produce their own crude'.²³ The following year, Mattei suggested to the EEC Commission that a consortium of European oil companies be created to deal directly with producer countries, as protection against the risks represented by both OPEC and the cartel. Such a consortium could reach unique buying agreements with producers and link the European Development Fund (EDF) to oil revenues. It would create a system that could use part of the revenues to promote different

development projects in producer countries. While the EEC called Mattei's ideas 'impressive', it also discarded them as impossible to realize. Furthermore, the EEC suggested that abolishing the tariffs on imported oil products, as Italy and France were doing to expand their refining system, would lower prices more than the arrival of Russian crude on the Western European market.²⁴ ENI was not particularly keen to promote OPEC's supplies to Italy and Western Europe. When in 1962 NATO's Committee of Economic Advisers – a study group created in 1960 to examine the consequences of the 'Soviet offensive' on the energy market – released a report recommending that Western European countries stop signing agreements with the Soviet Union, Italy protested, arguing that Russian oil imports were not more dangerous than imports from OPEC countries; if anything, the contrary (Cantoni, 2017b; Bagnato, 2003).

ENI's oil policies after Mattei's death

Mattei died in October 1962, in the explosion of the company's twin-engine plane that was taking him from Sicily to Milan. Speculation regarding his death continues to occupy the headline news of the international press from time to time. In 2006, the last trial around his death concluded beyond doubt that the reason for the explosion was a bomb on board; but who placed it, and why, has not been determined. Different lines of investigation have looked at the French OAS, the Sicilian mafia, and, most popularly, the CIA or the Seven Sisters directly (Li Vigni, 2003; Galli, 1976).

In his obituary, *The New York Times* wrote that the most powerful man in Italy had died.²⁵ However, in October 1962 neither Mattei nor ENI were in a solid position of power. Five years after the signing of the first contract with Iran's NIOC, the company was involved in a series of long-term investments that gave limited economic results. Exploration activities in Iran and Egypt were below expectations: only a small discovery in the Bahrgansar area had proven successful, while the very expensive exploration of mount Zagros in Western Iran had not produced any outcomes. Both Iran and Egypt were dissatisfied with the revenues coming from ENI: they were higher than what the cartel offered on paper, but lower because of the smaller size of the oil exports compared to the investments the governments were called to make. As a result, most of their profits continued to come from their agreements with the cartel. Furthermore, the small quantities of oil imported to Italy did not lead to a significant transformation in the balance of Italian (or Western European) supplies.²⁶

On a domestic level, Mattei was losing his political backup and was worried that the government would not renew his mandate as president of ENI (Pirani, 2012). In the last year of his life, Mattei introduced a series of important changes that deeply transformed the company's policies, both domestically and internationally. After the deal with the Soviet Union, the American government decided to find an agreement with Mattei. In March 1961, W. Averell Harriman – John F. Kennedy's foreign policy advisor – visited Italy and held a private meeting with ENI's president. During what was the first talk with a representative of the American government, Mattei denounced American oil companies' forms of discrimination against smaller oil companies like ENI, stating that they had pushed him to establish a deal with the Soviet Union. The US administration discussed offering ENI large supplies of crude oil and natural gas in exchange for its willingness not to 'increase further the present average daily rate of importation of Soviet crude oil into Italy'.²⁷ These deals radically transformed ENI's international oil policies in North Africa and the Middle East and, more generally, its relations with oil producers.

Mattei's successor, Eugenio Cefis, directed ENI until 1971 and abandoned the company's more radical approach to the decolonizing world, while at the same time bringing to completion a series of policies introduced during Mattei's presidency. Given that ENI had too many investments in both upstream and downstream activity, Cefis restructured the firm, focusing only on the downstream sector. He considerably reduced the exploration and extraction activities ENI carried out in the Middle East and North Africa and made a deal with several US majors to buy the crude needed by the Italian market. In 1963, ENI's president signed an agreement with SONJ – which Mattei had been secretly negotiating –

according to which the US oil company would provide ENI with the crude oil and natural gas it extracted in Libya in exchange for services and equipment such as pipelines and the transport and processing of crude in the refinery of Ingolstadt, in Bavaria. The treaty provided ENI with 25 percent of its requirements and considerably reduced Italy's dependence on Soviet oil, while it allowed SONJ to find a cheap outlet for the hydrocarbons it extracted in Libya. In 1965, another agreement set the terms for the import to Italy of three million cubic meters of Libyan natural gas per year. The deal caused angry reactions on the part of Algeria, which was about to sign a similar agreement with ENI. Because the Algerian government had just taken direct control over much of its gas industry, ENI's shift was charged with deeper meanings and interpreted as Italy refusing to deal with an Arab country that controlled its reserves, preferring to sign an agreement with the cartel.^{28 29} It is impossible to know what would have been Mattei's reaction to this criticism; Cefis chose to ignore it. In general, by reducing upstream investments to focus on distribution in Italy and Western Europe, ENI also reduced its international stance. After 1963, the company rarely appeared in the reports written by OPEC or in the proceedings of the Arab Petroleum congresses.

While ENI cut its investments in the upstream sector, it still took advantage of the opportunities offered by the decline of the oil cartel. Furthermore, it continued to draw on the prestige it had acquired in the oil-producing world during the 1950s as a 'rogue company', even though the more radical stances proposed by Mattei were significantly toned down. ENI thus differentiated its oil supplies by signing a series of deals with OPEC and non-OPEC new producer countries such as Madagascar, the Congo, and Argentina, as well as the Soviet Union. Thanks to these agreements, ENI increased the number of its concessions sevenfold, and reached a production of 10.5 million tons of crude oil in 1971, compared to 3.7 in 1962 (Labbate, 2014). Cefis insisted, like Mattei, on the importance for Western European countries of promoting a common strategy to challenge the continent's growing dependence on foreign supplies, warning that a decision by OPEC could lead to an increase in prices. Unlike Mattei, though, Cefis did not promote any form of nationalization, instead arguing that oil majors should be the main partners in any negotiations between Western Europe and OPEC.³⁰ Given that throughout the 1960s oil prices kept decreasing, Western European countries (with the exception of France and Italy) preferred market-based solutions to keep prices low rather than shared negotiations with OPEC.³¹ Oil majors, on their part, reassured that lower oil prices would be permanent.³²

Producer countries, through OPEC, kept working to overturn this situation. In 1971, the Tehran and Tripoli agreements seemed to confirm Cefis' premonition that oil prices would rise. On 23 February 1971, OPEC countries signed an agreement by which all producers demanded an immediate raise in the price of crude of about 11 percent per year. Against the threat of a general embargo on the part of OPEC, the cartel decided to sign the deal. Two months later, a new agreement in Tripoli imposed a raise to \$3.45 per barrel. After almost fifteen years, which were also the heyday of Western European economic development, oil prices started to rapidly increase. For the first time, producing countries had also agreed upon a tax raise that increased prices worldwide; and it was consumers, not extracting companies, that paid the price – the agreements cost Europeans 1.7 billion dollars a year^{33 34 35} (Petrini, 2012; Turner, 1978).

ENI decided not to join forces with the majors, and maintained a neutral position during and after the Tehran-Tripoli agreements.³⁶ An internal note written in 1970 emphasized the choice the company faced between 'maintain[ing] (and expand[ing]) the political credit which it benefits from and try[ing] to take advantage from it, or [...] align[ing] itself with the position taken by the big companies'.³⁷ In a report to the Italian parliament, Cefis explained the reason for the price increase, this time criticizing the actions of the companies, but mostly attacking the inability of consumer countries to establish a common front. The oil crisis, explained Cefis, was caused by the fact that the cartel controlled 70 percent of crude produced in the world outside the US and the USSR, and that price formation was a truly global matter, with the US market as the point of reference. According to ENI's president, companies in the US had

strong fiscal advantages, which allowed them to refuse producer countries' requests when they could not offload the costs on to consumers. The lesson to learn from Tehran, stated Cefis, was that oil companies were not in control of producer countries' actions anymore; that they did not and would never defend consumers' interests; and that they were not able to guarantee the security of supplies for the future. Cefis warned that for this reason, 'A common oil policy is indispensable for the importing countries in the general landscape of the economic and energy situation.' He stressed that consumer should join together and form a united front. The alternative was to have the oil industry ruled by a new oligopoly: that of OPEC.³⁸

It is difficult to know whether Mattei's appeals for the creation of a state-state negotiation system between producer and consumer countries would have mitigated the consequences of the 1973 'oil shock' on Western European markets. What is sure is that Italy, OPEC's special consideration for ENI in the early years, did not receive any special treatment during the 1973 'oil shock'. The energy crisis was particularly detrimental for the Italian economy as it reduced the country's oil imports by 20 percent (the equivalent of 11 percent of its energy needs). Despite ENI's efforts to differentiate its sources of energy, 75 percent of Italy's total needs continued to be provided by oil. In a context characterized by an economic and financial crisis linked to the end of the Bretton Woods system, the possibility of having access to cheap sources of oil became crucial not only to fuel factories but also to prevent the outbreak of a social and political crisis (Battilani, 2008; Graziani, 1996; Castagnoli, 2015).

Conclusion

Enrico Mattei's fame as a rogue character is surely justified, although ENI's first president was far from being a revolutionary. While his rhetoric was aggressive, his actions show a willingness and need to mediate; Mattei's ultimate goal was to provide Italy with the cheapest energy prices possible, not to destroy the oil majors. While ENI's economists promoted the development of the oil-producing world, the company transformed their rhetoric into a tool to negotiate with oil producers, rather than using it as an actual corporate strategy. Even ENI's efforts to promote different forms of oil nationalism in Europe and in OPEC countries were ultimately a way to consolidate the firm's position as a strong interlocutor in the global oil industry.

In this respect, Mattei's legacy and plan to transform the oil industry were short-lived, even though ENI's first president did contribute to the dismantling of the cartel system, as OPEC and many producer countries highlighted at the time. Mattei's insistence on the importance of state-state negotiations in the oil industry did not stem from an anti-capitalist ideology, but rather from an understanding that producers would not continue to accept the concession system, as it had been established after the First World War; and that state-level negotiations could lead to new forms of cooperation in a strategic field such as energy. The agreements ENI reached with SONJ in the early 1960s showed that the company did not aim to undermine the oil majors, but rather to limit their profits and activities through the action of state companies like ENI. Instead of fighting against oil producers, Mattei endorsed their requests and turned them to ENI's advantage. In many ways, the Italian company anticipated by twenty years a series of debates and struggles that exploded after the 1973 'oil shock': the tensions between producer and consumer countries, the need to re-channel oil profits into the economy (a problem that was later solved financially through petrodollar recycling), and the weakness of Europe as a consumer area vis-à-vis both the oil majors and OPEC.

Notes

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- 20 Archivio Storico ENI (AS ENI) (n.d.). Archivio Insmlì, Carte Enrico Bonomi, serie Problemi di politica energetica.
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- 36 Archivio Storico ENI (AS ENI) (n.d.). Fondo ENI, Servizio Pianificazione Energia ed Idrocarburi, b.441, f.1FBF; AS ENI, Fondo ENI, Direzione estero, b.293, f.38.
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Between the superpower and Third Worldism

Mexico and OPEC (1974–1982)

Claudia Jezabel Piña Navarro

Introduction

This article analyses Mexico's oil boom of the mid-1970s and the use of hydrocarbon as an instrument of foreign policy towards the United States and the Third World during the governments of Luis Echeverría Álvarez (1970–1976) and José López Portillo (1976–1982), in a decade marked by changes in the world economic system and by oil shocks that had a profound impact on the international energy market.

One aspect that stands out was the position of Mexico regarding the Organization of Petroleum Exporting Countries (OPEC). During the 1970s, Mexico had a very active foreign policy in line with the demands of the Third World, as was demonstrated by the Charter of Economic Rights and Duties of States proposed by President Luis Echeverría in 1972 at the United Nations Conference on Trade and Development (UNCTAD). Echeverría also supported the efforts of OPEC, the countries of the Non-Aligned Movement, the G77 and other multilateral forums where there was an intense debate against colonialism and in favor of a more equitable international order between industrialized nations and the developing world.

However, the use of oil was not necessarily consistent with the position of Mexico abroad at a time when the oil-producing countries organized in OPEC were radicalizing their demands. Although Mexico at that time was a net exporter, oil and its management was not integrated into an active Third World policy that had been promoted for years. On the contrary, a management more aligned to the United States was maintained, and this soon became inconsistent with OPEC demands. Analyzing this lack of coherence between Mexico's actions abroad and the use of its oil 'weapon' is the aim of the article, and with that purpose it is necessary to first review the substantial developments within the oil industry and Mexican foreign policy.

I will take these variables into account for the period 1974–1982, concentrating on Mexico's ambiguous relationship with OPEC, particularly between 1974 and 1976, when promising hydrocarbon discoveries in the southeast region encouraged a discussion about whether or not to become an exporting country. This discussion was important because since the nationalization of the oil industry in 1938, Mexico had maintained oil exports at a marginal level. Nonetheless, during the mid-1970s, the transition of government

between Echeverría and López Portillo led to a rethinking of the national economic strategy, and oil appeared then as a possible instrument to finance national development.

Situation of Mexico's oil industry, 1974–1976

The year 1974 was a turning point for the Mexican oil industry. After a critical situation due to a lack of supply for domestic consumption that forced the acquisition of oil abroad from September 1971, the country became energy self-sufficient in June 1974, when oil imports were halted, and on 17 September of that year Mexico placed its surplus production on the international market (Petróleos Mexicanos, 1975, p. 22).

This conversion from an importing country to an exporting country is also relevant because Mexico suffered from the effects of the global energy crisis following the Organization of Arab Petroleum Exporting Countries (OAPEC) embargo in October 1973. The first oil shock altered the international hydrocarbon market and the external commercial activity of *Petróleos Mexicanos* (PEMEX, the national oil monopoly) was significantly affected (Petróleos Mexicanos, 1974, p. 19). Although the embargo was decreed by OAPEC in October 1973, a price adjustment and hardening of the demands of the producing countries was foreseen months before. In that sense, PEMEX's director, Antonio Dovalí Jaime, said that 'oil exporting nations have put in place policies to raise their prices, which will surely continue for a long time' (Petróleos Mexicanos, 1973, p. 6). With this statement he warned that 'the only acceptable position' for Mexico 'was to ensure self-sufficiency at all costs' (Petróleos Mexicanos, 1973). For that purpose, at the end of 1973 PEMEX organized an expansion program whose main goal was 'to eliminate imports of crude oil and save a 20-year margin of availability of reserves' (Sordo and López, 1988, p. 46).

The pursuit of energy self-sufficiency was a goal set by President Echeverría from the beginning of his administration and was an integral part of his program of income redistribution and the rethinking of the development model followed during the previous decades, which was showing clear signs of exhaustion by the beginning of the 1970s. In addition, energy self-sufficiency had a political value because 'oil nationalism' was one of the pillars of the authoritarian regime since the expropriation of 1938.

To PEMEX's relief, the 1972 discoveries in Chiapas and Tabasco produced high yields, so by 1974 it was possible to have 'the assurance that the discovered reserves and the development of the fields could even generate exportable surpluses' (Sordo and López, 1988). Figure 17.1 shows the sustained increase in production of crude oil, condensates and liquids between 1973 and 1982.

The situation for PEMEX was a noticeable improvement over the course of 1974, as was emphasized in the commemoration of the 37 years of expropriation on 18 March 1975, when before President Echeverría and Carlos Andrés Pérez, president of Venezuela, the director of PEMEX spoke about 'the radical change of the national oil situation as it went from importing crude and distillates, to a healthy balance between the demands of domestic production, with surpluses that have been placed into international markets', which supported 'a well-founded optimism about the immediate future of the oil industry' (Petróleos Mexicanos, 1975, p. 17).

Thus, the idea that Mexico's oil wealth could mean an alternative to the problems of economic growth started to spread. This thinking was summed up by the director of PEMEX in that report from March 1975: 'The economic expansion that oil makes possible should be used to finance a policy of social solidarity such as the one President Echeverría has designed: agriculture support and general diversification of the productive apparatus' (Petróleos Mexicanos, 1975, p. 18).

However, it is important to underline that there were two positions regarding the conversion of Mexico into an exporting country. There were people who from a conservative position asked that priority be given to meeting domestic demand and guaranteeing the supply of hydrocarbons for as long as possible; therefore, they recommended minimizing exports (Morales, Escalante and Vargas, 1988, pp. 54–55). In

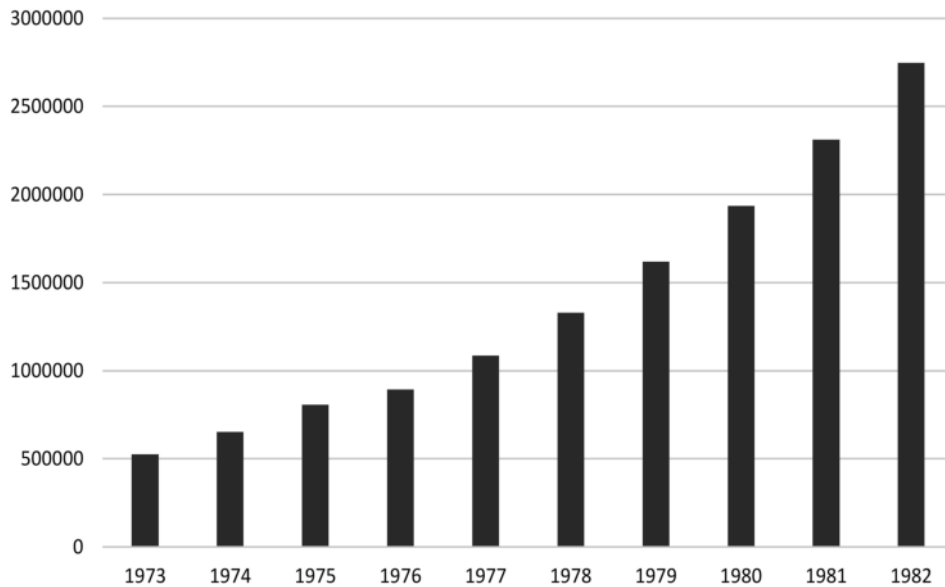


Figure 17.1 Production of crude oil, condensates and liquids, 1973–1982 (barrels per day)
Source: PEMEX, Memoria de labores, years 1973–1982.

contrast, a more pragmatic position saw in PEMEX's orientation towards exports the possibility of reducing economic problems and thereby gaining political capital.

President Echeverría remained 'between' these two positions during the last two years of his term and combined both when he defined the international oil position shortly before meeting Gerald Ford, USA's president, in October 1974, in response to a series of rumors leaked by the US press about the possibilities of a 'second Persian Gulf' in Mexico that would guarantee the supply to the US and weaken OPEC.

International position of Mexico towards oil: a path of contradictions

In October 1974, US newspapers reported that preliminary estimates calculated Mexican reserves at 20 billion barrels, which was interpreted as a possibility that Mexico might eventually (if it made the decision to increase production and became an exporter) keep prices at a level lower than those set by OPEC. *The New York Times* wrote:

A large discovery could give Mexico the capacity to break the high prices that have been fixed by [the] Organization of Petroleum Exporting Countries [...] They could underprice O.P.E.C. by 50 cents a barrel and we would buy all we could get [...] They would have a ready-made customer in the United States.¹

It is notorious that *The New York Times* published this days before the meeting between the leaders of Mexico and the US (which was held on 21 October), against a background in which the USA sought to diminish its dependence on OPEC for its oil supply and Mexico represented an advantageous alternative in the medium term.

A source quoted by *The New York Times* stated that the leak was intended as an attack on OPEC: 'Psychologically, it's not a bad idea to remind O.P.E.C. countries there might be oil elsewhere. We just

wanted to give them a gentle reminder that new oil field still can be found.² But Echeverría immediately made a statement in which he denied press estimates and emphasized that as far as the country's non-renewable resources were concerned, 'we must be profoundly nationalist and anti-imperialist'.³ Also, he described the report as a maneuver to weaken the prices on the barrel.⁴

Pressured by international speculation, Echeverría's government was quick to announce Mexico's international position towards oil. On 15 October 1974, the secretary of National Heritage and chairman of the board of directors of PEMEX, Horacio Flores de la Peña, stated that although Mexican oil exports were still small, it was necessary to define the country's position before the international oil market and particularly before OPEC, in line with the Third World-oriented foreign policy that President Echeverría had set in motion during his government:

Mexico sees and has always seen with sympathy and solidarity the struggle of OPEC member countries to obtain better prices for their oil and greater fiscal participation [as well] as to increase the degree of national control over this resource [...] OPEC is an eminent part of the world-wide struggle for the revaluation of commodities and raw materials and the search for a New International Economic Order, objectives that are in line with the principles that Mexico has proposed to be included in the Charter of Economic Rights and Duties of States. In the most immediate opportunity [] Mexico will seek to participate as an observer in OPEC meetings and will present proposals to increase its cooperation with the Latin American member countries of the Organization.⁵

The statement was consistent with the tone of Echeverría's international activism, which indicated absolute support for the common front of OPEC and contradicted claims that the Mexican government would collaborate with the USA in order to weaken OPEC. The statement by Flores de la Peña was blunt:

Mexico will be careful to ensure that its oil exports do not contribute in any way to depressing the prices of the product in the world market and that its participation in that market is not used as an element to weaken the common front of the producing countries. Mexico disavows any interpretation claiming that it could play a role in weakening the common front of the oil-exporting countries. As a pioneer country in the national and absolute control of oil resources, Mexico will never be the Trojan Horse of the transnational oil companies.⁶

Indeed, since mid-September 1974, Mexico had placed production surpluses on the international market and marketed them through the prices set by OPEC. That's how 35,000 barrels per day were exported to the USA and Israel, while Mexico also sought to diversify buyers and meet the energy needs of developing countries in Latin America and the Caribbean.

As regards the speculation on reserves, in a parallel communication that complemented Mexico's international position, PEMEX's director, Antonio Dovalí Jaime, stated that it was 'problematic and premature to try to quantify the magnitude of the newly discovered oil fields in the country', but he said that Mexico had export surpluses 'of 4.7 million barrels of crude in September-December of the current year and of about 40 million barrels in 1975, for a daily average of 111,000 barrels'. Those surpluses would be allocated to the 'international market, seeking the widest possible diversification of buyers and paying special attention to the needs of developing countries, especially in Latin America'.⁷

The statement also announced that offers had been made to Cuba regarding the acquisition of Mexican oil, and that Japan and Brazil had shown interest in buying it.⁸ The Mexican Foreign Ministry gathered the declarations of Flores de la Peña and Dovalí Jaime and circulated them to the representatives of Mexico around the world, requesting that this position vis-à-vis the oil issue be widely disseminated. The reactions were immediate. The *International Herald Tribune* reported that the Mexican left was inclined to join OPEC

but also favored the formation of a Latin American association of oil producers parallel to OPEC aimed at presenting a common front in the defense of their interests and in the fight against imperialism.⁹

The Jerusalem Post claimed that, according to OPEC sources, although Mexican exports were limited, the statute provided for the admission of new members whose interests and objectives were similar to those of the rest of the Organization, and concluded that 'Mexico would have no difficulty in fulfilling [this] condition'.¹⁰ However, an editorial about the Mexican oil industry in the same newspaper noted: 'There would be no sense in having escaped the bonds of the great oil companies 40 years ago only to become enslaved by the Arab oil sheikhs today.'¹¹ Israel was one of the buyers of Mexican oil and it was discomforted by the solidarity shown towards OPEC, as indicated by the communication transmitted by Mexico's embassy in Tel Aviv to the Ministry of Foreign Affairs, summarizing what was published by the press:

Mexico must remember the strength of the past and use its oil to build not only economic independence but also to protect and maintain its political independence. [...] [OPEC] is a political body hostile towards Israel and this is one of its main pillars and, in this regard, it warns that Mexico should not participate in that organization [...] Traditionally, cooperation between Israel and Mexico has been very effective and if [Mexico] joins OPEC, it jeopardizes the relationship with Israel, and may even end the aforementioned cooperation, either openly or through pressure.¹²

In Lebanon, the *Daily Star* of 18 October reported the news, adding that at the upcoming meeting of OPEC ministers in December, the Organization 'may consider Mexico's position if an application is lodged in time'.¹³ The same newspaper reported the declarations of Carlos Andrés Pérez, Venezuela's president, who sent a message to Echeverría in which he applauded Mexico's solidarity with the oil-exporting countries: 'The developing world has been getting together to face the unjust relations regarding exchange [with industrialized nations].'¹⁴

In telegrams from the US ambassador in Mexico, Joseph J. Jova, it was interpreted that '[Echeverría] feel [s] that Mexico needs to join OPEC to foster her credentials as a bonafide member of the third world and to exercise her oil strength to maximum benefit'.¹⁵ The State Department was aware of the weight of political sensitivity with respect to the oil in Mexico, and in the preparation documents for the Ford-Echeverría meeting it emphasized:

We should avoid appearing covetous of Mexican oil. Recent press speculation that the [US] hopes to use Mexican oil against the 'Middle East cartel' have caused adverse newspaper comments in Mexico. The Mexicans are sensitive to American influence over their natural resources. They are also wary of U.S. oil companies. Therefore, the [government of Mexico] would react negatively to any U.S. attempt to influence directly its production and price policies. Similarly, any U.S. attempt to persuade Mexico not to join OPEC could also be counterproductive.¹⁶

Thus, it proposed that the oil issue was addressed only if President Echeverría put it on the discussion table during the meeting with Ford, and, if the Mexican president requested assistance for the development of PEMEX, the answer would be positive, with the request that Mexico increase its exports as there would be space in the North American market.¹⁷

In the memorandum of conversation of the presidential meeting that took place on 21 October 1974,¹⁸ it is noted that it was Echeverría who tackled the oil issue, asking for Dovalí Jaime and Flores de la Peña to be present so they could outline the situation of the Mexican industry and its projections for the future. Echeverría mentioned that hydrocarbons in Mexico were 'as good as the Persian Gulf'¹⁹ – that is to say, he confirmed the comparison that days earlier he had condemned as 'international maneuver' by the US press to weaken the prices on the barrel.

The Mexican leader also told President Ford and Secretary of State Henry Kissinger that Mexico should sell at market prices, otherwise ‘the press would attack us if we sold at reduced prices’.²⁰ Echeverría assured that Mexico would undoubtedly seek the best price for its oil, but at the same time he was interested in promoting a system of international cooperation in which the price of a barrel would not affect the economy of the poorest nations.

The cover of *The New York Times* the day after the meeting emphasized ‘Mexico’s new oil for world sale’, and it was announced that during the meeting Echeverría had promised President Ford that Mexico would not join OPEC.²¹ According to the press, ‘the United States had been hopeful that Mexico would sell the oil on the world market and thereby help drive down the price [...] Mexicans intend to do that, charging the world price but driving that price down by increasing the supply.’²²

Mexico’s relationship with OPEC remained ambiguous until January 1975, when Kuwait’s minister of finance and petroleum announced that ‘Mexico has asked to be admitted to OPEC’ (FOIA, 1975). The Mexican press said that Mexico’s ambassador in the US, José Juan de Olloqui, had traveled to Kuwait for that purpose, but the report was denied by Horacio Flores de la Peña.²³

On 3 January 1975, Flores de la Peña, secretary of National Heritage, one of the most nationalist and radical members in Echeverría’s government, presented his resignation and was replaced by Francisco Javier Alejo. This change was unexpected and had several interpretations: ‘Echeverría has publically and privately repudiated any interest in full OPEC membership and removed from office secretary [Flores] de la Peña, leading [advocate] of OPEC Membership.’²⁴ It seemed that Echeverría would then remain at a mid-point between US interests (increasing production and possibly exports) and OPEC’s, taking advantage of the prices on the barrel imposed by the latter which favored Mexican trade.

The Mexican position was once again controversial in May 1975, when the Shah of Iran, Mohammad Reza Pahlavi, visited Mexico. Speaking at a press conference, the Shah declared that a further increase in oil prices was necessary and that ‘it would be a great pleasure to welcome Mexico to the OPEC’. Echeverría responded that Mexico would participate in the Organization as soon as the invitation was formalized.²⁵ A few weeks later 1975, Echeverría declared in Algiers that Mexico was ‘interested in joining the influential OPEC’.²⁶

In May 1976, a significant step towards the conversion of Mexico into an oil exporter was taken when the secretary of National Heritage announced a substantial increase in the Mexican reserves figure, stating that

the confirmed reserve of crude oil has reached 7 billion barrels [and] if other oilfields are discovered again one after another this year, there is a possibility of having 30 to 60 billion barrels, which corresponds from three to six times the oil reserve of the North of Alaska.²⁷

The CIA reported that Mexico had between 30 and 60 billion barrels, a figure that matched that of Kuwait, and later increased the figure by 75 billion barrels (FOIA, 1976). Figure 17.2 shows the volume of proven hydrocarbon reserves officially announced by PEMEX during 1973–1982. An increase was observed after the entry of the government of José López Portillo, reaching estimates of total liquid hydrocarbon proved reserves at 72 billion barrels on 31 December 1981. Probable reserves at the same date were 58.65 billion barrels, and potential reserves were 250 billion barrels. That is, between November 1976 (6.3 billion barrels) and December 1981 (72 billion barrels), there was an increase of 1,036 percent, and the production reserves ratio in 1981 was 60 years based on an annual production of total hydrocarbons of 1.19 billion barrels (Petróleos Mexicanos, 1981).

The debate over Mexico and OPEC was revived again. Secretary Alejo had stated at the same conference at which he gave the reserves figure that Mexico had a plan to affiliate ‘as soon as possible to OPEC’.²⁸ A telegram from Ambassador Jova reported on a meeting with Fernando Gutiérrez Barrios, the private secretary of President Echeverría, in which the ambassador referred to Alejo’s statements and

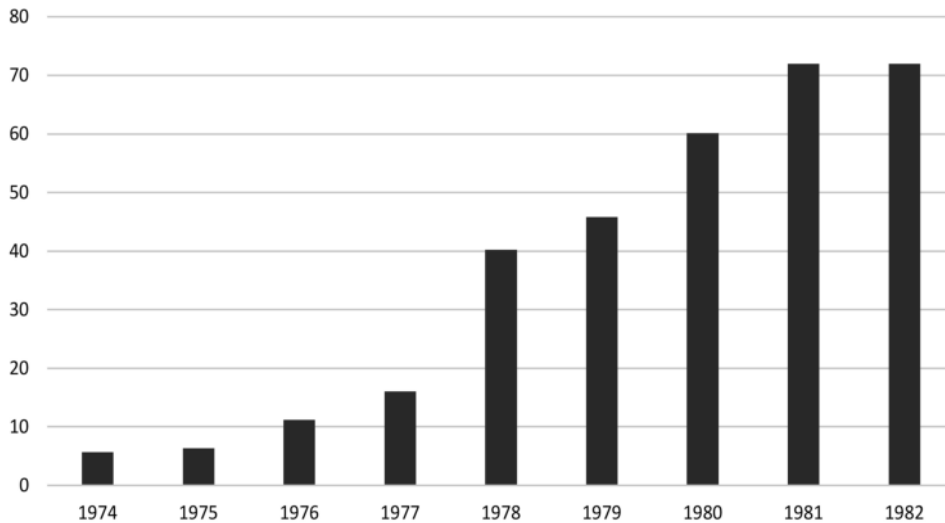


Figure 17.2 Proven hydrocarbon reserves until 31 December, years 1974–1982 (billions of barrels)
Source: PEMEX, Memoria de labores, years 1974–1982.

warned: ‘I would hope that it would be discussed with us first’, drawing the attention of the secretary to the provisions of the commercial law. Gutiérrez Barrios assured that there would be no entry to OPEC, but the diplomat’s comment clearly summed up the Mexican ambivalence:

Regardless of many reassurances we have had on OPEC and despite our understanding that there is no change in the Mexican position and that Mexico’s interest, as president Echeverría himself as told me, would not be served by membership in OPEC, we must not forget that we are dealing with a highly ideologically motivated government. There have been past instances where Echeverría as assured us of one thing and a few months later has done the opposite.²⁹

A few days later, Gerald Parsky, an assistant to the US treasury secretary, told reporters that the US would take action if Mexico decided to join the oil cartel:

Mexico will not be a part of OPEC, If Mexico is invited to join OPEC, this possibility will be considered, but will be ultimately rejected because of the enormous disadvantages that it would otherwise involve. Among other things, Mexico would fall under United States legislation, which has abolished a number of trade preferences on imports from OPEC member countries [...] The United States considers Mexico to be a great resource for using non-OPEC oil.³⁰

Reactions to this statement were immediate. Parsky’s statement was labeled as interventionist and interpreted as an intimidation (El Universal, 1976). In spite of media pressure, there was no change in the official position: Mexico expressed solidarity with OPEC, but in practice it continued to export to the US and Israel and there was no attempt to formalize its membership to OPEC.

The presidential succession was approaching and, as the campaign of José López Portillo progressed, a new oil project started to be developed. Thus, the López Portillo campaign moved the focus of the debate

on the development of the Mexican energy sector to the potential it had to solve, in the short term, the financial obstacles of the country.

In a meeting with President Ford once he was elected, López Portillo referred to what he saw as the limitations of PEMEX, where there were

old hands [who] think the oil should stay in the ground for the future. [But] I will have someone at my side to give me the information the old hands and technicians want to keep from me [...] It is hard to make a policy without the information. It is essential to outline our export [capability].³¹

The disagreement with PEMEX's conservative technicians came to an end partly because they were replaced by the new administration but also because the reserves were re-evaluated at 11 billion barrels once López Portillo's government took office (December 1976) (Morales, Escalante and Vargas, 1988, p. 76). Jorge Díaz Serrano, PEMEX's new director, announced that 'having more proved reserves, more could and should be produced. More could and should be exported' (Petróleos Mexicanos, 1977, p. 11). Mexico was shaping up as a net exporter of oil, and the new administration's relationship with the US and OPEC took a new turn.

The 'administration of abundance' and disagreements with OPEC

The governmental transition between Luis Echeverría and José López Portillo occurred in an environment of deepening economic crisis. On 30 August 1976 the peso devalued 59 percent, after 22 years of a stable exchange rate. Between 1971 and 1976, the foreign debt grew from 9.2 to 30 billion dollars (Revah and Chavez, 2015, p. 300). Thus, in September 1976 the Mexican government requested the intervention of the International Monetary Fund (IMF). In exchange for credit, the IMF imposed restrictions on public sector spending, an upper limit on indebtedness and the progressive liberalization of foreign trade.

Under these circumstances, Lopez Portillo's collaborators, particularly Jorge Díaz Serrano (whom he appointed as PEMEX's director), interpreted that oil should be used as a rescue tool. As he noted in his memoirs:

For us there was no doubt: oil was salvation. In order to regain general confidence it was necessary to show that not only good intentions and political fervor are enough to inspire [...] If foreign banks financed us based on the amount of our new reserves, we would receive the signal that recovery could begin.

(Serrano, 1989, pp. 65–66)

Díaz Serrano's endorsement was confirmation of the 11.2 billion barrels calculated by the firm De Goyler and McNaughton (Serrano, 1989, p. 64), and with that endorsement the new oil project found 'the financial base [which] greatly awakened the interested of international banks' (Serrano, 1989, p. 65).

PEMEX's new orientation towards the foreign market was further strengthened in 1977 largely by the discovery of the Akal and Bacab marine fields on the continental shelf of the state of Campeche (Sordo and López, 1988, p. 54). With the figure of 11.2 billion barrels of proven reserves in 1977,³² PEMEX's expansion program set a production rate of 2.25 million barrels of oil per day in 1982 (Sordo and López, 1988, pp. 53–55). The oil boom that followed allowed Mexico by mid-1978 to abandon the guidelines imposed by the IMF. In January of that year, López Portillo incorporated the idea of 'administering the abundance' to his speech, a phrase he repeated tirelessly throughout his government: 'First Petróleos Mexicanos and then the whole country have to start preparing to administer, not only problems and misery, but abundance' (Lopez Portillo, 1980, p. 36). Figure 17.3 shows the increase of crude oil exports in the period 1974–1982.

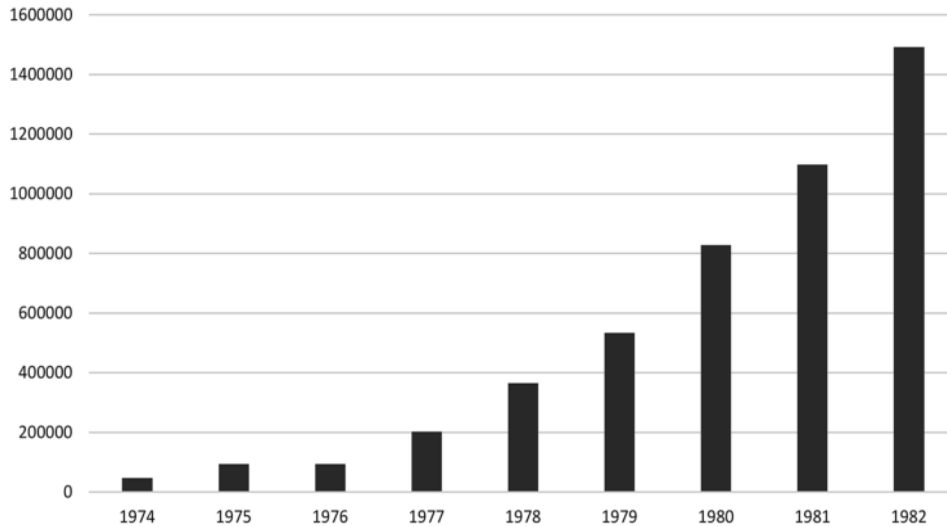


Figure 17.3 Crude oil exports, 1974–1982 (barrels per day)

Source: PEMEX, Memoria de labores, years 1974–1982.

With the recovery that the oil projected for the country, it was expected that the international position of Mexico would be in tune with that of the presidential predecessor –i.e. a foreign policy close to the Third World, this time reinforced with the instrument of negotiation that oil represented. López Portillo, like Echeverría, promoted an international activism that was not in line with the US, but this time it was aimed at Central America (Revah and Chavez, 2015, p. 303). Thus, the supply of hydrocarbons meant political support for the Sandinistas in Nicaragua, a case similar to that of 1973, when President Echeverría sent 400,000 barrels of oil and Mexican technicians in support of Chilean president Salvador Allende.

Among his foreign policy actions, López Portillo acknowledged the Farabundo Martí National Liberation Front and the Revolutionary Democratic Front as a ‘representative political force’ (Revah and Chavez, 2015, p. 309). ‘It was at a regional level that Mexico’s new capabilities in foreign policy were seen more clearly, founded in its newly acquired oil wealth’ (Revah and Chavez, 2015, p. 311). The initiative of the San José Agreement, under which Venezuela and Mexico supplied 160,000 barrels per day to Central America and the Caribbean, was perhaps one of the most specific actions in support of Third World countries.

As part of this dynamic, one of the outstanding issues was the relationship with OPEC. López Portillo defined the Mexican position:

The condition of Mexico is different from that of OPEC, from which, we take of course its price regulation within the market to which we concur [...] There are no regular conditions to participate in OPEC. One thing I want to clarify: we participate in the effort to value raw materials.

(López Portillo, 1980, pp. 27–28)

In this way, Mexico decided to play an individual rather than a collective role – that is, benefiting from the prices set by OPEC but avoiding the political consequences of being a formal member. The US National Security Council staff summed up the Mexican position:

It is unlikely that Mexico would join OPEC, however, because of its stubborn resistance to any outside influence on its oil policies. It already gets the benefits of high OPEC prices on oil, without paying the dues of membership [...] Mexico is determined to maintain the independence of its petroleum industry and resists adamantly any outside influence.³³

The same opinion was stated by the director of PEMEX: 'I believe that Mexico will not enter OPEC, because one of the essential reasons in the philosophy of our government is to preserve self-determination. At the moment a country joins a group like these, it loses its self-determination.'³⁴ In addition, Díaz Serrano viewed OPEC with great mistrust and had no intention of seeking new approaches: 'The OPEC members [...] have never agreed with each other or have complied with the rules which they themselves establish' (Díaz Serrano, 1989, p. 113).

Between 1976 and 1979 there were no major declarations regarding OPEC, but the policy of exploitation and export promoted by Mexico in 1979 'was increasingly aggressive and opted for policies of agreement, production and prices more favorable to the interests of industrialized consumers than to those of OPEC' (García Silva, 1985, p. 6). At the multilateral level, Mexico took a 'world energy plan' focused on long-term energy transition to the UN General Assembly in September 1979.³⁵ This plan ignored the debate on hydrocarbons in the short term and proposed to untie oil from the discussion on world trade of other raw materials, which was one of OPEC's basic demands (García Silva, 1985, p. 7). Consequently, the plan was barely supported by the international community and ignited the distrust of producing countries (García Silva, 1985, p. 8).

Following the second oil shock, the situation of the international hydrocarbon market in the early 1980s was characterized by an increase in non-OPEC production (Petroleum Intelligence Weekly, 1981c), a reduction in consumption in industrialized countries and an oversupply as a consequence of the decrease in demand that led OPEC to reduce production in order to maintain prices. Oversupply in the market similarly impacted on Mexico, and in March 1981 Mexico began to review the possibility of reducing the price of Maya crude (heavy, with 22.5 API) in response to pressure from its customers (Petroleum Intelligence Weekly, 1981a). While OPEC approved cutting production by 10 percent, on 1 June 1981 Mexico announced a price reduction, with the director of PEMEX lowering the price of export crude by four dollars per barrel (from 34.60 to 30.60 dollars): 'Mexico's dramatic \$4 a barrel reduction in official export prices all but ruins the negotiating position of producers trying to protect the crumbling edifice of OPEC's maximum selling prices' (Petroleum Intelligence Weekly, 1981b).

The decision resulted in the resignation of Díaz Serrano from the management of PEMEX since he had not consulted with his economic cabinet the decision to lower the price of the barrel. In an attempt to rescue the situation, Mexico's secretary of heritage and industrial development José Andrés de Oteyza announced that the price of the Mexican barrel would increase by US\$2 dollars, effective from July, and 'the customer who did not accept would not be sold again' (Díaz Serrano, 1989, p. 109). A drop in exports and consequent loss of revenue was the result. President López Portillo in his message to the nation on 1 September 1981 said that Mexico 'knew how to eat the crisis' after the depression of June and July that year, and that the prices of the Mexican oil blend would gradually align with the \$32 dollars of the Arab light (Petroleum Intelligence Weekly, 1981d).

In April 1982, PEMEX announced that it would maintain its export levels below 1.5 million barrels a day, 'to demonstrate its endorsement of Opec's March decision on production restrictions to bolster prices'. PEMEX also announced that it would accept OPEC observer status with the sponsorship of Venezuela (Petroleum Intelligence Weekly, 1982e).

Nevertheless, a formal invitation by OPEC to be an observer was rejected by the Mexican government between April and June 1982, according to Gilberto Escobedo, PEMEX's deputy commercial director, who acknowledged: 'Our position toward Opec is one of respect without losing our independence. This policy has been good and convenient so far for Mexico,' and he concluded: 'Some objectives of Opec are

coincident with Mexican international policy. But for us to become a member of an oil-producing group, we would have very little to gain and a lot to lose' (Petroleum Intelligence Weekly, 1982g). The official also acknowledged that the measure to cut exports had been a statement of solidarity that did not involve a specific commitment or deadline.

The ceiling was a personal offer by the minister of Patrimony as a support for Opec policies, but that does not carry as much weight as the National Energy Plan's 1.5-million b/d target [...] In any given day we can go to 1.6 or 1.7-million, as long as the average stays 1.5-million annually.

(Petroleum Intelligence Weekly, 1982g)

In August 1982 exports indeed totaled 1.65 million barrels per day (Petroleum Intelligence Weekly, 1982h), and during the same month Mexico accounted for 25 percent of total US oil imports (Petroleum Intelligence Weekly, 1982i). Also, in exchange for an advance financing of \$1 billion dollars, Mexico supplied the US Strategic Reserve (Petroleum Intelligence Weekly, 23.08.1982f). A similar type of transaction was made with customers from Spain and Canada (Petroleum Intelligence Weekly, 1982j). However, the new international scenario at the beginning of the 1980s, a new US administration that imposed high interest rates, and the depreciation of the oil barrel led Mexico to seek an agreement with the IMF in 1982. At the time, 'not even the announcements of larger reserves were sufficient to obtain loans as easily as they had been obtained in the past' (Garcia Silva, 1985, p. 12).

Conclusion

This essay reviewed the way in which the Mexican oil industry sustained growth from 1974, when the country achieved energy self-sufficiency due to the discovery of large hydrocarbon reserves in the south-east. Thereafter, oil production surpluses began to sell on the export market and debate arose regarding Mexico's position towards OPEC.

With the change of government from Luis Echeverría to José López Portillo in 1976, in the midst of a serious economic crisis, the new administration opted for oil to be used as an instrument for the capture of economic resources, which meant that deep changes in the economic structure of the country – for example, fiscal reform or the rethinking of measures to boost the agricultural and industrial sectors – did not take place.

In the international scenario, Mexico maintained a position that in some way continued the actions of President Echeverría. Thus, López Portillo supported Third World demands in favor of a New International Economic Order. For example, Mexico and Austria organized the North-South Dialogue in October 1981. Nevertheless, there was considerable ambiguity because, despite the pro-Third World agenda speeches in multilateral forums, Mexico never fully subscribed to either the Non-Aligned Movement or OPEC. Although the prices set by OPEC were used to its advantage, the decision was not to formally become a member. This was in part due to a reluctance to follow the policies of an external entity since the Mexican oil industry, nationalized in 1938, had a different status from that of the OPEC countries and the structure of the Mexican economy differed from that of OPEC members.

Autonomy abroad, particularly in Central America, was largely achieved and promoted on the back of the Mexican oil boom. But the scenario dramatically changed with the hard economic crisis at the beginning of the 1980s, when López Portillo's administration had to seek the help of the IMF and the US. By then, oil was being used not as an instrument of autonomy abroad but as a tool to obtain credit. Mexico's margin for action was then constrained by economic catastrophe largely derived from its disastrous 'administration of abundance'.

Notes

- 1 *New York Times* (1974). 'U.S. Officials Receive Reports Of a Major Mexican Oil Find', 12 October.
- 2 *New York Times* (1974). 'A U.S. Company Spread News of Mexico Oil Find', 20 October.
- 3 *New York Times* (1974). 'Mexico Tying Oil to Nationalism', 15 October.
- 4 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (21.10.1974). Folder III-6039-26(1). 'Noticias sobre nuevo yacimiento de petróleo en México', from Rafael Urdaneta, Mexico's Ambassador in Canada, to Minister of Foreign Affairs. Ottawa, 21 October 1974. Attached newspaper: 'Mexico oil wealth reports a "trick" to depress prices', *The Gazette*, 21 October 1974.
- 5 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (17.10.1974c). Folder III-6039-26(1). 'Telegram 53751, from Minister of Foreign Affairs to Mexico's Embassy in Chile. Mexico City', 17 October 1974.
- 6 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (17.10.1974b). Folder III-6039-26(1). 'Noticias sobre México publicadas en la prensa israelí. Yacimientos de petróleo', from Pedro González Rubio, charge d'affaires ad interim Mexico's Embassy in Israel, to Minister of Foreign Affairs. Tel Aviv, 18 October 1974. Attached newspaper: 'Mexico bids for role in OPEC', *The Jerusalem Post*, 17 October 1974.
- 7 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (17.10.1974b). Folder III-6039-26(1). 'Noticias sobre México publicadas en la prensa israelí. Yacimientos de petróleo', from Pedro González Rubio, charge d'affaires ad interim Mexico's Embassy in Israel, to Minister of Foreign Affairs. Tel Aviv, 18 October 1974. Attached newspaper: 'Mexico bids for role in OPEC', *The Jerusalem Post*, 17 October 1974.
- 8 *New York Times* (1974). 'Mexico Accepts Oil-price System', 16 October.
- 9 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (17.10.1974a). Folder III-6039-26(1). 'Comentarios en la prensa francesa sobre el hallazgo de petróleo en México', from Silvio Zavala, Mexico's ambassador in France, to Minister of Foreign Affairs. Paris, 17 October 1974. Attached newspaper: 'Mexico Urged By Leftists to Join Oil Cartel', *International Herald Tribune*, 17 October 1974.
- 10 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (17.10.1974b). Folder III-6039-26(1). 'Noticias sobre México publicadas en la prensa israelí. Yacimientos de petróleo', from Pedro González Rubio, charge d'affaires ad interim Mexico's Embassy in Israel, to Minister of Foreign Affairs. Tel Aviv, 18 October 1974. Attached newspaper: 'Mexico bids for role in OPEC', *The Jerusalem Post*, 17 October 1974.
- 11 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (28.10.1974). Folder III-6039-26(1). 'Noticias sobre México en la prensa israelí', from Pedro González Rubio, charge d'affaires ad interim Mexico's Embassy in Israel, to Minister of Foreign Affairs. Tel Aviv, 29 October 1974. Attached newspaper: 'Mexico and OPEC', *The Jerusalem Post*, 28 October 1974.
- 12 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (28.10.1974). Folder III-6039-26(1). 'Noticias sobre México en la prensa israelí', from Pedro González Rubio, charge d'affaires ad interim Mexico's Embassy in Israel, to Minister of Foreign Affairs. Tel Aviv, 29 October 1974. Attached newspaper: 'Mexico and OPEC', *The Jerusalem Post*, 28 October 1974.
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- 17 NARA, Central Foreign Policy Files (18.02.1974). RG 59, 'General Records of the Department of State, Diplomatic Records, Electronic Telegrams 1974'. 'Mexico's posture on the question of OPEC membership,' from American embassy in Mexico to Secretary of State. Available from: <https://aad.archives.gov/aad/createpdf?rid=234463&dt=2474&dl=1345>
- 18 Foreign Relations of the United States (FRUS) (1969-1976), volume E-11, part 1. 'Documents on Mexico; Central America; and the Caribbean, 1973-1976. 'Memorandum of Conversation'. (Magdalena de Kino, Mexico, October 21, 1974, 12-2:30 pm), document 70.

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- 20 Foreign Relations of the United States (FRUS), (1969–1976), volume E-11, part 1. ‘Documents on Mexico; Central America; and the Caribbean, 1973–1976. ‘Memorandum of Conversation’ (Magdalena de Kino, Mexico, October 21, 1974, 12–2:30 pm), document 70.
- 21 *New York Times* (1974). ‘Mexico’s New Oil For World Sale, Echeverria Says’, 22 October.
- 22 *New York Times* (1974). ‘Mexico’s New Oil For World Sale, Echeverria Says’, 22 October.
- 23 NARA, Central Foreign Policy Files (03.01.1975). RG 59. ‘General Records of the Department of State, Diplomatic Records, Electronic Telegrams 1975’, ‘Mexican membership in OPEC, the Trade Reform Act, and GSP’, from American Embassy in Mexico to Secretary of State. Available from: <https://aad.archives.gov/aad/createpdf?rid=125949&dt=2476&dl=1345>.
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- 27 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (11.06.1976). Folder III-6039–26(1). ‘Se remite traducción de un artículo sobre declaraciones del Lic. Francisco Javier Alejo en materia petrolera’, from Carlos A. Bado, charge d’affaires ad interim Mexico’s Embassy in Japan, to Minister of Foreign Affairs. Tokyo, 14 July 1976. Attached newspaper: ‘Circunstancias en torno al cambio de la política petrolera de México’, *Boletín Latinoamericano*, 11 June 1976.
- 28 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (11.06.1976). Folder III-6039–26(1). ‘Se remite traducción de un artículo sobre declaraciones del Lic. Francisco Javier Alejo en materia petrolera’, from Carlos A. Bado, charge d’affaires ad interim Mexico’s Embassy in Japan, to Minister of Foreign Affairs. Tokyo, 14 July 1976. Attached newspaper: ‘Circunstancias en torno al cambio de la política petrolera de México’, *Boletín Latinoamericano*, 11 June 1976.
- 29 NARA, Central Foreign Policy Files (06.05.1976). RG 59, ‘General Records of the Department of State, Diplomatic Records, Electronic Telegrams 1976’, ‘Mexican position on OPEC and North Korea’, from American Embassy in Mexico to Secretary of State, 6 May 1976. Available from: <https://aad.archives.gov/aad/createpdf?rid=241734&dt=2082&dl=1345>.
- 30 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (25.05.1976). Folder III-6052–5(1). ‘Se remite traducción de un artículo aparecido el pasado 20 de mayo en el International Herald Tribune’, from Frumencio Saldana Alcalá, charge d’affaires ad interim Mexico’s Embassy in Norway and Island’, Oslo, 25 May 1976.
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- 32 The increase in reserves was a result of ‘the introduction of a different method of quantification of reserves, less rigorous than the previous one, which included another type of reserve: the proved non-perforated, that is, that which is pending development in a geologically delimited producer site’ (Sordo and López, 1988, pp. 51–52).
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- 34 Archivo Histórico Genaro Estrada de la Secretaría de Relaciones Exteriores México (AHGE). (1977). Folder III-6052–5(1). ‘Declaraciones del Director General Jorge Díaz Serrano 30/V/1977. Conferencia de prensa. Oficinas del Ing. Jorge Díaz Serrano, en el edificio de PEMEX’.
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From foes to friends

The relationship between OPEC and Norway¹

Dag Harald Claes

Norway: becoming an oil producer – of some importance

After the discovery of the gigantic gas field Groningen in The Netherlands in 1959, international oil companies (IOCs) became interested in the potential for oil or gas deposits in the North Sea. At that time, the area was not under state jurisdiction, apart from the internal waters. The first Conference on the Law of the Sea (UNCLOS I) had provided a treaty covering the Continental Shelf in Geneva in 1958, but this had not entered into force, nor had the North Sea coastal states ratified the treaty. Thus, Norwegian authorities simultaneously negotiated delimitation lines with UK and Denmark and conditions for exploration with international oil companies like Shell and Philips Petroleum. The first licenses were announced in 1965. The first commercial discovery was made in 1969 and production commenced in 1971. The exploration was intensified and several large discoveries were made in the early 1970s. In 1972 the Norwegian government established the state-owned company Statoil (now Equinor) and introduced various instruments of state governance and participation in oil and gas production. As Thomassen shows in his chapter (see *infra*, chapter 19), this was largely inspired by models in OPEC countries. The conflicts between IOCs and OPEC governments also increased IOC interest in alternative oil provinces, benefitting the development of the UK and Norwegian parts of the North Sea and Alaska.

Direct political ties with the OPEC countries were strongly limited by the political confrontation between the US and Middle East producers following the embargo of the US in 1973. Norway was (and is) a close ally of the US within the NATO alliance. Together with Turkey, Norway was the only NATO country bordering the Soviet Union. The oil crisis of 1973 also created strong security overtones behind the creation of IEA as a consumer defense against the oil producers. Norway decided to balance its role as oil producer by becoming an associated member of IEA, not part of the oil-sharing instruments of the organization. One can say that the political interests trumped the emerging common economic interests with the established oil producers in OPEC. As the Norwegian oil production increased (Figure 18.1), the common economic interests with other oil producers became more visible. At peak production around the year 2000, Norway was the world's third largest net exporter of oil (Norwegian Ministry of Petroleum and Energy, 2001, p. 46). New discoveries in the last decade will extend the present level of production at about two million barrels per day.

Sellers in a market can simultaneously compete for market shares and face product prices as collective goods (Underdal, 1987, p. 175). When actors, in such a way, have both common and conflicting interests,

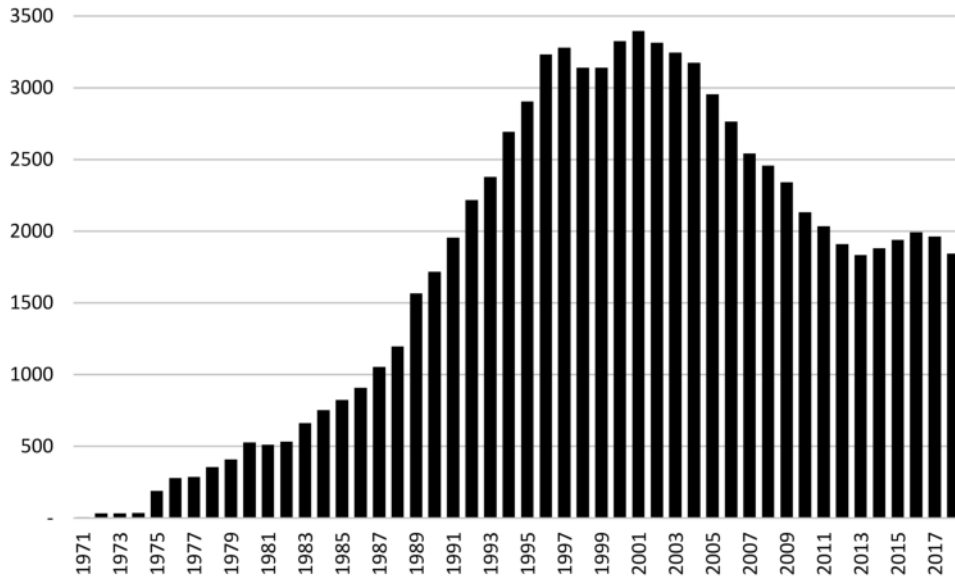


Figure 18.1 Norwegian oil production, 1971–2017 (th. barrels per day)

cooperation presuppose that all actors ‘eschew their dominant strategy. In addition, they must not greedily attempt to obtain their most preferred outcome once they have settled at the unstable outcome they prefer to the stable equilibrium’ (Stein, 1990, p. 32). These observations from the theoretical literature on cooperation among states have their parallel in economics in cartel theory.² According to Crèmer and Isfahani (1991, p. 30), a cartel must be able to do the following: (i) determine a price for the group as a whole; (ii) determine a production level for the group as a whole; (iii) allocate output among members; and (iv) detect and punish cheaters. These defining characteristics of a cartel do not determine how successful a cartel is when it comes to the ultimate goal – increasing the wealth of the members – since a number of structural factors and factors related to market changes influence the successfulness of the cartel. The first two points in the list above have to do with the cartel’s relations to the market, while the last two points have to do with internal bargaining problems. In this paper, the focus is on the third factor: allocating output among members. In periods with weak prices, this implies limiting production and distributing quotas.

The special ‘twist’ of this chapter is the attempt by OPEC to extend this allocation of output beyond the members of the organization. In the process of setting the total production level correctly and thus achieving the desired price level, the sellers find themselves in a traditional prisoner’s dilemma situation. All producers have an interest in limiting overall production to ensure a high oil price, but at the same time it is in the individual producer’s interest to sustain (or increase) their own production. In such a case, the actors can gain by cooperating (reducing production), but individually they can gain more by not cooperating, presupposing that others do. This dilemma is the same for producers both inside and outside of OPEC. The dilemma became particularly pressing in the mid-1980s. In 1973, OPEC had a 52 percent share of world oil production. The price policy of the organization during the rest of the 1970s put constraints on the increase in oil consumption. During the first half of the 1980s, OPEC, or more correctly Saudi Arabia, tried to defend the price by cutting production. However, the price stimulated increased production in non-OPEC oil-producing countries. The challenges triggered a desired by OPEC to include key non-OPEC producers in their market sharing arrangement. A political bargaining process was opened also towards Norway, which in 1986 agreed to contribute by limiting the increases in its oil production – at least on paper.

The OPEC–Norwegian bargaining process

Norwegian conflict behavior, 1982–1985

In the first half of the 1980s, OPEC, and particularly Saudi Arabia, found stabilizing the market an increasingly costly matter. At the meeting in March 1982, the organization initiated a quota-sharing system among its members. In the wake of this OPEC meeting, the first moves were made towards Norway and Britain to help limit oil supplies: ‘OPEC will now seek contact with countries such as Norway and Britain, and of course Mexico too, to arrange cooperation on the oil prices.’³ In November 1982, OPEC secretary general Nan Nguema was invited to Oslo. OPEC seemed interested in some sort of consultations with certain members of the International Energy Agency (IEA).⁴ OPEC convened several times in the spring of 1983 for the purpose of stabilizing the market through production limitations. On 11 February 1983, Saudi Arabian oil minister Sheik Yamani stated, ‘Saudi Arabia will no longer play the role of defending the benchmark price and will let others bear the responsibility for their own mistakes’ (Terzian, 1985, p. 314). Yamani later admitted that OPEC had not understood that oil was overpriced: ‘But when OPEC supplies started to decline sharply in 1981 and 1982, as a result of the fall in demand and the rise in non-OPEC supplies, we recognized too late that oil was overpriced’ (Yamani, 1986, pp. 11–12).

On 19 February 1983, the British National Oil Company (BNOC) reduced the oil price by \$3 to \$3.5/barrel. Norway and Nigeria followed suit. OPEC production had declined to 14 million barrels per day. At the extraordinary OPEC meeting in March 1983 the official reference price was lowered from \$34 to \$29/barrel, and the production ceiling was fixed at 17.5 million barrels per day (OPEC, 1990, p. 208). This official price was sustained for about eighteen months, while Saudi Arabia continued to swing down production. Concurrently, British and Norwegian production continued to increase. Despite repeated appeals by OPEC, Norway showed no signs of considering production limitations. The Norwegian government rather tried to establish political commitments to their planned production level. When representatives of Venezuela’s state oil company, PDVSA, visited Norway in February 1983, the Norwegian host concluded as follows: ‘They [Venezuela’s representatives] showed understanding of the quite special situation Norway and Great Britain find themselves in, with such large production costs it is impossible to organize a variable production for purposes of regulating the prices.’⁵ The Norwegians were obviously aware of their common interests with OPEC:

We have coinciding interests with OPEC in maintaining a steady oil price development. For that reason we would do well also in future to continue to develop the price cooperation with the organization on an informal basis.⁶

Nevertheless, Norwegian contribution to OPEC’s efforts were ruled out, ‘Not least the heavy costs connected with North Sea exploitation indicate that Norway will never be able to become a swing producer.’⁷ All Norwegian oil production takes place offshore and requires large investments in production platforms and infrastructure such as land bases, helicopter traffic, and various support vessels. Norway has always been a high-cost producer. Thus, weak market price in the 1980s could create losses for both companies and the government. Within the Norwegian Ministry of Oil and Energy, the weak oil price was a constant concern, and by the spring of 1984 the ministry had prepared alternative responses to OPEC’s demand for contributions.⁸

In August 1984, Saudi Arabia’s production had declined to just above four million barrels per day, while OPEC total production was around 16.5 million barrels per day. The general perception in OPEC circles was that when the oil companies started their usual stockpiling for the coming winter, the market would tighten up. While OPEC prepared an extraordinary meeting on 28–29 October 1984, Norway

entered the international oil political arena and created a new crisis in the oil market, 'a crisis nobody had expected, not even those who triggered it off, the Directors of the Norwegian state oil company Statoil. The OPEC conference that had been called to raise the organization's production ceiling was in fact forced to lower it by 1.5 million barrels a day, in a desperate attempt to save oil prices from the North Sea turmoil' (Terzian, 1985, p. 329). Statoil had offered an official reduction in price of about a dollar and a half.⁹

The immediate reaction in OPEC to this news was strong. 'Norway received rough treatment in Friday's UAE newspapers. Gulf News writes that the Norwegian decision to reduce the price of North Sea oil is extremely difficult to understand.'¹⁰ On October 26, Yamani came to Norway. He had talks with Prime Minister Kåre Willoch and Minister of Oil and Energy Kåre Kristiansen. Yamani was assured that the Norwegian step constituted an adjustment to the market and certainly not an attempt to undermine OPEC's market-stabilization measures. At the same time, Kristiansen gave assurances to Yamani that Norwegian production in 1985 would not exceed that of 1984.¹¹ This turned out not to hold true. Considerable irritation arose in OPEC when further Norwegian production increases became a reality.¹² At the OPEC meeting in Geneva three days later, OPEC's concern regarding the Norwegian policy was expressed: 'The Conference reviewed with great concern the recent developments in the world oil market following the price cuts undertaken by Statoil of Norway and the British National Oil Corporation (BNOC) of the United Kingdom, as well as by Member Country Nigeria' (OPEC, 1990, p. 220). The Saudi Arabian weekly magazine *Igraa* ran an article in the November 15 issue entitled 'The Latest Oil Price Crisis: A Saudi View'. As pointed out in *Middle East Economic Survey*, which printed a translation, the article was billed as 'having been written by a 'neutral international oil expert' – but the article clearly reflects an insider's viewpoint'.¹³ Probably the views were those of Yamani. The article states that demand was picking up in the last quarter of 1984, until the big surprise – Norway's decision to reduce its price by \$1.35/b.

10 days before Norway's decision, the prevailing Norwegian view was that the price of oil would begin to rise in November and December as demand increased and that there would be no problems with prices or production until March or April. Therefore the Norwegian decision was based on non-economic considerations [my italics]. Normally Norway does not take the initiative on pricing but follows the British lead. It is remarkable that in this case the smaller producer took the initiative ... Some people believe that internal reasons were behind the Norwegian decision, since the president of the national oil company Statoil ... belongs to the opposition political party and wanted to embarrass the present government ... There are also those who say that there was American pressure on Norway.¹⁴

The general opinion regarding the market situation was that the OPEC measures had stabilized the market, demand would soon increase, and everything would recover. Yamani said oil prices would rise sharply in the coming months due to greater demand and because the importing companies were draining their stocks: 'I don't care about what Norway will do. The situation will right itself when demand increases and the market improves.'¹⁵ He was to be proved wrong.

With the 'October crisis' of 1984, Norwegian innocence in the political game of international oil was gone. The argument that Norway was a marginal producer with high production costs, and thus exerted no influence on the international oil market, became less convincing. Norway had shown that it could, in certain situations, actually influence market developments. On the other hand, the high production costs continued to be an applicable argument for self-commitment. As pointed out by Thomas Schelling (1980, p. 22), bargaining power is the ability to deprive oneself of action alternatives and at the same time make sure that the opponent perceives the deprivation. The first turn of events in this bargaining process was that Norway revealed it could actually influence the market, which made it more attractive for others to influence Norwegian behavior. The next step was for OPEC to put diplomatic and market pressure on Norway.

OPEC changes market strategy, 1985

By 1985, OPEC's share of the market had dropped to 28 percent. The economic consequences of the reduced market share hit hard as the dollar exchange value dropped in 1985. The pressure on Saudi Arabia increased steadily when other member countries attempted to compensate for reduced income by increasing production above quotas. In the course of spring 1985, Saudi production fell toward two million barrels per day in order to keep the price at a level between \$26 and \$30/barrel. The Norwegian side made few moves.

In March 1985, the Norwegian oil minister, Kåre Kristiansen, visited Saudi Arabia for talks with Yamani. This meeting was described as 'idyllic' compared with the meeting in October 1984. Kristiansen again gave assurances that Norwegian production would not rise beyond the present level in the next years. At the meeting, both actors seemed to regard the market as stable and perhaps tending to rise. Yamani desired Norwegian production limitations, though he did not express this directly. Kristiansen made it clear 'that Norwegian oil production cannot be reduced due to the high level of investment on the continental shelf and the long-term development projects'. Kristiansen said also that informal channels had been established from the Norwegian authorities and from Statoil to OPEC, and especially to Saudi Arabia, for the purposes of directly communicating reasons for particular market behavior if circumstances should demand it.¹⁶

The market conditions did not improve, and at the OPEC meeting in Geneva on 9 December 1985, the members agreed to change their market strategy from defending a high oil price to defending the OPEC countries' market shares. The resolution promptly triggered a price drop for crude of \$3 in three days.¹⁷ 'The market has gone mad,' an oil broker told *Aftenposten*. 'No serious oil expert dares to predict what the oil price will be tomorrow, next week, or in 1986.'¹⁸ The rhetorical game around this resolution had the objective of drawing attention just as much to producers outside OPEC as to those within the organization who were failing to keep to their quotas. Thus, strong complaints and threats concerning a price war were expressed: 'OPEC still harbors the hope that other producers will cooperate in trying to maintain prices by curbing their output. But implicit in the communiqué issued yesterday is the threat of a price war if they do not.'¹⁹ Some OPEC representatives made threats of retaliation unless North Sea producers cut production.²⁰ The only official Norwegian reaction was a statement by Kristiansen to the Norwegian Broadcasting Company saying that Norway was unable to cut its oil production in the short term as requested by the organization.

The first question concerning the bargaining relationship in this phase is whether Norway interpreted the move as a direct and open threat to initiate a price war if Norway did not limit production. Statements made by Kristiansen indicate that Norwegian authorities did *not* interpret OPEC's action as directed toward Norway:

There is no doubt that the main reason for the price drop is the strong production increase by Saudi Arabia and other OPEC countries. When before it has been indicated that Norway ought to reduce production, the point has been precisely to avoid the price drop that has just occurred. No motive any longer exists for Norway to lower production. I fail to see what we can do today.²¹

In hindsight, the situation has been interpreted as the main objective of Saudi Arabia's policy of being a threat to those OPEC countries not sticking to their quotas:

It was clear, however, to the Norwegian authorities that the collapse of the oil price was wanted. Saudi Arabia wished both to achieve a larger share of oil sales for herself by forcing other OPEC countries to accept lower quotas and to reverse the general decline in OPEC's joint share of the market by means of a generally lower price level. It was clear that any early steps taken by Norway

would be contrary to Saudi Arabia's policy – they would be meaningless, because they would not help to achieve the desired objective: a higher and stable oil price.

(Udgaard, 1989, p. 65)

However, the point for the government was not Norway's high or low volumes of production but rather their realization that not much importance would be attached to Norwegian policy because the internal conditions of OPEC could be considered as decisive.

(Ramm, 1989, p. 57)

The second question is the solidity of the Norwegian self-commitment. The content of section 20 of the Petroleum Act²² gave the necessary legal provisions for the authorities to regulate production. It must have been obvious to OPEC that, should the Norwegian authorities have wished to limit production, they had the means of doing so. Thus, there was every reason for OPEC to continue to exert pressure on Norway. It soon turned out that the latter started to yield.

The Norwegian promise to cooperate, 1986

In the spring of 1986, the OPEC diplomacy of the Norwegian government steered a somewhat unsteady course. On 21 January, Kristiansen told *Aftenposten* that the price drop was due to the large increases in production by Saudi Arabia and the other OPEC countries.²³ The following day *Norges Handels & Sjøfartstidende* wrote: 'Oil and Energy Minister Kåre Kristiansen has opened the door a crack for production limitations on the Norwegian continental shelf. The aim is to help to attain a stable oil price.'²⁴ *Aftenposten* wrote: 'Norway might be willing to reduce oil production if oil prices continue to fall.'²⁵ Two press releases from the Ministry of Oil and Energy followed in close succession, one supporting OPEC and one a disclaimer. 'As far as OPEC is concerned, measures taken by Norway are only conceivable in a situation where OPEC is willing and able to regulate production in an effective manner.'²⁶ 'The oil and energy minister describes it as misunderstood when he is interpreted as going in for a change in Norway's long-term production and price policy.'²⁷ The international oil press had already reported the Norwegian support for OPEC's policy, and Yamani had made a statement praising Norway, which had to be disclaimed immediately on the Norwegian side: 'Sheik Yamani commended on Thursday Norway's fundamental support of limitation in oil production' 'In a statement to the Norwegian press agency NTB the oil and energy minister said that Sheik Yamani's statement was made on the basis of false premises – 'such measures (production limitations) are not decided by Norwegian authorities', the minister pointed out.'²⁸

A year later, Kristiansen described the situation as follows:

I recall an odd episode. Now, it was not my mistake, but a press release went out from the Ministry concerning an address I was to hold at a seminar in Sandefjord just after OPEC had caused the dramatic oil price to drop in the winter of 1986. A secretary wrote in the press release something quite different from what I said—namely, that Norway was willing to cooperate with OPEC on certain conditions. But that was not what I said in Sandefjord.

(Lindøe, 1987, pp. 102–103)

On the question that he had gotten cold feet and deleted the paragraph before his speech, Kristiansen replied, 'No, the paragraph was part of an earlier draft, but we had discussed the speech in the Ministry and decided to delete it. However, it became part of the press release' (Lindøe, 1987, pp. 102–103).

This episode may have been caused by the suggested failure in communication between the minister and the civil service, but it soon appeared that Norway had adjusted its policy:

It was gradually made clear that Norway 'would not work against' any measures OPEC might reach agreement on. This was one of several factors the Government took into account when it debated a proposal early in 1986 to step up the development of the Gullfaks field and finally decided against such a course

(Udgaard, 1989, p. 66)

The official explanation was consideration for the investment pace on the shelf, but there is reason to believe that the signal was interpreted by OPEC as a positive cooperative measure. On February 9, Kristiansen met with Venezuela's oil minister, OPEC president Arturo Hernandez Grisanti. The meeting was described by both parties as useful, despite the lack of tangible results. Kristiansen expressed willingness to cultivate diplomatic contact with OPEC countries. 'I have personally given very high priority to contact with representatives of these [OPEC] countries.'²⁹ In April 1986, Undersecretary of State Torbjørn Frøysnes said,

We will not be the ones to take the first step. However, if the OPEC countries, especially Saudi Arabia, make concrete moves with the objective of raising the oil price to a higher level, it has been the Government's view that we on the Norwegian side have been obliged to consider our own moves.³⁰

That the Norwegian argument about the country's irrelevance in the oil market was weakened is apparent from the following statement made by the undersecretary at the Prime Minister's Office, Morten Udgaard,

There has never been any doubt that the Government's attitude has been that Norway has a role and a responsibility [in the oil market] relative to our oil production, which is modest in scope viewed internationally, but which nevertheless involves a certain share of responsibility.³¹

Although Norwegian authorities still did not consider supporting OPEC actively by means of production limitations, the traditional free-rider attitude had changed. However, now the decision-making process itself appeared somewhat labile. Several actors, both politicians and civil servants, made statements that increased the confusion regarding the Norwegian position (Engesland, 1989). For instance, at a press conference on 19 March 1986, in connection with a meeting between the OPEC ministers and representatives from Egypt, Mexico, Malaysia, Angola, and Oman, President Grisanti stated that 'signals have been received to the effect that countries outside OPEC, which until the present have consistently said no to cooperation, may perhaps cooperate after all'.³² This statement may refer to remarks made by the director of the Norwegian Central Bank, Hermod Skånland, a few days earlier, when he expressed the idea of limiting Norwegian oil production purely out of Norwegian self-interest.³³

In May 1986, the Norwegian domestic political scene took a turn of events that made 'the OPEC connection' a top political priority. A government crisis developed over the revised national budget proposal put forward by the Conservative government. The outcome led to the appointment of Gro Harlem Brundtland as prime minister of Norway. In her new Labor government's inaugural address, it was stated, 'If the OPEC countries agree on measures capable of stabilizing the oil prices at a reasonable level, the Government will contribute to such stabilization, which may in turn ensure future supplies of oil and gas.'³⁴ The change of government made it easier to change the policy towards OPEC in full openness.

Out of consideration for opposition at home, as well as abroad (read: the US), the government had to put its policy into practice with caution. It pointed out that it was a matter of limiting production *growth*, not the total produced volume. The Norwegian measures would be dependent on OPEC itself enforcing

measures inclined to stabilize prices. However, the new policy was probably not yet clearly formulated and internally communicated. For instance, Minister of Finance Gunnar Berge at this point stated, 'We must act jointly with Britain,'³⁵ and Statoil director Arve Johnsen, influential in the Labor Party, strongly criticized cooperation with OPEC.³⁶ Through the spring of 1986, Norwegian measures remained somewhat unclear. The new minister of oil, Arne Øien, explained this situation as follows:

This [the form the measures would take] has not yet been clarified. Even when this has been decided, there would be no point in publicly unfolding such a strategy because we may find ourselves in something resembling a bargaining situation with OPEC.³⁷

The direct diplomacy between OPEC and Norway was intensified.

In June 1986, Yamani and Øien met for the first time, in Venice. The atmosphere pervading this meeting provides insight into the type of bargaining relationship the parties entered into. In accordance with Yamani's security routine,³⁸ the Norwegian representatives were informed only of the time of the meeting, not the place. It proved to be the Hotel Daniel, the very hotel the Norwegian representatives had checked into the previous evening.³⁹ There is reason to believe the first part of the meeting was characterized by strong invective from Yamani, prompted by the Norwegians' lack of will to actively limit production. *Aftenposten* wrote, 'Yamani put forward requirements that were turned down by his colleague.'⁴⁰ He is said to have used consideration for the poorer OPEC countries' dependence on oil revenues to feed their people as an argument for Norwegian production limitations. This must be assumed to have created a highly tense atmosphere. Yamani's refusal to comment on the meeting or meet photographers after it (he allowed himself to be photographed after meetings with Kristiansen) was also a sign of tough discussions. At this juncture, the Norwegian strategy toward OPEC was clarified, and the delegation was probably prepared for just this kind of confrontation. The Norwegians made it quite clear that Norway could limit only the growth of production, and that any measures would be conditional on OPEC's own policy. Moreover, the resolution would be a unilateral one and would not be a result of pressure or threats from OPEC.⁴¹ Here again the Norwegian representatives employed a self-commitment strategy, consistently referring to the existing parliamentary situation in Norway. With a minority government, there is an obvious limit to what a government can do if it is to avoid jeopardizing its own position. The alternative would have been a less pro-OPEC government. Thus, any measures beyond those indicated were not to be considered. Furthermore, there was a need for Norway to receive unambiguous positive signals expressing OPEC's satisfaction with Norwegian policy so that the policy could be 'sold' at home. This was also explicitly conveyed to OPEC. This strategy created a commitment on the part of OPEC, as speaking of Norway in laudatory terms made it more difficult for OPEC at a later date to demand further measures from Norway. As long as there are other non-OPEC producers who have failed to make any limitations, new attempts to exert pressure on Norway would appear dubious. In this specific bargaining situation, Norway possessed the aces. The Norwegian self-commitment was perceived as credible. The sharp invective from Yamani can be regarded as an attempt to put Øien to the test, to determine whether he could be induced to yield. Toward the end of the meeting, Yamani is said to have adopted a more conciliatory attitude.⁴² The follow-up to the Venice meeting consisted of the establishment of regular contact between the OPEC Secretariat and the Ministry of Oil and Energy in Norway. This channel has later been used to clear up misunderstandings and clarify positions.⁴³

Norwegian cooperation acknowledged by OPEC, 1986–1990

At the OPEC Conference in Brioni in June 1986, which took place immediately after the meeting between Yamani and Øien in Venice, the retiring president, Grisanti, said in his opening address,

A noteworthy development was the policy position taken recently by the new Norwegian Government and its declared intention to open its doors to dialogue with OPEC with a view to contributing to the Organization's efforts towards market stabilization. This position by a major industrialized oil producing exporting country could open the way for a concerted all oil producers' effort to stabilize the market in face of a possible price disaster.⁴⁴

The new president, Rilwanu Lukman, expressed the same opinion. On the other hand, Iraq's oil minister, Qassim Taki al-Oraibi, thought the measures described by Norway were completely inadequate and pointed out how unprofitable Norwegian oil production was, considering the price level of the day.⁴⁵ The Brioni meeting failed to provide 'the clarification necessary for the Norwegian government to assess national measures as a contribution to the stabilization of the oil price'.⁴⁶ The OPEC discussion continued in Geneva on July 28. On August 5, OPEC established new production quotas, and the market reacted spontaneously with a price increase. Norway's reaction was positive; the resolution was regarded as 'an important step in the direction of stabilizing the market'.⁴⁷ A Norwegian move was promised before the entry into force of the OPEC resolution on 12 September 1986.

On September 10, the Ministry of Oil and Energy issued a press release stating that

the Government has formed a plan to limit growth in Norwegian oil export. In the fourth quarter of 1986 the authorities will do this by refining and building permanent emergency stocks of Government revenue oil that is today sold in the market. This will make it possible to reduce the net export of crude by around 10% in November and December.⁴⁸

The resolution resulted in some 70,000 to 80,000 barrels per day being removed from the international market. The following official statement was promptly made by OPEC's President Lukman, 'We are pleased about Norway's action. It is extremely encouraging, and we hope that other North Sea producers will follow the good example [Norway has] set.'⁴⁹ On 13 September, Yamani came to Norway for a short meeting with Øien at the Park Royal Hotel at Fornebu Airport. Once more, the meeting was held behind closed doors. This time no invective was heard against the Norwegian position. The whole meeting was held in a highly conciliatory atmosphere and proceeded amicably.⁵⁰ Yamani granted an interview to the Norwegian Broadcasting Corporation and praised the Norwegian measures.⁵¹

At the OPEC meeting in October, Norway was again referred to in highly positive terms. Toward the end of October, Øien and OPEC representatives held two meetings. These were regarded more as courtesy visits and a confirmation that cooperative relations had been established. The tug-of-war aspect of the relationship prominent at the Venice meeting in June had disappeared altogether. A cooperative relationship had been established and was to be cultivated; the joint interests were stressed. Moreover, Norway indicated that follow-up of the measures subsequent to January 1987 was to take place.⁵² This was, in fact, effected by Norway on 13 January 1987: 'The Government aims at reducing Norwegian oil production in the first half of 1987 by some 80,000 b/d commensurate with the approved production framework.'⁵³ The measures were subsequently extended, at first to the end of 1987, in approximately the same form. The Norwegian Labor government held office until 1989. The Norwegian production limitation was sustained throughout this period.

When the Conservative coalition assumed government after the election in 1989, rumor held that the regulation was to be abolished. For the first half of 1990 the production limitation was cut from 7.5 percent to 5 percent. The decision to cut back on the limitation was a compromise between the Conservative government and the Labor Party, which wanted to uphold it. In June 1990, the Norwegian government decided to abolish production-limitation measures altogether. In an interview a few days before the decision, the Norwegian oil minister, Eivind Reiten, stated that political considerations (such as human rights in the OPEC countries) had no place in the discussion of Norwegian support for OPEC. In fact, the

Norwegian measures were not to be regarded as cooperation with OPEC at all, and he claimed that 'this production regulation has not triggered off any contacts with OPEC countries which we would not have had as an oil producer anyway'.⁵⁴ OPEC noted the Norwegian decision without any official criticism; on the contrary, OPEC secretary general Subroto was sympathetic.⁵⁵ The main explanation behind the Norwegian decision and lack of criticism is the fact that the oversupply in the market had turned into a perceived demand pressure. By the summer of 1990, demand for oil had picked up substantially, and the midterm outlook indicated an upward price pressure, making producer cooperation to keep prices up superfluous. Furthermore, Middle East politics intervened as the Iraq-Kuwait War increased the price from \$16.88/barrel in July 1990 to \$34.55/barrel in September. The other oil producers compensated for the loss of Iraqi and Kuwaiti oil, and the oil price returned to an average of \$20.05/barrel in 1991 and \$19.37/barrel in 1992.

Norway's abstention in the 2016 OPEC–non-OPEC cooperation

Following the dramatic price fall in the autumn of 2014, new efforts to establish cooperation between OPEC and non-OPEC producers emerged. The situation was very similar to the early 1980s, and the lessons from then were prominent in the minds of the Saudi Arabian leadership:

The experience of the first half of the 1980s was still in our minds. At the time, we cut our production several times. Some OPEC countries followed our lead, and the aim was to reach a specific price that we thought was achievable. It didn't work. In the end, we lost our customers and the price. The Kingdom's production dwindled from over 10 mmb/d in 1980 to less than 3 mmb/d in 1985. The price fell from over \$40 per barrel to less than \$10. *We are not willing to make the same mistake again.*⁵⁶

In October 2015, OPEC invited several non-OPEC producers, including Norway, to consultations regarding the market situation and possible coordinated efforts to balance the market. The Norwegian Ministry of Oil and Energy confirmed that Norway would not participate.⁵⁷ In April 2016, 18 producer countries met in Doha with the aim to freeze production increases. The meeting failed (Claes, 2018, pp. 152–53). However, following the OPEC decision to cut production by 1.2 million barrels per day in November 2016, OPEC met with 11 non-OPEC producers the following month. The non-OPEC producers cut their production by an additional 558,000 barrels per day. The so-called OPEC+ cooperation was established. It has been prolonged over the following years. Norway has not participated in these efforts.

From conflict to cooperation

In explaining the described change from conflict to cooperation between OPEC and Norway, the first task is to examine why they would or would not be interested in cooperation. The second task is to understand how the actors bring the cooperation about, i.e. analyzing the bargaining process.

The actors' interests in cooperation

OPEC's economic interests in cooperation with Norway come from the fact that production limitations on the Norwegian Shelf will mean less oil on the market and consequently less competition for OPEC oil. Reduced competition, even if only marginal, will affect the price positively and increase the stabilizing effect. Furthermore, if cooperation with Norway could increase the likelihood of achieving similar arrangements with other non-OPEC producers, this would no longer be a marginal question for OPEC. When it comes to political interests involved in cooperation with Norway, OPEC has stated that improved

relations with Norway will have the effect of improving OPEC's standing in the industrialized world as a whole. This would represent a political gain for OPEC in addition to the purely economic aspect. Even verbal support from Norway would be better than nothing. Another aspect of OPEC's interest in cooperation with Norway is the effect this has on OPEC's internal cooperation. This is manifested particularly in Saudi Arabia's attitude to cooperation with Norway. A cooperative attitude on the part of Norway could increase the possibilities of maintaining discipline within OPEC.

It is harder to see the Norwegian interests in cooperation with OPEC. Prior to OPEC's altered market strategy in December 1985, it was commonly thought that Norwegian interests were best served if Norway did not cooperate with OPEC. However, after the December meeting in 1985 and the subsequent fall in price and pressure brought to bear by OPEC against Norway, it was generally held that if Norwegian measures could play a part in stabilizing the market, this would also serve Norwegian interests. It was assumed that unilateral measures on the part of Norway would fail to have any effect on price developments. On the other hand, it was thought conceivable that Norwegian measures could affect, in a positive direction, measures introduced by OPEC or other oil producers. This would of course give the Norwegian measures greater significance than if they had been viewed in isolation. Nevertheless, Norway did not have any interest in changing its policy towards oil-producer cooperation as long as it could continue its strategy of free-riding on the cooperation among the members of OPEC.

The bargaining process

Understanding the relationship between OPEC and Norway in 1986 as a bargaining game, we can regard OPEC's altered market strategy in 1985 from defending the market price to defending market shares as a *threat* towards Norway (inter alia) that she must alter her policy by limiting production or face the consequences of a price war. However, the threat failed when the Conservative government preferred the outcome that OPEC increased production and Norway maintained her rate of production increase unchanged, rather than contributing to production limitations. Norway could have considered OPEC's change of strategy as an empty threat of a price war. Even in the 1980s, OPEC's dominant position in the market would suggest that a few free riders were less costly than an all-out price war. In fact, OPEC's threat was to inflict costs on itself in order to have others reduce their utility.

However, the Labor government that took over in May 1986 was of the opinion that if OPEC arrived at effective stabilization measures, Norway too would be willing to contribute to such stabilization through production limitations. However, the Norwegian authorities did not immediately yield to OPEC's threat. The Norwegian move was rather to put forward a *promise* to cooperate if OPEC proved its ability to increase the price by internal cooperative measures first.⁵⁸ No formal agreement or signed document exists following the Norwegian cooperative market policy established in 1986. In fact, as mentioned above, representatives of the Norwegian government have suggested that the relationship with OPEC does not constitute any kind of cooperation at all. I hope this chapter has made a convincing argument to the contrary. In the 1990s the need for cooperative efforts between OPEC and non-OPEC producers disappeared due to the Iraq-Kuwaiti war. From 2003, increased demand made any kind of production cuts obsolete. The price fall following the financial crisis in 2008 was short-lived, thus no market interventions from OPEC emerged. The challenge from US shale oil production, on the other hand, created a more lasting challenge to OPEC (Claes, 2018, pp. 178–180). The oil price fall in November 2014 initiated renewed efforts from OPEC to create a broad producer cooperation. A key element in this effort was to bring one of the top exporters, Russia, on board. In 2016, the so-called OPEC+ cooperation emerged. By time of writing, September 2019, this cooperation between 24 oil producers is a key element in the market governance efforts of OPEC.⁵⁹ Norway is not part of OPEC+. Although Norway is among the top 15 exporters, Figure 18.1 shows how Norwegian production has fallen since its peak around the year 2000. The earlier argument of Norwegian insignificance is again relevant in helping explain Norway's holding back from direct cooperation in OPEC's production efforts.

Table 18.1 Appendix: Meetings between OPEC and Norwegian representatives 1984–1987

Year	Month	Date	Place	OPEC repr.	Norwegian repr. ^a
1984	Oct.	26	Oslo	Yamani	Kristiansen, Willoch, Frøysnes, Stray, Johnsen
		27	Lusanne	Davidwest	Kristiansen
1985	March	18	Riyadh	Yamani, Chalabi	Kristiansen
1986	Feb.	9	Geneve	Yamani, Grisanti (p)	Kristiansen
		17	Caracas	Grisanti (p)	Brundtland
	22	Venezia	Yamani, Chalabi	Øien, Himle, Sandvold, Tønne, Bjerke, Dahl	
	Sept.	13	Oslo	Yamani, Chalabi	Øien, Himle, Sandvold, Tønne, Bjerke, Dahl
	Oct.	22	Oslo	Grisanti	Øien, Himle, Sandvold, Tønne, Bjerke, Dahl. At lunch: others incl. Haraldsen and Nesgård
		25	London	Lukman (p)	Øien, Bjerke, Haraldsen, Nesgård
1987	Jan.	22–24	Oslo	Nazer	Øien, Brundtland, Frydenlund
	Feb.	3	Davos	Lukman (p)	Øien, Bjerke
	June	3–4	Oslo	Lukman (p)	Øien, Brundtland
	Sept.	11	Oxford	Lukman (p)	Øien, Bjerke
	Oct.	9	Oslo	Nabi (Algerie)	Øien, Bjerke, Braathu
	Nov.	?	Riyadh	Nazer	Øien, Bjerke

Note: ^a The list of participants is not exhaustive.

Notes

- 1 This chapter is partly based on (Claes, 1990) and (Claes, 2001).
- 2 I deliberately avoid the discussion whether OPEC is a cartel or not. The aim is only to identify the cooperative incentives among oil producers.
- 3 *Stavanger Aftenblad*, 22.03.1982. The author is responsible for all translations from Norwegian-language publications.
- 4 *Stavanger Aftenblad*, 03.11.1982. The Norwegian government had established informal and irregular contacts with the OPEC secretariat, at least as early as 1981. Ministry of Oil and Energy Archive, Serie: D – 065.3 OPEC, 1978–1985, Box: D-0774.
- 5 Statement by Oil and Energy Minister Vidkun Hveding in *Stavanger Aftenblad*, 26.02.1983.
- 6 Statement by the prime minister's personal advisor, Terje Osmundsen: *Aftenposten*, 13.09.1984.
- 7 Statement by the prime minister's personal advisor, Terje Osmundsen: *Aftenposten*, 13.09.1984.
- 8 *Ministry of Oil and Energy Archive*. Serie: D – 065.3 OPEC, 1981–1984, Box: D-0774.
- 9 *Financial Times*, 16.10.1984.
- 10 *Stavanger Aftenblad*, 20.10.1984.
- 11 *Aftenposten*, 27.10.1984.
- 12 Yamani was asked about his impression of Arne Øien (Kristiansen's successor) and described him as able and sympathetic. To the question of his impression of Kåre Kristiansen, he stated, 'Oh, he is a politician' (Lindøe, 1987, p. 104).
- 13 *Middle East Economic Survey*, 3.12.1984.
- 14 *Middle East Economic Survey*, 3.12.1984.
- 15 *Stavanger Aftenblad*, 29.11.1984.
- 16 *Aftenposten*, 19.03.1984.
- 17 *International Herald Tribune*, 11.12.1985.
- 18 *Aftenposten*, 12.12.1985.
- 19 *Financial Times*, 10.12.1985.
- 20 Iran's oil minister, Hussein Kazimpur Ardebili, as quoted in *Stavanger Aftenblad*, 27.01.1986.

- 21 *Aftenposten*, 22.01.1986.
- 22 'When weighty social considerations render it necessary, the Government can establish other production rates than those already established or approved pursuant to the above provisions.' Section 20.5 of Chapter III of the Petroleum Act, 22.03.1985.
- 23 *Aftenposten*, 22.01.1986.
- 24 *Norges Handels og Sjøfartstidende*, 23.01.1986.
- 25 *Aftenposten*, 23.01.1986.
- 26 Ministry of Oil and Energy, press release 21.01.1986.
- 27 Ministry of Oil and Energy, press release 22.01.1986.
- 28 *Stavanger Aftenblad*, 24.01.1986.
- 29 *Aftenposten*, 17.02.1986.
- 30 *Stavanger Aftenblad*, 03.05.1986.
- 31 *Arbeiderbladet*, 21.01.1986.
- 32 *Aftenposten*, 20.01.1986.
- 33 Skånland's reasoning was that under the assumption that the price will actually rise in future, it may be rational, at any rate from an economic point of view, to simply allow the oil to remain in the ground while awaiting a price rise *Aftenposten*, 13.03.1986.
- 34 The government's inaugural speech in Parliament, 13.05.1986.
- 35 *Aftenposten*, 15.05.1986.
- 36 *Aftenposten*, 06.02.1986.
- 37 *Aftenposten*, 23.05.1986.
- 38 These were established after Yamani was kidnapped by Venezuelan terrorist Illitch Ramirez Sanchez, alias Carlos Martinez, alias the Jackal (Terzian, 1985, pp. 219–234).
- 39 *Aftenposten*, 24.06.1986.
- 40 *Aftenposten*, 23.06.1986.
- 41 *Arbeiderbladet*, 24.06.1986.
- 42 A spaghetti meal, not appearing on the program, was served in the hotel restaurant. The talks became more relaxed, with the probable aim on the part of Yamani to build up trustful relations between the two parties.
- 43 *Ministry of Oil and Energy Archive*. Serie: D – 065.3 OPEC, 1987–1991, Box: D-0776.
- 44 *OPEC Bulletin*, July/August 1986.
- 45 *Aftenposten*, 30.06.1986.
- 46 Press release from the Ministry of Oil and Energy, 01.07.1986. The government's view was explained by Øien in *Aftenposten* (05.07.1986) and elaborated on in a reply to Kristiansen in *Aftenposten* (24.07.1986).
- 47 Press release from the Ministry of Oil and Energy, 06.08.1986.
- 48 Press release from the Ministry of Oil and Energy, 10.09.1986.
- 49 *Stavanger Aftenblad*, 12.09.1986.
- 50 Yamani arrived with gifts (sweetmeats and dates) for the Norwegian representatives.
- 51 This reportedly occurred at the request of the Norwegian representatives, who needed this as a means for domestic opinion making.
- 52 *Aftenposten*, 27.10.1986, and *Arbeiderbladet*, 08.12.1986.
- 53 Press release from the Ministry of Oil and Energy, 13.01.1987.
- 54 *Aftenposten*, 23.01.1990.
- 55 *Aftenposten*, 26.07.1990. Also, Ministry of Oil and Energy Archive, Serie: D – 065.3 OPEC, 1990–1991, Box: D-0776.
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- 57 Framstad, A. P. (2015). *Norge deltar ikke på ekstraordinært Opec-møte*. E24, 21.10.2015. Retrieved from: <https://e24.no/energi/norge-deltar-ikke-paa-ekstraordinaert-opec-moete/23546524>.
- 58 'A promise is a commitment to the second party in the bargain and is required whenever the final action of one or of each is outside the other's control. It is required whenever an agreement leaves any incentive to cheat' (Schelling, 1980, p. 43).
- 59 In addition to the OPEC members, Azerbaijan, Bahrain, Brunei, Kazakhstan, Malaysia, Mexico, Oman, Russia, the Republic of Sudan, and the Republic of South Sudan, participate in the cooperation.

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Taking a leaf out of OPEC's book?

The significance of developing producer country models for state involvement in North Sea oil production

Eivind Thomassen

The introduction of state involvement in Norwegian and British oil production was one of the most dramatic and significant developments in the history of the North Sea petroleum province.¹ A measure of such involvement had been formally introduced in both countries in the 1960s, but it was substantially scaled up in the 1970s, epitomised by the creation of entirely state-owned, 'national' oil companies.² The Norwegian State Oil Company, later known as 'Statoil', was created in 1972 and the British National Oil Corporation (BNO) was established in 1975. While Statoil expanded greatly over the next decades and is today (under the name Equinor) one of the most important operating companies in the North Sea, BNO was nipped in the bud, was given quite a different role from what had been anticipated, and was eventually dissolved entirely and privatized by the Thatcher government in the 1980s.³ Throughout the 1970s and much of the 1980s, however, the extent and form of the state's involvement in oil production, including the distribution of financial rights and obligations that went with it, remained the core topic and point of contention in the petroleum policy debates of both countries (see in particular Kemp, 2012a and 2012b; Hanisch and Nerheim, 1992; Lie, 2012).

To many contemporary observers, the introduction and form of state involvement in North Sea oil production in the 1960s and 1970s was clearly inspired by those existing in older oil-producing countries in the developing world.⁴ In particular, the emergence of the 'national' oil companies seemed to follow a developing producer country pattern: Iran had established its National Iranian Oil Company in 1951, Indonesia its Pertamina in 1957, Algeria its Sonatrach in 1963, Iraq its Iraq National Oil Company in 1966, Libya its National Oil Corporation in 1970, and Abu Dhabi the Abu Dhabi National Oil Company in 1971 (Marcel, 2006). By doing the same in 1972, Norway was, according to one journal, taking 'a leaf from OPEC's Book', and the UK was seen as following suit. The presumption that these policies derived from the developing world was highlighted by journalists giving British and in particular Norwegian authorities such telling epithets as 'the Sheikhs of the North Sea' and 'The Blue-Eyed Arabs' (Zakariya, 1976, p. 546).

However, the contemporary claims that the introduction and organisation of state involvement in North Sea oil was influenced or copied from developing producer countries have not featured prominently in the scholarly literature examining the two countries' petroleum policies in the period. Although global trends

have been duly noted, when it comes to *explaining* why, when, or in what form the states involved in the production of oil, the significance of the developing oil-producing countries, or of the OPEC organisation within which many of them had joined forces, is rarely if ever addressed. On the contrary, the significance of a set of deep-rooted *domestic* political traditions is often highlighted as important for the development of oil policies in the two countries, clearly suggesting a limited role for external inspiration.

To what extent were the petroleum industry observers of the 1970s right? To what extent did the introduction and organisation of state involvement in the Norwegian and British oil industry follow domestic traditions or developing producer country models?

This chapter will address these questions by exploring the development of state involvement in North Sea oil as an example of policy transfer. A rich and growing literature exists on the value of studying similar policies and organisational patterns that occur across borders as instances of transfer. Identifying the ‘joint venture participation’ form of formalized state involvement in oil, as developed in some Middle Eastern producer countries from the late 1950s, as a model among other available models for state involvement, enable us to demonstrate that this form, and the arguments underpinning it, were reflected in the organisation of state involvement in the UK and Norway. The chapter demonstrates that, even though there were differences between Norway and the UK in the extent to which elements of the ‘joint venture’ model for state involvement were successfully implemented, and though they were implemented in a quite different institutional context from that of the Middle East, the ‘joint venture participation’ model and the rationale behind it, contributed to shaping the form of state involvement in the North Sea of the 1960s and 1970s.

‘The shadow of the past’ and the nation-centric literature

Although few if any scholars have been solely or primarily concerned with state involvement in British and Norwegian oil production as such, a wide range of historians and political scientists have, in various ways, studied the development of oil policies in the 1960s and 1970s. Many of them have called to attention the contemporary trend to create national oil companies among the producer countries in the developing world (Austvik, 2007, Hanisch and Nerheim, 1992, Sejersted, 1999, Toye, 2002).⁵ However, all these scholars have in the end placed less emphasis on possible cross-border influences than on domestic explanations for the introduction and organisation of state involvement in oil production. In this literature there seems to be a rather broad consensus that the introduction and organisation of state involvement in the North Sea oil industry was firmly rooted in domestic Norwegian and British political traditions

This consensus has been most concisely summarized by political scientists Brent Nelsen and Svein Andersen in two almost identical theories for the development of North Sea oil and gas policies 1962–c.1990 (Andersen, 1993; Nelsen, 1991). Nelsen and Andersen’s theories identify (although they use different terms) domestic political traditions as the crucial explanatory variable. These traditions include both traditional practices and traditional ideas, although emphasis is placed on the latter, more precisely ideas about public–private sector relationship in the economy.⁶ A strong ‘statist’ tradition, i.e. a desire to let the state take a powerful role in the production and provision of certain key goods and services, existed, according to Nelsen and Andersen, across the political spectrum in postwar Norway, and within the incumbent UK Labour party 1964–1970/1974–1979. This tradition, what Nelsen, echoing Ikenberry, refers to as ‘the shadow of the past’, exerted an autonomous push for state involvement in oil production from the 1960s onwards (Nelsen, 1991, p. 183). The ability to let ‘the shadow of the past’ guide policy was bound, however, until the mid-1970s by the reliance on foreign multinational oil companies for the exploration of the continental shelves.⁷ The economically viable discoveries made from 1970 onwards shifted Britain and Norway’s bargaining power vis-à-vis the multinationals. And it is this shift that Nelsen and Andersen identified as the crucial event that triggered the formation of state oil companies and an active state involvement in the oil production process.

Many historical accounts confirm this alleged fundamental significance of domestic political traditions, although they are usually not as fixated on causality, and do not apply the same conceptual frameworks, as Nelsen or Andersen. Several historians have associated the creation of the Norwegian State Oil Company in 1972 with a traditional Norwegian preference for state involvement in key sectors of the economy, as well as an alleged age-old concern with national sovereignty over natural resources. The desire for state involvement, spanning back at least to the 19th century, has been explained originally as a way of compensating for a lack of private capital (Andersen, 1993; Sandvik, 2018, pp. 72–73, 92; Sejersted, 1991; on state involvement in the 20th century, see Gronlie, 1989; Lie, 2012; Slagstad, 1998). Support for this allegedly strong Norwegian concern for national sovereignty over natural resources has been found in the regulation of foreign access to Norwegian waterfalls in the early 20th century and the debates that accompanied them (Andersen, 1993; Ryggvik, 2009; Sanders and Sandvik, 2015; Sejersted, 1999; on the regulations themselves, see Sanders, 2018).

Historians examining the British case seem also to confirm the significance of political or ideological traditions within the UK Labour party for the introduction and organisation of state involvement in oil (Chick, 2011; Kemp, 2012a; Kuiken, 2013; Toye, 2002).⁸ Labour had, by nationalising the coal and gas industries in the 1940s, seemingly demonstrated a preference for state-owned enterprise, particularly in the energy sector. When the second Wilson Labour cabinet took office after the February 1974 elections (and secured a narrow majority in the October elections of that same year) amidst rising oil prices and supply shortages, few have found it necessary to ask where Labour's desire for a state-controlled oil company originated.⁹ However, in Britain, the preference for state involvement was less widespread than in Norway. State involvement in oil production was contested by the Conservative opposition and the policies that had created the British National Oil Corporation were eventually reversed entirely after the Conservatives regained power in 1979. In the words of historian Martin Chick, BNOC appears as 'a curiously old-fashioned, last, weak flicker of the flame of nationalization before it was doused by the privatisation program of the 1980s'.¹⁰

The shadow of the past and its limitations

The strong emphasis on domestic political traditions evident in the existing literature, highlighted most explicitly by Nelsen and Andersen, is surprising – for two main reasons. First is its wobbly empirical foundation. When examining the historical facts closely, some of them seem not at all sufficiently explained by the alleged power of precedent. The introduction of British state involvement in oil production was, for example, far from a typical nationalisation proposal. The British National Oil Corporation was only allowed to 'participate' in the petroleum exploration and production licenses awarded to private companies with a 51 percent share (Chick, 2011). If, as Nelsen, Andersen and others suggest, public sector control of oil was the ideologically prescribed aim of the UK Labour party, or if it followed from a Labour precedent for nationalising key industries like coal and gas, why then did not the 1964–1979 Labour governments suggest, hardly even *consider*, full nationalisation of oil?¹¹ And why, if the state-owned oil company was the result of Labour 'statism', was the introduction of a 100 percent state-owned company prepared under the *Conservative* government of Edward Heath (1970–1974), as recently demonstrated by both Alex Kemp and Jonathan Kuiken? (Kemp, 2012a, pp. 257–267; Kuiken, 2013, pp. 432–440). We will return to the empirical merits of statism and domestic political traditions later. It appears at any rate that such an explanation needs, at least, to be modified in light of the available evidence.

The other reason to be surprised by the strong emphasis on domestic traditions is, as has already been suggested in the introduction, the extent to which the introduction of state involvement in oil was part of a broad international trend. The 'national oil company' is a prime example of a widespread organisational form, as it emerged in a wide range of countries over the 1950s, 1960s and 1970s (Kobrin, 1985). So is, as we shall soon see, the system of contractual joint venture participation by producer states. The almost

simultaneous emergence of these forms in many different countries obviously calls for explaining them by other means than pointing at domestic Norwegian and British Labour party traditions – or, at any rate, not to do so in isolation from outside processes. Looking at Norwegian and British domestic factors in isolation leaves the irking question of why organisations referred to by similar names with similar functions were being created more or less simultaneously as far away from the UK and Norway as in Abu Dhabi and Venezuela.

Many scholars, particularly in the fields of sociology and political science, have, although not occupied with the oil industry, shown great interest in other such sequential patterns of policies between countries.¹² The patterns suggest, according to these scholars, that organisational and institutional forms are somehow ‘transferred’ or ‘diffused’ (see e.g. Béland, 2009; Campbell, 2004; DiMaggio and Powell, 1991; Simmons, Dobbin, and Garrett, 2006). Looking at the institutional and organisational patterns that surround us in our everyday lives, everything from rules of the road to national constitutions, from youth clubs to armies, it becomes fairly obvious that, even though they may have special national characteristics, few institutions or forms of organisation are exclusive to one’s own country and only some forms seem, at best, to first have originated there (DiMaggio and Powell, 1991). The alternative to envisaging some kind of transfer of the ideas or conceptions underpinning the institutions (by whatever mechanism), is envisaging that similar organisations and institutions evolved autonomously, or were somehow miraculously ‘discovered’ independently, in several, widely different countries more or less at the same time. This is rarely encountered as an explicit theoretical position. Nevertheless, oil policies in Norway and the UK have traditionally been analysed as if they were.

This is not to say that seeing the introduction of state involvement in oil as some sort of transfer process requires that domestic political or ideological motives, whether rooted in tradition or not, played no role. On the contrary, it is fairly obvious, and finds support in recent literature on organisational transfers (Ban, 2016; Johnson, 2016; Thomassen, 2017), that transfer of institutional forms and policies in most instances require both domestic motives and a measure of ‘embedding’ into the domestic political context in order to succeed.

Rather than questioning the ultimate explanatory factors for the decisions to introduce state involvement, studying these decisions as instances of transfer requires comparing the policies of the UK and Norway more closely to the policies of the producer countries of the developing world. It requires directing attention to the *content* of policy and *how* it was arrived at, rather than ultimately *why*. Doing so will, however, as has already been shown, highlight the limitations of the causal explanations emphasized in previous literature.

The joint venture participation model

Could we derive from the sources and literature on producer country oil policies a model, a dominant form of organising state involvement in domestic oil production that existed in the oil-producing developing countries in the 1960s and 1970s, at the time such involvement was introduced in the North Sea?

The joint venture participation agreements developed in several developing countries from the late 1950s matches this description fairly closely.¹³ The joint venture model for state participation is routinely claimed to have first emerged in 1957 in contracts between two Egyptian national oil companies and the Italian national oil company ENI, then, a few months later, copied in an agreement between the ENI subsidiary AGIP and the National Oil Company of Iran (NIOC) (Dam, 1976; Zakariya, 1976; Marcel, 2006). These agreements seem to some extent, however, to have been modeled on the agreement between the Kuwaiti ruler and the Aminol consortium in 1948.¹⁴ The principles of the Egypt and Iran agreements were at any rate copied extensively. In Saudi Arabia, national oil companies entered joint venture agreements with foreign companies in 1965 and 1967 and again in the 1970s; in Kuwait, a new joint venture agreement was made in 1967 and in Algeria, Libya and Abu Dhabi in 1968. A report

compiled for the Norwegian Ministry of Industry in 1972 listed 36 participation agreements of this kind around the world.¹⁵

In the joint venture participation agreements, the state, represented by a 'national', state-controlled oil company, entered a formal, contractual 'joint venture' with a foreign oil company, sharing the rights and obligations pertaining to the exploration for and (in particular) production of petroleum within a specified area. By the beginning of the 1970s, certain common features could be clearly identified for such joint venture agreements: first, for the national and foreign partner(s) to hold equal shares, 50 percent each, of the venture, thus giving the national company (at least) an equal say in the venture's decisions. Second, for the foreign partner to cover all the exploration costs of the venture until a discovery was made, i.e. 'carrying' all exploration risk (Zakariya, 1976). Although there was variation in detail, these elements were seen by observers by the late 1960s and early 1970s to constitute a fairly specific and uniform model for state involvement in oil.¹⁶

Joint venture participation between national and foreign oil companies was not the only available model for organising state involvement in the petroleum industry. To the extent we can talk about a dominant Continental European model for organising state involvement in oil at the beginning of the 1960s, it was certainly something closer to granting *de facto* (if not *de jure*) monopolies for the 'national' agent(s). National companies were in practice, if not always in principle, given privileged right to explore for petroleum resources in Finland, Sweden, Spain and, more interesting perhaps, in Austria, Denmark, France and Italy – countries where petroleum reserves were found. The degree of public ownership varied, and in some countries, like Italy and Spain, cooperation with foreign companies in joint ventures was by the early 1970s encouraged in some less prospective territories. In all of these countries, however, the national oil companies enjoyed a highly privileged position vis-à-vis foreign and other domestic oil companies and bore all costs and risks associated with exploration and extraction themselves.¹⁷

Even among the developing producer countries there were competing models. Some producer states sought full nationalisation. Some, like Indonesia, developed other formalized forms of cooperation vis-à-vis the foreign partners, known as service contracts and production sharing agreements, in order to more clearly subjugate the foreign partners to the national company (Zakariya, 1976, pp. 562–566). Ironically, such formalized arrangements could seem to eclipse joint venture participation in popularity just as Norway and the UK introduced their national oil companies in the 1970s (Zakariya, 1976, p. 554).

The Indonesian arrangements and the Middle Eastern joint venture participation agreements were different responses to the calls for producer state sovereignty over natural resources made by several developing producer countries and their advocates over the course of the mid-20th century.¹⁸ This general call for sovereignty stemmed from the significant extent to which the exploration for and extraction of natural resources in the developing countries, and particularly oil, had been concentrated with a small set of large, Western multinational companies. The power of these companies – in oil known as the 'majors' – rested upon generous concessions granted to them by the local governments. Some of the most lucrative concessions, such as in Iraq and Iran, had been granted by the governments when they had still been under heavy Western dominance, giving the majors effective control over the countries' natural resource management and of the revenue derived from it.¹⁹ De-colonisation and the rise of nationalism in Latin America and the Middle East from the interwar years onwards, fostered a continuous push for abandoning or adjusting the old concessions and to limit the multinational oil companies' position in these regions (Dietrich, 2017).

In theory, one could have imagined that a stricter concession regime and systems for regulating and taxing foreign/private producer companies would have enabled host regimes to exert greater sovereignty over oil without involving directly in production. Better terms for the producer countries were indeed achieved by the late 1950s, increasing their share of the revenue. The strong desire for state involvement stemmed clearly from the idea (although it was rarely explicitly stated) that the multinational oil companies operating in the industry had different interests in the management of the resource from those of the state.

Given the scale and complexity involved in exploring for, extracting, transporting and further refining petroleum, the multinational companies' ability to pursue these 'non-national' interests could only be effectively curbed by the state if it involved itself intimately in the details of the production process. The almost universal establishment of 'national' oil companies as the agent of the producer countries' involvement in oil was the clearest manifestation of this idea. For a state agent to involve itself in a sector thus far dominated by multinational oil companies, it had to assume some of the characteristics of these large multinationals, becoming an oil company itself.

The joint venture participation agreements represented a compromise between, on the one hand, the desire for less multinational involvement in domestic natural resource management and, on the other, the recognition (grudgingly in many countries) of the need to retain access to the multinational oil companies' technical expertise, capital and market access (Dam, 1976; Zakariya, 1976). The first impulse of some of the oil-producing countries had been to outright replace the multinational majors with the national oil company, entirely nationalising their domestic assets. This strategy was pioneered most famously by Mexico in 1938.²⁰ Even though Mexico consumed its oil itself, nationalisation came with political and economic costs. These were significantly aggravated when Iran, a large net exporter of oil, followed the same strategy in 1951. The country quickly faced the dual menace of the oil majors strangling its exports and the West orchestrating a coup d'état against its government. The pitiful experiences with nationalisation in Mexico and Iran played a central role in promoting the idea of joint venture participation from the 1950s, not least by Iran itself (Marcel, 2006; Zakariya, 1976).

The defining principle of the joint venture participation model as opposed to nationalisation and other models, was the 'jointness', the partnership, and thus legal equality, between the national oil company and the multinational oil companies. Such a partnership had, in the eyes of contemporary observers, many tangible benefits compared to outright nationalisation. Unlike nationalisation, joint venture participation relieved the state from some (or all) of the exploration risk, secured inflow of foreign capital investment and technology, as well as access to foreign markets for the country's oil. At the same time, joint venture participation would, like nationalisation (although to a lesser extent), secure for state decision-making power in production and added, by giving a direct title to production and sales revenue, to the overall 'government take'. Although joint venture participation may have appeared to some as a pusillanimous alternative to nationalisation, it was over the 1960s regularly portrayed as a more successful mechanism to increase developing countries' sovereignty over oil (Zakariya, 1976; Mughraby, 1966; Evensen, 1971).

The move to joint venture participation was, importantly, just as much the result of oil company ingenuity as it was of producer country desires. The first joint venture agreements of 1948 and the late 1950s, and most agreements of the next decade, were all offered by so-called 'independents', smaller oil companies that did not hold old lucrative concessions. The independents were often Western European 'national' oil companies, most notably Italy's ENI. These companies saw the offering of joint venture participation to producer states as a way to compete with the 'major' oil companies for access to the areas previously covered by concessions. The majors resisted the idea of state participation for fear of undermining their existing concessions. By the early 1970s, however, even the majors entered joint venture participation agreements covering areas previously under concession, most importantly in Saudi Arabia, adding significantly to the legitimacy of the model (Marcel, 2006, pp. 28–29).

State participation in the North Sea

State involvement by national oil companies in North Sea oil production over the 1970s came to resemble the joint venture participation model as developed by producer countries in the late 1950s.²¹ In both Norway and the UK, state involvement was in the 1970s based on partnerships (*interessentskap*) between the national oil company and one or more private/foreign companies.²² The state held an option for 50 percent (at least) participation in each partnership, and the partner companies were expected to 'carry' the

national company's exploration costs. Although the national oil companies were established in the 1970s, these principles were first introduced in the North Sea in the 1960s.

Despite the many claims that historical precedent was important for the emergence of state involvement offshore, there is hardly any older domestic 'models' for state industrial involvement suggesting the kind of organisation introduced in the North Sea. True, there were several state-owned enterprises in both the UK and Norway, but they were not normally operating in joint ventures, and especially not with foreign private firms. Full ownership by the state was the British Labour Party's model for state involvement in coal and gas. A principle of total state control also seems to have guided the Norwegian postwar policies towards the production of hydropower.²³ In the Norwegian mineral resource industries, as for instance the modest Norwegian coal industry, the state allowed all kinds of public-private sector constellations well into the 1970s.²⁴ A committee investigating the organisation of the Norwegian state's industrial involvement in 1957 concluded explicitly that the organisation appeared 'random', even 'confusing', and that there existed no 'system' for such organisation (Grønlie, 1989, p. 123.).

This is not to say that no one sought to extend other pre-existing models, 'national' or otherwise, to the exploration and extraction of oil and gas in the North Sea. In the UK and Norway, proposals seeking to influence petroleum policies in the direction of domestic or Continental European models were explicitly rejected. In the UK, the Labour government 1964–69 rejected a 1964 call from the Trades Union Congress (TUC) for a complete nationalisation of UK oil and gas exploration along the lines of coal (Kemp, 2012a, pp. 85–86; Toye, 2002). In Norway, a centre-right coalition government (1965–1971) rejected in 1967 calls for granting a monopoly on exploration to a Norwegian state company.²⁵

The British government allowed public enterprise to enter partnerships on the British continental shelf from the very first licensing rounds, in 1964 and 1965. In these rounds, the Gas Council participated as an ordinary partner, with shares of 33–50 percent of the various licenses it participated in. The National Coal Board was allowed to enter partnerships with a 50 percent share and on a partly 'carried' basis from 1965. Although these arrangements were clearly not 'joint venture state participation' entirely by the book, the arrangements were justified inside the government apparatus by direct reference to producer country experiences. It was noted, according to Alex Kemp's resumé of the official documents, 'that it was rare for public sector enterprises to shoulder all the exploration risks, and in countries where it had been tried [...] the results had not been outstandingly successful'. The more recent arrangements in the Middle East were seen as more desirable alternatives to this model (Kemp, 2012a, p. 91). Judging by Toye's account of the process leading up to the first proposals in the UK Labour Party for a 'National Hydrocarbons Corporation' in 1967, the need for this company to avoid copying the mistakes of certain producer countries was clearly recognized, and the case made for it instead to cooperate with private companies along joint venture lines (Toye, 2002, p. 95, 98).

Unlike the developing country pioneers of state involvement in oil, however, the British governments prior to 1975 actively *avoided* creating a national oil company to act as the state's participating agent, opting instead for the Coal Board and Gas Council. This, according to Kemp, was because creating a British national oil company would be 'extremely embarrassing' to British oil companies, presumably London-based British Petroleum (BP) and Royal Dutch Shell, two of the 'major' oil multinationals, in their international operations (Kemp, 2012a, p. 92).²⁶

It is tempting to attribute significance to this fact, that BP and Shell were themselves considered British. This meant that British authorities, unlike the authorities of Norway and the developing producer countries, could rely on two of the largest multinational oil companies, restrict state and *still* retain a substantial 'national' involvement in domestic oil production. This may well have moderated the urge for state involvement compared to other countries and may well have played a part in the abandonment of state involvement in production in the 1980s. This argument is, however, not of much interest to the question here, since involvement in oil production by a national oil company was introduced anyway.²⁷

Producer country arrangements also influenced the first introduction of state involvement in Norway. Jens Evensen, head of the Ministry of Foreign Affairs' Legal Division, and the leading oil bureaucrat and *de facto* Norwegian policymaker for much of the 1960s, initiated and negotiated these deals. Evensen was particularly attentive to producer country developments.²⁸ Evensen pointed out at various occasions that Norway entirely lacked experience as an oil-producing country. It was thus not only natural but also necessary, according to Evensen, to turn to the experiences of oil-producing countries in order to find the right solutions for Norwegian petroleum policies.²⁹

Evensen, together with Nils Gulnes – Evensen's secretary and from 1966 head of the Ministry of Industry's temporary 'Oil Office', purposefully sought from the mid-1960s to exploit all sources, not least the oil companies, to gather information about other producer countries' experiences. Data on various Western regimes were carefully studied, but the developments of the Arab producer states seem from a very early point to have received special attention (Hanisch and Nerheim, 1992, p. 36). In 1967 Nils Gulnes visited OPEC's new headquarters in Vienna, Austria.³⁰ According to Gulnes, the developments within the OPEC countries, and the information and justifications for these developments gathered by the OPEC organisation, was important in convincing himself and Evensen about the benefits and feasibility of introducing participation in Norway (interview with Nils Gulnes, 5 June 2018). From 1967 Evensen and Gulnes started tacit negotiations with the multinational oil companies, and on the basis of these negotiations, the first two 'state participation agreements' were finalized in 1969.^{31 32}

Nils Gulnes was explicit about the model for these arrangements. In a memorandum of November 1968, Gulnes remarked that the question of state involvement in oil production had been raised in many traditional producer countries over the recent years, and that they had developed a range of different forms of such involvement according to the particular conditions in each country. The form guiding the Norwegian negotiations with the oil companies, however, was identified by Gulnes as a joint venture/carried interest system, which he described as having become 'common' among the producer states over the previous years.³³ The introduction of joint venture state participation on the Norwegian continental shelf immediately spurred discussions among civil servants, not about *whether* to introduce a national oil company, but when and with what organisational capacities.³⁴ The process of actually creating the company was, however, delayed until 1972 for various, primarily political, reasons.^{35 36}

Hasan Zakariya in Norway

There were a few links between Norway's key oil bureaucrats Evensen and Gulnes and one particular developing producer country, Iraq, which deserves some special attention. One link, which has not been recognized in previous literature, is the use of the Iraqi national Hasan Zakariya as an advisor to the Norwegian Ministry of Industry c.1969–1972.³⁷

Hasan Zakariya was a friend of Jens Evensen since well before the advent of Norwegian oil. Evensen had first been acquainted with Zakariya in the early 1950s, when they had studied law at Harvard. In 1958, Zakariya had become an important figure in the new Iraqi administration following the coup d'état of Abd al-Karim Qasim and, in the turmoil of the coup, allegedly helped release Evensen (then acting as a Norwegian special envoy to the country) from a Baghdad prison (Retzer, 2017). From 1967, Zakariya became head of OPEC's Legal Section. The year after, Zakariya played a key role in drafting OPEC's resolution 90 of 1968, calling for the general extension of state participation in oil production as far as feasible (Parra, 2005, pp. 111–113). Hasan Zakariya has been defined by historian Christopher Dietrich as a central member of the 'anti-colonial elite' who promoted the ideas of sovereignty over natural resources and, in the 1960s, state involvement in oil (Dietrich, 2017).

Zakariya came to serve the Norwegian Ministry of Industry as an advisor. While the Ministry of Foreign Affairs officially held OPEC at arm's length, Nils Gulnes quickly established contact on behalf of the Ministry of Industry. In 1969, on Gulnes' invitation, Zakariya held a lecture in a remote Norwegian

mountain resort, on the recent OPEC resolution promoting state involvement in oil production. In an enthusiastic letter to Zakariya thanking him for his efforts, Evensen claimed that Zakariya's lecture 'gave us new views and thoughts on petroleum economics and state participation'.³⁸ In 1971 Zakariya was hired to write a special report for the Norwegian government in which the extent and character of a future Norwegian policy on state involvement were discussed³⁹ (the report probably served as a basis for Zakariya's 1976 article). A contract was set up for Zakariya to extend the report and make 'a detailed draft agreement of state participation' to be used in the licensing round set for 1972.⁴⁰ The licensing round was not held and the draft is missing, but the initial report remains.

In this report, Zakariya promoted the principle of 50 percent state participation on a joint venture/carried interest basis for the future Norwegian national oil company, a principle that was adopted in subsequent Norwegian licensing rounds. It is possible that Norwegian civil servants were already thinking along these lines independently of Zakariya, and there is no trace of the report being referred to explicitly in internal memoranda or official documents. It is nevertheless clear, not least from the commissioning of the report following Zakariya's lecture in 1969, that the Ministry's civil servants found Zakariya's opinions relevant and interesting.⁴¹

In addition, the personal friendship with Zakariya may have strengthened Evensen's and Gulnes' sympathy with the producer country position. A degree of sympathy for the developing producer countries is evident from the writings and initiatives of Evensen and Gulnes. In a 1971 report, Jens Evensen for example used the term 'unreasonable' (*'urimelig'*) when writing about the old concessions and major oil company actions against producer states, especially when referring to Iraq (Evensen, 1971, p. 84). Unreasonable deals and unreasonable actions by the multinationals was, according to Evensen, the reason why producer countries, 'in order to protect their legitimate self-interests', had demanded 'a more active participation' for the state.⁴² Evensen was explicit that Norway had to move in the same direction.

It is worth noticing that the relatively moderate joint venture participation system was increasingly dissimilar to the system established in Zakariya's own home country. Since Iraq was among the countries most restrained by the old concession regime, Iraq was also among those who, eventually, chose the most radical response to it.

Increasing state involvement

Following several substantial discoveries in both the British and the Norwegian sectors of the North Sea 1970/71, state involvement in oil production was catapulted to the centre of political public debates in both countries, and expanded significantly. On the surface, the expansion appeared not to be influenced by developing country models. Key motives in these debates, such as the desire for securing oil supplies to the domestic economy, had not been important for introducing state involvement in many developing producer countries, and the policies of the developing producer countries were not often referred to explicitly. The expansion of state involvement which followed, nevertheless made the Norwegian and British systems of state involvement in oil, the latter in principle at least, even more similar to the joint venture model.

In Norway, this was demonstrated by the gradual scaling up of state participation in licensee partnerships towards the symbolic 50 percent mark. A state participation option of 36 percent was reached in one license in 1971, and in 1973 the 50 percent principle was followed for the first time when the government took a 50 percent share of what would become the giant Statfjord field. The policy change was also evident in the creation of a national oil company and the reiteration of the carried interest principle. In 1971 the government announced the establishment of a national oil company to handle all existing state participation rights, and that the company should be given participation options on a carried interest basis in all future licenses.⁴³ In 1972 the Norwegian State Oil Company was created. In subsequent years participation was in some instances allowed to go beyond 50 percent, but never, not for any single license, was the

national oil company allowed to hold a license as a single owner. Within the Norwegian civil service, the Norwegian model was continuously referred to as ‘joint venture’ (or ‘carried interest’) and contrasted to other models, such as production sharing and service contracts.⁴⁴

In the UK, the expansion was more abrupt. After the Gas Council and Coal Board had been awarded new licenses together with their partners by both Wilson’s Labour and Heath’s Conservative governments in the licensing rounds of 1970 and 1971, respectively, the second Wilson Labour cabinet, after taking office in 1974, suddenly proposed a British National Oil Corporation to exercise 51 percent participation rights in all North Sea licenses, new and old on a ‘carried interest basis’, and to receive all existing options currently held by the Coal Board. The sudden shift in participation policy followed the dramatic oil price rise and the many discoveries 1970/71, combining to form the notion that much of Britain’s new-gained oil wealth had been ‘given away’ and had to be taken back.

Although the percentage of state participation was marginally higher than in Norway, and even though the level of participation would cover both old and new licenses (and though the extent of the ‘carrying’ would later be contested), this model seemed clearly inspired by the Norwegian system, something that was also pointed out in the parliamentary debate and elsewhere (Corti and Frazer, 1983, pp. 59–60).⁴⁵

As noted above, the introduction of state involvement in the industry by means of national oil companies in the developing producer countries had been motivated by a desire for greater sovereignty over the national oil resources. Although both Norway and the UK by the mid-1970s could be seen as pursuing very similar strategies, there were important differences between the two countries in the extent to which this objective was adopted and reflected in the domestic political debate.

UK civil servants or politicians never seemed to link state involvement in oil production with the maintenance of British sovereignty. There was certainly ambivalence towards the major multinational oil companies, including BP and Shell (Benn, 1989). Yet, there are few signs that they actually saw British sovereignty, or the ability to reach the goals that were arrived at politically, threatened by them, at least not to an extent that could not be resolved by taxation, regulation or other measures. True, there was talk of national control when BNOC was proposed to parliament, but explicit references to ‘the people’ rather than the ‘nation’ suggests that this control was seen first and foremost in a class perspective, where ‘national’ control implied a more fair distribution of petroleum income within the population and not, after all, reinstating national sovereignty vis-à-vis foreign oil companies.⁴⁶

This was all very different in Norway. Here, the political debate about the state oil company came to focus heavily on the company as a vehicle with which to create onshore petroleum-based industry. Underpinning the notion that a state oil company was necessary to create such an industry was the presumption that creating it would not be in the best interest of the multinational oil companies, and that they would use their technological, financial and political power to avoid doing so. There were several warnings in the parliamentary debates of the early 1970s about the danger to ‘national’ objectives represented by the large, multinational oil companies.⁴⁷

It appears that the parliamentarians’ knowledge about the oil industry, as it surfaced in these debates, was to no small extent influenced by oil bureaucrat Jens Evensen.⁴⁸ Both Evensen and his secretary Nils Gulnes organized seminars for ministers and MPs from about 1970 to educate them about oil industry matters. Evensen’s above-mentioned 1971 report was presented to parliament as an attachment to the white paper on the government’s petroleum policy guidelines in 1971 – and it was explicitly referred to by parliamentarians in the subsequent debate.⁴⁹ This important debate paved the way for the introduction of the Norwegian State Oil Company in 1972.⁵⁰

Conclusion

The chapter has explored whether the introduction and organisation of state involvement in North Sea oil production in the 1960s and 1970s can be perceived as an instance of policy transfer. Contrary to what

previous literature has suggested, the organisation of state involvement in North Sea oil production does not seem to conform to earlier domestic patterns of state economic involvement.

By identifying 'joint venture participation' as developed in the Middle East since the late 1950s as a possible model for British and Norwegian policies, we have demonstrated that the system developed by the UK and Norway during the 1960s and 1970s resembled the joint venture model in crucial ways. The creation of national oil companies in the 1970s, the granting to them of an (at least) 50 percent share of all new license partnerships, and the principle that the partners should 'carry' the national company's exploration costs, all were characteristics of the Middle Eastern formalized joint venture contractual agreements. In addition, in both Norway and the UK, participation by the state in oil production was chosen and formed under more and less explicit reference to the allegedly successful, formalized joint venture participation agreements in the Middle East, and contrasted to the unfortunate attempts by some countries at full nationalisation.

Analysing the joint venture participation model as a model that could be transferred between countries allows us to identify important differences between the UK and Norway in the way that the foreign model was accepted and adopted. In Norway, elements from the 'joint venture participation' model were promoted by civil servants who evidently regarded the experiences of developing producer countries as transferrable. Through a systematic evaluation of these experiences they came to identify their own proposals for state involvement in oil production with the joint venture participation system. The policy debate that ensued following economic oil discoveries in the North Sea c.1970 – resulting in the creation of the Norwegian State Oil Company in 1972 – came to partly build on and partly to find complementarity with these civil servants' views.

In the UK on the other hand, the 'joint venture' model was adopted somewhat more piecemeal and hesitantly and, it appears, without finding the same degree of complementarity between national political objectives and the full rationale for joint venture participation as formulated by developing producer country advocates. However, here also there was acceptance, based perhaps also on Norway's adoption of the model, that joint venture state involvement represented a fairly successful means to achieve petroleum policy goals.

The degree to which both Norwegian and British policymakers turned to producer country experiences ought to come as no surprise. When entering a global industry for the first time as a producer state, it seems only natural for a country's policymakers to be occupied by the experiences of other countries. The oil companies operating in the North Sea were to a large extent the same companies that operated in the Middle East, and some of them were already part of joint venture participation agreements with Middle Eastern national oil companies. What ought to surprise is the extent to which British and Norwegian oil policies, despite all this, have been explained in previous literature by the power of domestic political traditions, the 'shadow of the past'.

The recognition that transfer of ideas and organisational forms played a role in shaping the role of the British and Norwegian states in North Sea oil production does not, however, necessarily invalidate the significance of domestic political factors, including political traditions. First, such traditions may well have been important in forming *other* elements of petroleum policy with which we have not been occupied here but which influenced the role and significance of state involvement in production. Involvement in production was, after all, but one out of many aspects of petroleum policy, and the overall policies of the North Sea came arguably to differ quite dramatically from that of most Middle Eastern oil states. Second, existing desire for strong state involvement among Norwegian politicians in general, and among British Labour politicians in particular, may well have been a prerequisite for seeking state involvement in the first place.

The extent to which the actual policy outcome, the organisation of the state's involvement in oil, actually was defined by the principles and forms of Middle Eastern joint venture participation agreements testifies, however, to the *limits* of purely domestic factors, and in particular domestic traditions, in

explaining policy outcomes. Studying the emulation, adoption and translation of foreign ideas and organisational models seem a prerequisite to explain how and why state involvement in the North Sea was initially organized the way it was.

Notes

- 1 Many people have provided useful comments on the paper at various stages in its development. My fellow PhDs in the history department at the University of Oslo and John Peter Collett, together subjecting an early draft to sharp but constructive criticism, deserve special mention. Useful were also the comments I was so fortunate to receive from Ada Nissen, Einar Lie, Espen Storli, Marten Boon, Christel Koop and Martin Chick. Jonas F. Gjersø deserves my special gratitude for helping me significantly sharpen the argument – not to mention his indispensable help in camouflaging my shortcomings in the English language. The sole responsibility for the remaining flaws and insufficiencies, in style and content, is of course all mine.
- 2 By the term ‘state involvement in oil production’ I am referring to the involvement of an organisation in the state’s name and under the state’s legal control in the exploring for, extraction and sales of petroleum (and sometimes further processing into products) from domestic sources. By the ‘form’ of state involvement in oil production, I am here concerned with aspects of the formalised relationship between the state and non-state actors in the production. It was to a large extent by such formalised relationships (in countries where non-state actors in the industry existed) that the extent and character of state involvement was defined, including the state’s say in investment decisions, the state’s share of risk, investment costs and sales revenues. I exclude from this concept other state oil-related activities such as e.g. taxation, legislation, regulation etc. – although a state’s policy in these areas may significantly affect the importance, politically or financially, of a state’s involvement in production.
- 3 The Norwegian Continental Shelf stretches beyond the North Sea proper into the Norwegian and Barents Seas. State involvement in petroleum production was from the early 1980s introduced here as well.
- 4 I will not discuss the character of state involvement in the other North Sea states, i.e. the Netherlands, Denmark, West Germany and Belgium. State involvement in production was of a different and, generally speaking, far more modest character than that of Norway, and from what was anticipated in the UK in the mid-1970s.
- 5 Kuiken (2013) and Bamberg (2000) are, by studying big multinational oil companies, combining domestic and global dimensions into the narrative. Corti and Frazer (1983) claim the British National Oil Corporation was influenced by the establishment of the Norwegian State Oil Company.
- 6 Andersen refers to ‘political paradigms’, Nelsen largely to ‘precedent’.
- 7 There is reason to question this notion. As pointed out by Nore (1979), independent multinational companies would probably have been willing to explore parts of the continental shelves without being awarded extensive ownership in the form of licenses, enabling the North Sea states to establish some form of direct state involvement at an earlier point. This would, however, have caused a slower pace of exploration.
- 8 Although Kemp (2012a), Kuiken (2013) and Kuiken (2016) conduct a very different kind of analysis, their narratives seem to confirm the importance of Labour political objectives and thus of domestic factors, see e.g. Kuiken (2013, p. 135). Many authors touch upon the issue of whether the Labour government was sincere about its policies. Hann (1986) claims, interestingly, that the BNOC was not a means to an end, but an end in itself. Both Chick (2011) and Mabro, Bacon, Chadwick, Halliwell and Long (1986) warn against seeing BNOC solely in the perspective of Labour ideology, but do not really develop an ultimately alternative explanation.
- 9 Toye (2002) does, but he as well ascribes the desire for state involvement ultimately to ideological concerns and motives.
- 10 Chick (2011, p. 146) argues against seeing BNOC solely in this perspective, emphasising as well the general increase over the postwar period in government involvement in issues concerning ownership of common resources. Chick is still, however, primarily concerned with this development in the UK context.
- 11 Many would be quick to point out the significance of greater risk when explaining this difference. However, the acknowledgement of the evaluation of risk as modifying the impact of domestic policy traditions also clearly testifies to the *limitations* of such traditions in explaining policy outcome.
- 12 The only study with a transfer or diffusion perspective on national oil companies appears to be Kobrin (1985). Other studies of national oil companies are Beltran (ed.) (2010), Grayson (1981). See also McPherson (2003).
- 13 ‘State participation’ or just ‘participation’ was commonly used in the 1960s as a term for state involvement in oil production together with non-state agents. The term ‘partnership’ is in some works employed synonymously, see e.g. Mughraby (1966).
- 14 Report State participation in the field of hydrocarbons exploration and production, made by Bureau d’Etudes Industrielles et de Cooperation de l’Institut Francais du Pétrole, undated, probably 1972, folio ‘Statsdeltagelsesavtale

- 1972', box D/Da L0433, Ministry of Industry Archives, today part of the Archive of the Ministry of Oil and Energy, Norwegian state archives, Oslo. The archive will hereafter be referred to as 'Ministry of Industry Archives'.
- 15 Report State participation in the field of hydrocarbons exploration and production, op. cit. Evensen (1971, pp. 68–79), Zakariya (1976, p. 557).
 - 16 See next section on Participation in the North Sea. Additional evidence can be found in Comments of state participation, unsigned commentary to a Ministry proposal for a new state participation agreement, dated by hand 31 August 1972, the contents of which seem to have been written by someone affiliated to a foreign oil company, folio 'Ny statsdeltagelse 1972', box D/Da L0433, Ministry of Industry Archives; see also Zakariya, (1976), Mughraby (1966), Evensen (1971, p. 68).
 - 17 In Spain, national company INI held a privileged position in exploration for oil and gas. In Finland, fully state-owned Neste, in Sweden partly state-owned Oljeprospektering AB and in Denmark, entirely private Maersk Oil and Gas, enjoyed a similar privileged position. In France, a set of corporations had exclusive privilege to exploit the gas field at Saint-Marcet in Aquitaine. These companies merged in 1965 to form ERAP, later Elf Aquitaine. In Italy, the gas reserves of the Po valley were reserved for the Ente Nazionale Idrocarburi (ENI), and in Austria, the Matzen oil field was exploited by Österreichische Mineralölverwaltung (ÖMV). The major exception to the Continental European 'rule', besides the Netherlands, was West Germany. Report State participation in the field of hydrocarbons exploration and production, made by Bureau d'Etudes Industrielles et de Cooperation de l'Institut Français du Pétrole, undated, probably 1972, folio 'Statsdeltagelsesavtale 1972', box D/Da L0433, Ministry of Industry Archives.
 - 18 See in particular OPEC resolution XVI 90 1968, points 1 and 2, OPEC, 1980; on the sovereignty debate more broadly, see Schrijver, 1997.
 - 19 The character and consequences of the concession system is described and analysed in numerous works, see e.g. Blair (1978), Mikdashi (1966), Odell (1970) and Penrose (1969). An interesting recent interpretation is offered by Mitchell (2013).
 - 20 For a summary of Latin American experiences with multinational oil in the 20th century, see Bucheli (2010).
 - 21 Unlike in many Middle Eastern countries, the granting of licenses on the British and Norwegian continental shelves from the mid-1960s was fairly (although not entirely) standardised. The shelves were divided into standard-sized blocks, of which a limited number were licensed away, often individually, to different partnerships in fairly regular 'licensing rounds'. Although there have been several exceptions to these rules, the principles have been maintained.
 - 22 The extent to which the joint venture was formalised in the form of a legal body or a partnership, varied among the developing producer countries. American companies preferred partnerships because this would give them a more direct title to the oil, entitling them to depletion allowances and deductible expenses in the US tax system, see Zakariya (1976, p. 562).
 - 23 Even in hydropower, however, this strategy was quite pragmatic, see Skjold (2006, p. 40).
 - 24 See the 1948 report from the committee for the investigation of the mining interests of the Norwegian state, *Framtidig organisasjon og forvaltning av Statens berginteresser*, Innstilling I fra Komiteen for statens berginteresser av 1948, attachment to St. prp. (parliamentary proposition) 126 1950 *Om organisasjon og forvaltning av statens berginteresser m.m.* (on the organisation and administration of the State's mining interests) Although the committee recommended a state holding company to coordinate the state's interests, these interests did not comprise all mineral extraction in the country. The state acquired more of the national mining interests in the 1970s but was not explicitly motivated by principal considerations about the organisation of state involvement in mining, or in the economy more broadly, see St. prp. (proposal to parliament) 125 1975–1976 *Statens erverv av samtlige aksjer i Store Norske Spitsbergen Kulkompani A/S.* (on the State acquiring of all shares in the Spitsbergen coal company). All Norwegian public policy documents referred to in the footnotes, propositions, reports, etc., as well as the associated parliamentary debates, are collected in *Stortingsforhandlinger 1814–2005*, hereafter referred to as *Proceedings of the Norwegian Parliament*, available online in Norwegian from the website of the Norwegian parliament, Stortinget (www.stortinget.no/no/Saker-og-publikasjoner/Stortingsforhandlinger/) (retrieved 11 February 2019).
 - 25 *Proceedings of the Norwegian Parliament (Stortingstidende)* (18.10.1967). Interpellation from Member of Parliament Helge Jakobsen about the government's stance on exploration of the continental shelf (om Regjeringen vil ta initiativ til utforskning av vår kontinentalsokkel), 1967–1968, pp. 265–269, available in *Stortingsforhandlinger 1814–2005* (Proceedings of the Norwegian Parliament), available online in Norwegian from www.stortinget.no/no/Saker-og-publikasjoner/Stortingsforhandlinger/.
 - 26 See also Ministry of Industry Archives (07.11.1968). Report from meeting at the Ministry of Power, *Referat fra konferanse i Ministry of Power, London, 7 November 1968*, folio 'Statsdeltagelse generelt 1968–1971', box L0432, series D/Da, Olje- og energidepartementets arkiv (Archive of the Ministry of Oil and Energy).

- 27 Although BP was partly state-owned, it was obviously not being considered a state-controlled company, see e.g. Kuiken (2013) and Bamberg (2000).
- 28 Evensen's centrality to Norwegian petroleum policies is largely undisputed for the period 1962–c.1968. See e.g. Hanisch and Nerheim (1992) and Ryggvik (2009).
- 29 Evensen wrote: 'In the large petroleum producing states the oil policy has developed for decades and these countries therefore possess a fund of experience for better and for worse in oil policy questions which will be of great help when new problems arise.' ('I de store petroleumproduserende stater har oljepolitikken utviklet seg gjennom årtier, og disse land har derfor et fond av erfaring på godt og ondt i oljepolitiske spørsmål som vil være dem til stor hjelp når nye problemer oppstår.') (Preface to Evensen, 1971).
- 30 Gulnes also visited Jean Masseron of *L'Institut Francais du Pétrole* in Paris, on whom the oil office came to rely for counsel in subsequent years. At the time of the first encounters, Masseron was finishing his later widely translated book, *L'Économie des Hydrocarbures*, containing, among other things, an overview of recent developments in state participation agreements (Masseron, 1969); see also Ministry of Industry Archives (16/17.09.1968). Report Referat fra konferanse ved L'Institut Francais du Petrole. folio '440.5 Kontinentalsokkelen – fremtidig oljepolitikk I 1966–1969', box L0391, series D/Da, Olje- og energidepartementets arkiv (Archive of the Ministry of Oil and Energy).
- 31 Independent companies Phillips Petroleum and Elf/Total (the latter two united in the Petronors Group) accepted joint venture participation on a carried interest basis. The major companies eventually rejected this model, however, Esso managing instead to reach a net profit-sharing agreement and Shell put Evensen off with offering an educational programme for civil servants.
- 32 Ministry of Industry Archives (23.08.1968). P.M. vedrørende utlysning av suppleringsblokker på den norske kontinentalsokkel. Spørsmålet om deltakerrett for staten, Jens Evensen August 23 1968, folio 'Kontinentalsokkelen. Fremtidig oljepolitikk mappe 1 1966–1969', box Da L0391, Olje- og energidepartementets arkiv (Archive of the Ministry of Oil and Energy).
- 33 Ministry of Industry Archives (14.11.1968). PM, Kontinentalsokkelen. Statsdeltagelse i utlyste suppleringsblokker, NG/BK, folio 'Statsdeltagelse generelt 1968–1971', box D/Da L0432, Olje- og energidepartementets arkiv (Archive of the Ministry of Oil and Energy).
- 34 Ministry of Industry Archives. (15.10.1968). Statement from the Oil Council to the Ministry of Industry, folio '440.5 Kontinentalsokkelen – fremtidig oljepolitikk I 1966–1969', box D/Da L0391, Olje- og energidepartementets arkiv (Archive of the Ministry of Oil and Energy).
- 35 Calls for state involvement in exploration and future production in 1967–69 were partly based on optimism spurred by discoveries which subsequently proved less prospective. Political tensions and unstable cabinets 1970–1973, partly related to the question of Norwegian membership in the EEC, probably delayed the process of creating a state oil company.
- 36 Ministry of Industry Archives (14.11.1968). PM, Kontinentalsokkelen. Statsdeltagelse i utlyste suppleringsblokker, NG/BK, folio 'Statsdeltagelse generelt 1968–1971', box D/Da L0432, Olje- og energidepartementets arkiv (Archive of the Ministry of Oil and Energy).
- 37 Another Iraqi, Farouk Al-Kasim served as a consultant for the Norwegian Ministry of Industry from 1968, contributing among other things to draft the first draft proposal for the Norwegian State Oil Company in 1972. Other civil servants were, however, also involved in drafting the proposal, and the political leadership played an important role in defining its final content. Al-Kasim's contributions are thus probably somewhat overrated by some, see e.g. *Financial Times* (29.08.2009). The Iraqi who saved Norway from oil; see also Tonstad and Al-Kasim (2010).
- 38 Ministry of Industry Archives (27.01.1969). Letter from Jens Evensen to Hasan S. Zakariya, box D/Da L0121, Olje- og energidepartementets arkiv (Archive of the Ministry of Oil and Energy).
- 39 Ministry of Industry Archives (March 1972). State participation in the future development of petroleum resources on the Norwegian Continental Shelf, a preliminary report, box D/Da L0432, Olje- og energidepartementets arkiv (Archive of the Ministry of Oil and Energy).
- 40 Ministry of Industry Archives. (April 1972). Contract of consulting between Dr. Hasan S. Zakariya, Vienna, and The Royal Norwegian Ministry of Industry, April 1972, box D/Da L0432, Olje- og energidepartementets arkiv (Archive of the Ministry of Oil and Energy).
- 41 The point has also been confirmed in conversation with Nils Gulnes, then head of the Ministry's oil office.
- 42 The paragraph reads: 'That this special form of organisation may have caused incidents which for the producer countries have presented themselves as unreasonable, is natural enough. It has also led the producer countries, in order to protect their legitimate self-interests, to demand a more active participation on the side of production and marketing. In my opinion, Norway as well must draw the consequences of these peculiar conditions.' ('At denne spesielle organisasjonsform kan ha ført til foreteelser som for produksjonslandene har fremstilt seg som urimelige, er naturlig nok. Den har også ført til at produksjonslandene for å beskytte berettigede egeninteresser, har krevet en

- mer aktiv deltagelse på produksjons- og omsetningssiden. Etter min mening må også Norge trekke konsekvenser av disse spesielle forhold') (Evensen, 1971, p. 95).
- 43 This share would later be supplemented by an option to increase the share even further according to a 'gliding scale', defining the final state share according to estimated peak production of a discovery.
 - 44 Ministry of Industry Archives (19.09.1974). PM Deltagelse og samarbeidsavtale, OW/GM, box D/Da L0139, Olje- og energidepartementets arkiv (Archive of the Ministry of Oil and Energy).
 - 45 See Secretary of State for Energy, Eric Varley (col. 484) and Mr Hardy (513) in the House of Commons April 30 1975, Second Reading of the Petroleum and Submarine Pipe-lines Bill (Hansard, vol. 891).
 - 46 See Secretary of State for Energy, Eric Varley, in the House of Commons April 30 1975, Second Reading of the Petroleum and Submarine Pipe-lines Bill (Hansard, vol. 891 col. 487).
 - 47 White paper (St. meld.) 25 (1973–74). Om petroleumsvirksomhetens plass i det norske samfunn, available in Stortingsforhandlinger 1814–2005 (Proceedings of the Norwegian Parliament), available online in Norwegian from www.stortinget.no/no/Saker-og-publikasjoner/Stortingsforhandlinger/.
 - 48 Notice e.g. the explicit reference to Evensen in Innst. S. 294 (Proposal of the parliament's Industrial Committee about the white paper 76) 1970–71, 636.
 - 49 Innst S. 294 (1970–1971). Proceedings of the Norwegian Parliament. Proposal of the parliament's Industrial Committee about the white paper 76, available in Stortingsforhandlinger 1814–2005, available online in Norwegian from www.stortinget.no/no/Saker-og-publikasjoner/Stortingsforhandlinger/.
 - 50 There is broad consensus on the importance of the 1971 debates, see i.e. Hanisch and Nerheim (1992). The importance of the civil service's views on these debates has been less readily admitted. Hanisch and Nerheim (1992) points to the significance of internal memos in the Norwegian Labour party written by party member Arve Johnsen in 1970 for the subsequent formulation of policy Johnsen's memoranda, although less occupied with the Middle East, shows some of the same concern with sovereignty as e.g. Evensen's (1971) report.

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OPEC and Russia

A happy pro forma marriage

Mikhail Krutikhin and Indra Overland

Russia has long been a potential dream partner for the Organization of the Petroleum Exporting Countries (OPEC). Russia could greatly enhance the cartel's market power and has several allies among the OPEC member states. During the 2010s it seemed that the potential of the OPEC–Russia relationship was finally being realized as they grew closer. However, in this chapter we argue that the strengthened dialogue has little impact on physical oil output and the level of mutual commitment remains low. What they do share is an interest in the semblance of cooperation to push oil prices upward through impacting market psychology. This strategy is in line with the postmodern turn in Russian foreign policy, as proclaimed by Vladislav Surkov and others. It also has some important foreign policy side benefits for Russia, such as weakening its international isolation after the conflict in Ukraine and making it possible to simultaneously befriend various Middle Eastern countries that are at odds with each other. The OPEC–Russia dalliance is also convenient for a third party – the USA. Although the USA is still a net oil importer and its consumers dislike high oil prices, they benefit American oil companies and their employees and investors, especially in the shale oil sector. Arrangements between OPEC and Russia are thus not only a happy pro forma marriage but also a successful ménage à trois.

A match made in heaven?

There are several reasons why Russia might seem like a good candidate for cooperation with OPEC. First, like OPEC, the Russian government would like to see stable, high oil prices, as the petroleum industry is the backbone and main source of income for the Russian economy. Exports of crude oil, natural gas, and refined petroleum products account for 64.4 percent of total Russian exports.¹ Second, as the world's second largest oil exporter, Russia could give a powerful boost to OPEC's market power. Third, the Russian state seems to have a good basis for functioning as an OPEC member. The state's share in Russia's production of crude oil approaches 65 percent; it has a controlling interest in country's largest producer (Rosneft) and owns the fourth largest producer, Gazprom Neft (Overland et al., 2013). In addition, the Kremlin has considerable informal power to induce oil companies to do what it wants through the mechanisms of selective law enforcement, suspended punishment, and *kompromat*. *Kompromat* is compromising information about people held in store as a lever in future conflicts or as blackmail material and plays an important role in Russian society (Ledeneva, 2006, p. 60; see also Baekken, 2014; Lauth, 2000; Lauth, 2004).

However, experience shows that an alliance between Russia and OPEC is not easily achieved (Boué, 2004) and the current cooperation between OPEC and Russia may be more of an opportunistic dalliance than a genuine alliance. This interpretation is in line with the self-proclaimed ‘postmodern’ political strategies proposed by influential Kremlin advisor Vladislav Surkov, who argues that we live in a post-truth world and what matters is the semblances and impressions that can be created and how they can be used (Yaffa, 2015). From this perspective, the purpose of the seeming alliance between OPEC and Russia may be to drive up oil prices in the long term rather than to form a lasting bond.

Why it is difficult for Russia to join OPEC?

All member countries of OPEC have national oil companies that can either determine the policy for their governments or follow a policy dictated by the governments. By contrast, perhaps surprisingly, Russia has no formal mechanisms to regulate the volume of oil production, consumption, or export apart from its general tax regime – and changing the flow of oil with a tax amendment is not accomplished swiftly. Thus, the Russian government has few tools apart from the informal ones listed above to change the volume of production and export quickly and thus contribute to OPEC’s market management. This situation contrasts with even with non-OPEC member Norway. Although Norway is averse to mixing politics and business in its oil exports, even the Norwegian system leaves the door more ajar for government intervention than does the Russian system. Paragraph 4–4 of the Norwegian petroleum law states that the government can change the rate of oil production when this is justified by ‘important societal considerations’ (*vektige samfunnshensyn*).²

Despite the powerful informal levers that the Russian government seemingly has on the country’s oil companies, there is more to the decision-making hierarchy in Russia’s oil industry than meets the eye. The Ministry of Energy functions mainly as a lobbyist for the interest of oil companies in the Council of Ministers, where the companies’ main adversary is the Ministry of Finance. Consequently, it is normally the ministry that heeds the recommendations of the companies, rather than vice versa, and the ministry’s role in relations with OPEC is mostly limited to declarations, which often have little practical significance for the actual behavior of the Russian oil producers.

Certain technical specificities of Russian oil production further cloud its prospects for OPEC membership. Most Russian oil wells are located in northern areas with low temperatures where stopping the oil flow can lead to ice plugs that damage the wells and require costly maintenance. The high-water content of the wellhead fluid of many Russian oil wells, in which water flooding is the main method of enhancing oil recovery, increases the danger of plugs when a well is stopped. For many Russian upstream operators, it is therefore difficult simply to suspend ongoing work and wait for oil prices to rise.

Finally, Russia’s ability to regulate oil production and exports is also limited by the absence of any large storage facilities for crude oil, leaving little flexibility in the country’s oil exports. Once oil is pumped out of Russian oilfields, it has to keep flowing through the pipelines to consumers and tankers without too much delay.

In combination, the reasons listed here ensure that Russia is not as useful a partner for OPEC as might seem at first sight. This is also demonstrated by the history of their relations, to which we turn in the next section.

The history of relations between OPEC and the USSR

In the first years after the founding of OPEC in 1960, the Soviet Union regarded the organization as a possible addition to the ‘anti-imperialist’ camp, a counterweight to the Western petroleum monopolies, and an element in the national liberation movements of developing countries. Soviet leaders even believed that OPEC could potentially become a fully fledged socialist organization if only the ‘reactionary

monarchies' among the organization's member states could be overcome (Dasgupta, 1975, p. 357). Moscow hoped that its allies within the organization – particularly Algeria, Iraq, and Libya – might facilitate increased Soviet influence.

In the 1970s, the USSR considered becoming a member of OPEC, but this idea was never implemented.³ There were several reasons for this. If it were to become an OPEC member, the Soviet Union would want to play an important role in the organization, but the founding states did not want to be overshadowed or dominated by the Soviets. Moreover, the OPEC statute included requirements that were incompatible with the USSR's communist agenda, for example, a 'fair return' on capital for investors in the petroleum industry⁴ (OPEC, 2012). OPEC's most important member country, Saudi Arabia, had even broken off diplomatic relations with Moscow in 1938, accusing the Soviets of inciting revolution among Muslims. Diplomatic relations between the two countries were not resumed until 1992. Finally, as the Soviet oil and gas industry continued to develop, natural gas became increasingly important both in the internal Soviet energy system and as an export to other communist bloc countries and to Western Europe. OPEC is an oil cartel, not a gas cartel.

As a result of these factors, the idea of joining OPEC, or even cooperating with OPEC, lost its relevance. Instead, OPEC and the Soviet Union came to be seen as rivals rather than potential partners in many contexts (Stein, 1980; Dasgupta, 1975).

The post-Soviet track record

Post-Soviet Russia inherited a strained relationship with OPEC from the USSR (Mann, 2009). During the 1990s, Moscow was in any case more focused on improving its relations with the West than on courting OPEC (Elass and Jaffe, 2009). Russia did not become an observer in OPEC before the summer of 1998 when it started attending all the conferences of the organization in that capacity. The leading members of OPEC showed an interest in expanding cooperation with Russia and, in 1998/9, non-OPEC member Mexico and OPEC members Saudi Arabia and Venezuela allegedly jointly suggested forming an informal super-alliance of oil producers dubbed 'The Big 8'.⁵

Over the next 20 years, Russia agreed several times with OPEC to cut production, but never fulfilled its pledges (Elass and Jaffe, 2009). In 1998, Russia assured OPEC it would trim its oil production by 7 percent, but in fact left it unchanged.⁶ The promise had been dictated by the decline of global oil prices, which fell from USD 25 per barrel in early 1997 to USD 10 at the end of 1998. The decline had been provoked by OPEC's 1997 decision to boost daily oil production by 2.5 million barrels and by shrinking demand for oil because of the Asian financial crisis of 1997/8. In March 1999, OPEC plus Mexico, Norway, Oman, and Russia agreed on a production cut of 2.1 million barrels per day. Russia's share in that cut was supposed to be 100,000 barrels per day.⁷

Following that agreement, oil prices recovered: one barrel of Brent was sold for USD 23 at the end of 1999 but increased to USD 32 by March 2000. However, Russia broke its promises and increased its daily oil production from 6.17 million barrels to 6.18 million barrels in 1999 while other members of that temporary alliance either reduced their output (as Saudi Arabia did) or kept it at the same level (as Norway did).

By the summer of 2000, it became clear that Russia was not going to join OPEC and the Russian government said so officially. Russian officials and media claimed there had been 'oral' invitations, but this could not be confirmed⁸. Moscow-based experts argued that if the country joined OPEC it would still only be 'a minor partner' of the cartel and would be obligated to lower oil exports and abandon its work towards reviving oil production after the 1990s collapse.⁹

Within Russia at that time, there was no consensus on cooperation with OPEC. Some of the major Russian oil companies, such as Sibneft, Surgutneftegas, and Yukos, believed that low prices would help them defeat competitors and expand their share of international markets. By contrast, Bashneft, Lukoil, and

Tatneft, which were experiencing problems with reserves and upstream projects, wanted prices to be as high as possible.¹⁰

In the first quarter of 2002, the Russian government announced that it was reducing its oil production by 150,000 barrels per day under an agreement with OPEC to keep prices from plummeting¹¹ (Mann, 2009). By the end of the quarter, however, it became obvious that the majority of Russian oil companies were following their previous production plans and were paying little heed to the government's recommendations.¹² In the third quarter of that year, Russia's production grew at the fastest rate in the whole post-Soviet period. OPEC expressed displeasure with Russia's reluctance to honor its promises and only the growth of international oil prices due to other developments prevented further conflict.¹³ After that period of empty promises and 'misunderstandings', it is unclear whether OPEC and Russia have made any genuine mutual commitments or attempts at cooperation and coordination for purposes of *physical* oil market manipulation – regardless of their public declarations of unity.

Russia did not join OPEC in the organization's periodical production cuts, such as the October 2008 agreement to decrease daily production by 4.2 million barrels. Igor Sechin, deputy prime minister at the time, attended OPEC sessions and agreed to such cuts, but Russia continued raising its oil output. Relations between OPEC and Russia at the time were limited to regular exchanges of opinions at the annual sessions of the OPEC–Russia Energy Dialogue, which was formalized from December 2005 onwards, without any tangible results.¹⁴

OPEC had a weak basis for its displeasure with Russia. During the period 1999–2007, as oil prices trended upwards, most OPEC member states did all they could to boost their own oil output. Between May 2002 and December 2006, OPEC increased its overall production by 16 percent (Simoniya and Zhukova, 2008).

Cooperation after 2014

A new form of cooperation between Russia and OPEC started taking shape after the decline of oil prices in late 2014 under the weight of the shale revolution and the financial crisis. The approach of Saudi Arabia, OPEC's dominant member state, stunned the world when it unexpectedly decided not to draw down its output to help prices recover. Similarly, Russian companies continued their production programs as usual. By the end of 2016, however, the Saudis realized that low prices were not shutting down American shale operators and OPEC was forced to act. Russia and other producers were invited to join forces to stop prices from going lower.

Russia's new cooperation with OPEC was motivated by both political and economic considerations. The Russian leadership viewed international cooperation as a symbolic and practical countermeasure against the attempt by Western states to isolate Russia through sanctions (Fjaertoft and Overland, 2015).

Initially, when the Russian Ministry of Energy was negotiating possible cooperation with OPEC in the fall of 2016, the Kremlin was skeptical about the outcome of this initiative but allowed Energy Minister Alexander Novak to go ahead with a deal. The idea of production cuts made little sense in light of the same ministry's well-publicized expectations of production growth. Still, the prospects of seeing oil prices rise were highly attractive, as it could help save Russia's budget from some of the acute problems it was experiencing at the time due to the oil price collapse, sanctions, and inflation¹⁶ (Grigoriyev et al., 2015). And the financial effect of the cooperation was indeed significant.

It should have been relatively easy to achieve the production cuts agreed upon, as they were to be counted against a benchmark in October 2016 when Russia was producing at the record-breaking rate of 11.23 million barrels per day. The accord with OPEC called for a reduction of just 300,000 barrels per day from that high level.¹⁷ In practice, Russian oil production remained flat in 2016/17.

In late 2016, OPEC and Russia joined forces to confront the challenge of American shale oil production and the new alliance resulted in cooperation between 24 oil-producing countries that agreed to restrict

their production and keep prices from falling. The first tangible results of this cooperation became evident in the second half of 2017 when the surplus supply started to shrink; by January 2018, prices edged up above USD 71 per barrel for Brent, the highest level since December 2014.

Moscow played an important role in the OPEC+ deal, which helped enhance Russia's reputation in the Arab world and with some non-Arab oil-producing countries and also put a dent in the international isolation that Western countries were trying to impose on Russia in connection with the conflict in Ukraine (Fjaertoft and Overland, 2015). Furthermore, the cooperation with OPEC helped the Russian media maintain Vladimir Putin's image as an influential politician in the global arena – especially in the eyes of Russian voters, which is obviously what matters most to the Kremlin.

A happy pro forma marriage

In addition to reputational and diplomatic benefits for Moscow, cooperation with OPEC has had a considerable effect on the Russian economy through higher oil prices. In 2017, when the joint decision on production cuts was in effect and oil prices headed upward again, Russia received additional income of USD 117 million per day according to calculations by the International Energy Agency.¹⁸

The effect of the price hike on Russian budgetary revenues in 2017 was estimated by Minister of Energy Alexander Novak at 1.2 trillion rubles, or USD 20.6 billion at the average exchange rate of that year.¹⁹ Since the expenses of the federal budget in 2017 totaled 16.6 trillion rubles, the effect was equivalent to almost 14 percent of the government's expenditure. In December 2018, Novak stated that Russia had gained an extra USD 120 billion in 2017/18 thanks to its cooperation with OPEC.²⁰

This extra revenue enabled the Russian government to extend the life of one of its sovereign wealth funds, the Reserve Fund, which had been expected in 2016 to be depleted in early 2017. As result of the higher oil prices, the fund's life was prolonged until early 2018, by which time it had been fully spent and was merged into the National Welfare Fund, another sovereign wealth fund.

Oral interventions in the oil futures market aside, Russia's actual contribution to production cuts under the OPEC+ deal is dubious. Russia's oil output in 2017 amounted to 546.8 million tons (10.981 million barrels per day), just 0.1 percent less than in 2016 (see Figure 20.1). Since 2016 was a leap year, Russia's average daily oil production actually grew slightly from 10.965 million to 10.981 million barrels per day.²¹

In 2018, oil production in Russia accelerated, defying the Russian officials' declarations of solidarity with OPEC. During that year, Russia produced 555.84 million tons (11.45 million barrels) of crude oil per day, 1.6 percent more than the previous year.²² This means that rather than falling below the October 2016 benchmark, as Russia had promised, its production in fact increased by 0.3 percent against that benchmark (see Figure 20.1).

In theory, Russian oil companies should have been compelled by the government, which declared compliance with the OPEC+ deal, to slow down production and decelerate profit generation because the state takes the bulk of the gains from higher prices in the form of a progressive export tax on oil introduced in 2004. The tax rate is adjusted every two months, increases gradually when the oil price rises above USD 25 per barrel, and may reach 65 percent when the price of oil is high.

The limited number of large-scale oil producers in Russia (see Figure 20.2) and the power of informal administrative pressure in Russia means that the government expects to achieve a decrease in production without using fiscal measures or other formal tools. It boils down to a simple equation: the government boosts its revenues from the oil industry through seeming cooperation with OPEC that raises prices and thus taxes; the companies receive the part of the price increase that is left over after taxes, but they have to sacrifice some of their investment programs and marketing plans in order to stay on the safe side of the government.

Regardless of the short-term financial gains for the Russian government, Deputy Prime Minister Arkady Dvorkovich believed that the government-induced restriction of the oil industry's investment plans might

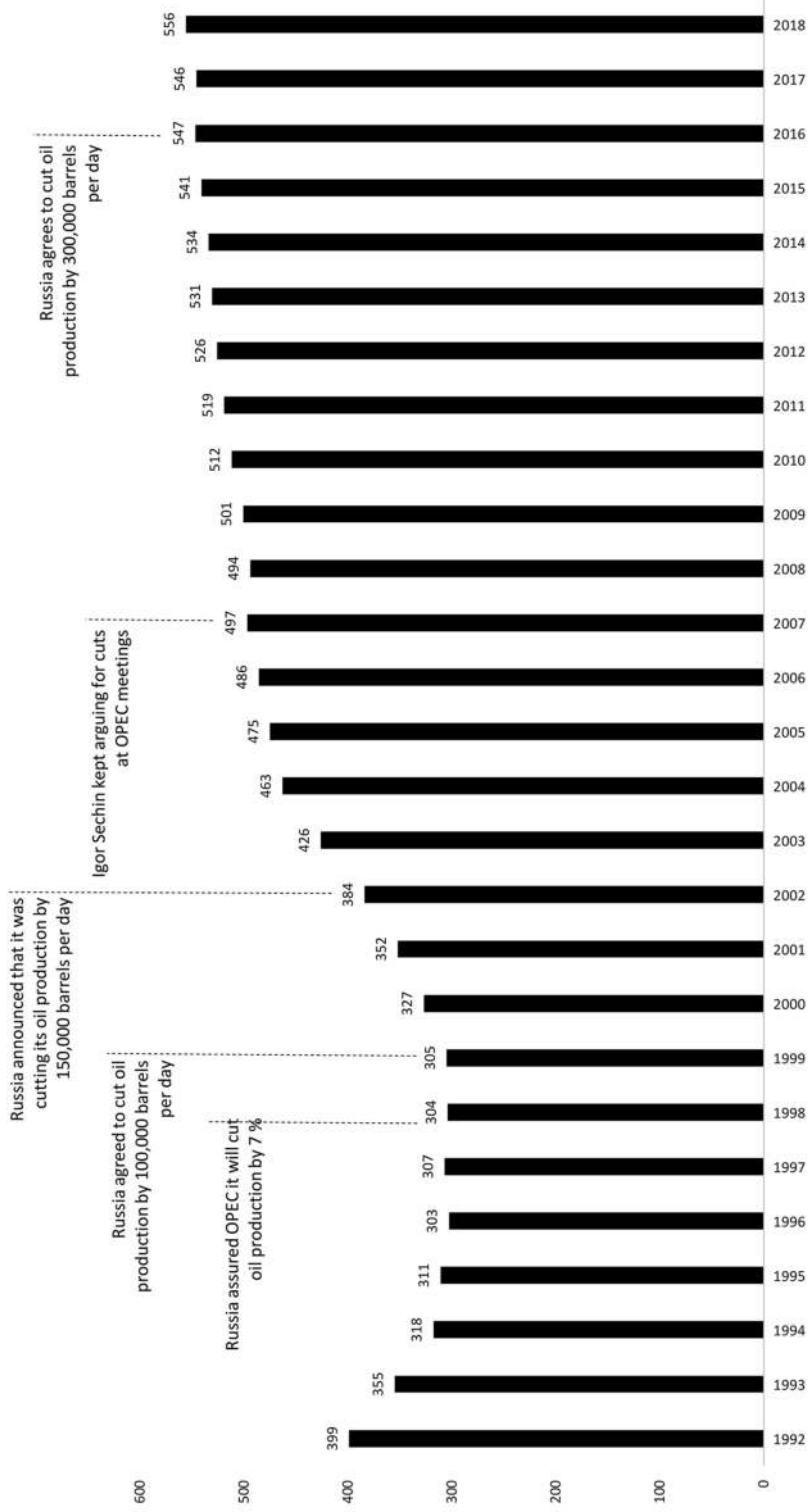


Figure 20.1 Russia's oil, condensate, and NGL production in million metric tons
Source: Russian Ministry of Energy.¹⁵

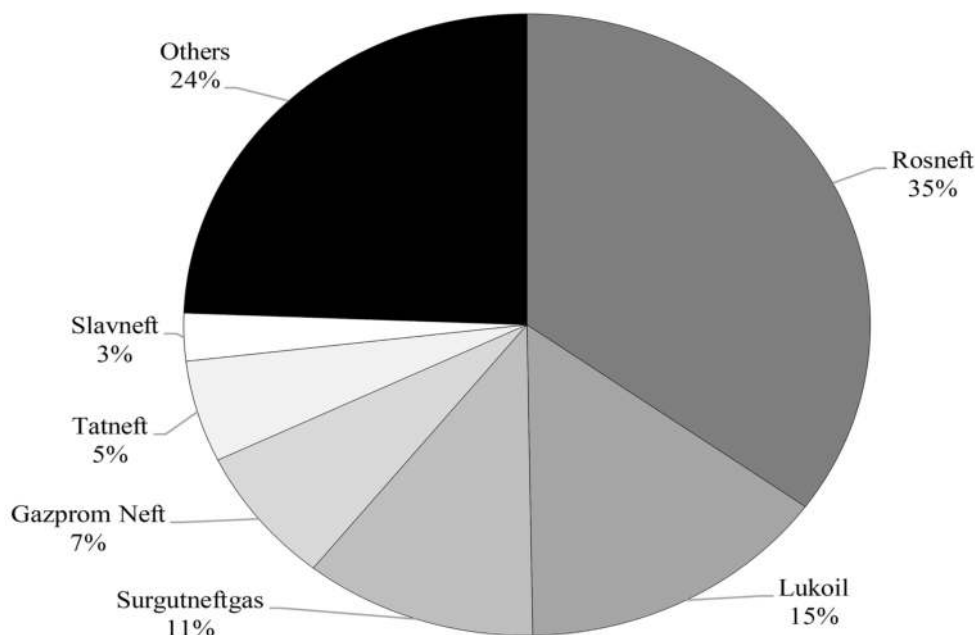


Figure 20.2 Russian crude oil production by company, January–November 2018²³

have a long-term negative effect on the economy. He warned that stagnating oil production would translate into lower GDP growth because the oil industry plays a vital part in the national economy.²⁴

The agreement with Russia was seemingly beneficial for the OPEC members, too, as it was associated with higher oil prices. Saudi Arabia alone, according to IEA statistical data, was earning an additional USD 100 million daily in 2017 thanks to the deal, and OPEC as a whole was taking in about USD 362 million of extra revenue per day (IEA, 2018).

It would be impossible to invite oil companies in the United States and some other countries to join OPEC's production cuts, the cooperation with Russia was decisive for OPEC's recent success in driving up oil prices. For some actors in the USA it was clearly helpful to have OPEC – 'morally' supported by Russia – doing the hard work to keep oil prices from falling too low. Although the USA is still a net oil importer and American oil consumers dislike high prices, the USA is also the world's largest oil producer, American oil companies and their owners and employees benefit from higher oil prices, and they constitute important interest groups. Especially the shale oil industry, in which many large-scale and risky financial bets have been made, benefited from higher oil prices brought on by the cooperation between OPEC and Russia.

The show must go on?

The Saudis and other OPEC members insist that the cooperation between OPEC and Russia to hold back production will continue for a long time. The OPEC/Non-OPEC Joint Ministerial Monitoring Committee in Muscat in January 2018 stated that producers should extend their cooperation beyond 2018 in order to assure 'stakeholders, investors, consumers, and the global community that this is something that is

here to stay' and that producers 'are going to work together' within a longer time frame. Saudi energy minister Khaled al-Falih acknowledged, however, that the mechanism for long-term cooperation remains to be defined and that extending the cooperative framework would not necessarily mean sticking to current production targets.²⁵

OPEC was determined to continue playing along with Russia and reduce the likelihood of abrupt termination of the cooperation. By calling for cooperation beyond 2018, Saudi Arabia charted the route it desired for the market, in which OPEC+ plays a permanent role in managing market expectations and revenue maximization, rather than output maximization, is the main guiding principle.

Financial considerations

If the cooperation between OPEC and Russia evolves beyond the declarative level in the future, some Russian companies could in principle be forced, through government pressure, to curb their operational plans and limit activities to brownfield projects instead of investing in new exploration and development. However, such policies would accelerate the ongoing depletion of Russian reserves and national production might start falling at a quicker pace than expected.

If prices fall despite the OPEC+ accord, Russia will face a big challenge: a shrinking supply of hard currency from oil exports could force the government to alleviate the tax burden on the oil companies to enable them to develop new, higher-cost production. Otherwise, production will decline naturally due to the gradual depletion of existing fields. In any case, lower oil prices will translate into smaller revenues for the federal budget.

When income flows become dangerously small, Russia will have two options for its relations with OPEC: either to continue cooperation and hope that Saudi Arabia's market management scheme keeps prices at a reasonably comfortable level or to abandon OPEC+ and try to maximize the volume of oil exports over prices. For the time being, the probability of Russia remaining in the OPEC+ alliance appears higher.

Off the record, officials at the Russian Ministry of Energy admit that negotiations about production cuts with OPEC members are often contentious and domestically controversial. Saudi representatives, they say, accuse Russia of being unable to meet the agreed cuts; the Russian delegations respond by pointing out the well-known fact that there is little discipline within the cartel and many OPEC member states fail to stick to their quotas.

In late 2017, the Russian government was considering gradual abandonment of the cooperation with OPEC. Opponents of the cooperation, including Rosneft CEO Igor Sechin, argued that the production cuts and the ensuing higher oil prices encouraged the USA and other oil producers to invest heavily in the development of shale and deep-water reserves, and that the OPEC+ agreement would therefore be counter-productive in the long term.²⁶ They also pointed out that Saudi Arabia itself seemed to be preparing to abandon attempts at boosting oil prices through production cuts. In February 2019, Igor Sechin came forth with a warning: cooperation with OPEC had become a strategic threat to Russia's oil industry.²⁷

By contrast, the Russian government officials and experts who advocated an extension of the agreement with OPEC believed that even a short period of higher oil prices would help the Russian oil industry and prevent the imminent decline of production due to lack of investment.

Conclusions

The continuation of the OPEC+ constellation has political side-benefits for Moscow. In the context of Western sanctions and attempted international isolation, any international organization prepared to engage with Russia is of interest to the Kremlin. Cooperation with OPEC, even without joining the organization

as a member, is a way for the Russian government to show both foreign and domestic audiences that Russia continues to play a role in global affairs. Conversely, should the sanctions be weakened, the international relations incentive for Russia to cooperate with OPEC might also be weakened.

Apart from the sanctions, the Russian government regards OPEC+ as an opportunity to ally itself with some of the most important regimes in the Middle East as well as Venezuela and some African countries. Moscow also sees OPEC+ as a means to compete with the USA internationally. However, American oil companies are beneficiaries and even free riders on this effort when it succeeds in talking up the oil price.

The cooperation with OPEC is also regarded by the Kremlin as a way to reconcile some tensions in Russia's relations with countries in the Middle East as Russia seeks to establish good bilateral relations and even to strike alliances with regimes that are in conflict with each other. Iran and Saudi Arabia have long been at odds, but both countries are OPEC members and have to sit at the same table in Vienna to draw up plans of joint action in the oil markets. Russia, seeking to befriend everybody in the region – Iran, Iraq, Qatar, Saudi Arabia, Syria, Turkey, etc. – is often treated with suspicion by enemies of each of these countries (Freedman, 2010). The cooperation within the framework of OPEC+ may help Moscow to iron out some of these 'misunderstandings'. In practice, however, OPEC+ has not accomplished much in helping the Saudis understand why Russia is courting the Iranians, and the Iranians are wary of Russia's intentions to befriend the Saudis.

Today, Russia can hardly be regarded as an aspiring leader of decision-making in the world oil market, partly because of its international political isolation and partly because its oil production may be approaching a 20-year peak before declining again.²⁸ Russia's alliance with OPEC has lacked significant contributions in terms of production cuts and remains limited to speeches that have a largely short-term impact on the oil derivatives markets. The deterioration of OPEC as a cartel and its resulting loss of influence²⁹ make the OPEC+ alliance less significant (Mann, 2012). However, for the time being, this alliance can still influence market psychology and provides side-benefits for Russian foreign policy; it is therefore likely to continue for some time.

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Part IV

OPEC and international energy
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Beyond the Texas Railroad Commission

Thirty years of American precedent for OPEC

Ellen R. Wald

The Organization of Petroleum Exporting Countries (OPEC) was formed in 1960, but it was not the first group to attempt to regulate oil production or prices. Preceding OPEC's founding, various efforts in the United States set examples of what could and could not be accomplished through governmental control and inter-party coordination in the oil industry. The Texas Railroad Commission of the early 1930s is a well-known early American model for OPEC, as Venezuelan oil minister and OPEC co-founder Juan Perez Alfonso studied the commission and its methods of regulating oil production as a way to raise prices. However, there was precedence for cartel-like behavior in the US dating back to the late 1920s and as far forward as the Suez Canal crisis during the late 1950s. The successes and failures of these efforts demonstrated the possibilities and the limits of different methods of collusive and coordinated behavior in the oil market. Indeed, many of the shortcomings found in these early models are evidenced in OPEC's beleaguered attempts to support oil prices in oversupplied markets.

Texas Railroad Commission and overproduction

The Texas Railroad Commission (TRC) is a state regulatory agency established in 1891 to protect consumer interests in rail travel. With roots in the Progressive Era, it originally issued rules and regulations to prevent price gauging, ensure safety, and support economic growth in Texas. Later, it turned its regulatory attention to oil pipelines, oil and gas production, natural gas, bussing, and trucking. Between 1910 and the 1930s the TRC attempted to regulate oil production in Texas with the ultimate purpose of raising the price of oil. The TRC's primary method of accomplishing this was through a method of restricting oil production known as prorationing.

The agency is a well-known precursor to the OPEC oil cartel, particularly because OPEC co-founder Juan Perez Alfonso studied its records when he resided in the United States, but often fell short of its price and production targets. The TRC's control was limited because it could only attempt to influence oil production in the State of Texas. Although Texas was an important part of the US oil market, its oil industry still only accounted for 24 percent of US domestic oil production in 1927 (McNally, 2017). Exercising central control over a large enough segment of the oil market, which the TRC, as a state institution, could not do, would prove vital to effective production regulation. At the same time, the TRC did achieve some limited success. Although the TRC commissioner lacked the legal means to compel producers to comply with production quotas, he was most successful at persuading producers to comply

through force of personality and political maneuverings (Childs, 1991). Similarly, OPEC has no legal method or mechanism to compel oil producers to comply with production quotas. Success at regulating oil prices came either through voluntary cooperation with production quotas or involuntary drops in production due to physical destruction, sanctions or natural decline in production capacity.

The TRC's purported authority to regulate oil production came from two laws passed in 1917 and 1919. The Pipeline Petroleum Law, passed in 1917, declared that pipelines were common carriers similar to railroads and provided the TRC with jurisdiction over them. In 1919, the Texas Legislature passed the Oil and Gas Conservation Law (Railroad Commission of Texas, cited in McNally, 2017, p. 22). In 1927, the TRC concluded that these two laws provided the commission with the legal authority to approve proration agreements. Proration is a method used by oil field operators to ensure that oil production occurring in the same field but with wells owned by different operators functions equitably (Childs, 1991, p. 307). Proration was seen as a necessary method of conservation because of a principle in American property rights known as 'rule of capture'. According to the rule of capture, a property owner has the right to capture all minerals beneath the surface of his property. However, crude oil is unlike other minerals in that it flows into wells regardless of property lines (Isser, 1991). The practical effect of this in Texas was that property owners were drilling too many wells in order to capture their oil before a neighbor captured it. As a result, more oil was being produced than was needed and significant amounts of oil were being wasted – in some cases evaporating in the sun (Childs, 1991, pp. 302–302).

The TRC used its regulatory authority to help major oil firms negotiate what were seen as fair and equitable proration agreements. In 1927, when the TRC issued its first field-wide production quotas, its goal was to eliminate wasteful practices not impact prices. These regulatory agreements were developed by TRC commissioners in conjunction with industry executives and professionals. As a result of the mutual trust and respect between parties, the production restrictions were largely adhered to. These proration agreements proved effective at conservation but did not affect prices because relatively few fields were actually subject to the agreements (McNally, 2017, p. 71). The TRC did not even attempt to include most Texas oil fields and oil producers in the voluntary quotas, and unsurprisingly the un-prorated fields continued to overproduce. As a result, oil prices fluctuated wildly during this period. The TRC found itself unable to expand the proration agreements to more fields because of widespread claims that the agreements violated, at least the spirit if not the letter, of anti-trust laws and amounted to price fixing (Childs, 1991, p. 308).

In 1930, the discovery of the East Texas oil field starkly revealed the limitations of the TRC's ability to regulate oil production (Childs, 1991, p. 312). The disastrous collapse in oil prices that resulted finally brought the federal government into the oil market, but still revealed significant limitations on centralized production regulation in the United States. The East Texas oil field was the largest oil field discovered in the United States at the time (McNally, 2017, p. 72). Production on this field was not dominated by the major oil companies that the TRC was used to working with on proration agreements. In fact, the discovery of this field (much like the shale oil revolution today) substantially fragmented and diversified the oil industry in the early 1930s. By 1931, over 1,000 different oil companies were producing oil from 12,000 wells in East Texas, whereas before this discovery, integrated oil majors owned 23 percent of all oil wells in production in the US.

The impact on the oil industry was immediate. Prices dropped from an average of \$1.00 a barrel in 1930 to around 15 cents a barrel in May 1931. Some spot prices were even lower, averaging between six and two cents a barrel (Yergin, 2009, p. 230). Proration, which had only worked on a limited basis based on personal connections between the commissioners and the oil executives, was impossible. The TRC attempted to set limits on production but only some producers adhered to the quotas. Producers profound distrusted each other to the point where they feared that neighboring producers would get their oil 'first' (Childs, 1991, p. 316). The panic led to the creation of 'teakettle' refineries – makeshift refiners set up right next to the wells that produced a brand of light oil that locals took to calling 'Eastex gasoline' and

was so low in value that stations accepted barter in exchange (Yergin, 2009, p. 230). By August 1931, the East Texas field was producing over one million barrels of oil a day despite the TRC's proration order of 220,000 barrels a day (Childs, 1991, p. 317).

Nearby Oklahoma experienced similar problems, despite the fact that Oklahoma state laws provided the government with significantly more enforcement power over the state's oil production than Texas law granted the TRC. In fact, Oklahoma's governor sent in the state's militia to assert control over major fields in the state after declaring a state of emergency and martial law. His objective, despite the fact that Oklahoma's proration laws were currently being challenged in federal court, was for the troops to keep control until production decreased and prices rose to \$1.00 a barrel (Yergin, 2009, p. 233). The governor of Texas followed suit and sent in the National Guard and the Texas Rangers in August 1931, to enforce the TRC's proration agreements (Childs, 1991, p. 317).

The troops were able to impose a complete shutdown of the oil industry in East Texas. By April 1932, oil prices rose to nearly \$1.00 a barrel. Shortly thereafter, the Texas legislature passed new laws that allowed the TRC to act to counter 'economic waste' and the TRC issued new proration regulations. Even though the TRC no longer had to hide behind conservation rationale and had the power to regulate production for economic reasons, many in Texas considered the proration quotas tantamount to price fixing. Enforcement was weak and producers found ingenious ways to hide oil illegal production. A particularly inventive producer built cement walls around a well to try and conceal its presence (McNally 2017, p. 75).

Oil prices failed to respond to the TRC's new production regulations for two reasons. First, the TRC set production quotas too high to support prices in the \$1.00 range, and second, the TRC failed to crack down on excess oil production known as 'hot oil' (Yergin, 2009, p. 234). Even in 1933, the TRC continued to lack legitimacy in the eyes of most oil producers. It did not help the commission that 19 of its proration orders in 1932 had later been overturned by the courts (Childs, 1991, p. 322). The 'hot oil' problem continued to grow in 1933 and spilled over into neighboring Oklahoma. Smugglers were illegally transporting hot oil from Texas into Oklahoma and dragging down oil prices supposedly supported by that state's proration laws (McNally, 2017, p. 76). Prices fell from 75 cents a barrel to 10 cents a barrel (Yergin, 2009, p. 234).

The New Deal and the oil code

The inauguration of the Roosevelt Administration and the package of legislation known as the 'New Deal', brought an unprecedented level of federal involvement in the oil industry. The federal government's attempt and ultimate failure to regulate oil production at a national level yielded several lessons for the future OPEC cartel. The voluntary association and demand-based consensus that oil-producing states eventually formed to keep prices stable also yields valuable examples for OPEC today, especially concerning quota compliance.

In 1933, amidst the Great Depression, the Roosevelt administration took office. FDR promised the American people a 'New Deal' and that the federal regulation his administration would wield on the devastated American economy would bring new prosperity. With regard to oil, Roosevelt's new secretary of the interior, Harold Ickes, was named 'Oil Czar' and granted an unprecedented degree of control over the US oil industry. With prices in East Texas as low as four cents a barrel only two months after the inauguration, even the traditionally territorial and staunchly independent oil industry executives were asking FDR to intervene in the market (Yergin, 2009, pp. 235–237). Ickes was very clear that his approach would be to bring price stability to the oil industry through federal control over both production and prices (McNally, 2017, p. 77; Childs, 1991, p. 324).

This unprecedented control came from the National Industrial Recovery Act (NIRA), a piece of comprehensive legislation that aimed to establish federal regulation over multiple aspects of the US

economy. The NIRA went into effect in June 1933. It essentially suspended antitrust laws and charged various industries with developing industry-wide codes of 'fair competition' (Maier et al., 2006, p. 712). Industries would be permitted to set prices and even allocate markets as long as the government appointed members of the National Recovery Administration (NRA) approved the industry's codes. In the interim, while these industry codes were under development, the federal government turned its attention to the issue of hot oil (Nash, 1968, p. 136).

This illicit oil was still being siphoned off from pipelines and illegally transported across state lines. Harold Ickes had President Roosevelt issue an executive order on July 12, 1933, that prohibited the transportation of hot oil and allowed the Department of the Interior, which Ickes also headed, to enforce this executive order. According to Ickes, about 500,000 barrels of oil were being shipped in contravention to state laws that prohibited it. Smugglers from Texas and Oklahoma were the worst offenders. To combat the sale of hot oil, the president's executive order authorized the Department of the Interior to issue federal certificates of clearance to oil producers to transport oil out of state and to shut down operations that were not in compliance (Childs, 1991, p. 329). Federal enforcement made all the difference in Texas and Oklahoma, as officials were able to stop rail shipments of hot oil from crossing state lines within a week of deployment (McNally, 2017, p. 77). For a short time, during the summer of 1933, oil production and prices were under control.

That control did not last, primarily because the industry, the states, and the federal government could not reach a consensus regarding the oil code mandated by the NIRA. Producers and transporters of hot oil found ways to subvert the federal agents, including one particularly ingenious driller who devised valves that twisted in the opposite direction so that they appeared shut off when in fact they were turned on (McNally, 2017, p. 78). Production began to surge and prices fell while industry representatives and government officials squabbled over proposed oil codes. When industry players proved unable to agree amongst themselves, the NRA administrator, Hugh Johnson, prepared his own code for consideration. Johnson's proposal did not include price-fixing, an issue that had divided the oil industry, but did impose limits on working hours that were designed to limit production (Nash, 1968, p. 138).

When Johnson proved unable to rally industry support behind his proposed oil code, Ickes finally took it upon himself to construct and administer an oil code himself. Ickes proposed a heavy-handed code with price-fixing and production limits imposed by the government. Still, Johnson and the industry representatives were unable to work out their differences. Ultimately, Roosevelt ordered Johnson and Ickes to reach a compromise. That compromise was reflected in the Oil Code, which allowed the federal government to recommend production quotas but not to implement them. Although the production regulation model won out over the price-fixing model, the Oil Code did permit the president to set oil prices for a period of 90 days. Ickes, not Johnson, was named administrator of the Oil Code (Nash, 1968, pp. 138–140).

Roosevelt also appointed an industry advisory group, called the Production and Coordination Committee, comprising individuals from oil companies who were nominated by trade industry groups to serve. Ickes had the power to set monthly production quotas based on recommendations made by the Production and Coordination Committee. Ickes was also permitted to limit imports of foreign oil to that imported between June and December of 1932 (Nash, 1968, p. 140). Ickes initially focused on controlling production. He used recommendations from the Production and Coordination Committee to get monthly production quotas for each state. Combined, these quotas called for a 300,000-barrel per day reduction in production, nationally. States were responsible for enforcing the production limits on their own. In Texas, that duty fell to the Texas Railroad Commission. Enforcement was a challenge because the TRC lacked the information necessary to identify overproducers and, even when it could, the penalty for overproduction was not a severe deterrent.

Hot oil production continued to depress prices in the second half of 1933 and Ickes began discussing potential price fixing. The reaction from the industry was so vociferous and varied that Ickes eventually

ceased his efforts to control oil prices through means other than production quotas (Nash, 1968, p. 142). At the same time, the State of Texas passed several laws that strengthened the TRC's enforcement ability and made over production punishable with jail time. Stronger enforcement efforts in Texas eventually helped lift oil prices across the nation, though implementation took some time.¹

Still, the production and distribution of hot oil hindered the federal government's ability to lift oil prices by controlling production. Under section 9(c) of the NIRA, Ickes established the Federal Tender Board in October 1934. This agency, which was welcomed by the Texas Railroad Commission, issued permits necessary to transport oil out of state (Childs, 1991, p. 329; Nash 1968, p. 145). Ultimately, this action helped curb the production and transportation of hot oil. Despite the presence of oil producers and state legislators in Texas who continued to resent the federal government's intervention, the process appeared to work well and resulted in higher oil prices throughout 1934 (Childs, 1991, p. 329).

The end of the Oil Code

However successful federally managed production quotas had been at lifting oil prices, the process could not continue. In January 1935, the Supreme Court declared section 9(c) of the NIRA, which prohibited hot oil, unconstitutional. The court ruled that federal officials did not have the power to enforce the production quotas. In its place, Congress rushed to pass the Connolly Hot Oil Act to prevent hot oil from entering interstate commerce (Nash, 1968, pp. 145–146). The Connolly Hot Oil Act grew out of the Federal Tender Board, which preserved state sovereignty (Childs, 1991, p. 329). It simply prohibited the transportation of 'contraband oil', however, it did allow for the president to suspend this prohibition if the president believed that conditions would lead to an imbalance of supply and demand. President Roosevelt also re-established the Federal Tender Board by executive order, which regulated the transportation of oil (Nash, 1968, p. 146).

Then, in June 1935 the Supreme Court overturned the entirety of the NIRA and stripped Harold Ickes of any authority to set and enforce state production quotas. Despite this blow to the Roosevelt administration, oil production and prices remained steady. The Connolly Hot Oil Act ensured that the federal government continued to enforce the ban on hot oil even though the Department of the Interior could no longer institute production quotas. However, the Bureau of Mines continued to prepare and circulate monthly demand estimates that had formed the basis of the quotas (Yergin, 2009, p. 239). Through the regulatory framework and methods of cooperation established during the year of production regulation, oil-producing states continued to use those demand figures as the basis for their own proration agreements. Many states adhered specifically to the figures provided by the Bureau of Mines, although the TRC often used higher production levels for proration than the demand figures published by the Bureau of Mines (Yergin, 2009, p. 240).

In December 1934, the governor of Oklahoma invited the governors of oil-producing states to meet in Oklahoma to discuss forming an intra-state oil compact. Only the governors of Kansas and Texas attended the meeting, but they began to develop the framework for intra-state cooperation on oil production. Again, states were divided on whether the target should be production or prices, although almost everyone involved agreed that their goal should be to stabilize the oil industry (Nash, 1968, pp. 148–149).

Initially, Oklahoma envisioned the group as a state organized cartel. Texas, however, balked at the loss of state control joining such a group would entail. As long as the federal government regulated hot oil and oil imports, the governor of Texas opposed regulating production and prices (Nash, 1968, p. 149). By the end of 1935, the oil-producing states had formed a group called the Interstate Oil Compact, which President Roosevelt supported. The Interstate Oil Compact was formed not as a cartel, but along the lines of Texas's vision – a multi-state council for the discussion and exchange of information, legislation, proration agreements, and oil conservation plan (Yergin, 2009, p. 240). More oil-producing states joined the Compact, which became known as the Interstate Compact to Conserve Oil and Gas. It was eventually

approved by Congress in August 1935, although that approval was limited to two years. That approval was renewed every two years until 1943, when it was renewed for a four-year period (Nash, 1968, p. 151). The voluntary association between oil-producing states, even with the TRC's persistently higher proration rates, did help keep oil prices stable. In fact, between 1934 and 1940 the average price of a barrel of oil ranged from \$1.00 to \$1.18 (Yergin, 2009, p. 242).

The early failures and later successes of the TRC reveal several key lessons for OPEC. The most important lesson was that the oil trade does not exist in a vacuum. The TRC's efforts were futile in the absence of inter-state trade regulation. Until the federal government stepped in to regulate the interstate oil trade, attempts at controlling production within Texas could not work. Coordination, cooperation, and compliance (whether voluntary or enforced by a greater power) were necessary for production regulation to keep oil prices at a stable level.

Like OPEC, the oil-producing states in the 1930s struggled with production quota compliance, particularly once the federal enforcement mechanism was no longer available to them. Ultimately, achieving a level of compliance relied on mutual trust and reciprocal interests. When it was in the collective interests of all oil-producing states to coordinate production based on demand estimates they trusted, the states were able to keep production at levels that could ensure a stable price. This is clearly an issue OPEC countries continue to struggle with, especially as many of the oil-producing nations that make up its organization diverge greatly in their economic and political interests.

Export Petroleum Association

In 1928, while the Texas Railroad Commission was still trying to assert some regulatory influence on Texas oil production through its voluntary proration agreements, three of the world's largest oil companies were dividing global markets and attempting to set standard oil prices. The CEOs of Jersey Standard, Royal Dutch Shell, and Anglo-Persian (later British Petroleum) met in the Scottish Highlands castle of Achnacarry to negotiate a solution to oil price fluctuation (Falola and Genova, 2005, p. 40). Their primary concern was similar to that of the TRC – overproduction and declining prices – but they also sought to assert control over global markets (Pelletiere, 2009, p. 49). To this end, the three companies worked to divide markets between themselves, arranged to share storage facilities and refineries, coordinated oil transportation, and pledged to use the American Gulf Coast benchmark as a basis for setting prices on oil sold around the globe. The formula agreed to was the price of the American Gulf Coast benchmark plus the freight rate calculated for the distance between the Gulf of Mexico and the point of sale regardless of where the oil was produced (Pelletiere, 2004, p. 50; Yergin, 2009, p. 247).

No documents were ever signed by the companies who crafted the Achnacarry (or 'As Is') Agreement, but each participant agreed to produce only its allotted quota for its assigned markets. The quotas were based on the percentage of the company's total sales depending on its share of the market in 1928. A company could only increase production in fixed percentage with its share of the market, and only then, in concert with demand growth. Right from the start, the three major oil companies knew their arrangement would not be successful unless they enticed other oil companies to join it. In 1929, a major Russian oil company agreed to join the Achnacarry group, but the US, a major producer at the time, was still a problem (Yergin, 2009, pp. 247–248).

At the time, US oil exports accounted for one-third of all oil consumed in the US (Yergin, 2009, p. 248). In order to exert some measure of control over US exports, Jersey Standard and 14 other American oil companies formed the Export Petroleum Association, essentially a legal cartel. The association was incorporated in 1929 and issued a hundred shares of stock to 15 American oil companies including Jersey Standard, Standard Oil of New York, the Texas Company, Gulf Refining Company, Vacuum Oil, and Shell Union (Royal Dutch Shell's subsidiary in the United States) (Randall, 2005, p. 41).

The Export Petroleum Association, which added two more companies to its roll in 1930, set prices, established export quotas, and arranged coordinated shipping for member companies (Bamberg and Ferrier, 1994, p. 111). Generally, this kind of collusion would be illegal under American anti-trust law. However, the 1918 Webb-Pomerene Export Trade Act permitted companies doing business outside the United States to coordinate their efforts jointly as long as that business took place outside the United States. Essentially, that act granted immunity to from anti-trust prosecution to companies that engaged in cartel-like practices (including price fixing, quota enforcement, market allocation, and coordinated marketing) (Dick, 1996, p. 241). According to the Webb-Pomerene Act, the cartels formed by US exporters had register with the Federal Trade Commission (FTC) and members had to adhere to the terms set by their cartels (Dick, 1996, p. 245).

By 1930, the Export Petroleum Association controlled 45 percent of US oil exports and had grown to include some petroleum derives products as well (Bamberg and Ferrier, 1994, p. 111). However, the Expert Petroleum Association proved unsuccessful at controlling the price of oil exported from the US and ultimately disbanded in 1936. Cartel members experienced great difficulty reaching a consensus on prices. When the group attempted to use the same formula as the Achnacarry Agreement, it was found to be in violation of the Webb-Pomerene Act for its association with domestic oil sales. According to the law, exporting cartels could have no affiliation with domestic sales. Disparate interests and conflicting demands meant members of the Export Petroleum Association often failed to reach a consensus on prices and quotas that members could and would adhere to (Bamberg and Ferrier, 1994, p. 112).

The other problem the group faced was that 45 percent of the US export market was not a large enough portion of the market to control prices. The Export Petroleum Association's failure, along with the Achnacarry Agreement's global failure to control markets and prices, demonstrated the necessity of true centralized planning at government level. With so many different companies involved, most without control over globally significant amounts of production, market coordination simply proved impossible to effectively manage. The government-centric model adopted by OPEC (in which most oil production is controlled by a national oil company that takes direction on production from the government) eliminates these issues.

The Suez Canal crisis

When OPEC was established in 1960, it was not only envisioned as an organization that could exert control over oil prices and oil production, but also as a mechanism for oil-producing countries to take control of their oil resources from the Western oil companies that operated on their soil (Wald, 2018, p. 131). When OPEC was formed in 1960, many countries, including Saudi Arabia, did not yet run their own oil industries. Western companies managed the oil industries. What control, then, could the oil-exporting countries have over their oil resources if they were run not by the governments but rather by foreign companies? As it turned out, control over exports and transportation could be an effective tool even if a government lacked control over production.

This was a lesson that Abdullah Tariki, OPEC's Saudi co-founder, likely learned from the Suez Canal crisis in 1956, when the Middle-Eastern oil industry faced a crisis of transportation precipitated by the closing of the Suez Canal. This crisis caused an acute oil shortage in Western Europe that the United States was prepared to alleviate through a coordinated supply effort directed by a cartel-like association of American and European government committees and companies. The US was prepared to allow companies to participate in activities that blatantly violated anti-trust laws because President Eisenhower believed it was in America's best interest to assist its European allies.

However, when Britain and France (along with ally Israel) attacked Egypt, the United States changed its position. The Eisenhower administration decided not to permit these oil companies to collude. Following the lead of Saudi Arabia, which had closed its ports to oil exports bound for Britain and France, the US

used its control over global oil supplies to influence geopolitical events. The combined economic pressure compelled Britain and France to capitulate, withdraw their troops from Egypt, and abandon plans to overthrow Nasser. The implications for OPEC, and particularly the Arab members of OPEC, were clear – effective control over the supply and movement of oil could be used to achieve geopolitical aims.

The Suez Canal is a narrow man-made waterway of a hundred miles, stretching between the Gulf of Suez in the Red Sea and Port Said in the Mediterranean Sea. It was originally built by the French, but by 1956 it had become a British and French venture (Yergin, 2009, p. 461). The Suez Canal was integral to British and French trade in the 19th and 20th centuries. By 1956 it had become the primary vehicle through which Persian Gulf crude oil reached refineries in Western Europe. Approximately two-thirds of the crude oil refined in Western Europe came from the Middle East and two-thirds of that supply arrived through the Suez Canal (Bamberg, 2000, p. 76; Yergin, 2009, p. 642). The remainder traveled through a network of pipelines to ports in Syria and Lebanon on the Mediterranean Sea and was then shipped to Western Europe by tankers.

The British occupied Egypt beginning in 1882 and, from then on, controlled access to the canal by force. After World War II Britain withdrew its troops but maintained political and economic control through close association with Egypt's monarch, King Farouk. In 1952 growing nationalism led to King Farouk's overthrow in a military coup. Two years later, Colonel Gamal Abdel Nasser, an ardent Egyptian nationalist, came to power. The British government and French interests still owned the Suez Canal Company, which, to Nasser, symbolized latent European colonialism and a loss of profit from the Canal's near-constant use (Yergin, 2009, p. 463). In 1954 Nasser began harassing British troops and the Suez Canal Company workers stationed in the Canal Zone. At the end of 1955, he boldly turned away from the Western powers by contacting Moscow and purchasing arms from Czechoslovakia. This move alarmed the United States, which had initially taken Nasser's position, viewing British and French control of the Suez Canal Company as a vestige of the colonial era and a source of strife between the Western world and the Middle East. Nasser's growing association with communist countries and the Soviet Union ignited American and British fears that Nasser might take control of the canal and close the waterway to Western shipping (Yergin, 2009, p. 464).

In response, the US concluded that if Nasser closed the Suez Canal to Western shipping, major oil shortages would result because of insufficient numbers of tankers to transport oil from the Persian Gulf around the Cape of Good Hope.² Production could be increased in the United States, Canada, and the Caribbean to account for the loss of oil from the Middle East, but it would take at least 90 days to achieve this increase. In addition, increasing oil production at such a rate could deplete known US sources of oil and might be unsustainable over long periods of time.³ Though this would not negatively impact American consumers, it was clear that resulting oil shortages would cripple America's European allies.

Nasser indeed nationalized the Suez Canal Company on July 26, 1956. This precipitated the formation of an oil industry coordinating group called the Middle East Emergency Committee (MEEC). Through this group, American, British, and French oil companies, through their respective government agencies, designed methods of coordinating oil exports and transportation in the event of a Middle East oil crisis so that Western Europe could continue to receive enough oil from American and South American sources to keep their economies from collapsing during the crisis. At the time, American oil production was high enough that it could afford to divert domestic oil resources to aid Britain and France as long as various companies cooperated and colluded to do so.

Such activities would normally be illegal under US anti-trust laws, but the Eisenhower Administration granted the MEEC a special exemption from anti-trust prosecution because the US believed it was in its best interest to support its allies.⁴ Britain and France set up a similar committee composed of representatives from British Petroleum, Shell, and CFP called the Oil Emergency London Advisory Committee (OELAC), with functions similar to those of the MEEC and designed to work with the MEEC.⁵ The two committees immediately began drafting plans to coordinate the transportation of Middle-Eastern oil to

Europe using existing tankers and to accommodate for shortages by reallocating oil from the United States, Canada, and the Caribbean to Europe. By October of 1956, the oil companies and governments involved had established the mechanisms for international government-business coordination to combat oil shortages and were prepared to act if and when Nasser blockaded the canal.

Britain and France considered Nasser's nationalization a threat to their interests and sought to retake the canal and topple Nasser. When the two countries began airstrikes against the Egyptians in the Suez Canal on November 1, 1956, Nasser responded by closing the Suez Canal to all shipping by sinking 30 Egyptian ships at six points throughout the waterway.⁶ On November 3, 1956, the Syrian army, at Egypt's behest, demolished three pumping stations from the Iraq Petroleum Company's pipeline from Iraqi oil fields to ports in Syria and Lebanon to complete the strangulation of European oil supplies.⁷

This essentially halted the flow of oil from all Middle Eastern sources except Saudi Arabia. Kuwaiti, Southern Iraqi, and Iranian oil all traveled from ports in the Persian Gulf around the Saudi peninsula, through the Red Sea and the Suez Canal to the Mediterranean. Northern Iraqi oil flowed through two pipelines emptying into ports in Lebanon and Syria and was then transported by tanker through the Mediterranean. Then, Saudi Arabia closed its ports to oil bound for Britain and France as well. Even though the company producing its oil, Aramco, was an American company, the Saudi government controlled the country's ports and could, with its absolute control, prohibit Aramco from shipping oil to European destinations. With the Suez Canal closed and IPC's pumping stations sabotaged, only Aramco's oil was able to leave the Middle East through the Trans-Arabian Pipeline (Tapline), which emptied into a port in Lebanon and remained untouched.⁸ All other oil would have to be loaded onto tankers and shipped around Africa (Bamberg, 2000, p. 78).

However, the Americans and the British had prepared for this situation. European countries would have to ration their oil supplies, but the MEEC and its European counterpart had prepared tanker schedules and alternative shipping routes to make up for the loss of the Suez Canal and the IPC pipelines. Great Britain had some stores of petroleum to fall back on, but all of their rationing, transportation, and purchasing plans depended on oil from American companies and permission from the US president to engage in cartel-type coordination.⁹ Without cooperation from the United States, Great Britain and France would soon experience crippling oil shortages.¹⁰

However, President Eisenhower decided not to allow the committee to put its coordination plans into action or to redirect oil supplies from US, Canadian and Caribbean sources to Europe.¹¹ This news shocked the British, which demanded an explanation. Specifically, President Eisenhower objected to the fact that Britain and France (along with Israel) had conspired to invade and occupy the Suez Canal in an unprecedented display of military aggression and refused agree to a cease-fire that the US wanted. In order to compel Britain and France to withdraw from Egypt, the United States used oil to exert economic pressure (in addition to diplomatic pressure) on its own allies by denying the oil companies antitrust immunity. As expected, the American oil companies declined to participate in joint operations with British and French oil companies.¹²

Without any action from the United States or its oil companies, the oil shortage in the U.K. and France became 'extremely serious'.¹³ The United States persisted and refused to help alleviate European oil shortages until Britain and France withdraw their troops from the Suez Canal zone. By mid-November European countries began to ration oil and, had the crisis continued for an additional four to six weeks, it appears that most of Europe would have faced a series economic crisis (Neff, 1981, p. 420). Finally, on 29 November 1956, Britain and France agreed to withdraw their troops from Egypt. As soon as France and Britain agreed to withdraw their troops, President Eisenhower gave American oil companies antitrust immunity and the National Security Agency activated the MEEC to begin coordinating oil relief for Britain and France.¹⁴

The lessons for OPEC from the 1956 Suez Crisis were twofold: 1) sovereign oil-exporting countries can impact diplomacy and control the energy economy even without national control of oil resources or oil

company participation simply by controlling exports; and 2) coordinated export policies are ineffective when instituted by companies because they can be overruled at the whim of the government. The United States was able to effectively ‘wield the oil weapon’ even though the US oil industry was not nationalized. Instead, the government effectively controlled company behavior through its power to grant or withdraw exemptions to antitrust laws. Even though the oil companies were prepared to participate in the effort to supply Britain and France with oil, their efforts were halted by the sovereign power of their nation. At the same time, OPEC learned from Aramco and Saudi Arabia’s actions during the Suez crisis that regardless of who produced a country’s oil, the sovereign nation ultimately controlled exports. Aramco, an American company operating in Saudi Arabia, would have continued to ship oil to Britain and France from its ports but was prevented from doing so by the sovereign power of Saudi Arabia acting in solidarity with Egypt.

Conclusions

OPEC improved on American cartel practices and experiences. The success of OPEC’s advances was proven in 1973, when OPEC countries exerted their control over exports and production to unilaterally raise the price of oil without the agreement of the international oil companies who produced and distributed that oil (Wald, 2018, pp. 292–294). With the US no longer a net exporter, OPEC (knowingly or not) used the lessons of prior attempts by the United States at production, price, and export regulation to successfully influence the price of oil in 1973. The limited impact of the Texas Railroad Commission on production and prices revealed that voluntary participation in production quotas along with regulatory control limited to only a segment of the market could not produce the desired effect on the price of oil. The failure of the Export Petroleum Association demonstrated the difficulty of reaching a consensus when too many important players and different goals much reach a consensus and that participation of 45 percent of exporters is not sufficient to impact prices. The Suez Crisis taught OPEC that national sovereignty ultimately trumps corporate control when it comes to oil production and exports. This was an especially important lesson for OPEC countries that did not have national oil companies in 1973, like Saudi Arabia. Even though Aramco, an American company at the time, was responsible for producing and distributing Saudi oil and did not necessarily support Saudi Arabia’s participation in the OPEC production cuts, the company had no choice but to acquiesce because ultimately Saudi Arabia controlled access to its oil.

Many of the failures – or less than successful attempts to control prices – found in US history mirror some OPEC’s continued difficulties in maintaining stable oil prices. For example, lack of consensus due to disparate interests was a primary reason why OPEC was unable to set new quotas at its November 2014 meeting and why a later attempt to freeze oil production at the April, 2016 Doha meeting failed. The growth of non-OPEC oil production also made it more difficult for OPEC cut production and see a corresponding increase in prices. In fact, this was the primary reason why OPEC needed to bring in non-OPEC producers like Russia, Mexico, Kazakhstan, and Oman in November 2016 for its joint OPEC and non-OPEC production cut agreement. On the other hand, OPEC’s ability to cut prices by increasing oil production remains a powerful tool.

Notes

- 1 *Texas State Library and Archives Commission*, ‘The Era of State and Federal Cooperation’. Industry, Regulation, and the Texas Railroad Commission. Available from: www.tsl.texas.gov/exhibits/railroad/oil/page9.html.
- 2 *Foreign Relations of the United States (1955–1957)*, volume X. ‘Memorandum for the Record, Prepared in the Oil and Gas Division, Department of the Interior’ (Washington, 14 August 1956), pp. 590–592.
- 3 *Foreign Relations of the United States (1955–1957)*, volume X. ‘Memorandum for the Record, Prepared in the Oil and Gas Division, Department of the Interior’ (Washington, 14 August 1956), pp. 590–592.
- 4 *Foreign Relations of the United States (1955–1957)*, volume X. ‘Memorandum for the Record, Prepared in the Oil and Gas Division, Department of the Interior’ (Washington, 14 August 1956), p. 620.

- 5 *BP Archive* 59138 (19 September 1956). 'Personal Cable From London'.
- 6 *BP Archive* 59138 (13 November 1956). 'Suez Canal Blockage'.
- 7 *BP Archive* 59138 (6 November 1956). 'Letter to William Fraser'.
- 8 *BP Archive* 59138 (7 November 1956). 'Interruption of Movements of Oil from Iraq to Eastern Mediterranean', p. 78.
- 9 *Foreign Relations of the United States* (1955–1957), volume X. 'Memorandum for the Record, Prepared in the Oil and Gas Division, Department of the Interior' (Washington, 14 August 1956), p. 934.
- 10 Even with some reallocations of petroleum resources and tanker tonnage, Europe expected to be 'confronted with the immediate prospect of a reduction in oil supplies that approaches 25 per cent of its total requirements'. This was expected to cause a 15% drop in industrial output, and a subsequent drop in employment of 4.5 million people (*BP ARC* 59138. 17 November 1956, 'The Suez Canal Crisis: The major Economic Impact on Europe', enclosed in 'Letter from Fraser to Drake').
- 11 *BP Archive* 53332 (7 November 1954). 'Memorandum for the Chairman, "O.E.L.A.C."'
- 12 'While there was little doubt that we could get oil to Great Britain and France by the simple collaboration of the American oil companies without invoking the program outlined by the MEEC, this course of action might invite difficulties under the existing anti-trust laws of the United States' (*BP ARC* 53332. 7 November 1954, 'Interruption of Movements of Oil From Iraq to Eastern Mediterranean', p. 630).
- 13 *Foreign Relations of the United States* (1955–1959), volume XVI, document 54. 'Telegram from Embassy in the United Kingdom to the Department of State' (1 November 1956), p. 934.
- 14 *Foreign Relations of the United States* (1955–1957), volume X, document 238. 'Editorial Note' (Washington, 30 March 1957), p. 644.

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The road not taken

Frank Hendryx and the proposal to restructure petroleum concessions in the Middle East Aater the Venezuelan pattern

Juan Carlos Boué

In memoriam Robert Mabro, dearest and much missed friend.

In 1959, during the First Arab Petroleum Congress in Cairo, the foremost oil exporters of the world (Iran, Saudi Arabia, and Venezuela) for the first time ever agreed to defend their economic interests in unison, in reaction to a unilateral reduction in posted prices by the major oil companies. This initial *entente cordiale* between oil exporters, known as the Gentlemen's Agreement, was the direct forerunner of the Organisation of the Petroleum Exporting Countries (OPEC), founded a year later in response to further downward adjustments in posted prices.

The conversations leading up to the Gentlemen's Agreement were held in secret, and their significance only became evident in hindsight. That is not to say, however, that the Congress itself was uneventful. In particular, a part of the proceedings that attracted much attention was a speech that the legal advisor to the Directorate of Petroleum and Mineral Affairs of Saudi Arabia (headed by Abdullah Tariki) delivered to the study group dealing with economic and legislative issues.¹ This speech – entitled 'A Sovereign Nation's Legal Ability to Make and Abide by a Petroleum Concession Contract' – made the case for altering 'the general legal bases of the relationship created by contract in the granting of petroleum concessions by [... the] independent sovereign government[s]' of the Middle East, a region already seen at that point as the center of gravity of the world petroleum industry (Platt's Oilgram News, 1959).

It is difficult to overstate the fright that this speech gave oilmen and consumer country governments. The impact of its message was greatly magnified by the identity and nationality of its bearer: as a dismayed executive attending the Congress complained to journalist Wanda Jablonski, 'we [had] expected politics, of course, but we did not expect them to originate from an American' (Duguid, 1976, p. 100). And not just any American, mind: Tariki's legal advisor happened to be an attorney from an Ivy League school who, until a few months before, had occupied a very senior position – legal counsel – within the corporate structure of the Creole Petroleum Corporation of Venezuela (the most profitable among all the affiliates of the Standard Oil Company of New Jersey – nowadays ExxonMobil – and, up until 1951, the largest single producer of crude oil in the world). The name of this once notorious personage was Frank Clifton Hendryx.

Hendryx and Tariki were to work together closely from 1959 until the latter's dismissal from ministerial office in March 1962. The aim of their collaborative efforts was to substitute what they saw as lopsided concessionary arrangements with a more equitable and hence sustainable *modus vivendi* for the oil industry as a whole, based on mutual compromise and respect between concessionaires and their host governments. Their efforts in this direction were decried by oil companies and the governments of their home countries as communist-inspired larceny. However, the positions that Hendryx advocated during his short time in the limelight were not born out of left-wing radicalism (Hendryx was a man of patrician upbringing, and expensive pastimes, like African hunting expeditions).² Instead they reflected his frustration at the intransigent, often revanchist and invariably counterproductive postures that guided the interactions of oil companies such as Creole/Jersey with the sovereign governments of countries like Venezuela and Saudi Arabia.

À propos such interactions, in an interview dating from February 1960, Hendryx confessed his stupefaction as to 'how established and experienced overseas oil producers, in daily working contact with the governments of the producing countries, can be unaware of the economic and political thinking of those nations'. In Hendryx's eyes, such condescension ignored the rather important fact that '[t]hese are now sovereign nations ... [that] are important to the world, and no intelligent end can be served by considering them or their national aspirations as not important or worthy of respect'. This path, Hendryx observed, would lead the companies down a cul de sac: '[t]hose nations would be really grateful for the collaboration of the oil companies. But without them, the oil-producing countries can and will go forward' (Terzian, 1983, pp. 49–50). However, Hendryx's warnings went unheeded and, instead, the oil companies persisted in their habit of trying to settle complex and weighty political and economic questions through the ritual invocation of the mantra *pacta sunt servanda*. The ultimate result was the one Hendryx had foreseen: the oil-producing countries did indeed go forward and, in so doing, they ended up by nationalizing the petroleum concessions in toto (thereby proving that Keynes was right when he said that 'the absolutists of contract are the real parents of Revolution') (Keynes, 1924, p. 68).

To Cairo, by way of Brazil and Venezuela

Hendryx's journey to Cairo began in mid-1948 when, together with his family, he embarked for Rio de Janeiro to become general counsel to the Standard Oil Co. do Brasil – an affiliate of Jersey Standard. Before joining Jersey, Hendryx had been a litigating attorney in Washington, DC, and Philadelphia.³ Then, in 1946, he had moved to Mexico to represent the interests of an arms manufacturer. Hendryx was minded to settle in Mexico, but he had to revise his plans when one of his daughters contracted polio, forcing the family to return to the US to seek treatment for her.⁴

Hendryx arrived in Brazil at a time of heightened political tension arising from, among other things, a campaign – which kicked off in 1947 – to assert state control over the country's petroleum resources (and which would culminate with the creation of Petrobrás in 1953). During a stay in Brazil lasting nearly ten years – and which encompassed the final disintegration of Getúlio Vargas' political project in 1954 – Hendryx witnessed at first hand the problems and contradictions inherent to development policies predicated on the subordination of urgent national priorities (notably addressing the poverty in which the bulk of Latin American populations lived) to the bottom line of foreign investors. He also noted that a principle of government that he considered 'quite beyond substantial question and ... indeed so accepted throughout the civilized world as to be beyond necessity for repetition', was nevertheless stridently denounced by the paragons of this civilized world whenever underdeveloped countries such as Brazil (or post-revolutionary Mexico) dared invoke it.

Hendryx would later summarize this principle of government thus:

any sovereign nation has both the right and the obligation - in good faith and necessarily incident to its duties to its citizens - 1) to alter its legislation, 2) to alter its contracts, and 3) to alter its treaties, if and when because of relevantly changed circumstances and for substantial reasons these enactments and documents no longer serve the important needs of those citizens but on the contrary have come to operate against those needs ... [because n]o sovereign nation can waive or barter away the means of effectuating its duties to its people

(League of Arab States, 1960, p. 77)

It is not possible to ascertain whether this lapidary formulation might already have been embryonically present in Hendryx's mind when he left Brazil. But Hendryx had certainly fleshed it out in full by the time he called a day on his Jersey career, after a relatively brief stint in Venezuela.

Hendryx's views on 'a sovereign nation's legal ability to make and abide by a petroleum concession contract' owed much to the arguments that key Venezuelan policy makers - notably Manuel Egaña, the first (and, to this day, most talented) holder of the petroleum ministerial portfolio in the country - had put forward in relation to the sovereign management of petroleum resources (Egaña, 1947). But, far more importantly, his views reflected facts on the ground that he had witnessed at first hand in Venezuela, a country where these policy arguments had been put into practice with resounding success.

When Hendryx arrived in Venezuela, the country was still ruled by an authoritarian dictatorship (not unlike the one that took over post-Vargas Brazil). Nevertheless, in terms of overall direction of travel, the 'feel' that prosperous Venezuela gave off contrasted strongly with Brazil's maelstrom of violence. In Hendryx's eyes, this contrast was proof positive of the advantages attendant to a sovereign which refused 'to by contract bind itself and hence its people against the subsequently altered substantial interests of the people' (League of Arab States, 1960, p. 79). Such a refusal, Hendryx would insist time and time again, was not tantamount to a governmental license to break, unilaterally and without consequences or compensation, any and all solemn contracts ratified by a country's highest authorities. Rather, it simply signaled a government's commitment to the fundamental tenet that '[i]n any future balancing of the financial interests of producing companies with the financial, economic and social interests of the host producing nations, the scales must no longer indicate that the former outweigh the latter' (League of Arab States, 1960, p. 77).

As Hendryx saw matters, in discharging their basic duty of serving the interests of their citizens, states could very well find themselves having to take 'action contravening existing contract provisions ... either by legislative or administrative act', a prerogative well established in international law, and the municipal administrative laws of the home countries of the oil majors. For good measure, Hendryx stressed that this duty to act did not, and could not, exist in isolation:

if, for instance, it appears that other nations similarly situated have obtained for their citizens much greater benefits, a contract alteration may become, in principle, mandatory ... [A]n oil producing nation by the law of civilized nations may clearly, in a proper case, modify or eliminate provisions of an existing petroleum concession which have become substantially contrary to the best interests of its citizens.

(Platt's Oilgram News, 1959)

Hendryx had no doubt as to where he thought that oil-producing countries of the Middle East needed to look for guidance in terms of the management of their relationships with their concessionaries:

Venezuela, by proper sovereign legislative activity has increased through general taxation that nation's share in the profits of oil producers within its boundaries ... [an increase] met with bitter comment and with what opposition, including charges of ill-faith, could be mustered against it.

(Platt's Oilgram News, 1959)

The legislation that Hendryx was referring to was the epochal Petroleum Reform of 1943, by means of which the government of President Medina Angarita had extended the concessions then in force (and imminently due for expiry) by forty years and waived all claims related to their myriad dubious aspects, in exchange for the concessionaires' acknowledgment, *without any reservation*, of the sovereign prerogative right of the Venezuelan state to levy income taxes on their activities (Mommer, 2002, pp. 113–115).

The break with Creole

Hendryx's opinion that the 1943 Hydrocarbons Reform was the bedrock upon which Venezuela's economic prosperity rested was a widely shared one, not least by observers and officers from other oil exporters. Ashraf Lutfi (secretary general of OPEC, 1965/6) characterized Venezuelan institutional arrangements in the following terms:

In my references to OPEC's problems about the need for financial adjustments and revision of the abnormal legal provisions in oil agreements, I should, of course, have made exception for Venezuela ... [where] [m]any of the problems discussed ... have been to a large extent solved ... The oil operations, foreign and local alike, are subject to the law of the land and pay whatever taxes the government sees fit to impose generally on all sectors without discrimination ... In general therefore, the Venezuelan Government is free from any fetters on its authority to formulate the oil policy of the nation

(Lutfi, 1968, p. 72)

In view of Hendryx's stated opinions about the 1943 Reform (and in light of the subsequent turn of events), it is safe to assume that Creole's newly minted legal counsel would have been dismayed when, upon arriving in Venezuela, he found that his assignment would involve assisting his employer to implement a legal strategy which sought to undermine the foundations of the Venezuelan economic success story, by (to paraphrase Lutfi) re-fettering the government's authority to formulate the oil policy of the nation regarding existing oil exploitation arrangements.

In a nutshell, what Creole – in cahoots with Shell de Venezuela – wanted to do was negate the substance of the 1943 Petroleum Reform. This was to be achieved by retrospectively (and through subterfuge) investing the Fifty-Fifty principle with a contractual character, in the process repudiating these concessionaires' unreserved and unconditional acknowledgement of the sovereign powers of taxation of the Venezuelan government.⁵ The legal gymnastics whereby this objective was to be attained were convoluted in the extreme (Mommer, 2002, pp. 116–117). They involved, *inter alia*, characterizing the payment of certain 'back taxes for which no legal obligation at all existed' (and which the companies had *volunteered* to liquidate) as a *settlement* that, from that point on, 'established the even division of petroleum profits as a basic principle in Venezuela' (Wayne et al., 1955, p. 30).⁶ Such a settlement had been necessary because, as Creole itself had to accept that 'the fifty-fifty principle was not fully spelled out in the 1943 law'⁷ (Wayne et al., 1955, p. 29).⁸

The resulting arrangement was one of 'satisfying simplicity':

Creole's own tax experts ... cooperated in drafting legislation requiring them to split the profit difference with the government in any years in which normal taxes and royalties leave the companies with a bigger take than the tax collector ... it is perfectly true that the law's operation, while assuring the government of at least 50 per cent in prosperous times, gives no assurance that the companies in bad times will get their 50 per cent. In general, however, the oil industry – and Creole most emphatically – *does not worry so much about the effects of the fifty-fifty tax as it does about future politicians who may have sixty-forty or even seventy-thirty ideas.*

(Fortune, 1949, p. 178, italics ours)

Unfortunately, in political terms, in satisfying simplicity was tantamount to the oil majors embarking on a path of sabotage and confrontation, predicated on reneging their previous commitments *vis-à-vis* the Venezuelan government.

Hendryx Cairo speech leaves no doubt as to what he thought about the political stance that Creole assumed regarding the 1943 Hydrocarbons Reform. Needless to say, harboring grave reservations about Creole's legal strategy was not something that would have endeared Hendryx to his superiors, or enhanced his career prospects. Fortunately for Hendryx, his path was about to intersect –somewhat fortuitously – with that of another fervent admirer of Venezuela's institutional arrangements for the petroleum industry: Abdullah Tariki.

Hendryx and Tariki cross paths ... thanks to Creole

Tariki and Hendryx met for the first time in Caracas, on the occasion of the former's second trip to Venezuela in 1956. The timing of this trip suggests that its prime objective was to extend an invitation to Venezuelan officials to attend the First Arab Petroleum Congress (supposed to take place in November of that year but, in the event, postponed on account of the Suez crisis). As part of this visit, Tariki took time to visit Creole and talk to some of its officers, among whose number was the company's recently appointed legal counsel. Hendryx and Tariki clearly hit it off well, so much so that, while Hendryx still in post in Caracas, a preliminary agreement was struck regarding the terms pursuant to which he would be retained as an advisor by the Directorate of Petroleum.⁹

Given the reasons that prompted Hendryx to seek to end his association with Creole and its underhanded plans, it is ironic that Tariki and Hendryx only met thanks to the Saudi's abiding admiration for Creole, conceived during his first trip to Venezuela in 1951. Tariki recounted in the following terms how that trip had come about:

In reading the oil trade literature, it came to my attention that a national petroleum congress was to convene in Venezuela in August 1951. I decided to invite myself to the congress, and for that purpose I contacted the executives of Aramco to assist me in obtaining a visa. There were no diplomatic relations between Saudi Arabia and Venezuela at the time, and the Saudi government had failed to invite the Venezuelan delegation which visited the area in 1948 [*sic*]. ... The late Cy Hardy [who was to become President of Aramco in 1958] succeeded in obtaining a visa for me from the Venezuelan Embassy in Washington, and I was able to attend

(*Tariki, 1983, p. 29*)¹⁰

According to this account, Tariki undertook the trip as a frolic of his own, but there are grounds to doubt this. For one thing, the mention of the 1949 tour of the Middle East by a Venezuelan delegation (and its failure to visit Saudi Arabia) suggests that, in 1951, Tariki sought to establish a political connection that had been frustrated two years before (because the holder of the Saudi concession, the Arabian American Oil Company, 'Aramco',¹¹ had convinced King Abdul Aziz that visas not be extended to the members of that delegation) (Rivas, 1999, p 94). For another, Venezuelan newspapers reported Tariki's attendance to the Congress and gave extensive information on his background, a reception not accorded to just anybody who happened to turn up in Venezuela on a whim.¹²

Tariki's first trip to Venezuela was a fruitful one. He made the acquaintance of Manuel Egaña, who would be instrumental in organizing the attendance of a Venezuelan contingent to the Cairo congress (where Tariki and Juan Pablo Pérez Alfonzo were to be introduced to one another by Egaña himself). Tariki was also able 'to visit the oil fields in the eastern and western parts of the country ... [and] compare the treatment workers received in Venezuela with that in Saudi Arabia' (Tariki, 1983, pp. 27–28). In the course of this tour, Tariki witnessed at first hand labor and human resource practices

that appeared enlightened by the segregationist and inhumane standards prevalent at the Aramco camps at the time (Vitalis, 2009). It was because of this that Tariki came to regard Creole ‘as the model of a model oil company’, which in turn accounts for why he was visiting Creole’s headquarters in 1956.¹³

Impact of the Cairo speech

The topic of Hendryx’s Cairo speech had not been circulated to delegates beforehand, but a confidential dossier put together by Aramco reported that the session ‘attracted such a large audience that the room set aside for it proved too small. The session was transferred ... [to a room] where no public address system was available’ (First Arab Petroleum Congress, 1959, p. 47).¹⁴ As a result, ‘Hendryx could be heard by only a few of those present, which necessitated postponement of the discussion of Hendryx’s paper until the following morning, by which time the delegates and members had an opportunity to read his printed text’ (First Arab Petroleum Congress, 1959, p. 8).

The ensuing discussion saw Hendryx’s speech lambasted by delegates from the ranks of the oil companies and the Western governments, and even from the Arab contingent. Typical of the reception accorded to Hendryx was the intervention by Harley Stevens, legal counsel of Aminoil, who said the speech was as legally unsound as it was gratuitously inflammatory, and considered that its sole redeeming feature lay in the contribution it made ‘to dispel the stiffness that earlier surrounded the sessions of the Congress ... [thereby making] it easier ... to discuss other controversial items on the agenda’ (Middle East Journal, 1959, p. 276). The compilers of the Aramco dossier, aghast at the overall thrust of Hendryx’s speech, drew vestigial comfort from the fact that ‘[a]t the close of the discussion there was no applause for Mr. Hendryx’ (First Arab Petroleum Congress, 1959, p. 28).

Hendryx and Tariki were not surprised by the hostility that the Cairo speech elicited and were rather more worried by the perception that ‘the most effective rebuttals [to the arguments they advanced] came from Arab delegates’, not so much in the form of direct responses but, rather, by way of general statements about sanctity of contract, reliance on international arbitration clauses and so on (The World Today, 1959, p. 248). Acting on these concerns, in late October 1959 they convened a meeting of the Arab League Petroleum Committee, in Jeddah, to discuss Hendryx’s ‘Thoughts of New Petroleum Tax Legislation for the Arab Producing Nations’.¹⁵

Hendryx explained to the Jeddah gathering that most ‘oil producers of the world ... taxed petroleum producers ... upon a basis presumably dividing more or less equally the net profits of the producer’s operations’ (the famous 50/50 profit split). However, such a division of the spoils had become increasingly untenable in the Middle East because, ‘[w]hile risks continued to exist with respect to the capital of the producing ventures, they were not the original risks either in quantity or in quality’ since the bountifulness of resource discoveries had been such that ‘the producing ventures were recovering their invested monies, and in many instances had already recovered them, and while they continued to make large investments, they were reaping tremendous profits’. While Hendryx acknowledged that ‘at the time and under the circumstances of its adoption’, the 50/50 scheme had afforded a ‘new and valid basis’ to underpin ‘the harmony between host nations and their guest producing ventures’, he also pointed out that ‘the percentage figure which was involved had no significant legal or moral justification nor had it any sanctity [and, I] like all legislative enactments, permanence was not inherent in it’.

Now, the contractualization of the 50/50 arrangement seemed to invest it with just such permanence, but Hendryx let his audience know that, from his former employer Jersey down, ‘every international oil interest knows that the ‘50–50’ profit concept at least so far as major producing ... nations are concerned ... is now as extinct as the dodo’. For this reason, Hendryx concluded, ‘[i]t would seem proper that the Arab producing nations should increase their portion of the profits of petroleum producing ventures within their borders by income tax legislation’. The key question, in light of this political imperative,

concerned what the concessionaires (and their home governments) would do.¹⁶ Would they, as Hendryx '[d]elude themselves into thinking there won't be changes'? (First Arab Petroleum Congress, 1959, p. 56). Or, alternatively, would they be ready to display the kind of forward-looking vision that had made the 1943 Venezuelan petroleum reform such a success?¹⁷

These questions were at the core of Hendryx's address to the Second Arab Oil Congress (held in Beirut towards the end of October 1960), entitled 'The Same World'. The Middle East Economic Survey (MEES) summed up Hendryx's intervention as being a 'reiteration and amplification of the paper he delivered to ... [the] Cairo congress ... [albeit] both stronger and more specific'.¹⁸ Hendryx brought this speech to a close with the proposal that companies abandon the defense *à outrance* of the absolute inviolability of concessions granted in colonial or semi-colonial political contexts, and instead embrace 'a new and entirely bilateral concept of the relationship between (the producing nations) and the producing companies' (League of Arab States, 1960, p. 80).

Once again, Hendryx's intervention prompted the ire of delegates not present on behalf of governments of oil-producing countries. For example, a New York investment banker stressed that 'there were many places where capital could go,' and that 'the only way underdeveloped countries could obtain the investment capital they needed from abroad, was by living up scrupulously to their contracts,' which should never be 'abrogated at any time under any circumstances unilaterally' (Hendryx's curt reply to this enduringly popular formula was that, 'if in order to get this kind of capital the nation must barter away its sovereignty, he would suggest that it refuse the capital').¹⁹ The Aramco representative decried Hendryx's proposition as 'unsound law, whether from the standpoint of Islamic law, American law, English law or international law', and, for good measure, indignantly suggested that it was an 'unsound philosophy not conducive to the best interests of either the state or the concessionaire'.²⁰ Tellingly, though, fewer Arab professionals shared such damning views. For instance, Samir Shamma, former legal advisor to the Saudi Directorate of Petroleum, reminded the Aramco representative that, while 'no violation of contract in Saudi Arabia' had occurred, there were 'many important issues between Aramco and the government ... still pending because attempts to solve them by mutual agreement had been unfruitful'.²¹ And a perceptive and knowledgeable observer like George Stocking reported that his 'familiarity with the oil industry ... of more than half a century ... as an employee, student, author and government regulator' had left him completely 'unprepared for the hostility, bitterness and suspicions manifested by congress spokesmen for the host countries' (mirrored by equally strong feelings 'of insecurity, uncertainty and resentment manifested by representatives of the oil industry') (Stocking, 1970).

It is easy to see why the contemporary account of the debate on Hendryx's proposals presented in MEES characterized it as being 'heated and, at times, acrimonious'.²² That may also explain why, in bringing the Beirut proceedings to a close, Tariki sought to strike a more harmonious note:

speaking on behalf of Mr. Hendryx, I can say that he is not suggesting dumping the contracts into the sea. What he is suggesting is the creation of an atmosphere of understanding between the companies and the governments. Even if the governments possessed such rights they would not make use of them except in cases of national necessity.²³

At the Third Arab Oil Congress, held in Alexandria in October 1961, Hendryx duly took his cue from Tariki and delivered a paper called 'Tomorrow's Petroleum Concession Agreement', where he suggested that even though the concession agreements were riddled with infelicities that needed to be addressed and solved bilaterally, these negative aspects were partly a consequence of the ignorance and negligence of host governments and not entirely due to rapaciousness on the part of the oil companies. The tone of Hendryx's speech prompted the BP representative at the congress to state that, whereas 'on two previous congresses he had crossed swords with Mr. Hendryx ... on this

occasion his paper seems so useful and interesting ... that I want to express my opinion with my sword remaining in its sheath'.²⁴ Hendryx's conciliatory stance was to bear no fruit, however, because Tariki's political position had weakened significantly by the time of the Alexandria Congress and, in March 1962, a flare-up in a long-running dynastic tug of war between King Saud, Crown Prince (later King) Faisal and Prince Talal saw Tariki sacked, to be succeeded by the more conservative and emollient Ahmed Zaki Yamani. Hendryx's contract with the Ministry was not renewed upon its expiry.

End of the road: the OPEC revolution

Hendryx's exit from the Saudi scene marked the end of the road for the idea that the major concession agreements could be redrafted by the parties to them, in a spirit of cooperation. The oil companies opted instead for holding the line à *outrance*, and informed those who had proven receptive to Hendryx's message that, in fact, the oil-exporting governments had nothing to complain about. H. W. Page of Standard of New Jersey²⁵ put the matter thus:

I doubt if it is generally realized that oil concessions in the Middle East are already nationalized. That is, all the facilities are either the existing property of the Government, or a government entity, as in Iran, or become the sole property of the government under terms of the contract after termination. Rights are then granted for a period of years in return for the performance of certain obligations ... If a country were to ... prevent a company from exercising its rights under such a contract it is ... nothing more or less than the abrogation of a solemn contract which is part of the law of the land.

(Page, 1960, p. 625)

Such legal acrobatics could not, and did not, succeed in undoing the damage that Hendryx had wrought on the aura of the oil concessions as 'something inherently sacred in origin and operation, separate and distinct in law from other commercial agreements ... to be governed by special and separate legal rules' (League of Arab States, 1960, p 77). Furthermore, throughout the 1960s, the resonance of Hendryx's modest proposal was amplified by a rapidly tightening world petroleum market and booming petroleum demand. These objective conditions doomed the rear-guard efforts by the companies to maintain the status quo because, for the price of a subscription to *Platt's*, governments in the Middle East and North Africa could see resource owners elsewhere (notably the USA) realizing much higher relative takes, in fields less bountiful by orders of magnitude than theirs. Thus, a re-balancing of the economic outcomes of the Middle East concessions was inevitable and duly happened, with effective government takes in extant concessions climbing far beyond the basic 50/50 profit split.

Crucially though, this re-balancing took place in an adversarial, rather than a collaborative, context. Since lip service had to continue to be paid to the purported inviolability of the concession terms, their readjustment could only be secured via the circuitous form of tense and protracted collective negotiations centered on tax reference prices and royalty expensing, predicated on the fiction that the object of the exercise was to determine *more accurate* ways to calculate the 50/50 split. Contractualization also meant that, as prices continued to rise, further adjustments could only be secured by way of governments becoming shareholders in the concessions themselves, a route which ultimately led to their full nationalization. This was a radical outcome which, at the start of the process, no relevant actor (especially the OPEC governments) had visualized – much less desired – and which conceivably could have been avoided altogether had the companies been amenable from the start to deal with these governments not as contractual counterparts but as sovereigns, along the lines that Hendryx had proposed.

Hendryx after Saudi Arabia

King Faisal's animus against Tariki crimped the latter's employment possibilities in Arab countries of a conservative bent but being disowned by the Saudis did no comparable harm to Hendryx. Instead, Hendryx quickly found himself advising other Arab governments, and setting the stage for a much more hands-on governmental approach to the petroleum concessions of Libya, a country also ruled at the time by a conservative monarchy.²⁶

Libya would end up playing a starring role in the OPEC Revolution,²⁷ and conventional wisdom explains this prominence in terms of an abrupt about-face in Libyan oil policy brought about by Colonel Qaddafi's assumption of power in 1969. However, this version of history is at radical variance with the facts, as Ian Skeet notes:

[i]t would be misleading to suggest, as the Revolutionary Government subsequently did, that previous governments had been passive; in fact, they had shown considerable toughness ... with the application of royalty expensing and ... with their attitude to posted price and their introduction of new legislation. It is true, however that they preferred to negotiate rather than win their case simply by threats

(Skeet, 1988, p. 55)

The toughness that Skeet highlights has been attributed to the presence of a future OPEC secretary general (Nadim Pachachi) among the advisors to King Indris (Kubbah, 1964, p. 78). However, it is somebody else's fingerprints that are all over a crucial document outlining both the reasons for Libya's unhappiness with its existing petroleum arrangements as well as the legislative program crafted in response. This document, issued by '[t]wo public relations firms retained by the Libyan Government in London ... and New York', took the form of 'a lengthy background memorandum explaining Libya's reasons for the issue of its new oil law ... written by a special oil adviser (*sic*) to the Libyan Government'.²⁸

This unnamed special advisor was likely Frank Hendryx (making the memorandum the last of his major writings to be widely published and circulated). The attribution of this memorandum to Hendryx can be supported not only on stylistic grounds but also, and more pertinently, because its contents amount to a reasoned practical application of Hendryx's theses to the case of Libya, aimed at bringing the fiscal arrangements of this newcomer to the world petroleum market into broad alignment with those of other OPEC countries (Mughraby, 1966; Catton, 1967). The adoption of this policy objective by the conservative government of Libya 'was a situation that required either application of the Law of Changing Circumstances or a revolution. It got the latter' (Skeet, 1988, p. 54). And it got the latter in the form of Col. Qaddafi, thanks once again to the intransigence and short-sightedness of the absolutists of contract in the ranks of the oil companies and the governments of their home countries.

Hendryx continued advising the Libyan revolutionary government, and he even moved to Tripoli for a couple of years at the start of Qaddafi's long period in power.²⁹ In 1973, Hendryx decided to stop advising Libya, whereupon he decamped to what would turn out to be his last big gig before retirement: Norway.³⁰ There, Hendryx's work as an advisor seems to have been completely anonymous, and any remaining trace of it or memory of him is either lost or confined to inaccessible archives.³¹

Postscript: Hendryx today

None of the statements in Hendryx's three major speeches would have looked out of place in the United Nations Resolution on Permanent Sovereignty over Natural Resources, which was adopted in 1962 and before long became a generally accepted principle of international law.³² Thus, one might have perhaps

expected to see Hendryx's profile becoming increasingly prominent even after he stopped working for Saudi Arabia. In fact, the exact opposite happened.

In the immediate aftermath of the Cairo conference, the major oil companies agreed that it was necessary to 'prepare for the discussions at the next Congress, particularly on highly controversial subjects such as Hendryx's thesis' (First Arab Petroleum Congress, 1959). Some companies considered that it was necessary to go on the offensive. Others thought that it was silence that was called for, to ensure that – in the words that an Arab officer of one of the major oil companies used in a secret report submitted to the UK Foreign Office – '[t]his infamous paper may not see light again'.³³

In hindsight, it was the latter counsel that prevailed, as reflected by the fact that the Cairo speech was only ever reproduced in an issue of *Platt's Oilgram News* and not subsequently reprinted in its entirety and original form anywhere else. The texts of Hendryx's second and third speeches, in turn, were summarized in *MEES*³⁴ but were never reproduced anywhere else, not even *Platt's*. And away from the sphere of the specialist trade journals, in academia and the press, a deafening silence descended upon Hendryx. The Cairo speech met with an almost instantaneous rebuttal in the *Fordham Law Review*, but from that point on Hendryx's pronouncements tended to disappear from view without creating so much as a ripple (Kissan and Leach, 1960). A mere ten years after Cairo, in a review article on the state of play in international arbitration on oil matters, an accomplished legal scholar like Professor Arghyrios Fatouros confessed that he had been 'unable to locate the, by now legendary, papers by Mr. Frank Hendryx, submitted to the First and Second Arab Petroleum Congresses, 1959 and 1960', and betrayed no awareness about the existence (let alone the contents) of Hendryx's third speech in Alexandria (Fatouros, 1968, p. 969). This shows the rapidity with which Hendryx faded from public consciousness. Indeed, there is barely a mention of Hendryx in the tidal wave of literature on all aspects of petroleum policy that the era of the Oil Shocks produced.

It is not difficult to grasp why making sure that Hendryx's speeches never saw the light of day again would be in the political interests of both oil companies and consuming country governments. What is more difficult to visualize is why OPEC countries would suffer this to happen, considering that Hendryx's theses articulated their own political and economic interests so effectively.

Hendryx proved ready to pay a heavy price, courting opprobrium and worse, to cast his lot with policies and ideas devised and developed away from the traditional centers of power of the world. Building upon lessons learned in Venezuela, Hendryx made important contributions to the definition of OPEC's overall policy agenda for the 1960s, as well as to the design of early Saudi oil policy. Hendryx was no gun for hire, but neither did he come to hold his political positions on account of having 'gone native' (in the manner of, say, Harold St John Philby). Rather, Hendryx was a kindred spirit of Keynes, and shared the latter's natural inclination for 'arguments, which the most obtuse cannot ignore, against a policy of spreading and encouraging further the economic ruin of great countries' (Keynes, 1971, p. 187). Hendryx clearly thought that policies encouraging the ruin of lesser countries were also deplorable, which is why he refused to go along with Creole's plans to eviscerate Venezuela's 1943 Petroleum Reform.

In view of this, it is paradoxical that Hendryx should have been more thoroughly forgotten precisely by those whose interests he sought to advance. This paradox is symptomatic of why OPEC today is but a pale shadow of the organization that seemed to bestride world politics during the 1970s. Many are the factors that have contributed to OPEC's enfeeblement, of course, not least the various shooting wars which a number of its member countries have waged on one another, whether directly or by proxy. But among these factors, as Hendryx's descent into obscurity illustrates, is the manner in which OPEC member countries have tamely and uncritically allowed their collective and individual histories to be hijacked by their unconditional detractors, thereby denying themselves the chance of coming to a reasonable understanding of their objective position both *vis-à-vis* one another and the world economy at large.³⁵

Piecing together Frank Hendryx's checkered career would have been impossible without the help and suggestions of Dag Harald Claes, Giuliano Garavini, Einar Lie, Scott McLachlan, Ed Morse, Tyler Priest, Brigitte Wolek and, most especially, Mrs Betsy Perrier Hendryx.

Notes

- 1 The Saudi Ministry of Petroleum and Mineral Resources was created in 1960 to succeed the Directorate (with Tariki as first holder of the portfolio).
- 2 In June 1961, the *Cornell Alumni News* (1948, 50(17), p. 668) reported that Hendryx would be embarking on his second safari in two years. Hendryx held his *alma mater* in high regard and kept its alumni magazine abreast of his whereabouts through communications which are a key (and often sole) source of public information for much of his peripatetic career.
- 3 Some cases in which Hendryx was involved are: *Hendryx v. Atkins*, 79 F.2d 508 (5th Cir. 1935); *Kansas, O. & G. Ry. Co. v. Helvering*, 124 Fed. (2d) 460; *The Sharples Solvents Corporation v. Commissioner of Internal Revenue*, 45 B.T.A. 841 (B.T.A. 1941).
- 4 Personal communication from Mrs Betsy Perrier Hendryx.
- 5 The text of article 46 of the 1943 Law of Hydrocarbons contains no trace of conditionality: 'cessionaires shall pay all general taxes, of whatever kind, and shall also pay the legal charges, contributions, and dues for the services that may have rendered them'. Official Gazette, Venezuela, 13.03.1943, 31.
- 6 In Creole's view, 'voluntarily contributing a sum that equalized the government's income from Creole with the company's profits since 1946' meant that, 'although the fifty-fifty principle was not written into the law until 1948, it has been the effective basis of taxation for Creole since 1946' (Wayne et al., 1955, p. 29).
- 7 Personal communication from Mrs Betsy Perrier Hendryx.
- 8 That Creole saw this as a matter of regret represented quite the change from what the company had told *Fortune* in 1949; namely, that 'it did not accept the fifty-fifty principle at the time [i.e. 1943]' (*Fortune*, 1949, p. 178).
- 9 Hendryx's definitive retainer letter from the Directorate is one of a handful of personal papers of his to have survived.
- 10 Tariki's recollection is deficient in certain respects: the Venezuelan delegation toured the Middle East in 1949, and Pérez Alfonzo was not a part of it.
- 11 The shareholders of Aramco were as follows: Standard Oil of New Jersey (30%); Socony Vacuum (10%); Standard Oil of California (30%) and the Texas Company (30%).
- 12 Últimas Noticias, 9 September 1951.
- 13 Tariki's view of Creole was both romanticized and politically naive: '[Creole] is, above all, run out of Caracas. Ten of its 14 directors reside in Caracas. It is run in Venezuela, in the interests of Venezuela' (Jablonski, 1957, p. 22).
- 14 This document, marked 'strictly confidential', is a typescript collection of reports summarizing the Congress. Oddly enough, the Aramco dossier makes no mention of Hendryx's prior employment by Jersey.
- 15 The text of the Jeddah speech was reproduced in a letter from G. A. MacBain, UK Ministry of Power, to J. T. Fearnley of the Foreign Office, dated 25 November 1959 [FO371/141210].
- 16 All of the quotes in the preceding two paragraphs (except where noted) are drawn from the Jeddah speech.
- 17 The visionary acceptance of the 1943 reform was not down to the oil companies, which assumed a position of absolute intransigence similar to the one that had led them to disaster in Mexico five years before. However, they were forced into an agreement with the Venezuelan government by the Roosevelt administration.
- 18 *Middle East Economic Survey*, October 21, 1960, III, 50, p. 10.
- 19 *Middle East Economic Survey*, 21 October 1960, III, 50, pp. 11–12.
- 20 *Middle East Economic Survey*, 21 October, 1960, III, 50.
- 21 Shamma would later on become an advisor to the government of Kuwait. *Middle East Economic Survey*, 21 October 1960, III, p. 50.
- 22 *Middle East Economic Survey*, 21 October 1960, III, 50, p. 50.
- 23 *Middle East Economic Survey*, 21 October 1960, III, 50, p. 13.
- 24 *Middle East Economic Survey*, 27 October 1960, III, 51, p. 9.
- 25 Page was the Jersey representative in charge of negotiations on royalty expensing.
- 26 After the end of Hendryx's assignment in Saudi Arabia, the magazine published by students of the Cornell law faculty reported: 'Frank C. Hendryx writes a note to say "I am still alive and working in the Arab world in oil matters ..."'. *Cornell Law Forum* (1967–1968, p. 33).
- 27 Libya joined OPEC in 1962.
- 28 *Middle East Economic Survey*, 31 December 1965, IX, special supplement.

- 29 Personal communication from Mrs Betsy Perrier Hendryx
- 30 In May 1974, the *Cornell Alumni News* (1974, 76(10) p. 39) informed that Hendryx was ‘doing a special job in Norway— something about North Sea oil’ and that he ‘hope[d] to stay on a few months longer’.
- 31 There is no trace of Hendryx in either the archives of the Ministry of Petroleum, Statoil or The Norwegian Oil and Gas Archives.
- 32 General Assembly Resolution, 14.12.1962, 1803 (XVII).
- 33 Foreign Office. FO371/141209. 2B. 9 May 1959. Dispatch no. 1535/59 G from Political Agency, Doha, to Arabian Department, Foreign Office, 20 June 1959, enclosing a report by Mr H. M. El Khalidi, Shell Company of Qatar.
- 34 *Middle East Economic Survey*, 21 October 1960, III, 50, p. 51.
- 35 There is, for example, no mention of Hendryx in Yergin (1991).

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OPEC's struggle for international recognition (1960–1965)

How a denied seat agreement in Switzerland influenced the early development of OPEC

Fabian Trinkler

Introduction

This chapter deals with the struggle of OPEC in regard of its constitution and international recognition between 1960 and 1965.¹ OPEC – founded in 1960 – had established its first headquarters in Geneva a year later and was looking to consolidate its constitution by acquiring an official status – expressed through the before-mentioned seat agreement and diplomatic privileges for its agents – in the international hub of neutral Switzerland. This recognition was the precondition to gain access to the international committees affiliated with the growing organization of the United Nations (UN) such as the United Nations Economic and Social Council (ECOSOC) and the United Nations Conference on Trade and Development (UNCTAD). Participation in these bodies was intended to enhance the standing and the policies of the new organization as well as the countries behind it. Switzerland was still keen to perpetuate its reputation of neutrality and solidarity in the international framework of states – especially among the Western OECD countries – after the temporary discretization by the Allied powers after the Second World War over allegations of cooperation with the Nazi regime. Its reaction to the advances of the potentially disruptive idea brought forward by OPEC was therefore in line with that of other Western states from the OECD and ranged between cautious at best and dismissive at worst, ultimately causing the negotiations to fail. OPEC moved to Vienna in the beginning of 1965.

Three key aspects that shaped the early development of OPEC are especially important for the arguments made in this article. The first section will set the context and sub-sequentially explore the strategy of OPEC to break into the international committees, especially bodies close to the UN. Acquiring an official status – expressed through a seat agreement in a state of good standing – was a vital precondition for this endeavor. This point is illustrated by the success of membership in the international bodies shortly after OPEC changed its headquarter to Vienna in 1965. Section two sheds light on how the host countries of the so-called ‘Seven Sisters’ capitalized on the informal status of OPEC by employing a stance of neutral non-recognition in order to hamper the impact of the newly constituted organization. The third section dives into the question of what motivated Switzerland to deny the seat agreement in the first place. A comparison with other international organizations that received a seat agreement during a similar time

frame points to the political dimension of the Swiss considerations when rejecting OPEC. The conclusion will point to unresolved issues that still await clarification by further research. The argumentation is to a large extent based on an extensive review of source materials from the Swiss Federal Archives in Berne (BAR) and a collection of source material published by Anita Burdett that originates from the British administration.²

The importance of international recognition

The foundation of OPEC was to a large extent an expression of self-determination by a group of resource-rich Third World countries and an act of opposition to the unilateral domination of the cartel of the Seven Sisters. The wave of decolonization after World War II resulted in the emergence of increasingly nationalistic agendas – in the Middle East perpetuated through a movement commonly described as Nasserism – and a growing aversion to the political predominance of the former colonial powers of Western Europe. One pivotal goal within this development was to take the control over domestic natural resources – including petroleum, which by the end of the 1950s had become the key energy source globally. This claim was in strong discrepancy to the oligopolistic market structure of the Seven Sisters' cartel that controlled the flow rate and the prices for crude oil in the markets outside the US and the Soviet Union at will (Maugeri, 2006, pp. 63–103). The underlying concessions that regulated the oil extraction rights were rooted in the colonial past, when European and American entrepreneurs secured long-lasting concessions in virtually all the most productive oil regions of the world from Venezuela to Indonesia. These concessions remained largely intact even after the political independence of the oil-producing countries, while the international oil companies often constituted a state within the state and unilaterally determined the conditions of oil expropriation. This rigid regime was reinforced by two main factors. First, the economic growth of the developed countries was reliant on cheap energy imports and the Seven Sisters' companies were directly backed by their home countries (sometimes via direct investments or shares as in the case of British Petroleum). Second, they were very well organized in coordinating their policies towards the producer countries. The coup d'état in Iran (1953) against Mohammed Mossadegh, who nationalized oil production, and the reinstatement of the Shah with the help of the British and American secret services proved the determination of the West to defend this framework (Skeet, 1988, pp. 1–14; Yergin, 1991, pp. 518–543; Trinkler 2015, pp. 19–23).

The governments of the producer countries themselves were only united by a common rejection of the existing situation and by the intention to benefit to a larger extent from the resources extracted from their territory. However, they disagreed heavily on the strategy on how to achieve this goal and mostly followed their own agendas and interests. Especially the approaches of Iran and Venezuela could not be more different in this regard. The Shah – reinstated by the American and British aid in 1954 – was predominantly concerned with keeping in good favor and was ready to increase the promotional volume for low prices. Venezuela, on the other hand, was steadily losing market shares and was therefore looking to coordinate and lower export quantities and thereby forcibly raise the price. The rest of the later founding countries of OPEC stood somewhere in between these extreme views and occasionally went back and forth between different strategies. It is not surprising, that it was relatively easy for the well-coordinated Seven Sisters' cartel to enforce the oil prices in individual negotiations towards the separate countries. Their negotiation partners were often utterly uncoordinated in their policies against the Seven Sisters, divided by political and religious (Shi'i, Persian Iran vs. the Sunni Arabian states of the Middle East) diverges and on top of that frequently internally unstable – for different positions of the member countries and their respective interests, see Trinkler (2015, pp. 25–26) and Skeet (1988, pp. 15–34).

The idea to form an organization to coordinate and promote the oil policies of all the member states on the international stage was transformed into OPEC in the aftermath of substantial – and once more unilateral – price reductions for crude oil from the Middle East by the Seven Sisters in 1959. The objective of

the newly formed OPEC was to pool the interests and the negotiation weight of the various oil-producer countries and to strengthen the coordination of the policies of the member states towards the oil companies. One major channel in order to achieve this ambitious goal was the ability to gain observatory status in multilateral bodies, preferably influential ones within the UN system or the oil committee of the Organisation for Economic Coordination and Development (OECD). The main precondition to perform these activities was the recognition of the organization by a host state through the granting of a seat agreement and the accompanying diplomatic privileges for its agents. This was perceived as a seal of legitimacy within the community of sovereign states and was a potential door opener to various multilateral committees.

The chosen location was neutral Switzerland, where the city of Geneva presented an ideal stage for this endeavor. Geneva had already acquired an international profile by hosting the headquarter of the League of Nations after World War I and evolved into one of the main international hubs for countless international institutions after World War II. Most importantly, one of the two main quarters of the UN permanently settled down in the city. Its large community of diplomats and government representatives promised significant network and lobby opportunities. Moreover, receiving a seat agreement in Geneva would enable OPEC to be recognized as an international organization in its own right. This, in turn, was a step toward forcing the oil companies to acknowledge OPEC as a meaningful entity and to open direct negotiations with it. But the precondition was being recognized by a sovereign country from the West. This recognition was commonly expressed by allowing the organization in question to conduct a seat agreement within the territory and to grant its agent special diplomatic privileges.

After moving into a building in at Rue du Rhône 31 in central Geneva in 1960, Fuad Rouhani – the first secretary general of OPEC – expected the request for a seat agreement to be conducted swiftly. A retrospective statement from Rouhani’s book on OPEC illustrates this optimistic expectation:

It [OPEC] pointed out that the Swiss Confederation had clearly recognized the existence of a customary rule concerning the grant of certain privileges and immunities of an international organization whose juridical personality under the law of nations had been recognized and which had been admitted to establish itself on Swiss territory.

(Trinkler, 2015, p. 45 and Rouhani, 1971, p. 134)³

As will be shown in section 5, the Swiss refused to grant a seat agreement despite tolerating the setup of an OPEC headquarter in Geneva. Therefore, OPEC was prevented from being officially recognized as a multilateral actor in its own right. OPEC ended up being on the awkward position of having a physical existence without any formal international status. In effect, this uneasy *modus vivendi* left the organization in a grey area of undefined standing. Rouhani’s approach was to justify the entitlement for a seat agreement on the basis of three arguments that clearly aimed at portraying OPEC as a legitimate, universal and uncommercial entity, not as a political pressure group or private commercial entity that could be described as a cartel:

- 1 All of the members are nation states and not administrative bodies, which makes OPEC an inter-governmental body comparable to similar institutions.
- 2 The nature of OPEC is not exclusive or exclusionary as it is – without exception – open to every country that produces crude oil.
- 3 OPEC undertakes no commercial activities but is solely an instrument for coordination and information exchange among the oil-producing countries.

(Trinkler, 2015, p. 35; BAR Dossier E2003A #1974/52#18)*

If Rouhani was to obtain a seat agreement on the argumentation laid out above, Switzerland would recognize the sought-after universal purpose of the organization and – from a legal point of view – equate

OPEC to any institution with a seat agreement in Switzerland. This in turn would legitimize OPEC internationally and strongly reinforce its case when asking for membership in supranational bodies or when attempting to participate in international activities. On the other hand, the denial of the recognition allowed the Western OECD countries to treat OPEC as somewhat officious. We will see further down how exactly this semi-official status was being used by OPEC's adversaries.

The importance of the Swiss decision in this process became apparent when OPEC realized that Switzerland was not going to budge on the issue and decided to change location. After a last fruitless attempt to come to terms with the Swiss Federal Administration in 1964, OPEC decided to move to Vienna. The Austrian capital had a far less international profile than Geneva, but the Austrian government swiftly gave assurance of a seat agreement in the case of relocation. The connection to official recognition is best expressed by a note from the British administration to its embassy in Austria upon learning about the potential change of locations:

OPEC have been dissatisfied for some time with the refusal of the Swiss Government to accord the organization recognition, and its representative's diplomatic privileges. [...] However, the organisation is actively seeking recognition in the ECOSOC and other U.N. bodies, and the Secretariat may feel that recognition by the host government would strengthen this case elsewhere.

(Trinkler, 2015, p. 70; Dawn, 1973, p. 610; Burdett, 2004, vol. 3, p. 610)

The effect addressed in the statement was noticeable almost immediately, with OPEC breaking into the ECOSOC and UNCTAD within less than a year during 1965. The new status and associated legitimacy of OPEC over the next few years resulted in a) an elevation of its status within the framework of sovereign states and b) an internal consolidation of the still recent organization that facilitated OPEC's development in the coming years.

Thus, the symbolic recognition of OPEC by a host state was a vital precondition for progressing the policies of the new organization. The Swiss refusal of such privileges resulted in a partial blockage of OPEC's international activities and therefore the early development of OPEC in general. The dilemma for OPEC was only partially resolved by the move to Vienna in 1965 and the following admission into ECOSOC and UNCTAD. The next section will explore the dynamics of how the Swiss decision was situated within a strategy of non-recognition at the international level (Trinkler, 2015, pp. 6–74; Mansfield, 2013, pp. 169–268; Cleveland and Bunton, 2013, pp. 159–344; Rouhani, 1971; Skeet, 1988; Frei, 1983; Gälli, 1979; Kubbah, 1974; Terzian, 1985; Tibi, 1997; Yergin, 1991).

The Seven Sisters' response: a strategy of neutral non-recognition

Accomplished author Anita Burdett has published an extensive five-volume body of internal documents from the British administration that deals with issues around OPEC. A review of the documents provides insight into the strategy of opposition of Her Majesty's Government towards the early OPEC. In monthly meetings usually known as the 'Oil Tea Party', the British consulted with representatives from the American administration and the private oil industry, exchanged viewpoints and also aligned their position towards OPEC.⁴ The minutes of these meetings as well as other internal notes, protocols and summaries reveal not only the British stance on OPEC, but paint a clear picture of a coordinated strategy of the Western players in the oil industry (governments and private industry alike) in order to minimize the negotiating position and the impact of the newly founded player in the oil business.

OPEC was already perceived as a potentially disruptive threat one month after its formal constitution. The issue of how to encounter OPEC was for the first time extensively discussed in the Ministry of Power in the presence of US delegates on 29 September 1960:

But OPEC was now an established fact and had to be reckoned with as a potential menace to the interests of the oil companies and the consuming countries. If the Middle East and Venezuela began to coordinate their policies, it was far from clear what forces could be brought up to bear on them.

(Internal note of the Ministry of Power, 29 September 1960; Trinkler, 2015, p. 65; Burdett, 2004, vol. 2, p. 103)

In view of the sensitivity of the issue, the delegates also discussed a common attitude towards the new organization. It was agreed that any demands or claims by OPEC concerning prices should be categorically prevented in order not to create a dangerous precedent or encourage OPEC to place further demands. The best strategy for achieving this goal was a policy of neutral non-recognition, as the internal divisions of the member countries of OPEC was identified as its biggest weakness. The efforts to prevent a build-up of OPEC should be kept at a level that did not give the impression of open opposition. It was feared that showing open hostility would provoke an act of defiance and therefore be counter-productive, simply uniting the producer countries in their quest. By ignoring the organization it was hoped that OPEC would get bogged down in internal divisions and eventually bring the looming threat to an end itself:

We continue to regard OPEC as a potential threat both to the security of the supplies of the United Kingdom and the West and to the United Kingdom's financial earnings in oil. [...] Meanwhile, although it is not in our interest to appear to look with favour on the Organisation, it is equally important that we should not at this stage adopt a critical attitude which might help to give fresh impetus to the Organisation [...].

(Confidential dispatch of the Foreign Office to several British embassies, September 1960, Trinkler, 2015, p. 65, Burdett, 2004, vol. 2, p. 185)

This two-sided approach formed the cornerstone of the measures to contain the efforts of OPEC for the next several years and was pursued even after 1965. The best way to put the plan into practice was by not recognizing OPEC as a formal institution and side-stepping any sort of dialogue. The idea was to prevent any informal or formal contact with the organization and therefore deny it an opportunity to express its point of view. Arguably, this task was much easier to accomplish without the organization having a recognized international headquarters in Switzerland and therefore a formal status. This line of argument was presented when the private oil companies were included in the talks:

Sir R. Ayres (Ministry of Power, Anm. d. Aut.) asked whether the companies did not consider the OPEC standing machinery as dangerous. Mr. Loudon (Shell, Anm. d. Aut.) thought that an office in Geneva would be so and Mr. Wilkinson (Shell, Anm. d. Aut.) said that Shell was by no means complacent.

(Minute of an 'Oil Tea Party' on 22 November 1960; Trinkler 2015, p. 66; Burdett, 2004, vol. 2, p. 166).

How this strategy was handled in practice was demonstrated when OPEC started to ask for observatory status in several international bodies, starting in 1962 (UNCTAD/ECOSOC). Enquiries for participation in these bodies were successfully channeled into an informal exchange of views and any kind of formal acknowledgment was successfully diverted. A request for observatory status in the oil committee of the renowned OECD in 1963 stirred considerable fuss and triggered extensive diplomatic action in order to deny the advance.

At the Anglo-American oil talks in Washington in 1963 it was agreed that there was no alternative to the policy of neutrality and non-commitment towards OPEC. [...] It also involves the avoidance of

any dealings with OPEC, even if only indirect, which might tend to enhance its status or secure its recognition in international circles. To this end, it was agreed that the U.S Government and H.M.G. (Her Majesty's Government, Ann. d. Aut.) should ask the OECD not to have any dealings with OPEC, and this was done.

(Recorded in an internal overview 1965; Trinkler, 2015, p. 67; Burdett, 2004, vol. 3, p. 635)

This intervention was coordinated with the Dutch emissaries and accompanied by extensive lobbying within the OECD and with the secretary general directly. An abundance of documents reports the consultations between the different parties and the alignment of the positions. The efforts proved successful when the official request arrived in Mai 1963, as the secretary general did not grant any formal privileges to Rouhani and also worked out an informal compromise that left OPEC with zero influence, no codetermination at all and therefore no additional status.

In the same year, another approach by OPEC in its efforts to increase its visibility proved more fruitful. After extensive resistance from the private oil industry, Secretary General Rouhani was able to install himself as the chief negotiator for oil prices on behalf of all OPEC countries except Iraq.⁵ The scope of this development was not only the acknowledgment of OPEC itself as an organization capable of acting, it was also a trend reversal in the nature of the oil price negotiations. Previously, the well-organized Seven Sisters (who combined almost all the buying power in the independent oil market) had dictated the terms by individually bargaining with each producer country. Rouhani's move levelled the playing field by uniting the interests of the major oil exporters in the world. The danger for the private industry was obvious, and it is not surprising that this issue brought about considerable dissent between the Sisters themselves. BP and Gulf Oil in particular objected to Mr Rouhani as negotiator for all OPEC countries, but ultimately to no avail⁶:

After this move the international oil companies could no longer affect to ignore the existence of Mr. Rouhani and his organization; [...] it was agreed that Mr. Rouhani would have to be accepted as the concessionary countries' negotiator.

(Protocol of the British Foreign Office from 6 Sept. 1963; Burdett, 2004, vol. 2, pp. 787–788)

After this success, the matter of international status subsided for a few years, only to resurface with more virulence after OPEC obtained the seat agreement in Vienna in 1965. As the sources quoted from Burdett have demonstrated, OPEC's attempts to receive observatory status in ECOSOC, UNCTAD or the OECD were dismissed at an early stage because the organization remained semi-official until the move to Vienna in 1965. The countries at odds with OPEC within these councils were always able to and did refer to the informal state of the organization in order to prevent a dialogue. This strategy was also deployed after 1965 but, as shown in chapter 2, with considerably less success.

The logical follow-up question is to ask what motivated Switzerland to show OPEC the cold shoulder – and whether its reasons were connected to the neutral non-recognition policy of Great Britain, the US and the associated international oil companies. Answers to this set of questions is buried in another collection of sources and will be explored in the next section. Why did Berne tolerate a physical establishment of OPEC in Geneva but subsequently deny official recognition? (Jonkers et al., 2007a; Jonkers et al., 2007b; Martens and Schulze, 2012; Sampson, 1975; Turner, 1978).

Self-interest: why Switzerland rejected OPEC

The federal archives in Berne hold an extensive body of correspondence documents concerning the negotiations of the federal administration with OPEC between 1960 and 1965. This section will map out

the motives behind Switzerland's behavior in the matter (tolerance of physical establishment but refusal of seat agreement) and emphasize the political dimension of the Swiss rejection of the seat agreement.

Switzerland was already pursuing the developments around the formation of OPEC even before the first semi-official contact between a board member of the National Iranian Oil Consortium (NIOC) and a delegate of the Swiss embassy in Iran took place in the autumn of 1960. Early sources show that the responsible Office of International Organizations (OIO / Abteilung für Internationale Organisationen)⁷ already viewed an institution like OPEC as a possible threat to the existing order in the oil markets. OPEC was seen as a predominantly Arabian pressure group and a political vehicle to further the interest of the producing countries. Consequently, the nature of the response was already shaped when OPEC's request of a headquarter and diplomatic privileges in Geneva became concrete:

The underlying conflicts of interests may only be economical in nature and do not constitute a legal reason for a refusal: however, the well-known political contradictions have to be taken into consideration behind the scenes.

(Internal document of the OIO from 27 October and 5 November 1960; Trinkler, 2015, p. 32; BAR, Dossier E2003A#1974/52 #18)*

The statement shows that while the Swiss had no interest in hosting an OPEC headquarters, the OIO was under the impression that a physical establishment was not preventable by the federal institutions according to customary law. The Swiss tried to discourage the representatives of OPEC from setting up camp in Geneva by signalling their lack of interest but were unable to formulate a clear prohibition.⁸ A meeting between federal representatives and the Iraqi Petroleum minister during his visit of Geneva in February 1961 was intentionally denied (Internal note covering a message to the Canton of Geneva; Trinkler, 2015, p. 33; BAR, dossier E2003A#1974/52#18*). The answer to the first official request for diplomatic privileges by Rouhani a month later described the prospects of success for a seat agreement as very improbable.

However, while the Swiss were still internally evaluating the strategy towards the growing possibility of OPEC settling down in Switzerland, Rouhani – without having received a clear interdiction – put wood behind the arrow: after obtaining the permission of the Canton of Geneva to open an office, he swiftly leased an apartment at Rue du Rhône 31. The federal administration was taken by surprise as the OIO was not aware of these developments when Rouhani communicated the news in May 1961 (for some reason, the information was not passed from the Canton of Geneva to the OIO). From that point on, OPEC was an established fact, and the Swiss involuntarily found themselves in the role of judging over the formal recognition – and therefore to a certain extent the legitimization – of OPEC in international politics (Trinkler, 2015, pp. 34–36).

Dr Carl Burckhardt – who headed the OIO office at the time – met with Rouhani on 14 June 1961 and subsequently initiated a wave of consultations within the Swiss federal administrations in order to evaluate the granting of diplomatic privileges. The first concern was the customary law normally appropriated by the Swiss government for a case presented by OPEC. The assessment of the legal service clearly favored OPEC case, which was already emphasized by Rouhani's statement on page 5 of this chapter. The argument goes as follows: Switzerland could have prevented the establishment of OPEC in the presence of a due cause (it is questionable whether such a cause existed) but failed to do so by tolerating the opening of the office in Geneva (which was a misunderstanding between the cantonal and federal levels). Furthermore, the report credited OPEC as worthy of the status of international organization from a legal point of view. This should have necessarily entailed the usual diplomatic privileges for the organization and its agents.

The next step of the OIO was extremely relevant in shaping future negotiations. Based on the concern of the potential political reverberations of OPEC, Dr Burckhardt decided to consult interested partner countries on the matter. On 18 July 1961, the Swiss embassies in the host countries of the Seven Sisters –

France, the Netherlands, Great Britain, Italy and the US – were asked to informally sound out the attitude of a) the government and b) the private oil industry towards OPEC. The incoming answers mostly confirmed the political concerns already expressed by the Swiss towards OPEC. Most of the official governments agreed that OPEC – while still of recent origin and hampered by internal divisions – constituted a potentially disruptive threat to the oil industry, while the answers from the private oil industry contained a wide variety of perceptions, including support and open hostility. As might be expected from what has been discussed so far, the stance of non-hostile passivity towards the new institution was – in one way or another – implicit in the answers. None of the countries directly objected to a physical headquarters in Geneva but preferred an informal status of OPEC.⁹

Based on this information, several units of the Swiss administration met on 22 August 1961. As the following statement from the internal protocol of the meeting shows, political concerns took precedence over the legal arguments:

But the essential point is that the OPEC does only unite a part of the oil production countries and that it wants to reinforce its negotiation position towards other countries or towards the international oil companies.

(Trinkler, 2015, p. 38; BAR, Dossier E2003A #1974/52 #18)*

This decision was communicated to Rouhani roughly a month later on 26 September 1961. The official notification did not mention the political motives influencing the decision but gave procedural and administrative reasons for the refusal, which were mainly: (a) that Switzerland was neither part of the organization nor ever wanted to be, (b) that OPEC only united some of the oil-producing countries (the US and Soviet Union were the two missing major producers) and (c) that for this reason OPEC would be pursuing its own particular commercial goals on behalf of the member countries. We will see later on how these guidelines were violated on other occasions.

By factoring in their own interests, the Swiss were essentially following standard practice in international diplomacy. States commonly weigh their own wellbeing higher than universal principles of conduct:

The issue of granting special treatment (to an international body, authors note) may be assessed from case to case by taking into account the Swiss political and trade political interests.

(Trinkler, 2015, p. 46; Dossier E2003A#1978/29#26)*

Despite its political neutrality, Switzerland was deeply embedded in the state framework of Western Europe. This was especially true in the case of economic cooperation and therefore the international oil markets. Cheap energy imports played an essential part in Europe's post-war recovery and the subsequent economic growth that resulted in three decades of rising living standards. The Swiss were almost fully dependent on a stable and cheap flow of mineral oil stemming from the framework of the Seven Sisters.¹⁰ Major jumps in prices or a change in this proven system threatened to significantly impact the economic wellbeing of the state. From this point of view, the Swiss had plenty of pragmatic reasons to remain skeptical towards Mr Rouhani's organization.

Comparing OPEC to other international organizations asking for diplomatic privileges during the late 1950s or the 1960s, the behavior of Switzerland towards OPEC can be put into a broader perspective. One obvious comparison is the Arab League (AL), which repeatedly sought to establish a subsidiary office with official status in Geneva during this time. As with OPEC, the Swiss permitted a semi-official office to be set up in 1957 but refused any diplomatic privileges. This office repeatedly overstepped the boundaries of the usual diplomatic conduct; in addition, representatives of the office tried to trick the Swiss administration into granting the desired privileges by disguising employees of the office as members of the diplomatic staff of any of the AL's member states. The Swiss were repeatedly forced to issue warnings towards

agents of the AL and the embassies of its member states. The sources show that this experience influenced the Swiss response to OPEC – the same organizational unit from the administration was in charge of the requests. Granting privileges to OPEC (whose members, apart from Venezuela and Iran, were also members of the AL), would have set a dangerous precedent for the tedious troublemaker (Trinkler, 2015, p. 46; an internal protocol from the OIO from 12 Nov. 1962; BAR, Dossier #1974/52 #18★).

On the other hand, the conclusion of a seat agreement with the Organisation of American States (OAS) was swiftly conducted in 1964 while the negotiations with OPEC were still ongoing. It is striking that the main administrative reasons to officially refuse the request of OPEC also applied to the OAS: (a) Switzerland was neither part of the organization nor was it – by definition – ever possible to join it, (b) it was a regional confederation of states that clearly excluded others and aimed at furthering the interests of its members, and (c) one of its main goals was pursuing commercial interests by furthering and increasing the economic activities of the American member states. But the Swiss saw clear advantages in setting up favorable relations with the newly founded institution, especially from an economic point of view:

The establishment of a OAS delegation in Geneva offers the commercial-political advantage of an improvement of the mutual orientation, relations and ties between Switzerland – Central- and South America [...]. The recognition of special treatment is therefore also from the point of view of Switzerland's interest affirmative.

(From an official request to the Federal Council on 7 October 1964; Trinkler, 2015, p. 61; BAR, Dossier E2001E#11978/84#848★)

This comparison is the last piece of evidence that the refusal of a seat agreement was purely of a political nature. The Swiss clearly weighted their own political and economic interests (stable source of oil) higher than the customary legal basis and universal treatment of international bodies (Breisinger, 2012; Eberlein, 1993; Frei, 1983; Jenks, 1961; Kutscher, 2012; Linke, 1995; Michaels, 1971; Weiffen, 2012).

Conclusion

This chapter has shown the importance of official international recognition for the early constitution of OPEC. Taking the considerations of the three main sections into account, the following main insights were gained:

- 1 Official recognition – expressed through a seat agreement and diplomatic privileges for the organization – were a vital precondition for OPEC to participate in international committees. This point was illustrated in the first section by demonstrating that the seat agreement in Austria was almost immediately followed by admission into the ECOSOC and UNCTAD. The seat agreement in a Western European state was perceived as a signal of legitimacy by the community of sovereign states and allowed OPEC to consolidate its existence within the framework of international organizations.
- 2 The sources from the British archives in section two have shown that at least three host countries (Great Britain / the US / the Netherlands) of the Seven Sisters and a part of the private oil industry itself have employed a strategy of neutral non-recognition towards OPEC. The goal was to minimize the influence of OPEC by negating its official existence without expressing open hostility. This endeavor was greatly helped by the refusal of the Swiss to grant the seat agreement and acknowledge OPEC as a legal entity in its own right. This strategy was pursued even after OPEC's move to Vienna at the beginning of 1965 but was complicated by OPEC's foothold in the above-mentioned international bodies.
- 3 Last but not least, section three explored the reasons for Switzerland's refusal of a seat agreement and whether there was a connection to the policy of neutral non-recognition at the supranational level.

The sources from the federal administration has clearly shown that the Swiss consulted with other interested countries and that the refusal was motivated by political self-interest. A comparison to similar cases (AL, OAS) has conclusively shown that the Swiss responded selectively to requests of diplomatic privileges and that the official reasons (formal and administrative) for the refusal of OPEC were fabricated and negligible in other circumstances. Switzerland – while not being directly invested in the private oil industry – was inherently interested in a continuous flow of cheap energy imports and weighted this interest higher than an objective treatment of OPEC. In turn, the Swiss refusal of recognition served to reinforce the policy of neutral non-recognition at international level.

Merging these findings, it is apparent that OPEC was – immediately after its constitution – recognized as a potentially disruptive entity for the oil markets in Switzerland and for other Western countries and the oil industry. The Swiss were never interested in hosting OPEC and only granted it physical establishment due to a lack of communication between the canton of Geneva and the federal administration. Switzerland thereafter consulted with other major stakeholder within the oil markets (host countries of the Seven Sisters) when assessing the treatment of OPEC and implicitly took part in the policy of neutral non-recognition. It is important to note at this stage that there is no proof of direct coordination between Switzerland and the host countries or the Seven Sisters apart from the informal *démarches*

of the Swiss embassies. Based on the evidence presented in this article, it seems probable that the Swiss, through participation in ECOSOC, UNCTAD and the OECD and other more informal channels (diplomats talk a lot informally ...), were aware of the policies of Great Britain and the US.

Notes

- 1 The notes and references in this article will be kept to a minimum. Only direct quotes from source material and extended information for the understanding of the content are directly quoted. References to further reading of secondary literature are provided in a collective note at the end of each section.
- 2 Federal Counsellor Max Petitpierre took over the Foreign Ministry in 1944 and led Switzerland out of his temporary isolation by following the two maxims of strict neutrality and solidarity (Trachsel, 2011).
- 3 For the sake of the reading flow, the citations in this article will always be quoted in English and are translated by the author. A reference will indicate where the wording in the original language can be found.
- 4 According to Burdett, the state had no direct possibility to yield influence on the decisions of the private oil companies (despite holding extensive amounts of shares). But because of the regular exchange of information and opinions, the state was able to participate in the decision-making processes. OPEC was only one of several issues that were discussed in the meetings (Burdett, 2004, vol. 2, p. 166).
- 5 Iraq remained absent from OPEC after the unilateral expropriation of the Iraq Petroleum Company and the failed invasion of Kuwait until the removal of Abd al-Karim Qasim in February 1963 (Skeet, 1988, pp. 27–33).
- 6 The detailed documentation to the negotiation process described in this section can be found in Burdett (2004, pp. 759–796).
- 7 The OIO was part of the Federal Department of Political Affairs that was renamed into Federal Department of Foreign Affairs in 1979 (Eidgenössisches Politisches Departement EPD, from 1979 Eidgenössisches Departement für Auswärtiges EDA).
- 8 A clear prohibition was impossible to formulate as there was no law preventing to set up an international organisation in Switzerland without pertinent reasons of objection. The matter was furthermore complicated as the ultimate decision for the establishment of a physical headquarter was within the competency of the Canton of Geneva.
- 9 The responses reached Switzerland on 25 July (France), 27 July (Great Britain), 2 August (the US) and 7 August (the Netherlands, Italy). The results are summarized in an internal memorandum on 8 August 1960 (Trinkler, 2015, p. 38; BAR, Dossier E2003A #1974/52 #18*).
- 10 There were very few options in order to substitute the needed oil imports: the US became a net importer of oil already in 1947 and the only other major producer outside OPEC was the Soviet Union, which was deemed a political threat.

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When modern terrorism began

The OPEC hostage taking of 1975

Thomas Riegler

Never before and never since have so many high-ranking politicians been in the hands of terrorists: The hostage taking during the minister's conference of the Organization of the Petroleum Exporting Countries (OPEC) in Vienna¹ on 21 December 1975 is a pivotal event in the history of terrorism. Six gunmen under the command of the 26-year-old Venezuelan Ilich Ramirez Sanchez (better known as 'Carlos') took 62 people hostage, among them 11 oil ministers. There were three casualties: one Austrian policeman, an Iraqi bodyguard and a Libyan delegate. Austrian chancellor Bruno Kreisky² struck a deal, which allowed the terrorists to leave by plane to Algiers and take 33 hostages (including the oil ministers) with them. After a harrowing back and forth flight between Algiers and Tripoli, the remaining hostages were finally released on 23 December 1975. This 'coup' received worldwide attention. One observer recently called it one of the 'biggest media campaigns of all times' and compared it to 9/11.³ The present article explores the OPEC hostage taking based on primary sources from Austrian and German archives and focuses (1) on the operational background, (2) on the event itself and (3) on the political and judicial consequences.

'Operation OPEC': aims and motifs

The OPEC hostage taking was a major step in the development of modern terrorist violence. Contrary to 'older' forms with a primarily nationalistic outlook, it was planned and carried out transnationally. A Palestinian splinter group under the leadership of Wadi Haddad was responsible. Haddad, who is known today as the 'godfather' of modern terrorism, had enrolled two members of the Western German Revolutionary Cells (RC), Hans-Joachim Klein and Gabriele Kroecher-Tiedemann. 'Joseph' and 'Yousef', two men from Haddad's group, also took part. Carlos was the designated leader, with Anis Naccache as deputy. By attacking OPEC, Haddad wanted to attract worldwide media attention to the so-called 'Palestinian problem' and acquire funds for the 'armed struggle' (Schröm, 2002, pp. 54–62). But there was also a hidden agenda. To a large degree the OPEC hostage taking was the result of the power struggle inside the cartel itself. The real sponsor and initiator was Libyan dictator Muammar al-Qaddafi. He wanted to affect the price policy of the cartel and used Haddad's group as a proxy force to put his main rivals, Saudi Arabia and Iran, under pressure (Schröm, 2002, p. 54). Qaddafi was notorious for his support of terrorist groups and 'liberation movements', which went beyond the Middle East and Africa to Latin America, Thailand and the Philippines. He also forged alliances with the Provisional IRA, ETA and other Western European groups. In his study of state-sponsored terrorism, Daniel Byman noted:

Terrorism for Qaddafi served several purposes. When he came to power, Qaddafi was a genuine revolutionary leader who believed in backing other movements that opposed what he saw as oppressive imperial powers. [...] In addition, terrorism extended Qaddafi's reach, enabling him to be a placar against Israel or in other causes of concern to him.

(Byman, 2005, p. 290).

The links between Qaddafi's regime and Palestinian groups were especially strong. At the time of OPEC hostage taking they were at the forefront of international terrorism. Between 1968 und 1980, according to US researcher Bruce Hoffman, the Palestinians were responsible for more international terrorist acts than any other movement (Latsch, 2004). Originally, Palestinian terrorism emerged during the late 1960s, when the intention to wage a classic guerrilla war, had ended in defeat. As an alternative, the various groups choose to 'internationalize' their struggle – in order to seize headlines and exercise pressure on Western countries in favour of a political settlement. From 1968 on, small commando units began to hijack commercial flights, first Israeli ones and then, increasingly, international ones (Hoffman, 1998, p. 85). Furthermore, the Palestinians established a vast network, which combined various terrorist groups. Until the early 1980s, at least 40 organizations from Asia, Africa, North America, Europe and the Middle East would send their members to train in Palestinian-operated camps in Jordan, Lebanon and South Yemen (Hoffman, 1998, p. 108).

In this context, Haddad played a substantial role. Until 1977, his group would claim responsibility for nine hijackings, over 40 terrorist attacks, 100 people killed and 250 wounded (Ridder, 2013, p. 89). Born 1927 in what is today Northern Israel, the son of Greek Orthodox Christians, had studied medicine at the American University in Beirut. There he met up with like-minded Georges Habash and together they launched the Arabian Nationalist Movement (ANB), a pan-Arabian and socialist group. In 1967, Haddad and Habash transformed the ANB into the Popular Liberation Front for Palestine (PLFP), and Haddad soon took command of its armed wing, the so-called Special Operations Group (SOG). In this role he was responsible for the first plane hijackings (Robinson-Skelton, 2006, pp. 831–838). Haddad viewed this tactic as an appropriate means to counter the overwhelming conventional superiority of Israel. To execute the complex missions, he forged alliances with Western German left-wing extremist groups like RC and the Red Army Faction (RAF). The Germans agreed to take part in Haddad's operations in return for training, supplements of weapons and financial support (Latsch, 2004, pp. 86–92).

But Haddad also attracted international volunteers. During autumn 1969, the then-20-year-old student Ilich Ramirez Sanchez walked into a Jordanian office of the PLFP and was recruited. At first, PLFP spokesman Bassam Abu Sharif only noticed a 'baby face', but quite rapidly he recognized his potential as a valuable fighter: well read, good at speaking languages, full of political belief. Abu Sharif gave him the nom de guerre 'Carlos' inspired by the Arab name 'Khalil' (Abu-Sharif, 1995, p. 69). He soon rose to deputy commander of the PLFP's operations in Western Europe. Carlos took credit for the assassination attempt of Joseph Edward Sieff (1973), a grenade attack on a Paris café (1974) and two botched tries to blow up an El-Al-plane in Paris-Orly (1975) (Schröm, 2002, p. 28). But he achieved worldwide notoriety on 27 June 1975 when he shot dead two unarmed agents of the French domestic intelligence service and executed his PLFP superior, Michel Moukharbal, whom he suspected of being an informer (Schröm, 2002, p. 42). After the shooting, rumours appeared that Carlos had been recruited by the KGB during his studies at Moscow's Patrice Lumumba University and sent for training to Cuba.⁴ Actually, this was disinformation on the part of Western intelligence services (Hänni, 2018, pp. 125–129). But this did not mean that the Eastern bloc was not involved at all. Haddad for instance enjoyed close links to the KGB. From the early 1970s, the USSR and its satellite states had begun to sponsor not only so-called 'national liberation movements' in Asia, Africa and Latin America but also terrorist groups in the Middle East. But this did not amount to control over terrorism, as was claimed by experts like Claire Sterling, Brian Crozier and others.

Organizations like that of Haddad retained their autonomy and were not an extended arm of Soviet foreign policy (Naftali, 2005, p. 16). In 1999, KGB defector Vasili Mitrokhin and co-author Christopher Andrew presented evidence that Haddad had been handled by the KGB since 1970 under the codename 'NATIONALIST' (Andrew and Mitrochin, 1999, p. 472). Thus, it is likely that the KGB had advance knowledge of the OPEC hostage taking (Andrew and Mitrochin, 2006, p. 370).

In 2000, an until then relatively unknown insider came forward and commented on the background of the OPEC hostage taking: Carlos's already mentioned deputy Naccache. Back in 1973 he had joined Fatah and soon become an operative of its intelligence service. Naccache's job was to infiltrate other Palestinian groups in order to learn their plans and possibly avert terrorist attacks that would harm Fatah's interests – especially in war-torn Lebanon, where it protected US installations on the basis of a secret agreement. For this reason, Naccache infiltrated Haddad's group and was involved in the planning and execution of the hostage operation from the start.⁵ According to him, the central motivation was to extort money in order to finance the resistance in Lebanon, which was the main safe haven for various Palestinian groups since their expulsion from Jordan in 1970. Since the Gulf States would not fund their cause, Haddad conspired with the allied Syrian Nationalistic Party of Kamal Kheirbek to conduct a 'finance action'. When civil war broke out between Palestinian and Christian militias on 13 April 1975, the situation made the issue of funding even more pressing. According to Naccache, during the preparations two further operational goals were placed on the agenda: the murder of the Iranian and Saudi-Arabian oil ministers, Jamshid Amouzegar and Ahmed Zaki Yamani, as a sort of punishment for their 'moderate' governments, which had aligned themselves with 'Western imperialism' (Schröm, 2002, p. 53).

During the 2000/2001 trial of Hans-Joachim Klein for his involvement in the OPEC hostage taking, new evidence was presented, that a state sponsor had also been involved. Among this was the protocol of the debriefing of Carlos after the event. The paper originated from the archive of the PLFP-SOG and had been handed to the court by an informant:

Carlos reports in this document among other things, how he tried several times to meet up with the Libyans in Vienna in order to get the weapons and information as agreed – but several attempts failed and only on 19 December 1975, it worked out. On this day, the weapons and the information were delivered. Elsewhere, [...], Carlos mentions that he negotiated in Tripoli and thereby had said, that the Libyans would have to implement, what had been agreed upon. Furthermore, he calls Libya an unreliable ally in this regard.

Several times in the protocol it is stated that the killing of the two oil ministers had been the main objective of the operation (Landesgericht Frankfurt am Main, 2001, p. 52). According to a testimony provided by Carlos himself, in October 1975 Kheir-Beik had been invited by an Arab president (the court reached the conclusion that this was Qaddafi). At the meeting, the oil policy since the death of King Faisal ibn Abd al-Aziz in early 1975 was discussed. The unnamed head of state demanded a terrorist operation against the responsible oil ministers to bring off a propaganda coup, but also to eliminate especially Yamani, the main player behind the controls of OPEC. Kheir-Beik then proposed to task Haddad with the execution, whereupon the sponsor agreed to acquire the necessary intelligence and weapons (Landesgericht Frankfurt am Main, 2001, p. 50). Qaddafi indeed had reasons to target both Yamani and his close ally Amouzegar. Saudi Arabia pursued price stability in the long run and resisted Libya's demands for an increase. Qaddafi eventually achieved his aim to some degree: in January 1977, Saudi-Arabia stopped ceased resisting and accepted a price rise of 10 per cent, followed by a further increase of 5 per cent in July 1977 (Hagger, 2009, p. 106). But Qaddafi's success was short-lived. By the early 1980s, the oil price collapsed again and OPEC saw its power greatly diminished (Timney, 2015, p. 23).

To get back to the question of who was responsible for the OPEC hostage taking, in 2012, Carlos's biographer, Colin Smith, reported an alleged confession by the former Libyan oil minister Ezzedin Al-

Mabrouk. Before he died of cancer in the late 1980s, Al-Mabrouk allegedly unburdened himself of a secret. He told a lifelong friend, who had been one of the hostages, that two days before the operation started the oil minister had received instructions from Tripoli to meet somebody in Vienna. This turned out to be Carlos. Al-Mabrouk briefed him on the layout of the OPEC building and the security arrangements. On his deathbed he asked his friend for forgiveness and it was granted (Smith, 2012). According to Klein, the mentioned meeting with the Libyans took place on 19 December 1975, just two days before the operation. Carlos and Naccache were provided with six 9-mm Berretta pistols, two machine guns, several hand grenades and explosives, as well as ‘inside information’ (Landesgericht Frankfurt am Main, author’s copy).

In addition to the substantial role of Qaddafi, it is likely that other state actors were also involved in the plot. For example, it was noted at the time that only three members of the 13-strong Iraqi delegation were present on the morning of 21 December 1975 (Robinson, 1988, p. 171). Doubts were also raised when the Iraqi chargé d'affaires, Rijad Al-Azzawi, who also headed the embassy’s intelligence section, appeared at the scene ‘by coincidence’ (Yallop, 1994, p. 451). He offered his services and for the next 19 hours fulfilled a crucial role: Al-Azzawi was present in entrance hall of the OPEC building and acted as a go-between Carlos and the Austrian authorities. Several times Al-Azzawi walked the few hundred yards to the chancellery to brief Kreisky personally on the developments. This eased the negotiation process considerably (Demaris, 1977, p. 11). Especially since the Libyan ambassador – whom the hijackers had originally demanded to negotiate with – was nowhere to be found and arrived only late at night (Dahlke, 2011, p. 256).

What was also puzzling was that the minister’s conference had originally been scheduled to end on 20 December 1975, but it had to be postponed to the following day because at the end of the meeting the Algerian representative had engaged in a lengthy debate with his Iraqi colleague.⁶ The reason for this could have been the long delay in the handover of weapons, which almost led to the cancellation of the whole operation (Klein, 1979, p. 61). In this regard, on 3 February 1976 the Austrian ambassador had a revealing discussion with Yamani. The oil minister made it clear that the terrorists had not acted on their own initiative but that the hostage taking had been organized at ‘state level’. Yamani articulated the view that ‘Libya in the first place, then Iraq (and at most the Iraqi Baath party) and South-Yemen, but only in the function of granting asylum’ had been involved. Yamani also hinted that Algeria likely had some fore-knowledge. Both Iraq and Algeria were outspoken opponents of the ‘moderates’ stance on the Middle Eastern conflict and of OPEC’s economic policy in general.⁷

The hostage taking

The first two members of the terrorist commando – Carlos and Klein – arrived in Vienna in early December 1975 via train from Zurich. According to Klein, Carlos used the time to shop and bought the beret that became his trademark (Klein, 1979, p. 55). A logistic support group from the RC had been already been in Vienna for some time. They had scouted the OPEC building, rented two flats as well as cars and researched the media coverage of past OPEC conferences in libraries. When these preparations were concluded, the four RC members left (Follain, 1998, p. 79). The six members of the terrorist commando were fully assembled only on 18 December 1975 (Landesgericht Frankfurt am Main, 2001). Due to the last-minute crisis with the Libyan weapons, the operation was reset for Sunday, 21 December 1975 (Landesgericht Frankfurt am Main, author’s copy).

The target, the OPEC secretariat, occupied the first two floors of a modest seven-storey structure at Dr Karl Lueger-Ring 10, one of Vienna’s busiest boulevards. The building was not particularly secured – since it housed an embassy, several businesses and private tenants, precautions were only minimal and there were no controls at the main entrance (Demaris, 1977, p. 3). Although Austria had experienced a hostage taking by Arab terrorists in 1973,⁸ there was little risk awareness on part of the authorities. As chancellor Kreisky

had to acknowledge in parliament in early 1976, a ‘crucial mistake’ had been made. In what proved to be a short-sighted assessment, OPEC had been considered the ‘least endangered institution’ because some of its members were known contributors to the terrorist cause. It therefore seemed unlikely that OPEC generally would be in the crosshairs. ‘We reached the conclusion that this organization – it arrived at the same conclusion itself – constituted no security risk. We have been mistaken in that regard,’ Kreisky said.⁹ Yamani later stated, critically, that OPEC had in fact pressed for more security: ‘There had been a minor incident in the same building. The Canadian embassy was there and I think there had been a bomb scare or something. So, the OPEC secretariat asked for security. But nothing was ever done.’ As Yamani put it, there had been

some sort of understanding or gentleman’s agreement, if you will, that terrorists will not operate inside Austria. But twice there were terrorist attacks – that time with Carlos, and once, if I remember correctly, terrorists attacked a train bringing Jews from Russia. So that gentleman’s agreement wasn’t very valid. Vienna wasn’t that secure.

(Robinson, 1988, p. 170)

On the morning of 21 December 1975, a solitary policeman was standing in front of the OPEC building, his only job being to manage the traffic. Therefore, he simply saluted when a group of six strangers carrying large Adidas sport bags simply walked in and up the stairs. Further ahead, in OPEC’s premises, two plain-clothes state policemen, aged 60 and 59, were on duty. But they were only lightly armed and had no radios (Landesgericht Frankfurt am Main, 2001). The only other security detail was a former Iraqi employed by OPEC and he was unarmed.¹⁰ Shortly after 11.30 all hell was breaking loose. Carlos and his six accomplices broke into the reception, emptied warning shots into the ceiling and herded people towards the conference room, where the meeting of the oil ministers was taking place. Upon hearing the violent commotion outside, Yamani’s ‘first thought was that the attackers must be Europeans protesting the rise in the price of oil. I thought they came to avenge themselves on us’ (Robinson, 1988, p. 154).

The two state policemen did not put up a fight: Josef Janda phoned for assistance, then hid his gun in a desk-drawer and mingled with the hostages. Anton Tichler tried to get outside help but when he entered the lift he was challenged by Kroecher-Tiedemann. After asking if he was a policeman, she executed Tichler with a pistol shot from behind. The inspector had been killed just a few weeks from retirement. He was the first of the three casualties. In the confusion, the bodyguard of an Iraqi oil minister, Ala Sacés al Khafazi, also ran into Kroecher-Tiedemann and tried to wrestle her down, but in the melee she shot him down (Follain, 1998, p. 83). The third victim, Jusuf Izmirli, was a Libyan delegate who had instinctively charged Carlos when he checked a room and almost got hold of the terrorist’s machine gun (Landesgericht Frankfurt am Main, 2001, pp. 65–73). Carlos is said to have pulled a pistol from the waistband and fired five times – one of the bullets passed through Izmirli’s body and struck the right arm of a member of the Kuwaiti delegation (Demaris, 1977, p. 6).

The terrorists were finally getting control of the chaotic situation when, at 11.50, an eight-man alarm squad of the Viennese police arrived at the scene. They had no special training, and consisted of elderly officers because at that time experienced men were regarded as best equipped to deal with emergency situations. But against a heavily armed and paramilitary trained enemy the force was, of course, inadequately prepared (Smith, 2012, p. 241). Since the situation was unclear, three men of the alarm squad were detached to inspect the building. But instead they engaged in a careless firefight with the terrorists once they reached the lobby of the secretariat. Klein and ‘Jusuf’ had been posted there to fight off any intruders, which they did: before the policemen retreated, their 52-year-old leader was wounded by a stray bullet. Klein suffered the same fate, being hit in the abdomen (Demaris, 1977, p. 7).

Carlos had no choice but to demand emergency treatment for Klein in a Viennese hospital. Doctors there successfully fought for hours save Klein’s life and ensure that he was transportable for the getaway

next day. The other demands Carlos had set out in a letter called for a communiqué to be read on Austrian radio and a DC-9 to be readied for a flight early next morning, so that the terrorist commandos could leave with their hostages. The Austrian government met in an emergency session from 16.27 and as a first step agreed to the broadcast. At 18.22, one of Kreisky's aides began to read the communiqué of the 'Arm of the Arabian Revolution', a cover name adopted by Haddad for the OPEC operation. The text had been drafted in French, which hampered its understanding. It denounced 'American imperialism' and 'Zionist aggression', while calling for oil resources to be nationalized. The record was repeated every two hours until four o'clock the following morning. The aide's poor pronunciation has since been the subject of sarcastic comments (Follain, 1998, p. 91).

Kreisky, who had just arrived at his Christmas holiday destination on the morning of 21 December 1975, had to undertake a return journey of several hours and was thus not present until 18.00. Once he took the chair he made several counter demands to Carlos: the release of all OPEC employees residing in Vienna before the transit journey to the airport and the transmission of written agreements by the remaining hostages to be flown out.¹¹ This face-saving measure was part of Kreisky's strategy to 'internationalize' the event and take the pressure off Austria. He therefore kept in close contact with the ambassadors of the OPEC countries and asked for their consent at every major stage. A destination for the flight was also set. On his own accord, Algeria's foreign minister, Abd al-Aziz Bouteflika, had called in the afternoon and offered to accept a landing in Algiers (Bundeskanzleramt, 1976). When Kreisky faced the international media at 01.10 on 22 December 1975, he was satisfied with the turnout: 'We have achieved more than we had anticipated.'¹² When he was later confronted with criticism of his crisis management, Kreisky defend his position: 'Fighting terror through complete refusal of terrorist's demands has resulted in the terrorist's capitulation only in a minority of cases, but all too often in more victims. Apart from that, a strategy of retribution has brought about an escalation of terrorism.' But he conceded that so far negotiations had also not been successful in tackling the problem (Bundeskanzleramt, 1976).

At 08.45 on 22 December 1975, the convoy carrying the terrorists and the remaining 33 hostages, including 11 oil ministers, arrived at Schwechat airport. Klein was also brought by an ambulance and was accompanied by a doctor during the whole flight. The necessary oxygen for Klein's life support posed an explosion hazard throughout the journey, but this risk was taken.¹³ When boarding was completed, Carlos came up to the interior minister Otto Rösch to say farewell. The exhausted Rösch shook the terrorist's hand while the whole procedure was broadcast live on television, which caused a major embarrassment (Petritsch, 2010, p. 259). After the arrival in Algiers, Klein was again transferred to hospital and Carlos released further hostages. But he also set a new destination: Tripoli. The plan was to get a plane there with a longer range in order to fly to Baghdad and further to Aden. There, as Carlos explained to Yamani, the Saudi Arabian oil minister would be executed as well as his Iranian colleague. But this did not work out: once in Libya the authorities were completely uncooperative. It is said that the killing of the Libyan delegate had angered Qaddafi so much that all arrangements were null and void. Thus, Carlos had no choice but to return to Algiers in the early hours of 23 December 1975 (Follain, 1998, p. 95). He then entered into personal negotiations with Bouteflika. The terrorists were offered a substantial ransom, but they were also threatened with certain death if anything happened to Yamani and Amouzegar (Kopp, 2007, p. 94). Carlos gave in and released the last 12 hostages.¹⁴ He later put the ransom at \$50 million and explained that it had been paid by Saudi Arabia in their name and on Iran's behalf. But the money was 'diverted *en route* and lost by the Revolution'. Klein on the other hand quoted Carlos as admitting that he put a large share in a safe place in Algeria (Follain, 1998, p. 102).

Aftermath and reckoning

Upon his return to Haddad's base in Aden, Carlos was dismissed from the organization. The PLFP-SOG leader was furious with the decision to spare the two oil ministers: 'Stars are very bad at following

instructions. You have not followed my instructions. There is no room for stars in my operational teams. You can go' (Follain, 1998, p. 105). Carlos went on to start his own terrorist enterprise, offering services to both Middle Eastern and Eastern bloc intelligence services. In 1994, after years on the run, Carlos was delivered by his Sudanese hosts to French agents. Serving a life sentence for the 1975 murders of Mouk-rabal and the two counter-intelligence officers, he was further convicted of attacks in France and sentenced to an additional life term in 2011 and then a third life term in 2017. Haddad on the other hand pulled off further spectacular terrorist attacks, but both ended in failure: in 1976, Israeli commandos freed a hijacked plane in Entebbe; the following year, a Western German counterterrorist achieved the same result in Mogadishu. Haddad died only a few months later in East Berlin after supposedly suffering from leukemia. According to recent revelations, Haddad was assassinated by the Israeli intelligence service Mossad, which poisoned his toothbrush (Bergman, 2018, p. 261).

Up to now, only Klein has been convicted in relation to the OPEC hostage taking. Carlos's accomplice publicly renounced terrorism in 1979 and went underground in France for some decades. In 2000, Klein was arrested and tried in a German court. He was released in 2003. Kroecher-Tiedemann had already been captured in a shootout with Swiss police in late 1977 but was only charged for her role in the hostage crisis in 1990. Mostly because Austrian authorities had recorded the crime scene inadequately, she was acquitted, but died of cancer in 1995 at the age of 44.¹⁵ The two Arab members of the commando were never identified. Naccache joined the Iranian intelligence service. In 1980, he took part in an assassination attempt on Shapour Bakhtiar, the Shah's last prime minister, who lived in exile in Paris. But the hit squad headed to the wrong apartment and killed a neighbor of Bakhtiar's. Naccache was pardoned in 1990 as part of a deal and is now a businessman in Beirut.¹⁶ The insufficient law enforcement with regard to the hostage taking had many reasons. The forensic examination had been done in a rush because OPEC had given Austrian police too little time.¹⁷ From the start the cartel showed little interest in pursuing the case – obviously because some of its most powerful member states were actively involved. But Austria also acted in a restrained way. After some delay, a request for extradition was sent to the Algerian authorities. But they responded on 9 January 1976 that the members of the terrorist commando unit had left its territory and therefore the request could not be pursued. Nonetheless, the warrants continued to stand.¹⁸ But in a government meeting on 14 January 1976, Foreign Minister Erich Bielka reported that the Austrian demands had caused some consternation in Algeria since the government's acceptance of the terrorists had contributed to the bloodless resolution of the crisis. Kreisky reached the conclusion that one had to 'acknowledge' the opinion of the Algerian authorities (Dahlke, 2011, p. 298).

In the following years, Austria did not confront the states suspected of involvement in the OPEC hostage taking. When Yamani in the wake of the event proposed a resettlement to Paris or Geneva, Libya, Iraq and Algeria all supported the idea of keeping the OPEC secretariat in Vienna.¹⁹ At that time, the Austrian capital was positioning itself to become one of the four major United Nations office sites. Just two years before the OPEC hostage taking, the groundbreaking ceremony for the Vienna International Centre had taken place (Schmidl, 2012, p. 128). On 23 August 1979 it was formally opened. The support of 'Third World' countries had proved crucial to Vienna's success (Petritsch, 2010, p. 291). As Bielka advised Kreisky shortly after the hostage taking, an exodus of OPEC would not have been 'beneficial' to these efforts to get more international organizations to settle in Vienna.²⁰ In his memoirs, Kreisky stated that some leading members of OPEC had wanted to leave after the 'incident' and that it took an effort to prevent this since he feared that others might follow suit (Kreisky, 2000, p. 321). But it did not happen. In August 1976, OPEC signed a rental contract for a new office building at the Danube channel. From now on, security was very tight (Dahlke, 2011, p. 295). All costs for the renovation of the damaged offices at the former headquarters were covered by the Austrian taxpayer.²¹ The OPEC secretariat remains in Vienna to this day. In 2013 it relocated to a newly built structure at Helfferstorferstrasse 17.

With regard to the further criminal prosecution of OPEC hostage takers, Austria remained uncommitted: there were no efforts to get members of the terrorist commando unit extradited once they were

arrested in other countries. When Kroecher-Tiedemann was captured in late 1977, Kreisky regarded proceedings against her in Austria as too risky – despite the fact that Kroecher-Tiedemann in the meantime had taken part in the kidnapping of Austrian industrialist Walter Palmers in autumn 1977.²² When Carlos himself was apprehended in 1994, only an examining magistrate flew to Paris to question him. But the interview was quickly terminated when Carlos behaved uncooperatively. He extended his arm in greeting, but the magistrate refused to take it, not wishing the same controversy as Roesch in 1975 (Follain, 1998, p. 93).

When it came to counterterrorism policy, Austria enacted measures to prevent a repetition of the OPEC hostage taking. Kreisky argued strongly that terrorism could only be tackled if its root causes were addressed. In order to fight terror, the grievances causing it to have to be removed. Kreisky specifically focused on the Middle Eastern conflict, which, from his point of view, could only be solved by means of a just peace. To achieve this, a legitimate political representation of the Palestinian cause had to be fostered. Therefore, Kreisky contributed to the international legitimization of the Palestinian Liberation Organization (PLO) and its chairman, Yasser Arafat. On the practical level, a secret pipeline was established between Austrian authorities and the PLO's own intelligence service in order to get advance warning of suspicious travel movements. To further minimize security risks for Austria, Kreisky cultivated contact with Qaddafi. He even received the Libyan dictator's first formal visit to a Western country in 1982. Kreisky remained convinced that Qaddafi had not been involved in the OPEC hostage taking. When British journalist David Yallop pressed him on this subject, the chancellor assured him that 'neither Qaddafi nor any other Libyan had a hand in the OPEC attack'. According to him, Austrian authorities had investigated such claims thoroughly: 'It could not be verified' (Yallop 1994, p. 190, author's translation).

Conclusion

In 2010, Olivier Assayas presented his film *Carlos*, a biography of Ilich Ramirez Sanchez, which also enacted the OPEC hostage taking. According to Assayas, a key element was the depiction of Cold War terrorism as a form of covert warfare commissioned by states: 'Terrorism is about one state sending a message to another.'²³ He has a point here: without state support and international cooperation among the groups themselves, terrorists in the 1970s and 1980s would most certainly not have been as effective as they were. The superpower rivalry of the Cold War provided ample opportunity for terrorist surrogates – they benefited from financial and logistical support, as well as from training and other resources.

Contemporary radical Islamist terrorism is not dependent on state sponsors. On the contrary, it flourishes in failed states, is mainly funded by private individuals, and constitutes a highly flexible network with flat hierarchies. No matter how confusing and destructive Cold War terrorism proved to be, it served concrete aims and interests. Radical Islamist terrorists, on the other hand, do not pursue a similar clear agenda. The death toll also differs. Largely, violence inflicted by Cold War terrorists was applied in relation to the desired results. The OPEC hostage taking, for example, had a clearly defined aim: once the oil ministers were in the hands of the terrorists, unnecessary bloodshed was avoided. In more than four decades since, terrorism has become a threat to the public at large and its calculus has blurred into the provocation of an apocalyptic 'war of civilizations'.

The OPEC hostage managed to attract worldwide media attention and made Carlos a notorious 'poster boy' of international terrorism. But its hidden aspects are still becoming apparent: Libya chiefly wanted to influence the price policy and exploited terrorism as a form of covert warfare. The execution was left to Haddad's organization, which could not only claim ransom but also send a message to the 'compromising' and 'reactionary' Arab states. Yet despite modern elements like the 'hijacking' of the media and the strike at a key international organization in a Western country, the OPEC hostage taking belongs to a past age. Now, terrorism expresses itself primarily in suicide bombings and a willingness to use indiscriminate violence on a large scale.

Notes

- 1 On 24 June 1965 the then foreign minister Bruno Kreisky and OPEC General Secretary Ashraf Lutfi signed an agreement establishing the OPEC secretariat in Vienna. After the International Atomic Energy Agency (IAEA), it was the second major international organisation to move to Vienna. OPEC had previously been based in Geneva (*Die Presse* (24.06.2015) Als de OPEC nach Wien kam. Available from: <https://diepresse.com/home/zeitgeschichte/4762088/Als-die-OPEC-nach-Wien-kam?from=simarchiv>)
- 2 Bruno Kreisky (1911–1990) served as foreign minister from 1959 to 1966 and as chancellor from 1970 to 1983. He achieved an absolute majority for his Social Democratic Party three times in a row.
- 3 *In the Darkroom*. 2013. [Documentary], Nadav Schirman dir.
- 4 According to former Soviet counterintelligence officer Oleg Kalugin, KGB surveillance officers were astounded ‘that this infamous international criminal would turn out to be such a playboy; he seemed to spend all of his time in Moscow at parties; and our agents marvelled at the number of women Carlos courted in the Soviet capital. After a couple of weeks Carlos left without incident’ (Kalugin, 1994, p. 175).
- 5 Fisk, R. (2001). ‘My friend Carlos: A hitman looks back’. *The Independent*, 18 March.
- 6 Operation OPEC – Terroranschlag in Wien. 2007. [TV-documentary]. Dirk Laabs dir.
- 7 Stiftung Bruno Kreisky Archiv (Kreisky) (03.02.1976). VII.5. ‘ÖB Djeddah an Bundesminister für Auswärtige Angelegenheiten’. Internationale Organisationen – Überfall auf die OPEC 1975.
- 8 On 28 September 1973, two Arab gunmen had entered a train with Jewish émigrés and took three people hostage. After long hours of negotiation, Kreisky granted them a plane to fly out of the country, leaving their hostages behind.
- 9 Stenographisches Protokoll 16 (27.01.1976). 1397. ‘Sitzung des Nationalrates der Republik Österreich’.
- 10 Stiftung Bruno Kreisky Archiv (Kreisky) (02.01.1976). VII.5. ‘Niederschrift mit Mahmood Nail’. Internationale Organisationen – Überfall auf die OPEC 1975.
- 11 Stiftung Bruno Kreisky Archiv (Kreisky) (23.12.1975). ‘Tagebuch Josef Staribacher, Eintragung Sonntag, Montag und Dienstag’.
- 12 *Kurier* (23.12.1975). ‘Mehr als wir annahmen’. *Kurier*.
- 13 Stiftung Bruno Kreisky Archiv (Kreisky) (21.12.1975). VII.5. ‘Verhandlungsschrift Nr. 8a über die Sitzung des Ministerrates’. Internationale Organisationen – OPEC-Überfall 1975, 30.
- 14 In 2000, Anis Naccache mentioned a realistic sum. According to him Iran and Saudi-Arabia paid each \$5 million ransom. Maamoun Youssef, Naccache enthüllt Mörder-Geheimnisse as reported in *Associated Press*, 21.11.2000 (Landesgericht Frankfurt am Main, 2001).
- 15 Baur, A. (2008). ‘Direkter Abschied vom Terror’. *Die Weltwoche* 40/2008. Available from: www.weltwoche.ch/ausgaben/2008-40/artikel/artikel-2008-40-diskreter-abschied-vom-terror.html.
- 16 Simons, M. (1990). ‘France releases five terrorists and sends them to Teheran’, *New York Times*, 28 July.
- 17 Operation OPEC – Terroranschlag in Wien. 2005. [TV-documentary]. Christoph Feurstein dir.
- 18 Stenographisches Protokoll 16 (27.01.1976). 1380. ‘Sitzung des Nationalrates der Republik Österreich’.
- 19 Stiftung Bruno Kreisky Archiv (Kreisky) (29.03.1975). StBKA, VII.5. ‘Außenminister Bielka an Bundeskanzler Kreisky’. Internationale Organisationen – Überfall auf die OPEC 1975.
- 20 Stiftung Bruno Kreisky Archiv (Kreisky) (29.03.1975). StBKA, VII.5. ‘Außenminister Bielka an Bundeskanzler Kreisky’. Internationale Organisationen – Überfall auf die OPEC 1975.
- 21 Stiftung Bruno Kreisky Archiv (Kreisky) (29.03.1975). StBKA, VII.5. ‘Außenminister Bielka an Bundeskanzler Kreisky’. Internationale Organisationen – Überfall auf die OPEC 1975.
- 22 Stiftung Bruno Kreisky Archiv (Kreisky) (16.05.1978). StBKA. ‘Tagebuch Josef Staribacher’.
- 23 ‘I won’t be doing Bin Laden, I’ve done Carlos!’ French director, as reported by *rt.com*, 14.12.2010.

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OPEC and the financialization of the oil market

Dag Harald Claes and John H. Moe

One of the most important developments in the oil market in the last ten years has been the greater participation in oil futures and derivatives markets by players such as hedge funds, pension funds, insurance companies, and retail investors, with no business in the production or consumption of the physical product.

(Fattouh and Mahadeva, 2012b)

For consumers and producers alike, the price of oil is of the utmost importance, and price formation is a serious issue for all industry actors. The oil-pricing regime, i.e. who sets the price and how it is done, has changed radically over the past seven decades but has been fairly stable the past three decades. In the current regime, financialization, prices are flexible and set at public exchanges, and a wide variety of financial products and derivatives have been established based on the oil prices formed at exchanges. An important consequence of financialization is that the financial industry can be exposed to the industry and the oil price directly and is not limited to funding companies or countries. Investors who operate in the commodity space have been subject to a fair amount of criticism. In particular, the rise of the index investors, who wish to be directly exposed to commodity prices, has resulted in much debate, although the prominence of other types of investors such as hedge funds has also been controversial. Collectively, these non-industry actors are labeled speculators, and they have been blamed for both sharp price rallies and increased volatility. For OPEC as an organization, the question of financialization of the oil industry is highly relevant for two reasons. First, as a steward of international oil price stability (at high levels), it matters deeply if sharp price changes occur because of non-fundamental reasons. And second, if financialization is here to stay, it is important for OPEC to consider if it is, or can be, a force for good for the organization. And if not, an adequate policy response should be adopted.

We will return to the evaluation of good or bad for OPEC at the end of the chapter. As indicated above, the global financial industry interacts with the oil industry on a broad spectrum of issues. In this chapter we will confine the discussion to the aspects directly relevant for the trading regime and the oil price.

The evolution of oil trading regimes

The administrative pricing system

A very visible change with the financialization of the oil market is the potential influence of non-oil market actors on the daily and long-term fluctuations of the oil price. After the Second World War the oil price was set through an administrative pricing system amongst the international oil companies (IOCs). The international pricing system was posted prices, but this is somewhat of a misnomer. Before the Second World War, the posted price was the price the refiners, i.e. the buyer, put at the gate, but in the post-WWII administrative system the prices were posted by the seller (Parra, 2010, pp. 61–62).

In addition to this administrative pricing system, the major IOCs were vertically integrated companies. Thus, their dominance followed the oil from the well to gasoline pump. They could ensure profit in all stages of the value chain and were able to balance world oil demand and supply through this vertically integrated system.

It is well known that the IOCs dominated the market in the post-WWII era. The system of administered prices seems old-fashioned and inefficient today. Yet this was a time when government price controls were popular in the West. Flexible prices were considered speculative, and a system of price controls was believed to be prudent and just.

For the US independent oil companies, in particular in Texas, the inflow of Middle East oil created great problems in the 1950s, and at the end of the decade, more than 10 percent of the oil refined in the US was foreign (Prindle, 1981, p. 75). The Gulf-plus pricing system was very profitable for the majors, but the imported oil created problems for the independents. The Texas Railroad Commission lobbied on behalf of the independents in Washington (Prindle, 1981, p. 76), and in 1959, President Eisenhower introduced the Mandatory Oil Import Program stating that foreign oil should not exceed 13 percent of US consumption (Maugeri, 2006, p. 84). The import control remained in place until 1971 and kept US oil prices roughly 30 percent higher than world prices (Ikenberry, 1988, p. 154). Concurrently with the dollar devaluation, President Nixon introduced a system of price controls, including on oil (Ikenberry, 1988, p. 152). In 1973, the confluence of fixed prices domestically, high world prices due to the Arab oil embargo (with the US as a primary target), and oil exports being allowed led to lines at the petrol stations, and soon after the US banned oil exports (Bini, Garavini and Romero, 2016). Oil price controls introduced in 1971 had all sorts of unintended consequences and were changed hundreds of times to address the new unintended consequences of the previous change (Murphy, 2018, pp. 63–64). Price became more flexible from 1979 (Ikenberry, 1988, p. 151), and by 1981 the controls had largely been removed and replaced by flexible prices (Murphy, 2018, pp. 77–78).

The spot market of the 1980s

The spot market proper, i.e. more than crude long/short adjustment, emerged in the seventies: ‘The advent of government participation crude in 1974 led to a flourishing spot market for crude oils, with a substantial number of transactions being concluded through brokers’ (Parra, 2010, p. 209). Given the shift in market power from majors to producer nations, it is surprising that the spot market was not promoted by the oil-exporting nations. According to Parra, spot markets were developed without ‘any contribution to it by OPEC or any other major crude supplier to the international markets, such as Mexico or the Soviet Union’ (Parra, 2010, p. 320). Nevertheless, when the new spot market was launched, Mexico was a first mover, and others quickly followed (Fattouh, 2011, p. 6). During the 1970s, OPEC increased its official selling price. This attracted oil producers outside OPEC, in particular in Alaska and the North Sea, to develop their oil reserves. The non-OPEC producers were not subject to the official selling price of OPEC. After the second oil shock in 1980/81, the trend of increasing oil demand dampened off. With

increased supply and no increase in demand, the spot price started to fall. This created a gap between the spot price and the OPEC official price, a development that prompted more and more buyers to make their purchases on a spot basis (Mossavar-Rahmani, 1986, p. 5). This development also gave the spot-related contracts a competitive advantage. While about a third of the internationally traded oil was sold directly on the spot market (up from 10 percent in 1979), almost 85 percent of it was sold with some form of spot-related price formula (up from 15 percent in 1982) (Fesharaki and Razavi, 1986, p. 1). While the spot price in 1979 and 1980 had pushed the official price upwards, it now contributed to the decline of official prices of OPEC (see Figure 25.1). The companies that signed long-term contracts in the early eighties suffered because they had to pay the determined price while there was plenty of oil available in the spot market at substantially lower prices.

The spot market is characterized by short-term contracts, a high rate of turnover, and sensitivity to outside events. The physical spot market is a market for single crude oil cargos, in which it is not unusual for a single cargo to be sold dozens of times before it arrives at a refinery. This renders it difficult to establish to what extent the transactions should be designated spot or contract sales, since a company may purchase oil from a producer according to a contract formula, only to sell some of this oil in the spot market afterwards. Central in this marketing of oil is NYMEX (New York Mercantile Exchange) and IPE (International Petroleum Exchange). However, the market is in no way bound to these bourses, as state-of-the-art information technology makes possible the sale of these ‘paper barrels’ quite independent of geography. The international oil trade subsequently became highly disintegrated. Under increasingly competitive pressure, producers adopted pricing formulas linked to day-to-day fluctuations in spot prices (for a discussion of the immediate role of new trading mechanisms in the 1980s, see Fesharaki and Razavi, 1986, and Mabro, 1987). Under these market conditions individual producers, both OPEC and non-OPEC, had no guarantee concerning the long-term loyalty of their customers. The daily market actors, the traders, obtained an increasingly important position in the market.

The spot market was soon supplemented by a so-called ‘tertiary market’ that included barter, counter-trade, processing arrangements, crude-crude or crude-product packaging, and outright discounts (see

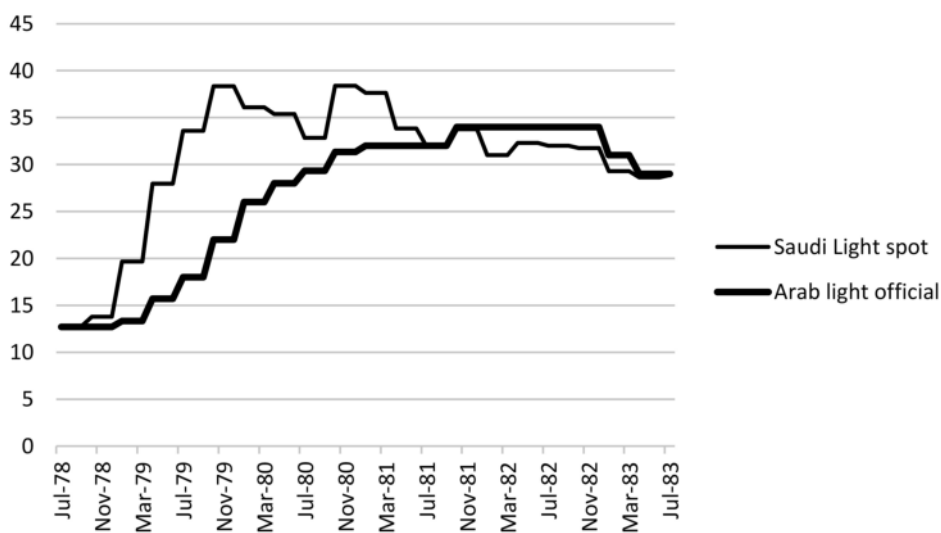


Figure 25.1 Spot and official prices, July 1978–July 1983 (\$/barrel)
 Source: OPEC Bulletin, various issues.

Table 25.1). The OPEC countries faced a dilemma. They did not wish to contribute to a price collapse but at the same time were eager to ensure sales of their own crude. By the mid-eighties the tertiary market was being used by several OPEC countries as a method of giving buyers concealed discounts in various ways. Mossavar-Rahmani calculated this to constitute some 50–55 percent of all OPEC oil sold, while the contracts covered some 30–35 percent and the traditional spot market, only 10–15 percent (all 1985 figures) (Mossavar-Rahmani, 1986, p. 12). The actual price in this market is difficult to determine as all agreements between seller and buyer are veiled in secrecy. However, it can be assumed that the price has been somewhere between the spot price and the official price. This reflects the buyers' willingness to pay a little more for ensuring deliveries, rather than rely on spot sales alone, though not as much as the official price would indicate:

With over half of all OPEC crude oils traded on a discounted basis, the pressure on the remaining crude oils grew. Even though the formal OPEC price structure was prevented from collapsing to tertiary market levels, through the end of 1985 official prices became increasingly meaningless as the share of tertiary transactions continued to gain at the expense of term and spot sales (Mossavar-Rahmani, 1986, p. 15).

This caused Saudi Arabia, which had previously strongly opposed discount arrangements¹ to introduce so-called netback pricing.² Netback agreements are '[t]he sale of crude oil with the buyer paying the producer a price which is dependent on the proceeds obtained from the sale of refined products' (Jenkins 1986, p. 423). This method of price-fixing ensures the refineries a profit on oil purchases, as the price is not decided before the refinery has sold the product and is fixed in such a way that the crude price equals the product price minus refining, transport, insurance, loss, and interest costs in processing of the oil. 'In fact, netback was yet another form of discounting, but importantly for Saudi Arabia, without the stigma of

Table 25.1 Taxonomy of trading

<i>Type</i>	<i>Volume</i>	<i>Duration</i>	<i>Price</i>	<i>Physical condition</i>
Term				
Standard term	Multiple cargoes	Months or years	Government-determined: official sales price (OSP)	Wet
Equity	"	Years	Special arrangements	"
Market-related	"	Months	Adjustable	"
Spot				
Single spot	Single cargo	One-time basis	Set by prevailing market conditions, below or above OSP	"
Daisy chain	"	Multiple transactions of same cargo	"	"
Tertiary	Multiple cargoes	Weeks or months	Discounted below OSP (\$1–2/barrel)	"
Netbacks	Multiple cargoes	"	Spot product price-related	"
Forwards	Single cargo	One-time basis	Set by expectations of future market conditions	"
Futures	Less relevant	Less relevant	"	Paper
Derivatives				
Swaps	"	"	Set to reduce price risks	"
Hedging	"	"	"	"

Source: Mossavar-Rahmani et al. (1988, p. 12) and Roeber (1993, pp. 31–53).

cheating that had come to surround other tertiary transactions' (Mossavar-Rahmani, 1986, p. 15). The drawback of the netback pricing system was its complexity and the transaction costs connected with negotiating individual agreements to match the circumstances of different refiners (Roeber, 1994, p. 262).

A simultaneous development diminished the need for netback agreements. Through communication technology and the frequent publishing of oil-price data (e.g. in *Platt's Oilgram News* and through Reuters), the spot price transparency increased. This caused the value of the crude oil in the product markets to be reflected in the spot price. The netback pricing was subsequently replaced by market-related pricing. In the market-related pricing system, the other features of the contract between the seller and buyer can vary at the same time as the price is set according to the different spot crudes. The contract can be a long-term contract or single cargo deal. The important feature of spot-related pricing is that the frequency of price changes is increased compared with the term market. Spot prices are changed almost constantly. The problem of a mismatch between the contracted price and the market price is thus more or less resolved.

The futures market of the 1990s

During the latter half of the eighties and into the nineties, one of the most prominent features of oil trading has been the increased activity in the 'paper market' or 'semi-paper market'. The forward market is actually a market for spot transactions in which oil is traded for delivery at a future time. So the forward market is a semi-paper market, as it is actual physical crude that is traded. A more genuine paper market is the so-called futures market.³ Futures contracts are at the outset designed for financial purposes. There was no regular futures trading in the oil market until the seventies as the major international oil companies had no interest in such a development. The increase in futures trading in the early nineties was tremendous:

The WTI [Western Texas Intermediate] crude contract was launched by NYMEX in 1983 and is now [1993] trading at a level equivalent to 100 times WTI production The Brent contract on the IPE is traded at 40 times Brent production during the first half of 1993.

(Roeber, 1993, p. 48)

The futures market provides 'those in the physical market with the opportunity to offset the inherent risks associated with their business' (Battley, 1989, p. 27). The futures market might also reduce price uncertainty and thus the possibility of arbitrage (Sykuta, 1994, p. 4). Hedging is the prominent instrument for risk reduction in the futures market. An oil producer can buy himself an insurance against loss from a fall in the oil price by selling an amount of oil on the futures market, which can be regarded as a promise to supply oil on a future date. If the spot price changes, the financial impact on the producer is softened. If the spot price falls, part of the producer's loss is reduced by having locked in part of his production at a higher price. On the other hand, if the spot price rises, the financial benefit of the producer is reduced. Part of his gain is offset by the production locked in at a lower price.

The oil producers outside of OPEC gain market shares rapidly in the 1980s, as OPEC (read: Saudi Arabia) cut production in order to sustain the oil price level. In 1985, OPEC held a market share of less than 28 percent, down from over 45 percent in 1979. The oil producers outside of OPEC had a more commercial perspective on oil trade than some of the dominating producers inside of OPEC. These oil producers and their customers needed a mechanism to protect against future price movements. In the North Sea this led, in 1988, to the creation of Brent futures contracts by the oil industry in consultation with the International Petroleum Exchange. Today, this is known as the ICE Futures Europe. Brent quickly became a global price benchmark for crude oil. The idea is to provide 'stakeholders with continued access to effective mechanisms for hedging oil price risk in changing market dynamics'.⁴ The average daily volume of Brent paper crude contracts has increased tenfold over the last 15 years. The growth in the liquidity and volume in the spot and futures market has made it easier to build new crude-related

financial products. The Brent futures market now includes more than 400 related Brent-based trading instruments.⁵

There are several ‘paper barrels’ for each ‘wet barrel’, and with the price of even long-term contracts related to the price developments of Brent and WTI, the relatively few traders operating in these markets have a disproportionate influence on the day-to-day price developments. None of the OPEC countries, and only a few of the companies, are actually involved in futures trading.

Thus, they are deprived of information and the opportunity to understand the formation of prices. This, of course, makes it more complicated for OPEC and the oil companies to influence the oil-price development. By the end of the eighties, the short-term development of the oil price was left in the hands of the oil market traders. If pessimistic about the OPEC countries’ capacity to govern the market, one could argue that the long-term oil price is nothing other than a series of prices of short-term oil deals, wet- or paper-based. It is fairer to say, however, that the new trading mechanisms have introduced a new layer that the oil producers have to penetrate in order to gain control over the oil price. Previously they could make secret deals with consumers and discriminate among them. Now they have to play the game of convincing the short-term market dealers that they have reason to believe prices will go up in the future, and they should therefore buy more oil in order to hedge against the price increase (Claes, 2001 p. 82).

Financialization of oil and the financial crisis of 2008

When the oil prices increased rapidly in the run-up to the financial crisis in 2008, there were several hearings in the US Congress where oil experts of various shapes and forms testified regarding the impact of financialization on the oil price. One of the more famous testimonies was by Michael W. Masters, who suggested that the inflow and impact of index investors could be compared to the increased demand from China.⁶ Others, such as James Burkhard, suggested that the fundamental reasons are most important. On the issue of speculation, he pointed out that individual non-commercial investors cannot move the price, but that ‘the direction of a given price trend can be accentuated’.⁷ Kevin Book made a similar statement on the relationship between fundamentals and financial investors:

other investors may rely in the absence of empirical evidence on the signals generated by financial markets for futures contracts, in which case the endless trumpeting of rising WTI contract prices may create a ‘feedback loop’ that seems to suggest enduring scarcity.⁸

The president and CEO of NYMEX, James Newsome, disagreed with this view, and stated that ‘non-commercial participants are not providing disproportionate pressure on the long (buy) side of the crude oil futures market’.⁹ The economist James Angel mentioned the dangers of a ban on the paper market: ‘Even if institutions have contributed to the current situation through herd-like behavior at the wrong time, it is not clear that a permanent ban is in the public interest.’¹⁰

In recent years, the most important change to the international price was the removal of the US ban on crude exports. After the advent of US tight oil production there was a deep Brent-WTI spread, in part due to the legacy ban on US exports. Tight oil producers lobbied the government effectively to have the export ban lifted, with the consequence of swiftly removing the deep discount of the WTI to the Brent. The discount has since grown again due to capacity constraints.¹¹ In 2018 there were two events that could become important changes in the future but have so far just been curiosities. The first was that Venezuela introduced a currency, the petro, which is backed by oil assets and uses blockchain technology. And the second is that in March 2018, a crude future denominated in renminbi was launched in Shanghai. Only time will show if cryptocurrencies or the yuan will alter the dollar’s central position in the oil market.

Implications for market behavior

When market actors make simultaneous and instant moves in the marketplace, the behavior of all other actors could be regarded parametrically – in other words, they could be taken as given. Or if the actor should make assumptions about other actors' behavior it would have to be exactly that – assumptions, as no observation about others behavior is possible. However, when the market transactions are extended in time a new kind of uncertainty enters the calculations of market actors. In such a market, actors are concerned not only with the price of the traded good today, but also the price some time in the future; the price of the good today will be influenced by the traders' expectations about the price tomorrow. This price will in turn be influenced by the expectations about the price the day after tomorrow and so on. This does not necessarily change the formation of expectations, but it creates room for more and extended strategic interaction among the market actors.

A rational agent will recognize that the price tomorrow will depend upon the actions of all other agents tomorrow, and hence upon their theories of price formation ... The potential then exists for a rational agent to believe that certain events will affect the price ... simply because (he believes) other agents believe these events matter.

(Burnell, 1989, p. 394)

This makes possible the influence of factors that cannot reasonably be claimed to affect the market fundamentals – such as endowments, preferences, or production capacities – but that *can* be claimed to affect other actors beliefs. Factors that have an effect on the fundamentals are *intrinsic* to the economy, while other factors are *extrinsic*. The activity of the sun in creating sunspots is one such extrinsic factor. 'Sunspots' have thus become the name for such factors in the economic literature. The economic literature on sunspots has primarily been focused on how equilibrium emerges in such markets. The empirical cases have mostly been the stock market and to some extent the foreign exchange market. But commodity future markets, including the oil market, could also be regarded as having the characteristics making the market vulnerable to sunspots.

In such markets price formation can be thought of as a social convention. This idea of price formation as a social convention was developed by Keynes, in his book *The General Theory of Employment, Interest and Money* from 1936:

The essence of this convention lies in assuming that the existing state of affairs will continue indefinitely, except in so far as we have specific reasons to expect a change. ... We are assuming, in effect, that the existing market valuation, however arrived at, is uniquely *correct* in relation to our existing knowledge ... and that it will only change in proportion to changes in this knowledge.

(Keynes, 1936, p. 152)

Keynes then goes on to discuss different weaknesses in this convention. For the purpose of this paper one such weakness is particularly important. Keynes argues that a

conventional valuation which is established as the outcome of the mass psychology of a large number of ignorant individuals is liable to change violently as the result of a sudden fluctuation of opinion due to factors which do not really make much difference. ... In abnormal times the market will be subject to waves of optimistic and pessimistic sentiment, which are unreasoning and yet in a sense legitimate where no solid basis exists for a reasonable calculation.

(Keynes, 1936, p. 154)

This more than 80-year-old insight from one of the greatest minds of economics seems to point directly to the present situation both in the oil market and in financial markets in general, suggesting that sunspot markets are volatile with inherently unpredictable dynamics. Governing such markets seems a tall challenge. Actors seeking to influence such markets will have to convince the oil traders that their previously held perceptions are wrong. Utterances made for instance by politicians could be regarded as *extrinsic* factors influencing the market convention, not in themselves altering any fundamental parameters of the oil market but influencing the assumptions held by market actors, in particular the traders, about the future conditions of these parameters. By influencing the traders' assumptions about the future, the sunspots (read: political statements) influence the price of oil in the forward and future markets. There might be a resurgence in this way of thinking of markets. In his manifesto statement, the political scientist-turned-fund manager W. Ben Hunt proposes that investors should look beyond the traditional alpha (idiosyncratic) and beta (market) elements of returns, and look more at the epsilon (error) element. Hunt's view is that game theory is an essential complement to traditional investment methodology. In his view of the market, it is important to understand what he calls narrative and common knowledge. Common knowledge is the 'consensus view of the consensus view'. This is intuitively a key part of understanding markets, but as Hunt points out, 'there is nothing – absolutely nothing – in the standard model of modern portfolio theory or the fundamentals of the market or any alpha or beta factor that can help you with this effort'.¹² In other words, active oil market participants should also play the players and not just the barrels.

Although most, or all, observers and academics agree that the market determines the oil price, there is some disagreement as to how free the market really is. With regard to the latter, Robert Mabro (1992) suggests that the market price of oil is not really a free market price because it is a market with upper and lower bounds that are agreed upon in practice between major importers and major exporters. In other words, the market sets the price within certain boundaries; the market 'does not have the freedom to bring prices down to the competitive cost floor and to take this floor as the normal level around which fluctuations will occur'. (Mabro, 1992). This argument is much easier to accept the less one sees the boundaries as actual hard boundaries.

There is also great disagreement on the relationship between spot prices and futures prices and if and how financial players impact the price (level and volatility). Plenty of academic work has been done to try to analyze the effect financial investors have on the oil futures market. There is no consensus as to whether speculation increases the price, reduces volatility, creates volatility, has no effect on price at all, or if it has an effect but that it is unknown.

In the speculation reduces volatility camp we find Chicago economists such as Gary Becker¹³ and Milton Friedman (1960) providing conceptual arguments for this view. Brunetti and Büyüksahin (2009) found, based on statistical analysis of CFTC numbers, that speculation does not cause price movement and that it reduces risk. In another CFTC publication, Harris and Büyüksahin support this view: 'Our results (...) find that herding among hedge funds is countercyclical and does not destabilize the crude oil futures markets, respectively, during recent years' (Harris and Büyüksahin, 2009). Their findings also suggest that index trades do not impact prices.

In the academic discussion, Dwight Sanders and Scott Irwin found that the algorithm used by Masters incorrectly estimates the gross index investment, and that 'the deviation in the first half of 2008, the period of greatest concern about the market impact of index investment, is directionally wrong' (Manera, 2013). Rouwenhorst and Tang (2012, pp. 449–467) suggest that index investors do not impact the market: 'Moreover we find no evidence of a positive feedback from index investor positions to commodity returns.' Further, Fattouh and Mahadeva (2012a) do not find support for financial actors having an 'important effect on oil market variables' or that their participation in the oil market 'harmed final consumers'. Fattouh et al. (2012) have done a review of the key findings from the academic work done on financialization of the oil markets. Their key findings included that there is 'clear evidence of the increased financialization of oil futures markets', 'no evidence that oil futures prices significantly improve the out-of-

sample accuracy of forecasts of the spot price of oil', 'the simple static model that has been used to explain how an influx of financial investors may cause an increase in the spot price of oil is inconsistent with dynamic models of storage', and that 'the presence of index funds has, if anything, been associated with reduced price volatility'.

Edward Krapels separates those who 'believe the financial markets have a sui generis impact on oil prices' and those who do not.¹⁴ The authors of this article are firmly in the sui generis camp. Our belief is that technology and financial markets make it easier and faster to trade on sentiment or psychological factors. It seems logical that more activity at a faster pace is likely to increase volatility. Financialization and technology make it possible to trade much more often than in an analogue world. John Parsons (2010) supports this view: 'I do not argue that the oil price spike was exclusively caused by financial speculation, but financial speculation is part of the story.' Sarah Emerson points out the change in pace that has taken place: 'Futures markets and the liquidity provided by speculators have transformed the global oil market from one dominated by month-to-month pricing to one driven by minute-to-minute pricing.'¹⁵

The chief economist at the CFTC, Jeffrey Harris, pointed out that 'While speculation is critical to well-functioning markets, excessive speculation can be detrimental to the markets.'¹⁶ This is in line with OPEC statements, e.g. when 'volatility becomes extreme, with wild and uncontrollable swings, (...) there are no winners — apart from the unscrupulous speculators that cause it'.¹⁷ The question, of course, is what impact does this have on OPEC members?

Implications for OPEC's market control

In general, these changes in international oil trade make it more complicated for producers, consumers, and companies to influence the oil price. By the end of the 1990s, the short-term development of the oil price was left in the hands of the oil market traders. It still is. Thus, all international oil companies now experience a situation where they make investments decisions without any control over the price of the product. With the recent volatility of prices combined with the increasing size of investments needed for development of new resources, like offshore Brazil, financial strength and risk willingness become important aspects of companies' competitiveness.

Under these market conditions, individual producers, both OPEC and non-OPEC, have no guarantee of the long-term loyalty of their customers. Nor does it make any sense for them to isolate the security of supply of an individual consuming country. The oil traders have gained an increasingly important position in the short-term market, making it very hard for the authorities of producing or consuming countries to determine the actual flow of traded oil. Thus, long-term supply stability should not be confused with price stability. Supply stability is primarily aimed at securing predictable volumes of oil over an extended period; price stability is primarily a matter of guaranteeing predictable costs. One may very well have a situation with ample supplies in which the price fluctuates widely. In fact, during the last three decades there have hardly been any actual physical disruptions of oil supplies. Even when the oil price was \$147 in the summer of 2008, no refinery had any difficulty acquiring crude supplies. No consumer suffered lack of deliveries.

As mentioned above, the impact of financialization on prices is inconclusive in the literature. If the impact on the price is upwards pressure, it means that the need for OPEC to enforce quotas is less than it would have been otherwise. In other words, if there is upwards pressure on the price due to financialization, OPEC gets high prices without managing the supply side as much as it might do otherwise. OPEC can increase production, and the problem with member states producing more than the quota is much less pronounced. If true, this is a good thing for OPEC. In extremis, this argument becomes absurd. It would mean that if enough index investors wish to hold oil, the increases in the supply side would not matter for the price. Intuitively, it seems likely that paper demand increases the price on the margin, but that an important question, as indicated in the discussion above, is whether or not paper demand is constant or

varies with the price. If the propensity to hold paper increases and decreases with the price, index investors can be accelerators of price changes.

If the effect of financialization is increased volatility, the impact on OPEC is much more complicated. Volatility means that the price changes are sharper and shorter in period than changes due to demand shocks or supply shocks. Volatility can have many causes, e.g. supply shocks or changed sentiment. When prices are very high, OPEC is blamed for not producing enough, and when prices are low, OPEC is blamed for producing too much. Volatility means that the price is sometimes very high and sometimes very low and sometimes it just varies a little bit. In a sense, volatility implies that the price represents more noise than signal. Separating the signal from the noise is very difficult, as is underscored by the inconclusiveness in the academic debate.

OPEC Statute Article 2 paragraph A states that ‘The Organization shall devise ways and means of ensuring the stabilization of prices in international oil markets with a view to eliminating harmful and unnecessary fluctuations.’ If the organization wishes to have a stated or unstated price target range, there is a great chance that responding to the volatility will lead to managing supply too much, too soon or too little, too late. In other words, volatility due to financialization runs the risk of increasing supply/demand imbalances that could make the distance between the peaks and troughs in prices even greater.

Conclusion

Contemporary developments in the petroleum market are the result of a complex and dynamic inter-relationship between different factors: unexpected increases in demand over recent years which, together with other factors, contributed to rising prices that have attracted newcomers, either with short-term profit motives or with long-term aims, to set up production and/or marketing and distribution channels; and the emergence of a financial crisis that is being globalized and seriously affected the ‘real economy’ at the beginning of 2009. The international oil market of today differs along several important structural features compared with the international oil market of the 1970s. In the short term, the oil traders are in charge of the price formation. The ownership of oil cargoes is potentially impossible to trace from producer to consumer. In this respect, the producer and the consumer are detached from each other. Setting the price of oil by political decision is no longer an option either for oil producer or for oil consumers. In the past, the producers could make secret deals with consumers and discriminate among them by giving preferred customers a better price. Today, the only way to influence prices is to change the traders’ beliefs about the future price of oil. Political actors are of course not totally without means for achieving this, but the days of producer-determined contract prices covering most of the market are gone forever.

Financialization has increased in the last decade and looking back it seems like the arc of history is pointing towards ever more capitalism and financialization. This may be true, but these things change over time, and there is certainly nothing deterministic about this trend. Francisco Parra (2010, p. 335) writes that ‘Price in the industry has always been a political price, in the broadest sense of the term.’ Consequently, if circumstances change, the current trends in the oil market can be altered significantly by politics or other factors.

Increased financialization has on the whole been good for OPEC producers. The members get a fairer price for their crudes, which are sophisticatedly adjusted for e.g. the assay. Volatility can be an issue for certain producers, but as Luciani (2011) has pointed out, measures can be taken to offset some of these problems. The thing is, however, that oil producers wish to be oil producers rather than passive rentiers – and this involves being exposed to all the risks that the oil industry entails.

For OPEC, at least for Saudi Arabia, Kuwait, and the United Arab Emirates, increased financialization is a decent bargain. Volatility entails some risks of overshooting if the organization tries too actively to maintain price floors and ceilings, but it is not too problematic. Additionally, blaming financial markets and

speculators is probably good politics for OPEC. It is, however, out of touch with the underlying reality of the oil-pricing regime. Like Captain Renault in the 1942 film *Casablanca*, it seems OPEC is shocked to learn that gambling is going on in the oil market, while happily collecting its own winnings.

Notes

- 1 'I think one of the very few countries that is still selling on terms of contracts is Saudi Arabia', interview with Sheik Yamani in *Petroleum Intelligence Weekly*, 17.06.1985.
- 2 The concept has been used earlier by other producers (e.g. Nigeria), but not in the same strategic way that Saudi Arabia did in 1985.
- 3 'It is in some ways helpful to see forward markets as unripe futures markets. There is a logic in the evolutionary sequence that runs from spot to forward, and on to futures' (Roeber, 1993, p. 45).
- 4 www.theice.com/brent-crude.
- 5 www.theice.com/brent-crude#related-brent-products.
- 6 Masters, M. *Testimony before the Committee on Homeland Security and Governmental Affairs*. United States Senate, 20.05.2008.
- 7 Burkhard, J. *Statement to the Committee on Energy and Natural Resources*. United States Senate, 03.04.2008.
- 8 Book, K. *Statement to the Committee on Energy and Natural Resources*. United States Senate, 24.06.2008.
- 9 Newsome, J. *Testimony before the U.S. Senate Committee on Homeland Security and Governmental Affairs*. United States Senate, 24.06.2008.
- 10 Angel, J. *Testimony before the U.S. Senate Committee on Homeland Security and Governmental Affairs*. United States Senate, 24.06.2008.
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- 15 Emerson, S. *Background article to statement to Committee on Energy and Natural Resources*, 03.04.2008.
- 16 Harris, J. *Statement to the Committee on Energy and Natural Resources*, 03.04.2008.
- 17 OPEC Bulletin Commentary. 2014. 'Counting the cost of speculation'.

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OPEC as a political club

Jeff D. Colgan

Popular wisdom holds that the Organization of the Petroleum Exporting Countries (OPEC) can and does manipulate the global price of oil, but economic studies investigating OPEC's market impact have had difficulty finding conclusive evidence. This generates two questions. First, does OPEC operate as a cartel, meaning that it significantly restricts its members' oil production in order to affect prices? Second, if OPEC is not actually a cartel, why do so many people believe that it is, and what is it really doing?

This chapter shows that OPEC is not a real cartel. True, in OPEC's early days from 1960 to 1973, the organization facilitated some cooperation between its members. The 1973 oil crisis gave the organization a lasting reputation for having significant control over world oil prices. In 1982, it began to assign formal production quotas to limit oil supplies. Since then, OPEC has failed as a cartel. Economists define a cartel as a group of producers that creates agreements about quantities to produce or prices to charge and, further, that it 'must not only agree on the total level of production but also on the amount produced by each member'. (Mankiw, 2011, p. 351). I conduct four empirical tests in the period 1982–2009 to see if OPEC meets that definition and consistently find that it does not. Perhaps OPEC could restrict oil supply in principle, but it did not do so in practice in that period. This is due in part, but not principally, to endemic cheating by OPEC members (i.e. oil production in excess of their quotas). A cartel needs to set tough goals and meet them; OPEC sets easy goals and fails to meet even those.

The concepts of cartel, economic influence, and price influence need to be distinguished. A cartel is an organization that reduces its members' production levels from what they would have been, counterfactually. By doing so, a cartel can have economic influence, meaning that it substantially affects average prices or production amounts over the long run, relative to the counterfactual. OPEC is neither a cartel nor has economic influence. It does, however, have influence on market prices in the short term. It does so in part because oil prices are affected by market psychology in addition to 'fundamentals' like production levels, and OPEC's statements can affect market psychology. OPEC also affects prices by acting like a spokesperson, revealing information about key market actors, particularly Saudi Arabia.

If OPEC does not operate as a cartel, why do so many people believe that it does? The idea of OPEC as a cartel is a 'rational myth' that supports the organization's true principal function, which is to act as a political club that generates benefits for its members. Scholars have found that various organizations adopt rational myths (McNamara, 2002; Meyer and Rowan, 1977). OPEC's current role is obscured in part by the complexity of the world oil market, in part by the fact that one of its members, Saudi Arabia, probably does have some market power on its own (distinct from that of the organization to which it belongs), and

in part by misdirection by OPEC itself. OPEC's perceived market power is a useful fiction that generates political benefits for its members with domestic and international audiences.

I test my argument using a cross-national data set on diplomatic recognition, and show that OPEC membership is significantly correlated with increased diplomatic representation from other countries (e.g. ambassadors). Consequently, policymakers within OPEC have no incentive to undermine the idea that OPEC economically steers the world oil market. They are not necessarily lying, but they have an incentive to behave in ways that are consistent with the cartel idea so long as that behavior is not too costly. The incentive is that OPEC's cartel image boosts its members' international prestige and provides other political benefits. Other knowledgeable actors outside of OPEC fail to dispel the myth for various reasons. In sum, the story of OPEC is mostly about politics, not economics. The evidence that OPEC is not a cartel calls into question research in political science that is based on that premise (Blaydes, 2004; Alt, Calvert and Humes, 1988).

OPEC's cartel image

OPEC was established in 1960. Its founders, modeling it after the Texas Railroad Commission, hoped that it would act as a cartel (Parra, 2004; Yergin, 2008). Initially this proved impossible because OPEC member countries did not gain control of their own oil production decisions until the 1970s (Dietrich, 2017; Claes, 2001; Garavini, 2011). Collectively, OPEC produces about 40 percent of the world total (41 percent in 2009), though individually even its largest producer has a relatively small market share (Saudi Arabia, 12 percent)¹. If OPEC were able to cooperate flawlessly, it might exert significant market influence. The significant oil price increases of the 1970s convinced many observers that OPEC had become the cartel that its founders envisioned (Krasner, 1974; Adelman, 1982; U.S. government reactions in Qaimmaqami and Keefer, 2011).

Yet over time many studies have cast significant doubt on the idea that OPEC is a cartel (for instance Johany, 1980; Dahl and Yücel, 1991; Barsky and Kilian, 2004). Some scholars suggested a 'dominant producer' model, namely that Saudi Arabia alone exerted market power, because it seems to be the only state with sizeable surplus production capacity (Moran, 1982).² More recently, scholars have noted a series of limitations on OPEC's effectiveness³ (see Kaufman et al., 2008; Hyndman, 2008; Goldthau and Witte, 2011; Brémond et al., 2012; for broader studies of global energy governance, see Colgan et al., 2012; Claes, 2001; Colgan, 2009; Colgan and Van de Graaf, 2015; Colgan and Van de Graaf, 2017).

Still, many scholars continue to believe that OPEC is a cartel, albeit imperfect. Hyndman asserts, 'OPEC is obviously a cartel that restricts output in order to obtain super-competitive profits,' an assertion shared by other economists (Hyndman, 2008, p. 812; Smith, 2009). This is true also among many political scientists (Blaydes, 2004; Shaffer, 2009). Given the extent of scholarly debate, it is perhaps not surprising that many journalists and policymakers continue to view OPEC as a cartel. Consequently, we need to have a fresh look at the evidence.

Is OPEC a cartel? Tests and results

Many observers note that cheating on OPEC quotas is widespread but pay less attention to other problems that might be even more important, such as the extent to which OPEC sets targets that are actually different from what an actor would have done counterfactually (Downs et al., 1996). I consider four major tests of OPEC's market impact. The tests focus exclusively on OPEC's impact on oil production, which is a necessary element of cartel behavior (Mankiw, 2011, p. 351).

The key counterfactual question for evaluating OPEC's market impact is: what would each member state's oil production levels have been had OPEC not existed at all? Counterfactuals are, by definition, unobservable. So, we cannot answer this question directly, but we can assess it indirectly by looking for

signs of how a cartel would change its members' behavior. This is a tricky task. In a situation where demand is increasing, even if OPEC production rises, OPEC might be restraining production compared to the counterfactual. Yet there are certain patterns that ought to be true regardless of the market situation.

What evidence should we observe if OPEC is a cartel? A gap between market price and marginal cost of production is not by itself evidence of a cartel. Instead, we need to see signs that the organization is cooperating to restrict production (to drive prices up).⁴ We should see the following kinds of evidence: new members of the cartel have a decreasing or decelerating production rate (test #1); members should generally produce quantities at or below their assigned quota (test #2); changes in quotas should lead to changes in production, creating a correlation (test #3); and members of the cartel should generally produce lower quantities (i.e. deplete their oil at a lower rate) on average than non-members of the cartel (test #4).⁵ Failure to observe any of these phenomena would cast doubt on OPEC's status as a cartel, though no one is totally determinative. The fourth test is perhaps the strongest because it is difficult to imagine how an organization that does not restrict output compared to non-members could be called a cartel – how else could it increase average prices?⁶ OPEC fails all four of the tests.

First, how does joining OPEC affect the oil production of its new members? I answer this question using an event history method. If OPEC is having a constraining influence on oil production, states that join OPEC should have a decreasing or decelerating oil production rate. OPEC does not appear to have such an effect. Figure 26.1 shows the average oil production rate of all states in the five years before they join OPEC and the five years after they join OPEC. Each state's oil production is standardized to a value of 100 in the year that it joined OPEC so that the relative increase or decrease can be compared. The average production rate increases at a similar rate before and after the state joins OPEC – thereby providing little indication that OPEC constrains oil production.

The second test focuses on cheating. A strong cartel would have little cheating, but OPEC cheating is endemic. Over the period 1982–2009, the organization as a whole overproduced a staggering 96 percent of the time. I use monthly production data, drawing on data from the US Energy Information Agency.⁷ Table 26.1 shows the variation among OPEC members. All but two members overproduced more than 80 percent of the time. Moreover, some OPEC countries manage to avoid having quotas for significant periods of time.⁸ The magnitude of overproduction varies over time and across states, but it is not trivial: on average, the nine principal members of OPEC produced 10 percent more oil than their quotas allowed.⁹ This is equivalent to 1.8 million barrels per day, on average. Even on the relatively rare occasions when member countries are not overproducing, the root cause is often involuntary production constraints such as a strike or accident, rather than a conscious decision by the government to obey its OPEC quota.

One might wonder how much cheating actually undermines OPEC. One possibility is that it anticipates a certain amount of cheating and sets quotas accordingly. The real questions are whether OPEC quotas affect production rates, and whether they are lower than the counterfactual in which no quotas were set. The remaining tests investigate those questions.

The third test reveals that OPEC quotas have almost no effect on production levels. Returning to Table 26.1, it shows the R-squared value of a linear bivariate time-series regression between changes in an OPEC member's production and changes in its quota.¹⁰ For all but two of the states (Libya and Algeria), changes in the OPEC quota are *not* correlated with production at standard thresholds of statistical significance. The R-squared for the nine major OPEC producers as a group was just 0.018, meaning that at most 1.8 percent of the variation in the month-to-month changes in this group's oil production can be explained by changes in their OPEC quotas. In other words, at least 98 percent of the variation is explained by factors other than changes in their OPEC quotas.

Even in the face of this evidence, one could still argue that OPEC acts as a cartel in one of two ways. First, one could argue that OPEC states change production levels between OPEC meetings because they anticipate forthcoming changes in the quotas (Parra, 2004, pp. 321–322). Second, one could argue that even if OPEC's quota system is entirely meaningless, OPEC still affects oil production over the long term

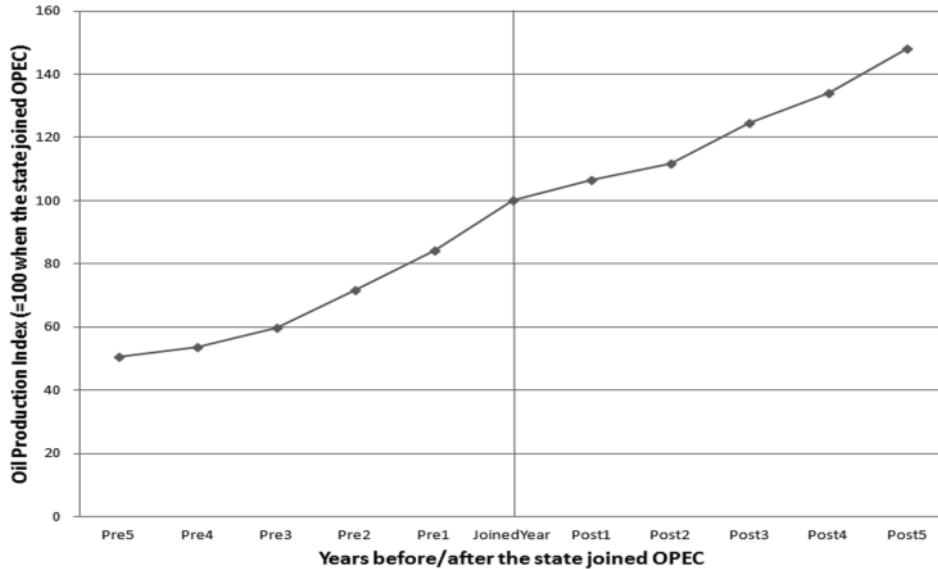


Figure 26.1 Impact of joining OPEC on oil production

Source: Colgan, Jeff D. (2014). *The Emperor Has No Clothes: The Limits of OPEC in the Global Oil Market. International Organization* 68(3), pp. 599–632 (doi:10.1017/ S0020818313000489). © Cambridge University Press. Reprinted with permission.

Table 26.1 Relationship between OPEC quotas and production, 1982–2009

OPEC member	% months production exceeds quota	Correlation between production and quota*		
		Beta coefficient	P-value	R-squared
Algeria	100%	0.105	0.035	0.014
Iran	72%	0.002	0.981	0.000
Iraq**	82%	0.065	0.819	0.000
Kuwait	90%	0.106	0.450	0.002
Libya	83%	0.183	0.038	0.014
Nigeria	88%	0.138	0.383	0.002
Qatar	90%	0.118	0.245	0.004
Saudi Arabia	82%	0.138	0.130	0.007
UAE	96%	-0.140	0.170	0.006
Venezuela	77%	0.095	0.472	0.002
OPEC-9 (excludes Iraq)	96%	0.153	0.017	0.018

Source: Colgan, Jeff D. (2014). *The Emperor Has No Clothes: The Limits of OPEC in the Global Oil Market. International Organization* 68(3), pp. 599–632 (doi:10.1017/ S0020818313000489). © Cambridge University Press. Reprinted with permission.

** Up to March 1998 only. Iraq was not assigned an OPEC quota after March 1998.

because it encourages the adoption of a slow depletion policy and underinvestment in production capacity (Smith, 2009). Both of these propositions have a clear empirical implication: the oil production or depletion rate of OPEC member states ought to be significantly less than the rate of comparable non-OPEC members. This leads to my fourth test.

A country's depletion rate is equal to its oil production divided by its proven oil reserves. Broadly speaking, depletion rates will vary according to three supply-side factors (in addition to global demand for oil): the business climate of the producing country; the 'lift costs' of oil production (costs of getting oil to the ground); and the government's depletion policy. OPEC membership could affect depletion policy, but so could other factors.

I investigate the cross-national variation in depletion rates over a 30-year period, 1980–2010.¹¹ The analysis includes all 42 oil-producing states for which data are available.¹² The analysis includes the *OPEC*, a dichotomous measure indicating whether the state is a member of OPEC in a given year, and several other explanatory variables. The latter includes *fiscal strength*, measured by the natural log of oil reserves per capita, the state's *investment risk* (which affects the ease with which international businesses can operate), and *world economic growth*, a proxy for global demand for oil. Details of the analysis and robustness checks are described elsewhere (Colgan, 2014).

Table 26.2 presents the results of regression analyses. Model 1 shows a simple bivariate model that indicates that OPEC membership is statistically associated with low depletion rates, as expected by the conventional 'OPEC-as-cartel' hypothesis. The statistical significance of OPEC membership disappears in model 3, however, when other variables are added in the subsequent models. As expected, *investment risk* and *fiscal strength* are negatively correlated with the depletion rate, reflecting the fact that poor investment climates inhibit oil production (Jensen and Johnston, 2011), and oil-rich states have long time horizons for depletion.

The findings imply that, to the extent that OPEC members under-produce compared to non-OPEC members, they do so because of other factors in the model (e.g. fiscal strength, investment risk) that have nothing to do with their OPEC membership. Some OPEC members might restrict their depletion rate as a conscious act of policy, but they appear to do so out of their own self-interest, without institutional support from OPEC. For instance, Saudi Arabia appears to maintain spare production capacity that it uses strategically to alter the oil supply (Yergin, 2008; Parra, 2004). Models 4 and 5 provide supportive evidence about Saudi Arabia's strategic behavior. As in all statistical models, it is impossible to affirm the null hypothesis (i.e. to *prove* that OPEC has no impact) but there is no evidence that OPEC is having a causal impact.

One other striking feature of the market for oil is its remarkable resilience to the impact of international events such as wars and economic sanctions. Although wars do matter in some circumstances (e.g. Kuwait in 1990), it requires massive violence for disruptions to occur, and even then they are quite short lived. International sanctions, such as those placed on Angola, Libya, Syria, Sudan and Iran, appear to have had very little impact on oil output.

In sum, I used four tests to try to identify the market impact of OPEC, and each test returns the same basic result: there is no evidence that OPEC is restricting its members' oil production rate as a cartel would.

Understanding OPEC's persistence

If OPEC is not a cartel, why does it live on and what exactly is it doing? I argue that OPEC can be understood as a political club that generates diplomatic and other political benefits for its members and that its cartel reputation is an integral source of political strength for the organization. It therefore sustains a 'rational myth'. A rational myth is an idea that is illusory or false but persists in part because some actors have incentives to sustain it (McNamara, 2002). Some non-OPEC actors realize that this image is

Table 26.2 Regression analysis on states' oil depletion rates, 1980–2009

	(1)	(2)	(3)	(4)	(5)	(6)
OPEC member – all	-3.9569 (-4.08)**		-0.733 (-0.76)			-0.81 (-0.84)
Saudi Arabia				-1.625 (-1.59)	-1.734 (-1.26)	
OPEC member – non-Saudi				-0.683 (-0.71)		
OPEC core member		-			-0.911 (-0.6)	
OPEC non-core member					-0.627 (-0.62)	
Polity score		0.039 (0.73)	0.034 (0.68)	0.03 (0.59)	0.028 (0.5)	0.052 (0.91)
World economic growth		0.051 (0.76)	0.044 (0.67)	0.045 (0.68)	0.046 (0.68)	0.047 (0.71)
Fiscal strength		-0.992 (-4.42)***	-0.91 (3.18)***	-0.905 (-3.15)***	-0.892 (2.68)**	-0.905 (3.16)***
Investment risk		-0.084 (-2.59)**	-0.079 (-2.33)**	-0.08 (-2.36)**	-0.081 (-2.4)**	-0.079 (-2.37)**
International war		1.097 (0.8)	1.155 (0.86)	1.112 (0.83)	1.043 (0.69)	1.104 (0.86)
International sanctions		-0.649 (-1)	-0.61 (-0.98)	-0.654 (-1.05)**	-0.677 (-1.1)	-0.57 (-0.92)**
Lift cost						-0.17 (-1.09)
Observations	1286	993	993	993	993	993
R-squared	0.181	0.373	0.376	0.377	0.377	0.379

Source: Colgan, Jeff D. (2014). The Emperor Has No Clothes: The Limits of OPEC in the Global Oil Market. *International Organization* 68(3), pp. 599–632 (doi:10.1017/ S0020818313000489). © Cambridge University Press. Reprinted with permission.

Notes: t-scores in parentheses (robust standard errors clustered by state). * significant at 10%; ** significant at 5%; *** significant at 1%.

incorrect, but few of them have strong incentives to contradict it. Most people simply do not know enough about the details of OPEC and quite rationally rely on others' judgment. Given that (almost) no one directly and forcefully contradicts the idea that OPEC is a cartel, the myth persists.

OPEC's incentives to continue as a political club

For OPEC states, the belief that they are members of a cartel generates significant political benefits, both at home and abroad. So long as OPEC is viewed as powerful, its leaders can claim credit at home for their 'economic stewardship' of the global economy. Leaders of OPEC member states have sought to take credit for their rising economic fortunes in exactly this way. For example, Venezuelan President Hugo Chavez, who was elected in 1998 as oil prices were plunging, argued that he revitalized OPEC and thus caused world oil prices to rise. This narrative gave Chavez a significant political asset in Venezuelan domestic politics. Similarly, Iranian leaders have sought to use OPEC to take credit in the eyes of the Iranian public

(Colgan, 2014). OPEC thus serves as a useful tool for state leaders when communicating with their domestic constituency.

In addition, the perceived power of OPEC allows its members to reap political rewards in terms of diplomatic influence and attention paid to them. Perceived power brings prestige, and prestige is the currency of international diplomacy. One empirical implication of this hypothesis is that OPEC members ought to have greater diplomatic recognition by other countries than comparable non-OPEC countries, all else equal.

The evidence suggests that OPEC helps its member states receive more diplomatic recognition than they otherwise would. For instance, Ecuador is noteworthy because it joined, left and then rejoined OPEC, unlike most other OPEC members. Ecuador joined OPEC in 1973, and by 1975 11 countries had newly sent diplomatic representatives (an ambassador, *chargé d'affaires*, or other representative), whereas only one had withdrawn its representative (Ethiopia).¹³ The 11 countries with new representatives – Canada, Haiti, Luxembourg, East Germany, Poland, Hungary, Bulgaria, Romania, Russia, South Korea and India – represented a broad cross-section of the world, geographically, economically and politically. By contrast, when Ecuador suspended its OPEC membership in 1992, it sustained a net *loss* in diplomatic representation. When Ecuador rejoined OPEC in 2007, it again enjoyed a net gain in diplomatic representation, this time consisting of 18 new embassies or consulates over the next five years. Similarly, when Gabon joined OPEC in 1975, it gained diplomatic representation from 19 new countries and lost representation from four; when Gabon left OPEC in 1992, it gained representation from only one country and lost it from four others.

These examples are illustrative of a wider pattern. Statistical tests confirm that OPEC generates diplomatic benefits for its members, even after controlling for many other potentially confounding variables (Colgan, 2014). For instance, the statistical models controlled for the following variables: each state's military capabilities; each state's status as a nuclear power; the political regime type of each state; the geographic distance between the states in the dyad; whether the dyad contains an alliance and/or a political rivalry; and whether the state is an oil producer (regardless of OPEC membership). In short, OPEC membership is strongly and positively correlated with levels of diplomatic recognition, indicating that OPEC members are more likely to be diplomatically recognized (and reciprocally, to recognize other states) than comparable non-OPEC members. This finding is true for all OPEC members, not just Saudi Arabia.

One striking result is the magnitude of the impact that OPEC has on diplomatic representation. The results suggest that OPEC membership has roughly the same impact on diplomatic representation as having nuclear weapons. On average, OPEC membership is correlated with an increase in diplomatic representation from nine additional states, compared to an equivalent (oil-producing) country that is not an OPEC member.

The value of increased diplomatic representation is hard to gauge, but it is not trivial. For instance, many of the new diplomatic connections were with relatively rich countries, which therefore represented opportunities for increased trade, investment and tourism. Specifically, about 40 percent of the countries that sent diplomatic representatives to a new member of OPEC had income (GDP per capita) higher than the world average. Trade and investment can be beneficial economically (Colgan, 2005). Moreover, during the Cold War, the new diplomatic connections spanned the divide between East and West. Many OPEC members were otherwise rather marginal to global geopolitics, so diplomatic connections to both sides of the Cold War could bring valuable information and perhaps diplomatic leverage. Diplomatic recognition also brings a certain amount of status and prestige that is hard to measure objectively.

Given the political benefits OPEC generates for its members, they have no incentive to expose OPEC as an ineffective cartel. To the extent that they are aware, they are willing to go along with the rituals of acting as a cartel. There is also the potential for cognitive dissonance, in which policymakers inside OPEC do not reconcile their understanding of the oil market with their desire to believe in OPEC as a cartel.¹⁴

Note that in recent years, OPEC staff have sought to avoid use the word cartel because of various legal challenges they face in the EU and the United States. Even so, they publicly say that OPEC aims to ‘coordinate and unify the petroleum policies of its Member Countries and ensure the stabilization of oil markets’,¹⁵ and it does so by attempting to prorate supply – which is exactly what a cartel aims to do.

Non-OPEC members’ incentives and beliefs

Why hasn’t the rest of the world seen through the ‘rational myth’ of OPEC as a cartel? Informed oil market participants outside of OPEC such as commodity traders and oil companies have the analytical skills and data to assess OPEC’s behavior and impact. They might be able to see that OPEC is not a functioning cartel. But market participants and commercial analysts are not necessarily interested in the question of whether it is a cartel. Instead, they want to know whether at least one of the members of OPEC has some market influence at least some of the time. The answer to this is probably yes. Saudi Arabia appears to have market power: it claims to have significant spare capacity, which is plausible; it depletes its oil quite slowly and probably far below its marginal cost of production; and it makes major, observable changes to its oil production levels that correlate (imperfectly) with its statements about its desire to loosen or tighten global oil supply. Other states like UAE and Kuwait might also have market power, though the evidence is less clear. The question of whether at least one member of OPEC has market power is important to non-OPEC market participants because it means that the behavior of OPEC (as a group, not as an organization) can affect market prices and production, and thus the strategies of oil market participants.

Consequently, market participants probably understand, to varying degrees, that OPEC is not a cartel, but they do not care. They still pay attention to OPEC for signals about present and future Saudi behavior. This is comparable to the way observers pay attention to the White House press secretary for clues about the president’s thinking, even though the press secretary has no real power of his/her own. Thus, OPEC’s announcements could affect market perceptions, which matter in the short term for commodity traders (Hyndman, 2008). It is rational for market participants to observe OPEC even if they believe that the organization itself does not alter market fundamentals. Instead, they are principally interested in OPEC as shorthand for ‘the members of OPEC’, just as other market analysts are interested in the BRICs as shorthand for ‘Brazil, Russia, India, and China’ without implying that these countries are in some way colluding.

What about other informed analysts, such as academic scholars? Scholars have difficulty reaching a unanimous or even dominant view on questions that involve complex causality and where experimental testing in laboratory conditions is infeasible. Indeed, scholars face professional incentives to generate debate by providing novel arguments and contrarian empirical findings. The topic of OPEC as a cartel is causally complex. Not surprisingly, consensus has been difficult to achieve, as the literature reviewed earlier indicates. Given the ongoing debate among scholars, and the fact that academics often find it difficult to sway public opinion even on matters where there is considerable scholarly agreement, it is not surprising that they have failed to persuade non-academics to change their view about OPEC. The problem is made worse by the incentives facing journalists. Certain journalists might have the knowledge necessary to question the cartel myth, but they seem to find OPEC’s image as a cartel useful: it provides a simple, convenient narrative to explain increases and decreases in the price of oil.

Government analysts are also well informed, and their failure to realize that OPEC does not operate as a cartel and/or to forcefully articulate that point to their political masters is more surprising and puzzling. It is not entirely clear whether the problem is one of knowledge or of communication. Government analysts are presumably capable of conducting the same analysis this paper describes, but to date either that analysis has not been done or it has not been widely disseminated. Personal discussions with various officials suggest that there is a wide range of beliefs about OPEC in the US government, and some analysts are indeed

quite skeptical of OPEC's ability to behave as a cartel. Even so, the modal belief of government analysts seems to be that OPEC is a semi-functional cartel (for details, see Colgan, 2014).

The mistake by government analysts should be understood in light of the topic's analytic complexity. For instance, in the first half of 2008, oil prices rose to over \$140 per barrel in July, before plunging to below \$40 per barrel in January 2009. OPEC's oil production rose significantly as prices increased and fell when prices were falling. This looked to many like evidence of OPEC's cartel behavior. Yet OPEC's behavior might be simply a profit-maximizing response to price changes – non-OPEC behaved almost exactly the same way. Moreover, only one OPEC country (Saudi Arabia) made an especially large production cut reduction, which is hardly evidence of cartel coordination. There is no evidence that cuts made by other OPEC members were larger than a perfectly competitive market response (see also Claes, 2001, chapter 7 on this point).

For everyone else – policymakers, the public, and most scholars and journalists – the question of whether OPEC is a cartel is not something that much matters. Quite rationally, they choose not to devote time and effort into investigating this question because they have other jobs and concerns.

State leaders and other senior government officials appear to fall into this group. We cannot directly observe leaders' beliefs but clues can be obtained from their memoirs. For instance, in one of the few mentions of OPEC in Bill Clinton's autobiography, he writes 'Energy was a huge issue [in 1980] because of OPEC's steep increase in the price of oil, which raised prices for everything else, too' (Clinton, 2005, p. 268). Elsewhere he writes, '[In 2000] I wanted to see the price stabilize at between \$20 and \$22 a barrel and hoped OPEC could increase production enough to do that' (Clinton, 2005, p. 900).¹⁶ Those statements seem to indicate that Clinton viewed OPEC as a cartel, though they are not definitive. Bill Richardson, Clinton's secretary of energy, is somewhat clearer in his memoirs, stating that 'What we faced was a combination of OPEC power in the marketplace, our dependence on imported oil, and demand pressures' (Richardson, 2005, p. 266). He also recalls making many trips to various OPEC countries 'to jawbone for hikes in output that would moderate the increase in prices' (Richardson, 2005, p. 269).

Does the myth about OPEC really matter? Yes, though the consequences are not huge. I discussed one of those consequences earlier: domestic audiences in oil-producing countries tend to give credit to OPEC leaders like Hugo Chavez for raising the price of oil, even though there is no real evidence that he actually caused such a change. A second example is that many people outside of oil-producing countries are psychologically disposed to pay more attention to OPEC members like Iran or Venezuela when prices are high or rising. This might generate a tendency for diplomats to defer to OPEC members and offer favors in exchange for promises of increased or decreased OPEC oil production (Richardson, 2005, pp. 266–274). Some studies suggest that, regardless of whether policymakers actually should let oil politics affect their policies, they do in fact behave that way (Clayton and Levi, 2012). For instance, policymakers are willing to incur considerable material costs in order to increase oil imports from one country (e.g. a friendly neighbor) or lower them from another (e.g. a potential risky supplier), despite the tendency of a fungible world market to readjust the flow of oil to reach equilibrium.¹⁷

A third example of the negative consequences of misunderstanding OPEC comes from legislative politics. Politicians in the United States and other oil-importing states blame OPEC for manipulating world oil markets, especially during times of high oil and gasoline prices. For instance, the No Oil Producing Exporting Cartels (NOPEC) Act of 2004 introduced in the US Senate served as a rallying point for those who sought to blame OPEC. Other NOPEC bills have been introduced at least 15 times since 1999, though to date none have passed (Verrastro et al., 2011). The continued introduction of these bills distracts Congress and the public, thereby imposing an opportunity cost on the political system.

Understanding OPEC as a political club also helps answer certain puzzles. One such issue is the variation in OPEC's membership. In the 1970s, OPEC enjoyed a certain level of prestige when developing countries saw it as an organization that 'took on' the developed countries and won (by raising oil prices). Several oil-exporting developing countries that were not already members wanted into the club: Ecuador and

Gabon joined the organization in 1973 and 1975 respectively, only to leave the organization as its prestige fell in the 1990s. Then in the 2000s, with oil prices on the rise, OPEC membership became fashionable again: Ecuador rejoined, Angola was accepted as a new member in 2007, and Sudan sought membership, though it has not yet been accepted.¹⁸ This variation in OPEC membership is counter-intuitive behavior if OPEC is a cartel because membership in the organization would be most costly (in terms of forgone oil sales, to the extent that such exist) at times when oil prices are high. The fluctuations in OPEC's membership, which correlate with oil prices, make more sense when viewed from the perspective of the perceived political clout and prestige of the organization.

Member states perceive OPEC membership as a signal of status and prestige. For instance, when Angola joined the organization in 2007, it took out full-page advertisements in *The Economist* to announce that it had joined OPEC and should be seen as a country of rising importance. Implicitly, the advertisements tied these two claims together: i.e. Angola was rising in importance in part because it had joined OPEC.

Conclusion

OPEC quotas are irregularly applied, frequently ignored by its members, and have at most a modest effect on actual production. Probably Saudi Arabia has market power. One might say that OPEC probably has market power because it includes Saudi Arabia, but only in that sense; the findings in this paper undermine the idea that the OPEC as an organization per se manipulates the world oil supply.

By 2012, the organization was openly struggling with its identity and purpose. In that year it stopped even trying to assign individual production quotas to its members, instead only identifying a (largely useless) production target for the group as a whole. Moreover, OPEC members faced new challenges in an era of climate change and declining per capita oil revenues. Some analysts see OPEC in a 'perfect storm' (Van de Graaf, 2017). It is squeezed between decelerating global demand, in part due to climate change and alternative energy technologies, and rising global supply, in part due to fracking and unconventional oil supply in the United States and elsewhere (Van de Graaf and Verbruggen, 2015; Colgan and Van de Graaf, 2017).

Yet OPEC's favorable geology means that its oil will likely remain competitive in a low-cost environment, even if it does not generate the massive profits it once did. Moreover, starting in November 2016 OPEC began a comeback bid by forming a partnership with Russia. It is difficult to assess just how much the Russia-OPEC agreement to constrain oil production is actually affecting behavior relative to the counterfactual or how durable it might be, but it is possible that this new form of cooperation will prove more than skin deep.

Overall, my findings have implications for both theory and practice. The fact that a widespread belief about the world's most important commodity market appears to be wrong should alter how we study international political economy. One implication is that scholars should be careful about how the bargaining dynamics within OPEC are studied and conceptualized because they do not occur within the context of a classic economic cartel (Blaydes, 2004). Second, this study adds to the scholarly research into the causal effect of international institutions and regimes (Martin and Simmons, 1998). OPEC appears to be an important case within the category of international regimes that have outlived their original mandates (Gray, 2018). We should view OPEC as a political club rather than an economic cartel.

In the realm of practical politics, journalists and pundits should stop using the assumption that OPEC's actions are key drivers of world energy markets. They are not. Most of the credit or blame for changing oil prices in recent years rests with the energy demands of new Asian customers and the development of fracking and the tight oil industry in the United States, not diabolic moves by OPEC. Moreover, policy-makers in oil-importing countries should stop being so fearful and resentful of OPEC. With the world price of oil set by market forces almost entirely outside of its control, OPEC is mostly along for the ride like everyone else.

Notes

- 1 BP (2018). *Statistical Review of World Energy*. Available from: www.bp.com/en/global/corporate/energy-economics/statistical-review-of-world-energy.html.
- 2 Adelman (1982) suggests that OPEC wobbles between acting as a dominant firm and as part of a cartel depending on market conditions.
- 3 See also Victor, D. (2008). "OPEC Is Irrelevant: The Once All-Powerful Oil Cartel Now Mostly Just Rides the Waves of Supply and Demand". *Newsweek*, 01.08.2008.
- 4 Producers who stop producing before marginal costs equal market price (like some OPEC producers, possibly) are not behaving perfectly competitively, but that does not necessarily imply cartelization.
- 5 Ideally, we might have additional tests, such as comparisons between production and installed capacity. Unfortunately, cross-national time-series data on installed capacity are not available. Moreover, the occasional country-specific estimates of installed capacity that do exist are of uncertain accuracy.
- 6 One of OPEC's stated goals is to stabilize prices. It is possible that an organization could seek to stabilize prices without affecting the long-run average price or production levels of its members. Yet such an organization could not be considered a classic cartel because it would not be profit-maximizing.
- 7 EIA estimates can differ from OPEC's reported production data. OPEC's data are not fully credible because they are self-reported by member countries which have an incentive to dissimulate when they are overproducing.
- 8 Iraq has not had a quota since 1998. Iran, Angola and Ecuador have also had periods without a quota.
- 9 The nine members are: Algeria, Iran, Kuwait, Libya, Nigeria, Qatar, Saudi Arabia, UAE and Venezuela. Calculated using data from the US, EIA for actual production, and from OPEC for market allocations, 1982–2009. Note that Smith (2008) estimates that overproduction averages just 4 percent using ostensibly the same data (though for a different time period).
- 10 Formally, the dependent variable is the first difference in oil production, and the independent variable is the first difference in oil quota. The observations are monthly, although the values are measured in barrels per day.
- 11 BP *Statistical Review of World Energy* provides data on proven reserves starting only in 1980.
- 12 BP *Statistical Review of World Energy* provides data on forty-seven oil-producing countries, but Brunei, Chad, Equatorial Guinea, Turkmenistan and Uzbekistan are not included due to data availability for other variables.
- 13 Diplomatic representation is measured only once every five years in the COW dataset, so I describe changes in diplomatic representation in the five-year window within which the state joined or left OPEC.
- 14 For instance, a former secretary general of OPEC insists that OPEC shapes world oil prices: "The control was, and remains, long-distance, erratic, imprecise, and unpredictable – but in the end, very real The system is slow, clumsy, partly dependent on necessarily inaccurate demand forecasts, and bedeviled by indiscipline within OPEC's ranks. But, by and large, it works" (Parra, 2004, pp. 321–322).
- 15 OPEC website: www.opec.org/opec_web/en/about_us/23.htm.
- 16 On the same page, Clinton writes: "I spoke with King Fahd of Saudi Arabia about the possibility of OPEC increasing its production."
- 17 Arguably there might be wartime benefits to manipulating oil imports in this way, but those benefits are highly dubious (see Gholz and Press, 2010).
- 18 Indonesia's departure in 2008 has less to do with prestige and more to do with its new status as a net importer of oil. Puzzlingly, it rejoined OPEC in 2016.

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OPEC – from peak to peak

The history of ‘peak oil’ and its relevance for OPEC

Øystein Noreng

Perceptions matter

This paper discusses the recurrent concern about ‘peak oil’ from a geological, economic and political perspective and the interaction with the management of the oil market through the Organization of Petroleum Exporting Countries, OPEC, with a concern about ‘peak oil demand’.

In the oil market, perceptions are the key to price formation, even if from time to time they are corrected by the physical realities. The huge oil price swings cannot be explained only by changes in costs or demand, market imperfections are also part of the equation. Geology makes an effective barrier to entry, limiting the number of suppliers and enhancing the oil market sensitivity to disruptions, whether by accident or crises such as coups and wars, especially in the Middle East. Oil market sensitivity has provided opportunities for financial agents and the importance of perceptions (O’Sullivan, 2009, p. 49). In contrast to changes in physical consumption, inventory changes are critical to the call for oil in the market, and they are largely based on perceptions.

The underlying sentiment is fear of scarcity, a concern about supply security, and ultimately the terror of oil drying up and supplies dwindling, i.e. ‘peak oil’. A common concern has been that peak oil in the near future would lead to a shortage of key resources and input factors in our economy that will force undesirable changes in living and social conditions. Some observers have predicted that financial crisis, unemployment and lack of growth prospects will be the consequences of a nascent shortage of oil and higher energy prices (Jeff, 2009).

The discussion of peak oil often ends in apocalyptic visions of widespread disaster as demand for oil outstrips supply. One widely held view is that supply and demand evolve independently of each other; consequently, a disaster *must* occur when supply does not cover demand (Roberts, 2004, p. 44). This view negates the significance of the market and prices (Holland, 2008, pp. 61–79). In practice, oil consumption *cannot* exceed available volumes through production and inventory reduction. Demand for oil is predicated on consumers having greater utility from using oil than from *not* using oil at the available price. From this perspective, oil prices are determined less by production costs than by utility for consumers. For the latter, not consuming oil, e.g. to get to work, may incur a heavier loss, in this case of forsaken income, which can exceed the cost to be paid for oil consumed. Indeed, there is an argument for differentiating oil demand by uses, by necessity and users’ economic benefits. Put simply, in some cases the loss, i.e. the cost of *not* using oil, may exceed the cost of oil, even at a high price, meaning that for consumers in need the most

expensive oil is the volume that is not available on the market. Therefore, many consumers willingly pay a premium for secure supplies.

On the supply side, if oil prices are too low, incentives to explore for oil and develop oil fields will weaken and supplies will gradually decline. The oil market is characterized by imperfect competition; the price can stay well above production costs as long as producers cooperate and consumers pay. Fear of scarcity is an effective incentive. These concerns give a value to secure supplies, at times much higher than the technical cost of production (Dannreuther, 2017). The consumers' concern for secure supplies permits producers to raise prices above the costs of production and governments to levy taxes and duties.

If, by contrast, oil prices are too high, demand will decline and sales will shrink; unsold oil is worthless; oil in the ground that cannot be sold has no value. This is the perspective of 'peak oil demand', prompting an anxiety among producers that their oil the ground will lose value and ultimately be unsellable. Fear of an oil glut is a powerful incentive for price moderation. The advent of unconventional oil, essentially in the United States, electric vehicles and renewable energy enhances anxieties about future oil demand. These concerns give a value to secure outlets.

Historically, attempts have been made to overcome the contradiction between the inherent instability of oil prices and the need for stability in order to promote investment. In the early 20th century, vertical integration, connecting supplies with refining and marketing within the same company, was the answer. For many decades, this form of management successfully avoided excessive supplies as well as shortfalls in the world oil market.

By the end of the 1920s, the oil market was being managed by the Texas Railroad Commission (TRC) in conjunction with a cartel of international oil companies. The TRC was originally set up in 1891 to protect consumers from excessive rates. In 1917 it was given the responsibility to regulate pipelines; oil production was added in 1919. In 1930 the TRC began to prorate oil output by allocating quotas in order to raise and stabilize oil prices as well as conserve resources. The move was welcomed by the large oil companies, as lower volumes were offset by higher prices. The New Deal permitted the TRC to set US oil policy. By the 1950s the TRC controlled more than 40 percent of US oil production. Indeed, TRC can be seen as the forerunner and model for the Organization of Petroleum Exporting Countries (OPEC) (Childs, 2005).

OPEC is an interest organization for major oil exporters, established in 1960 to coordinate the taxation of foreign oil companies. Since the 1970s, when the member countries took control of oil supply decisions, OPEC has *occasionally* acted as a cartel by setting oil prices and allocating quotas. Historically, OPEC has intervened to stabilize oil prices at a high level after price rises caused by political events, as in 1973/74 and 1979/80, or driven by strong demand, as after 2003, rather than unilaterally raising prices. At times, non-member oil exporters have participated in market stabilization efforts, as Mexico and Norway did in the 1980s and around 2000 and as Russia does currently. OPEC power is based on the fact that the conventional oil market is a natural oligopoly, comprising a few dominant sellers with large volumes and low costs, which have more to gain by cooperation than by competition. After successfully cooperating with Russia stabilizing the oil market in 2016 and 2017, curtailing supplies to reduce the inventory overhang, causing rising prices, by the summer of 2018, concerns for stability called for volume increases.

Oil prices rising above a certain, unspecified, level are sometimes perceived as potentially leading to 'peak oil demand'. The term needs clarification. Simplistically, it is perceived as a counterpart to peak oil, a turning point after which oil demand cannot but decline, regardless of prices, ostensibly due to substitutes, consumer preferences and policies. History offers a more differentiated view.

Peak oil demand and energy transitions

The world has already experienced a moment of peak oil demand. In 1979, world oil consumption peaked at 64 million barrels a day, mb/d. For the next four years, through 1983, it fell by altogether 8 percent.

The 1979 consumption level was reached again only in 1989, ten years later. In the meantime, nominal oil prices had declined by more than 40 percent and real prices, adjusted for purchasing power, had fallen by two-thirds. Oil prices first peaked in 1980 with the price (Brent) at \$36.83/bl. It took 24 years, until 2004, for the *nominal* oil price to reach the same level. Measured in *real* terms, i.e. purchasing power using 2017 values, the oil price (Brent) first peaked in 1980 at \$109.56/bl. It took 28 years, until 2008, for real oil prices to recover to that level. The bottom was hit in 1998, when the average nominal oil price (Brent) was \$12.72 /bl. In real terms (2017 prices), the price was \$19.12/bl. On several occasions during the ‘lean years’, the oil market was rescued from further meltdown by cooperative efforts of oil-exporting countries to limit supplies.

In 2009 and 2010, oil prices subsided, but they rose again in 2011 and 2012. The nominal oil price (Brent) peaked in 2012 at \$111.67/bl. Real oil prices (2017 values) had already peaked in 2011 at \$121.24/bl. Shortly afterwards, in late 2014, OPEC opted for greater volumes and lower prices. In 2016, the nominal oil price (Brent) was \$43.63/bl. The real price (2017 values) was \$44.67/bl. These prices, both nominal and real, were at the levels of 2004, 12 years earlier. In 2016 and 2017, oil prices recovered, partly due to cooperation among major oil exporters such as Russia and OPEC and partly due to robust demand. The lesson is that oil demand seems to be dependent on the state of the world economy, in which oil prices are an important factor.

The massive oil price increases in the mid-1970s had a macroeconomic effect harmful to oil demand, together with a sectoral effect, driving substitution for oil by coal, natural gas and nuclear in heating and power generation. Thirty years later, oil demand was more concentrated in the transportation sector (which had more limited substitution potential). Consequently, oil demand could prove more robust facing the price rises. Moreover, as oil by that time accounted for a smaller part of the economy, the macroeconomic effect was more limited.

Since the end of World War II in 1945, the world has been in a continuous energy transition. The driver has been the rise of oil and natural gas within a context of increasing total energy demand. In the first decades after 1945 in North America and Western Europe, oil made a large-scale entry in heating and power generation, besides the rapid increase in road transportation, but coal demand also increased. New oil-fired capacities, especially in power generation, were essentially a supplement to incumbent coal-based plants rather than a substitute.

On a worldwide scale, by 1973 oil had become the leading fuel, with an energy market share of 50 percent. That was also the year of the first oil price shock. Two successive oil price rises drove oil’s energy market share to 40 percent by 1987, a level stable until 2000. Later high prices contributed to reducing oil’s share to 34 percent by 2017. Major beneficiaries are natural gas and coal. The share of natural gas in world energy demand has risen gradually from 15 percent in 1965 to 23 percent in 2017. The coal share was 37 percent in 1965. By 1973 it had fallen to 27 percent, a level that with some variations since has been stable. In 2017, coal had a share of 28 percent of world energy demand.

Volumes traded strengthen the impression of gradual change and structural stability. Between 1965 and 2017, world total energy demand rose by a factor of 3.6, from 3,733 million tons of oil equivalent, mtoe, to 13,511 mtoe. During these years, oil demand grew by a factor of 2.9, from 1,584 mtoe in 1965, to 4,622 mtoe in 2017. Natural gas demand rose by a factor of 5.8 during this time, from 542 mtoe in 1965 to 3,156 mtoe in 2017. Coal, the incumbent energy leader, saw demand rising by a factor of 2.7, from 1,389 mtoe in 1965 to 3,731 mtoe in 2017.

The word is that the world is in the middle of an oil age. It is important to distinguish between absolute and relative figures; even if oil’s market share declines, a relative figure, oil volumes consumed increase in absolute figures. But the notion of peak oil demand seems preposterous as long as the world remains in a coal age, as indicated by robust demand and market shares. And the world also seems to be entering a natural gas age, as indicated by demand growth. As already mentioned, the issue is less substitution than complementarity and capacity growth.

So far in the overall picture, non-fossil fuels have played only a small part. In 1965, fossil fuels represented 94 percent of world energy demand; in 2017 the figure was 85 percent, out of a total three to four times as large.

The key position of oil is caused by inherent comparative advantages. No other energy carrier is similarly efficient in terms of energy content by volume and weight, in addition to versatility. Oil is easy to store and transport, and it can be used for multiple purposes in heating and power generation, as motor fuel and as a chemical feedstock. This is the reason why oil has had a robust position through changing market conditions.

Electric cars represent a major challenge to oil, potentially announcing a decline in oil demand and oil's energy market share – in short, an element of peak oil demand (Helm, 2017, p. 62). However, electrification essentially concerns passenger vehicles. Current technology does not permit large-scale electric traction of utility vehicles, ships and aircraft, where oil may have a protected market for a long time (World Energy Outlook, 2018, p. 4). Moreover, electric cars need electric power.

The concurrent rises in electricity demand and in intermittent solar and wind power generation present serious challenges to power grid management. Solar and wind power plants need a back-up, reserve generation capacity for periods when the sun does not shine and/or the wind does not blow. It should be flexible, easy to switch on and off to respond to changes in sun and wind conditions. Because it will not run full time but only for parts of the day and the year, it should have low capital costs.

Nuclear power plants have high capital costs and are suitable for covering base load demand, not for intermittent uses. Coal-fired power plants are polluting and take a long time turning on and off. In contrast, gas and oil turbines are relatively inexpensive and simple to turn on and off. These characteristics make oil and gas turbines suitable as complements to solar and wind power. For gas turbines to represent a credible back-up, a gas delivery contract is required. Where natural gas is not available, oil turbines can provide the back-up. Against this backdrop, the growth of solar and wind power may provide new markets for natural gas as well as oil.

Recurrent concerns

Since the beginning of the US oil industry in 1859 there have been concerns about running out of oil. These concerns have always been checked by the new discoveries as the oil industry moved into new areas. Already in 1874, a geologist in Pennsylvania stated that the United States would run out of oil in 1878 (Anderson, 1984, p. 23).

After the First World War there were worries that a fast-growing fleet of vehicles would lead to a quick depletion of the country's oil resources (Tugendhat and Hamilton, 1975, p. 75). A proposal for a state-owned oil company, on the pattern of the Anglo-Persian (later BP), was not passed in Congress, but in 1921 the then secretary of commerce (later president) Herbert Hoover persuaded the seven largest US oil companies to form a syndicate to represent US oil interests in the Middle East. By acting concertedly and with government support the largest US oil companies got a foothold in the Middle East (Blair, 1976, p. 33).

At this time, the United States was a major oil exporter, unlike France and the United Kingdom. The collaboration between major oil companies was in violation of US competition law; ten years earlier, in 1911, Congress had passed the Sherman Act and broken up Standard Oil, which had almost monopolized the US oil market (Maugeri, 2006, p. 10). The move was facilitated by huge discoveries in eastern Texas that permitted oil to be shipped by tankers to markets in the north-east of the United States, circumventing the railways controlled by Standard Oil.

Later in the 1920s, the US oil problem was not scarcity but abundance and low prices. The depression weakened oil demand by 22 percent between 1929 and 1932 and the price fell from \$1.15/barrel to \$0.10/barrel (in 1930 dollars). The crisis caused government intervention and prorationing to raise prices.

A few years earlier, in 1927, the seven largest US and European oil companies began to cooperate in order to control the market (Tugendhat and Hamilton, 1975, p. 97). The strategy was not to compete for customers and at the same time to ensure control of oil supplies – that is, to keep competitors away, first of all in the Middle East (Blair, 1976, p. 47). For the oil majors, control of markets was complemented by control of supply sources, to avoid overproduction and a fall in prices. Vertical integration appeared as the most rational organization, with full control of the value chain, from exploration and development through transportation to refining and distribution (Copinschi, 2010, p. 33).

This was not only a financial integration, in which an owner through a holding company could spread the risk by positions in the various parts of the value chain, but also an operational integration, in which the flow of oil between the branches was administrated centrally by a few large companies. They had no interest in flooding the market, nor in maximizing exploration and development. In their concession areas, primarily in the Middle East and North Africa, the companies had no interest in finding and developing oil reserves beyond their needs in the immediate future – for example, 10–15 years (Adelman, 1993, p. 329). This curtailed exploration activity in the world's most prospective areas.

As a collective monopoly the major oil companies had a common interest in *not* maximizing the recovery and supply of oil, and therefore also not in a high pace of exploration and development. Their interest was rather a controlled growth in the supply of oil, sufficient to meet a gradually increasing demand at a price that was competitive against coal but well above the factor cost.

In the 1970s, nationalization of the oil industry in most OPEC countries broke up the integrated circuits that had controlled the oil flows. The result was a growing supply risk for consumer countries, which resulted in a second oil price recovery in 1979/80. The outcome was also a weakened bargaining position for consumer countries that individually faced a cartel of oil exporters. To strengthen the negotiating position of the United States, Henry Kissinger led an attempt to unite the Western importers of oil in a buying cartel, but failed. The IEA has never been an effective counterpart to OPEC (Maugeri, 2006, p. 154).

The oil-exporting countries have no interest in flooding the market with cheap oil but aim to get higher prices by controlling volume. If OPEC was tempted to flood the market to increase market share it would run the risk of retaliatory measures, such as customs barriers and import duties. Instead, members of OPEC can use the oil companies as tax collectors (Nersesian, 2009, p. 173). Therefore, the major oil exporters had – and have – no immediate interest in strongly escalating exploration and development of capacity. However, this does not imply resource scarcity. For example, in Saudi Arabia approximately 300 exploration wells were drilled in the years 1936–2004, i.e. approx. four exploration wells a year (Cavallo, 2005). The limited exploration was not due to failure to find oil, but rather to success. There was little need for more exploration. Prioritizing price rather than volume has been recurrent OPEC strategy, with disagreement over *how* high oil prices should be, given revenue needs and market concerns.

Controversy about the limited supply of oil began in recent times with the report, 'Limits to Growth', published in 1972 by the Club of Rome, written by researchers at the Massachusetts Institute of Technology (MIT) (Meadows, 1972). The report built on a system-dynamic model to analyze the world's access to and use of resources during the period 1900–2100, and included population growth and environmental impact. Different scenarios came to the same conclusion: the world would consume too much, environmental damage would increase dramatically, the supply of food and raw materials would decline. The use of energy was an important parameter, and the message was that oil supplies would come to an end, probably by the early 1980s. The misery resulting from this would lead to economic collapse and mass deaths, and populations should start to adapt to a limited supply of resources. The report initiated the concept of sustainable development.

The model excluded factors that could alter the conclusion, such as efficiency improvements and technological development. It ignored human ingenuity and adaptability. An extensive use of synthetic indicators with a mixture of quantitative and qualitative factors is a methodological obfuscation that makes it

difficult to control the analysis and verify the results. The report has since been characterized as an exercise in disinformation and confusion rather than an objective analysis with the aim of delivering new insights (Smil, 2003, p. 168). In retrospect, it seems as if the aim was to present a disaster as inevitable, regardless of economic and technological conditions or political choices (Cole, 1973, p. 32).

The oil price quadrupling in 1973/74 led to greater awareness of potential oil scarcity. It apparently corroborated the warnings of the Club of Rome, but the reality was different. The control of volumes supplied to the world market shifted from a group of international oil companies to a group of oil-exporting countries with an interest in higher export prices. As prices went up, the marginal production shifted from high-cost North America with limited reserves to low-cost Middle East and North Africa with abundant resources. This phenomenon is contrary to conventional economic theory, but it did occur.

A larger study published in 1977 and sponsored by Shell among others, concluded that at the latest in 2000, the supply of oil would not be able to meet demand.¹ One prerequisite was a continued high growth in consumption, irrespective of price. The report recommended investment in coal, shale oil and nuclear power. In 1979, during the Iranian revolution, the CIA published a study arguing that oil demand would imminently surpass supplies, and that oil extraction would decline during the 1980s (National Foreign Assessment Center, 1979).

Instead, high prices prompted a transition from oil to coal, natural and nuclear power, as well as energy efficiency. By the mid-1980s, oil prices were falling and the real price, measured in purchasing power of US dollars, reached its 1985 level only in 2005.

The peak oil debate was again set in motion by the British geologist Colin Campbell and his French colleague Jean Laherrère in an article in *Scientific American* in March 1998. Briefly, their argument was that an oil field has a natural threefold development path: a fast rise, a top (peak) and a corresponding decline. This pattern should also apply to regions and the world. The decline in oil extraction was estimated on the basis of figures for total reserves, time of extraction start, and ascent curve. This gives a logistic curve, conditioned by the physical properties of the reservoirs. The argument was that the world's supply of oil is declining because extraction and consumption surpass new discoveries. In hindsight, they seem to have ignored the fact that many years of low oil prices had provided little incentive for exploration and development.

Their argument was also that the member states of the Organization of Petroleum Exporting Countries, OPEC, were exaggerating their reserve estimates in order to increase their quotas and improve creditworthiness with international financial institutions, particularly the World Bank. Discovery rates of oil reached a peak in 1964; the depletion of the older, larger fields had not subsequently been offset by new discoveries, so that oil extraction would reach a peak and then decline. Proven oil reserves are the world's inventory. For decades, outtake had exceeded input. The peak of possible oil extraction was likely to be imminent; decline would inexorably follow from physical conditions and could not be halted by technology or economics.

Campbell assumed in 1989/90 that world oil production would peak in 1998. He predicted a worldwide economic depression as a result of a shortage of oil and high prices. He and other peak oil theorists have been criticized for a mechanistic approach to the problem and assuming that all the important parameters are static and that the production curve is not conditioned by economics and technology (Clarke, 2007, p. 15).

Campbell and Laherrère focused on discovery, not reserve growth, in line with Hubbert. If production exceeds the growth in oil reserves, measured by volume, it will, over time, naturally decline. The counter arguments, in brief, are that the difference between recovery and discoveries will be covered by growth in proven reserves through new technology, investments and better organization. New technology and lower costs make new resources available (Bret-Rouzaud and Thom, 2005). Smaller, less accessible prospects become profitable and the volume of oil estimated when a new discovery is made is often only a small fraction of the total volume extracted over the lifetime of a field, so the discovery rate is not representative

of reserve growth. In other cases, reserves are overestimated. When the aggregate volume is underestimated, this generally leads not to a higher production peak but to flatter tail production after more wells are connected to production facilities and thus greater total production volume. The discovery rate must be linked to deposit size and the total volume found; those arguing for peak oil looked at the discovery rate on its own.

Historically, concerns about peaking oil supplies have been ignited by assumptions about geology – that ultimately finite oil reserves would lead to a fairly immediate volume decline, implicitly regardless of prices. These concerns have been strengthened by the properties of the oil market, namely capital intensity and long lead times, which mean that supply volumes do not respond quickly to price changes. Moreover, political events, essentially in the Middle East, have caused sudden oil supply reductions and price rises, demonstrating the precarious state of the oil market. Finally, the intervention of OPEC has from time to time overruled conventional market forces. The lesson is that a tight oil market does not necessarily reflect resource scarcity, and certainly not peak oil.

The theory of peak oil

The peak oil theory is often illustrated by a simple, symmetrical logistic distribution curve, portrayed graphically, with a gradual rise to a peak, followed by a decline that is the mirror image of the upturn. The theory was developed by American geologist Marion King Hubbert on the basis of observations of various American onshore oil fields. In brief, the theory is that recovery rate grows exponentially until half the resources in the field have been depleted, after which the decline is continuous and also exponential, at the same rate as the upturn so that the production profile is a logistic distribution curve.

The assumption is that the landowner or operator who wants the fastest possible earnings will maximize recovery to reach the peak rapidly without regard for resource conservation and volume maximization over a longer period. The theory also presupposes continuous exploration and subsequent development and recovery, unimpeded by economic and political factors.

Hubbert's theory implicitly assumes that oil demand and the market do not represent an obstacle to production. Hubbert's theory is the central reference in the discussion of peak oil, but little attention is paid to its assumptions and limitations. Hubbert developed his theory based on observations of a large number of oil fields in the continental United States in the 1950s and 1960s. In 1956 he presented the aforementioned Hubbert's curve, a symmetrical logistic distribution curve that would predict the oil production trend in a given oil province. The method is to estimate remaining reserves and production in a group of fields on the basis of data for discovery, for production start-up, its flattening and for aggregate recoverable reserves in an oil province. The peak discovery rate is important to predicting the subsequent production peak. On this basis, Hubbert predicted that US oil production would reach its peak around 1970 and thereafter inevitably decline. Hubbert was right about the time; US oil production reached its peak in 1970 and has since declined gradually until recently, but he underestimated the volume. He also overlooked the impact of high prices on the breakthroughs of shale gas and oil.

Ever since, Hubbert's curve has been used to predict oil production in various oil provinces and globally, with varying success. Any estimate of future oil production according to Hubbert or any other model must be based on an estimate of recoverable reserves and producers' interests and strategies, but this is tantamount to aiming at a moving target. In the US, for example, the ratio of recoverable reserves and annual production has been about 10:1 for the last 30 years, but the US is still one of the world's leading oil producers.

In sum, Hubbert's model and the theory of peak oil are based on five assumptions:

- 1 Knowledge of global recoverable oil reserves is reasonably complete
- 2 Estimated reserves are fixed

- 3 Production should take the form of a symmetrical curve
- 4 Technology is constant
- 5 Oil prices are constant or irrelevant.

None of these assumptions have any basis in reality. Hubbert's model provides a basis for estimating oil reserves and production profiles under static conditions. Like all models, it is not perfect. Technology and the discoveries made affect recovery, but more so in marginal fields and new areas than in the easiest areas that are usually found first, but they generally contribute to extending production time for established fields. Technology and oil prices are particularly significant in relation to difficult and smaller fields and for opening new petroleum provinces, such as the Arctic and large ocean depths, as in Brazil.

It is difficult to apply the model under dynamic conditions. Important parameters in the oil industry are dynamic: costs, reserves, prices, profitability, competition and regulations are constantly changing. No scientific knowledge indicates that oil production will follow Hubbert's symmetrical curve. Instead, oil production is determined by a set of physical, economic and political factors. The alternative to a quick peak is that recovery is kept on a plateau at a lower level for a long time, which may contribute to an increase in final recoverable volumes.

Today, most of the world's oil reserves are not privately owned, but owned by states, which in many cases *do not* maximize short-term revenues. The relationship between discovery and production is used to support the theory of peak oil. In the 1960s, annual discoveries of oil were nearly ten times recovery measured in volume. At that time, the Middle East and North Africa were open to the oil industry, albeit with limited exploration. Since the 1970s, exploration has been sharply reduced in the major OPEC countries and Russia. Since the 1980s, global oil production has exceeded discovery by approximately 50 percent of the volume.

The ratio between reserves and annual production has remained fairly constant due to growth in reserves through new technology, investment and better organization. Access to large areas has been and remains limited or impossible for the international oil industry. The imbalance is creating fear that the world will soon run out of oil; there have been few major oil discoveries since the 1970s.

Many of the biggest fields are showing clear signs of maturation, with declining reservoir pressure, increasing demand for water injection and falling production volumes. Volume is essential to profitability in the oil industry, and the replacement of oil from large fields in decline with smaller new fields entails large investment and higher production costs. Global oil discoveries outside the US peaked around 1970. A direct parallel to the US would yield an expected production peak around 2005; government regulation and a more long-term recovery policy may postpone this by several decades.

The general expectation was that the decline in global production had begun and there was no turning back. The downturn was unlikely to be sudden, but it was believed to be almost impossible to replace the decline of large, mature fields with production from new fields.

The geological discussion of peak oil has provided the basis for broad discussion of possible economic, social and political consequences in addition to the environmental consequences of consumption of petroleum products. Hubbert's theory is accepted as a clue on a global basis. For this reason, a sudden decline in recovery and sharp upturn in prices are expected. A further premise is that because there are no substitutes for oil, a physical shortage of fuel is inevitable. As mentioned, the result will be an economic crisis of declining employment and living standards, poorer nutrition and deterioration in the health of the population. It is presumed that the economic crisis will lead to social conflicts and wars over the remaining energy resources.

This apocalyptic view overlooks consumers and markets. If oil prices are too high, demand will decline and recovery will decrease; unsold oil is worthless. If oil prices are too low, incentives to explore for oil and develop oil fields will weaken and recovery will gradually decline. The oil market is characterized by imperfect competition, which means that the price can stay well above production costs as long as

consumers pay. Correspondingly, they can stay below replacement costs to the extent that major suppliers opt for taking market shares.

The oil market is dominated by an oligopoly centred in the Middle East, which has the largest reserves and the lowest costs. Because demand for oil is not very price elastic, there is a high risk that increasing supply in the market will lead to price declines rather than volume gains, resulting in revenue losses. In the oil market it is sometimes more profitable *not* to produce than to produce. When higher prices do not lead to increasing supply, then it may be reasonable to assume that the world is running out of oil.

Trends in the oil market have not followed the forecasts based on the theory of peak oil. Demand has increased less than expected and supply has been more robust than anticipated. The price mechanism has worked, sometimes in a brutal manner with strong discontinuities and high social costs. Oil prices are unstable at any level.

Historically, short periods of high oil prices have alternated with long periods of decline in real prices. Low oil prices stimulate demand and weaken investments in energy conservation and new production. High oil prices weaken demand and encourage investment in energy conservation and new production.

The validity of Hubbert's theory is conditioned by place, time and political constraints. It is based on lessons learnt in the US in the 1950s and 1960s and is not universally applicable. The recovery of oil may assume many different profiles, conditional on geology, technology, economics and, not least importantly, owner preferences. There is no physical shortage of oil in the world. Large prospective areas have been little explored or not at all. There is great potential to increase production from established oil provinces. Because the most available and least costly prospects are exploited and depleted first, the oil industry is facing a permanent cost problem that makes it difficult to replace the volume from large mature fields. This is the key challenge for oil company research and development.

Technology is the key to lowering costs and acquiring new reserves. Research and development have led to technical and organizational change in the oil industry that has significantly lowered the costs of exploration, expansion and operations. This means that as the most available and least expensive reserves are depleted, new reserves will be added at affordable costs. So far, technology has won the race against depletion (Fagan, 1997). Combined, new technologies and new organizational forms are making it possible for the oil industry to move towards smaller and more difficult prospects and increasing the recovery rate for fields already in operation. Higher volumes and longer lifetimes result in better utilization of capital investments, as fixed costs decrease relative to recovered volume. Moreover, unconventional oil, such as heavy oil in Venezuela and shale oil in the US, are profitable and gradually become available in the market.

The OPEC dilemma

For OPEC, technology development in the oil industry represents a mounting challenge, sharpening the dilemma of giving priority to prices or volumes, weighing short-term needs against long-term strategic concerns. By 1974, when the OPEC countries took control of volumes and prices, OPEC had an oil market share of 51 percent; with a production of 30 million barrels a day, mb/d, and a total income of 125 billion US dollars, USD (based on a simple calculation of volumes and current oil prices). Six years later, in 1980, after two oil price jumps, OPEC's market share was 41 percent; with an output of 26 mb/d, total income was 350 billion USD. By 1986 fortunes had reversed: OPEC's market share was 31 percent; with an output of 19 mb/d, income was 98 billion USD. This experience is part of the collective OPEC memory.

The new oil order is based on the breakthrough for unconventional oil, marking a structural shift. The advances in unconventional crude extraction, especially in the United States, and the erosion of the predominant position of oil in the transportation sector are modifying important features of the oil market; both supply and demand are becoming more price sensitive. In economic terms, price elasticities have

strengthened. More than before, raising prices risks compromising oil demand, whereas lowering prices may undercut competition and secure long-term volume and income growth—but at the expense of short-term earnings. Consequently, because of shale oil, the market may be setting limits to drastic oil prices lasting more than a year or two, the time to increase volumes.

Historically, as a major oil importer the United States had an interest in moderate oil prices. Greater energy self-sufficiency makes the United States less vulnerable to the world oil market convulsions, underpinned by political setbacks in the Middle East, but its production increase is based on high oil prices. Low oil prices would threaten the US oil industry and self-sufficiency. Judging by a few years' experience, oil prices in the range of \$60–70/bl. seem to suit US interests, but price volatility is harmful to high-cost US oil. To have stable and high oil prices, the United States needs cooperation among the major oil exporters, not least the GCC countries; it also needs an effective OPEC as well as cooperation from Russia. The alternative would be for the United States to impose an oil import duty or a minimum price regime, for which there are historical precedents. This risk is a reminder to OPEC to restrain the drive for market share at the expense of the US oil industry. It is a matter not of resource scarcity but of politics.

Since 2016, Russia has been actively cooperating with OPEC, first in a drive to restrict volumes supplied to the oil market in order to reduce inventories built up during preceding years, then to boost supplies in order to moderate prices.

Sanctions are not the only reason for stagnation and low productivity in large parts of Russia's oil and gas industries. From a petroleum geology perspective, most of Russia consists of mature petroleum provinces, i.e. areas that have been extensively explored, where the largest deposits have been found and developed and much of the oil has been pumped out. The trend is rising costs and declining output because the remaining resources are in old prospects in need of additional investment or in new prospects with a remote location, technical obstacles, etc. These problems are not unique to Russia; they have been evident for decades in North America and the North Sea.

Due to past investment, Russia's oil industry has proved to be robust considering sanctions and low oil prices since 2015.² In terms of volume, not profit, Russia is likely to remain a leading oil producer and exporter for the foreseeable future. In the oil market, Russia is both a competitor and a potential partner for the GCC countries. In the short term, Russia and the GCC countries face a common competitor in the US oil industry. Consequently, there is a basis for cooperation on oil market and oil price stabilization.

Interests reversed

In the old oil order, the swing producer was the GCC countries, and particularly Saudi Arabia, which by adjusting volumes could influence prices. In the new oil order, the swing producer is the United States, whose volumes are price sensitive but also moderate price movements.³ In the old oil order, the axis between the United States (the major importer) and the GCC countries (the major exporter) was decisive, with the latter often adjusting sales volumes to the fluctuations of US imports in order to stabilize prices. In the new oil order, the axis has been retained, but it tends to function differently, with the GCC adjusting volumes to stabilize prices at a level favorable to US unconventional oil.

In the old oil order, the United States was a market for oil from the GCC and Russia. In the new order, US oil competes with oil from the GCC countries and Russia. In the old order, the United States as a large importer had an interest in moderate oil prices. In the new oil order, high costs and a higher self-sufficiency make the United States a champion for high oil prices. Simply put: in the old days, the United States had an interest in the GCC countries boosting their oil exports in order to moderate oil prices; these days, the United States has an interest in the GCC states managing their oil exports in order to keep oil prices at a level favorable to US shale oil, but not as high as to burden US consumers.

The GCC countries, with huge reserves and low costs, have historically had an interest in moderate oil prices because of long-term market concerns, but today the GCC states seem unconcerned about the

competitiveness of conventional oil and future demand – so far at least (Petroleum Intelligence Weekly, 2018a). Remarkably, Saudi Arabia seems to favour high oil prices. The motive is to cut deficits, to raise capital for ambitious economic reform, and especially to enhance revenue from a proposed partial privatization of the national oil company Saudi Aramco. This may be a temporary position, but the immediate effect is to realign Saudi Arabia with the United States on this issue. This realignment may be coincidental, but the effect is to distinguish the oil price interests of the GCC states and the United States from those of Russia, Iran and China.

Russia, by contrast, because of large reserves and lower costs, has an interest in more moderate oil prices in order to limit competition and to safeguard a long-term market for conventional oil (Petroleum Intelligence Weekly, 2018b). Iran has similar concerns. China, as the world's largest oil importer, has an interest in moderate oil prices, but also in secure supplies.

Nevertheless, stagnation and decline are threats for the longer term. Russia's interests in relation to oil are briefly stable, moderately high prices as well as access to technology, managerial expertise and international supply chains. Cooperation with OPEC, especially the GCC states, are a response to the first point. On the other points, cooperation with the GCC states and China are at best makeshift solutions as long as EU and US sanctions remain in place.

The GCC countries are pivotal in the world oil market. With their large reserves, low costs and usually available spare capacity, they can influence oil prices, if not decide them. They are also important in the world economy; through huge oil revenues, import policies and recycling of surpluses they influence trade patterns and financial flows. The combination of resources, money and a strategic location makes the GCC countries a key element in geopolitics as in geo-economics. Historically, the GCC countries have been politically and militarily aligned with the United States (before 1971 some of them with the United Kingdom). Positions in the GCC countries make an essential part of the US military primacy.

Since the turn of the century, oil price interests have realigned. Historically, the United States as a large importer had an interest in moderate oil prices, and Russia, as a large exporter, had an interest in high oil prices. The US interest in price moderation was shared by the GCC countries concerned about the future market for conventional oil. The breakthrough for unconventional oil has given the United States an interest in higher oil prices, an interest shared by Saudi Arabia in the run-up to Saudi Aramco partial privatization and facing budget deficits. By contrast, Russia has signaled an interest in more moderate oil prices out of concern for the rise of US unconventional oil. Likewise, the rising importers China and India have an interest in moderate oil prices. Consequently, the GCC countries as oil market pivots face conflicting interests from old and new partners.

The concurrent rise in US oil production and in China's imports is creating a new oil order. The axis between Saudi Arabia and the United States that contributed to oil market stability in the old oil order is unlikely to be replicated. This tandem was built on a wider reciprocity of interests including security and finance. In the new order, Saudi Arabia is but one of several large oil suppliers to China, together with Angola, Iran, Iraq, Nigeria, Russia and Venezuela. Likewise, China is but one of many markets for Saudi oil, together with Europe, Japan, Korea and the United States, and an increasingly important India (Nakhle, 2018).

Consequently, supply and outlet risks are becoming more diversified, giving market forces an edge over politics. This secular trend obstructs China's policy of developing comprehensive bilateral economic ties with key oil exporters. Flexible and shifting trade patterns make an obstacle to conducting oil trade in Yuan unless it should replace the US dollar as the leading international currency.

Even if the share of oil in the world energy market is diminishing, oil demand is rising in volume and oil remains a driver for change in the world economy. The rising oil self-sufficiency of the United States and rising Asian oil imports, to China especially, are restructuring the world oil market with profound consequences for international trade, the world financial system and the world economy. This restructuring also has important ramifications for security policy.

Peak or hills?

The issue of peak oil may be irrelevant. Even though oil is a finite resource, it is unlikely that the end of oil, so dramatically trumpeted in certain quarters, is an immediate problem. The question is rather what types of fuel from which sources will be available at what cost using which technology. The limitations are also found in the market, in consumer preferences, and in technological progress, as well as energy and environmental policy. Within this overall picture, real prices may vary from market to market.

Since the early 1970s, OPEC has had a real impact on the physical balance in the oil market, the perceived market balance and the price of oil. OPEC probably has the resources to play the same role for several decades to come, given a certain consensus on strategy and the distribution of market shares and revenues. Oil prices below current levels in order to weaken and delay investments in alternatives are probably in OPEC's long-term interest.

Shale gas and shale oil are changing fundamental conditions in the international energy markets, primarily in the United States but with ripple effects throughout the world. Only a few years ago, the outlook was for the United States to become a major importer of liquefied natural gas LNG, straining the world market. Instead, the technological progress in shale extraction is leading the United States toward natural gas self-sufficiency and possibly net exports, as well as a significant growth in US production of oil and reduction of oil imports. For the US economy, immediate benefits include a reduced trade deficit, likely to strengthen the dollar, and a competitive advantage for manufacturing industry through lower energy costs.

For the United States, the breakthrough in shale gas and shale oil will once again defer the American encounter with the mandate to improve energy efficiency by means of taxes and fees. When peak oil and peak gas are put off once again, energy savings can also be put off. Oil use in the United States is economically far less efficient than in Europe or Japan, indicating a large potential for energy conservation. However, it is politically difficult to tax motor fuel, which would provide incentives for oil use efficiency and government revenue. A coalition of the automobile industry, oil interests and real estate and construction interests has sufficient influence in Congress to prevent harsh measures to reduce such oil demand. The preference is for increased supply incentives that benefit private business interests.

The conclusion is that no one knows the extent of the world's oil resources or how much the industry will recover with what technology, at what expense, at what price and at what time. Therefore, the theory of peak oil should not be accepted without reservations. Large areas of the world have been little explored.

Any estimate of future oil production by Hubbert's or other models needs assumptions on reserves and the producers' interests and strategies, but they are not constant. In the United States, the oil reserve-to-production ratio has been about ten-to-one for the past thirty years, but the country is still one of the world's leading oil producers.

None of the assumptions of the peak oil theory corresponds to reality. Knowledge of the world's oil reserves changes through exploration. Insight and technology cause a continuous update of reserves. The actual extraction can take many different shapes depending on the interests and strategies of the resource owner, in addition to technology and economics. Technology is not constant, new equipment and new methods lower costs and open new opportunities. Oil prices do matter, especially for investment in marginal resources. Not all oil producers have the same objectives.

It is important to emphasize uncertainty about resources and recovery rather than the scarcity or abundance, not least since the definition of oil is unclear and the supply of substitutes for conventional oil is uncertain. Geologists often have a pessimistic view, emphasizing scarcity. The counterpart is a temptation among economists to overestimate the effects of incentives on energy demand and supplies, regardless of the physical resource base.

Notes

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- 3 Morse, E. (2016). Welcome to the new oil order. *Financial Times*, 28 January.

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What role for OPEC in the last generation of oil?

Greg Muttitt

The world's transition to a low-carbon economy presents a fundamental challenge to the future of oil exporters. While OPEC members face significant vulnerabilities from the physical impacts of a changing climate (Mebayedh, 2013, pp. 2–3; UNDP, 2018), this paper focuses on the transitional challenge for oil-dependent economies. For governments to achieve the Paris Agreement goals, global emissions must reach net zero early in the second half of the 21st century (UNFCCC, 2016, article 4.1). With dramatic reductions in fossil fuel use needed over the next thirty years, we are entering the last generation of oil.

This paper begins by examining OPEC's (and especially Saudi Arabia's) strategies on climate change since the issue emerged on the political scene in the late 1980s. It then assesses the prospects for oil demand, based on current political and technological trajectories, and the challenges for OPEC members. Finally, the paper considers how decisions on oil supply may offer opportunities for OPEC to contribute to addressing climate change.

OPEC and the politics of climate change

OPEC's interpretation of climate change

During the early years of international climate politics in the late 1980s and 1990s, OPEC largely interpreted the problem within the frame of its existing battles with oil-consuming countries over capture of economic rents and relative economic power. Much of OPEC's political effort went into opposing European proposals for a carbon tax. The reason was that consumption taxes increase the revenue obtained by consuming country governments, at the expense of producers. Saudi oil minister Hisham Nazer (1992, p. 6) commented,

As oil producers and exporters, we have seen our main export commodity, and the engine of our growth, excessively taxed in the industrialized consuming countries and more so in the EC, the latest of which is the taxation under the environment pretext.

OPEC (2018) estimates that in 2017, over 50 percent of the price of fuel in the OECD went to consuming country governments in tax, while just 27 percent represents the price of crude oil (which is shared between costs, producer government revenue and company profit). Noting that industrialized countries

subsidized their domestic coal industries while taxing (largely imported) oil, OPEC¹ rightly argued that a true carbon tax would apply to all fossil fuels in proportion to their carbon content. Less reasonably in the context of climate change, OPEC has also criticized subsidies for renewable energy sources such as solar and wind.²

Following the oil price rises of the 1970s, consuming governments supported oil production in their own countries, as well as acting to reduce oil demand. These two responses led to a collapse in the oil price in 1986. Less than three years later, the World Climate Conference in Toronto initiated international climate negotiations.

OPEC's communications thus portrayed climate change as a ruse for consuming countries to reverse the gains OPEC had made over the previous twenty years³ and questioned the scientific evidence for climate change. For example, OPEC's 1997 statement to the Kyoto climate summit said, 'Scientific opinion is far from unanimous about the very existence of such a threat, let alone about the causes and effects.'⁴ However, rejection of the science become progressively untenable over the course of the 1990s.

OPEC members resisted progress towards the UN Framework Convention on Climate Change in 1992 (Kjellén, 1994, pp. 156–157). Then during the first Conference of Parties (COP1) in 1995, OPEC and the US blocked the start of negotiations that would lead to the Kyoto Protocol, until the US was eventually pressured to back down, leaving OPEC unable to prevent progress alone (Oberthür and Ott, 1999, pp. 45–46). Often these efforts were coordinated with Don Pearlman, a US lawyer representing fossil fuel interests.⁵

If OPEC had recognized the genuineness of the science and that ultimately climate change would mean a limit to the oil economy, OPEC might have taken the issue as a warning sign to get serious about economic diversification. It could also have been involved in framing the solutions – for example, a rational transition away from fossil fuels with negotiated prices rather than the tax-based, market-oriented approach that took hold.

Conflict with developing countries

OPEC has always identified as a part of the Global South, indeed as its champion. After all, OPEC members' oil nationalizations in the 1970s marked the most significant success in the battle for permanent sovereignty over natural resources, the issue that dominated North–South relations in the immediate post-colonial period. In marking its fiftieth anniversary, OPEC (2010) explained,

The formation of OPEC was a brave act, a pioneering act, an act that demonstrated that even developing countries had rights. Their indigenous resources were more than just a convenience for others.

Within climate negotiations, OPEC often couched its discussion of impacts on its members as impacts on developing countries as a whole, noting that fossil fuels account for 34 percent of OECD countries' total imports from developing countries (al-Sabban, 1992). However, OPEC's opposition to international action was at odds with the views of most Southern countries, as the worst impacts of climate change are felt by the poorest people and countries.

When OPEC called for its members to be compensated for any economic losses arising from climate mitigation,⁶ many developing countries objected to the idea that limited funds to support the most vulnerable might be diverted to relatively well-off countries that had benefited from fossil fuels.⁷

At COP1 in 1995, as OPEC tried to block the start of negotiations towards a protocol, an ad hoc 'Green Group' emerged comprising most of the G77⁸ excluding OPEC, which agreed to cooperate with the EU to start progress (Oberthür and Ott, 1999, p. 46). The following year at COP2, when OPEC members argued against using Intergovernmental Panel on Climate Change (IPCC) reports as the basis for

a protocol, the meeting chairs navigated around the blockage by ‘taking note’ of the summit declaration rather than formally adopting it, so that OPEC members could file reservations but not prevent its recognition (Bodansky, 2001, pp. 35–36).

After being isolated twice from developing countries, OPEC members moved to strengthen their position within the G77. However, OPEC members’ stances diverged and OPEC ceased to operate as a bloc in the negotiations. Several members – including Iran, Nigeria, Ecuador and sometimes Venezuela – moved into somewhat more cooperative positions, reflecting both their own relative dependence on agriculture alongside oil (Dessai, 2004, pp. 26–27) and growing alliances with climate-vulnerable countries, especially in Africa and Latin America.⁹ For instance, despite initial fears about its OPEC membership, Nigeria was seen as a constructive and flexible chair of the G77 in 2000.¹⁰

Saudi Arabia on the other hand continued to resist progress, at times doing so through the G77. By 1999 however, the Earth Negotiations Bulletin reported, many developing countries were ‘challenging the Saudis’ attempts to usurp some of the Group’s negotiating positions for its own ends’.¹¹ A survey by Suraje Dessai (2004, p. 20) finds that G77 delegates saw OPEC as having a negative, obstructive role in the process, which created resentment among other delegations. In a study of Saudi Arabia’s behavior in climate negotiations, Joanna Depledge (2008, p. 10) accuses the Kingdom of ‘the sustained and aggressive use of obstructionist tactics ... actively seeking as little progress as possible, as late as possible’. These tactics included seeking postponement of negotiating items, refusing to negotiate (sometimes asking for more time to read documents), refusing to join a consensus on resolved items, citing procedural rules to frustrate talks or proposing text they knew would be unacceptable to other parties (Depledge, 2008, pp. 23–26; Dessai, 2004, pp. 23–24). The Kingdom was commonly supported by other GCC members, especially Kuwait (Luomi, 2011, p. 262). Nonetheless, they have been forced to moderate their positions when faced with enough counter-pressure from other G77 members, unwilling again to fully split from the G77 group (Kjellén, 2008, pp. 75–77).

Partial participation

Saudi Arabia (2005) implicitly acknowledged the reality of climate change in 2005. However, the Kingdom has remained one of the most active states calling for changes to IPCC reports, usually for weaker conclusions,¹² and has opportunistically attacked the science in public from time to time.¹³

Saudi Arabia has continued to push the negotiations to address the impact of climate ‘response measures’ on economies such as its own. At times, Saudi insistence that response measures be part of any negotiated package has held up discussions on supporting more vulnerable countries’ adaptation to climate change impacts (Depledge, 2008, p. 16). Today, the Kingdom only occasionally requests compensation, more often asking for technology transfer and investment. These latter requests are eminently reasonable, but in light of the previous negotiating positions they are not generally warmly received.

After the failed Copenhagen climate summit of 2009, Saudi Arabia sought to ‘find a way to climb down gracefully from the country’s tough negotiating position’, according to a US diplomatic cable leaked to WikiLeaks.¹⁴ In 2012, Saudi Arabia replaced its long-standing negotiator Mohammed al-Sabban, who was widely seen as driving the Kingdom’s negative position.¹⁵ Saudi Arabia subsequently moved closer to powerful developing countries, joining a new negotiating bloc known as the Like-Minded Developing Countries, along with China, India and 18 others. Saudi Arabia put more emphasis on echoing demands that industrialized countries should do the most to address a problem they largely caused and should provide finance to enable developing countries’ efforts. While these demands were (up to a point) reasonable and widely held, they had not been Saudi Arabia’s priority, suggesting it was at least partly motivated by political positioning.

Despite participating constructively now in most aspects of climate negotiations, Saudi Arabia opposed a review of the adequacy of the global long-term temperature goal. In 2010, when numerous countries

requested the UNFCCC Secretariat prepare a technical paper on options for limiting global temperature rise below 1.5°C or 2°C, Saudi Arabia blocked the proposal, supported by Kuwait, Qatar and Oman. This became a rare occasion when OPEC countries openly disagreed, with both Nigeria and Venezuela opposing the Saudi position. Meanwhile the Barbados delegation commented that it is ‘ironic that other developing countries are blocking it,’ and asked whether ‘this is the solidarity and brotherhood they speak so eloquently about’.¹⁶

When other countries later overcame Saudi objections, a three-year review was conducted, which found that 2°C should be considered a dangerous level of climate change (UNFCCC 2015, p. 18). Saudi Arabia tried to keep the review’s conclusions out of the wider negotiations¹⁷ and then out of the COP decision at the Paris summit.¹⁸ Ultimately, Saudi Arabia’s efforts to prevent the increase in ambition failed, as the Paris Agreement tightened the goal from aiming for 2°C above pre-industrial levels to keeping warming *well below* 2°C and pursuing efforts to keep it to 1.5°C (UNFCCC 2016, article 2.1(a)). Today, global average temperatures are about 1°C above pre-industrial, which is already resulting in more frequent extreme weather events and exacerbating chronic tensions such as damage to food production and increased migration.

In sum, although OPEC and Saudi Arabia have not been the most important barriers to progress in the international climate process,¹⁹ their confrontational stance has delivered diminishing returns as the science has hardened and climate limits are approached. It has also come at three costs. First, it has deprived OPEC of the opportunity to influence the frame of negotiations in ways that are less damaging to its interests. Second, it has incurred diplomatic and reputational damage, crucially among developing countries. Third, it has created a legacy of distrust such that even reasonable positions tend to be met with suspicion.

Oil demand and climate change

Peak oil demand

Despite its opposition to the 1.5°C goal, Saudi Arabia quickly ratified the 2015 Paris Agreement, which was also welcomed by OPEC as a whole (OPEC, 2016, p. 1). It has been signed by all 15 OPEC members and ratified by all except Angola, Iran, Iraq and Libya. If governments achieve the emissions pledges they made in Paris, oil demand could peak in 2029, according to OPEC’s World Oil Outlook (OPEC, 2016, pp. 333–334). The Agreement includes periodic review of the adequacy of pledges, which are likely to tighten as they currently set the world on course for 2.6–3.2°C of warming²⁰, falling short of the Paris goals.

According to scenarios used by the IPCC, achieving the Paris goals would require global carbon dioxide emissions to be cut by half by the 2030s compared to 2010 levels, and to reach zero by some time between 2045 and 2070 (Rogelj, 2015, p. 520). This implies a major reduction in combustion of all three fossil fuels, coal, oil and natural gas, to near zero within a few decades.

Even while now accepting the science of climate change, Saudi Arabia has adopted an inconsistent position of insisting emissions reductions must not affect the use of oil. For example, seven months before the Paris summit, the oil minister stated

The Saudi oil industry cares about, and gives priority to, the environment and climate change. ... That said, we will stand up, firmly and resolutely, in solidarity with a number of countries, against any attempt to marginalize the use of oil.²¹

To try to square this circle, since 2007 OPEC has promoted carbon capture and storage (CCS) as a means to reduce emissions while still burning fossil fuels. However, CCS technology has fallen short of expectations, leading many governments and companies to drop their support (Muttitt, 2016, p.48), with experts

judging it too expensive compared to renewable energy.²² In the words of Francesco Starace, CEO of Italian utility Enel and chair of trade association Eurelectric, ‘I think CCS has not been successful. It doesn’t work, let’s call it what it is – it is simply too expensive, too cumbersome, the technology didn’t fly.’²³ Even if there were a CCS breakthrough, fossil fuel combustion would still need to shrink by an order of magnitude. CCS cannot be applied to transport, the primary use of oil, only to stationary emissions sources. The International Energy Agency (2016, p. 327), a promoter of CCS technology, projects that only three billion tons per year of carbon dioxide could be captured by 2040. Emissions from fossil fuels are currently 36 billion tons per year (Le Quéré et al., 2017, p. 429).

Today, politics are no longer the sole driver of a transition to clean energy. Recent years have seen significant technological progress in renewable energy and – more importantly for oil – vehicle electrification. Combined with existing structural trends including greater fuel efficiency, OECD saturation of private transportation and lower car ownership within the millennial generation, this has led to increasing (though hotly debated) talk of oil demand peaking, perhaps as soon as the 2020s²⁴ (DNV GL, 2018, p. 12, 30).

A losing hand

On the face of it, OPEC ought to be competitively well positioned to succeed in a declining market for oil as its oil generally costs less to extract. This is particularly the case for the Middle Eastern OPEC members, whose oil on average costs \$9 per barrel to extract compared to \$24 for non-OPEC members (Rystad Energy, 2018).²⁵ If demand is constrained and the global oil price falls, non-OPEC’s production will generally become unviable before OPEC’s. But the timeframes matter. While international oil companies aim to extract fields as quickly as they can, OPEC members generally do not do so, in order to both conserve reserves for future generations and sustain a higher oil price. At current rates of extraction, OPEC reserves would last 85 years, compared to 25 for the rest of the world (BP, 2018, p. 12).

If the world were to rationally allocate the remaining carbon budgets to the lowest-cost resources, the majority would therefore go to OPEC production. In reality, markets operate over a shorter timeframe than the decades over which carbon budgets are depleted; and climate policy will progressively tighten over that period. As a result, higher-cost, non-OPEC resources continue to be viable in the near term, while some of OPEC’s longer-lived reserves will get left behind as climate policy bites. A study by Christoph McGlade and Paul Ekins (2015, p. 189) finds that with an escalating carbon price, 38 percent of Middle Eastern and 39 percent of Latin American oil reserves will get left unburned by 2050, but only 6 percent of US reserves.

Several studies use game theory and/or integrated assessment models to explore options for OPEC’s production strategy in an emissions-constrained world. Commonly they find that revenues will decline due to mitigation of climate change, even if OPEC behaves optimally while it occurs (Ghanem et al., 1999; Loulou et al., 2008). They also find that racing to extract the reserves before markets disappear, as suggested in Hans-Werner Sinn’s ‘Green Paradox’ (2012), would actually leave the oil exporters worse off, because the resulting fall in price would outweigh the increase in volume (Loulou, 2008, p. 21; Cairns, 2013). OPEC members face a severe threat to their economies from reduced oil demand.

New urgency for diversification

To mitigate the economic threat, OPEC members will need to reduce their dependence on oil (Van de Graff and Verbruggen, 2015, pp. 460–461; Fattouh et al., 2018, p. 21). As early as 1936, Venezuelan writer Arturo Uslar Pietri proposed ‘sowing the oil’: using its revenues to build up non-oil sectors of the economy (Uslar Pietri, 2016). The need to diversify oil-dependent economies has been a common refrain ever since. In the case of the GCC members, as the Economic and Social Commission for Western Asia

(ESCWA, 2001, p. 1) puts it, ‘Economic diversification has been the by-word and catch phrase of economic policy in the Gulf countries ever since the first oil boom.’

Success to date has however been very limited. Nouf Alsharif and colleagues (2016: 44) assess the change of oil’s share of exports since 1960 in 35 countries. Only in eight countries did oil’s share consistently decrease over the period. Even in a relatively successful case, Indonesia, oil’s share took 30 years to fall from 50 percent in 1970 to about 15 percent in 2000. In Saudi Arabia, oil’s share fell from 95 only to 85 percent over the same period, despite diversification being a top policy priority and despite having significant resources to invest in alternative sectors.

There are significant difficulties in moving away from heavy oil dependence. Oil activity generally inflates the currency, wages and land values, making non-oil sectors uncompetitive (Alsharif et al., 2016, pp. 10–12). Oil-rich governments often rely on political patronage, creating political barriers to change. High oil production is strongly correlated with external debts, and ongoing debt service commitments create a further need for export revenues (Kretzmann and Nooruddin, 2005). Diversification can increase inequality: Michael Herb (2014) shows that diversification in the UAE has primarily benefited private capitalists, while in low-population countries, oil revenues tend to be better shared among citizens. Finally, one popular route to diversification through building sectors with linkages to the oil sector, such as refining and energy-intensive industries, may be partially also closed off for the low-carbon transition.

Faced with these structural obstacles to economic diversification, OPEC members would likely benefit from technical assistance, investment and coordination. This need recalls what was arguably OPEC’s greatest historical success, coordinating member countries’ actions in their battle for a fair deal from the ‘Seven Sisters’ that ran their oil industries in the 1960s and 1970s. Oil producers today face a challenge at least as large as their earlier exploitation by multinationals: how to adapt their economies in a carbon-constrained world. This profound transition, faced by all members, suggests a strong potential role for the organization. Help is unlikely to come from elsewhere as long as OPEC holds its negative reputation on climate.

Oil supply and climate change

Reframing climate change mitigation

Drawing lessons from the history of OPEC’s engagement with climate change in Part I, could OPEC shed its negative reputation enough to earn sympathy and assistance from other countries? Furthermore, could it reframe the international approach climate policy in a way that makes its members’ transitions less difficult?

To date, international climate policy has sought to limit carbon is tackled where it is burned rather than where it is extracted, with any carbon taxes shifting revenues from producers to consumer governments. OPEC’s longer-lived reserves will be disproportionately left in the ground, while other producers continue to develop costlier sources. Meanwhile, G7 countries are estimated to provide \$37 billion per year of subsidies to fossil fuel production in their territories (Bast et al., 2015, p. 41) and have shown considerable reluctance to reform or even recognize the subsidies. Pete Erickson and colleagues (2017) calculate that nearly half of yet-to-be-developed US oil production is dependent on subsidies to be profitable. Removal of these subsidies would serve both climate mitigation and OPEC; however, as long as climate policy focuses on consumption of fossil fuels, these production subsidies get far less attention.

Looking at things more broadly than the policy orthodoxy, the climate problem is driven by a flow of carbon from safe underground stocks, via the human economy, to the atmosphere. A ton of extracted carbon ultimately becomes a ton of combusted carbon in the form of carbon dioxide. A growing body of literature suggests that restricting fossil fuel supply can also be an effective part of efforts to mitigate climate change (Lazarus et al., 2015; Fæhn et al., 2017; Green and Dennis, 2018). Indeed, it is arguably a necessary

part: capital-intensive investments tend to *lock in* emissions, as the resulting infrastructure economically and politically incentivizes its continued operation (Unruh, 2000; Seto et al., 2016).

This literature is beginning to shape policy. The World Bank Group announced in December 2017 that it will no longer finance upstream oil and gas after 2019, in order to ‘align its support to countries to meet their Paris goals’. Shortly afterwards, France passed legislation to end new oil licensing, and to end all production by 2040. Licensing bans exist in Costa Rica, Belize and offshore New Zealand, and Ireland is currently legislating a ban. Some larger producers are facing calls to join this group. In Norway, an opinion poll found 44 percent of respondents favored curbing oil production to protect the climate; Canadian public opposition to new tar sands pipelines has created a political crisis for the Trudeau government; in California, over 750 environmental, labor, health and social justice groups called on Governor Jerry Brown to phase out oil production within the state (Muttitt, 2018, p. 5).

Could OPEC members, with a very large share of oil reserves and production, contribute to climate change mitigation by restricting their extraction? After all, OPEC co-founder Juan Pablo Perez Alfonso commented, ‘Most people see OPEC as a way to raise oil prices, but I see it as a way to lower the use of energy.’²⁶ To date, two concrete proposals have been made towards restricting OPEC supply: to leave some oil unextracted in exchange for compensation and to apply an export tax on oil.

Ecuador’s Yasuní-ITT proposal

In 2007, Ecuador proposed to leave untapped its ITT oilfield in the Yasuní National Park in return for compensation from the international community for half of the forgone revenues. Ecuador would act to limit oil extraction (and hence emissions) if others were willing to share the costs, given Ecuador’s own limited means and pressing developmental needs (Rival, 2010, pp. 358–259). Ultimately, the initiative failed: it was abandoned in 2013 after only \$116 million of the requested \$3.6 billion was pledged. One reason was that some donors – notably Germany – did not want to set a precedent (Sovacool and Scarpaci, 2016, p. 165). After all, Yasuní-ITT accounts for just 0.05 percent of the world’s oil reserves.

It is quite reasonable that countries dependent on fossil fuels should ask for support in transforming their economies as part of a cooperative effort to address a global problem. But on top of the problem of scalability, the notion of *compensation* – determined by the size of unextracted reserves – raises the question of why Ecuador should be deserving of international funds when its right to extract lies only in its geological fortune, in contrast to a developing country without oil resources that would be doing no more to help or harm the climate than Ecuador. The present author suggests elsewhere (Muttitt and Kartha, 2019) that oil-dependent countries might better request transitional support rather than compensation.

However, an important lesson from the Yasuní-ITT proposal is that it was more warmly received than OPEC’s earlier claims for compensation in the UNFCCC. Ecuador was offering to proactively restrict its extraction as its share of the bargain and as an earnest contribution to solving the climate problem; it requested only half of the revenues it would have received from extraction (Larrea and Warnars, 2009, p. 221, 223). As Sivan Kartha et al. put it (2016, p. 4), ‘A country is only likely to succeed in inducing reciprocal effort among its negotiating partners if it is perceived to be doing its fair share of the effort.’

Export taxes

While OPEC has raised concerns about carbon taxes transferring more of the oil rents from producing to consuming governments, a long-term alternative might be to locate carbon pricing at the point of production or export. Economist Herman Daly (2001) proposes such an approach, on grounds that with fossil fuel extraction more spatially concentrated than combustion, OPEC may be a stronger place to locate a tax than the diffuse collection of consumers. In 2007, Ecuador adopted a version of the proposal, whereby 3–5

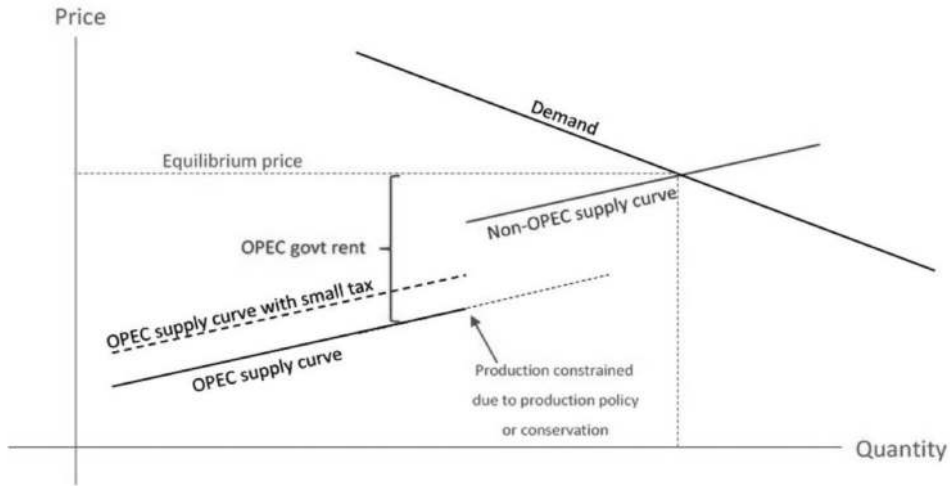


Figure 28.1 Demand/supply graph showing OPEC vs non-OPEC, and impact of export tax
Source: adapted from Loulou et al., 2008, p. 3.

percent of revenue from oil exports to industrialized countries would be used as climate finance, to support the most vulnerable countries.

At present, such an approach would be necessarily limited. The oil rents received by government are determined by the interaction between global demand and the cost of producing the marginal barrel, which is generally in the costlier non-OPEC, as shown in Figure 28.1. A small tax, less than current rents, will not change the market balance between producer and consumer, it would just become an alternative means of capturing the same rent.²⁷ In order to shift the market dynamics, a tax would have to exceed current rents, push OPEC into the higher part of the cost curve, including the marginal barrel of production. OPEC would lose some market share but sell at a higher price. We turn to the question of volume versus price in the next section.

Winding down production

One of OPEC's most obvious tools is making decisions about production and investment levels. Could OPEC restrain its production in line with climate limits, using increased revenues (due to a higher oil price) to help finance the transition, and perhaps also to rebuild Southern solidarity by supporting climate adaptation and transition in the poorest developing countries?²⁸

The economics literature has extensively explored optimal OPEC strategies (see Fattouh and Mahadeva, 2013 for an overview). There are two limits to OPEC's ability to maximize revenues by restricting production. First, too high a price may induce consumers to consume less oil and switch to alternatives. Second, and more importantly, OPEC accounts for only about 40 percent of global oil production. If the price increases too much, that will make the more expensive, non-OPEC production viable; and as that production increases, OPEC market's share will progressively decrease. This happened following the oil shocks of the 1970s: OPEC's share of production fell from around 50 percent in 1975 to 30 percent in 1985. So, a higher oil price leads to greater production elsewhere and at the same time reduces demand. The balance between these two effects – which depends on the price elasticities of demand and supply (Lazarus et al., 2015, pp. 13–15) – determines the net emissions reduction.

It is not the aim of this paper to model a progressive reduction in OPEC supply. However, we can sketch the outlines of the issue. In contrast to most modeling studies, the question here is not what level of production optimizes OPEC members' income; rather, it is whether expansions elsewhere (such as the US) would cause OPEC's market share to drop to the extent that a supply reduction strategy becomes economically unviable. At the time of writing, it is unclear how much non-OPEC producers could potentially increase production in the event of a rising oil price. Rystad Energy (2018) suggests that non-OPEC production could increase by about 10 mb/d by 2024, equivalent to a quarter of OPEC production. However, this includes an increase in US production of 9 mb/d, of which 6.5 mb/d is in the Permian basin alone; given fracking's uncertain geology, often challenging finances and limited infrastructure, it remains to be seen whether this can be achieved.

One dimension of this question is whether in signaling a long-term intention, OPEC gives competing producers confidence that price will remain high and thus that they can increase investments in high-cost production with less risk. Another is that climate policy and technological change will ultimately lead to sustained reduction in oil demand for the first time since the early 1980s: this may further reduce OPEC's market share as well as driving down price (or alternatively deter competing, high-cost investment); evidence also suggests that when demand is falling, quota compliance is hardest to achieve (Fattouh and Mahadeva, 2013, p. 13, 20; Fattouh and Sen, 2015, pp. 82–83). The economic potential for OPEC to progressively reduce production as part of a long-term phase-out plan warrants further study. More interesting still is the political questions of what impact such a policy could have on reframing climate discussions, the extent to which it would encourage or pressure other producers to follow suit and whether other countries would welcome OPEC's commitment to climate action versus (more self-interestedly) objecting to higher oil prices.

Conclusion

In the 1990s, OPEC adopted a confrontational stance towards international climate negotiations, an approach that was subsequently continued by Saudi Arabia and its Gulf allies. They were forced to beat a progressive retreat due to pressure from other developing countries and to a hardening scientific consensus on the climate threat. The politics of the climate negotiations are today unpredictable, with Trumpism on the one hand and significant drivers for greater ambition on the other as climate impacts are felt more strongly. At the same time, rapid technological development may lead to a peak in oil demand in the coming years. In this context, there may be little to be gained by attempting to hold back a transition away from fossil fuels.

The confrontation came at a cost. While rejecting the science and opposing actions to reduce emissions, OPEC missed an opportunity to shape the framing of climate solutions in a way that could have enabled its members' economies to adapt, such as putting the onus on reducing extraction of expensive, non-OPEC oil and the significant subsidies given to it. Now, in spite of OPEC members' participation in the international process, the legacy is one of distrust, such that even reasonable proposals tend to be seen as blocking tactics.

Given the need and potential for a rapid energy transition, OPEC members will urgently need to transition their economies away from dependence on oil exports. Yet the historical record shows that attempts to diversify commodity-dependent economies have rarely succeeded. OPEC can play an important role in supporting its members through the transition, but wider assistance from the international community is unlikely to be forthcoming unless OPEC sheds its negative reputation on climate. Though ultimately unsuccessful, the warmer response to Ecuador's Yasuní-ITT proposal compared to earlier OPEC claims for compensation indicates how trust may begin to be rebuilt. Ecuador asked for compensation for only half of the forgone revenues: the country was prepared to give something up itself.

While OPEC cannot solve climate change on its own, this paper has argued that it can play its part. Accepting a long-term reduction in oil exports and the need to undergo a difficult economic transition, OPEC could start to show that it is serious about addressing climate change, which would help dispel the legacy of distrust. Going further, OPEC could commit to restraining its oil production in line with climate limits. The full positive or negative economic impacts on OPEC members of such a course will depend as much on political reactions as on market responses. It would put the spotlight on subsidized oil expansion in countries like the US, UK and Canada while creating significant space for others to follow suit in restricting production. Climate change presents a challenge to oil exporters perhaps even greater than when their economies were dominated by foreign companies. OPEC once again has an opportunity to lead.

Notes

- 1 *Middle East Economic Survey* (1997). OPEC makes case for 'balanced agreement' from Kyoto Climate Change Conference. No. 49, 8 December.
- 2 Bergin, T. (2009). OPEC says oil not to blame for climate change. *Reuters*, 2 April. Available from: www.reuters.com/article/opece-environment-idUSL225721020090402
- 3 *OPEC Bulletin* (1994). Commentary: Is oil still in for a taxing time? February, p. 3.
- 4 *Middle East Economic Survey* (1997). OPEC makes case for 'balanced agreement' from Kyoto Climate Change Conference. No. 49, 8 December.
- 5 *Der Spiegel* (1995). Hohepriester im Kohlenstoff-Klub. 3 April. Translation at <http://research.greenpeaceusa.org/?a=download&d=2167>
- 6 *ENB (Earth Negotiations Bulletin)* (1996). COP2 Summary, 22 July. International Institute for Sustainable Development, p. 3. Available from: <http://enb.iisd.org/enb/vol12/>.
- 7 *ENB (Earth Negotiations Bulletin)* (2010). SB32 (7), 11 June. International Institute for Sustainable Development. Available from: <http://enb.iisd.org/enb/vol12/>.
- 8 The G77 is the official negotiating bloc comprising all developing countries.
- 9 This has included participation respectively within the Africa Group, ALBA and CELAC negotiating blocs.
- 10 *ENB (Earth Negotiations Bulletin)* (2000). SB12 Final, 19 June. International Institute for Sustainable Development, p. 14. Available from: <http://enb.iisd.org/enb/vol12/>.
- 11 *ENB (Earth Negotiations Bulletin)* (1999). COP5 Final. 8 November. p.15. Available from: <http://enb.iisd.org/enb/vol12/>.
- 12 *ENB (Earth Negotiations Bulletin)* (2013). IPCC36 Final, 29 September. International Institute for Sustainable Development, pp. 4–5. Available from: <http://enb.iisd.org/enb/vol12/>.
- 13 Black, R. (2009). Climate e-mail hack 'will impact on Copenhagen summit'. BBC News. 3 December. Available from: <http://news.bbc.co.uk/1/hi/sci/tech/8392611.stm>
- 14 US Embassy Riyadh (2010). Two faces of Saudi Arabia's climate negotiating position. Cable 10RIYADH184_a. 12 February. Available from: https://wikileaks.org/plusd/cables/10RIYADH184_a.html
- 15 Hmaidan, W. (2016). The wind of change hitting the Arab region? Heinrich Böll Stiftung. 12 December. Available from: <https://fb.boell.org/en/2016/12/12/perspectives-9-wind-change-hitting-arab-region>
- 16 *ENB (Earth Negotiations Bulletin)* (2010). SB32 (11), 11 June. International Institute for Sustainable Development, p. 1. Available from: <http://enb.iisd.org/enb/vol12/>.
- 17 *ENB (Earth Negotiations Bulletin)* (2014). COP20 (6), 6 December. International Institute for Sustainable Development, p. 4. Available from: <http://enb.iisd.org/enb/vol12/>.
- 18 *ECO* (2015). COP21 (3), 2 December. Climate Action Network, p. 1. Available from: http://www.climateactionnetwork.org/eco-newsletters?field_event_nid=5377; *ECO*. (2015). COP21 (5), 4 December. Climate Action Network, p. 2. Available from: www.climateactionnetwork.org/eco-newsletters?field_event_nid=5377.
- 19 The US withdrawals from the Kyoto Protocol and the Paris Agreement did more damage.
- 20 Climate Action Tracker (2018). Temperatures. Available from: <https://climateactiontracker.org/global/temperatures/>
- 21 Al-Naimi, A. (2015). Address to the Saudi Economic Association, Riyadh. 7 April. Available from: www.saudiembassy.net/statements/minister-al-naimi-address-saudi-economic-association
- 22 Rissman, J. and Orvis, R. (2017). Carbon capture and storage: An expensive option for reducing U.S. CO2 emissions. *Forbes*, 3 May.

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- 24 Katakey, R. (2016). Energy giant Shell says oil demand could peak in just five years. *Bloomberg*, 2 November. Available from: www.bloomberg.com/news/articles/2016-11-02/europe-s-biggest-oil-company-thinks-demand-may-peak-in-5-years
- 25 Global opex plus capex divided by production.
- 26 Steiner, S. (1979). The man who invented OPEC – to conserve energy. *Washington Post*, 16 September.
- 27 It may contribute to determining the relative shares of host government and private companies in the non-nationalized countries – this is the case, for example, in Russia and Argentina.
- 28 Let us assume for now that faced with an existential threat, OPEC can overcome its poor record of quota non-compliance (Colgan, 2014). Notably, the period from late 2016 to 2018 has shown significant compliance with quotas.

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