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OIL AND THE INTERNATIONAL OUTLOOK

Víctor L. Urquidi
Ruth R. Troeller, *Editors*

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Preface

The immense gap that has opened during the last few years between oil-exporting and oil-importing developing countries is certain to have changed the human geography of Asia and North Africa. At the same time the equally drastic changes in the balance of economic and political power which have taken place between the oil-exporters and the more developed world are rapidly being channeled into a new but nevertheless viable situation so that the first impact of the rise in the price of oil has been almost overcome.

The remaining recession and what is left of the strong inflationary trends —wich were accelerated though not caused by the increase in the price of oil— are slowly abating and even the current accounts of most Western countries with oil-exporting countries are quickly moving into surplus. Indeed, with increased imports by the oil-exporters and the gradual development of alternatives to oil, OECD countries, in the aggregate, should be able to show a substantial current account surplus.

Not so the oil-importing developing countries. For most of them, up to now, the situation has found only *ad hoc* offsets — mainly via new borrowing facilities on more or less concessional terms. No ready and lasting solution seems to shine on the horizon since these countries' import bills cannot possibly be matched by their export possibilities, except for those oil-importers whose cultural or political links with an oil-exporter —or group of oil-exporters— allow them to receive their oil under favorable conditions.

The social and political implications of such a sudden change are not less overwhelming for oil-exporters. They are faced with the possibility of almost 'instant' idustrialization and diversification and the immense riches that daily accrue to them are altering traditional patterns and shifting the balance of internal and external political

power relations, while psychological and social adjustment is necessarily slower. Simultaneously, the growth pattern for the Asian and North African oil-importers has been interrupted and basic needs, such as food and capital formation, have become apparently insurmountable issues.

It was in the light of these new developments that we organized a seminar entitled "Consequences and Alternatives of the New Energy Situation" within the framework of the 30th International Congress of Human Sciences in Asia and North Africa.

We invited scholars from Asia, North Africa and Latin America as well as from 'Western' countries in the hope that the presence of academics and men of action in the economic, political and social field who had given thought to the new situation would help shed more light on at least some of the most important and urgent aspects of this as yet unsettled and novel situation.

Our approach was interdisciplinary since we believe that the changes that are in the process of working themselves out are not restricted to any particular field. Thus, we drew up a programme that included the effects of the new energy situation on the social, economic and political life of the people, both in Asia and North Africa, and in Latin America. In addition, we felt that we could not omit the issues of changes in energy strategies and energy consumption —absolute or relative— as well as the development of alternatives to oil in the Western world since such changes will necessarily have far-reaching and amplified repercussions in Asia and North Africa.

The organizers are especially grateful to all the participants for the effort and interest that they demonstrated through their papers and during the meeting to elucidate the topics set up for discussion. We are also grateful to Professor Graciela de la Lama, President of the 30th Congress, for her personal support in holding this Seminar. We wish to acknowledge the assistance of the Ministry of Finance of Venezuela, through the Minister, Dr. Héctor Hurtado, for its financial support which made possible the presence in Mexico of the participants. Finally, the organizers are grateful to Mrs. Marcela Serrato for her valuable contribution in the preparation and revision of the materials that are now included in this book.

Mexico City, November 1976
Víctor L. Urquidi
Ruth R. Troeller

Summary of Discussion

The papers discussed in the Seminar dealt with the problem from four different approaches. First, a technical and economic focus was adopted to define the role that hydrocarbons may have in energy supply for future generations. Second, three basic problems related to the financial impact of the new situation were analyzed: balance of payments prospects of oil producers, impact of bilateral oil agreements upon the economic development of LDCs and the problems created by import lags, financial recycling and international monetary imbalance for the group of oil-exporting countries. Third, problems of a juridical nature raised by the emergence of raw material-producers' associations were discussed. Finally, the participants considered the general and social impact of the new situation for oil-importing countries.

In the following pages we present a résumé of some of the most important topics analyzed during the discussions, under the different approaches presented above.

1. *Economic and technical approach*

The starting point for the analysis of the present and future energy situation must be, according to Doctor Juan Eibenschutz, the fact that hydrocarbons are of a finite nature and that there is a definite time factor involved. In view of the so-called "energy crisis", humanity has become aware of the vital importance of oil for the satisfaction of energy needs and of the probability that major supply shortages may arise, especially at the regional level. In the short run, it is necessary to adopt measures to optimize output and to accelerate the transition towards new sources of energy to guarantee a sufficient energy supply. Nonetheless, in the

long run it will be impossible to satisfy humanity's energy needs without a reconsideration of oil uses, and ultimately, without a change in the scale of values of the human being. Some decades are needed to achieve technical changes.

The problem of hydrocarbon depletion is closely related, on one hand, to the stage of development in which new oil-producing states find themselves today and, on the other hand, to the prospects of practical application allowed by each of the alternative energy sources. Doctor Issam El-Zaim stated that inflation has weighed heavily upon the production costs of new oil fields, so that the spectacular results foreseen three years ago have not materialized. Insufficient production in the North Sea together with the limited success of nuclear programs in the United States and the European Economic Community, have stimulated technological research in the energy field in the direction of underground coal gasification. For the moment the latter appears as one of the most likely and plentiful future sources of energy; in his opinion, if one half of the coal reserves should be turned into gas, humanity would be assured the energy requirements for the next seven centuries.

From a technical point of view, the most important consequence of the oil price increase has been the reappraisal of the use of hydrocarbons. Undoubtedly, today there is a greater awareness of the future importance of oil as an industrial product and, in the near future, as a source of protein. Even assuming that in the short run humanity will still depend on hydrocarbons due to the impossibility of rapidly developing alternative energy sources and carrying out drastic changes, mainly in the present transport system, it is possible if not to avoid, at least to retard the foreseeable depletion of hydrocarbons.

According to Doctor Ian Smart, the replacement of hydrocarbons with new sources of energy should be seen in terms of a transition from cheaper to more expensive energy sources. The period over the next 8 to 10 years will be critical because immediate alternatives are not yet in sight. Moreover, the exploitation of new energy sources will have an increasing cost, as is already evident, until the day comes when dependence on nuclear fusion is established. This will mark the return to cheap energy. Until then, the development of new sources will be determined by the present structure of the oil sector, the fiscal policy of consumer and producer countries and the overcoming of the general economic crisis industrialized countries face due to the increase in the cost

of energy. The application of different alternative sources will also depend upon their environmental effect.

The influence of hydrocarbon depletion upon the development policies of industrialized countries will be decisive. Nonetheless, the participants in the Seminar also pointed to the negative effects a shortage of hydrocarbons may have on developing nations. As to the oil-producing countries, a decrease in oil income would undoubtedly aggravate the political, economic and ideological differences that keep them apart today. In regard to non-oil LDC's the shortage of hydrocarbons would preclude, for example, the adoption of techniques designed to improve agricultural production based upon a high consumption of energy.

The significance of the oil price increase in 1973 was amply discussed. Several participants noted that up to now the terms of oil traded for industrial products had deteriorated considerably, this being the reason why OPEC was created in 1960. According to one opinion, oil had not been the most convenient source of energy from a technical point of view, but essentially the cheapest one. Increases achieved in 1973 had been discussed and prepared some time before, and it would be difficult to accept the new oil price as a "political" price, but rather as the result of the structural market situation. Nevertheless, other participants noted that the price of any basic product is part of a political process because it is not possible to separate one group of factors from another. in any event, the fact is that the new prices —which in nominal terms will certainly continue rising to maintain the real purchasing power of oil, but that even at constant prices may increase— have brought about a transition in the strategy of the energy problem. Considering the prospect of depletion in the short or the long run, there is no other alternative than to put the transition from one source to another into practice, an expensive process in terms of financing and allocation of resources more within the reach of industrialized countries than of LDCs.

2. *The financial approach*

Seen from the financial angle the oil question seems to raise two major problems: one for the oil importing countries and another for the oil exporters.

For the industrialized oil importing countries, the problem is to recycle oil funds which cannot be readily transformed into ex-

ports to OPEC countries either because of a relative lack of sufficiently developed infrastructure in these countries or, for a great number of them, because of the small size of the population. Surprisingly, though, despite initial fears of collapse, the private international banking system has coped very successfully with the dramatic increase in petrodollar flows and the ensuing general shift from longer term investments to shorter maturities.

Oil exporting countries, on the other hand, are faced with a quite different problem. They can change the rate of depletion at will, but they must make such a choice in order to best protect the value of their future imports and their freedom to alter import patterns in accordance with future needs. However, since the oil price is expressed in dollars and since the value of the dollar is subject to change in terms of the value of other oil importing countries' currencies, oil automatically becomes cheaper for those countries whose currency appreciates against the dollar. This, Dr. Ruth Troeller pointed out, creates a measure of uncertainty on the part of the oil exporting countries, which can be avoided by using a unit of account based on a moving average of a number of currencies, such as Special Drawing Rights (SDRs).

Nonetheless, Dr. Troeller continued, oil importing countries should not peg the value of their currencies to a neutral unit of account, such as SDRs, unless the weighted percentages underlying SDRs or the like resemble closely the actual import pattern of each individual oil importing country. In fact, with the possible exception of Venezuela, no such correspondence exists. Dr. Troeller, therefore, proposed —and this proposal has already been adopted by a number of OPEC countries— that each oil exporting country create its own flexible, periodically revised currency basket in order to determine the value of its currency *vis-à-vis* the rest of the world, the basket being calculated according to some formula reflecting the country's import and investment pattern. Such a basket would allow adaptation to changing import and future investment patterns and thus not only prevent the erosion of the country's import potential but also ensure sufficient freedom for future financial planning.

Dr. Troeller's remarks raised a series of interesting comments mostly referring to the feasibility in practice of the OPEC countries providing for the administration of such a complex system. Some commentators reminded the panel that tradition should not be underrated and that, by and large, OPEC countries seemed to

exercise as much prudence as is generally ascribed to central bankers in their exchange rate policies. Dr. Troeller responded by pointing out that the large majority of OPEC countries had already chosen to adopt new exchange rate policies, including the innovation of individual currency baskets.

Dr. Haim Barkai stressed the importance of variation in interest rates should a country choose to manage its own currency basket, an observation with which Dr. Troeller wholeheartedly agreed, taking the occasion to expand on the need for carefully planned domestic financial policies in such a case.

Overall, the comments emphasized the urgency to reform the international monetary system in order to adapt it to the present state of economic relations.

With a longer run perspective, the participants devoted one session to the analysis of the present and future balance of payments position of oil countries. Doctor Wolfgang König's analysis started in this regard with the formulation of five basic questions: Who will be able to supply oil in the future? For what purpose? How much? At what price and under what conditions? His analysis allowed him to conclude that, in the short run, OPEC's supremacy will not be threatened, but that, due to the different income needs of oil countries they will be forced to maintain the price at its present level. Consequently, only the oil countries with a large amount of currency reserves and a small population, or those that have average reserves and important industrialization plans, will have a balance of payments surplus. But Indonesia and Nigeria, which have a large population and limited resources, will not accumulate any financial surplus in this period.

Following Doctor König's analysis, during the transition period 1978-1985, the access of new producers to the world oil market, as well as the development of new energy sources, will aggravate OPEC's internal conflict regarding the definition of the purpose oil should serve, the income requirements and the degree of urgency with which they are needed. A consequence of this dispute will undoubtedly be the weakening of OPEC and even the lowering of prices. In this period, the surplus accumulated from the preceding one will be smaller in oil countries with more resources; it will not exist in countries that sustain ambitious industrialization plans; and will turn into a deficit on current account in the case of countries with scarce resources. From 1985 on, the oil price will be determined basically by the importance that new sources of

energy may have. By then, if OPEC still exists, its main task will be to balance a policy of export diversification with the dependency derived from a policy of import substitution.

Most of the participants' interventions in the Seminar completed this basic scheme of analysis. It is not likely that consumer countries will continue importing oil at the same rate as in 1974 and 1975, nor that the present import pattern of oil countries will remain unchanged. The day will come when the latter derive benefits from their investment programs, and stop using oil as their only source of income. But, on the other hand, it may be considered easier to profit from the idle capacity of oil countries than to put development projects of alternative energy sources into operation, assuming it is desired to increase world energy supply. Until now, the amount of real income oil countries receive as benefit from their foreign investments is very limited; consequently, it is imperative to adopt effective measures to assure an export diversification policy in the oil countries. The need to allocate a part of the oil income for food imports together with the rapid depletion of oil deposits may ultimately wipe out the surplus of every producing country.

The data supplied by Doctor Rinaldo Pecchioli on the impact of the oil price increase upon the state of current account balances showed that the crisis of confidence that occurred in the international market during mid-1974 was only indirectly due to the accumulation of great surpluses in the oil countries. Furthermore, it was precisely these countries which played an important role in the stabilization of the Eurodollar market, allowing the international private capital market to provide the necessary financing requested by deficit countries as a consequence of the 1973 oil crisis. Anyway, it should be kept in mind that although this goal was attained, it was in fact responsible for the growth of the external indebtedness of the countries most seriously affected by the oil crisis, and, in the long run, it may force them to reconsider their financial and economic policies.

3. *The juridical approach*

The juridical problems created by recently formed associations of raw material producing countries are part of the scope of new methods brought about by changes in the international normative

order. According to Professor Covey T. Oliver, the establishment of cartels is contrary to the interest of humanity, for their goal is to protect individual and not collective interests. In his opinion, states should abide by the rules set by customary present law without attempting to substitute mechanisms of collective action for individual actions of each state.

Professor Oliver's views where the subject of a lively dicussion centered on two main points: the existing parallelism between state cartels and raw material producers' associations on the one hand, and the procedures followed today for the creation of rules of international law, on the other. Professor Sepulveda pointed to the substantial differences that keep state cartels apart from associations of raw material producers. These differences refer, among others, to the different goals they pursue and the opposite mechanisms one and the other resort to in fixing prices. Such associations are a clear expression of disagreement with the existing order and their demands should be considered legitimate for they propose to introduce a fairer and more equitable international economic order.

As to the creation of international rules through new procedures. the participants recognized the validity of the resolutions of the United Nations General Assembly as a new source of international law emerging from the adjustment of opposed forces. The procedure to arrive at special resolutions is a dynamic and flexible one, and therefore subject to improvement; a legal mechanism more in accordance with the needs of newly arrived members of the international community. In the legal field the new energy situation evidenced the need to replace a scheme of uneven economic relations by an order in which greater justice in distribution may prevail. In this context, the Charter of Economic Rights and Duties of States approved by the General Assembly, appears to be the best of all available instruments to control anarchy and regulate economic relations between States.

The problems of economic injustice have a long historical origin and, therefore, their solution will not only require assistance for development but also creation of new opportunities for poor countries through trade, opening of markets, access to less onerous loans, etc. In the case of oil, it will be necessary to adopt measures to eliminate waste and any negative environmental impact that the use of different energy sources may have.

4. *The general and social approach*

The topic upon which the debate about the political effects of the new energy situation centered was the argument put forth by Doctor Rajni Kothary,* who believes that this situation will possibly encourage a new development strategy for the less developed oil importing countries. In the short run, the energy crisis has been unfavorable to this group of countries due to the price increase of foodstuffs, the reduction in savings capacity and the disregard for necessary investments to keep up with production growth.

But in the long run, there is a possibility to profit by the temporary situation created by the oil price increase. First, OPEC set a guideline of behavior that could be followed by other raw materials producers, if one takes into account that the increase of energy consumption has slowed down the development of synthetic products, therefore having a psychological impact on industrialized countries to the benefit of developing nations. Second, the new situation has allowed the revaluation of domestic natural resources, expanding the viability of a new technical and economic labor-intensive model. Finally, the energy crisis has increased the possibility of adopting a self-sustained growth approach that may stimulate internal savings, exploitation of natural resources and the development of infrastructure. Briefly, Doctor Kothari proposed to adopt an integral development policy defined by the consequences of the new energy situation which he considers stimulating to developing countries.

Most participants did not share the optimistic view of the speaker. Professor Urquidi emphasized the exceptional character of the oil price increase, and its insufficiency in bringing about radical changes in human behavior. It should not be forgotten that the transition towards more advanced industrialization models implies an increased use of energy, nor that any development process, even a "selfsustained" one, requires close international cooperation in the field of foodstuffs, technological transfer and financial assistance.

Other participants pointed out that it is difficult to adopt an optimistic attitude in view of the current extent of indebtedness on the part of oil-importing developing nations. Such indebtedness is an evident demonstration of the economic and psychological

* In Doctor Kothari's absence, his paper was presented by Professor Urquidi.

impact of the energy crisis. Even though no other raw material source can receive the same treatment as oil, according to Doctor Smart, it is important that OPEC's negotiation procedures are maintained as reference standards in the establishment of other raw materials prices.

The analysis of the general impact of the new energy situation was completed with an evaluation of bilateral agreements that have been established between oil and industrialized countries for the purpose of recycling the financial surplus and accomplishing joint investment programs.

Professor Antoine Ayoub expressed that, as long as terms of trade are unfavorable to developing nations, it will be difficult to achieve capital accumulation, an indispensable requirement to stimulate economic development. Therefore, the agreements signed by oil countries on a bilateral level should be directed towards achievement of suitable means to improve the terms of trade. If importing countries continue using a strategy designed to disintegrate OPEC through bilateral agreements, it will be much more advantageous for oil countries to conclude multilateral arrangements.

The new energy situation brought about a large deficit in the balance of payments of non-oil developing countries, in addition to an increase in the level of external indebtedness. In the view of Doctor Gérard Curzon, the debt contracted by developing countries is no longer used for new investments but to sustain consumption, and the time will come when it will be impossible to sustain the level of oil consumption of developing countries because this would aggravate the problem of international liquidity. Still more, OPEC's aid to developing countries has been limited. It is likely that the latter have obtained greater benefit from the price increase in primary products between 1972 and 1975 than from the assistance of oil-producing countries.

Policy-makers in developing countries should keep past experiences in mind when formulating a strategy to negotiate with developed countries, whether on bilateral or multilateral bases. The meager achievements of GATT and the recent UNCTAD meeting in Nairobi proved, according to Doctor Curzon, that the list of demands of the developing nations is still too extensive and that the possibilities of reaching a better understanding will continue to be limited as long as more specific matters are not dealt with.

In view of the rise in import prices to the oil countries, two years after the increase in the price of crude oil, its real price is now at the same level it was twenty years ago. No matter how strange it may appear, never before were industrialized countries able to buy oil as cheaply as now; perhaps this explains the delay in the process of substitution of hydrocarbons. After the Geneva agreements, oil countries made their first attempt to adjust the oil prices to the real monetary devaluations; since then they have been blamed for world inflation. In spite of successive increases in the energy field, recession and what was left of the strong inflationary pressures —which were accelerated but not caused by those increases— are beginning to disappear in Western countries, while non-oil developing nations continue to be immersed in a process of growing indebtedness not only in regard to OPEC countries but to industrialized countries as well.

The participants in the Seminar ended their discussions with an analysis of the future of OPEC. According to Doctor Hasan Zakariya*, the Organization will face external and internal dangers which will threaten the continued cohesion and survival of OPEC. External threats arise from the enmity major importers have shown towards OPEC after its recent gains, expressed in the announcement of some "final solutions" they intend to apply in case of emergency; of the adoption of measures designed to modify market conditions in order to force prices down and cause strain within OPEC, and even of manoeuvres to dismember OPEC. As to internal threats, oil countries are facing the problem of determining the relative value of their various crude oils above or below the price of the marker crude, as well as the danger of projecting a public image of complete dominance by one member country or group of countries over the Organization. Doctor Zakariya emphasized the fact that current disagreements within OPEC are not as serious as it might seem, and that only marginal questions are actually discussed, such as how much and how soon oil will be produced. In the near future, OPEC will have to solve three basic problems: the indexation of the price of crude oil in relation to the prices of a number of manufactured goods exported by major oil importers; the regulation of production in order to bolster the price and share the losses of falling demand on an equitable basis and, finally, the admission of new members.

* In Doctor Zakariya's absence his paper was presented by Doctor Rinaldo Pecchioli.

In Doctor Zakariya's opinion, it is highly important that OPEC members be Third World countries if the Organization's cohesion and harmony are to be preserved.

Participants in the discussion of Doctor Zakariya's paper argued that OPEC's future position will have a more defensive than offensive character. As Doctor Barkai pointed out, it is impossible to maintain full production levels at a price five times higher than that of 1973, or to underestimate the industrialized countries' great capacity to adapt to the new situation and the widening gap that separates oil countries from the rest of Third World countries. The admission of new members could increase the risks of introducing heterogeneous interests in the monopolistic power of the Organization if its executive functions are not increased. Anyway, in Doctor Nobumitsu Kagami's opinion, there is a fundamental question that leaves the way open to further debate: in the light of the consequences and alternatives of the new energy situation, to what extent is it feasible that advanced industrialized oil-producing countries join OPEC?

Other participants stressed the importance of OPEC in the world context because it has forced rich countries to strive for a greater understanding of the Fourth and Fifth World problems, with all the consequences that affect them in international economic relations.

The impact of the oil situation upon the new international economic order was examined in a paper presented by Doctor Leslie Manigat. According to his judgement, OPEC has been an accelerating factor in the crisis of the international economic order, a crisis of reorganization that had already become evident before. In particular, this crisis has intensified North-South problems in which variables of a non-economic nature appear, such as the process of decolonization and its consequences and the dependence and underdevelopment situation of Third World countries. One can even speak of a "redress" mentality, that is, that the North should "pay" the South the debt accrued throughout the entire historic experience. A collective awareness is growing in the Third World and for the first time it has access to the power play, to the decision-making process, and to technology. The dominant position of industrialized countries will no longer exist thanks to OPEC and its performance. Nevertheless, as Professor Manigat stated, a distinction should be made between the real and the perceived impact, because there may be a great difference between

both, considering that the search for a new order will be a long and difficult process.

Several participants noted in this respect how intricate the international relations system has become and underlined the complexity of solutions, which cannot be radical but must be reformist. Almost all of OPEC members belong to the international capitalist system and most of them have not changed their internal régime. Their purported wish for cooperation, especially towards Fourth World countries, may not be real.

The nature of the new international economic order was also discussed, at a time when it begins to be examined and defined on the basis of discussions at the United Nations, particularly during the Organization's Seventh Special Assembly, as well as based on the Charter of Economic Rights and Duties of States. Professor Manigat stressed the importance of the moral dimension of the problem, which is one of the reasons for the Charter's approval by most countries. The basis for the new order cannot be merely economic, because the problem involves satisfaction of human needs and creating equality of opportunity for development. The idea of international justice should prevail.

The new energy situation has also been interpreted by some as an opportunity to hasten the industrialization process in several countries. In his paper, Dr. Joseph Hodara used a comparative approach to discuss the situation in Iran and Venezuela in order to establish the favorable and unfavorable aspects of a so-called "instant industrialization". The massive transfer of financial resources that followed the energy crisis offered oil-producing countries the short-term possibility of considerable advancement in the industrialization process. The feasibility of instant industrialization is limited, according to Doctor Hodara, because of restrictions of a temporary nature that are translated into sudden price changes and variations in the amount of oil income, and structural factors such as unemployment, social dissatisfaction and the excessive promotion of state technobureaucracy. This does not eliminate the possibility for countries like Iran and Venezuela to benefit from a series of favorable conditions to hasten the industrialization rate provided they attain a highly effective yield from the interdependence created by the present industrial system.

In general, there was agreement on the limitations of future industrialization which momentary oil wealth does not remove. Besides, industrialization based partially upon the export market

presupposes that OPEC countries will have secured foreign markets, when in fact they have not been studied and it is likely that a struggle for them takes place due to the lack of coordination of industrial plans among oil countries, particularly those of the Persian Gulf.

It was also mentioned that in most countries engaged in a process of "instant industrialization" technology with a high degree of capital intensity is used with little regard to employment problems, especially in those countries where the population growth rates are very high and a future labor surplus can be foreseen. There was general agreement on the lack of selectivity of development plans, but for the moment there is no alternative to the scheme of "instant industrialization".

Finally, based upon the paper by Doctor Ian Smart, a discussion took place on the degree to which the evolution and possible settlement of the political conflicts of the Middle East might have been determined by the oil crisis. In his opinion, there are good reasons to question the influence that is commonly ascribed to the "oil factor" upon the superpower policies in the Middle East. In fact, oil played a minor role in the start or end of the Arab-Israeli conflict. Even though the United States as well as the Soviet Union derived important benefits from the oil "embargo" and OPEC's price increase, it is possible that in the long run the situation may turn out to be less favorable for both countries, due to the inclination of the area's balance of power in favor of the "oil states" and the increasing polarization of attitudes in Israel. The increasing vulnerability of Israel, as long as the United States depends upon Middle East oil, was especially noted.

Nevertheless, Doctor Barkai pointed out that the oil price increase took place before the October 1973 war and that there was never a shortage in oil supply. Oil scarcities were more apparent than real. Therefore, the threat of the oil embargo cannot be considered as an important factor in the solution of the political crisis. Other participants also argued that additional conflicts have appeared among Arab countries themselves due to the oil crisis, aggravating the North-South as well as the East-West problems.

Doctor Smart stated that the oil crisis came together with other problems in the demand and production areas that had been exerting some influence before the Middle East war, among others the coal strike in Great Britain, the gasoline production shortage

in the United States, etc. Nevertheless, the speed at which prices increased was undoubtedly a short-run disturbing factor; there is no price crisis in the long run.

5. *Conclusions*

The Seminar was considered as a good opportunity to study the implications of the oil crisis from several angles. The international economy was already in crisis insofar as indebtedness of the Third World, North-South trade and financial relations and in the monetary field were concerned. Changes in the structure and the economic policy of industrialized countries are greatly needed. The sudden increase in the price of oil, although it reestablished the oil purchasing power lost in the two preceding decades, caused a disturbance of major proportions in reorienting the flow of monetary resources to a small group of countries, having their own interests to look after besides representing the Third World, some of them of a political nature as in the case of the Middle Eastern nations where the interests of the superpowers are also at stake.

The consequences for the oil-importing developing nations have not only been economic but also political as they have worsened their dependency. There does not yet exist a mechanism to recycle financial resources that may fully meet the needs of these countries, even if oil countries have reallocated resources towards some of them. On the other hand, most of the recycling has taken place in the direction of industrialized countries.

Briefly, new and severe international imbalances have been created that affect primarily the countries which import energy and foodstuffs. No way is foreseen as of now to solve these problems in the short run. However, the long run impression left by the Seminar is that oil price increases will be absorbed by the world economy and that long run investment flows will be reestablished. Many countries will restate their development strategy in order to be less dependent on oil. Others will industrialize more quickly and will enter international markets in order to substitute a variety of manufactured goods for their energy exports.

Nevertheless, all these changes will not come about as a consequence of the free play of supply and demand but will require adoption of several measures. Hence the importance of implementing a new international economic order, currently

in the process of definition. One of the new elements is the organization of raw materials, producing countries and their negotiations with industrialized countries to supply their products in exchange for concrete benefits in the areas of trade and investment.

Part I

Technical, Economic and Financial Aspects

Hydrocarbons in Transition

Juan Eibenschutz

I. *Present situation*

Within the framework of the economic disparity between countries hydrocarbons can be conceived to have, among others, the following two characteristics:

—everybody depends on them.
—those who have them enjoy a certain superiority.

The dependence is different in the different countries, but hydrocarbons have become sufficiently important to make them indispensable for the national economies, whatever the level of development of the latter.

World economic progress, with its advantages and disadvantages, has relied to a large extent on oil and gas. Its weight in international politics has been enormous, and it continues to be extremely important in spite of the efforts towards independence of the producing countries.

The present decade has witnessed changes, mainly in the level of awareness in relation to oil products and their application. A historical analysis of the utilization patterns would show that, in general, sufficiency or the unlimited existence of hydrocarbons were implicitly considered. Had there been a clear understanding of the finite of a resource that took millions of years for nature to accumulate, it is likely that neither private automobiles would exist nor gas or oil would be used to generate electricity, and even that the level of air pollution would be much lower.

These considerations, that in the past would have allowed a better planning, are relatively recent in every country, whether it produces oil or not. Hydrocarbons have not yet reached their production peak and already their decline is foreseen.

The new tendency is due undoubtedly to the recent price change, but curiously, the increase in international prices was not

a consequence of production problems reflecting the beginning of declination; it was rather a political matter.

With the new prices and the physical impossibility of doing without hydrocarbons, the international financial situation changed and, at the same time, a great impulse was given to research in the field of development of new energy sources.

Developed nations have assigned important budget appropriations to programs intended to use coal as a substitute for oil products, as well as to develop geothermal energy, solar energy, nuclear fusion, breeder reactors, etc. Those developing countries which are rich in oil have initiated the search for ways to make a profitable use of their hydrocarbons, or to say it better, of their export earnings in order to still have energy when hydrocarbon reserves are depleted.

The "energy crisis" has also promoted the proliferation of energy planning techniques. Governments, universities, international organizations, large enterprises, etc., are actively developing methods to plan the evolution of the energy supply. Mathematical programming techniques, economic theories, technological forecasting and many other disciplines are being oriented towards energy problems.

Even concern about the pollution effects of some energy sources is losing weight because of the new prices and the awareness about supply difficulties.

In many countries a decrease in consumption is observed or at least in its growth rate. Some countries are launching massive nuclear programs to substitute hydrocarbons, even if only as a partial substitution.

As a consequence of the new oil prices, a considerable increase in prices in general is also noted, especially for equipment used in the energy field. The price of coal and uranium has also increased, almost in the proportion that the oil price was raised. The superiority of the developed nations is thus being felt.

However, those countries that are rich in oil enjoy a favorable situation. They are creditworthy, they receive technology offers, they have access to participation in multinational industrial projects and they acquire a new strength in international fora.

From a technical point of view, the hydrocarbons transition is in progress.

II. *Alternative resources*

According to experts, hydrocarbons are not the most abundant energy resource. They do represent, however, the most convenient form of energy. With internal combustion engines and gas turbines, they allow rapid transportation. Their transport in pipelines or large tankers is very cheap. Liquids produced from petroleum are easy to distribute for their wide range of applications. Natural gas permits very efficient systems of urban distribution, although relatively expensive.

Coal, the most abundant energy resource, has been displaced. The fact that coal reserves are extremely large has not determined its consumption.

According to V.E. McKelvey, who refers to the World Energy Conference (1974), the measured reserves of coal amount to 14 x 10^{18} BTU; those of crude oil to 3.7 x 10^{18} BTU and those of natural gas to 1.8 x 10^{18} BTU. In spite of the fact that hydrocarbons meet more than two thirds of world energy demand, the measured reserves of oil and gas are approximately 40% of the coal reserves. In regard to the "geological potential" estimated for hydrocarbons and coal, the situation is even more impressive, since according to estimates the ratio between the thermal energy stored in hydrocarbons and that stored in coal varies from 1 to 6 to 1 to 9.

This disparity between the size of reserves and the volume of production has a logical explanation in the relative difficulties that the exploitation of each resource offers. Coal mining is, in spite of mechanization, one of the hardest, most unpleasant and dangerous activities for the human being. Even though the exploitation of oil and gas requires hard work, it is a good deal more acceptable.

Now, one of the fields where the research and development effort has increased most is the *in situ* use of coal; the objective is to use the energy contained in coal without having to mine it. The prospects are reasonably good, and according to some publications, it will eventually be possible to produce gas and synthetic crudes from coal processed underground.

One of the most serious problems in the replacement of hydrocarbons as energy sources is related to the structure of utilization systems. If two thirds of the energy comes from hydrocarbons, the equipment to use them will not accept very different energy

sources. Partly, this is the reason for producing synthetic hydrocarbons from coal.

A more important participation of electrical energy can be foreseen in the meeting of energy demand. Electricity can be generated in different ways and the utilization equipment is not affected by the primary energy source used. Besides hydrocarbons, energy resources include in the short run: coal, uranium, hydroelectric potential and, marginally, geothermal energy and solar energy.

It is expected that the energy scene will change when practically inexhaustible energy sources such as nuclear fusion or the use of solar energy for hydrogen production become available.

III. *Strategic considerations*

It is generally assumed that the world production of hydrocarbons will reach its peak towards the end of the present century. This assumption will not necessarily be valid for all producing countries, but it allows some considerations on the strategies needed to avoid an economic collapse caused by an unforeseen lack of hydrocarbons.

Evidently, the decrease in output levels will be relatively slow and it is very likely that output levels during the early decades of next century will be similar to the present ones. It is also very likely that the overall energy demand by that time will be considerably higher than the present demand.

The relative economic position of the countries, whether producers or not, will have a great influence upon the distribution of the available hydrocarbons, since the richer will either be able to pay more or will have more power to acquire them.

It is important to bear in mind the variance in the unit indices of energy consumption. Countries with high consumption indices are more sensitive to the lack of energy than those countries that consume less. This gives a relative advantage to poor countries, which could conceivably choose a pattern of development requiring less energy, in order to avoid the severe repercussions derived from scarcity.

Per capita energy consumption is closely related to the degree of material wellbeing. However, material progress in now being questioned. Nobody doubts that the human being must enjoy a minimum of goods and services and it is well known that roughly

one half of the world population lacks that minimum. At the same time, those who have abundant supply of goods and services will not be willing to do without them.

Great technological developments take place in the rich countries, at least according to recent experience. Developing nations need to increase their energy consumption and they have the opportunity of doing it rationally, since the patterns of development followed by the more developed countries serve them as models.

When examining the future situation, a decrease in the availability of hydrocarbons appears always, sooner or later. As a consequence, the need to diversify primary energy inputs becomes evident. However, there does not seem to be enough understanding of the importance of the structure of the consumption sector.

With the exception of electricity, production of which can be obtained from different primary energy sources, and of some heating applications, hydrocarbons can only be substituted if the utilization systems are fundamentally changed.

According to United Nations energy statistics (1970-1973), the share of hydrocarbons in energy consumption rose from 37% in 1950 to 66% in 1973 for the world as a whole. The average for developed countries shows a 41% share of hydrocarbons in 1950 and 74% in 1973, while for the countries classified as developing, the participation of hydrocarbons in 1950 was 59% and surged to 79% in 1973.

The change in the relative participation of primary energy sources in favor of a wider use of hydrocarbons cannot continue indefinitely, but due to their noticeable importance it is imperative to point out that the transition from hydrocarbons will demand a substantial effort to change the consumption patterns and thus make the substitution possible.

Electricity is a real alternative to hydrocarbons, within the present technological frame. The difference between developed and underdeveloped countries gives the opportunity to make some interesting considerations. Independently of the primary energy source, the proportion of electrical energy with reference to the total energy consumed is an index of the structural dependence of the consuming sector.

According to United Nations statistics, on a world level electricity accounted for 37% of the total energy consumed in 1973; the average for developed countries being 41% and for developing countries 25%.

This means, in general terms, that the developed countries' consumption structures are better equipped to accept substitutions *via* electricity than those of the developing countries and, as a consequence, that one measure to be taken into consideration is the promotion of electricity use to induce structural modifications in the consumption patterns, which will in turn make the transition easier.

For the producing countries that are rich in hydrocarbons a paradox appears: the natural trend is to satisfy their own needs with hydrocarbons and, depending on the amount of reserves as well as on other political and economic considerations, to export more, or less; the structure of dependence on hydrocarbons is thus maintained and, as their availability decreases a crisis will arise, varying in magnitude proportionally to the dependence on them.

The transition from hydrocarbons is a rather complicated problem. Some measures are almost obvious; others depend very much on the specific characteristics of each country. Among the first ones, the following can be pointed out:

- increases in the efficiency of utilization
- adequate rates and prices
- avoidance of useless consumption

In other words, the universal measures are rationalization and saving measures that may be applied in all types of countries.

At first sight, the saving measures seem to make more sense for countries that have high per capita consumption rates, than in less energy consuming countries. However, the effects of rationalization measures could have a greater relative importance in countries with low energy *per capita* consumptions, since on the whole, the energy economized will allow a wider access to the resources. It should be mentioned in this context that some of the saving measures imply additional capital expenditures that make them inaccessible to poor countries.

Logically, one of the most important parameters in the selection of specific measures for each country when hydrocarbons are available is the amount of reserves, since their relationship to the rate of output makes the evaluation of alternative energy policies feasible. The sequence in this case is to try to know how much oil

and gas there is; how much can be extracted and at what rate should production take place.

Information on reserves and characteristics of deposits is expensive and difficult to obtain, but it has an enormous value. It is here where the existence of national efficient organizations becomes very important for national interests. This is one of the motivations of the world trend towards nationalization of oil companies or, at least, towards a real and informed control on the part of governments.

Concerning technological developments, two main aspects are relevant: the possible increases in the recovery of hydrocarbons through non-conventional methods and the possibilities of transforming hydrocarbons into proteins.

If it were possible to extract from the subsoil all the hydrocarbons, the petroleum and gas era would prolong itself well into the next century, since availability of both resources would be roughly multiplied by three.

As in other mining operations, it is unlikely that it will be possible to extract 100%; however, substantial increases in recovery that would extend significantly the existence of hydrocarbons can be forecast.

Concerning the transformation of oil into food, it can be said that the development of the appropriate techniques would open a completely new field for the use of hydrocarbons which would imply qualitative changes of great importance in their value for humanity, and as a consequence, a practically complete displacement of hydrocarbons as energy sources in favour of their use as energy inputs for the production process.

In this sense, the advances in petrochemistry suggest also the possibility of using hydrocarbons more as a raw material than as an energy source.

Aside from what has been said up to now, there are a series of considerations about the future of oil and gas that lead to the same general conclusion: hydrocarbons are in transition, because they will be insufficient to meet the overall energy requirements of mankind. Their relative share as energy sources will have necessarily to decrease, and their value as raw material for industrial processes will be considerably higher than their value as energy sources.

The challenge is in finding the best way to carry out the transi-

)n, in such a manner that the national economies may benefit to e maximum extent possible.

The case of the underdeveloped producing countries

The situation of hydrocarbons in these countries is not very fferent from that of raw materials in general. The general trend ould be towards achieving their widest possible use for the :nefit of the national economy, independently of whether they are :ported or not.

The volume of available resources compared with domestic :mand tends to determine export policies, but the benefits for e exporter will be proportional to the degree of processing of :ported products. Certain temporary world situations during hich the price of crude has been higher than that of its products, ust of course be allowed for.

The advantages of processing tend to increase in the course wards scarcity. It is not impossible that the processing technologies exported products become efficient weapons for developed ations in order to obtain hydrocarbons from the producing)untries. This phenomenon, which occurs already, will be enhanced ıring the culmination of the transition.

For this reason, it is important to carry out serious efforts to- ards the local or at least regional generation and development technologies.

The availability of financial resources, organization systems and :illed human resources imposes some limitations on those coun- ies that wish to achieve independent energy developments. he OPEC countries have overcome financial limitations. With ıe new prices not only did restrictions of this kind disappear but roblems arose due to an excess of liquidity.

In spite of the enormous financial resources that are available ı several producing countries, the organization systems and the uman resources are not enough to achieve certain national goals. he task of training personnel to manage complex enterprises and) control advanced techniques is difficult and time-consuming. qually hard is the creation of efficient institutions, capable of xpanding and developing as technical complexity and the volume f operations increase.

Fortunately, in most cases there is already a clear understand- ıg of the need to apply long-range criteria to the development

of the national energy industries. The transition period of hyd carbons will be long, and if it is well managed, it will allow developing producing countries to benefit from it in order develop and be ready for the next energy era.

Balance of Payments Prospects of OPEC Countries*

Wolfgang König

Balances of payments are interrelated worldwide and bound to reflect important developments regarding the level and structure of economic activity as well as extra-economic forces. Thus, any outlook for OPEC's balance of payments developments may be an exercise in speculation to a high degree. In effect, economists have rarely been able to predict the future course of complex developments over a wider time horizon. This may also be seen to apply to subject matter of this paper. The first part therefore deals with the importance and scope of the topic as well as outlines the approach for analysis followed in the paper. Each of the following three parts takes up a specified period of time in the future, i.e. 1976-1978, 1978-1985 and beyond 1985.

I

The importance of the topic arises on three major accounts. First, up to now OPEC has been the most successful international cartel in economic history so that it may serve other developing nations as an example for actions to be taken as suppliers of raw materials. Its impact and success is demonstrated *via* balance of payments performance as will be its future strength. Furthermore, any such demonstration effect of OPEC would also increasingly include the kind of use made of its newly acquired wealth as it influences the development and structure of the corresponding economies. Second, the balance of payments outlook for OPEC is, to a large extent, a prediction about the future behaviour of this cartel as far as pricing and volume policies involving the exportation of oil are concerned. Third, analysis of the topic would establish certain implications for international financial requirements involving world-wide capital markets and for the possible redirection of investment and production of a number of oil-importing nations.

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Analytical questions to be raised are, however, extremely complex and, in general, would refer to expected short, medium and long term shifts in supply and demand conditions not only of hydrocarbons but also of present and potential sources of energy. This involves, for example, the economic growth performance of major oil-importing countries in general and in particular their elasticity of energy consumption to GNP and price elasticity of demand for oil as well as possible developments in the indigenous energy base.[1] Other questions relate to the international monetary system as a mechanism for the transfer of wealth, in particular whether it will be able to sustain the huge amounts involved, whether new financial mechanisms may be necessary and whether the oil consuming countries will be able and willing to absorb the immense investments that producer countries may wish to make in the future. How will countries make internal adjustments to the external energy shock without severe dislocation and would further oil price increases accelerate the inflationary spiral and thereby have a depressing effect in terms of growth performance?

These and other questions relating to economics have to be supplemented by a series of issues relating to other fields, in particular the structure and stability of international political relations which are also bound to have an impact on future balances of payments. Would the energy crisis serve as a catalyst for a fundamental confrontation between industrialized and Third World countries because part of the latter may not be able to cope with the problems caused by the oil crisis or because other nations set up OPEC-like producer organizations for raw materials? Which political changes are likely to take place in the Middle East over the next ten years or so?

Such complexities determine that any detailed projection of items of OPEC's balance of payments is a futile attempt. Even for the recent past, there is only limited information; basic continuities appear somewhat obscured given a number of uncertain variables. To come to grips with a future outlook would therefore mean to draw a very general picture of OPEC's external accounts and, in doing so, to proceed on a rather narrow economic ground, abstracting from a series of possible influences of subtle economic and non-economic nature.

[1] To demonstrate one issue involved, estimates of the total U. S. oil resources differ to such an extent that the country would exhaust this energy source anywhere between the years 1998 and 2075. *Science*, Vol. 187, 21 March 1975, p. 1064.

For the purpose of this paper, the following five questions would lead to such an approach: (i) who can provide oil; (ii) for what purpose; (iii) how much; (iv) at what price; and (v) under which conditions. The first relates to OPEC's relative share in worldwide oil markets and to the issue of membership. The second refers to the motivation, interest and viability of this cartel in terms of balance of payments needs and management of its members. The third raises issues relating to oil production programming and again to the relative share of OPEC in the international oil markets. The fourth, together with any conclusive answers on the foregoing (iii), will relate to the expected foreign exchange proceeds of these countries. Finally, the fifth question is meant to refer to a number of variables partly difficult to predict, some of which were mentioned above and would comprise aspects ranging from the balance of payments adjustment process and international financial intermediation to the worldwide environment as it is affected by the so-called energy crisis and feeds back on the balance of payments performance of OPEC nations.

These five questions will be raised for each of the following three future periods which appear to be important stages of OPEC's balance of payments development: the short-run, comprising two years from mid-1976 to mid-1978 which may be coined "predictable"; the medium-run, from mid-1978 to 1985 which may be termed a "transition period"; and the long-run, beyond 1985 as an "unpredictable" time span.

II

The short-run is quite predictable because for this period relatively safe answers may be found to the above five questions in the light of the experience gained since the end of 1973.

As far as question (i) —who can provide oil— is concerned, OPEC's power is likely to be felt quite as unchallenged as it has been in recent years because there are no substitutes available at short notice and this cartel may be assumed to play a leading role in shaping international energy relations.

For which purpose, question (ii), or in a narrow sense, how would OPEC like to see its external accounts, motivation may be considered to be also essentially the same as it was recently concerning the deployment of investible surpluses and the need for additional imports. However, there are differing interests

among individual OPEC nations as far as the relative importance of these two goals is concerned. To be sure, to all of these countries, oil is the principal source of foreign exchange and a key to further development, but they differ significantly as to the urgency with which these revenues have to be acquired. The possibility that this may cause seriously conflicting views leads to a classification of OPEC nations on the basis of the following basic criteria:[2] volume of oil reserves in relation to levels of production; size of investible surplus; and stage of development with particular reference to absorptive capacity and size of population. Although there are some borderline cases, one may essentially distinguish between three groups of countries. Group I, comprising Saudi Arabia, Lybia, Kuwait, Abu Dhabi, Dubai and Qatar, and representing a total population of not more than 10 million, is bound to register sizeable surpluses because the stage of their development and the structure of their economies do not permit imports to rise rapidly. At the same time, this group has considerable reserves in comparison with the rest of OPEC. Group II countries, made up of Venezuela, Iran, Algeria, Iraq and Ecuador, have substantial import needs in view of the economic progress already achieved and can be expected not only to use up their oil reserves relatively rapidly but also to spend their increased oil revenue largely on imports rather than on investments abroad. The rest of OPEC, Group III countries, Indonesia and Nigeria, with a relatively modest share of oil resources appear to have excess absorptive capacity so that they cannot be expected to accumulate any financial surpluses even in the short run.

Most Group II and all Group III countries are bound to be pushing for higher oil revenues in view of stepped-up domestic development plans, vast needs for socio-economic reforms and military expenditures. For them, the goal of establishing diversified and self-sustaining economic activities ranks very high whereas for Group I countries the issue is rather the maintenance of financial wealth since it will possibly take them far beyond 1985 to absorb their oil revenue in the form of imports. Thus to the latter a decision to reap higher oil revenue is equivalent to a decision to invest abroad in the short and medium run and they apparently recognize, by considering the need to maintain the real value of

[2] For this classification see also Hollis B. Chenery, "Restructuring the World Economy", *Foreign Affairs*, January 1975, p. 250.

their investments abroad and of the income to be derived therefrom, that there are limits to the deployment of expanded investible surpluses.

In the light of this situation, it will matter which of the OPEC nations are in a leadership position since the conflicting goals referred to may be projected towards policies on the volume and price of oil. There can be no doubt that countries with huge oil reserves, i.e. Group I nations and Iran, are by implication in a controlling position and are bound to take a long-term view as far as oil revenues are concerned because of the fact that their reserves would last up to 50 or more years and that most of them do not have other natural resources, whereas the rest of OPEC may want to exploit a short-term bonanza time.

The question (iii), how much, entails supply and demand aspects and as for the former, it has been apparent that at least some of the countries in Groups II and III would want to push for higher incomes *via* a volume reduction. Such a policy, however, would necessarily be at the cost of the resource-abundant members of Group I, plus Iran which, as we saw, are in a controlling position. The latter can therefore not be expected to provide the umbrella for effective production controls. Furthermore, such controls were imposed only by Arab countries in the past and it may be concluded that they are not likely in the predictable short-run.

As for demand, oil imports have somewhat fallen off recently due to the world-wide recession and to some extent price-elasticity of demand, as well as conservation efforts. Although economic activity is clearly recovering in 1976, it may be predicted that consumption levels will not be much above the 1973 mark at the end of the short-run. In conclusion, rather than introducing production controls in a push for higher incomes, OPEC countries may find themselves producing below capacity and therefore face the decision of how to share reductions among each other.

Many of the foregoing considerations have implications for question (iv) concerning price, inasmuch as Group II and III countries, pushing for higher incomes *via* volume reduction are by implication looking for further oil price increases in the immediate future in the intent of exploiting to the fullest a period of rather inelastic demand. This is, however, not in the interest of the controlling members of OPEC because the higher the price of oil, the stronger may be the pressure on the resource-abundant members

to hold back production. In other words, any push for more oil revenues *via* price increases is likely to be kept in check by the controlling members. In view of this and the fact[3] that there is even at present a certain price competition among OPEC members, it may be predicted that oil prices are not bound to go up much higher in the short run; rather there is some likelihood that the price trend for this energy resource will be declining in terms of general commodity prices.

Regarding the fifth and last question which concerns the general circumstances surrounding international oil relations, a number of problems were forecast some time ago and are still seen to affect in the ultimate instance investment, saving and financial intermediation, the determinants of capital formation. The change in corresponding conditions, brought about by the energy crisis, has indeed required a reshaping of such processes, the single major problem being to put petro-dollars to productive use and to minimize the loss of welfare. To be sure, there has been some polarization of economic performance among and within major groups of oil-importing countries due to oil price increases. However, problems have not been as dramatic as was anticipated some time ago and appear to be of manageable proportions at least for industrialized countries and the more advanced developing nations. First of all, there has not been a huge international transfer problem because internal and external adjustment processes have taken place rather quickly, demonstrating the flexibility of market economies, and the financing of balance of payments imbalances was greatly facilitated through official and private international institutions as well as to some extent, conservative investment policies followed by OPEC nations. Second, there has not been, as it appears now, a major and persisting growth problem although the shift in foreign exchange reserves would equal a significant portion of the national income of OECD and non-OPEC Third World nations.[4] In retrospect, it was the suddenness of the energy crisis rather than its magnitude which warranted more concern. This would imply for the next two years that no dramatic changes stemming from international energy relations may be expected in the

[3] See also Hasan S. Zakariya, *The Future of O.P.E.C.*, infra.

[4] The increase of OPEC's oil revenue of US$80 billion in 1974 due to oil price increases was equivalent to 2% and 3% of national income in OECD and non-OECD Third World countries, respectively. Hollis B. Chenery, *loc. cit.*, p. 246.

conditions under which international trade in general and the oil trade in particular are going to take place. In the context, it may also be taken into account that during this time span, important discussions on a new world economic order are likely to be initiated, conditioning perhaps a restrained behavior of the important actors in world-wide economic and financial relations, including OPEC.

In the light of the recent experience and with the above answers to the five investigative questions in mind, a general picture may now be drawn for OPEC's balance of payments in the predictable short run. Group I countries will clearly have significant current account surpluses and thus substantial investible funds.[5] Some of Group II and the two Group III nations will register current account deficits during this period and thus be in need of financing.

The investible surplus of OPEC as a whole amounted to US$57 billion in 1974 and US$33 billion in 1975,[6] the decline being accounted for by a rather strong expansion of OPEC imports from OECD countries, including military goods, and a decline in oil shipments which more than offset a moderate rise in oil prices. This investible surplus which can be considered a measure of trade imbalances due to the energy crisis may be predicted to come up to a cumulative total of US$60 to 70 billion over the next two years, taking into account a picked up demand for oil imports, particularly by OECD nations, and, as a slightly more than offsetting development, a further stepped-up import demand on the part of OPEC nations. Thus, by mid-1978, the latter are bound to have accumulated since 1974 some US$160 billion which represents a figure far below that which was anticipated some time ago and only a few percentage points in terms of the expected value of OECD stocks and bonds.

III

The medium-term from mid-1978 to 1985 is considered a transition period because many elements relating to the five ques-

[5] The investible surplus is understood to refer to the amount available for new financial investments abroad, i.e. the current account surplus on a cash basis after capital transfers.

[6] For these data see Rinaldo Pecchioli, *OPEC Financial Surpluses and the International Capital Markets, infra.* This paper draws on research carried out within the Financial and Fiscal Affairs Directorate of the OECD.

tions may be assumed to be under considerable change. Answers to these questions will thus be more difficult to give but not impossible.

As regards question (i), who can provide oil, new aspects will arise on the following accounts. First, some OPEC nations such as Venezuela and Algeria may want to take increasingly into consideration certain constraints that may be seen as far as their reserve/production ratios are concerned. Secondly, and more important, present oil prices and those of the short run are and will be tying a significant amount of capital to the exploration and production of oil elsewhere with the result that in the medium-run new reserves, particularly in Alaska and in the North Sea, will make an impact on the international oil market. Any increase beyond installed capacity would take Persian Gulf countries about a year between the decision to raise output and actual production, whereas for these newly discovered oil fields such time span would range from three to five years after which little continued effort would be needed to sustain the flows.

Although data presented on such prospective developments may in part be considered a weapon of psychological warfare in international oil relations, it is not unlikely that the aforementioned new sources will cover some 60 percent of the additional demand for oil by the industrialized countries by the year 1980. In fact, Western Europe's dependence on petroleum imports was predicted to be reduced from about 85 percent of petroleum consumption in 1972 to about 60 percent in 1985.[7] In addition, oil will also be increasingly supplied by non-OPEC developing countries. There are at present already 13 such nations that may double their oil export volumes between 1974 and 1980.[8]

In view of this, the international oil markets are bound to undergo substantial changes in the transition period, with OPEC

[7] Efrain Friedmann, *Energy Supply/Demand Outlook 1980-1985*, paper presented at ECLA's Symposium on Latin America and the Energy Crisis, 2-6 September 1974, p. 10. Data presented in this paper are partly based on research carried out by the World Bank.

[8] Adrian Lambertini, *Energy and Petroleum in Non-OPEC Developing Countries 1974-1980*, World Bank Staff Working Paper No. 229, Washington, D. C., February 1976. According to this paper, non-OPEC developing countries would be able to reduce their dependence on energy imports from other groups of countries from about 30% in 1974 to between 12% and 6% in 1980 by annual investments equivalent of 1.3% of GDP in energy production over the next 5 years.

nations facing increased competition. On this account only, the rate of growth in demand for their oil will fall off.

A decline in the monopoly power of OPEC will have an impact on the performance of this cartel, particularly its authority and purpose. The possibility that this decline would be arrested to some extent by an increase in its membership is again a matter mainly to be decided by the controlling members. Such a move is not easily accomplished because any nation qualifying as a new member would share the characteristics of Group II and III countries and thus challenge the policies pursued by the leadership Group I. In short, in the transition period the effectiveness of OPEC co-operation may be at stake as it is a function of the conditions and objectives of individual member governments.

This relates to question (ii), on purpose. Indeed a sharpened conflict may be seen to arise as the development programs of Group II and III countries project a substantial increase in import demand and a decline of their investible funds, whereas Group I is unlikely to change the position taken towards balance of payments management during the short run. Thus, the urgency for acquiring oil revenues would differ among OPEC nations more than before at a time when the conditions for a cartel success deteriorate, i.e. price-inelastic demand for OPEC oil, high barriers to market entry, high market concentration, shared experience and values among producers, lack of consumer resistance, etc.

As for question (iii) on the volume of OPEC sales, the above predicted decline of the cartel's market share can be further substantiated by pointing out likely changes in indigenous supplies of non-OPEC energy. OPEC now supplies about one-third of total world energy and any such changes are bound to have a significant effect in this respect. As far as nuclear power alone is concerned, projections are that between 1974 and 1985 this source would represent about 30 percent of the total energy supply additions.[9] Thus, at the end of the transition period OPEC nations may actually face an absolute decline in their export volumes so that they may need to agree on the distribution of below-capacity production among them. This may, in effect, pose the most serious threat to the survival of this cartel during the transition period.

Implications for question (iv) are that there will be a tendency for the price of oil to decline during that time span. The extent of

[9] Efrain Friedmann, *op. cit.*, p. 8.

such a price change may most of all be determined by the level of long-term costs of non-OPEC sources of energy involving policy measures on the part of oil-importing nations, possibly even guaranteed prices for private companies producing oil in the industrialized countries as well as surcharges on oil imports. In other words, oil prices may be held up by the very action of those nations that nowadays depend to a high degree upon OPEC oil. Initiative in this field would thus partly be taken away from OPEC Group I countries, the dominant members in terms of reserves. If these OPEC nations would not cut back production and prices were to come down rapidly, OPEC would most likely face dissolution.

Any answer to question (v) on general conditions would be rather tentative because the international environment in the transition period is difficult to predict. Particularly at stake may be issues relating to confrontation or co-operation in terms of a new world economic order or at least a search for a new international equilibrium. Means may be found by which international economic inequalities are reduced and a number of non-OPEC Third World countries which are most hit by international energy relations are able to repay their staggering petro-debts.

Assuming no major upheavals in world economic relations, the balance of payments position of Group I of OPEC during the transition period may be predicted as being roughly one of still substantial oil surpluses and therefore investible funds. The latter, however, are bound to be declining thus leading to a reduction in the growth rate of corresponding foreign investment positions. Group II countries will increasingly register current account deficits and thereby be forced into international disinvestment. Quite a few of them will thus join those countries originally placed in Group III. By implication, the recycling of petro-dollars will increasingly involve OPEC members as recipient nations.

The investible surplus of OPEC may average as low as US$10 to 15 billion per year in the transition period not counting, however, substantial income flows from previous investments abroad. Taking into consideration the likely current account development of OPEC as a whole, indebtedness of other countries to this cartel may reach its peak around the early 1980s, the debt service equaling by this time perhaps some 1-1½ percent of GDP of the corresponding non-OPEC nations. Towards the end of the transition period, the level of this indebtedness can be expected to decline rapidly.

IV

The long-run beyond 1985 is rather unpredictable because the questions may either be very hard to answer or may even become obsolete in view of the strong likelihood that energy supply and demand will undergo radical changes.[10]

Oil as a source of energy will still be important, but, independently of any oil politics, there will be increasing awareness that alternative energy sources have to be developed because the oil on this planet will eventually be expended. The long run will therefore be characterized by a substantial dependence on nuclear energy, possibly to be followed by a growing contribution of geothermal and solar energy.

As far as the speed with which such changes are going to take place is concerned, energy prices are crucial, particularly the long-term costs of major alternative energy sources in relation to oil. The reason is that the considerable amounts of investment required would be uneconomical if low prices of oil were to prevail during the initial phase of the long-run, let us say up to the year 2000.

With reference to the questions, it may briefly be noted that (a) relative market shares in the international oil markets will not be any more an important issue; (b) the purpose of OPEC nations, if this cartel should still exist, may increasingly relate to pressing development needs; and (c) volume and prices of OPEC oil exports will be two closely related elements since the exploration of alternative sources of energy will determine an increase in the price-elasticity of demand. The latter point is likely to be important for Group I countries whereas most of the rest of OPEC may soon confront constraining reserve/production ratios in the neighbourhood of 10:1. Finally, the conditions for worldwide economic relations in general and international energy relations in particular, as they would reflect on balances of payments, are very much an open question and any prediction about them may be considered a futile attempt at this stage.

Any appreciation of likely balance of payments developments of OPEC nations in the long run beyond 1985 may have to take

[10] In the context, the year 1985 is considered a landmark also by the US Federal Energy Administration. See its *Project Independence Report*, US Government Printing Office, Washington, D. C., November 1974.

into account that the absorptive capacity of Group I countries will increase considerably, leading to a rapidly declining investible surplus as well as to international disinvestment and thus a reduction in the indebtedness of non-OPEC countries to this cartel.

For the rest of OPEC, a major question is whether by then international capital will significantly flow in the opposite direction compared with present times in order to support the continued growth of these countries. Crucial will be the pattern of development achieved by them because it will determine whether or not their external accounts will be balanced.

This relates to the nature of development policies followed by and the structural change to take place in the majority of OPEC nations in the years ahead as an indirect balance of payments effect of short-and medium-term oil revenues. In general terms, the issue for these countries is to find a proper balance between import substitution and export oriented industrialization, two options that are not mutually exclusive but may rather be considered interlinked successive phases of a successful development process. While specific guidelines would not apply to all OPEC nations alike because they differ to a high degree with regard to size, resource endowment, etc., the following issues are important to all of them: (a) injection of skills into their domestic economies in order to increase labor productivity; (b) avoidance of an excessive degree of self-sufficiency and of wasteful expenditures; (c) development of adequate infrastructure facilities; (d) transfer of suitable capital equipment and technologies; and (e) determination of the proper speed of modernization, avoiding excessive expectations and too fast a push of investment activities.

Concluding remarks may be initiated by recalling two major assumptions that are implicit in the above considerations on the three future periods. First, oil prices are bound to come down within limits over the course of the years, at least in relative terms following a deflationary trend already set in motion at present; or alternatively, such prices may be held up artificially by action of the governments of major oil-importing nations. Second, present-day oil prices and those to be expected in the short run are at such a level as to significantly stimulate the further exploration of non-OPEC oil resources and the development of alternative sources of energy, an irreversible process that is already under way although its speed has as yet not been established.

These assumptions determine that OPEC's balance of payments

performance in terms of oil revenues may be, in the long run, less favorable to these nations than one that would develop if oil prices were lower during these years. In other words, there is the possibility that OPEC has already over-shot the optimal price which would be dictated by proper long-run balance of payments considerations.

Thus OPEC faces presently the monopolist's dilemma of having to estimate the speed with which alternative energy supplies will be developed and to determine whether the increase in oil surpluses in the short and medium-run will exceed their decline in the long run. The interesting aspect of this cartel is, however, that individual members are in quite a differing position as far as such optimization is concerned. Furthermore, assessments are also being made on the demand side involving considerations of future prices and volumes of oil, particularly to decide on the speed with which alternative energy sources are to be developed. Therefore, these expectations would constitute a major determinant of the balance of payments prospects of OPEC countries.

OPEC Financial Surpluses and the International Capital Markets

The Experience of 1974-1975

Rinaldo Pecchioli*

Major consequences of the dramatic increase in oil prices in 1973-74 were a staggering alteration of world current account balances (table I) and the resulting need for unprecedentedly large compensatory financing through international capital flows. The new international payments situation called not only for a sharp restructuring of the geographical pattern of international flows but also for a far-reaching change in the environment of international private capital markets, requiring a shift of emphasis from the usual activity of industrial and commercial financing to financing for balance of payments purposes. In particular, it was clear from the outset that the international banking system would have to play a major rôle in ensuring an efficient recycling of funds from OPEC members facing extremely large surpluses to those countries which would not be, in the short run, in a position to correct their current account imbalances through appropriate domestic policies and/or to finance them *via* official and bilateral government-to-government channels. The following pages are intended to provide a short review of main overall developments concerning private capital markets in 1974-75, focusing on those aspects which were apparently affected most directly by the investment activities of OPEC countries.

Financial surpluses of oil-exporting countries

The overall investible surplus[1] of OPEC countries amounted to some $90 billion in the two years 1974-75. This cumulative figure conceals a markedly different pattern of the oil-exporters' financial

* This paper draws heavily upon researches carried out within the Financial and Fiscal Affairs Directorate of the Organization for Economic Co-operation and Development. The views expressed are, however, the resposibility of the author and do not necessarily represent those of the OECD.

[1] The investible surplus may be defined as the amount available for new financial investments abroad. In balance of payments terms it is conceptually equivalent to the current account surplus on a cash basis, after capital transfers.

Table I

World current account balances
($ billion)

	1973	Average 1974-1975
OECD countries	2 1/2	−19 1/4
OPEC members	3 1/2	52 1/2
Non-oil LDCs	−2 1/2	−21 3/4
Others[1]	−4	−12 1/2
Discrepancy	1/2	1

[1] Sino-Soviet area and developed countries outside OECD.
Source: OECD Economic Outlook.

positions during the two years under review. In 1974, the sharp increase in oil revenues was accompanied by a moderate (in absolute terms) increase in OPEC imports and, as a result, the overall investible surplus reached a staggering total of some $ 57 billion. In the following year, however, the combination of marked declines in oil shipments, a more moderate rise in oil prices and −especially− an extremely strong expansion of imports from OECD countries, resulted in the investible surplus being cut to around $ 35 billion.

This overall trend was accompanied by noticeable shifts in the position of individual OPEC members. Countries in the "low import absorbers" group (Saudi Arabia, Kuwait, the Gulf Emirates, Libya) continued to run very sizeable surpluses in spite of rapidly accelerating imports whilst "high import absorber" countries saw their surplus positions shrinking severely or recorded current account deficits. As a result of these developments, a dichotomy has emerged within the OPEC group of countries. On the one hand, the few countries in the first group continue to influence the pattern of international financial flows through their investment policies whilst, on the other hand, large financing requirements connected with ambitious industrial and infrastructural projects have compelled many "high absorbers" to make use of the financing possibilities provided by the international capital market.

Thus, the international financial market has been called upon to function as a recycling vehicle not only between the oil-exporting surplus countries and the industrialized and non-oil LDCs who have had to absorb higher oil prices, but also between the few OPEC members who enjoy large, and probably lasting, surpluses and other oil-exporters whose financing requirements cannot be covered in their totality by oil-export revenues.

The estimated deployment of the investible surplus on recipient markets is shown in Table II. Over two-fifths of the total was invested directly in developed countries through the acquisition of deposits, securities, equity participations, or in the form of direct government-to-government loans. The main beneficiaries of such investments were the United States (around 19 per cent of the total in both 1974 and 1975)[2] and the United Kingdom (in 1974 only). Comparatively smaller amounts were channelled directly to France, Japan and Canada. As far as non-oil developing countries are concerned, direct lending may be estimated to have totalled around $ 7 billion, mostly concentrated in Arab countries. OPEC members have also extended grants to a number of LDCs, possibly totalling some $ 3½ billion. The two major channels for indirect recycling of oil funds were the multilateral development institutions (World Bank and IMF) and, especially, the eurocurrency markets. The latter absorbed $ 28½ billion, or almost one-third of the overall investible surplus. The ability of the euromarket to redeploy such a large amount to a wide spectrum of countries facing balance-of-payments difficulties has been a major factor in ensuring the financing of massive current account deficits and has, therefore, reduced greatly the risk of these countries being forced to introduce restrictive trade policies on a large scale.

The disposition of the investible surplus by instruments appears to have changed significantly during the period under review. Identified bank deposits accounted for about half the surplus recorded in 1974 but fell to around 20 per cent the following year. Conversely, the share of investments in securities and other long-term paper rose sharply as indicated by data on investments in the

[2] The figure in Table II refers to *direct* placements by OPEC countries in the United States and, therefore, is likely to underestimate the actual total insofar as it does not take into account investments carried out *via* third countries and markets. In particular, sizeable amounts are likely to have been chanelled to the US in 1974 through OPEC "trust accounts" with banks in Switzerland and other off-shore banking centres.

Table II

Estimated OPEC external financial surplus *

Investment in:	Cumulative 1974-1975	
	US$ billion	Per cent of total
1. United States	17 1/2	19.4
2. United Kingdom (sterling assets)[1]	7 1/2	8.3
3. Other developed countries	12 1/2	13.9
Sub-total	37 1/2	41.6
4. Non-oil LDCs	7	7.8
5. International organizations	7 1/2	8.3
6. Eurocurrency markets	28 1/2	31.7
7. Others[2]	9 1/2	10.6
Total	90	100
Memorandum item:		
Identified bank deposits	35	39

* Conceptually equivalent to the current account deficit, on a settlements basis, excluding official transfers.

[1] Including foreign currency loans totalling $ 1.4 billion.

[2] Residual item.

Source: Elaboration of data published by US Treasury, the Bank of England and the BIS.

UK and the US[3] and information concerning investment activity on the eurobond market. Moreover, the average maturity of bank deposits showed a clear tendency to stretch out noticeably. This development reflected to a large extent the reversal of interest differentials between short- and long-term rates which took place

[3] See Bank of England *Quarterly Bulletin* and the monthly US *Federal Reserve Bulletin.*

in late 1974 and 1975 in all major national and international markets. It denotes, in particular, the eagerness of OPEC investors to adjust their portfolios to changing market conditions as well as their growing interest in investments of a longer-term and, probably, more stable nature in response to a more adequate interest rate structure.

Information on the distribution of the surplus by currency is extremely scanty but there are indications that the bulk of investible funds was placed in dollar-denominated instruments. Investments in sterling were sizeable in 1974 but negligible thereafter, mirroring the steady decline in the share of oil exports paid in that currency. Placements in other currencies were much smaller, though some OPEC member countries have been reported to have made not-negligible investments in strong currencies such as the Swiss franc, the Deutsche mark and the yen.

Globally speaking, it would seem that OPEC countries have followed a cautious investment policy during the last two years. Funds have been spread between a relatively large number of markets and countries, and this portfolio diversification has been accompanied by careful adjustments to changing market conditions and prospects, with a steady trend towards longer-term types of placement. The oil-exporting countries' approach in the management of their financial surpluses has been characterized as follows: "The monetary authorities of the OPEC countries have been most careful to avoid disruptive actions that, merely because of the huge amounts involved, could have unsettling effects on the international financial markets. In carrying out their responsibilities, the monetary authorities in the oil-exporting countries have also recognized the desirability of cooperation with the central banks of other countries of the world".[4]

Recycling through the euromarkets

The accumulation of huge financial surpluses by oil-exporting countries exerted major influences on the functioning of the eurocurrency markets in a number of ways. The most striking impact is discernible by considering the capital supply structure of the

[4] Address by Mr. R. A. Debs, First Vice-President, Federal Reserve Bank of New York, before a meeting of the Forex Association of North America on January 9, 1976.

market. Until 1973, oil-exporting countries had accounted for a negligible portion of funds placed with eurobanks, in the region of around 5 per cent. In the two following years, OPEC placements became the most dynamic supply factor, largely determining the growth pattern of the market. They accounted for almost 40 per cent of the increase in total eurocurrency deposits and by the end of 1975 the OPEC share in total outstanding liabilities of eurobanks reporting to the BIS had risen to around 17 per cent (Table III). The extent of the importance of OPEC investments on euromarket activity is even greater in relation to the *net* supply of funds. In 1974-75, oil-exporters were the only net providers of funds to the euromarkets, to the tune of some $ 13 billion on an annual basis. All other major economic areas increased their net indebtedness *vis-à-vis* the market, in several instances by very sizeable amounts indeed. The concentration of the sources of funds with a single group of countries contrasted sharply with the experience of previous years when industrialized countries, developing countries and, at times, Eastern European states had alternated in providing the market with a net inflow of funds.

The capital demand structure of the market was also directly affected by the new international payments situation. Most industrialized as well as non-oil developing countries were faced with massive current account deficits and the prospects of sizeable financing problems for a number of years. Therefore, all countries which had a credit standing enabling them to do so stepped up markedly their recourse to eurocurrency lending facilities. The increase in the aggregate euroborrowing by developed countries in the two years 1974-1975 amounted to some 40 per cent of their outstanding debt at the end of 1973. The ratio for non-oil LDCs was even more impressive, of the order of 65 per cent. A number of countries relied mostly on short-term banking facilities in the expectation that domestic measures designed to counteract the adverse impact of the oil-price increase on their trade balance would be sufficient to restore a more equilibrated position in a relatively short period of time. Most borrowing countries had, however, no alternative but to try to raise medium-and long-term finance to cover their structural balance of payments disequilibria. Industrialized countries were theoretically in a position to borrow at longer-term either through the floatation of fixed-interest securities on the international bond markets or by arranging medium-term loans carrying variable interest rate conditions with inter-

Table III

Eurocurrency markets: sources and uses of funds
(Banks of nine European countries reporting to the BIS)
($ billion)

	Cumulative changes 1974-1975	Outstanding at end-1975
1. *Sources*		
Developed countries	35.3	123.1
Oil-exporters	28.3	34.6
Non-oil LDCs	−2.1	16.2
Off-shore banking centres	9.3	21.8
Eastern Europe	1.4	5.1
Unallocated	0.8	4.2
Total	73.0	205.0
2. *Uses*		
Developed countries	35.6	125.5
Oil-exporters	2.8	5.3
Non-oil LDCs	7.7	19.5
Off-shore banking centres	16.9	35.6
Eastern Europe	8.2	15.6
Unallocated	1.8	3.5
Total	73.0	205.0
3. *Net positions (1 −2)**		
Developed countries	−0.3	−2.4
Oil-exporters	25.5	29.3
Non-oil LDCs	—9.8	−3.3
Off-shore banking centres	−7.6	−13.8
Eastern Europe	−6.8	−10.5
Unallocated	−1.0	0.7
Total	−−	−−

* A *minus* sign indicates that the area in question is a net user of eurocurrency funds.
Source: Bank for International Settlements Annual Report.

national banking syndicates. The former alternative, however, had no practical applicability in early 1974 as the prevailing interest rate structure (short-term rates markedly higher than long-term yields) had brought about a virtual standstill in eurobond market activity. Therefore, recourse to the syndicated eurocredit market proved to be the only available source of medium-term finance for deficit countries.

The surge in demand for medium-term euroloans was accompanied by a certain stiffening of terms and conditions but borrowers had no difficulty in raising huge amounts through the international banking system until mid-1974. By that time, however, the market was showing clear signs of strain, and concern was growing within the banking community about possible dangers connected with a too-rapid expansion of the market and the implications for banks' balance sheets of the maturity transformation resulting from the recycling of short-term funds deposited by OPEC investors to deficit countries requiring medium-term finance. The build-up of OPEC eurocurrency deposits was far from uniformly distributed, the bulk being invested in a limited number of large financial institutions. Reduced market homogeneity led to the development of a multi-tiered interest rate structure, institutions other than the major money-centre banks being asked to pay increasingly high premia for interbank funds, with a consequent squeeze on their profit margins. On the other hand, banks receiving large inflows of funds found it difficult to redeploy them within the limits of prudent banking practice. In addition, many banks' deposit-to-capital ratios tended to get out of line at a time when the possibility of enlarging their capital base was limited severely by the generally depressed state of stock markets. On the lending side, the sheer size of medium-term borrowing operations by a number of countries became a matter of growing apprehension, adding to the individual banks' reluctance to take in extremely large loans; and, as expectations about a significant improvement in the short-run of the international payments situation faded away, the financial community became increasingly uneasy about the extent of lending for purely balance of payments purposes. A series of foreign exchange mishaps contributed to heighten the fears that the international markets could not continue to perform as a major vehicle for the recycling of OPEC surpluses and resulted in a sudden and sharp contraction in interbank market activity which, in turn, was reflected in a noticeable slowing down in the volume of new

international syndicated eurocredits. In the fall of 1974, the market situation started to improve, due to corrective action by the banks themselves and steps taken by the authorities of some of the major financial centres. In particular, the announcement of measures intended to strengthen banking supervision was instrumental in restoring confidence and enabling the market to resume a more normal pace of activity. A major consequence of the mid-1974 confidence crises was the setting up of a healthier market structure insofar as it induced financial institutions to adopt a more cautious approach in extending loan facilities, especially in relation to the scrutiny of borrowers' economic and financial prospects, and helped them to re-establish more appropriate lending conditions.

The recovery of the market was facilitated by technical factors such as the disappearance of the reserve interest rate differential and the subsiding of inflationary pressures which made possible the re-activation of the international security markets and, therefore, contributed to the lessening of pressures on bank lending activity. Medium-term borrowing through eurocredits by OECD countries slowed down noticeably in the latter part of 1974 and 1975 as borrowers took the opportunity of raising longer-term finance at fixed interest rates on the eurobond markets. Overall demand on the eurocredit market remained, however, comparatively strong as non-oil developing countries took the relay, raising substantial amounts in spite of the noticeable hardening of spreads and commission fees and the concomitant shortening in loan maturities. It is to be noted that though becoming large in absolute terms, medium-term syndicated lending to LDC borrowers continued to remain strongly concentrated in favour of a relatively small group of countries with well-established links with the market and/or rich endowments in natural resources.[5]

All in all, identified medium-term euroloans exceeded $ 48½ billion in the two years under review, a 60 per cent increase over the volume recorded in the two previous years (Table IV). Thanks to the spectacular expansion of 1975, borrowing by non-oil developing countries more than doubled whilst the increase of OECD borrowing in relative terms (40 per cent) was roughly in line with that experienced in the early seventies. The discrepancy between the growth of eurocredit borrowing by developing and

[5] Details on individual syndicated eurocredits are published regularly in *OECD Financial Statistics*.

OECD countries is largely to be ascribed to the availability for the latter of other important forms of external financing, bond issues in particular. A development which characterized market activity in the latter part of 1975 was the strong comeback of several OPEC members (e.g. Algeria, Iran) which borrowed large amounts, mainly for the financing of big infrastructural and development projects. This added to some rundown of eurocurrency balances by a number of oil-exporters faced with rapidly increasing import payments.

Table IV

Recorded medium-term syndicated eurocredits
(US $ billion)

Borrowers	1972-1973	1974-1975
OECD countries	17.2	24.5
OPEC members	3.8	3.9
Non-oil LDCs	7.1	15.2
International organizations	—	0.1
Others*	2.0	4.9
Total	30.1	48.6

* Eastern Europe, South Africa, Yugoslavia and unallocated.
Source: OECD Financial Statistics.

The strong expansion of the euromarkets was accompanied by important qualitative changes, two of which deserve particular mention. Firstly, a number of Arab financial institutions set up, or enlarged, joint ventures with European, Japanese and US banks in early 1974, with the purpose of expanding their international activities. The possibility of having access to and of managing together huge capitals with the know-how provided by institutions already operating in international markets made possible a rapid growth of their activities and greater participation in international syndicates. This, adding to the growing importance of some Gulf States —Bahrain in particular— as off-shore banking centres,

Table V

*Foreign liabilities and claims reported by US banks** (Cumulative changes; US $ billion)

	1972-1973	1974-1975
A. Liabilities to:		
OECD countries	6.4	4.6
OPEC members	1.2	10.5
Non-oil LDCs	3.0	4.0
Off-shore banking centres[1]	0.8	3.4
Others	2.8	2.9
Total	14.2	25.4
B. Claims on:		
OECD countries	5.2	11.7
OPEC members	0.4	0.9
Non-oil LDCs	3.2	10.0
Off-shore banking centres[1]	0.9	9.2
Others	0.1	0.9
Total	9.8	32.7
C. Net positions (A −B)[2]		
OECD countries	+1.2	−7.1
OPEC members	+0.8	+9.6
Non-oil LDCs	−0.2	−6.0
Off-shore banking centres[1]	−0.1	−5.8
Others[2]	+2.7	+2.0
Total	+4.4	−7.3

* Including long-term liabilities and claims.

[1] Caribbean area, Panama, Hong Kong and Singapore.

[2] A *plus* sign indicates that the area in question is a net creditor whereas a *minus* sign indicates it is a net debtor.

Source: US *Federal Reserve Bulletin.*

contributed towards strengthening the position of Middle Eastern countries in international banking activity.

A second major development concerned the return of US banks as large net lenders to non-residents. The lifting of the US capital export control measures in February 1974 ensured that banks located in the United States would be in a position to participate actively in international lending operations and, therefore, facilitated greatly the redeployment of OPEC funds invested in the US markets.[6] This is what actually happened and, in the two years under consideration, US banks' claims on foreigners expanded at an annual rate of over $ 15 billion, or more than three times the figure for 1972-1973 (Table V). As the volume of liabilities to non-residents rose at a markedly lower pace, US banks were able to improve markedly their net financial position which had deteriorated substantially in previous years. It is interesting to note that, apart from large lending to Japanese banks, the recycling role of US banks was particularly important as regards lending to non-oil LDCs, these countries raising some $ 10 billion through direct loans by US-based institutions as well as obtaining very sizeable amounts (probably well over $ 5 billion) on-lent through foreign branches located in off-shore centres, the Caribbean area in particular.

International bond markets

Although the bulk of OPEC surplus funds has been invested in eurocurrency deposits or placed directly in the United States and —to a lesser extent— in a few other countries, international bonds would appear to have attracted a non-negligible volume of OPEC investments. Following on a long period of very modest issuing activity, international and foreign bond markets showed a strong revival in late 1974 which continued into the following year. As a result, the overall volume of external bond offerings reached an all-time record level of some $ 34½ billion in 1974-1975. More than 10 per cent of new issues was accounted for by

[6] In addition to enhancing the redistributory role of the US banking system, the removal of capital export controls led to a further strengthening of the interconnections between the US financial system and the euromoney and credit markets.

direct placements in Middle Eastern markets (Table VI). A number of loans were denominated in OPEC currencies (Kuwaiti dinar and UAE dirham)[7] and placed almost exclusively with OPEC investors. In addition, a sizeable volume of dollar-denominated loans was taken up directly and entirely by OPEC financial institutions (so-called "off market" private placements). Most of these borrow-

Table VI

External bond offerings
(Gross international and foreign bond issues; US $ billion)

Borrowers	1972-1973	1974-1975
OECD countries	14.4	24.8
OPEC members	0.2	0.1
Non-oil LDCs	1.1	0.7
International organizations	4.2	7.4
Others*	1.3	1.5
Total	21.2	34.5
Memorandum item: Offerings placed directly on Middle Eastern markets**	0.4	3.9

* Eastern Europe, Israel, South Africa, Yugoslavia.
** Issues denominated in Middle Eastern currencies and "off-market" private placements in the Middle East.
Source: OECD Financial Statistics.

ing operations concerned OECD entities. Finally, large amounts were channelled by OPEC countries to international development institutions (the World Bank in particular) through the placing of "special" bond issues with OPEC monetary authorities and governments.

Despite a certain expansion in recent years, the utilization of OPEC currencies in the denomination of international bonds

[7] Details on international and foreign bond markets are to be found in *OECD Financial Statistics.*

remained sporadic and of little overall importance. This situation reflects to a large extent the reluctance of international borrowers to make extensive use of OPEC currencies in loan agreements (in spite of the generally favourable terms) because of the limited hedging facilities offered by currencies for which well-functioning exchange markets practically do not exist at present. Of much greater relevance to the development of the international bond issue market was the support it received from OPEC institutions. Although Middle Eastern investors had been participating in international offerings for many years, it was only in 1974 that OPEC financial institutions emerged as important members of issuing syndicates, when the growing availability of funds and the desire to increase the diversification of portfolios prompted a number of Middle Eastern investment banking concerns to step up markedly their activity as issuing houses, both in relation to managing and underwriting and to participation in selling groups. There is no precise information as to the volume of international bonds taken up by OPEC institutions during the last two years, but it seems unquestionable that OPEC investors have become an important source of funds for the issuing market. Thus, a sizeable number of new public offerings was co-managed by OPEC institutions and, in addition, virtually all major dollar dominated issues carried an OPEC participation in the selling group. Finally, undisclosed but probably very large amounts were placed by OPEC investors, both private individuals and financial institutions, on secondary bond markets, thus contributing effectively to the broadening of such markets recorded in the most recent period.

Conclusions

Available information on the pattern of OPEC investments in 1974-75 suggests that they followed a conservative approach in the context of international financial problems in general. This conservatism has made it easier overcoming some of the financial problems caused by large current account imbalances resulting from higher oil prices. The stability of international markets has not been threatened by massive and sudden modifications in investment policies which, instead, adapted themselves gradually to changes in the international market situation and its prospects. The confidence crises experienced by the euromarket in mid 1974 can, however, though indirectly, be attributed to the new

international financial situation originated by the accumulation of large surpluses by oil exporting countries, while there is no indication that OPEC investors played an active role in promoting such disturbances. On the other hand, it may be said that the mid 1974 euro-currency market turmoil resulted in a restructuring of the market activity that ultimately contributed to a strengthening of the euro-markets. It should be stressed that the good overall functioning of the international private capital market was instrumental in providing deficit countries with the financing required to limit the domestic implications of the oil crisis of late 1973. It remains, however, that such a goal was obtained at the cost of a huge accumulation of debts on the part of the most seriously hit countries. This is likely to have exacerbated the longer-term balance of payments problems of these countries and might call for a drastic reappraisal of their overall economy and financial policies in the years to come.

Import Lags, Recycling and International Monetary Imbalances

Ruth R. Troeller*

Preamble

The price at which most international transactions take place is calculated from a posted price in terms of a single currency whose price, in turn, is quoted in terms of other currencies. Discussions on export income, therefore, have both a posted price and an exchange rate aspect. Oil is no exception.

An oil exporting country's ability to import depends not only upon the dollar price of oil and the rate of oil extraction, but also upon the exchange rate of the dollar *vis-à-vis* other currencies. To a great extent an oil exporter can eliminate the risk of a variation in his export revenue. The policies which will achieve this are concerned either with the posting of prices or with the rate of exchange. Some economists would prefer to price oil in a currency other than the dollar, whose value is not liable to fluctuate significantly. Others argue for the use of an exchange rate index instead of a series of binary exchange rates in order to determine the value of an exporter's currency. Still others, including the present author, recommend a combination of both policies.

All policies to eliminate exchange risks try to allow for the fact that export receipts and import payments may occur at different times and that the currency in which the export price is posted may be different from the currencies necessary for the purchase of imports. The need thus arises to invest export receipts as and when they are obtained in such a way as to minimise the damage that relative exchange rate changes may inflict on the country's future import potential. This is especially important for a number of OPEC countries with substantial export receipts but who, in the short run, might not be able to translate these into imports of goods and services because of low absorptive capacity. Consid-

* The author acknowledges with thanks the suggestions and contributions of John Lepper.

erable time lags in import consumption are then to be expected.

It is essential that the *relationship between the posted price of oil and the currency in which the price is posted be treated in quite a different way than the linkage that exists between the oil country's currency and the international asset to which it is pegged.* Indeed in this paper we will attempt to show that the most appropriate way to express the price of a barrel of oil is unlikely to be equally the most appropriate way to peg the exchange rate of an oil exporting country's currency.

This, of course, is not surprising once we consider that though before 1971 the dollar was the key currency, the major reserve currency, the intervention currency and the transaction currency, since then countries chose to separate these functions and may well use Special Drawing Rights as their reference currency, invest their foreign reserves in a number of different currencies, employ the D-Mark as intervention currency (especially if they are a contracting party to the European 'snake'), and pay for most of their foreign commitments in dollars.

The duality of the exchange risk problem suggests a duality of treatment. In this paper we shall first be dealing with the relationship of the posted price of oil with the posting currency, i.e. the relationship of an internationally quoted price with the international money in which this price is expressed. Subsequently we shall consider the criteria which determine the choice of a key index to safeguard the purchasing power of a country's currency against parity changes.

For this purpose we shall investigate whether it is more advantageous for an oil producing country to be part of a currency area; to let its currency float freely according to the laws of supply and demand (or not so freely, using supply and demand as indicators only and in fact administering the rate at which the currency is to be quoted); to peg it to an existing index such as the SDR; or to create an individual 'currency basket' as an index through which to express the value of the currency.

Posted price and posting currency

Oil price indices

No index describes reality: it simply represents part of it; nor does the price of oil or any price when taken as an index. It cannot be interpreted on its own terms. An index is always founded

on a base which harbours an aspect of change. In constructing an index, therefore, the end which it will serve and the type of information and guidelines sought must be clearly set out.

One cannot use the international price of oil as an index of purchasing power. One has to add at least one other element and since oil is expressed in dollars, this will clearly have to be the price of the dollar in terms of other currencies. One's domestic currency cannot be used either as an index for the posted price of oil since any variations in the latter's exchange rate towards third countries alters the foreign revenue from oil in domestic terms as well as in terms of other foreign currencies.

Conscious of the fact that the US dollar, —the currency in which the oil price is posted—, had since 1971 first sharply deteriorated and is now fluctuating quite considerably, OPEC countries have made several attempts at safeguarding the real value of their oil receipts without yet having found a satisfactory index.

Indeed even before the sudden drastic increase of the oil price in the autumn of 1973, the Gulf States felt that the dollar, while an internationally useful currency, was hardly a good store of value. In addition to a high domestic inflation rate, its rapidly declining exchange rate in terms of other major Western currencies was felt to necessitate repeated upward adjustments of the oil price to offset the decline in the value of the dollar.

Already in January 1972, an agreement was reached in Geneva, under the terms of the existing Teheran Agreement on Pricing, between the Gulf States and the oil companies in which it was agreed that adjustments in the dollar price of oil would take place according to movements in an exchange rate index. The formula was exceedingly crude in that it did not attempt to weight exchange rates according to their importance to oil-producing states. Indeed it is likely that even in the absence of the increase in the oil price in October 1973, the agreement would have broken down since it inevitably led to such a high degree of instability in foreign exchange receipts that the value of oil-producers' reserves would have decreased in real terms.

As it was, the use of a badly consructed index impeded the internal adjustment of real import demand for oil, perpetuating in this way the imbalance by keeping the income of the deficit country higher than it would have been if the deficit currency had been allowed to devalue and reduce the disequilibrium.

In the euphoria of the increase of the oil price the habit of pricing oil in 'unsecured' dollars crept in again. At a time when the oil price more than trebled, a one or two per cent decrease in the value of the dollar seemed to matter little. The desire to post the oil price in terms of a more stable money soon reappeared, and when in June 1974 the value of an SDR began to be pegged to a basket reflecting the movements of the sixteen major trading currencies against each other, OPEC countries focused their attention on SDRs as an index. This, it was felt, would give a greater measure of stability to the value of a barrel of oil, since not only are the currencies in the basket underlying SDRs weighted according to their country's share in world trade, but each movement by definition is compensated to a great extent by a 'counter-movement' of the other currencies. Therefore, the actual value of the basket —and thus of SDRs— is unlikely to fluctuate significantly.

This reasoning of course applies to any commodity agreement in which the posted price is expressed in an international money and it is largely irrelevant whether the percentage weighting of the currencies in the SDR basket does in fact approximate the import pattern of any of the contracting parties. What is needed is a figure that expresses a value and which by virtue of its very composition will exhibit minimal fluctuations.

Indeed, in a world in which not all currencies float and in which international reserves are felt to be rather too plentiful, the SDR, detached as it now is from gold, may fulfil a greater need as a posting currency for internationally traded commodities than as an actual reserve asset for which it had initially been designed. *Thus reference to the considerable shortcomings of SDRs as a transaction currency, though legitimate in the right context, in no way affects the SDR as a unit of account and should be treated as irrelevant.* What matters is that the International Monetary Fund calculates one figure or index every day and that this figure undergoes insignificant fluctuations and therefore forms a good basis for the oil price.

We conclude that SDRs are the best alternative for expressing the price of oil. They evidently will not eliminate all exchange risks but will considerably limit the possibility of erosion in the value of export receipts. SDRs are superior to a national currency as international money since their value is determined objectively in such a way as not only to ensure an appreciable degree of

stability, but to reduce the risk of domination by the agency issuing the national posting currency.

Since, however, SDRs will not safeguard the future import potential of export receipts, this question must be considered separately. It is considerably more complex. We shall analyse it in the next section.

Exchange lines

The problem

Every country and in particular every oil exporting country is vulnerable to the effects of changing exchange rates upon its ability to develop its economy with the benefits of imports from other countries. For OPEC countries the ability to import technology they desire is crucial, and variations in the currency of one industrialised country against another change the spectrum of opportunity costs they face even if their own currencies are fixed.

Several indices can be constructed in order to preserve the purchasing power of export receipts, depending upon what sort of guarantee is desired. It is imperative to sort out this problem because it is not possible to construct an index that provides insurance against all risks. Indeed the use of one index will in general mean that other risks are either not covered or are even intensified. It is up to policy makers to assess the risks and to employ the index which best serves their purpose. Each index can also be modified so that the purchasing power in respect of certain goods may be guaranteed and there appears no reason why other modifications should not be built into the index as and when required.

Attempted solutions

The variety of solutions that can co-exist in a relatively small geographical area can be observed in the methods that Middle Eastern oil-producing countries use to express and stabilise their currencies. Gold, the dollar, SDRs, freely floating rates, individual currency baskets —the composition of which in some cases is secret— have each been combined with varying degrees of convertibility; with straight exchanges against their currencies, with exchanges through the dollar with official parallel foreign exchange

markets, with heterogeneous sets of margins within which the currency is allowed to float against the dollar, against gold, against SDRs, even against its own currency basket, and to the complexity.

Indeed Iran, Qatar and Tunisia have each pegged the value of their currencies directly to the SDR index and indirectly to the dollar, which they use as an intervention currency; the Saudi Arabian riyal is formally pegged to the SDR, but with 7.25 per cent margin (within which it is linked to the US dollar), thus making it effectively unpegged; Kuwait expresses the value of the dinar in terms of a weighted but undisclosed individual currency basket, as does Algeria; Bahrain and Iraq are still pegged to the US dollar; Abu Dhabi and the United Arab Emirates continue pegged to gold.

The co-existence of these different systems does not seem to present a problem, even between countries as closely knit as those which form the nucleus of OPEC. Such diversity appears to be not only tolerated but also overtly promoted by the IMF.

Alternative solutions

Though flexible exchange rates are widely adopted at the moment, we shall not discuss them formally here because we consider such a mechanism to be wholly undesirable for small developing countries, especially for those with a significantly lopsided economy such as OPEC countries. Indeed under a flexible system the fluctuations of the oil price would be followed *pari passu* by movements in the exchange rate in the same direction and of a similar magnitude, amplifying both gains and losses disproportionately. No attempt at securing the value of future imports could possibly be successful and the country's fortunes would be utterly exposed to all the vagaries of the international demand for their product.

Another solution, the fixed but adjustable exchange rate system, the IFM regime —which officially lasted to January 1976 but in fact has been only partially adhered to since May 1971—, is not under discussion here because, by itself, it does not give any indication to what kind of a link would be the most suitable for insuring the future import potential against exchange rate fluctuations, while the declared purpose of this study is the search for a meaningful and relatively stable index in relation to which a country's parity can be fixed.

To belong partially, or even to be an integral part of a currency

area, exempts a country from having to seek for an index other than the reserve country of that area —such as the dollar. All it needs is the willingness to join a currency bloc and the readiness to float upwards and downwards against other currencies or currency blocs for reasons unconnected with and possibly even detrimental to its own economy.

Before the existence of eurocurrency markets, significant benefits could be reaped by a developing country from belonging to the dollar or the sterling area, i.e. pegging without margins to a Western reserve currency. At that time, to belong partially to a currency was often an optimal solution: foreign reserves could be held in one currency only, the domestic currency of the 'reserve' country, and if that country was also the major trading partner, such an arrangement reduced exchange risks to some degree, though by no means perfectly. Some of these advantages still persist.

On the other hand, the penalties attached to such an agreement can be onerous. Manipulations by the reserve country's monetary authorities of the money supply to cure domestic unemployment, as well as the threat of sterilisation measures for political rather than economic reasons, may have direct —and not necessarily desirable— effects on the developing economy. These may be difficult to counteract by the outer country's authorities. Even if it is possible to offset these detrimental effects, counter-active policies are wasteful and bring about a grossly sub-optimal situation because the funds employed cannot now be used directly to further development.

A strong and expanding eurodollar market has considerably reduced the attraction of belonging to, say, the dollar area. Direct and relatively unhampered access to the world's goods and investment opportunities, which used to be the privilege of members of a currency area, can now be enjoyed simply by dealing in the framework of the eurodollar market, without incurring the considerable costs of fixing one's currency to another without margins of fluctuation. The currency area link has ceased to be merely embarrassing and has become positively detrimental for a number of developing countries, whose export receipts have risen suddenly and drastically.

At a first view a depreciation of the reserve currency in terms of other currencies might appear to be unimportant since most inward foreign investments are likely to be made in that currency and most imports received from the reserve country, but a depre-

ciation of the dollar in terms of the deutschmark will allow one deutschmark to acquire an increased number of dollars, which in turn will buy more raw materials from a developing country in the dollar area. Thus a depreciation of the dollar means a de facto reduction in the commodity price expressed in dollars, to which must be added the presumption that imports from Germany have become dearer. This suggests that a developing country with perennial surpluses belonging to a partial currency area suffers considerable opportunity costs and that the disadvantages significantly outweigh the benefits.

We should, however, be aware that such an argument is not valid where countries at comparable degrees of development join in a full monetary union. The EEC, for instance, though in no way an optimum currency area, might find that the formation of a currency area might well be superior to most other alternative exchange rate systems open to it, especially as it need not even involve the creation of a common currency, but could function adequately with irrevocable and irredeemably fixed exchange rates without margins of fluctuation. The problem of valuation of a European currency would, of course, persist, though it is likely that the common currency or the various currencies (united in the 'snake' for instance) would be allowed to find their joint value by fluctuating in the foreign exchange market.

Alternative solution: SDRs

In our search to find a procedure through which a hitherto dependent currency can achieve a maximum of stability in the face of ever-changing exchange rates, we have to examine a number of new standards.

The ideal solution would lie in a uniquely defined reference (with or without margins) to some artificial unit of account, the value of which would be determined by a currency bundle rigorously proportionate to and varying with changes in the developing country's import pattern. But such a man-made currency —unlike SDRs— would fulfil only the skeletal function of a buffer and hardly warrant the complications that would arise: namely rigidity of the adjustment mechanism and increased need for domestic financial polices (in fact domestic policies not dissimilar to those needed during the full gold standard). We consequently hesitate to recommend it.

Some commentators might consider SDRs as a second-best solution. It is, however, unlikely that SDRs can really be considered an adequate standard to preserve export income and to create a climate of confidence in which investment and import decisions can develop into purposeful and long-term patterns. To base a country's currency on the SDR would certainly be superior to pegging it to a domestic currency such as the dollar or sterling. It could even operate with margins of, say, 2½ per cent either side – or 7.25 per cent as in Saudi Arabia's case – to make it more flexible. However, while SDRs were recommended as constituting the best posting currency for oil and international export commodities in general, they cannot be accepted without serious reservations as an index by which to value an oil exporting country's currency.

We would argue that while the value of SDRs as posting currency is readily acceptable as one figure which has the intrinsic quality of slight fluctuations, the precise composition and percentage weighting of the SDR currency basket becomes of considerable importance once we take account of the significant difference between most developing countries' import patterns and the percentage distribution of the SDR basket. This makes the SDR basket an inappropriate instrument for reducing their foreign exchange risk.

Instead of viewing SDRs as a single figure, we will have to analyse the SDR as a particular currency basket and compare the exact proportions of world trade which are represented with the exact proportions of a developing country's trade as expressed by imports from its various trading partners. Advocates of simplicity might well object to this somewhat complex argument. However, any wisely managed exchange policy, especially in an era of extreme international monetary uncertainty, must clearly take these factors into consideration. It must also be realised that OPEC countries are confronted with a completely new situation which necessitates readjustment in traditional values, customs and behaviour patterns.

This is not to argue that there is no virtue in an SDR standard. Indeed, should OPEC finish by fixing their commodity price in SDRs, some adjustment costs could be avoided on the international payments side if the developing country's currency was also linked to the SDR standard. But even those who take the view that a uniform standard should be adopted, in spite of the defects it may entail, must realise that the argument cannot be decided on theoretical grounds only, since a number of developing countries have

spontaneously opted for currency baskets different from the SDR proportions and considerably nearer to their own trade patterns.

Thus it would appear that an SDR standard does not solve the most urgent problems of oil exporting countries since only a part (and for a great number of them a minute part) of exchange risks are covered. It may be a considerable improvement on most existing exchange rate links, but we feel that the cost paid for this incomplete insurance is too great and we would certainly hesitate to advise countries whose import patterns are in flux to tailor their import plans in such a way as to make them conform to the proportions of the SDR basket. Since it would be spurious for OPEC countries to take yesterday's —or even today's— trade as a model for their future import pattern, a premature pegging of the exchange rate to any index which does not allow for continuous structural readjustment must be avoided. Indeed, unless the new standard adopted is flexible enough to allow all the effects of increased export receipts to work themselves out, it will turn into a straight-jacket.

In the next chapter, therefore, we shall lead the argument to its logical conclusion and propose the adoption of currency baskets designed for each petroleum exporting country's particular needs and fully allowing adjustments at every future stage.

Currency baskets

Our argument has led us to suggest that developing countries —and eventually all countries— might be better off by adopting a currency basket tailored to their particular trading and investment plans. This would involve the establishment of an indexing system which would see to it that the country's imports as well as its investments are weighted correctly and the currencies adjusted within the basket as and when the need arises, thus assuring that the actual proportions conform to the country's trading patterns. In addition the index would take into account relative inflation rates.

Discussing the criteria upon which an individual currency basket should be based, the most decisive element to be considered is the country's trade pattern. The foreign investment spectrum is only slightly less essential since the two may well show a marked interdependence. They may indeed be so closely linked that a decision about one can be made only after a decision about the other, leading to a chicken and egg problem, which can best be overcome by

constructing models in which decisions about the levels of all policy variables are made simultaneously and thus all problems of negative feedbacks are eliminated. (We shall return to such a model later.) For the moment, however, we shall attempt a solution in a more realistic, 'step-by-step' way.

To calculate a particular currency basket is, in principle, a very simple matter. Provided the currencies in the bundles are correctly chosen and the percentage weighting given to each equals the proportion of payments made in that currency, the future ability to purchase goods from abroad is protected against changes in countries' exchange rate movements against each other.

In a mature Western trading country a basket could easily be constructed by taking the propensity to import particular goods denominated in particular currencies as a guide. One would then perhaps adopt the procedure of averaging out, say, the last five years' imports or taking the year with the highest trade figures in order to find the appropriate weights for each exchange rate in that basket, or else —like in France— take 'indicative planning' as a guideline and work from there. For an OPEC country, however, this cannot be the right method. Past trade figures would necessarily lead to completely erroneous projections into the future and —as does the linkage with the dollar at the moment— prevent new import and investment patterns from emerging. It is thus inadvisable to rely on past trade even as an indicator.

Clearly, any programme that tries to regulate economic activity ahead can be used. Care should, however, be taken that the problem is not merely shifted and will subsequently reappear in the choice of the supplying country, since the very existence of a currency basket that levels out much of the exchange rate instability might also iron out a number of previously unnoticed distortions of comparative —in certain cases even absolute— advantage. Thus even where domestic policies are purposefully conducted towards determining the internal and external needs of the country, according to a preestablished plan, and therefore the quantities to be imported are given, it will not be easy to project beforehand the exact composition and currency weighting of the basket. Only gradual and perpetual re-adjustment will eventually result in yielding correct proportions, for even these will undergo continuous changes, since the basket is built on the living economic reality of ever-evolving trade patterns of the country. The more dynamic the changes, the more essential will be the flexibility of the basket.

It is even possible for a situation to arise in which the feedbacks amplify each other over time in such a way as to make the evaluation of an index unachievable, since the decision to import is based upon such factors as the exchange rate and the exchange rate is based, *inter alia,* upon the level of imports. Provided, however, we assume exchange markets are sufficiently elastic (which it is likely to be in OPEC countries) such a cobweb situation will not occur and we can expect to find a stable solution to the index. In this case it is a matter of convenience whether the values of instruments are decided upon by one agency at a given time or by several agencies separated in time. A system of simultaneously solved equations gives a picture of the stable solution to the index problem, not a description of the way the solution is obtained.

When the feedback of one instrument of change upon another becomes so significant that a stable solution is precluded, then the method of solving economic problems takes on a new tenor. In these circumstances it is possible to impose a solution on the situation by setting the level of all instruments simultaneously. If this can be done, the feedback process is eliminated, though if there is a discrepancy between planned and actual values of the instruments the feedback process may well lead to instability. To find out whether the process of unstable solutions is significant must await a full econometric exercise of the country concerned.

Evidently with or without a basket, one way of safeguarding the value of a country's future imports in physical terms and to protect them against exchange rate alterations is for it to invest its international reserves abroad in proportion to the distribution of currency payments for these imports. An appreciation of the currency of one import source would then automatically be compensated by the assets held in that currency and —in the worst case— their liquidation would pay without loss for the dearer imports.

We shall investigate only a few of the many objections to this view. First, such hedging completely ignores the yield or profit motive. Managers of large funds cannot ignore with impunity international covered interest considerations, especially where forward markets exist, and even more so where governments intervene occasionally in the forward market. Even though profit is unlikely to be the prime concern of government, there is a limit to the implicit loss a nation is prepared to take for the sake of merely hedging. Indeed since such a hedge is in essence an artificial commercial policy, welfare costs may be high, though it is just possible that the

ensuing bilateral trade expansion be great enough to elimitate them.

Second, the 'merchant banker's view' requires that investment decisions and import decisions should be closely co-ordinated. For if they are not, the hedging country may find itself more exposed to exchange risk than if no hedge were attempted. In practice, the two decisions are made by separate agencies for different reasons. Consequently, to require these agencies to co-ordinate their activities may lead them to fail to achieve the ends for which they were set up, as well as not achieving the hedge desired. But since in any case a one-to-one correspondence between targets and instruments is to be preferred, the creation of a new instrument for the reduction of exchange risk is advisable.

Third, while such a policy if, and only if, faithfully implemented would do away to a considerable extent with exchange risk, albeit at a price, it is, of course, not designed to safeguard against stiffening rates of inflation. Inflation is clearly a factor which poses a much larger threat to oil exporters than exchange risks. This will be increasingly so as some kind of currency basket —SDR or other— is introduced. The latter criticism is not confined to the view that import decisions should be backed by parallel investment decisions; it can evidently be levied against many other proposals as well. It is, however, appropriate to discuss it here since bankers in general tend to present hedging policy as a wholly adequate risk-averting exercise.

Fourth, any argument which advocates that exchange risk inherent in trade should be covered with the proportionate investments of the importing country's foreign reserves in the relevant currencies ignores the fact that there are countries whose exports are highly prized and welcome in international markets but in which no responsible government or private agency might wish to invest. (Examples are Italy and the United Kingdom.) In cases where there is no confidence in the value of currency, the risk of loss in holding it outweighs the benefit of a hedge to be gained thereby.

Why then not take the reverse view and advocate that trade should follow investment? At a first glance absurd, the argument gains much on closer analysis. In actual fact, whether trade follows investment or investment trade can presumably not be answered any more convincingly than was the controversy on whether in colonial times imperium followed dominium or dominium imperium. In such a circumstance, the use of models in which all factors are determined simultaneously to reach a solution may be

justified. In employing such models, however, –which are associated with the work of Meade, Tinbergen and Mundell– we must be aware that they can work only where they approximate the decision-taking process. They are inoperable, for instance, when the interactions between factors tend to amplify changes resulting from an initial disturbance. Clearly, only if trade and investment are associated in a stable fashion such simultaneous models may be useful and even in the best case the interaction will remain dialectic and at least one further instrument is needed to achieve the target of reducing exchange risk; that instrument is a currency basket.

Thus, however analytically satisfactory, theoretically respectable and empirically correct, none of the methods considered until now is able to indicate how the weights of a given currency in a currency basket are to be calculated and since the use of a currency basket will help to override comparative advantage, it is clearly impossible to proceed further without valid criteria to determine these weights.

We might thus have to be content with a basket calculated in a more intuitive, though not less dialectic way. The general climate of future plans, past trade patterns and the anticipated medium-range future of the world into which a rapidly growing developing country might wish to project itself could all influence the basket. In this way, the currency basket would have to reflect the kind of foreign relations the country would desire and in turn help shape these relations. In addition, factors such as unequal rates of inflation in industrial countries could be included to give the currency basket more relevance in the real world.

Precision at any point in time is evedently desirable, but since one of the essential characteristics of such a basket –and this no doubt makes it superior to the basket underlying SDRs– is its inherent fluidity, the weights which will ultimately be employed will be arrived at by continuous adjustment. Indeed the basket needs to be flexible enough to conform to any domestic or international aspiration so that the operating country can choose without fear or favour the international relations, political or economic, it prefers.

Any well informed and capable team thus should find it quite simple to fix these weights, especially since initial mistakes are easily –and almost automatically– corrected and smoothed out in the ensuing rounds of adjustments. No doubt internal flexibility is the necessary condition for the success of the scheme since it guarantees that a slow but certain movement eventually leads to correct proportions. This is particularly important when rapid

development and change in international economic relations mean that even the criteria that are right at a point in time will progressively become obsolete.

However, just as structural changes within the national debt of a country are able to change the entire liquidity structure of the economy, whilst not altering the level of the debt, the currency basket will prove a powerful management tool in the regulation of the whole foreign sector of the economy provided an intelligent and capable team administers it.

Depending on what kind of risk the currency basket is expected to cover, transactions related to the basket may finish by correcting or radically altering the existing position. For example, if existing import proportions are required to continue into the future and if imports depend solely upon exchange rates, then exchange rates will be fixed. As a result, real income adjustment *via* exchange rate changes will be impossible.

On the other hand, if the exchange rates in the basket are allowed to alter they may simultaneously alter the efficiency of monetary and fiscal adjustment policies with the effect that both the principle of effective market classification and the pattern of trade will change. In these circumstances, import targets must be set and monetary and fiscal policies made to accommodate the desired state of affairs. This is so even when import targets are not fixed but are intended to change though, in this case, tolerance levels will have to be set.

Evidently, once a currency basket has been introduced, a government will need to maintain exchange rate, monetary policy and fiscal policy in unison with the basket. Indeed to maintain a given exchange rate, a specific combination of monetary and fiscal measures must be employed. The same is true of a given interest rate where a fiscal policy alone or a combination of fiscal and exchange policy are to be used. As a matter of fact, the manipulation of the currency basket may entail a planning decision for the whole of the foreign sector of the economy. If the intended pattern of imports and exports is to be maintained, both monetary and fiscal policy must be tailored to fit these intentions. For if monetary policy is too lax or fiscal policy too expansionary, imports may be increased despite the changes wrought in the basket.

Apart from the trade position, it is possible to take account of other factors in our calculation of the weights in the currency bundle. Other factors such as the net uncovered position of the

country in various currencies as well as unequal inflation rates could also be included.

The adoption of a currency basket also allows the net uncovered position of a country to be taken into account. It may be that a country desires not just to guarantee its import capacity against exchange risk. Rather it may wish to take account of capital account items as well. If so, it need only consider the amount by which its portfolio of investments in percentage terms is different from the distribution of its trade. Indeed, as we have seen earlier, investments could be seen as a hedge against past or all of the trade, leaving a portion of either trade or investments uncovered.

Inflation in a foreign country will make the price of imports more expensive. If the same rate of inflation persisted in all countries the fact would be irrelevant to the calculation of the weights of the currency basket. In reality, however, countries experience different inflation rates and so the relative prices of goods change and since the rate of exchange rarely adjusts in full to offset the movement, the demand for that country's goods is likely to be affected and cause import patterns to change. Indeed, we should expect that the greater the difference between one country's inflation rate and its nearest competitor, the faster the decline in its share of the commodity exporter's market is likely to be.

This lowering of market share may lead eventually but not directly to changes in exchange rates, either because of lack of confidence or for purely trade reasons. In calculating the currency basket weights, therefore, the cross effects between inflation and exchange rates must be taken into account. Moreover, factors such as confidence may not be adequately reflected in market prices and so give further reason for the employment of a flexible administration of the basket.

Flexibility, therefore, would appear to be the pivot around which the usefulness of the currency basket calculations would revolve.

Conclusions

It could be argued that a floating currency cannot possibly secure a country's future import potential as well as did gold before it was demonetised. Gold, however, was stable only as long as the US Treasury was ready to buy or sell it at $ 35 a fine ounce. The value of the dollar on the other hand was expressed by the single weight of the very gold the value of which it established.

This artificially closed-circuit system constituted the standard in relation to which the parities of the world's currencies were fixed. Such a situation could not last since it was inherently, though not obviously, unstable and the 1971 breakdown was inevitable. The myth of stability was exposed already in 1968, when the two-tier gold price was introduced and the value of the free-market gold climbed well above $ 35 an ounce. This meant a *de facto* devaluation of the dollar, but few chose to acknowledge it as such at the time.

Initially founded on gold, Special Drawing Rights since 1974 are based on a moving average of quoted exchange rates and actual international trade figures. Assumed immobility has been replaced by a quivering motion, both following and moderating international economic activity.

There is no straight line to be found in nature, nor is there or could there be complete immobility. This need not project us into a Heraclitian world of incessant movement. Archimedes demanded one stable point to explain and recreate the world. He failed. But far from limiting the usefulness of the currency basket, the internal fluidity and external mobility constitute its essential attraction. As a buoy, neither fixed nor free, it will always keep you afloat.

Oil Agreements and the Strategy of OPEC

Antoine Ayoub

It is clear that economic development requires, as a necessary but not sufficient condition, a certain rate of capital accumulation. This accumulation can hardly take place under terms of trade systematically unfavourable to the country or countries which seek to develop.

If we admit the two statements that I have just formulated, the matter set out for today's discussion can, therefore, be stated in the following manner: does bilateralism or multilateralism favour the maintenance and adequate evolution of the level of prices of OPEC's oil, given that this maintenance and this evolution are the necessary conditions for a sustained capital accumulation for such a group of countries?

In order to avoid complicating the debate with possible misunderstandings of a terminological nature, I shall simply define the bilateral agreement as an agreement between *one* of OPEC's members and an industrialized country setting out the conditions (prices and quantities) under which oil may be exchanged in return for commodities and services delivered by the second country. As to multilateral agreements, they designate an arrangement of the same nature which is drawn up between *all* the OPEC group and the whole of the industrialized countries (e.g. OCDE) or between two important subgroups (e.g. the Euro-Arab dialogue).

Having said this, I should like to argue, briefly, that multilateral agreements are to be preferred by OPEC countries, both from the point of view of the group and of that of each country taken individually.

I shall start by certain very general theoretical statements and shall refer later on to certain comments in regard to the subject.

I. *Automatism and strategy*

In the ideal world of normative theory of international economic relations, strategy is excluded. Everything happens, between enter-

prises in different countries or even between nations as such, according to automatic mechanisms that are derived directly from the basic assumptions of pure economic theory. In this sense, the economic unit is considered as a "receiver of prices" without any capacity to modify in its favour (and in a more or less prolonged way) the parameters of the market. There is no place therefore, in such a situation, to ask oneself about the "optimum strategy" that should be adopted (bilateralism, multilateralism or even autarchy) since, by definition, the behaviour of the unit leaves untouched the reality of the market.

If I make an appeal to such known "principles" it is in no way to open up a debate that perhaps does not have its place here. On the contrary, I should like to call attention to the fact that enterprises in industrialized countries as well as governmental bureaucracy do not cease to discourse on the virtues of the "free market" and the self-regulating automatisms while practicing, at the same time, their own "strategies" to assure a dominant position in the world market. This dichotomy in behaviour, without going any further, is the one responsible, from my point of view, for the failure of the dialogue between a North holding fast to its "acquired rights" and a South that awakens, finally, to its "inalienable rights".

The greatest innovation of OPEC, in this sense, is neither the revaluation of oil prices nor the accumulation of "surpluses" in the hands of its members. All these phenomena are, without any doubt, consequences and not causes. The main cause of OPEC's success is having understood that it was illusory, in a world of coalitions and associations between producers, to profit from the tensions of emerging scarcities in the market without putting up to the sellers of technology and manufactured products a common strategy of sellers of natural non-renewable resources, and therefore of basic products.

But to oppose in this way two strategies does not mean in any sense that the result of confrontation should necessarily be the break up and withdrawal of each group. On the contrary, this confrontation may very well lead to a new model of North-South relations. Under this model, rules and mechanisms may take better into account the interests of the disadvantaged without sacrificing for this reason the fundamental interests of the other party.

It is true that it would be very hazardous to predict the probable result of such confrontation, given that there is no scientifically controlled theory of conflicts, unless it is accepted that "historical

determinism" is a theory of this type. On the contrary, if one sticks to the zero-sum game theory and there are more than two players, it is known then that such situation leads to "indeterminacy".

Even if this situation is considered as being open, nothing prevents one from asking what means one of the parties (in our case, OPEC) should put into practice to increase its earning possibilities or, to use economic jargon, to optimize its objective function.

II. *Bilateralism or multilateralism*

In the light of these very general theoretical considerations and having always in mind that a country (or group of countries) —in a situation where the world market is characterized by a non pure and imperfect competition— a country can very well seek a national optimum that does not necessarily coincide with the world optimum, we can ask ourselves about an optimal strategy for OPEC in the matter of oil agreements. With this idea in mind, the following remarks may be in order:

1. It does not make any sense and is totally absurd to continue asking, as the majority of writers and even some "scholars" do, how and to what extent may the trade surpluses of certain OPEC countries be used rationally. This is a problem of national domestic decision that should interest others only in as much as a country seeks to adapt and adjust to its effects. It should be noted, on the other hand, that the unevenly distributed deficit among consuming countries on the oil account, has as its counterpart an equally uneven surplus among producing countries. However, the crisis and the "indigestion" of the international monetary system promised for 1974, 1975 and 1976 did not occur. At the level of the international monetary system it would therefore be wrong to pretend that its equilibrium necessarily depends upon bilateral oil agreements.

2. If, on the contrary, consuming countries seek by means of bilateral agreements to obtain advantages or discounts, explicit or implicit on prices and/or terms of delivery and payment, then grave risks for OPEC's cohesion as an association for the defense of producers' interests would emerge. In this sense, bilateral agreements will be a highly efficient instrument in a strategy that looks for the disintegration of OPEC. The proposal made by M. A. Adelaan, some months ago, relative to the creation of a market

of export quotas inside the United States is inspired to a great extent in this strategy (bilateralism) —although such agreements have not actually been signed between States.

3. To underline the dangers that threaten producing countries in this kind of agreement, the following evidence should be remembered:

(a) Even if the price of oil should never, under any circumstances, be equal to its average technical cost, a certain decline in its level would result from the resort of producing countries to bilateral agreements. In fact, even if the extraction cost —technical cost— is included in the "real" cost —plus a certain user cost responding to the depletion of this exhaustible resource— it is a fact that competition between producers will necessarily make them lose the cost of their economic development, that is, the margin that allows them to offset the increase in the price of technology and manufactured products, which is subject, in most cases, to the rules of oligopolies.

(b) If the rate of increase in oil prices proves to be less than that of industrialized products there will be no doubt about the "collective" impoverishment accruing to OPEC as a whole, even if one or the other of the members could improve its position momentarily.

(c) The dislocation of the OPEC front is bound to bring about a rearrangement of power relationships not only among OPEC members but in regard to all of the Third World countries. The dialogue, though difficult and full of pitfalls, held in Paris between the North and the South will make no progress by its own as dozens of meetings and stabilization projects of primary commodities have made no progress either.

4. In a world where the rule of "nothing for nothing" is in force, it would be highly improbable to believe that economic development of Third World countries (that is, their industrialization and some degree of autonomy in the management of domestic resources) is a goal for which industrialized countries would sacrifice voluntarily the welfare of their people in order to permit its achievement. The phenomenon of "aid for development" is there to definitely educate the unbelievers.

The points which I have just briefly underlined clearly point out, contrary to other opinions, that the optimum strategy for OPEC countries is, in my view, a strategy based upon multilateral agreements that should offer not only a solution to the problems of

indexation of oil and primary commodities prices but also of the conditions of access to technology, of control of transnational enterprises by national authorities, of the Third World's indebtedness; in sum, all the problems which the term "new international economic order" brings to mind.

At the moment in which a group of underdeveloped countries retain for the first time some negotiating power it would be highly regrettable to waste it in the search of short run interests.

Part II

General Aspects

Food Supply and Capital Formation in the Less-Developed Oil-Importing Countries

Rajni Kothari

One of the recurring themes in the critical discussion of the new energy situation is the plight of the oil-importing less-developed countries following the sharp increase in the price of oil by OPEC countries in 1973-74. The concern for the poor countries has been voiced not just by spokesmen of these countries but also by the oil-exporting countries who have reaped the main benefit from the dramatic redistribution of wealth that their oil diplomacy has brought about, and also from the richer developed countries who have suddenly awakened to the plight of the poor billions for whom until recently they had shown scant regard and measured indifference. The major media of mass communication, scholarly seminars and conferences of diplomats and government leaders have all voiced this concern with increasing intensity and vehemence.

Needless to say, there is some real basis to this logic. In the years following the hike in oil prices, the poorer among the LDCs experienced a substantial rise in their import bills, a significant part of which was due to the increase in oil prices. This led to serious dislocations in the economies of these countries for which there was no immediate resolution in sight. Let it also be noted straightaway that the behaviour of the OPEC countries themselves (with the single exception of Venezuela) towards their other Third World fellow-nations left much to be desired. Not only was their response to the appeals for sharing a portion of their newly acquired immense wealth with the poorer countries (or alternatively of differently pricing or subsidizing the purchase of oil by these countries) on the whole halting and often lukewarm; their diversion of these funds to investments in the major capitalist centres only helped accentuate the neo-colonial structure of the world economy; and their near-mad rush for armaments and other fashionable gadgets, many of which they did not know how to use, only served to perpetuate the tensions and inequities of the world from which

they —and others— stood to lose in the end. By so using their newly acquired wealth and power the OPEC countries (especially of the Middle East) also compromised themselves politically, lost the diplomatic initiative that they had wrested in the first instance, and exposed the internal contradictions and mutual suspicions and animosities from which they continued to suffer.

Finally, let us also recognize the fact that the Western countries and Japan have shown considerable dynamism and capacity to deal with immediate set-backs with the result that they have, in less than three years, come back into their own and indeed show some signs of benefitting from the 'crisis' that once appeared to break hell loose on them.

But while all this is true and must be admitted, it misses both the real dynamic of the process started by the actions of OPEC and the immense potentiality of recharting the course of development of the Third World countries that is inherent in it. In what follows we shall discuss these two aspects with a view to providing a frame of reference for dealing with the two specific issues that this paper is concerned with, namely food supply and capital formation in the LDCs.

As I see it, when development is looked upon in the global context with focus on satisfying the needs of the people everywhere, there are four main problems that need to be resolved. These are:

1. Distribution of *accessible* resources between the industrialized countries of the North and the Third World countries of the South, and consequent terms of trade between the two.
2. Discovery and mobilization of *new* resources by the Third World countries in their regions.
3. The model of economic development in respect of satisfying minimum needs of all the people.
4. The technological model in respect of providing an optimal mix of capital and human resources for evolving a viable economic model.

I shall argue that on all four of these the effect of the 'new energy situation' created by the actions of OPEC and reactions thereto in both the industrialized countries and the LDCs was disadvantageous to the LDCs in the short term but advantageous when considered in the medium and long terms. Thus the initial redistribution of resources that followed the rise in oil prices was accompanied by patterns of investment of petro-dollars, international trade and pric-

ing of manufactured goods and food which went against the interests of the LDCs. The transfer of investible funds that resulted from this also meant, in the immediate effect, a slowing down of mobilization rates of new indigenous resources in them. Again, the shift of economic policies that could provide employment and incomes to the mass of the people and a corresponding shift in technological policy also did not materialize immediately and, if anything, suffered a set-back as all attention was devoted to finding new foreign exchange to finance the sharply increased import bills, largely through added inputs into export-oriented industries. In sum, the LDCs started to lose on all four counts.

All this, however, was the immediate and short term impact. (Even here it is necessary to recognize that the years immediately following the hike in oil prices were also the years of severe drought in a number of LDC regions as well as of rise in import prices of food and manufactured goods which was independent of oil prices, so that it is misleading to trace the source of the problems faced by LDCs to just one factor.) Viewed in long term perspective, the same indicators seem to behave differently and, depending on an appropriate policy response on the part of Third World countries, can be made to behave in their favour. One of the key issues in global distribution of well-being are the terms of trade between the developed and the less-developed countries, the cost of imports of capital and manufactured goods from the former to the latter steadily rising and the cost of imports of primary goods and raw materials from the latter to the former steadily falling.[1]

The oil-producing Arab countries (and, following them, other oil-producing countries) made a major dent in this situation of inbuilt stagnation and continuing inequity for the Third World. Even though the position of oil was somewhat unique, it did show in a rather dramatic fashion the gross dependence of the developed countries on the Third World countries for keeping their economies and technologies going. The lead provided by OPEC was followed up by the producers of other raw materials while at the same time the increased cost of energy slowed down the growth of synthetics which had threatened the position of other raw

[1] Thus even in the period of relative price stability, 1952-62, the prices of cocoa, coffee and tea fell from 100 to 79; of fats and oils from 100 to 87; of rubber from 100 to 82 and of fibres from 100 to as low as 63. In the same period the prices of manufactured imports went up from 100 to 108. In the decade that followed the terms of trade declined further.

material producing countries and gave them a fresh lease of life. With most of these countries the problem was more psychological than economic. Given the debilitating effects of a typical colonial economy in which 'dependence' was structured in a one-way fashion, the *élites* of these countries had all along undervalued the worth of their own produce and allowed the foreign importers of it to continuously drain the resources of these countries at throwaway prices.[2] Always valuing the produce of factories far more than of land, these *élites* naturally led their countries into getting far less from international trade than they could have. The problem was accentuated by the fact that a large proportion of the plantations, oil fields and mineral production was controlled by foreign companies who alone had access to the technology necessary for excavation and processing. (If at all the local government, as for example under Mossadegh in Iran, tried to wrest this control, the companies were able, with the connivance of local vested interests, to defeat such moves.) In all these respects the series of actions of oil-producing countries —from nationalization to price fixation—provided a major psychological breakthrough.

The psychology of undervaluing indigenous resources and overvaluing the output of others also influenced the course of policies that were pursued for local economic development. Bewitched by the mythology of 'modernization' according to which capital-intensive and high-energy-consuming industries constituted the

[2] This phenomenon had been noticed by a series of early Indian nationalist leaders in the nineteenth century, whose most famous spokesman was Dadabhai Naoroji. In the words of Naoroji, a rather original thinker who propounded the theory of economic drain during the colonial period, there were 'two Indias' created by an internal drain that was an instrument of the external drain. "In reality there are two Indias —one, the prosperous; the other, proverty-stricken. The prosperous India is the India of the British and other foreigners. They exploit India as officials, non-officials, capitalists in a variety of ways, and carry away enormous wealth to their country. To them India is, of course, rich and prosperous. The more they can carry away, the richer and more prosperous India is to them . . . The second India is the India of the Indians— the poverty-stricken India. This India, 'bled' and exploited in every way of their wealth, of their services, of their land, labour and all resources by the foreigners — this India of the Indians becomes the poorest country in the world after one hundred and fifty years of British rule." See the authoritative study of Naoroji's drain theory by B.N. Ganguli, *Dadabhai Naoroji and the Drain Theory,* Dadabhai Naoroji Memorial Lectures 1964, Bombay, Asia Publishing House, 1965. Unfortunately, this thinking had little impact on the post-independence *élite* in India.

kernel of 'development', the economic planners in LDCs went for an uncritical adoption and emulation of the economic structure as found in the highly industrialized countries, rather than assessing indigenous resource endowments and harnessing them to the fulfilment of indigenous needs. Thus even in countries endowed with large human resources on the one hand and vast deposits of coal and rich water resources on the other, the model of agricultural and industrial development that was followed was one that depended on imports of both capital and energy. The result was a structure that was heavily dependent on imports and at the same time led to a gross underutilization of indigenous human and mineral resources.

Take the case of India, which had not only a large population that called for an employment-oriented economic policy but also one of the world's largest coal deposits as well as enormous water resources. Instead of evolving policies that would have utilized these, it went for a highly capital-intensive industrial policy and gave far more importance to oil-based energy, most of which it had to import, than to coal and electricity which in fact were highly underutilized. Even for its much celebrated 'green revolution' it went for oil-based fertilizers, insecticides, etc. rather than (a) basing these on coal and (b) utilizing other forms of manure and generation of gas and other forms of energy that was based on natural manure and waste. The result was that when oil prices shot up and capital imports had to be restricted, local development came to almost a standstill and the country was overtaken by an unprecedented incidence of inflation. (The inflation was, of course, partly a result of a series of droughts and the after-effects of the cost of Bangladesh refugees and the war, but partly also a result of faulty policies which made the country pay through its nose for oil and fertilizer imports.) At the same time its undervaluing its own massive produce of iron ore, jute, rubber, tapioca and other primary products meant on the whole stationary and in part declining export earnings.

The restoration of oil to its natural price by the OPEC countries has meant two things for a country like India: a better utilization of alternative energy sources that were indigenously available all along, and a true appreciation of the value of its own primary products, e.g. iron ore, whose prices were sought to be brought to their 'natural' level in concert with other iron ore producing countries (though some of the latter, especially from the developed

part of the world, have sought to restrain such a move). It also took major steps towards indigenous exploration of oil and natural gas which were all along known to exist but were neglected thanks to the availability of cheap imports. Together with this it also nationalized the various foreign oil companies and brought practically the whole of the oil industry and technology under government ownership. This has already, in the span of barely two years, produced major dividends both in terms of discovery of new oil and in terms of control of profits and technology. A good deal of the credit for these measures should go to the 'new energy situation' created by OPEC.

The above analysis of the consequences and alternatives of the new energy situation point to two major themes both of which have a bearing on the development strategy of LDCs in general and on food supply and capital formation in particular: (1) the need for an alternative model of techno-economic development which is sensitive both to a factor mix different from that of highly industrialized countries (limited machine capital and abundant human capital) and to the need for satisfying the minimum needs of the people at large through generation of employment and purchasing power in them, rather than production targets in the aggregate, and (2) the need for an alternative energy policy which is also based on indigenous resource endowments. Common to both themes is a search for a strategy of self-reliant development which puts an end to dependence and in the course of time leads to a more equitable distribution and control of world resources.

For the last several years the need to move towards an alternative model of economic development has been stressed. The rise in oil prices has given a fresh impetus to this thinking, which has now moved from mere academic exercises among scholars to serious thought by policy-making *élites* themselves (though the latter process has only just begun.) But oil prices is only one factor among the many that have contributed to such thinking. The rising cost and increasing difficulty in the availability of capital is another factor. The realization that industrialization based on heavy doses of capital and energy failed to generate adequate employment even in the longer run was another. And yet another was the growing criticism within LDCs that such a strategy of development widened disparities and, thanks to the peculiar structure of international investment and finance, led to a net and steady outflow of capital —in short, that given the capitalist-neocolonial framework, indus-

trialization only increased dependence and exploitation rather than leading to a 'take-off' into self-sustained growth.

Apart from these considerations, the major problem with a development strategy that relied so heavily on imports of capital and high doses of energy from the viewpoint of achieving self-reliance, was that it put far more emphasis on urban based industrial growth suited to the needs and fancies of the urban middle class than on agricultural development and production of consumer goods suited to the needs of the poor majorities of these countries located mainly in the countryside. A shift to an alternative strategy that both laid emphasis on employment and on smaller doses of and alternative sources of energy would, instead, give primary attention to increasing the production in the rural sector in both agriculture and other ancillary employment —not as some welfare measure or even as part of the race between population growth and increase in food supplies, but rather as a positive means of effecting increased production all round, in agriculture principally, but also in the non-agricultural sector through the release of income for other consumer commodities.[3]

In the new strategy capital is by no means considered unimportant. It is simply that the focus of public policy is seen to be agricultural output and rural development and the development of such consumer industries as will satisfy the demand generated by increased rural incomes. Capital formation and increased investment, in this thinking, are seen as somewhat more capable of taking care of themselves. Indeed, in the new strategy capital formation takes on a dispersed and spontaneous form in which widely available human resources, natural sources of energy and a decentralized structure of credit and servicing converge to produce new savings and investment which are then made available for the production of consumer commodities needed by the mass of the people. Not only does the supply of food improve markedly; capital formation also takes on a more indigenous and self-reliant form, and, what is more, capital tends to be channeled to the production of felt needs instead of being bottled up in the production of luxury items for the urban middle classes.

This is not to say that sophisticated technology is not needed

[3] See J.W. Mellor's paper on "The Choice of Development Strategy" presented at the 25th Pugwash Conference on Development, Resources and World Security, Madras, India, January 1976.

in the new approach. It is very much needed. One of the problems in a labour– oriented approach to development is that it relies a great deal on the availability of an increasing supply of agricultural commodities. And yet agriculture in its traditional form is subject to diminishing returns and requires disproportionate increases in inputs to a relatively constant land area, unless agriculture itself is subjected to rapid technological changes leading to increases in per acre yields at constant or decreasing costs. This calls for important inputs of science and technology to agriculture, complemented by major investments in irrigation, electrification, road-building, bunding, etc., as well as a major effort in new institution-building in the rural areas for mobilization of new resources, credit and marketing, and an efficient flow of inputs to and outputs from agriculture.[4]

All this does mean a major investment programme. But the difference in such an investment programme from investment in the earlier model of city-based industrialization is (a) that it is utilized for highly labour-intensive activities and (b) that much of the capital is in itself generated by indigenous effort and does not require any major 'transfer' of capital from abroad. And (c) as far as increases in food supply itself are concerned, they seem to depend far more on things like irrigation and pumping of groundwater, on the one hand, and electrification and the use of a wide variety of sources of energy, on the other, than on large doses of either imported oil or imported capital. As regards fertilizers, these can be switched from oil-based production to coal, electricity and natural gas base.

In sum, the 'new energy situation' far from impeding increases in food supply and capital formation, can provide a spur to focusing the whole development strategy on them and doing this in a manner that is truly self-reliant and which greatly reduces dependence.

All this is not to underrate the importance either of fossil fuel-based energy or the need for a minimum necessary industrial growth based on such energy to provide the necessary infrastructure for the production of fertilizers and other inputs needed for a dispersed model of development. Indeed, there is a great deal of scope for this too. The important point to note here is that, thanks largely to the artificially low price of Arab and Persian Gulf

[4] *Ibid.*

oil, very little effort was made to discovering it in other areas. Also there were structural constraints built into the existing framework of ownership and control which have not permitted such exploration. Thus, even if we consider the non-renewable resources alone, the evaluation of their total reserves and distribution is still a highly debatable matter. 'This is due to the fact that the discovery and the exploration of mineral deposits implies a cost; as a consequence, the mining enterprises only develop the resources needed to amortize their investments with a profit. It could be said then that the known reserves of a given mineral product are a function of the market demand'.[5] This can clearly be changed once national governments and their regional or functional groupings wrest control of these processes.

In fact, in the LDCs (which account for more than 60 per cent of the earth's surface) careful exploration has just begun. Thus 'in Latin America, geological mapping to a scale 1-250.000 or less, which constitutes the basic tool to guide the systematic search for mineral deposits, had hardly covered, in 1964, around 5 per cent of the total surface'.[6] The situation is not very different in other LDC regions. Also, most mineral resources that have been so far discovered are either due to their outcrops or at relatively shallow depths (approximately 300 m.) whereas geological surveys indicate the presence of deposits at much deeper layers, only a few of which have so far been extracted. It is thus 'highly probable that the number of deposits still unknown exceeds by far the number of those already discovered'.[7]

Thus the present energy situation is an outcome of the industrialized nations' assumption until recently of unlimited natural resources, at cheap rates, and under their almost complete control including their capacity to determine prices. Most poor countries adopted the same 'path of development' and in turn assumed cheap availability of mineral imports which retarded both (a) a truly indigenous response to application of energy to development needs and (b) discovering the mineral resources in their own lands as a supplement to other sources of energy. The 'new energy situation'

[5] A.O. Herrera, "The Problem of the World's Unevenly Distributed Resources", paper presented at the 25th Pugwash Conference on Development, Resources and World Security, Madras, India, January 1976.

[6] *Ibid.*

[7] *Ibid.*

caused by OPEC action is likely to spur thinking and action on both these fronts and lead to a far more diversified and on the whole more equitable distribution of and control over energy and other natural resources. And with this, as already indicated, it will also be possible to have a mixed and diversified approach to development with the main accent on agriculture and a pattern of capital formation and institutional growth that are meant to provide consumer goods that can satisfy the needs of the large mass of the people instead of that of a small *élite*.

As these developments take place, it will also be possible to bring about a better understanding between the present OPEC countries and the rest of the Third World, an understanding that is based on complementarities of both interest and capabilities. Already, these complementarities are being perceived, as for instance in the realization in the Middle Eastern countries, after a first flush of going in for the most sophisticated and capital-intensive industrialization, that it is much better for them to go for more intermediate forms of technology; or in the growing reliance of these countries on technical manpower from other LDCs (like India, Pakistan, Sri Lanka) as well as technological assistance from them, including for further mineral exploration, than on such inputs and assistance from the more industrialized countries whose background and sensitivities are unsuited to the conditions in these countries. The oil-exporting countries have also substantially increased their imports of consumer and intermediate goods from the other LDCs. All this is likely to grow in the years to come.

Also likely to grow is the greater attractiveness of investment in leading Third World countries (e.g. with the improved foreign exchange situation in India, world bankers have started offering investment at attractive rates). And with all this will also grow a sense of collective self-reliance of the Third World.

The present scenario of the OPEC countries graduating into the first world and the plight of the other LDCs steadily deteriorating is based on fixed notions of technology, spread of natural resources, and channels of capital absorption and political influence. In fact, however, these are not constants but variables and subject to major changes. The new energy situation is likely to catalyze major shifts in them and lead to quite a different scenario than is being painted by influential commentators and mass media from the North which unfortunately wield a disproportionate influence on thinking in the LDCs as well. The success of the alternative possibilities out-

lined above will depend crucially on the ability and willingness of the *élites* and decision-makers in the Third World to stop passively accepting the analysis projected from these media and to think for themselves and devise means – singly and collectively – to put an end to their dependence.

Instant Industrialization and Social Change

Joseph Hodara

I. *Introduction*

The economic, political and financial events which took place in 1973 —sometimes called, perhaps with excessive simplicity, "the energy crisis"— brought about diverse effects in substance and in magnitude. Although some place the emphasis on the presumably artificial and fictitious nature of the crisis,[1] the majority of the analysts recognize its tremendous importance; they do, however, present differing points of view and evaluations of the consequences of those events. Thus, Darmstadter and Landberg[2] argue that the new energy situation has come about from long-run tendencies affecting the geographic location of the supply of petroleum sources, the consumption patterns prevailing in the industrialized countries —mainly the United States— and the links between oil exporting countries and oil companies. The events of 1973 would signify not only the end of the "Pax Cartelia",[3] but also the mutation of the factors which have secularly determined the oil markets.

Other specialists stress the collateral effects of the crisis on the economic and international political stratification. Vernon[4] states emphatically that the vast transfer of resources from consuming to producing countries could have a tremendous financial effect; moreover, the latter may be able to fix the terms and even the style

[1] For example, F. Singer: "Energy Policy in the Oil Crisis", *Oxford Seminar on Oil Wealth, Discrimination and Trade.* Christ Church College, July 7-9, 1975. The mixture of fiction and reality characterizing the "crisis" has been accurately described by D.A. Rustow, "Petroleum Politics 1951-1974", *Dissent*, Spring 1974.

[2] J. Darmstadter — H. Landsberg, "The Economic Background", *Daedalus*, Winter, 1975.

[3] M. Grenon created this term in *La crisis mundial de energía*, Madrid, Alianza Editorial, 1974, p. 195.

[4] R. Vernon, "An Interpretation" and "The Distribution of Power", both in *Daedalus*, Winter, 1975.

for the negotiation with the former. Girvan, [5] sharing this point of view, points out that the crisis "abruptly disrupted the patterns of power which had been in effect between the center and the periphery", in this way it became "an inspiration", "a lever", for international change. Barraclough [6] places the stress on its structural and ideological implications, particularly in the viability of a new international economic order that would occasion the weakening of the West. Hodara, [7] however, thinks that the new energy situation contains various alternatives in so far as the future ordaining of international relations is concerned, which might involve different patterns of distribution of power and income. It does not seem justifiable to exaggerate either the strength of the new forces in ascent or the inflexibility of the supporters of the "old order".

Some authors have looked into the repercussions of the crisis upon the national economies. Others [8] put the accent on the tensions arising from the uncertainties of oil supply, and/or the abrupt rise in the price of oil and its by-products in industrially advanced countries; still others have pointed out the contradictory consequences for the exporting countries themselves. [9]

From another angle, attention has been devoted to the matter within a long-term perspective, linking it to statements about the physical limits to growth. Thus, for some the problem would not be limited to the financial or international domain; it would represent an unequivocal sign of a rapid process off depletion of resources and exhaustion of the patterns of development on which

[5] N. Girvan, "Economic Nationalism", *Daedalus*, Winter 1975.

[6] G. Barraclough, "The Haves and the Have Nots", *The New York Review of Books*, May 13, 1976.

[7] J. Hodara, "La coyuntura internacional: cuatro visiones", *Estudios Internacionales*, Buenos Aires, No. 31, July-September 1975.

[8] For example, T. Szulc, *The Energy Crisis*, New York, Franklin, Watt, Inc., 1974, and more precisely, A. Cockburn and J. Ridgeway, "Energy and the Politicians", *The New York Review of Books*, April 15, 1976. Events in 1973 also made the consumer countries take cognizance more rapidly of their limitations and blunders in the field of energy. Illustrative analyses of this matter are found in OECD, *Oil - The Present Situation and the Future Prospects*, Paris, 1973, and *A Time to Choose*, Final Report of the Energy Policy Project of the Ford Foundation, Ballinger, Mass., 1974.

[9] C. Andrés Pérez, the President of Venezuela, notes, for example, that "We find ourselves either at the first step of a high ascent... or on the edge of a precipice"... quoted by N. Gall, "The Challenge of Venezuelan Oil", *Foreign Policy*, 18, Spring 1975, p. 53.

industrial society is based.[10] For others it means, at most, the beginning of a new form of the international division of labor signifying not only opportunities for countries with raw materials,[11] but risks as well.

The purpose and limits of this paper are to be considered against this background. Our aim is to define the idea and context of the model of "instant industrialization" apparently valid for countries which today enjoy an unusual external prosperity as a result of the international marketing of oil. The analysis starts with an outline of the concept followed by a presentation of the main features which characterize the oil economies as a whole. The survey is illustrated by two empirical cases —Iran and Venezuela— which serve as a basis to consider the potentiality and limitations of this possibly new paradigm of industrial development.

II. *Instant industrialization: the concept*

The possibility of implementing a pattern of extremely rapid industrialization —on the rim of "instantaneous"[12]— in certain oil producing countries, implying the multisectorial accumulation of capital at a very fast pace, is very appealing for a number of reasons. The economic and sociological[13] literature has profusely discussed the external and internal impediments to industrialization that usually take the form of sharp disequilibria in the balance of payments, persistent deterioration of the terms of trade, saving-investment gaps, technological dependence and inelasticity in the supply of skilled man-power. These rigidities characterize the paradigm of industrial development in the low-income countries, thereby setting it apart from that which is applicable to the present developed nations.

[10] M. Mesarovic — E. Pestel, *Mankind at the Turning Point: The Second Report to the Clubof Rome*, New York, Dutton, 1975, Chap. VIII.

[11] For example, A. Ferrer: *Economía internacional contemporánea*, México, Fondo de Cultura Económica, 1976, Chapter III.

[12] This term is beginning to spread in the professional jargon. Cf., for example, D.M. Searby: "Doing Business in the Mideast: The Game is Rigged", *Harvard Business Review*, January-February 1976, p. 58.

[13] Cf., for example, H.J. Bruton, "The Two-gap Approach to Aid and Development: Comment", and H.G. Chenery "A Reply", in *American Economic Review*, LIX, 3, June 1969; also, more generally, R.B. Sutcliffe: *Industry and Underdevelopment*, London, Addison-Wesley, 1971, and the extensive bibliography cited therein.

The sudden removal of these limitations by means of an unexpected massive influx of oil earnings is not only of theoretical interest. It affects the style of industrialization in three main ways: the relaxed financing of the process, the rapid overcoming of secular institutional obstacles, and the substantial reduction of the social costs which are normally implied in industrialization. Otherwise stated, the considerable injection of external resources derived from the sale of oil at unprecedented prices would permit exporting countries endowed with certain factors and institutional experience —even though these have not yet extricated them from their state of underdevelopment— to achieve a sustained economic diversification that the dynamic impulses may begin to come forth from activities and intersectorial "non-oil" links. All this would result in an abrupt and qualitative increase in the levels of productivity.

This scheme of industrialization and development would be encased in a strategy of "skipping stages" which differs quite distinctly from the Stalinist or the "Rostovian" version.

In any case this is only one of the considerations which serve to enliven the interest in instant industrialization. Other considerations pertain to the particular temporary circumstances in which the idea attempts to acquire feasibility. By this we mean the international support that the scheme deserves on the part of countries that ordinarily represent divergent interests.

We have already suggested in the introduction that the massive transfer of resources takes place in a politically and ideologically loaded context.[14] The role of "Robin Hood" is assigned to the oil countries, and at the same time the financial and, in some cases, the military power which they can acquire in a relatively short time is fully appreciated.[15] Therefore, and this is the first element which we want to highlight, the initiatives that these countries take in the field of development are able to count *ex ante* on a vast amount of ideological legitimacy which emanates from the group of

[14] Darmstadter, Landsberg and Szulc, *op. cit.*, argue that the crisis in energy has been coming for a long time, that it would have occurred in any case. However, we believe that the timing of this crisis introduced a qualitative ingredient that would not have been present under other circumstances.

[15] The works of M.J. Williams, "The Aid Programs of the OPEC Countries", *Foreign Affairs*, January 1976, and Ch. Tugendhat: "Political Approach to the World Oil Problem", *Harvard Business Review*, January-February 1976, point to that twofold trend.

underdeveloped economies and fractions of the intellectual left in the advanced capitalist system. In this sense, it is appropriate to say that the OPEC is not just "a device to raise prices",[16] it has also succeeded in mobilizing sentiments which have their roots in the growing international gap.

But there is more. Aid comes, in addition, from the industrial countries themselves in the form of technical assistance, and even direct investment. In the short run, it is a form of contemporizing with the gains achieved by the producing countries and to make profitable use of the capital surplus which those countries produce; in the long run, it could mean a tactical expedient to disunite them.[17] Apart from these calculations, the oil economies should be able to receive, in any case, ample outside help which would facilitate the overcoming of administrative and technological restrictions. In this way, the decisions of the oil countries would take form in an especially favorable context wherein the ideological legitimacy which stems from the Third World is combined with the operative viability facilitated by the industrial bloc.

This situation would permit, on the other hand, the almost unlimited enjoyment of "the advantages of the latecomers": ample possibilities to absorb very recent innovations which, because of their preestablished rigidities, have still not penetrated in the developed economies themselves.[18]

In short, the model of instant industrialization would be based not only on the significant slackening of outside restrictions, a factor that in itself represents already a great advantage with reference to other underdeveloped countries which lack oil; in addition, it would thus rely on the ideological and technical backing of countries situated at dissimilar stages of development. Still more: thanks to the abundance of resources and the special international climate, governments can manipulate the material and psychological incomes so as to diminish resistance to change. Countries which went through alternative paths towards industrialization did not fare so well.

Having explained the idea and context of instant industriali-

[16] Here we concur with M. Grenon, *op. cit.*, p. 200. I. Mikdashi, "The OPEC Process", *Daedalus*, Winter, 1975, also shares this opinion.

[17] Tugendhat, *loc. cit.*, rationalizes, along these lines, the technical aid which the consumer countries ought to make available.

[18] Sutcliff, *op. cit.*, pp. 331, elaborates on this subject at the theoretical level.

zation, let us now characterize the features of two national economies where the pattern could be applied in principle.

III. *Venezuela and Iran: structural aspects and socio-economic evolution*

Some studies[19] on the long-run behavior of oil economies have clearly revealed their more significant traits, namely: dualism, the spatial imbalance, the inequitable distribution of income and opportunities, and external dependence.[20] Let it be said from the start that these traits are also present in other underdeveloped societies, but that in the oil producing ones they are sharper.

The dualism refers to the inter and intra-sectorial disparities which arise within these economies as a result of the insertion of a type of dynamic activity which is orientated abroad, but is capital-intensive in a traditional socio-economic context. This situation would tend to be perpetuated in time, in as much as the direct effects (through linkages between sectors) and the indirect (fiscal) effects of this activity are only to a limited extent disseminated throughout society by the mechanisms of employment and income. In this way tensions and acute discrepancies arise between the levels and rates of development of the various productive branches.

Dualism most assuredly does not imply an absolute structural dissociation. Linkages are thereby formed —more selectively than organically— as, for example, in the patterns of costs and consumption, in which the oil enclave wields a diffusing influence; but their true effects are limited, and sometimes even negative.

Secondly, one has to take note of the spatial imbalance, closely bound to the former. By this we mean the concentration trends of the product and the activity in the regions nearest to the oil wells and/or in those where the supply and support facilities are set up. Public expenditure —financed, to a great extent, by the revenue from oil— usually accentuates the phenomenon, by giving preferential attention to the social infrastructure of those regions.

[19] For example, UN-ECLA "The Development of the Venezuelan Economy in the Last Decade", *Economic Bulletin of Latin America*, Vol. V, I, March 1960, and J. Amuzegar - J. Ali Fekrat: *Iran - Economic Development under Dualistic Conditions*, University of Chicago Press, 1971.

[20] Of course there are important historical and cultural differences beween the oil economies; but in the framework of this analysis, they will not be emphasized.

Thus, clearly depressed areas arise alongside others covered by a "veil of fictitious prosperity".[21]

These societies further reveal signs of a regressive distribution of the income and basic services, particularly among the rural-agrarian and urban marginal sectors. At best a "mesocratic"[22] distributive profile appears which favors the first two deciles of the population; the rest is subject to various forms of relative and critical poverty.

Lastly, it is fitting to note the extreme sensitivity of these economies with respect to external fluctuations, particularly in the oil markets. The negative effects of this dependence are especially serious for three reasons: in the first place, because of the lack of an inner focus of dynamism which could compensate for the fluctuations in international trade; in the second place, because these economies show an unusual propensity to import reflecting the income and cost effects inherent in the enclave activity; and lastly, because the agricultural sector is weak, and can hardly cover the basic needs of the population.

Let us see how these traits[23] are manifested in Iran and Venezuela; emphasis will be placed on the sixties, although the judgments seem to be valid for the almost half-century of oil exploitation.

Different indicators reflect the importance of oil in the behavior of both economies.[24] In the period 1960-1970, the Venezuelan sales of oil represented approximately 91 percent of exports; the corresponding share for Iran was 89. The contribution of oil activity to the national product fluctuated between 23 percent in

[21] According to H. Malavé Mata, "Formación histórica del antidesarrollo en Venezuela", in *Venezuela - crecimiento sin desarrollo.* Mexico, Editorial Nuestro Tiempo, 1974, p. 197.

[22] Cf. J. Graciarena, *Tipos políticos de concentración del ingreso y estilos políticos en América Latina,* ECLA, Santiago de Chile, mimeographed, April 1976.

[23] They are not the only ones. Some authors have shown, for example, the existence of an "oil culture" which would make a Venezuelan appear like someone hungry for comfort and symbols whose prime concern is buying and consuming . . . E. Quintero, *Antropología del petróleo.* Mexico, Siglo XXI, 1972. p. 113. But we shall not include these aspects which are beyond the scope of this paper.

[24] The data are based on the sources indicated in footnote 19 and in ECLA, *Tendencias y estructuras de la economía de Venezuela en el último decenio* (E/CN. 12/930), July 7, 1972; Banco Central de Venezuela, *La economía venezolana en los últimos treinta años,* Caracas, 1971; OECD, *Report on the Economy of Iran,* Paris, July 1967; and United Nations, *Economic Survey of Asia and the Far East, 1973* E/CN, 11/L. 1157) Bangkok, 1974.

the first country and something less than 20 in the second. Exports were 63 and more than 50 percent, respectively, of the total tax revenues, and over 80 percent of direct foreign investments were in the oil industry and its by-products. Thus capital formation and the scope of government policy depend largely on foreign exchange from oil. It is à propos to add that the two countries combined were producing in that period approximately one fourth of the world supply; in the seventies Iran and Venezuela showed diverging trends in production.[25]

Oil exerts an influence in two additional spheres. On the one hand, by reducing budget deficits, it has softened the inflationary pressures (until 1973, they had scarcely registered 2% annually); on the other hand, it appeased the social unrest by facilitating the consensus and the cooptation of groups that were not in agreement.[26]

Having made these general remarks I shall proceed to illustrate empirically the four attributes already discussed.

It is mainly in the domain of productivity and employment that technological and economic dualism is reflected. In point of fact, the intersectorial relations of labor productivity indicate startling inequalities. Taking 100 to represent the average of the economy, agricultural productivity in Venezuela for 1969 was 25, productivity in industry and basic services was 152; and the index for oil and its by-products was 1 147. In Iran, the corresponding indices for 1967 were 48.3, 61.5, and 4 007.1. On the other hand, employment in oil activities barely constitutes 1.7 and 0.6% of the labor force of Venezuela and Iran, respectively; the relation tends to contract with time, due to displacements resulting from the introduction of capital intensive techniques and the ending of infrastructural investments (roads and pipelines). It should be borne in mind that both countries have a rate of population increase higher than 3.5% per year.

Spatial imbalance is reflected in the levels and rates of regional development. In both, income and output have been concentrated in urban zones or in those which are near the centers of extraction,

[25] Rising trends in Iran and decreasing trends in Venezuela. Cf. the table reproduced in *Daedalus*, Winter 1975, p. 288.

[26] With reference to this particular point, cf. the article cited of H. Malavé Mata; also M. Zonis: *The Political Elite of Iran*, Princeton University Press, 1971. Zonis designates "this consensus subsidized" by oil as "cooptation by seduction", *op. cit.*, p. 116.

refining and transportation of oil. And in spite of the fact that Venezuela and Iran initiated important agrarian reforms in the sixties,[27] the regional differential in terms of product, income and access to the basic services did not vary. Illiteracy —to which is added a marked ethnic— is a particularly serious problem in the rural areas of Iran; utilities such as electricity, housing and health show deficiencies in both countries. The situation has led some to affirm that "oil was sown", but that the seed was not scattered either widely enough or prudently.[28]

In addition, external vulnerability, instead of being mitigated with time, has become more intense. The industrialization by import substituting, its modest dynamism (industrial activity generated only 16% of total product in 1970, and 12% in 1964, in Venezuela and Iran, respectively),[29] and the pertinacious disregard for agricultural activity, all contributed to it.

Note should be taken of two additional elements in this situation. On the one hand, the scanty contribution of exports other than oil, occasioned by the high costs deriving from oil activities and, on the other hand, the considerably high rates of open unemployment, especially in the sixties when they actually reached 5.2 and 10.7% respectively, with their impact on purchasing power.

From this description it is possible to conclude that oil, after almost half a century of exploitation,[30] has not accomplished much to stimulate, either directly or indirectly, a sustained process of industrialization, or qualitative social changes that might leave their stamp of equity and long time viability on the national systems. "The oil industry has remained economically divorced from all other aspects of the economy";[31] still more, "in the ephemeral

[27] For Iran, cf. A. K. S. Lambton: *The Persian Land Reform: 1962-1966*, London, Oxford University Press, 1969; and for Venezuela, ECLA, *Tendencias y estructuras, op. cit.*

[28] ECLA, *El desarrollo de la economía venezolana, op. cit.*, p. 24.

[29] The Latin American average was 24.5. Cf. ECLA, *La industria latinoamericana en los años sesenta*, Cuaderno 8, Santiago de Chile, 1975, p. 17. As regards Iran, its degree of industrialization is considerably below that of other countries in Asia.

[30] In Iran it began in the first decade of the century; in Venezuela, in the twenties.

[31] J. Amuzegar - M. Ali Fekrat, *op. cit.*, p. 28.

periods of slackening of external restrictions, this has not succeeded in developing abilities to handle adverse situations".[32]

But some qualifications are due. Overall activity in both economies showed signs of dynamism (national product increased in the sixties at 6 to 8%); projects and programs in the social and agrarian field were put into operation, and the State reaffirmed its commitment with regard to national development by means of the institutional expansion of its functions and the launching of development plans which helped to define the problems of the country, to set priorities and to accumulate administrative experience.

The thesis that sustains that it is possible —under the new circumstances— to accelerate industrial development is based precisely on these advances. Both countries have today an infrastructure and a leadership (which were completely lacking or weak in the past) adequate to make use of the significant influx of resources and technical assistance in an ideologically and politically favorable international context. This type of statement could indeed find support in the recent behaviour (1973-1976) of both economies. Following are some remarks that seem to favour this view.

IV. *The basis of instant industrialization*

Since 1973, Iran and Venezuela have been receiving revenues from oil on an unprecedented scale. In 1974, for example, they amounted to 28 000 million dollars (17 400 million for Iran and 10 600 for Venezuela),[33] that is, approximately one third of the total receipts of OPEC members. In relation to 1970, the increase was almost 8 times for Venezuela, and 15 for Iran. The external prosperity rapidly translated into a significant increase in product as compared with the historical rate (4.5 and 30.3% in 1974, and 6.6 and 17 in 1975). In general, all the macroeconomic variables —including the balance of payments— are clearly affected in a positive manner.

On the other hand, various projects directed towards accelerat-

[32] ECLA, *Economic Survey of Latin America, 1973* (E/CN. 12/974/Rev. 1), New York, 1974, p. 99.

[33] According to the table attached to the issue of *Daedalus*, Winter 1975, p. 288. Other estimates show the value of Venezuelan exports, in 1974, as 14 669 million, declining in the following year to 10 530. Cf. ECLA, *Annual Economic Survey, Notes on Venezuela* (First draft), Santiago de Chile, April 1976.

ing capital formation have received unusual stimulation. Iran, for example, is embarking on a quinquennial investment program for 69 000 million dollars, including the establishment of iron and steel complexes, tractor and automobile industries, expansion of ports and the construction of naval bases.[34] Its government plans "constructing a Great Civilization, an ideal society", based on the oil resources wisely administered.[35] Venezuela, in turn, is vigorously following policies of diversification, which had, without visible results, constituted a part of its strategy of development. The establishment of Petróleos de Venezuela (PETROVEN), the public control of 19 foreign enterprises since January 1976, and the intensification of the search for new sources of oil in the Orinoco, the continental platform and the Gulf of Venezuela, are all steps directed to strengthening the exploitation of hydrocarbons for national purposes. To keep in step with these efforts, the government is embarking on an ambitious investment program in the basic industries (aluminum, steel and petrochemicals) to derive the greatest gain from its supply of cheap energy. In addition, it intends to set up bases for the construction of tankers and fishing vessels. To overcome the restrictions on the side of available qualified labor, the national authorities are launching a vast program ("The Grand Marshal of Ayacucho") of accelerated training of technical personnel in branches and activities in which investments are to be made.

But perhaps of greater importance than these massive injections of resources in different spheres is the qualitative change already beginning to emerge in governmental action. This deals with the initiatives in the field of agrarian reform, education and social services that intend, in part, to strengthen the results of the policies undertaken by both countries in the sixties; but which also constitute a substantial change of direction with regard to the degrees of commitment of the State to development. The latitude of the former is widened to accelerate capital formation and reduce the resistance and limitations of a structural nature as well.

Thus, Iran, for example, is reformulating its Fourth Development Plan, taking into account the constantly increasing revenues

[34] With reference to this point, cf. the list of projects presented by D.M. Searby, *loc. cit.*, and the article by H. Vicker: "Running Dry", *The Wall Street Journal*, May 5, 1976, p. 1.

[35] According to E. Pace; "How the big nations", *op. cit.*

from oil, and the easier credit position it enjoys in the international financial markets;[36] now Sate activities have a considerably greater scope, from the educational to the military fields. Venezuela, in turn, even though it is adopting policies somewhat more conservative in matters of oil production and foreign indebtedness, diversifies the institutional attainments of government action through the Venezuelan Investment Fund (FIV), the Credit Fund for Farming and Livestock Raising, and the Fund for Industrial Credit. An indicator of this active attitude with regard to development is the high number (995) of industrial projects which were initiated in 1975, at a cost of almost 2 000 million dollars.[37]

The change in direction in the economic and institutional behavior of both countries depends not only upon external prosperity; it also has its roots and is defined in terms of an economic nationalism richly nourished by the confrontation of the oil countries with the consumers and by the particular repercussion it has had on the periphery of the capitalistic system. The ideological impetus legitimates considerably the new attitudes of the State, especially when in both cases it is possible to count on aid, although limited, from the private sector.

In this way the past difficulties could be overcome by means of a fortunate convergence of circumstances: the massive influx of external resources; the greater scope of governmental functions and activities; and the emotional and ideological impulses of economic nationalism.

But this is only one side of the coin. There is another, less glittering side.

V. *Obstacles to instant industrialization*

The circumstances noted in the previous section seem to support the view that Iran and Venezuela are on the road to attain a sustained progress, without incurring the internal costs (forced mobilization of savings, institutional coercions), and external costs (segregation and hostilities) which other countries experienced when they undertook alternative paths towards industrialization. But this

[36] It seems that Iran relies not only on current revenues from the oil industry in order to accelerate its economic progress, but also on its international credit Cf. *The International Herald Tribune*, Paris, May 11, 1976, p. 1.

[37] Data from ECLA, *Annual Economic Survey—Venezuela* (draft), Santiago, April 1976.

optimistic vision can also, in the long run, prove to be premature and superficial. Further evaluations will be made precisely along these lines, dividing them in three categories: the current indicators, the structural limitations and the adverse trends in the oil markets. It is needless to explain that these statements do not intend to deny the validity and the prospects of success of a strategy of extremely rapid industrialization; they rather imply a plain call for caution.

We shall comment upon three of the indicators which can deter the rate of advancement towards accelerated development. Inflation is in first place. In both countries, prices have risen significantly, between 14 and 22% in 1974;[38] more recently, prices tend to either stabilize or increase. This phenomenon presents an ostensible contrast with the historic trends (barely 2% annually in the 1950-1970 period). It is obvious that the foreign exchange channelled towards the central government may lead to excessive liquidity and expansion of domestic demand when effective mechanisms of sterilization are not simultaneously put into effect. Although imports and investment abroad help to mitigate the overheating of the economy, nevertheless a good part of the demand created by public expenditure puts pressure on prices since it is impossible to overcome in the short run the traditional rigidities of supply, especially in the agricultural sector. Both countries have taken steps of a different nature to control the inflationary tensions and at the same time they have subsidized prices of basic foods. Despite all these efforts, the problem as such still continues, strongly accentuated by the inflationary tendencies in the industrial centers, which are filtered through commerce and investment.

The spurious increase in imports is also a matter of concern. Iran and Venezuela, with their two-fold design of sterilizing the impact of the enlarged money supply and diversifying their external interests, have made significant investments abroad, including financial aid to other developing countries.[39] Imports of

[38] According to United Nations, *Annual Economic Survey, 1974* (ST/ESA/26), New York, 1975, p. 139.

[39] In general, it can be stated that the aid from members of the OPEC is more than ten to fifteen times as much as that from the industrial countries, according to *Venezuela, Now*, Vol. 1, 13, January 30, 1976. The effective transfers were 709 million dollars by Iran and 465 by Venezuela, in 1875. Cf. M. J. Williams, "The Aid Programs of the OPEC Countries", *Foreign Affairs*, January 1976, vol. 54, 2, p. 320.

capital goods were also considerably increased in order to sustain industrialization. However, there are indications that the "spurious" fraction (luxury expenditures) in purchases is not insignificant. According to some observers it would have a great deal of weight,[40] and would be founded on cultural propensities that are difficult to modify, at least in the short run.[41]

A third current component refers to the drop in the aggregate surplus due to a number of different factors: lower consumption in the industrialized economies, increase in the price of imports, and the fall in output (in the case of Venezuela). Reduction in the net inflow certainly produces tensions and uncertainty in investment plans. In Venezuela, for example, it has already adversely affected the actions planned by the Venezuelan Fund for Investments (FIV);[42] in Iran it takes the form of a propensity to request external loans and to urge a new rise in the price of oil.

It could be argued that these three adverse indicators will have limited effects upon economic policy in both countries, and that they can be offset before too long. It so happens, however, that there are structural problems which instant industrialization still has to solve.

In the first place unemployment and underemployment. In both countries, population growth is rapid (above 3% per year), which implies significant pressure —not backed by productive contributions— on the basic services and employment opportunities. And in both there are indications that the increased investment in energy-intensive and capital-intensive fields will hardly translate into a substantial increase in labor force demand; on the contrary, partial data indicate that the rates of unemployment are noticeably high, especially in the less skilled strata. This trend would induce a regressive distribution of income and a contraction of the domestic market, which can hardly be hidden by generous measures of subsidy to basic foods.

On the other hand, the problem of the rising expectations of different sectors of the population is emerging. In a situation in which the financial limitations seem to evaporate and, at the same time, speculative accumulations of income and wealth become

[40] For example, P. Knight, "Crisis in Confidence?", originally in *The Times* (London), and reproduced in *Excelsior* (Mexico), April 11, 1976.

[41] In this connection, cf. the article in *Time* on Iran, May 10, 1976.

[42] Contributions to the Fund decreased from 3 000 million dollars in 1974, to 1 800 million in 1975. In 1976, an even smaller appropriation is expected.

apparent, the disadvantaged sectors will tend to make their social dissatisfaction evident through whatever means are available in each political system. This feeling of relative deprivation —if it persists without change— will raise an element of doubt as to the validity and stability of the development model, although the aggregate income level is higher than before. Recent events (demonstrations in Venezuela to protest against the excessive rise in prices, and frustrated acts of terrorism in Iran) would reflect this social and political unrest.

The rising dependence of economic activity upon State action also merits due consideration at this point. This relates to the counterpart of the vigorous governmental intervention which we have already remarked upon. Both cases represent economic regimes which, because they constitute a part of the capitalist system, encourage liberal policies which combine State enterprise with that of the private sector. In the long run, however, the scheme can become an inefficient bureaucratic centralization mainly sustained by the oil income and by traditional cultural configurations.[43]

The third type of consideration that weakens the basis of instant industrialization pertains to the trends that have already appeared in the oil markets.

We have already seen that one of the basic premises of the whole scheme is the sustained flux —and better still, an increasing one— of external revenues. But we distinguish four points which question the validity of this premise. The first pertains to the existence of reserves. These, most assuredly, do not constitute a fixed stock; they increase or decrease according to the rates of production and the search for new sources. However, they are limited. According to estimates, the reserves of Venezuela equal 11 to 13 years; Iran would have twice as much.[44] These are smaller magnitudes than those of Saudi Arabia. The basic question is: will the cycle of industrial accumulation and productive diversification run par-

[43] In this connection, cf. M. Zonis, *The Political Elite of Iran, op. cit.*, and D. Behnam, *Cultural Policy of Iran*, UNESCO, Paris, 1973. For Venezuela: H. Malavé Mata, *Formación histórica del antidesarrollo en Venezuela, op. cit.*; F. David Levy, *La planificación económica en Venezuela*, Comisión Nacional del Cuatricentenario de la Fundación de Caracas, 1968, and L. Lander - M. Josefina de Rangel, *La planificación en Venezuela*, Sociedad Venezolana de Planificación, Caracas, 1970.

[44] According to estimates in *Wall Street Journal*, May 6, 1976, p. 1.

allel to the decrease in the reserves? Or will a lack of synchronization between them arise?

To give a definite reply is far from simple. Before reserves are exhausted, industrialization might overcome the limitations which we have been pointing out in this section, or it could happen that reserves may be considerably increased by means of new investments. In any event, it is a disturbing unknown quantity.

Perhaps more important than the question of the reserves is actually the possibility of a sudden and not deliberate decrease of production levels in both countries due to a number of diverse factors. One has already been mentioned: the reduction in consumption in the large industrialized economies, a trend that now continues for the second consecutive year;[45] the other refers to the exploitation of new sources, a fact that has already become apparent[46] and which breaks down one of the prerequisites of control practiced today on the market by the members of OPEC;[47] the third points to the structural mutation of the energy sources to the detriment of oil, as demonstrated by the abundant literature on the subject.[48]

It could be argued that this foreseen decrease, in terms of *quanta,* is not necessarily decisive; the maintenance of high prices takes precedence over that. But the objection is not valid. First of all, because the enlargement of supply and the substitution of energy sources will influence prices; and secondly, because the negotiating ability of OPEC countries depends upon a delicate balance of factors that may be relatively easily upset in the future. Let us take a look at some of the reasons which would lead to this prospect.

OPEC is assuredly not a homogeneous group; members are distinguished by different resource endowments; by diverging attitudes towards development; by geopolitical location, and by institutional regimes.[49] Will it be possible to maintain unity in spite

[45] Cf. the article cited in *Wall Street Journal.*

[46] According to P. Odell: *Oil and the World Power, op. cit.,* pp. 220 *ss.* Cf. also Choan-Lo-Park - J. Alan Cohen: "The Politics of the Oil Weapon", *Foreign Policy, 20, Winter, 1975.*

[47] Cf. I. Smart, "Uniqueness and Generality", *Daedalus,* Winter, 1975.

[48] In U. Lantzke, "The OECD and its International Energy Agency", *Daedalus,* Winter, 1975.

[49] These factors are recognized by the most ardent advocates of OPEC. Cf. the interview of P. Pean with A.L. Khene in *L'Express,* Paris, January 8, 1975, and N. Girvan, *Economic Nationalism, op. cit.*

of these differences and the various pressures which the consumer nations may be able to exert? It is difficult to assure it. Past experience and the rigidities which even today are perceivable within these economies, as well as in the communication between them, do not allow us to be optimistic in this regard. In any case, changes already foreseen in the geography of hydrocarbon supply and in the prices will undoubtedly present a formidable challenge to the OPEC.[50]

A fourth element which must be given due consideration in this context pertains to the military aspects. On the one hand, military expenditure has increased tremendously in both countries compared to its amount in the past; this could generate unstabilizing inclinations that might take the form either of external conflicts or internal coups. Historical experience could support both possibilities. On the other hand, one must consider the subject of military intervention on the part of some industrialized nation or bloc of nations either with the limited intent of regaining lost power or within the framework of a generalized struggle for scarce resources. This matter has been widely discussed and should not be forgotten.

VI. *Recapitulation*

Let us tie together the threads of the above analysis: current restrictions resulting in sudden price changes, spurious imports and a shrinking aggregate surplus; fundamental factors such as unemployment, social unrest, and the disproportionate rise of a state technobureaucracy; uncertainties gravitating in the oil market such as quantitative and qualitative mutations in supply, the eventual weakening of OPEC and the unforeseen impacts of a constantly increased military expenditure. A scenario emerges which limits, in our opinion, the feasibility of instant industrialization.

However, it does not deny it. We have seen that Iran and Venezuela present favorable conditions for accelerating considerably the rate of industrialization, conditions which are not limited to the intensive injection of external resources. The signs of prosperity are also ideologic and emotional, in such a way that they strengthen the institutional means which prevail in both

[50] Intimations along these lines are to be found in J. Damstadter - H. Landberg, *The Economic Background, op. cit.*

countries. Finally, it would be a matter of taking an especially efficacious advantage of the interdependencies which have been created by the contemporary industrial system[51] to pave the way for a new version of the paradigm of industrial development. Whether the circumstances noted shall bring about contradictory or openly negative effects is, at best, an open question.

[51] The negative and positive effects of the interdependencies have recently been investigated by K. J. Holsti to determine how far self-segregation from the international stage is therein involved. However, there were no empiric explicit references presented for these matters. See "Underdevelopment and the 'gap' theory of international conflict", *The American Political Science Review*, LXIX, September 3, 1975. Reference is also made by G. Barraclough, "The Haves and the Have Nots", *The New York Review of Books*, May 13, 1976.

Oil, the Super-Powers and the Middle East

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Within the scope of public debate, it is a commonplace that the Middle East is an area of frequently violent international conflict, where the level of violence is subject to sudden and considerable elevation. It is a second commonplace that the two super-powers —the United States and the Soviet Union— have significant, and sometimes divergent, interests and influence in the Middle East, substantial enough respectively to encourage and support their involvement in Middle Eastern conflicts. It is a third commonplace that, as major industrial states, both super-powers, and especially the United States, must be concerned with trends in an international energy market which is itself decisively affected by the volume and price of oil exported from the Middle East and North Africa.

One is tempted to conclude immediately that three such commonplaces, linked by a common geographical focus, must be connected also by factors of causation and effect: in other words, to assume that they can be used as interdependent variables in some set of equations. Such an equation might, for example, demonstrate that the restriction of Arab oil exports in 1973-74 or the dramatic rise in oil prices during the same period (or both) affected the interests and relative influence of the two super-powers in ways which caused them to adopt policies whose implementation altered in turn the probability or form of violent conflict within the Middle East. An equation of that kind, if expressed in sufficient detail and substantiated by evidence, might well have political, as well as analytical, utility. It is not, however, axiomatic that such an equation can properly be constructed on the basis of the preceding assumption. In the first place, statements may be commonplace without being true. In the second place, even if they are both true and connected by circumstance, it cannot be assumed that they are also, therefore, causally connected.

The historical prevalence of political and military conflict between and within Middle Eastern states hardly needs to be proved.

The second commonplace is more questionable, however platitudinous it may appear. Soviet and United States interests in the Middle East are evident enough, even if they may frequently have been misunderstood. Influence is another matter. Despite the widespread advertisement over twenty years of their respective links with a list of 'client states' in the region, neither super-power has been notably or consistently successful in manipulating Middle Eastern politics or Middle Eastern conflicts to its own advantage. Indeed, as I have argued elsewhere, they have shared, especially since 1967, the predicament of having responsibility without control.[1]

The third of the commonplaces must also be open to question, on at least two grounds. First, it must be recalled that the United States and the Soviet Union, in addition to being two of the largest industrial economies, are also the two largest oil producing states in the world; whatever their dependence, if any, on imported oil, they can never be so vulnerable to its supply or price as the industrial states of continental Western Europe or Japan.[2] Second, the current dependence of the two super-powers on imported oil differs enormously: the Soviet Union is fully self-sufficient, whereas the United States, in 1975, relied upon imports for almost 38 per cent of its supplies.[3] Questions derived from these comments need not, of course, invalidate the commonplace as a whole; marginal dependence may be economically critical, while the impact of world prices for Middle Eastern oil may be important even to a country such as the Soviet Union which is not called upon to pay them itself. Nevertheless, the comments are to be borne in mind, not least because of their implication that, whatever else they may share, the super-powers do not share a similar attitude or sensitivity to the world market for Middle Eastern oil.

Having raised such questions about the influence and interests of the super-powers in the Middle East and its oil, it becomes appropriate to examine them in more detail. In doing so, it will be possible to address also the more general question about the

[1] "The Super-Powers and the Middle East", *The World Today*, 30.1 (January 1974), pp. 4-15.

[2] In 1975, the U.S. produced 473 million tons (mt) of oil (including natural gas liquids) and the U.S.S.R. 485 mt, compared with Saudi Arabian production of 357 mt. (*BP Statistical Review of the World Oil Industry 1975*).

[3] Out of a total consumption of 764 mt in 1975, the U.S. had net imports of 203 mt of crude oil and 87 mt of oil products. (*BP Statistical Review of the World Oil Industry 1975*).

existence of causal relationships between Middle Eastern conflict, super-power influence, and the case of oil. The necessary evidence should, after all, be available in recent history, and especially in the events of the last three or four years. By considering those events, it should be possible to identify the causal links, if any, which have operated.

The central question to which all this must be directed is, of course, the one that underlies the title of this paper. What effects, if any, have the dramatic events in the world oil market since 1973 had upon conflicts in the Middle East or upon the attitudes of the super-powers to those conflicts? To that, there must eventually be joined a further question about potential effects in a foreseeable future. The point of the preceding circumlocution is to draw attention, by implication, to some of the reasons why those questions are far from simple.

We all share a general awareness that the international oil market —indeed the world's energy economy— has undergone an enormous change since 1973, and that the primary motor of that change has been located in the Middle East. We are also generally aware that much has happened during the same period within the context of Middle Eastern conflict and the super-powers' involvement therein. We are naturally inclined to look to the former category of events for explanations of phenomena in the latter. We are further inclined to extrapolate from our sometimes superficial impressions of recent experience a number of far-reaching judgements about the influence of Middle Eastern oil upon Middle Eastern conflict in the future. One object of this paper will, however, be to argue that the impact of the oil factor on the Middle Eastern policies of regional and external powers has possibly been more uneven and, in some respects, less powerful than superficial impressions might indicate. Another object will be to suggest that the future interaction between those two contexts will not only be similarly heterogeneous but may also display features which differ markedly from those readily extrapolated from past experience or current impressions.

A major problem in analysing policies and events in or associated with the Middle East since 1973 is that of distinguishing between the effects of qualitatively distinct factors which have coincided in time. Indeed, the 'oil factor' is itself a misnomer, in that the term, as used hitherto, embraces at least three separate processes, each with its own economic and political significance. In the first

place, it is to be remembered (although it is now often forgotten) that a so-called 'energy crisis' was widely advertised and widely feared well before October 1973, especially amongst those who argued *inter alia* that the world's resources of hydrocarbon fuels were being depleted at a dangerously accelerating rate, and that one result was bound to be the concession of progressively greater international power to those Middle Eastern states which controlled so much of the remaining reserves of oil.[4] In the second place, there is the traumatic episode of the 1973-74 'embargo': the politically-motivated restriction of oil production and export to particular countries, including the United States, by some (but not all) of the members of the Organisation of Arab Petroleum Exporting Countries (OAPEC).[5] In the third place, there is the enormous increase in the world price of oil imposed, in a series of steps since 1970, and especially since October 1973, not by Arab producers alone but by the wider Organisation of Petroleum Exporting Countries (OPEC), largely, it should be added, at the instigation of two of its non-Arab members (Iran and Venezuela). Even if these three dimensions of the 'oil factor' are not unconnected, it would be naive to suppose that they are merely facets of a single phenomenon or to ignore the extent to which they have had distinct effects upon Middle Eastern affairs, on the one hand, or the super-powers, on the other.

It would also be naive to ignore the significance of two other series of events which have nothing directly to do with oil at all. One is that long sequence of contacts, explorations, negotiations and agreements between the two super-powers themselves, stretching back into the 1950s, which goes by the name of *'détente'*. The other is the much shorter sequence, confined within no more than three weeks, which constituted the October 1973 war between Israel, Egypt and Syria. Had oil never existed, or had none of it been contained within the Middle East, it is certain that each of those processes, the long and the short, would have had a considerable effect upon the pattern of inter-state conflict in the Middle

[4] See, for example, Walter J. Levy, "Oil Power", *Foreign Affairs*, 49.4 (July 1971), pp 652-668, and James E. Akins "The Oil Crisis: This Time the Wolf is Here", *Foreign Affairs* 51.3 (April 1973) pp 462-590.

[5] Iraq refused to join its OAPEC partners in restricting production and export, and, indeed, increased its own production significantly, during the term of the 'embargo' and since (from 72 mt in 1972 to 99 mt in 1973, 97 mt in 1974 and 109 mt in 1975).

East and upon the related policies of the United States and the Soviet Union. Just as it is sometimes difficult, in looking at Middle Eastern politics or super-power policies, to decide which dimension of the tripartite 'oil factor' has predominated in a particular case, so it is often difficult (and sometimes impossible) to judge whether super-power *détente* and/or the October 1973 war would still have created a particular effect without the intervention of the 'oil factor' in any of its forms.

The evolution of international conflict in the Middle East since 1973 has been largely, although not exclusively, linked to the apparently secular dispute between Arab states and Israel. The detailed story of the 1973 Arab-Israeli war and of its aftermath need not be set out here. Nor need the details of those intricate and sometimes confusing chapters in which the United States and the Soviet Union were seen to vie with each other in supporting the antagonists in war while simultaneously co-operating actively in bringing that war to an end. What does need to be pointed out is the patent or putative part played, in any of its forms, by the 'oil factor'.

There seems to be no reason for suggesting that the 'oil factor' made any *direct* contribution to the initiation or the military outcome of the 1973 war. Although Israel, Egypt and Syria all produce limited quantities of oil, and although one result of the 1967 Arab-Israel war had been to leave some of Egypt's most productive oil fields (in the Abu Rudeis area) in Israeli hands, competition for access to oil reserves in the ground has never played any significant role in the conflict between Israel and its neighbours.

That is not quite the same as saying that the issue of oil supplies has not figured in the conflict. Egypt's closure of the Suez Canal to Israel's shipping in and since 1948 had complicated the task of supplying crude oil to the refinery at Haifa, as, of course, had the parallel closure, by Jordan and Iraq, of the pipeline which had fed that refinery before 1948. More seriously, Egypt's blockade of the Straits of Tiran in 1967, which did so much to provoke the immediately subsequent war, threatened the vital traffic of tankers bringing oil, principally from Iran, to Israel's southern port at Eilat. The fact remains that neither oil reserves nor oil supplies were directly of more than marginal importance to the 1973 war itself.

A more interesting question is whether the issue of oil may have had a less obvious and more indirect relevance to the 1973 war—or,

at least, to the timing of the Egyptian and Syrian attacks with which it began. Two possibilities suggest themselves. The first is that the leaders of Egypt and Syria may have been encouraged to take the offensive against Israel by the conviction that, in 1973, those other Arab states, in the Gulf and North Africa, which produced so much of the world's oil were both more able and more willing than in 1967 to use oil as a political weapon in support of their own military endeavours. The second possibility is that a different and more subtle consideration, especially for Egypt, was that, unless determined military action against Israel were taken quickly, political leadership within the Arab world would pass irrevocably from the major actors on the 'armed struggle' stage, in Cairo and Damascus, to the major actors on the oil stage, in Tripoli, Baghdad and Riyadh.

There is some evidence to support the former possibility. In particular, the attitude of Saudi Arabia, which was clearly critical to any concerted use of the Arab 'oil weapon', appeared to have changed considerably since 1967. Whether because King Feisal's well-known anxiety to pray again in Jerusalem was growing with the advancing years or because he and his ministers were increasingly aware of their vulnerability to criticism or attack by more radical Arab states or forces if they held back, the Saudi Government had progressively become more openly exigent, especially of the United States, in pressing for Israel's total withdrawal from territory occupied in 1967.

The changing Saudi attitude is well documented. Speaking publicly in Washington in October 1972, the Saudi Minister of Petroleum, Sheikh Ahmed Zeki al-Yamani, had proposed a long-term bilateral agreement between Saudi Arabia and the United States, offering the latter an assured supply of Saudi oil in return for the exemption of that oil from quota restrictions and tariffs and the facilitation of direct Saudi investment in the United States, especially in the 'downstream' sectors of the oil industry. No policy 'strings' were directly attached. In April 1973, however, Sheikh Yamani, speaking again in Washington, openly linked his country's willingness to meet projections of the 1985 oil demand to the abandonment of the United States' policy of allegedly consistent support for Israel. Then, in August 1973, immediately after President Sadat of Egypt had secretly visited Riyadh, Saudi Arabia announced limitations on oil production growth, following this at once by repeating the warning to the United States that it would be difficult to satisfy the American demand for Arab oil unless

there were substantial modification of United States policy in the Middle East. Finally, most bluntly of all, King Feisal himself, through the medium of American television on 31 August 1973, openly threatened to use his 'oil weapon' against the United States unless 'complete support of Zionism' were abandoned.

It was hardly surprising if all of this persuaded the leaders of Egypt and Syria that they could at last rely upon the 'oil weapon', wielded by other Arabs, to be used in an effort to separate Israel from its Western friends in a new war. Nor were these expectations disappointed. On 17 October 1973, ten days after the new war began, OAPEC voted to impose progressively more drastic production cuts until Israel withdrew to the 1967 borders. During the next two weeks, the majority of OAPEC members imposed a complete embargo on supplies of oil to either the United States or the Netherlands. Further decisions on production cuts followed in November. All in all, the encouragement to military action which Egypt and Syria may well have drawn from the brandishing of the 'oil weapon' by Saudi Arabia and others before October 1973 seemed to be well justified.

Evidence in support of the second of the possibilities mentioned earlier is necessarily more difficult to find. Even if Egyptian or Syrian leaders were indeed afraid that their political prestige might slip away to other Arab rules unless they acted swiftly against Israel, they could hardly be expected to advertise the fact. Nevertheless, such alarm would not have been unfounded. President Qaddafi of Libya, for example, had already gained in stature within the Arab world through his country's militant leadership in the struggle by OPEC (and OAPEC) members since 1970 to obtain a higher economic return from oil exports and a larger share of control over oil production itself —a militancy which culminated in the Libyan seizure of American oil company assets and installations in August 1973. He had also acquired credit, as well as some odium, by his well-publicised financial support of Palestinian 'freedom fighters', of other radical groups in the Arab world, and of selected states and rulers farther south (such as President Amin of Uganda). Finally, and most directly, he had presented an open challenge to the Egyptian Government by his abrasive advocacy of a Libyan-Egyptian union, by his financial support for dissident groups within Egypt and, in July 1973, by his action in launching a 'union' march by 40,000 Libyans across the Egyptian border, further dramatised by his own rapidly withdrawn resignation. None

of this would have been either possible or credible had Libya not been in a position to exploit its oil and the income from its production.

Libya, however, despite its President's phrenetic activity, did not mark the direction from which the most serious challenges were arguably emerging to the status of Egypt or Syria within the Arab world. The capitals which seemed, in their control of massive oil resources, to present the real challenge were Riyadh and Baghdad, rather than Tripoli. The Iraqi challenge was admittedly potential, rather than actual, in that it was based on the expected existence of very large oil reserves, rather than on current oil production. Despite that, it was naturally of particular interest to Syria, given proximity, a history of strained inter-state relations and a frequently vicious enmity between the Ba'athist groups in power in the two countries. Saudi Arabia, however, represented the more immediately obvious challenge. Although other Arab oil exporters such as Kuwait had adopted similar policies, Saudi Arabia had progressively established itself as the most important paymaster of the Arab world: by making loans for general economic purposes, but especially by advancing money to Egypt, Jordan and others to finance their post-1967 purchases of foreign military equipment. With that role of paymaster, there went obvious and considerable prestige, as well as political influence – even if the role itself was assumed, in part, to protect Saudi leaders from political attack. More importantly, the very steps taken by Saudi Arabia in 1972-73 to prepare for the use of the 'oil weapon', which served, on the one hand, to encourage Egyptian and Syrian military attack served also, on the other hand, to remind Arabs, as well as the West, that it was King Feisal, rather than President Sadat or anyone else, who now had the power to move the wheels of Arab politics, to set the scene and the terms for action against Israel, and to deal from a position of strength with the United States itself. The Saudi 'oil weapon, was seen, as it emerged from its scabbard, to be an Arab sword with two edges. If one threatened to slice into the economic prosperity of the United States and its allies, the other seemed poised to cut down, in the same stroke, the political status of Egypt and its like. The Egyptian and Syrian attack on Israel in October 1973 might reasonably have seemed, in these circumstances, to have been a necessary exercise in pre-emption on two fronts: the military front of the Suez Canal and the Golan Heights, and the political front of relative status in the Arab world.

If oil represented, in any sense, a direct issue in the October 1973 war, its significance in that role was trivial. If, indirectly, it encouraged —or even impelled— the military attack by Egypt and Syria, the extent to which it did so may never be provable. What many have seen as both substantial and self-evident, however, is the part played by the factor of oil in bringing the war to an end and in promoting subsequent steps towards the military disengagement of the combatants. The 'oil weapon' was unsheathed and turned against the West. The impact of supply restrictions was enormously enhanced by the multiplication of prices. Thereafter, it is argued, the United States, threatened with real damage to its energy economy and with far more serious damage to the economies of its major allies, hastened to bring unprecedented pressure on Israel to accept a cease-fire and, thereafter, to accept progressively more extensive adjustments of the demarcation lines between its forces and those of Egypt and Syria.

The case, in approximately those terms, has been widely espoused — as has the general conclusion that the events of October 1973 and since, by demonstrating the vulnerability of the United States and the West to the 'oil weapon', have revealed the possession by Arab states of an instrument potentially capable over time of forcing one super-power, in effective collaboration with the other, to impose on Israel a settlement acceptable to its adversaries. But is the case or the conclusion a persuasive one?

Circumstantial supporting evidence certainly exists, especially in the declarations made by Western governments and their spokesmen in and after October 1973. The European Community countries and Japan, depending on the Middle East and North Africa for some 80 per cent of their oil supplies, were predictably swift in conforming, at least rhetorically, to Arab pressure: the Community by its public demand that Israel withdraw to the 1967 borders and recognize Palestinian rights (6 November), and Japan by its strongly pro-Arab statement on the territorial issue (22 November) and its subsequent haste to contribute most generously to Palestinian relief works and the economic rehabilitation of Egypt. The United States, drawing only some 8 per cent of its oil supplies directly from the Arab countries, was naturally less subservient.[6]

[6] Although in 1972 oil imports from the Middle East and North Africa (including Iran) represented only 4.4 per cent of U.S. oil consumption, equivalent to 2 per cent of U.S. energy consumption, the proportion rose sharply in the first nine

On occasion, however, it was a good deal more abrasive, and even belligerent, in its reactions.

President Nixon's request to Congress, two days after the Arab oil 'embargo' was announced, for massive new military aid for Israel was certainly regarded by the Saudi Arabian and other Arab governments as abrasive, as was his Secretary of State's proposal, in December 1973, that the industrialized oil-importing countries should establish a new consumers' bloc, the Energy Action Group, to concert their policies.[7] As to belligerence, the United States Secretary of Defense referred openly, in January 1974, to the possibility of military action being taken against oil-exporting states if their policies threatened to 'cripple' the industrial world (a studiedly imprecise threat, which attracted rather more attention when Dr. Kissinger repeated it in January 1975, substituting the idea of 'strangulation' for that of 'crippling'). And two days later, on 8 January, Vice-President (subsequently President) Ford added a new dimension, by hinting broadly that those oil-exporting countries which sought to exploit American dependence on their oil would do well to remember how dependent they were on American agricultural exports for their own food.[8]

On this evidence, there can be no doubt about the sensitivity of the United States and its closest allies to the 'oil weapon'. Nor is it in dispute that, from the middle of October 1973, the United States began to bring strong pressure on Israel, first to cease fighting and withdraw from the western bank of the Suez Canal and later to withdraw also from some of the territories it had conquered in 1967. What is not clear is the extent to which pressure on Israel was prompted by the effects of the 'oil weapon'.

Use of the Arab 'oil weapon' was directly linked, from the outset, to the current war against Israel and to the alleged responsibility of the United States for that war. The OAPEC resolution of 17 October 1973 made that clear. 'Considering', it said, 'that the

months of 1973. The estimate that U.S. imports from Arab states alone in June-October 1973 equalled 8 per cent of oil consumption is from Joel Darmstadter and Hans H. Landsberg 'The Economic Background' in *The Oil Crisis In perspective (Daedalus,* 104.4, Fall 1975), p. 22, where it is also estimated that an additional 2 per cent of U.S. oil supplies in that period came indirectly from OAPEC countries.

[7] The President's requests for $ 2.2 billions of military aid for Israel was submitted to Congress on 19 October 1973. Dr. Kissinger's proposal of an Energy Action Group was made publicly in London on 12 December 1973.

[8] Speech to the Manufacturing Chemists Association (USIA text).

United States is the principal and foremost source of the Israeli power which has resulted in the present Israeli arrogance and enabled the Israelis to continue to occupy our territories . . . The participants . . . recommended . . . that the United States be subjected to the most severe cut . . . The participants also recommended that this progressive reduction lead to the total halt of oil supplies to the United States from every individual country party to the resolution.'[9] Ostensibly, it was indeed, then, the United States which was to be brought under the greatest pressure – and to transfer that pressure to Israel. Yet, for obvious reasons, it was also the United States which, of all the Western industrial countries, was the least vulnerable to the pressure of the Arab 'embargo'. Although United States imports of Arab oil were cut from 1.2 million barrels a day in August/September 1973 to a mere trickle in January/February 1974, that reduction amounted to only 7 per cent of the country's oil consumption – enough to be troublesome, but hardly enough to cripple or strangle the economy.[10] In such circumstances, if would, in fact, have been astonishing if the direct impact of the 'oil weapon' alone had achieved a radical change in the Middle Eastern policy of the United States.

Indirectly, the impact of the 'oil weapon' on American interests was, of course, more serious, especially in as far as it threatened the economies of Japan and of American allies in Western Europe far more dependent than the United States itself on Arab oil. If the United States was unlikely to be forced into imposing a settlement on Israel by its own predicament, it seemed more plausible that it would be so forced by the predicament of its friends. President Nixon, indeed, said as much as the 1973 war ended:

> 'One of the major factors which gave enormous urgency to our efforts to settle this particular crisis was the potential of an oil cut-off . . . Europe, which gets 80 per cent of its oil from the Mid-East, would have frozen to death this winter unless there had been a settlement, and Japan, of course, is in that same position.'[11]

Yet neither the then President's words nor the superficial plausibility of his thesis make the case secure. Some countries certainly

[9] Resolution adopted by Oil Ministers of the OAPEC member states at Kuwait, 17 October 1973; reproduced in *Survival* 16.1 (Jan/Feb 1974), pp. 38-39.

[10] The figures are from Robert B. Stobaugh, 'The Oil Companies in Crisis', in *The Oil Crisis In Perspective, op. cit.*, pp. 179-202.

[11] Press Conference, 26 October 1973. (USIA text).

suffered, but none suffered greatly. Japan and the European Community members in any case escaped the full potential force of the 'oil weapon', by making placatory statements and gestures and, to a lesser extent, by scrambling with more alacrity than dignity for available supplies. There is no doubt that many Western governments were alarmed by the constraint of Arab oil production – largely because they had not done some simple sums – and that their alarm had some political effect. On looking back at October 1973 and the months that followed, however, there is a notable lack of evidence in support of the thesis advanced by President Nixon. Although oil consumption fell during the six months from October 1973 in Western Europe (but not in Japan), the cut-back seems clearly to have been due more to general economic recession than to Arab action. Moreover, there is no indication that, after their initial cries of pain, any of the allies of the United States sought, on grounds of oil hunger, to sway American policy towards Israel.

None of this is to say that the Arab 'oil weapon' was completely ignored by United States policy makers or their West European and Japanese counterparts in reacting to the 1973 Arab-Israel war or the various efforts to secure Israeli withdrawals which followed; the importance of Arab oil to the world energy economy is obvious, and the demonstration that its supply could and would be manipulated for political purposes has cast a diffuse shadow over the policy deliberations of all major states. But it is to say that the 'oil factor' has apparently played something much less than a determinant role in shaping United States policy, or even the policies of its major allies. Indeed, it is symptomatic that the passage from President Nixon's press conference quoted earlier not only exaggerated the facts beyond recognition but also represented almost the only public reference to the Arab 'oil weapon' or to the broader considerations of the international oil market in any contemporary official explanation of American policy. It is not the task of this paper to explain the strenuous efforts of the United States Government to impose a cease-fire on Israel in October 1973 or to bring about Israeli withdrawals in Sinai or on the Golan Heights thereafter. Arguably, however, the explanation lies much more in the context of the United States' political relationship with the Soviet Union and of the associated policies of *détente* than in the context of United States vulnerability, direct or indirect, to restrictions on the supply of Middle Eastern oil. For an explanation on the latter basis, there is little evidence.

Hardly surprisingly, a great deal more evidence exists of the effect upon the United States of the price of Middle Eastern –and other– oil. The price agreements reached between OPEC members and the international oil companies at Tehran and Tripoli in 1971 had had a 'guaranteed' life of five years. Eighteen months later, they were destroyed in the first stages of what, by January 1974, had become a fully-fledged revolution. The average price of the 'marker' crude (Arabian Light 34° f.o.b. Ras Tanura) was $ 1.73 a barrel in January 1973. On 16 October 1973 (one day before OAPEC decided upon its 'embargo'), the OPEC members in the Gulf, abandoning efforts to negotiate new terms with the companies, unilaterally decreed increases which brought the average price of the same oil to $ 3.55 a barrel. Encouraged in part by the artificially high panic bids made for small quantities of 'free market' oil during the OAPEC 'embargo', but urged on even more by some members, such as Iran, who were hungry to maximise their income, OPEC then threw caution to the winds and, in December 1973, imposed a further rise to $9.41 a barrel: an increase in the average price of the 'marker' crude over twelve months of 444 per cent. By January 1975, twelve months yet further on, it had reached $ 10.46 a barrel.

Increases of these orders were bound to have a dramatic effect on the import bills of all OPEC customers, including that one major customer of OPEC which was also a super-power. The cost of United States imports from the Arab states and Iran, almost all of which consisted of oil or oil products, shot up from $ 1.4 billion in 1973 to $ 6.1 billion in 1974 and $ 8.1 billion in 1975.[12] Evidence of a change in the terms of trade as they apply to Middle Eastern oil exporters could hardly be more striking.

The reactions to the enormous increases in the price of OPEC oil were, of course, immediate and tumultuous. OPEC's actions were seen as promoting both inflation and recession in the industrialized world, as creating a chronic imbalance of trade and payments which would disrupt the international banking and monetary systems, as threatening less developed –and some developed–

[12] These figures and those in Table 1 are taken from a newsletter ('Spending the Petrodollar Billions', 9 February 1976) written by Kenneth C. Crowe of *Newsday* for the Alicia Patterson Foundation, New York. They are there attributed to John Haldane of the US Department of Commerce, and are quoted here with credit to *Newsday* and the Alicia Patterson Foundation.

importers of oil with imminent bankruptcy. Not all the predictions were unjustified; despite attempts by some OPEC members to cushion the shock, the effect on a number of less developed countries remained extremely serious. But the predictions of grave damage to the American economy, with which we are particularly concerned here, proved generally fragile. The increases in oil prices between October 1973 and January 1974, as much by their speed as their extent, did reinforce the other factors already combining to inflate prices and constrain the level of economic activity in the United States. But their contribution to those processes appears, with hindsight, to have been subsidiary in scale and transient in duration. The hectic expansion of banking activity required to cope with 'petrodollars' did impose certain strains on the American banking system, amongst others, and a few casualties were sustained in the process.

But the banking system survived, and even prospered, as its managers learned to adapt not only to the problems but also to the opportunities presented by new oil wealth in the OPEC states. As to the trade balance of the United States, the prophets of doom, as Table 1 strikingly demonstrates, were out of season. Far from

Table 1

U.S. trade with Middle Eastern member states of OPEC (including Iran). 1973-75 (Thousands of dollars)

	1973	1974	1975
U.S. imports	1,438,800	6,086,900	8,128,100
U.S. exports	3,849,680	10,349,550	11,344,120
(of which: military equipment)	(2,531,680)	(6,114,550)	(3,957,020)
Balance	+2,410,880	+4,262,650	+3,216,020

Source: See footnote 12.

penalizing the United States economy, the multiplication of the world oil price created a vastly expanded market for American products in the Middle East, accelerating the recovery of the United States economy into a new period of growth and more than offsetting the additional bill for imports of oil. The United States was obviously more fortunate —or more successful— in this respect than many of its allies (although both West Germany and Japan prospered in a similar fashion). Moreover, these simple measurements take no account of other effects upon the American economy, in relation, for example, to investment in alternative sources of energy. The fact remains that, from this evidence, it would be difficult to conclude that the sixfold increase in world oil prices during 1973 and 1974 imposed any irresistible pressure upon the Middle Eastern policies of the United States, at least in regard to the promotion or resolution of international conflict.

There is one important caveat to add. The figures in Table 1 do show the success of the United States in balancing its higher 1974 and 1975 import bills for Middle East oil. But they also show how much of that success was initially due to only one factor: the increased sale of American arms. Non-military sales to Middle Eastern oil countries all but covered the counterpart import of oil in 1973. In 1974, however, the proportion of the oil bill thus matched fell to 70 per cent, and although it rose again to 91 per cent in 1975, it was above all the fact that military exports during those two years reached the remarkable total of over $10 billion which guaranteed the United States a continuing trade surplus.

In several respects, such a rapid expansion of the arms trade offers hostages to fortune. In the first place, it is always harder for a government to divorce the pattern of its country's military exports from its own political posture than it is to separate official policy from non-military trade. The sale of arms, and the associated commitments to train, maintain and re-supply, involve governmental sanction and imply governmental approval to a unique extent. In the second place, the more active promotion of arms sales to the Middle East by one super-power, in response to the demands of commerce even more than of security, tends to issue a licence to others, including the other super-power, to follow suit, thus revivifying those fears of a progressive strategic polarization of the region which were so widely expressed in the decade after 1955. In the third place, making any important trade balance heavily and persistently dependent upon military exports entails commercial risks for

the arms supplier concerned, simply because the pattern of such exports tends, in the longer term, to be so irregular. However high their ambitions, Middle Eastern states will not order a new generation of, say, combat aircraft or missiles each year; even assuming that the same supplier is retained, their major purchases of such expensive capital equipment will be relatively widely spaced, so that, the phasing of deliveries notwithstanding, the volume and value of the trade will be subject to rather large periodic fluctuations. All in all, therefore, the emphasis placed since 1973 on the sale of American arms to Middle Eastern oil exporters carries with it potentially considerable longer-term costs and, even if it marks no conscious or immediate change of political attitude, is likely, over time, to impose significant pressures upon American policy-making.

If one super-power has suffered little damage from the operation of the 'oil factor' in the Middle East, and may even have derived some short-term advantage from it, albeit at the risk of longer-term penalties, the other super-power appears, at first glance, to have obtained, in at least two respects, a clear-cut profit.

The Soviet Union, whether or not it has ever aspired since 1945 to dominate the Middle East itself, has constantly striven to prevent domination of the area by the West. The vision of OAPEC banning, with impunity, the supply of oil to the United States must therefore have been welcome, as must the demonstration, over a longer period, that the Western oil companies no longer had the ability to regulate the production or to control the price of Middle Eastern oil. It would, to be sure, have run strongly counter to Soviet interests and desires if the United States had, in fact, been driven to intervene militarily in the Arab world. It would also have been to the disadvantage of the Soviet Union, more subtly but perhaps even more substantially, if OAPEC or OPEC actions had caused a serious economic crisis in the major countries of the OECD. Neither situation arose – and there is no sign that the Soviet Government considered either likely. On balance, therefore, the greater independence from the West demonstrated by Middle Eastern oil-exporting countries, and the self-confidence obtained from its demonstration, may be set by the Soviet Government on the credit side of the account.

A more tangible credit also accrued to the Soviet Union from the events of 1973/74. The Soviet Union has hitherto purchased only trivial quantities of Middle Eastern oil, and almost all of that has immediately been re-exported. It is, however, an exporter of oil

in its own right, with the majority of its exports going to Eastern Europe but with a minority being sold for hard currencies outside COMECON. The dramatic increase in the OPEC price levels gave to the Soviet Union an ideal opportunity to raise the prices charged for that latter proportion of its own exports, and thus to increase very substantially indeed its earnings of hard currency. The opportunity was seized. Moreover, the effect of higher prices for Soviet oil was extended also to allies in COMECON, by means of a complicated agreement which means not only that East European states are likely to be paying something like the full OPEC price for Soviet oil by about 1978, but also that they are liable to pay for any such oil over a set quota out of their own scanty reserves of hard currency. All in all, therefore, the decisions taken by OPEC in 1973/74 on prices —even more than those taken by OAPEC in October 1973 on supply— represented a valuable windfall for Soviet leaders. There is no evidence that the Soviet Union actively encouraged OPEC's price increases, while the Soviet Government's welcome for OAPEC's use of the 'oil weapon' was, at most, muted. Nor is there any evidence that Soviet policies towards the Arab-Israel dispute or other international conflicts in the Middle East have been significantly affected by considerations connected with oil. It is not unreasonable to judge, however, that the Soviet Union was a net benefactor of the events in the Middle Eastern oil market in and after October 1973.

If the story were to stop here, it would seem to be a relatively simple one, with a relatively simple moral. The 'oil factor' has neither ignited nor extinguished Middle Eastern conflicts in the past three years, although it may conceivably have hastened the onset of the 1973 Arab-Israel war. What it has done, within the region, is to procure a progressive transfer of relative wealth and political influence from the Arab states bordering Israel, and especially Egypt and Syria, to the oil-exporting countries of the Gulf and North Africa. As to the super-powers, it seems to have played only a relatively minor role in determining their attitude to Middle Eastern conflicts — a lesser role, certainly, than that played by their mutual interest in improving and sustaining their own bilateral relationship. Indirectly, through its effect upon allies, it has clearly had some influence on the United States. By the same token, in ways not explored in this paper, it has had an impact upon relations between those allies and the United States. In neither the American nor the Soviet case, however, has it obviously been a determinant

of policy in the Middle East. It casts a shadow, but it does not draw lines. One corollary is that, if significant causal links have existed between Middle Eastern oil and Middle Eastern conflict, the flow of causation has been from the latter to the former, rather than the reverse. As 1973 so amply demonstrated, international conflict in the area is liable to affect the supply of oil and to provide occasions for, rather than to cause, rapid changes in its price. Those effects impinge in different ways upon the energy economies and policies of the super-powers. Thus, it is not so much that the 'oil factor' has shaped super-power attitudes to Middle Eastern conflict as that Middle Eastern conflict, by affecting the oil market, has borne upon super-power policies and positions in regard to energy. In the current equation, oil is more effect than cause.

The future may be different. That is properly a subject for a separate essay. Here, it must suffice to set out some of the considerations in the briefest form.

Within the Arab world, the long-term importance of shifting the political centre of gravity from 'warrior states' to 'oil states' is incalculable, but potentially great. Much will eventually depend on the intentions —and the identities— of those who, by one means or another, become the future governors of the 'oil states'. In the very long run, much will also depend on the ability of each of those states to translate its existing assets into alternative means of earning a comparable income in that inevitable future when either the supply of or the demand for oil has failed. Meanwhile, what may be more significant in the shorter run is the way in which events since the beginning of October 1973 have tended to reconnect the policies of oil-exporting countries in the Gulf and the Maghreb to the political and military situation in the more confined Arab-Israel context of the Levant. Religious fervour, national prestige, personal ambition, political prudence: all have recently combined, under the stimulus of the 1973 war, to prompt a more active commitment by a number of those who wield the 'oil weapon' to the imposition of territorial contraction upon Israel. It is far from certain that the effect will endure; other international problems and opportunities compete for attention, and the Lebanese civil war has already served as one violently divisive cross-current. In as far as it does endure, however, the re-orientation of the Gulf and the Maghreb towards the Levant will not be the least important outcome of the 1973/74 crisis, especially, of course, for Palestinian leaders who, controlling no oil themselves, must seek to obtain

its benefits, political and economic, at second hand. They have already learned to exploit the fact that those who are publicly very rich frequently find it politic also to be publicly very generous, but they would naturally wish to secure active political and diplomatic support as well as money. For their hopes to be realised consistently, the concern of distant oil exporters for the affairs of the Levant will have to be at least sustained, and preferably reinforced.

Turning to the super-powers, the effect of the 'oil factor' on their relative positions in the Middle East may well be reversed as time passes. The Soviet Union, having extracted some little advantage from a largely passive policy, may have to pay a price in the longer term. Those in the Middle East to whom oil is bringing the greatest international influence —Saudi Arabia, Iran, Kuwait, the UAE— are not, on the whole, its friends. Even Iraq is an uncertain quantity, while Libya is nobody's friend at all. Moreover, the Soviet Union has less than the United States to offer oil-rich friends. Above all, it is less able to serve the urgent desire of the oil exporters to equip their countries with modern and technically advanced industries. That, indeed, is arguably the other super-power's greatest long-term advantage. Over the next ten years, in fact, the Arab 'oil weapon' will progressively find itself facing an American 'technology weapon'. As the potential but reciprocal impact of those weapons increases —as it will—, surprisingly solid relations of mutual respect and advantage may be forged. In the process, however, the United States will find its own freedom of political action in the Middle East restricted in new ways — as it is already being restricted by the sale and purchase of arms. American influence in much of the Middle East may well increase, but American flexibility will, at the same time, decline. That possibility may reinforce other arguments for compensating by reducing the constraint hitherto imposed on American policy by close relations with Israel.

Viewing that specific contingency against the background of more various future uncertainties in the Middle East itself, those responsible for policy in Israel must be apprehensive, and may well become more so. The 1973 war, despite its outcome, delivered a brutal shock to the military confidence of most Israelis. The first concerted use of the 'oil weapon' and the subsequent conversion of new Arab oil revenue into new Arab armament have greatly encouraged the view thus formed that time is not on Israel's side. American diplomatic pressures for territorial 'disengagement',

especially in the context of continuing super-power *détente,* have srengthened fears of Israel's eventual diplomatic isolation. The overall effect has been to erode the essential foundation of that cautious middle-of-the-road strategy of 'nothing for nothing but something for anything' which has, in fact, dominated Israeli domestic politics and international policy alike since the 1950s.

Those who have led Israel during the last twenty years have done so consistently from positions within the middle ground of national politics, rejecting both the greater rigidity and the greater pliancy advocated by different domestic opponents. The rhetoric and gesture of positive policy notwithstanding, their ability to command electoral support has essentially depended throughout upon the largely unspoken but widely shared assumption that Israel's best course, like Mr Micawber's, must be to hold fast and wait for something to turn up. Israeli governments have, in fact, allowed almost all their significant foreign policy decisions since 1957 to be taken for them by external actors or external events – a strategy which has had much to commend it, but which implicitly assumes two premises: that the United States stands firm as the effective guarantor of Israel's security, and that, partly as a consequence, Israel can maintain sufficient diplomatic and military strength to deter or repel any foreseeable Arab attack. It is the challenge apparently offered to those premises by the fabrication and employment of the Arab 'oil weapon', by the use of larger Arab oil revenues to arm Arab forces and support Palestinian militancy, and above all by actual and potential reactions in the United States to these new factors, which threatens to undermine the popular case for a middle-of-the-road strategy and progressively to polarise Israeli politics between those who, fearing Arab strength and American defection, advocate unilateral concessions in the interest of settlement and those who, sharing the same fears, advocate military as well as diplomatic intransigence.

Partly because the latter advocates are at least as likely as the former to prevail, it is by no means impossible, in fact, that the 'oil weapon' will turn out in the longer term to have cast its deepest shadow within Israel. The crucial and precedent question, however, will be that of its longer-term influence in the United States. In 1973/74, considerations of oil supply and oil price seem to have played relatively little part in shaping American policies towards Israel in particular or the Middle East in general. The question is whether relations with Arab and other Middle Eastern oil exporters

will not come steadily to loom larger in American calculations over the next decade. On the one hand, the most recent OECD estimates are that United States dependency on oil imports, far from declining, will rise inexorably from 290 mt in 1975 to almost 430 mt in 1985, with much of that increment presumably having to come from the Arab Middle East.[13] On the other hand, there is the strong probability that many companies as well as many government agencies in the United States will, in any case, become increasingly involved in elaborating a pattern of closer and more complex commercial, technical, financial and even military relations with Middle Eastern oil-exporting states as the latter pursue their own development plans. If the pressures thus generated combine to alter substantially the United States attitude to Israel —as they will certainly combine to impose some more general limitations on American policy— then the fears which tend to polarise Israel's domestic politics will be both magnified and largely justified. In the longer term, the 'oil factor' could thus acquire some of that important causal status, in relation to super-power policy and regional affairs, which it seems not to have occupied in 1973/74. If so, the price of its doing so, not least in terms of Israeli desperation, may turn out to be high.

[13] This OECD estimate that net U.S. imports will be 8.6 million barrels per day in 1985 was presented in March 1976 to the Energy Commission of the Conference on International Economic Co-operation and subsequently quoted publicly by R.E. Hamilton of the OECD Secretariat ('Trends in Energy Consumption and Supply' Paper presented at the University of Cologne, 22 June 1976; mimeo., p. 16).

Export Cartels and International Justice

Covey T. Oliver

"Nature never dictates one thing and Wisdom another" —Juvenal, XIV, the satire on *Education in Avarice*, line 321

I. *Specification of the topic*

A. State export cartels

As is well-known, the "export cartels" of present concern are the Organization of Petroleum Exporting Countries (OPEC) and its would-be progeny as to other primary substances that produce energy. Excluded are arrangements related to the stabilization and elevation of prices of non-energy materials, such as coffee, aluminum, specialty metal ores, and the like. Food, for direct and indirect human consumption, however, is included, since the end use of foodstuffs is to produce energy—indeed, energy that under some grim scenarios may have to substitute for that presently derived from oil, coal and uranium-burning machines.

The export cartels to be considered by us are created and operated by states. States are the constituent juristic elements of the international legal order of the planetary community as it is presently organized. Under existing intenational law states have legal relationships (rights, duties, powers, and immunities) with other states but very few legal relationships with humans. Thus a number of actions that, if done by non-states would create legal liability, do not do so in the case of actions by states. Almost all of the law, most of it customary, of the responsibility of states relates to the actions of a single state. When states act in concert in the economic field they intend to achieve a degree of effectiveness as to the use of economic power that a state acting singly usually cannot mobilize. This is especially the case where several states between themselves represent a preponderant and indispensable portion of the planet's total supply of a vital energy commodity.

The energy cartel is a new situation under international law, and there is at least a question whether states acting in concert are, or should be, treated as if each of them had acted singly. Or to put the issue another way: if a state augments its capacity to produce economic effects upon another state beyond its normal capacity to do so by drawing upon the combined economic power of a group of states joined in a common purpose, does that state, normally free of responsibility to other states for damage to them through refusal to supply on market terms, become liable?

The question of the legality or not of an export cartel of states also involves variables related to the intentions of the parties in regard to their common use of the instrumentality (the cartel). The term "cartel" is drawn from the public law of particular states and of the European Economic Community as to the conduct of non-state actors who have entered into a horizontal arrangement between former competitors (or "ought-to-be" competitors) designed to avoid the rigors of market forces. Classic cartels flourished in western Europe until comparatively recently; and, generally speaking, their members combined: (i) to adjust total production to estimated demand in such a way as to maximize price; (ii) to allocate sectors of the total market so as to reduce or eliminate competition as to the supply of the cartelized commodity within each such sector; (iii) to standardize the terms on which the suppliers in the cartel would trade with customers; and (iv) to aggregate such great economic power to the product line as to make outside suppliers vulnerable to restrictive trade practices imposed upon it by the collective. In very extreme cases producers' cartels have employed illicit (criminal) force against opponents, usually competitors but sometimes including consumers.

In the developed world the trend has definitely been toward curbing the activities of non-state cartels by regulatory law. The most significant steps since World War II in this particular have been the enactment of the Restrictive Trade Practices Act and later the Monopolies Act in Great Britain,[1] the Cartel Law of the Federal

[1] Of vintages 1956 and 1965, respectively. Descriptive analyses, comments, and attitudes toward antitrust laws, particularly as to their reach beyond conduct solely within national territory, are collected in International Law Association, Report of the Fifty-first Conference, Tokyo (1965). I served as principal rapporteur for the Association's Committee on Restrictive Trade Practices but was unable to attend the meeting, due to a governmental assignment that unexpectedly arose after the preparation of my study.

German Republic,[2] and, above all, Articles 85 and 86 of the Treaty of Rome,[3] establishing the European Economic Community, and regulations of the Commission[4] and the decisions of the Community Court of Justice[5] in regard to the basic anti-cartel norms of the Treaty. Efforts to provide an international positive law as to restrictive trade practices and monopolies, however, failed with the refusal of a sufficient number of states to approve the Charter of the International Trade Organization, and revival of this effort is now opposed by the substantial number of states that actively support the desirability of OPEC-type export cartels.[6] Among the many outlooks that divide the developed and the less-well-developed countries are precisely their different perspectives on restrictive trade practices and monopolies. In contrast to the European

[2] This law, enacted in 1957, reflects the free enterprise ideology of the Adenauer period. Although (at the insistence of the United States) a tri-zonal decartelization and deconcentration law had been imposed as an occupation measure, the law freely selected by the FGR resembles more the Sherman Act and its progeny than it does the earlier rigid and extreme military government decree. The German antitrust law continues to be vigorously enforced, and it specifically applies to economic conduct outside the territory of the Republic that has economic effects within it.

[3] Article 85 proscribes restrictive trade practices, and Article 86 concerns itself with the abuse of monopoly power. The focus of Community antitrust law is protection of the most basic principles of the Treaty, free movement of goods within the Community, a focus that is managerial rather than ideological. The Sherman Act, passed in the United States by a Democratic Congress in the hey-day of populism (1890) reflects a distrust of "big business".

[4] See Council Regulation No. 17 (1959-62), *Official Journal of the European Communities*, 87, and its subsequent refinements.

[5] These decisions interpret a Treaty whose norms are directly applicable by community authority to persons and firms within the territories of member states. The Commission has consistently maintained the viewpoint that the Community antitrust law reaches acts outside the Community having economic effects within it. The Community Court has ageed in some situations; but in others, notably in the case of *Imperial Chemical Industries, Ltd. v. Commission,* Recueil Vol. XVIII, 1975-5, 619 (1972), the successful Community action against the "Dyestuffs Cartel", the Court chose, despite the advice of its Advocate-General, to apply Article 85 on the theory of external corporate control of the cartelizing companies within the Community. See footnote 28.

[6] The Havana Charter was, at the least, ahead of its time. The U.S. Senate so much dissaproved of some of its provisions on trade that the treaty did not even come to a vote. Other states objected to the "antitrust" aspects thereof, which the United States delegation had insisted upon. Of the Charter only its transitional organ, the "semi-international organization" known as the General Agreement on Tariffs and Trade (GATT) came into being and exists today.

common market treaty, for example, the common market treaty of the Andean Community does not address the problems of derogations from free competition in the private sector, nor does the Latin American Free Trade Association or the Central American Common Market.[7]

Thus, viewed from the standpoint of the classic purpose for which cartels have been used in the past by the private sector, there is concern in the developed world and disregard or unconcern in the Third, Fourth, and Fifth Worlds. This difference in outlook as to cartels *per se,* naturally, engenders differences in outlook as to the desirability or undesirability of states becoming the cartelizers.

States as cartelizers, however, either have, or easily could resort to, cartel-like arrangements for purposes (i.e., with the intention of effectuating purposes) that have not been associated historically with the cartel-like activities of private companies. For instance, OPEC has continued as an export price and production cartel but it came to world attention in relationship to an embargo of petroleum shipments to states whose foreign affairs stances (as seen by key OPEC members) were unsatisfactory. Thus export cartels of states have from their inception been used directly in a Von Clausewitzian way, i.e., as an instrumentality for the pursuit of the foreign policy objectives of the cartelizing states ". . . by other means". This aspect of state-dominated export cartels links directly—and will have to be considered along with— limitations in positive international law as to the use of power by states to seek to curb the volition of other states as to foreign policy lines of action.

Further, export cartels of states as we have seen them so far in operation have the possibility —and in the case of at least one chief of an OPEC state, the Shah of Iran, the present purpose— of allocating essential resources as between now and the future. Also, in regard to this function, which we might well call "social regulation of use", there is evidence that OPEC countries may be giving certain non-OPEC states preferences as to prices or other advantages for reasons related to developmental needs, dependence, political affinity, and other socio-political variables.

[7] The texts of these arrangements are usefully collected in Inter-American Institute of International Legal Studies, *Latin American Integration* (1962). Current information as to the course of regionalism in the Western Hemisphere is provided in the publication *Comercio Exterior,* published regularly by the Banco Nacional de Comercio Exterior, México.

Finally, the states associated in the oil cartel use their economic power over the price of oil to redress disadvantages that they see as otherwise existing in the terms of their trade with highly industrialized states. These last two apects of OPEC link to the laws or expectations that have developed in international trade.

To conclude this aspect of specification of the topic, the term "cartel" must be considered to have different semantic referents when it is used in regard to the concerted actions of groups of states, than those that clustered about the term in an earlier usage restricted to private sector activity. Also, the purpose for which states actually have used, or potentially can use, their combined economic power over vital exports of energy-source materials are political and regulatory, as well as merely commercial. To ensure that the differences are always before us during this presentation, I shall henceforth insert the term "state" before "export", viz.: "State Export Cartels".

B. Law and justice

A normative legal order is an expression of authoritative value preferences, and law-makers have almost always acted as if the norm they formulate (which is, essentially, a prediction of what licit force ought to require as a consequence if a certain act occurs) reflects a philosophic Good. But, of course, the Good so chosen as the justification of the law cannot in an imperfect world be deemed an Absolute Good but only expresses a relative value of the authority-asserter (the State). Some great legal philosophers, such as the late Hans Kelsen, exclude from legal science any concern (beyond the interpretative) as to matters of relative valuation. Others tend to focus upon those relative values that link to fairness, honesty, and humanity in the process of power-application (procedural justice) but do not expect through legal science to achieve substantive justice. Still others regard the fundamental purpose of law as the attainment of as much relative substantive and procedural justice as possible.Within this latter group some assert that law loses its justification (and, indeed, ceases to be law) when it becomes patently unjust. Others of this persuasion recognize that unjust law is still law but ought to be changed to remove or moderate injustice as quickly as possible by the most available just means. There is a tendency also to move energetically toward the proposal of legal arrangements or struc-

tures designed to achieve justice, i.e., to assume that the quest for justice through law leads society, rather than to accept the disappointing possibility that society leads law, just or unjust.

A very modern jurisprudential attitude, one that probably originated in the United States but that has had some influence elsewhere, perceives law, not as a normative system, but as a variable in the power process. The masters of these variables —the lawyer class, including judges, foreign ministers, international civil servants and the like— should apply them so as to minimize the instances in which human affairs are governed by "naked power" beyond law and to maximize the attainment of certain basic "goal values", which the writers deem to be so generally accepted as Goods as to be beyond debate. This assumption is, however, very much itself in debate.

A basic problem with the quest for justice in law is that some societal phenomena seem beyond justice: the way in which capacities are distributed genetically between different human beings; the haphazard distribution on the planet of its principal sources of wealth in raw materials, good land, water, climate; the genuine lack of alternatives to many grave problems. One thing seems certain: justice —or even its modest sibling, equity or fairness— cannot be frozen in time. What might have been tolerably just at one time, under a bygone set of conditions, cannot be uncontrovertibly asserted as just at a later time under a different set of human, social, and political circumstances.

A law (norm), however, continues to exist as such until it is displaced by a contradictory norm; and even when it becomes manifest that the norm, unobjectionable as to essential fairness at its inception, has become patently unjust, there arises an additional problem, that of effective, fair, or acceptable modalities for its change. In domestic legal systems the legislators and/or the courts provide such changes. In the international legal order there is no true legislature, and the judicial tribunals available have very limited potential, either in terms of what states refer to them or in terms of what responses will be respected.

The issue of how international law changes to reflect different perceptions of what is just is especially difficult as to consuetudinarian international law, i.e., those norms that develop through a *consentio juris* of states. The first difficulty is that of ascertaining that the proposal for change has been fully and effectively evaluated from the standpoints of science and of the ranges of interest of

the states and peoples concerned. The second difficulty is that of weighing interests of groups of people, rather than to sum up the wills of states. One generalized attitude, particularly among the developing countries, is to insist that the principle of the juridical equality of states and its translation into parliamentary diplomacy as the principle of "One country, one vote", equally mandates that the *consentio juris* on an issue of law is to be found by counting the wills of states, without regard to the wide array of human and societal variables that differentiate them.

II. *State export cartels and consuetudinarian international law*

When OPEC, created earlier, burst upon the world scene[8] in association with the oil embargo of 1973, it was commonly and correctly assumed that customary international law as it had so far developed did not include a principle of state responsibility for injuries to a state caused by the refusal of another state to provide it with essential energy materials in peacetime. Also, it was accepted that what is true for a single state is also true for a combination of states that aggregate their individual economic powers into a single overwhelming one.

In the period since, when the oil embargo of the Arab States has been lifted but OPEC polices world oil to ensure oil prices of $ 12 a barrel and upwards, analysis of the resulting issue of state responsibility, *vel non,* has received comparatively little attention, largely, perhaps, because it has been felt that on so highly-charged an atmosphere as that surrounding the functioning of the oil cartel it could not be expected that any *consentio juris* could develop in favor of a new state responsibility where one did not exist before.

The problem of the power of the oil producing states to affect economic conditions in (and the will of) consumer states has, instead, been approached either in terms of acquiescence, eventual

[8] As is well-known, Venezuela and Ecuador, the Latin American members of OPEC, did not participate in the embargo of the United States and the Kingdom of the Netherlands, while the role of Iran was ambivalent. The Arab members of OPEC unilaterally determined that the embargoed countries had in some ways unspecified by the self-appointed "judges" aided Israel in its responses to a first strike by Egypt. The unanimous decision of OPEC to intervene against normal market forces as to the price of oil, however, is very closely-coupled in time with the Arab embargo.

use of force against such states, or denial counter-measures, such as to foodstuffs.[9] Politically, some groups in consumer states have speculated as to various ways to bring about the dissolution of OPEC, either through encouraging dissention between its members or by stressing *vis-à-vis* the oil-poor portion of the developing world that it and the oil-rich states have few true interests in common.

Little attention has been paid by states opposing OPEC policies to the possibilities of resorting to principles of the United Nations Charter for the purpose of inculcating doctrine by asserting the notion that consuetudinarian evolution of law from general provisions of the Charter has occurred and that these oppose the policies and purposes of OPEC.

Such a course of action is not entirely fanciful: The new African states have convinced almost all the world by now that *apartheid* and colonialism are proscribed by the Charter, *inter alia,* because they have an inherent and unavoidable tendency to create threats to peace under Articles 1, 2(3), and 39. (Even though, of course, it would be the forceful responses of objecting states that would in fact create such threats.) Further, there is the 1970 Resolution of the General Assembly that seeks expressly to "prohibit" the use of economic measures to coerce another state ". . . in order to obtain from it the subordination of the exercise of its sovereign rights . . ."[10] Nonetheless, the only initiatives taken at the UN have been by the developing country majority through its phalanx-like support of the Declaration on the Establishment of a New International Economic Order[11] and of the "Charter" of Economic Rights and Duties of States.[12]

[9] Interesting questions as to an international law of retorsion lurk here if the position is taken that the use of concerted economic power (an oil-producers' embargo) to force the will of the subject state is either aggression under the United Nations Charter or illicit intervention under the Charter of the Organization of the American States. Viewpoints have more than once been asserted, particularly by Latin American states, that economic denial is intervention. Compare, however, the language of the so-called "Charter" on the Economic Rights and Duties of States maintaining that export cartels are so "legal" as to make counter-measures against them illegal.

[10] U.N.G.A. Res. 2625, 25 UN GOAR Supp. 28, 121 U.N. Doc. A/8028 (1970).

[11] U.N.G.A. Res. 3201 (S-VI), adopted without vote, U.N. Rep. A/9556 (Part II), May 1, 1974.

[12] U.N.G.A. Rep. A/9946, Dec. 12, 1974, adopted 120 to 6 with 10

The second of these 1974 General Assembly documents asserts the rights of producer countries to establish commodity cartels as a derivation from the greater power of "permanent sovereignty" over natural resources. Typically, this "Charter"[13] goes on to assert that this right to cartelize implies a duty on the part of other states ". . . to respect that right by refraining from applying economic and political measures that would limit it . . ." The disequilibria between the assertions of rights and the negations of duties in regard to the pretensions of the developing countries revealed in these two recommendatory actions of the General Assembly are well-known; and the whole effort is, on the whole, discounted as to either legal or political effect in the developed countries precisely because of this flaw.

The net effect, then, is that the United Nations has been neutralized as a source of new law in regard to state export cartels. Impartial analysis must lead to the conclusion that the international legal consequences of injury to a state by the activities of a cartel of exporting states is not actionable under any principle of customary substantive international law.

But there remains the matter of what consuetudinarian international law provides as to the jurisdiction of an affected state to apply its own national sanctions, such as under the antitrust laws of the United States, Great Britain, France, Germany, and the European Community, to such activities.

The fountainhead of authority on this matter of international rules about legislative jurisdiction remains the decision of the Permanent Court of International Justice in the famous *Steamship Lotus Case.*[14] But before we deal with the significance of that case as to whether a state has jurisdiction under its national law to

abstentions, a vote that polarized the developed and the developing worlds, with the so-called Second (socialist) world exploiting the existing contradictions as best it could.

[13] No action of the General Assembly can be positive law as such; Articles 10, 11, and 12 of the U.N. Charter. The use of the term "Charter" for the formulation of economic principles seems to have been deliberate, for the purpose of insinuating that the elaborate provisions of the document acquire, in some way, legal or quasi-legal effect by a General Assembly vote. While it is now established doctrine that General Assembly votes can under appropriate conditions be taken as evidence of the *consentio juris,* heretofore this has not been considered as applicable to highly detailed normative compilations, in contrast with a single, or a few related, norms of fairly general content.

[14] P.C.I.J. Ser. A No. 10, 1927.

reprehend conduct outside its territory producing discernible and deleterious economic effects whithin its territory, we must dispose of the issue of immunity from suit of the commercial instrumentality of one state (or of a group of states) in the courts of another state.

It is now generally accepted in customary international law that a state does not enjoy immunity from suit in foreign countries as to claims against it arising out of commercial, rather than *ordre public* (strictly governmental) functions.[15] Indeed, many civil law countries, of whom several are OPEC members, have long followed what is known as the *restrictive theory* of sovereign immunity. Eventually, the common law countries, led by the United States, have begun to abandon their long-held view that sovereign immunity is absolute (under the somewhat *royaliste* motto, "The King can do no wrong"). This is not the place for an elaborate analysis: suffice it to say that state-owned assets used commercially are reachable by attachment (for jurisdiction of courts) and probably leviable for the satisfaction of judgments.[16]

[15] The U.S. Department of State, prior to shifting to the restricted immunity theory by what has come to be known to international legal experts as "The Tate Letter", 26 Dept. of State Bill. 984 (1952), commissioned a full comparative law study of state practice worldwide. The results showed a heavy preponderance in favor of restricted immunity. The author, (now) Dean Joseph M. Sweeney of the Tulane University Law School, has continued to contribute discerning analyses of where the line runs as between state functions that are essentially acts of governance and those of entrepreneurship, Useful information on developments (transnationally) of the restrictive theory since 1952 is collected in Steiner and Vagts, *Transnational Legal Problems*, 658-665 (1975). The attitude of the U.S.S.R. (and of other state-trading states) is to resist drawing the governance/entrepreneurship line of demarcation. However, a proposed European Convention on State Immunity signed in 1972 sharply restricts sovereign immunity by the enumeration of situations in which a signatory state is not entitled to claim it. See 66 Am. J. Int. Law 923 (1972) for the text of this treaty, not yet in effect.

[16] Strictly speaking, the doctrine of restricted sovereign immunity relates only to the question whether a foreign state or its instrumentality may be subjected to enforcement (usually judicial) jurisdiction in another state. The question whether after judgment there may be execution against state property to satisfy an adverse judgment against a respondent state is one of *Remedies for Breach of State Responsibility* under international law, not one of jurisdiction. Proceedings strictly *in rem* against state-owned vessels in commercial service and proceedings by writ of foreign attachment to obtain jurisdiction over the property of a respondent foreign state that cannot be served *in personam* are, analytically, related to the acquisition of jurisdiction, not to the law of permissible remedies. However, there is confusion sometimes as to attachments *(proceedings quasi-in-rem)*. The

The United States, however, follows (except as Congress has provided otherwise) a judge-made "act of state" doctrine, which is national consuetudinarian law that courts in the United States will not sit in judgment upon the legitimacy of acts of a foreign state taken within its territory. This doctrine is, where applicable, seemingly more restrictive on suits against foreign state-owned commercial enterprises than the comparable civil law doctrine that a foreign official act will not be brought into question in a domestic court unless offensive to *ordre public,* taken as being fundamental to the interests and values of the forum state.

As the American act of state doctrine, Congress has mandated that the courts shall not apply it to forbid examination of the legitimacy of a foreign nationalization under international law, where the suit is between the nationalized former owner and a buyer with knowledge from the nationalizing state; and in such applications the notion of what international law provides in the way of remedies shows little evidence of having been derived from an enquiry into the *consentio juris.*[17] There is, therefore, the possibility that at some time, under certain types of provocations, OPEC might be reachable procedurally, whether

publicists tend toward the viewpoint that the property that a state uses for commercial purposes may be levied upon for the satisfaction of judgments that have been made possible as a result of the suability of the state under the theory of restricted immunity. See, generally, *Restatement of the Foreign Relations Law of the United States,* Section 69, Reporters' Note 2. The United States, however, generally follows (as a rule of international law) a principle against levy of execution on state property for the satisfaction of a judgment against a state, other than one relating to excise taxes on state commercial instrumentalities, etc. A proposed statute on sovereign immunity would change the "United States foreign affairs law" in this regard; see Section 1610, of Bill S. 566, H.R. 3493, 93rd. Cong., 1st. Sess., 1973, to permit execution against certain types of state assets.

[17] The tangled skein of the U.S. "Act of State Doctrine" and its partial legislative over-ruling (as to nationalization cases) in relation to the international consuetudinarian law of remedies is sought to be un-raveled in Leech, Oliver, and Sweeney, *The International Legal System* (1973). In a nutshell, the results of several American cases since the intervention of Congress through one of the "Hickenlooper Amendments" to the Foreign Assistance Act, i.e., 22 U.S.C.A. Sec. 2370 (e) (2), 1970, seem to assume that under the "international law" that purportedly is being applied by a domestic court (when the bar of the act of state doctrine is removed) includes a rule that *restitutio ad integro* is a recognized remedy. On the basis of the remedy usually provided (money damages) this is a dubious assumption.

it continues to act abroad through the oil companies or directly as an instrumentality of the OPEC states themselves. This legal possibility exists in many national legal systems, including that of the United States, regardless of whether there is or is not a consuetudinarian international rule of legislative jurisdiction pertinent to the problem. Only a few states provide in their constitutions, as does the German Federal Republic,[18] that national legislation in violation of international law is invalid. In many states it is a principle of interpretation of statutes that they are not to be construed in such a way as to violate international law; but if the legislature mandates a violation, the courts will perforce apply it.[19]

Thus, we return to the basic question: is there an international public law rule against applying national anti-trust laws to foreign states or their instrumentalities as to non-governmental transactions, such as the merchandising of petroleum and its derivatives?

The *Lotus Case* is not a sharply focused opinion as to its reasoning, but its basic premise is stated by the Court as follows:[20]

> Now the first and foremost restriction imposed by international law upon a state is that . . . it may not exercise its power in any form in territory of another state. In this sense jurisdiction is certainly territorial . . .
>
> It does not, however, follow that international law prohibits a state from exercising jurisdiction in its own territory, in respect of any case which relates to acts which have taken place abroad, and in which case it cannot rely on some permissive rule of international law. Such a view would only be tenable if international law contained a general prohibition to states to extend the application of their laws . . . to persons, property and acts outside their territory . . .

The Court then decided that France had no legal cause to object to the application of Turkish criminal law to a French deck officer

[18] Basic Law, Art. 25.

[19] Although vastly different as to separation of powers, both the British and United States constitutions seem to require this result. See, generally, Oliver, *The Enforcement of Treaties by a Federal State*, (I) Recueil des Cours, 1973, Hague Academy of International Law. It is rare for a national constitution to provide for the invalidation of national legislation on the ground that it is inconsistent with general international law. Several states, however, such as France, forbid a later statute or decree to contradict an earlier treaty as to internal legal effect.

[20] Sup. n. 14; cf. *Restatement*, sup. n. 16. Sec. 18.

on a French commercial vessel that had on the high seas collided with a Turkish vessel, killing certain Turks on the latter. The basis of the decision was not the "passive personality principle"[21] but the "objective territorial principle",[22] that is, effects produced on Turkish territory.

While it is generally outmoded as to the territory principle in respect of high seas vessels cases,[23] the *Lotus Case* is the basic authority for the "effects doctrine", i.e., that a state may attach legal consequences under its national law to defendants properly before its courts as to conduct outside the territory that produces significant effects within its territory.

During the gestation of the American Law Institute's[24] *Restatement of the Foreign Relations Law of the United States, 1956-65,* a determined effort was made by lawyers for international oil companies to deny the application of the "effects" doctrine to the economic consequences within national territory of an externally based private sector cartel. Nonetheless the authors of the Restatement (with the imprimatur of the Institute) prevailed in stating, on the basis of the best available

[21] The various possible bases of jurisdiction to attach legal consequences to conduct (legislative or prescriptive jurisdiction of a state) to a defendant properly before the tribunals or agencies of a state (judicial or enforcement jurisdiction) are listed and appraised as to the *consentio juris in Harvard Research in International Law: Jurisdiction in Respect to Crime,* 29 Am. J. Int. L., Suppl. 1, 435-445 (1935).

[22] Cf. RESTATEMENT, id., n. 20.

[23] The notion that a commercial (or even a naval) vessel of a state is a floating island of that state has generally been dismissed as overly fanciful, and the basis of a state's authority to make the law for a vessel is placed upon the nationality principle. In any event, the result of the *Lotus Case,* criminal liability of an officer of a flag of one state in the courts of another for a high seas incident involving a vessel (and its cargo, crew and passengers) is specifically rejected by Article 11 (1) of the Geneva Convention on the High Seas of 1958, 450 U.N.T.S. 82.

[24] The Institute is not a governmental organization. It is a voluntary, private association of practitioners, judges, and law professors sharing a common interest in the improvement and growth of the law. The "restatements" are efforts to state bodies of law that in the United States dereign from judicial decisions as well as statutes, in semi-code form. The "restaters" are required to "find" the law that is (*lex lata*) and may not propose what should be the law. However, some latitude is allowed when there are two or more identifiable trends in the decisional law. Under these circumstances the "reporters" (authors) are permitted to suggest the preferable trend as seen in legal science (because, it is assumed, such a trend will prevail). The Assembly of the Institute, however, finally controls such choices by vote.

evidence from state practice, a principle of consuetudinary international law that did not differentiate physical and economic effects. Section 18 of the Restatement applies to both, although the variables stated in the section may be of greater negating effect in some instances as to economic effects than as to the shooting of bullets or the sending of poisoned chocolates across frontiers. The Section reads:

Jurisdiction to prescribe with respect to effect within territory

> A state has jurisdiction to prescribe a rule of law attaching legal consequences to conduct that occurs outside its territory and causes an effect within its territory, if either
>
> (a) the conduct and its effect are generally recognized as constituent elements of a crime or tort under the laws of states that have reasonably developed legal systems; or
>
> (b) (i) the conduct and its effect are constituent elements of activity to which the rule applies; (ii) the effect within the territory is substantial; (iii) it occurs as a direct and foreseeable result of the conduct outside the territory; and (iv) the rule is not inconsistent with the principles of justice generally recognized by states that have reasonably developed legal systems.

It was foreseen by the writers of the *Restatement* that trends already discernible in the national laws of other countries as to economic effects would eventually lead to problems of the resolution of conflicts of the regulatory laws of different states where the law of no one of these states would be invalidated by general international law. Thus principles for the resolution of such conflicts are also stated, particularly at Section 40.[25]

The *Restatement* viewpoint has prevailed in the developed world. The antitrust laws of Germany, specifically, and of the United Kingdom, inferentially, do not stop at the national boundaries, if significant economic effects come into the territory. The Commission of the European Community has specifically relied

[25] Section 40 states it as a rule of customary (general) international law that an enforcement authority in one state, where there is a true conflict of jurisdiction with another state, must evaluate in good faith the respective basic interests of the two states concerned, and moderate the application of the forum's law when the effect of the evaluation points to greater governmental interest in the other state.

upon the economic effects doctrine to extend the reach of Articles 85 and 86 of the Treaty of Rome to acts outside the community territory that produce market-restricting effects within it.[26] The Community Court has upheld this notion in some cases[27] and has relied upon a parallel rationale in others.[28]

There seems little doubt, therefore, that consumer states finding themselves seriously damaged by the massive economic consequences of state export cartels have legislative jurisdiction under international law to reach such conduct as to defendants properly before their tribunals. Such defendants include foreign states and instrumentalities engaging in non-governmental activities.

It does not follow that damaged states will make use of their authority under international law if other means for adjustment as between the oil producers and themselves are available, for to take advantage of local sanctions that international law authorizes is an act certain to trigger confrontationalist responses from OPEC members. Nonetheless, it would be undesirably complacent for it to be generally assumed that state export cartels are invulnerable under existing customary international law. However, this is an instance in which the very existence of legal rights that *in extremis* may be asserted has a potentially destabilizing effect if too easily resorted to, instead of being used as an argumentative variable in the search for accomodations through negotiation and/or the substitution of new rules of positive international law (through law-making multilateral treaties).

Likewise, it would be counter-productive for the export cartel countries and their supporters in the Fourth and Fifth Worlds to assume that existing customary international law, such as that just described, can legally be set aside on the strength of majority votes in the General Assembly for propositions, such as those of the "Charter" on Economic Rights and Duties of States, that purport to proscribe all counter-action against states members of an export cartel. Admittedly, the world has before it a very serious problem as to the determination of the *consentio juris*

[26] Commission Decision in the *Dyestuffs* Case, Sup. n. 5.

[27] *Begelin v. Commission,* Recueil.

[28] That the antitrust violator is a corporation within the community controlled from outside the community and hence that community antitrust law may be applied to the controller, if properly brought before Community authorities, Court decision in the *Dyestuffs* Case, Sup. n. 5.

under present circumstances; but it is not to be expected that a well-established principle of general international law, one that has not been rejected in the past by any significant group of writers or number of states, can be done away with by the simplistic semantic device of mis-labeling a General Assembly recommendation as a "Charter".[29]

That OPEC and similar state-owned or controlled export cartels are not invulnerable to the reach of national law in economically affected states does not demonstrate that the consuetudinarian legal order contains within itself the bases of resolution of fundamental problems of equity and justice. Quite the contrary! A positive resolution of the present contradictions surrounding the concept of a world market economy on the one hand and the wide differences in enjoyment of the world's resources and opportunities on the other is urgent.When the need for resolution is felt and the politico-social decisions that must come are made, new law and new institutions created by law will begin to function, and both vested advantages of long standing in the old —rich world and the cartelization effort to create countervailing vested advantages in the new— rich world will fade away. Otherwise the planet is on collision course with itself.

III. *Toward a new positive law of distributive justice*

The widespread support that export cartels have received among developing countries as a whole strongly suggests that states other than those that stand immediately to benefit from the power and the high profits that a viable cartel (such one for oil) provides are approaching desperation in their efforts to induce or force more equitable allocations of goods, services, and opportunities. Of OPEC itself, it is highly doubtful that in its inception or so far much in its operations, the oil producers' cartel has been directed principally toward planetary distributive justice.[30] But have-not

[29] Sup. n. 5.

[30] OPEC began as an association of producer states desirous of exchanging experience and "know-how" as to dealings with the major oil companies. Eventually it achieved its present functions. For information on the development assistance activities of OPEC countries, see the contributions by Weintraub, Stanley, Jackson, Akbar, and Armstrong in an American Society of International Law and American University Law School publication, *A Symposium on Primary Resources Scarcity Effects on Trade and Investment*, 24 Am. U.L. Rev. 1087 (1975). Important

states, nonetheless, emotively support the cartel approach to greater equality.

Viewed from the standpoint of the developing (or "poor, poorer, poorest worlds") this essentially countervailing power approach is not unlike the "beggar-thy-neighbor" policies of the developed world during the trade crisis of 1929-1939, when the only solution seemingly available to an economically beleaguered state was to take offensive but negative counter-action. Cartels, like high tariffs and prohibitory non-tariff trade barriers, are antithetical to effective functioning of the global market. They are atavistic as well as restrictive.

And these evaluations, I submit, as being beyond ideologies. Socialist states in theory substitute planning for the market. But non-socialist states also plan. Putting to one side the reality that, notwithstanding doctrine, socialist states have not been able to eliminate the market domestically (either white or black), the market is absolutely essential to international exchanges so long as there is no overall, effective substitute, i.e., a world-wide planned economy. And, of course, there is little doubt but that certain well-known socialist states would be in the forefront of opposition to a notion so antithetical to national state "sovereignty".

Three important realities that have come into sharp focus of attention should be seen in relationship to each other. These are (i) the rich nations –poor nations syndrome (including the gap that grows instead of narrowing); (ii) the globalization of economic activity through transnational enterprises, public and private; and (iii) the raw materials exporters' drive for price "parity" with exporters of manufactures.

The globalization of economic activity (ii, above) is inevitable if human society in any civilized form is to continue on this planet. The present so-called multinationals, however, are only a primitive and still largely unacceptable response to the demands of globalization (i). Parity (iii) is a goal worthy of development objectives

econometric and substantive evaluations of OPEC country contributions to the development needs of poorer countries is contained in various studies of the World Bank Group and of the International Monetary Fund. There is considerable evidence of lack of developmental purpose "evenhandedness in the statistically slight contributions to development by OPEC countries so far". Venezuela has attracted attention by its generalized proffer of financial assistance to other developing countries for the initial financing of structures designed to achieve parity and stability in the pricing of non-manufactured exports by certain developing countries.

but the search for parity in use of the economic force of the territorial sovereign to command the market is a primitive and largely unscientific approach to parity. There are several reasons for this conclusion:

(1) The enhancement of the economic power (disposable income parity in hard currencies) of the oil-producing states does not as a matter of law (or even of political expectation) have to spread to the non-oil producing poor states. At the present time the OPEC seekers of parity deal only *ex gratia* or whimsically or on religious or political grounds— with their brethren of the rest of the developing world. What is missing is obligation to share, just as this element is also missing in the development assistance relationships between the old-rich world and the developing countries.

(2) The experience of the developed world with quests for parity between industrial and agricultural sectors in the domestic economy has been extensive, and it has shown that the struggle for parity cannot for long be managed unilaterally, i.e., by the parity-claimants.[31] The time has always come when unilateral efforts to establish the principle of parity have had to be succeeded by overall administrative authority. Essential notions of social justice require no less, for users have interests too; and hence some impartial force must balance their interests and those of the original mobilizers of the counter-force. OPEC, surely, cannot be the end, but only the first beginnings, of a quest for managed social justice on the transnational front.

(3) In the case of rapidly depleting liquid hydrocarbon energy resources —and fairly soon for some others, such as uranium— "price isn't everything". There is the Good called *provident use* to be stated normatively and policed. There is also a "for us—for our progeny" division of enjoyment to be enforced. It is beyond reasonable expectation that the fortuitous circumstance that this or that state is the source of a vital global energy resource is for all time to be accepted as the unquestionable basis of that state's authority to make such decisions as these. That latter-day ad-

[31] This principle is clearly seen in the history of the struggle of labor in market economy states for collective bargaining rights, the demands of ethnic groups discriminated against in democratic societies, and the efforts of women for equality with men. Social and economic pressure of a unilateral nature initiates the process but its culmination is in the institutionalization by law (through new norms and new administrative modalities) under which both sides are represented.

monisher of us all, the Shah of Iran, probably speaks ineluctable truth when he says, "Gentlemen, the days of cheap oil are over"; but he loses his television audiences when he launches into his strictures on abstemiousness—for others, of course. The world simply will not accept effective governance in which it does not have some sense of participation. The sheiks and bureaucrats of OPEC will not be permitted to make "laws to rule the whole world" from a base in oil.

The urgent and contemporary reality first stated, that of the unmet challenges of inequality on this small planet,[32] is the one among the three listed above that must tell us what we must do as to the other two. Abraham Lincoln said that the United States could not exist half slave and half free. Nor can the world of human beings exist half satiated and half starved. The single greatest challenge facing the species is the attainment of that minimum of human decency, the disappearance of absolute and ignominious inequality.

The way out of inequality is development, *total development:* social, political and economic. Development cannot be achieved without mighty capital transfers, although these alone cannot ensure it. Only the wills of peoples can do that, but determination and intention is no longer enough for most developing countries.

Capital for development can only be obtained by the deferral or abandonment of alternative uses by the suppliers of such capital. States must eventually be taxed for development upon an ability to pay basis. The developing countries are right to quest for the creation by positive international law of a *legal obligation* to contribute to development. But they must seek this obligation of all states, including OPEC states and other cartelizing states. The Fourth and Fifth Worlds ought not to ignore for emotive reasons the opportunities and alternatives open to them. The old-rich world, led by the American Secretary of State, has had much to say, since OPEC showed its power, about "inter-dependence". Elaborate proposals to broaden tremendously both the capital available and the modalities permissible for development assistance through multilateral entities have been proposed. These proposals

[32] Cf. Oliver, "Unmet Challenges of Inequality in the World Community", in *Owen J. Roberts Memorial Lectures,* University of Pennsylvania Press (1976). The lecture was given in 1969 and originally published in Univ. of Pa. L. Rev. (1970).

have their deficiencies. They, too, are primitive; but as in the case of the first steps toward trade liberalization, they are forward-looking and essentially affirmative.

A good first step would be to negotiate the end of export cartels in the context of the acceptance of a positive law of development assistance. This would also be a stong first step along the path to planetary justice.

Comments on Professor Covey T. Oliver's Paper

César Sepúlveda

The paper prepared by Professor Oliver gives rise to a number of comments since with a unique knowledge he deals most interestingly with highly important matters, from the industrialized countries' point of view.

A first comment which the paper suggests to me is that it is difficult to establish parallelisms between cartels of private interest and the producers' organizations such as OPEC, and that for this reason I believe that neither the notions nor the treatment destined to them can be applied in their case. Certainly, the *raison d'être* of associations of raw materials producers is not to eliminate competition, as the case is of other entities, nor to obtain profits, but to defend a vital resource which is the only and the most important source of income, a source that must be preserved and taken a maximum advantage of, because it implies the very survival of the State, the fulfillment of the basic needs of the population.

The fixing of a price for this resource is not made arbitrarily, nor to obtain an undue exploitation of the consumer, but in response and adjustment to a price determined by forces external to the producing State, without consideration of its interests. Let us recall that the petroleum companies, before transferring these resources to the State, established the world price at their convenience. OPEC countries insist that the price fixed is the real one according to world purchasing power.

Another characteristic that should be taken into account is that the price determination and the choice of buyers has been made in many cases *vis-à-vis* countries that are producers and consumers at the same time, that are in a position to compete with those prices, with a technical capacity to control distribution and demand. One more is that the buyers of petroleum are precisely private enterprises in control of marketing, so that they would result co-partners in the so-called "monopolistic conspiracy".

On the other hand, the price and the choice of buyers constitute an expectation and a dissatisfaction with the established order. At least, without the *consentio juris* of the majority or of everyone to adjust that order considered sacred by others, it is legitimate to establish a price leading to the creation of a more general, fair, equitable system.

Moreover, the action of oil producing countries is not entirely arbitrary, but it is naturally, consciously, subject to opposite actions of the affected state, e.g.: economic and commercial reprisals, or of some other sort, as has been occurring, e.g. with the Foreign Trade Law of the United States in January 1975, or in respect to foodstuffs, all of which leads to adjustment.

For those reasons I am inclined to believe that it is not feasible to apply to the producers' associations the antitrust laws, because they are beyond the basic assumptions of such legislation, without excluding that the immunity rules are applicable to them, and others contained in the so-called "Doctrine of State Acts".

These actions should be contemplated rather —in my view— as new forces that should be taken into account in order to establish the new general international law, acceptable to all and meeting emerging needs, hopes and interests of young and weak countries. Only in this way would it be possible to achieve the ideal of complete distributive justice.

Another comment is the reluctance which I seem to perceive in the paper to name the Charter of Economic Rights and Duties of States as a "Charter" and to consider it as an instrument to contribute to the solution of the confrontation between OPEC and its opponents. It was certainly not with the purpose of making it more valid in this way. What was proposed when launching it —by President Echeverría— was the elaboration of a "document with entire juridical validity, able to define clearly which are the duties and which are the rights of States in the economic field". The designation "Charter" is in no way inappropriate, since what was achieved was an inclusive instrument which gathers in an orderly and articulate manner, the hopes of all or a majority of countries to reduce anarchy, abuse, and exploitation and to regulate in this agitated world the economic relations between States.

In practice, it is a document of great importance, that acts as a constitution and therefore unquestionably deserves to be named a Charter, which it has received without objection. The merit of the Charter consists in that it assembles what exists, what is scattered

and presents it in a consistent way, in a harmonic overall, in a unique body.

The Charter is not legislated law. The new part is really brief. In the Charter there are principles taken basically from the United Nations Charter, and the Charter of the Organization of American States. In the Charter there are interpretations of past rules and the reaffirmation, with some elaboration, of existing principles: it contains a codification of other United Nations resolutions. In this document are included once again —nourishment for internationalists— known principles with some elaboration. In some parts of the Charter, customary norms are once again consolidated. Recommendations and demands upon international organizations are also ratified.

What is really new in the Charter, and answers the need to regulate new matters, are Article 2, (b), Article 6 on world trade in basic commodities, Article 14 on liberalization of world trade, Article 15 on disarmament, Article 19 which reaffirms the generalized system of preferences and, of course, Article 5 on producers' organizations, which seems to worry Professor Oliver.

It should be recognized that the Charter is the most serious and profound effort toward the regulation of economic relationships. It is far from being a perfect instrument, but it is the most complete that exists. It constitutes the "model of tomorrow's world economic order", an action program projected to the future. Its enormous function as catalyzer of present economic relationships should not be disregarde as a means of arriving at better forms. It should be recognized, besides, that there is no better substitute for the Charter in the predictable future.

These considerations about the Charter lead me to another pertinent comment: the so-called "revolutionary creation of international norms", but which more modestly could be called the new process of formation of norms, different from classical norms as found in treaties and conventions.

The Charter of Economic Rights and Duties of States is the consequence of an adjustment of opposing forces. It is the best result of a confrontation of interests, of ideologies, of systems, and though it is not an ideal outcome, it is the most approximate to a general, desirable, and one could say, almost definite solution.

The Charter, in my understanding, is the closest expression to what the practice of States is, and answers the present needs of the international community in the field of economic exchange. We

can assign to it without fear the nature of a juridical formulation, evidence of a general practice. It is clear that for traditionalists —what we lawyers are intuitively— this new source is of some concern, but we should recognize that the production of rules by resolutions of the General Assembly is highly valuable, and responds to a process of adjustment which will have to be improved with successive application, until the final perfection of the rule. Further, it is an active and living procedure, different from the slowness and uncertainty of other methods.

I should like to refer to the problem that apparently emerges from the application of Article 5 of the Economic Charter, in which there seems to be an imbalance between the assertion of the rights and the denial of duties, as Professor Oliver points out. I believe that this rule should be understood, apart from considering it in the entire context of the Charter, in connection with Article 24; it is a general prescription establishing, of course, duties such as that of conducting mutual economic relations in order, in such a way that they take into account the interests of other countries as a guiding principle.

Finally, I consider that we lawyers have a great responsibility in this matter of adjustment between producers, producers-consumers, net consumers and other interested actors. We are facing a new situation, in which no customary law is valid, that on the other hand could not be valid because of having been established without the participation of new actors. I totally agree with Professor Oliver in that it is urgent and necessary to find more appropriate norms and systems to solve the antinomies and establish what is most approximate to general justice. But for that some concessions are required; and the old positions, now under attack, are no longer tenable.

The question is that, from my point of view, lawyers —and with them political theorists, economists, diplomats acting as a team— should elaborate harmonic bases to regulate, in this case of producers' organizations, the facts of a symmetrical economic interdependence existing now in the world. A multilateral framework of cooperation is required between raw materials producers and the owners of technology markets, together with States that may balance the situation. In this task, it is very important that the larger developed countries act with patience and understanding.

Toward the New International Economic Order.
An Appraisal of UNCTAD IV*

Samir Amin

During the whole month of May 1976 the representatives of 120 Third World States have once again vainly tried to obtain from the developed countries a few modest concessions concerning raw materials prices, the conditions of access to the markets for manufactured products, the terms for repayment of foreign debt and the modalities for the transfer of technology. The global rejection of these highly timid demands, barely concealed by the last-minute voting of anodyne "compromise" resolutions, repeats the failure of the three previous conferences of Geneva (1964), New Delhi (1968) and Santiago (1972).[1] It clearly expresses the West's intention of accepting nothing which can translate into reality the principles of a "new international economic order", which was first boycotted and then accepted in the inoffensive form of a "Charter" —a catalogue of pious hopes.

Having obtained political independence, the Third World is now launched in a fight for economic independence which, as seen by the vast majority of the States, involves the transformation of the international economic order and, first and foremost, the transfer of the control of natural resources from multinational firms to the States and a substantial increase in the prices of raw materials. Are these goals realistic, and under what conditions can they be achieved?

It would seem to be self-evident that, as prices apparently result from the "laws of the market", it is necessary to act on the conditions of the market. It has long been known that a producers' organization, by acting on supply, can substantially raise prices and

* This requested paper did not arrive in time for its discussion in the Seminar on Consequences and Alternatives of the New Energy Situation.

[1] *UNCTAD III - A critical appraisal,* IDEP/ET/2463.

incomes. Thus, in the developed countries the monopolies which control production and distribution act on both ends of the chain: by imposing the price they want on the consumers and by dictating their conditions to the suppliers of raw materials. Moreover, more than a third of world trade now represents "exchanges" internal to the multinational firm, and the "prices" at which these exchanges are accounted are set in relation to the global strategy of maximizing the profits of such firms. If the monopolies in the developed countries can thus determine price rises for manufactured products without "consulting" the developing consumer countries, why should the latter have to "negotiate" in order to raise their own prices? Cannot they obtain that result by organizing themselves into producers' associations?

The results recorded by OPEC have stimulated awareness of these possibilities. True, the structure of the system is such that OPEC has been operating under particularly favourable conditions: zero substitution in the short and medium term, zero elasticity of demand, monopolization of oil exports by a limited number of countries, etc. . . Besides this, the producer countries have been able to exploit the current economic situation, the clashes between the United States, Europe and Japan, and to combine their economic and financial strategy with political objectives.

The fact remains that results —though probably with more difficulty— can be obtained by the same means in other sectors of the front. The idea of a "solidarity fund", for the purpose of supporting the producers' associations engaged in the price war, which was put forward at the meeting of the 77 held in Dakar in February 1975, falls within this strategy. For the producers' associations are in danger of being confronted with "retaliatory measures" and various pressures aimed at whittling down their impact. Many Third World countries, whose public finance and balance of payments are too vulnerable, cannot resist these pressures without foreign financial help. A solidarity fund constituted with this in view can only be financed by the developing countries; you do not ask those whose interests are opposed to your own to support you in combating them! This fund should therefore be financed by payments from countries which have already obtained a substantial rise in their prices, first and foremost the OPEC countries. This formula is the only one which really corresponds to a programme of solidarity in action: an extension of a solidarity manifested on the political plane to the struggle for economic independence.

It is true that the contributions of the OPEC countries to aid are already large (1.9% of the GDP of these countries in 1974) and far higher than those of the countries of the "North" (0.3% of their GDP). But so far the OPEC countries have been replacing the northern countries without changing the nature of the "aid" process, which is rightly criticized.

It is precisely this type of solidarity fund and producers' associations that the North wishes to prevent by all possible means. For this strategy not only enables a general rise in prices, but also a price stabilization by means of an efficient indexing, and constitutes the basis of a real control of natural resources. The latter implies more than mere nationalization, which is only a basic pre-condition and which, nowadays, has become "acceptable". It implies the regulation of their exploitation in relation no longer merely to the demand of the developed countries, but to the future needs of the Third World. But this objective can only be attained by means of an overall policy on the part of all the producers' associations; and indeed that is also the best way of acting on prices. Despite all the speeches about concern for natural resources, the West pays no heed to this legitimate desire to control the resources and prefers to continue its lucrative robbery. This is in any case the obvious aim of the proposal of an International Resources Bank made by Kissinger in Nairobi.

Between the Dakar declaration and the Nairobi resolutions, the idea of a solidarity fund has been gradually eroded, to be replaced by the inoffensive idea of a stabilization fund financed jointly by the producers and the consumers. The ideological preparation of this clever substitution was organized around the theme "negotiation without confrontation". The Manila declaration had launched the 77 on this doubtful path, while the UNCTAD Secretariat had prepared a modest "integrated programme" in this connexion. It is obvious that a stabilization fund without any action on output by the association will either go quickly bankrupt or at best will "stabilize" around a falling trend in the comparative real incomes of the producers: in a word, it will "stabilize" super-exploitation and poverty!

Why, under these conditions, has the North not subscribed wholly to the Manila proposals and those of the UNCTAD Secretariat? It certainly seems that the monopolies, whose rate of profit was seriously threatened by the crisis and worsened by the victorious offensive of the oil producers, made a preliminary at-

tempt to redress the situation by increasing the exploitation of the workers at the centre of the system, through inflation and the policy of recession aimed at creating once again a reserve margin of unemployed. But this strategy requires first of all that the working class in the centres be brought to heel; otherwise it might well entail a radicalization of the struggles. Hence, meanwhile, the monopolies preferred to throw the whole weight of the crisis on to the periphery, i.e. to refuse any concession, even an extremely limited one. From this angle, the roles were distributed for the Nairobi conference according to a pre-arranged scenario. The Germans, who have hardly any public opinion other than a "right-wing" one, repeated for weeks on end the ideological refrain praising the virtues of "spontaneous" supply and demand (ignoring the existence of their monopolies). The Norwegians, on the other hand, supported the stabilization fund which the Third World decided to create, "alone" if necessary, thus launching the major manoeuvre which was to lead to the final resolution. This resolution merely provides for the pursuit of negotiations by stages with a view to taking final decisions by the end of 1978 on the goals and modalities of operation of the Fund. Even here the United States found it expedient to weaken the impact of these negotiations still further by express reservations.

The Third World scarcely obtained more in the other fields. Tired of "appealing" for an "aid" which is on the decline, the States of the group of 77 thought it more useful to try to obtain a reduction of the burden of their foreign debt. There again they only succeeded in having the question placed on the agenda of the Paris negotiation, which last April was in danger of not reopening. Yet if the balance of payments deficit of the non-oil countries of the Third World rose from 9 billion dollars in 1972 to 35 in 1975 and 100 expected for 1980, the best way of reducing the burden is obviously to impose a rise in export prices. There is little likelihood of a reform of the international monetary system which could solve the problem by establishing a "link" between the issue of special drawing rights (SDR) and "development".

With regard to the transfer of technology, when the draft imperative code of conduct which they submitted had been rejected, the 77 accepted a vague promise of a revision of the Paris convention on industrial property; just as they ultimately accepted no less vague promises concerning access to the markets of the rich countries for their exports of manufactured products, and the

usual pious hopes concernig the "control" of the multinationals and "a special effort for the least developed countries". True, in theory, export industrialization would relieve the social contradictions in the periphery. UNCTAD, taking up the goals defined at the UNIDO conference held in Lima in March 1975, drew up a list of thirty "labour-intensive" manufactured products the output of which, if transferred to the periphery, could reduce the growth of unemployment estimated at 285 million people for the present Third World, and proposed a system of generalized preferences and a code limiting the non-tariff protections which the developed world uses and abuses so widely. But the fact is that the West is not ready at the moment to accept this "redeployment", although it is highly "profitable" (it would accentuate unequal exchange!), because large sectors of the working class of the centres would also suffer from this and the monopolies must first of all reduce the risks on that side. The alternative —the strengthening of trade between Third World countries— is only acceptable on two conditions: first that the imperialist multinationals be eliminated from the project and second, that the rules of this internal division of labour in the periphery be different from those of pure capitalist profitability, which would accentuate the inequalities within the 77 to the detriment of the "least developed".

But is not this "failure" of the negotiation actually a political victory, which may help the Third World to concentrate more on themes more appropriate both to its immediate and to its long-term interests? An opportunity is offered by the non-aligned summit of Colombo, scheduled for August 1976. Indeed, much can be obtained without negotiations, by unilateral decisions of the 77, strengthened by an organization which stresses their collective self-reliance. These possible victories would prepare the ground for more favourable terms in possible future negotiations.

As regards primary commodities, for example, the setting up of producers' associations and of a support fund is not in contradiction with the possible creation of a stabilization fund. On the contrary, the former initiative would strengthen the effect of the latter. Furthermore, this kind of decision does not require a formal unanimity to begin to be effective: majority groups in certain fields can prime the pump and exert a considerable attraction. The non-aligned, the successors of the Arab-Asian group and then the Arab-Afro-Asian group in the previous stage of solidarity in the independence struggle, have already attracted to their banner some

Latin American and Caribbean countries and have opened their ranks widely to the "77" (now 120).

As regards foreign debt, a decision of principle concerning the modalities of overall relief (conversion of the debt by instalments, according to the burden of the debt in terms of interest, maturity dates and its ratio to GDP and exports), would permit collective negotiation, and would have the advantage of limiting the attempts to divide the countries and the particular pressures on some of them.

Naturally we are more cautious with respect to the access of industrial products to the markets of the North, which will depend on the good will of the multinationals and could hardly become effective except within a long-term strategy for a new unequal international division of labour controlled by the imperialistic monopolies. The same applies to "access to technology", i.e. to a technology which is usually not adapted to the real needs of the peoples of the periphery and has a built-bias towards domination by those who hold the monopoly of it. In this area, rather than pursuing the phantom of a "cheaper transfer", it would be better to have the courage to proclaim the two genuine principles of efficiency in this connexion. First principle: it is recommended that the purchase of "developed" technologies be reduced as far as possible, and it is highly desirable to "filch" them when it is possible and useful. Second principle: it is of fundamental importance to give priority to organizing conditions for the flourishing of creativity with respect to technologies appropriate to the Third World.

These objectives, which lay stress on autonomy and self-reliance both in the national strategies and in that of the whole Third World community, are becoming more than ever feasible, as is the seven-point programme proposed in an article published by *Jeune Afrique* when the Nairobi conference was beginning (issue of 14 May 1976). A technical secretariat of the non-aligned, extended to the 77, could finalize these points. Again, this secretariat would not be "competing" with UNCTAD (which is an international institution, i.e. a meeting-place of the South and the North): it could, by strengthening the cohesiveness of the group of 77, help to provide more clear-cut prospects for the battle for a new, and less unfavourable, international economic order.

The Future of OPEC

Hasan S. Zakariya*

Preamble

In order to assess the future of OPEC, it would be useful to recall in brief, by way of introduction, not only its background and *raison d'être* but also to review some of the current problems and challenges facing it.

As must be well-known by now, the formation of OPEC was both an act of protest and of self-defense. Under the old concession regime, the privilege of fixing the price of crude oil was assigned exclusively to concessionaires, who were under no legal obligation even to consult with their host government – the true owner of this commodity – on this crucial matter. With their fully integrated system of operations, the companies disposed of most of the oil they produced through their own channels; thus the oil was seldom exposed in any real sense to the forces of a free market. In consequence, the price of crude oil which later came to determine the revenues each host country would receive, was to a great extent a bookkeeping device, to be juggled at will, to serve, first and foremost, the interest of that international fraternity. Apart from the intrinsic anomally of such a procedure, the price-fixing privilege was apt to be misused at times to the great detriment of the producing countries. The sudden price cut of 1959 and 1960, which was the immediate cause of the creation of OPEC, was a notable example of the potential danger involved in the unrestricted exercise of this prerogative. OPEC came into being not only as an act of protest against that particular incident, but also as an act of self-defense against further reductions in price.

The *raison d'être* being the price of crude oil, it was only logical that all the endeavours of OPEC, as a forum for consultation and

* The views expressed in the paper are strictly those of the author and therefore have no official standing as far as the United Nations is concerned.

coordination, should have been channelled so far towards that basic and all-embracing target. The initial concern was simple and modest enough: the restoration of the reduced price to the *status quo ante.* Literally speaking, OPEC never succeeded in realizing this initial target, although, ironically enough, it was destined to accomplish, a decade after its inception, something much more spectacular.

OPEC, of course, proved to be too dynamic a creature to confine itself to that modest initial goal. Over the years, it set its sights on wider horizons and tried, with varying degrees of success and failure, to tackle such issues as the expensing of royalty, elimination of market allowances, regulation of production and state participation. Although all of these new objectives had certain intangible aspects such as greater national control over the petroleum industry, the underlying concern was unquestionably the bolstering of the price of oil and the gradual improvement in the tangible cash benefits accruing to each member country from the exploitation of this non-renewable asset.

In its first ten lean and agonizing years, OPEC had little to show in terms of substantial achievement, but these were, nevertheless, very important as formative and consolidating years. The real turn in the fortunes of OPEC came about, as you know, just after its 10th birthday. Emboldened by the remarkable and rather unexpected victory of one of its members, Libya, in a confrontation in 1970 with its concession-holding companies, OPEC found itself all of a sudden in a position of strength where it could embark more confidently on a new course of action and avail itself of the opportunities and initiatives presented by the changed circumstances. Within three short years, starting from the Caracas Conference of December 1970 and culminating in the Teheran Conference of December 1973, OPEC managed to accomplish not only her original goal, but also to surpass it by leaps and bounds. The full story is such recent and current history that it need not be retold in all its fascinating details.

1. *Current threats and challenges*

Now that OPEC is basking in the sun of its remarkable success and has managed to withstand the threats posed by its adversaries, it might seem paradoxical, indeed inconceivable, to cast doubt on its continued viability or to question the security of its future, even on an abstract, hypothetical basis. In spite of this seemingly secure

and opulent position, OPEC survival has nevertheless been of late the subject of much concern to its friends. For menacing clouds have been gathering on the horizon and no sooner have some been dissipated than others have re-emerged. It is therefore submitted that the organizers of this Seminar were justified in placing this topic on the agenda; it is a timely topic which can be discussed here in a constructive and meaningful manner.

Before reviewing the external and internal dangers to the continued cohesion and survival of OPEC, one should first pose the obvious question: if OPEC has achieved most, if not all the goals for which it was created, why does it not start phasing out its work and gradually disappear from the scene? This of course is a simplistic and naive thought; this writer is aware of no occasion on which such a proposition was ever actually advanced by anyone, even only half in earnest.

If the proposition that OPEC has come to the end of the line and should therefore fade away in a natural manner is untenable or at least premature, the collapse of OPEC by a willful act of sabotage or suicide is a real possibility which should be soberly contemplated, no matter how remote it might appear to some at present.

External threats

For all practical purposes the case against the international oil companies is virtually over as far as OPEC is concerned. But the controversy with new and potentially more powerful adversaries has just begun. For more than two years now OPEC countries have been confronted by the major importers of oil, both individually and as an organized group, with vital objectives and policies of their own. Recent OPEC gains have understandably provoked varying degrees of enmity on the part of these major importers and consequently they have been trying to undermine its unity.

Certain major importers have not even attempted to conceal some of the "final solutions" they intend to use against some member countries in case of emergency. This will be contingent upon what they, themselves, would consider "economic strangulation", so-called. These threats of physical force have, of course, been repeatedly disowned, qualified or merely "hypothesized", only to be reiterated in a different form by different spokesmen,

with a view to maintaining the atmosphere of intimidation and confusion fully charged. Although these threats have become rather muted in the last year or so, they have not been totally discarded and therefore can be reactivated at any time, especially if and when the dialogue going on in Paris now becomes deadlocked or collapses completely. An indication of the likelihood of the reactivation of such threats might be the present stockpiling of crude reserves by some major importers.[1] To mention these threats is not, of course, to affirm that they can easily be implemented, or that, even if they are, they can fulfil their basic objectives.

If the threat to revert to old-style gunboat diplomacy were mere rhetoric or sabre-rattling not to be taken too seriously, then there is the other and perhaps more genuine one voiced, perhaps unguardedly, by some that the aim of the International Energy Agency is to dismantle OPEC.

Even if this type of threat were no more than unauthorized loose talk in the context of the psychological warfare unleashed against the oil exporters, then there is still the third, and more subtle threat by some —perhaps more in line with the normal rules of the game— to adopt measures which would shift market conditions in order to force prices down and cause strain and disarray within the ranks of OPEC. This last threat would seem to have been in operation for the last two years and although it fell far short of causing the complete collapse of OPEC, it has succeeded to some extent in causing temporary difficulties and internal tension among its members, as will be shown later.

In this connection, one should not fail to mention, in passing at least, the scheme concocted by the fertile imagination of some well-known academicians with the declared intent, in the words of *The New York Times,* "to sow a little confusion, perhaps ultimate

[1] It is reported that the US is currently engaged in building up an emergency stockpile of up to one billion barrels of oil, at a cost of $14 billion, which is designed to obviate the necessity for oil imports for six to twelve months. According to the *Middle East Economic Survey (MEES)* of 7 June 1976 (Supplement), this measure is viewed in OPEC circles as a "bare-faced confrontation maneuver vis-à-vis the oil exporters". It is to be noted that the press release issued by OPEC in the aftermath of the recent Bali Conference, contains a paragraph which is believed to refer to this matter. It states: "The Conference took note of actions being taken by certain consuming countries against the interests of member countries of the Organization and decided to take appropriate measures, if necessary, to protect the legitimate interest of the Member Countries".

havoc, in the ranks of the 13-nation cartel, the Organization of Petroleum Exporting Countries". According to this scheme, the government in Washington "can tempt the oil exporters to cheat on their high fixed prices by making cheating easier". The way to do it, it is argued, "is to set up a system of secret, competitive bidding for licenses to import oil into the United States". Under a cloak of secrecy, so the argument goes, "first one member of OPEC and then another would effectively cut prices in a bid for a larger share of the United States market". The import licenses would also remove, so the argument continues, the international oil companies as agents that market OPEC oil at stable prices. To make the scheme more effective, "false rumours and other dirty tricks" can be planted to nourish the seeds of suspicion among the OPEC members and to break their discipline.[2]

No matter how much one might admire the ingenuity of those academicians, the petroleum cold warriors, and the frankness with which they have disclosed in public their deep seated hostility towards the oil exporters, one cannot help but question at least the ethics of their espousing such questionably "cloak and dagger" methods.

Another serious threat is the repeated attempts to blame the recent rise in the price of oil for the financial and economic plight of many non-oil exporters in the Third World. These attempts which have been made, for example, before several international fora by high-level spokesmen of some major oil importers are designed naturally to drive a wedge between the two groups among the developing countries —the oil exporters and the rest— and to undermine their historical solidarity.[3] Instead of regarding OPEC as the suspect for their present economic predicament, the countries of the Third World fortunately proved astute enough not to fall prey to these designs and to maintain their traditional solidarity *vis-à-vis* their common adversaries. OPec is being rightly assessed as an "example of success" to be emulated by other developing countries in trying to achieve similar gains with regard to the raw materials they export. In trying to negotiate a new global deal, the devel-

[2] *The New York Times*, 15 September 1976, p. 27, citing a paper circulated privately by Professor M. S. Adelman of M.I.T.

[3] See, for example, the speech given by Mr. H. Kissinger on 11 February 1974 at the opening of the Washington Energy Conference and the two speeches delivered by President Ford before the 9th World Energy Conference in Detroit in August 1974 and the U.N. General Assembly in September 1974, respectively.

oping countries —OPEC and non-OPEC alike— are standing together and speaking with the same voice. It is no mean achievement that they have been able to do so in the face of all outside pressures and intrigue.

Internal tensions

It cannot be denied that, as a result of the new circumstances which the large increase in the price of oil helped to create, OPEC solidarity and unity of purpose have been exposed of late to recurrent difficult tests. Two major problems which pose potential threats to its continued cohesion are the following:

The differential: The fact that oil has suddenly become much more expensive has naturally reduced the level of consumption all over the world, both spontaneously by individual consumers and by deliberate action on the part of importing countries. This inevitable consequence should not only have been anticipated, but even welcomed by all concerned, including the OPEC members, as a step in the right direction towards the conservation and rational use of the world's limited and non-renewable petroleum resources. The current economic recession has understandably contributed also to a shrinkage in the consumption of energy. The fall in world demand for oil, however, has not been as dramatic and far-reaching as one might have expected. Generally speaking, it has been in the range of not more than an average of 10 percent compared with the 1973 levels. There is good reason to suppose that this margin will steadily decline as the western economy gradually recovers from the current recession.[4]

The temporary decline in the demand for oil has, to varying degrees, had its impact on the ability of OPEC countries to dispose of all the oil they produced and consequently it has had a negative

[4] According to the *Petroleum Intelligence Weekly (PIW)* of 10 May 1976, the drop in inland oil demand in 1975 of the three main consuming regions —Europe, North America and Japan— was an average of 8.4 percent from 1973, the last "normal" year. This represents an actual drop of 12.3 percent for Europe, 10.2 percent for Japan, 6.2 percent for the US and 0.2 percent for Canada. "Since 1973, the fall in energy consumption has not been significantly greater than the fall in industrial production provoked by the world recession. With economic upturn now underway, energy consumption is returning towards the old trend line. There has been a disquieting failure of all those grandiose plans announced in 1974 and 1975 to save energy". *The Hudson Letter*, Paris, 19 April 1975.

effect on the annual revenues some of them were anticipating they would earn. This in turn has curtailed the ambitious, perhaps even over-ambitious plans for economic development either already initiated or contemplated since 1974, to the extent that some members have had to borrow large sums on the world market. To varying degrees again, these countries have had to resort to the logical step of cutting their production, with Saudi Arabia probably bearing the brunt of this, quietly and magnanimously. Since this reduction was not successful in completely eliminating all the surplus supply, some members seem to have exercised wider discretion in deciding upon the relative value of their various crude oils, above or below the price of the marker crude which obviously cannot be tampered with. Because of its current importance a brief account of this issue would seem in order.

Crude oil, as is well known, is not uniform in grade and quality. The prices of the various crudes (about 40 in number) differ according to their degree of sulfur content, their weight and viscosity, their geographic location and a variety of other factors. However, the only type of crude which has been the focus so far of the pricing decisions of OPEC is the light Saudi Arabian crude —the so-called "marker" crude— which is now fixed at $11.51 a barrel. Beyond that, OPEC members have been free to set the price of their own different crudes, taking into account the freight differentials, low-sulfur premiums, gravity escalation, etc. The recent fall in world demand, particularly for the heavier crudes, has induced some of the countries concerned to reduce the price of their crudes somewhat to make them more competitive. This was done strictly on an individual basis, either by announcing such a downward adjustment or by *not* fully re-adjusting the price of their crudes in relation to the marker when an increase in the price of the latter was collectively agreed upon, as some other countries were rumoured to have done.

According to repeated press reports, this disparity has been a source of strain within OPEC which has led occasionally to some bitter public recriminations between various members,[5] posing a major internal threat to the continued solidarity and cohesion of the Organization. This was recognized by no less an authoritative body than the OPEC Economic Commission itself which warned

[5] See, for example, the reports published in *PIW*, 7 July and 14 July 1975 and *MEES*, 20 February and 26 April 1976.

of the great risks involved if the practice were allowed to persist.[6]

Whether these recriminations are justified or not, none of the countries involved in the controversy would seem to be at fault, technically speaking at least. If anybody is to blame, it is OPEC itself for failing so far to provide a well-conceived, effective and authoritative formula for regulating this thorny and long-outstanding issue. But as in the case of the regulation of production, OPEC cannot be blamed for lack of trying. It seems that the issue of the differentials and the monumental problems it involves, with the continued change in the pattern of world demand, has proved too cumbersome so far and too elusive to tackle successfully.

Be that as it may, OPEC appears determined to find a satisfactory and workable solution to this vexed question. One of the major items on the agenda of the abortive Conference in December 1975, the Consultative Meeting of Geneva last April, and the Bali Conference of 27 May 1976 was the question of the differentials. It is reported that during the Consultative Meeting, OPEC succeeded in clearing the air and reducing tension on this matter.[7] However, the Bali Conference was unable to settle this question once and for all, although a temporary solution involving a downward adjustment of medium and heavy Gulf crudes by 5-10 cents/barrel appears to have been reached. The Economic Commission, which came up with a proposed schedule of price bands for various OPEC crudes based on what has come to be known as the 'Algerian Formula', was instructed by the Conference to continue its work on this matter and to report to the next Conference to be held in December 1976.[8] It is hoped that OPEC will soon succeed in setting up an acceptable system for determining the relative values of its various crudes —on an OPEC-wide basis — which would be both coherent and flexible enough to respond to changing patterns of demand in the world market.

Further price increase: It must be common knowledge by now that the OPEC countries have not been of one mind with regard to whether the price of crude oil (the marker crude, that is) should be further increased, and if so, by how much and how often. This

[6] *PIW*, 7 July 1975.

[7] *MEES*, 26 April 1976.

[8] The proceedings of the Bali Conference were reported and commented upon by, among others, *The New York Times* of 29 May 1976, *MEES* of 7 June 1976 (Supplement) and *PIW* of 7 June 1976.

issue, which is probably the most critical single one currently facing OPEC, has generated recurrent and regrettable scenes of highly publicised discord over the last year or so.

The division in the ranks of OPEC on this issue has been far from even. As one well-known publication highlighted the situation once, the case is simply "Saudi Arabia against all the rest of OPEC"[9]. Of course, only a giant member in terms of reserves, production capacity and mounting financial surpluses like Saudi Arabia can dare to assume such a lonely stance and get away with it.

Ever since the major price rise in Teheran in December 1973, Saudi Arabia has been trying, with varying degrees of success, to play a moderating role with regard to any further increase. While most of the other members have been in favour of periodical increases to maintain the real value of their revenues which are being steadily eroded by rampant inflation in the industrialized countries, Saudi Arabia alone has been pulling in the opposite direction, towards a total price freeze. Except for the most recent Conference in Bali, where there seems to have been a complete deadlock, the result of this battle of wills within OPEC has often been a compromise of sorts – a modest price increase. Part of the credit for this is due to the unanimity rule of voting, which, incidentally, has been instrumental over the years in preventing fragmentation and the possible disintegration of OPEC.

It is to be admitted, of course, that there is nothing odd in the OPEC members taking different, even diametrically opposed stands with regard to the issue of price, or any other issue for that matter. This is part of the democratic process which should always guide their deliberations and endeavours, and does not therefore, in itself, constitute any serious threat to the survival of OPEC. In fact, the proceedings within OPEC over the decade and a half of its existence have not always been smooth, serene and completely harmonious. OPEC Conferences have been, more often than not, very active affairs indeed. Discussion can be very heated, even acrimonious at times. In spite of that, either a sensible compromise was reached, or the matter under dispute was temporarily shelved or swept under the rug.

The present situation, however, contains a new element which, if not checked soon, might pose a real danger to the continued unity of OPEC. This is the attempt to project a public posture of

[9] *MEES*, 26 April 1976.

complete dominance by one member country or a group of countries over the organization. OPEC friends should not, of course, be unduly concerned about the way some of the recent meetings have been portrayed in the international press, such as, for example, the recent report that "Saudi Arabia has emerged [from the Bali Conference] in the position of virtually dictating the major policy decisions of the group".[10] Obviously such a development, were it to occur, would reflect no doubt the wishful thinking of some outside quarters. But those friends do have a real cause of concern when they come across press reports attributing to the representative of an OPEC member such boastful assertions as "there will be an oil price freeze this year", two months before the Bali Conference was convened, or that "no one can increase without Saudi Arabia" in the aftermath of that conference.[11]

Such utterances, if authentic, are unnecessary, indeed harmful. They are certainly beyond the reasonable bounds of voicing publicly one's own opinion on any particular matter, and would only serve to compound the current internal strains within OPEC, exacerbate its bitterness and sharpen its edges.

Despite the above, the rift within the OPEC over the issue of price increase is not in fact as grave or irreconcilable as it might seem. The divergence between the two sides is not unbreachable. They both agree on the principal; it is only the rather marginal question of how much and how soon which is in dispute. This is evident from the fact that Saudi Arabia has been advocating the freezing of the price not only out of deference to the dialogue going on in Paris now but also to give the big oil importers, who happen to be also the major exporters of manufactured goods, a further opportunity to curb their rate of inflation and the continuously rising cost of the goods and services imported from them by the oil exporters. Should they fail to do so, or if no real progress is made in the present dialogue in Paris, the Government of Saudi Arabia has made it very clear, on more than one occasion, that it will stop advocating any freeze of the price of oil.[12]

[10] *The New York Times*, 30 May 1976.

[11] Mr. A.Z. Yamani, Saudi Arabian Minister of Petroleum, speaking at a press conference in Washington on 14 March 1976 as reported in *MEES*, 22 March 1976, and discussing the outcome of the Bali Conference on 29 May 1976 as reported in *The New York Times*, 30 May 1976, respectively.

[12] See, for example, *MEES*, 4 July and 29 August 1975, and *The New York Times*, May 1976, in which a long interview with King Khalid was published.

2. *The unfinished work of OPEC*

OPEC, which has already completed a decade and a half of its existence, might appear to have accomplished all its goals. We have already indicated that to conclude from this that it should quietly fade away from the scene would be rather naive. This is so, for at least the most simple reason that OPEC still has plenty of unfinished work to do. The following are among the more important tasks which OPEC has yet to tackle successfully.

Indexation: Although its gains with regard to the price of oil have been spectacular and there would seem to be little left to be desired, these gains are actually far from being secure and are being threatened, both directly and indirectly, on more than one front.

The sudden dramatic increase in the price of oil has, as expected, led to a shrinkage in the world demand for oil. As already indicated, this shrinkage, which was due to both the spontaneous and deliberate reaction of consumers worldwide, as well as to the fall in industrial production because of the economic recession, has not been as great as might have been anticipated. Consequently, OPEC has been able not only to withstand —admittedly with a few minor scars— this threat to the new price established late in 1973, but has even managed to increase it by a certain small margin on two or three occasions.

If the direct threat of spontaneous and deliberate energy-saving worldwide has so far proved not so effective in scaling down the price in nominal terms, the indirect threat of world inflation, on the other hand, has been much more effective in bringing about a *de facto* reduction in real terms.

This is an issue on which all OPEC members appear to agree, even those who are calling for a further freeze in the price of oil. Furthermore, there seems little or no dissent within OPEC as to the proper cure for this malady. They all seem to agree that the answer lies in the so-called indexation of the price of crude oil in relation to the prices of a number of manufactured goods exported by the major importers of oil. In fact, price indexation has been one of the preoccupations of OPEC since the sixties and has been the subject of several resolutions, notably the landmark one of June 26, 1968 which contained the first comprehensive statement of policy (Resolution XVI. 90). More recently, OPEC experts

were instructed to consider the matter once more by determining the effect of worldwide inflation on real revenues of member countries and proposing suitable common denominators for an indexing system based on a representative group of imported goods to which oil prices might be linked.

Whether price indexation can effectively be implemented by OPEC countries alone remains of course to be seen. But there is no doubt that this goal can be more effectively achieved through a constructive dialogue with, and the concurrence of, the large oil importers. It is to be hoped that the current Paris Conference on International Economic Cooperation (CIEC) will eventually succeed in removing the obstacles lying in the way of global consensus. Such a consensus would of course settle the controversy once and for all as to whether or not the price of oil should be increased periodically and the extent of such an increase, thus eliminating a major cause of recurrent confrontation and tension between oil exporters and importers. This would also remove a main source of the present internal strain among OPEC members themselves, and would spare them the irritation, indeed the agony of debating, or even fighting this issue out every year or so.

Regulation of production: This is the one single major issue which OPEC has tried for several years in the past to cope with and failed. No other issue has revealed to such an extent the conflict of interests which can exist at times among OPEC members. This is not, of course, the time to review in detail how and why this issue forced itself on OPEC from its early years, nor to trace its development over the years. Suffice it to say that, although a tentative programme to cover two consecutive years in the mid-sixties was eventually ageed upon by OPEC members, most of them felt extremely lukewarm towards the programme and therefore made no serious attempt to implement it.

The fall in world oil demand in 1974 and 1975 and the resultant supply surplus has naturally helped to revive this issue which has been somewhat dormant in more recent years. Early in 1975, three OPEC members sponsored a proposal for limiting output within the OPEC area according to market requirements and apportioning the allowed production among all the members in accordance with their financial needs. The proposal, which was reported to have won the support of most members, failed to gain a consensus due to the opposition of Saudi Arabia. As a result

of the rift on this issue, the OPEC Summit meeting held in Algiers in March 1975 could not, and was not expected to do more than piously reiterate the vague hope in its final communiqué that member countries would "establish close co-operation and co-ordination among themselves in order to maintain a balance between oil production and the needs of the world market".

It should be clear that the regulation of production is being viewed by OPEC now, as in the past, from the purely tactical angle of bolstering the price and sharing the losses of falling demand on an equitable basis. Perhaps one of the reasons why OPEC was not compelled to reach a common stand on this issue last year was the fact that the drop in OPEC output was not so great as to present its members with a serious challenge. It is estimated that the total OPEC output for 1975 was 27.2 m/b, down only 2.5 m/b from the 1974 average of 30.7 m/b. It is thought that OPEC can easily live with even double that drop before the issue of "sharing the losses" of revenues becomes a real problem indeed.[13]

It is to be noted that regulation of production has been envisaged and debated within OPEC mainly as a short-term tactical device to protect the price of crude oil and to prevent harmful, fierce competition for market outlets – a familiar aim which can hardly be assailed. There is, however, another and much more benign aspect to this matter, the long-term strategic one which the oil producers will have to face sooner rather than later, and that is to initiate a well-conceived and equitable plan for the conservation and rational utilization of their limited and non-renewable petroleum resources, for the benefit of future generations of producers and consumers alike. Certain member countries such as Kuwait, Libya and Venezuela have already been awakened to the fact that their oil reserves are being unduly depleted and have therefore set certain ceilings for allowable production in order to prolong the life of their threatened reserves. But OPEC is still called upon to face this issue in a concerted manner. The large oil consumers are also called upon to ponder this issue from the standpoint of their own enlightened self-interest, and to join hands with the producers in the search for a global formula which would be acceptable to all. It is a matter for regret that such a

[13] *PIW*, 3 March 1975, citing Mr. J. Amouzegar, the Iranian Minister.

vital issue is not being given the prominent place it deserves in the deliberations of the current CIEC meeting in Paris.

3. *OPEC viability and the future demand for oil*

It is axiomatic that the future of OPEC depends decisively on the future of petroleum, natural gas included, both as a fuel and raw material. All present indications suggest that petroleum will maintain, at least for the next decade, its position as the primary source of energy. The current efforts to develop alternative sources —commendable as they are— seem to be making little headway and the prospects of any major breakthrough in the near future are somewhat gloomy. Conservation measures in the large consuming areas seem, regrettably, to be faltering after their initial modest success. As a raw material, the demand for this blessed commodity knows no bound; it will be with us as long as oil can be extracted from the ground, permeating thousands upon thousands of manufactured articles to make a better life for mankind everywhere. Small wonder that some people are trying to romanticize petroleum, calling it by beautiful names, forgetting perhaps that it is not petroleum but rather the ingenuity of man that is transforming this black liquid and its invisible cousin into a cornucopia of worldly usefulness and comfort. But that is a different story for now.

Most current forecasts seem to conclude that the western industrialized countries will remain dependent on OPEC oil for the next decade at least. Thus at the north-south dialogue in Paris, the 18-nation International Energy Agency which was set up to coordinate consumer policies, has recently made projections on the basis of moderate economic growth of only 4% a year, with little energy saving, for most countries of the OECD. According to this new forecast, OPEC exports will rise by 23% from their 1974 peak to 35.7 m. b/d by 1985 and can rise even higher, on the basis of 4 1/2% growth rate, by 48% to 49.9 m b/d.[14] Many observers tend to think that such projections are realistic enough.[15]

[14] *The Economist*, London, 10 April 1976.

[15] See, for example, *The Hudson Letter*, Paris, 19 April 1976, which also pointed out that "increased exports at such a rate would, in our opinion, be more than enough to maintain a united front among the oil producers on production policy and prices".

According to another forecast presented to the Paris meeting, world oil consumption, including that of the socialist bloc, is seen as rising from 56.4 billion barrels in 1974 to 72 billion in 1980 and 90 billion in 1985. OPEC's exports will stay high because no other source of energy can meet world demand.[16]

Finally, the president of a major oil company has predicted that, even with new oil production from Canada, the North Sea, Alaska, and other areas, plus favourable energy policies, the world will not be able to dispense with OPEC oil. OPEC countries which now provide slightly over a third of the total of world energy will, according to him, still be called upon to supply about a quarter of the total in 1990.[17]

4. *Future membership of OPEC*

Another issue which might have some bearing on the future of OPEC, is whether or not the present membership should be expanded further, and if so, what types of country should be allowed to become full members. OPEC was created in Baghdad on 14 September 1960 by five countries only: Iran, Iraq, Kuwait, Saudi Arabia and Venezuela. Over the years, eight other countries joined these founder members, so that it consists now of 13 full members. The criterion for eligibility for full membership is enshrined in Art. 7 of the Statute. There are two conditions: the country should be a substantial exporter of crude oil, —substantial is not defined— and it should have fundamentally similar interests to those of existing members. At least a three-fourths majority, including all five founding members, must agree that these two conditions obtain in each individual case.

In certain cases, a non-exporting country, though no a substantial one, may be admitted as an associate member. Although associate members may be invited by the Conference to attend and participate in the deliberations of meetings at all levels, they have no right to vote. At present there are no associate members in OPEC; those countries which were admitted as such in the past have all been quickly promoted to full membership. In the two

[16] *General Analysis of the Energy Situation* (Energy Working paper, Supplement No. 1) presented by Saudi Arabia, 19 March 1976, as cited in *The Economist, supra* note 14.

[17] Howard C. Kauffman, of Exxon, *Oil and Gas Journal*, 20 October 1975.

recent cases, the shift from associate to full membership was achieved with oil production of about 150,000 to 200,000 b/d only. If that rather modest level of production is any guide, then several developing countries can reasonably aspire to membership now or in the very near future, such as Angola, Congo, Egypt, Malaysia, Mexico, Peru, Syria and Trinidad. Other non-Third-World countries may conceivably also present themselves as serious candidates now or in the near future, such as China, Norway, Soviet Union, and the United Kingdom.

Future membership is one of the key factors which might affect not only the proper functioning, but also the continued cohesion and discipline of the Organization. For the sake of this, similarity of interest should be taken to mean that the candidate country should be not only a substantial exporter of oil but also that oil should constitute its basic and principal export. Besides, OPEC is under no obligation —legal or moral— to accomplish universality of membership, even though a fairly good case may conceivably be advanced in favour of such universality. There are other ways to bring about a measure of consultation and co-operation between the two groups —those within OPEC and those without— to their mutual advantage.

So far the device of associate membership has not proved entirely successful. In practice, it has served only as a stepping stone to prompt full membership without any perceptible change in the production capacity of the country concerned. OPEC should certainly reconsider this question soon. Associate membership should either be abolished altogether, thus removing this "sneaking", and at times even embarrassing, entrance into full membership, or it should be more rigidly institutionalized as a completely distinct, and more permanent category of membership with no automatic guarantee to move into the other category.

While all the foregoing would apply to all potential oil-exporters regardless of their political and socio-economic status, it should apply even more forcibly, *à fortiori,* to those countries outside the Third World. It is no accident that all the present members of OPEC are developing countries belonging to the so-called Third World. This is a basic characteristic which has its deep roots in the historical circumstances and controversies which led to the creation of OPEC. It is in the interest of maintaining cohesion and harmony within OPEC that this basic characteristic should always be jealously guarded.

It is not certain, of course, whether any of the developed countries mentioned above, once they achieve the status of a substantial oil exporter, would seriously wish to join OPEC. Some recent and rather half-hearted, if not half-joking statements[18] not withstanding, this eventuality would seem at present a purely hypothetical one. Their political status and alliances might well prove incompatible with OPEC membership. Besides, OPEC membership would not probably offer these developed countries much additional tangible advantages over and above what they are getting now or would get in the future, as a result of the universal application of OPEC prices to members and non-members alike.

Since the controlling factor in deciding whether to grant or deny new membership is ultimately the rather stringent rule of the three-fourths majority, including the unanimous vote of the five founding members, the likelihood of a country not fully qualified, from one standpoint or another, being admitted would seem rather remote. Nevertheless, OPEC would do well at this juncture to reconsider this matter in depth with a view to setting better defined guidelines for the days to come, instead of dealing with it on a purely *ad hoc* basis, as is the present practice. It is submitted that by adding the words "basic and principal" to the word "substantial" in Art. 7-C of the Statute, as already indicated, the prospect of non-Third World countries becoming eligible for OPEC membership would be much more unlikely.

[18] "The question of the United Kingdom being a member of OPEC is no longer humorous but a strong possibility", Mr. Harold Wilson, Britain Prime Minister, at the Rome Conference, 2 December 1975.