Oil and the Gulf War

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No Blood for Oil! The rallying cry of many of those who took to the streets in protest against the Gulf War is simple. Is it too simple? "Even a dolt understands the principle," said one unnamed US official, "We need the oil. It's nice to talk about standing up for freedom, but Kuwait and Saudi Arabia are not exactly democracies, and if their principal export were oranges, a mid-level State Department official would have issued a statement and we would have closed Washington down for August."

To be sure, no conflict is one-dimensional. Some in Washington welcomed the crisis to demonstrate that the US still has a clear advantage over its economic competitors: military power. The military has tested its new weapons under realistic conditions, and the political leadership is glad to bury the "Vietnam syndrome." The conflict also deflected attention from domestic difficulties with a rousing foreign adventure.

Nevertheless, this war was about oil—access, prices and profits. US intervention needs to be seen against the background of an ongoing transformation of the world oil industry. Since the first signs, some 20 years ago, that the oil producing nations of the Third World might manage to assert greater...
control over the exploitation and pricing of their oil resources, the major international oil companies have shifted their capital spending and oil exploration efforts to the United States, the North Sea, and other politically safe non-OPEC areas. Some Western governments initiated programs to develop alternative energy sources. In the 1980s, the scales of power tipped away from OPEC. By 1985 OPEC’s market share of global production was 30 percent, down from 54 percent in 1973. Its ability to influence prices was minimal.\(^2\)

This strategy could not be sustained indefinitely. The growth of non-OPEC production has tapered off in recent years. The price crash of 1985-86 proved to be a turning point of sorts. It forced greater cohesion on OPEC’s members, and also made expensive non-OPEC production uneconomical. Non-OPEC output in the capitalist world, after peaking in 1985 with 44 percent of global production, declined to 39 percent last year (Table 1). OPEC’s capacity utilization went up from around 50 percent in the mid-1980s to 90 percent in 1990. OPEC’s share of the world oil market is expected to climb from a current 39 percent to around 50 percent by 1995.\(^3\)

This turnaround reflects underlying realities: the OPEC countries worldwide possess 74 percent of the world’s known oil reserves. Those in the Gulf account for 62 percent. The world’s largest consumer of oil, domestic production, steady from 1975 to 1985 thanks to Alaskan oil fields, is now in steep decline.\(^5\) As a result, imports are ballooning and their composition is changing. During the first half of the 1980s, supplies from Mexico and the North Sea displaced OPEC oil in the US. The Gulf producers now account for 28 percent of all US imports, up from 7 percent in 1985 (Table 2).

### Loyal Producers

A core of Gulf oil exporters is thus pivotal for the supply of oil to the world economy. This is a key reason for Washington’s intervention in the Kuwait crisis. In addition to the increasing dependence of major consuming countries on the oil deposits in the area, important ideological and practical affinities between the Gulf monarchies and the West make that reliance tolerable. Faced with rising oil import dependence, the Bush administration has made a strategic decision in favor of shoring up its Gulf allies militarily even while opposing policies at home that would constrain the American appetite for energy.\(^6\)

These countries—Saudi Arabia, Kuwait, and the United Arab Emirates—have by far the most extensive oil reserves in the world, rivaled only by Iraq and Iran, and the ability to expand production capacities to meet growing world demand.

### Table I. World Oil Production

<table>
<thead>
<tr>
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</thead>
<tbody>
<tr>
<td>Western Non-OPEC</td>
<td>29.2</td>
<td>32.7</td>
<td>43.8</td>
<td>39.4</td>
</tr>
<tr>
<td>United States(^1)</td>
<td>18.7</td>
<td>16.2</td>
<td>18.3</td>
<td>13.6</td>
</tr>
<tr>
<td>Western Europe</td>
<td>0.8</td>
<td>3.9</td>
<td>6.9</td>
<td>6.1</td>
</tr>
<tr>
<td>OPEC</td>
<td>53.5</td>
<td>43.7</td>
<td>29.9</td>
<td>38.8</td>
</tr>
<tr>
<td>Gulf states(^2)</td>
<td>36.3</td>
<td>29.9</td>
<td>18.9</td>
<td>23.3</td>
</tr>
<tr>
<td>Centrally-Planned Economies</td>
<td>17.4</td>
<td>23.6</td>
<td>26.3</td>
<td>22.2</td>
</tr>
<tr>
<td>World Production</td>
<td>58.5</td>
<td>62.8</td>
<td>57.6</td>
<td>65.3</td>
</tr>
</tbody>
</table>

\(^1\)US share includes natural gas liquids.
\(^2\)Including Oman, a non-OPEC state.


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They have an interest in maintaining relatively low oil prices to secure long-term markets for their resources, whereas the more populous OPEC countries—Nigeria, Indonesia, Algeria, Iran and, to a degree, Iraq—are hard pressed to finance an array of civilian and military needs and to pay off foreign debts. Higher revenues over a much shorter stretch of time are in their interest.

Kuwait and Saudi Arabia both have invested a substantial part of their petrodollar surpluses in Western countries. Kuwaitis acquired controlling or minority holdings in a large number of companies, while Saudi Arabia primarily invested in bank deposits and government bonds and securities. Declining oil revenues have forced Saudi Arabia to draw down these deposits for much of the last decade. Today they are estimated at no more than $50-$60 billion, compared with a peak of $150 billion at the beginning of the 1980s.\(^7\)

In addition, Kuwait and Saudi Arabia (and, outside the Middle East, Venezuela) have acquired refineries, marketing...
networks and other assets in the industrial markets. Structurally tied even more tightly to Western economies, they are unlikely to adopt production and pricing policies that might hurt the industrial economies. Kuwaiti income derived from foreign investments has exceeded the country’s revenues from sales of crude oil and petroleum products in recent years.9

Saudi Arabia has played a key role since the mid-1960s in keeping prices down. Riyadh opened the spigot in 1980 and 1981 to make up for Lost supplies in the wake of the Iranian revolution and after the outbreak of the Iran-Iraq war, to force fellow OPEC members to toe the line on pricing in 1986, and again following Iraq’s invasion of Kuwait to compensate for embargoed Iraqi and Kuwaiti crude.10

The trigger for Iraq’s invasion of Kuwait was the emirate’s production far in excess of its OPEC output quota. This weakened world oil prices and came at the direct expense of Iraq. If Iraq had been able to hold on to Kuwait, it conceivably

Iraq’s show of force in late July 1990 raises an interesting question. Was Washington happy to see Saddam Hussein “enforce” price discipline within OPEC? Baghdad’s interest clearly lay in moving prices upward to the $22-25 per barrel range to fill its depleted treasury. As the colloquy between Saddam Hussein and April Glaspie indicated, this did not exceed what US oil interests wanted.12

The US is playing a highly ambivalent role in the oil game. As the preeminent power seeking to preserve the conditions for the global capitalist economy to thrive, it promotes the flow of oil at reasonable prices. Japan and Western Europe are much more dependent on oil imports than the US (92 and 65 percent, respectively, of their consumption is imported—59 percent of Japan’s and 29 percent of Europe’s comes from the Gulf). On the other hand, the US has an interest in oil prices that permit higher-cost domestic production to remain competitive, a point not lost on President Bush, who made a

would have taken a portion of Kuwait’s production off the market in order to bolster prices. But Baghdad would not have been in a position to withhold any significant chunk of production from world markets. Oil accounts for over 90 percent of Iraq’s export revenues and 61 percent of GDP.11 Indeed, before the invasion, Baghdad was planning to expand its own production capacity considerably over the next five years. The supply of oil, at least in the short run, was plentiful. The longer-term implications of the Kuwait takeover, however, were less certain.

What Price Oil?

The Bush administration’s nonchalant attitude towards fortune in Texas oil.13 Recall the events surrounding the first oil crisis in the early 1970s: Kissinger and Nixon appeared to think that the United States could derive competitive advantages vis-à-vis the highly import-dependent Europeans and Japanese.14 In the past two decades, however, Japan in particular has adapted very well to higher oil import costs through improved energy efficiency and now uses less than half the energy the US does to generate a dollar of GNP. In addition, the weak dollar has dampened the impact of rising oil prices on Western Europe and Japan.15

The Bush administration was less concerned about any modest increase in the price of oil than about the prospect of strong Iraqi influence over the oil policies of Saudi Arabia and the other Gulf monarchies. The crisis once more underscored

Table III. The Twenty Leading Oil Companies

<table>
<thead>
<tr>
<th>Company†</th>
<th>Country</th>
<th>Oil Reserves (bn bbls)</th>
<th>Oil Production (thousands of barrels per day)</th>
<th>Refining Capacity (thousands of barrels per day)</th>
<th>Product Sales (thousands of barrels per day)</th>
<th>Ref.</th>
<th>Prod. Ratios</th>
<th>Prod. Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aramco*</td>
<td>S. Arabia</td>
<td>257.6</td>
<td>5,337</td>
<td>1,620</td>
<td>1,525</td>
<td>329</td>
<td>350</td>
<td></td>
</tr>
<tr>
<td>INOC*</td>
<td>Iraq</td>
<td>100.0</td>
<td>2,786</td>
<td>550</td>
<td>422</td>
<td>507</td>
<td>660</td>
<td></td>
</tr>
<tr>
<td>KPC*</td>
<td>Kuwait</td>
<td>97.1</td>
<td>1,411</td>
<td>852</td>
<td>966</td>
<td>166</td>
<td>146</td>
<td></td>
</tr>
<tr>
<td>NIOC*</td>
<td>Iran</td>
<td>92.9</td>
<td>2,870</td>
<td>766</td>
<td>915</td>
<td>375</td>
<td>314</td>
<td></td>
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<tr>
<td>PDV*</td>
<td>Venezuela</td>
<td>59.1</td>
<td>1,985</td>
<td>1,894</td>
<td>1,500</td>
<td>105</td>
<td>132</td>
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<tr>
<td>Pemex*</td>
<td>Mexico</td>
<td>52.0</td>
<td>2,894</td>
<td>1,679</td>
<td>1,274</td>
<td>172</td>
<td>227</td>
<td></td>
</tr>
<tr>
<td>NOC*</td>
<td>Libya</td>
<td>20.5</td>
<td>842</td>
<td>407</td>
<td>348</td>
<td>207</td>
<td>242</td>
<td></td>
</tr>
<tr>
<td>RD/Shell</td>
<td>Neth./UK</td>
<td>9.5</td>
<td>1,852</td>
<td>4,102</td>
<td>4,940</td>
<td>45</td>
<td>37</td>
<td></td>
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<tr>
<td>Sonatrach*</td>
<td>Algeria</td>
<td>9.2</td>
<td>1,221</td>
<td>475</td>
<td>472</td>
<td>257</td>
<td>259</td>
<td></td>
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<tr>
<td>Exxon</td>
<td>US</td>
<td>7.5</td>
<td>1,804</td>
<td>4,121</td>
<td>4,625</td>
<td>44</td>
<td>41</td>
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</tr>
<tr>
<td>BP</td>
<td>UK</td>
<td>7.0</td>
<td>1,412</td>
<td>1,848</td>
<td>2,683</td>
<td>76</td>
<td>53</td>
<td></td>
</tr>
<tr>
<td>Pertamina*</td>
<td>Indonesia</td>
<td>6.6</td>
<td>865</td>
<td>751</td>
<td>640</td>
<td>118</td>
<td>138</td>
<td></td>
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<tr>
<td>CFP**</td>
<td>France</td>
<td>3.8</td>
<td>370</td>
<td>996</td>
<td>1,123</td>
<td>38</td>
<td>33</td>
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<tr>
<td>Mobil</td>
<td>US</td>
<td>3.2</td>
<td>761</td>
<td>2,111</td>
<td>2,595</td>
<td>36</td>
<td>29</td>
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<td>Chevron</td>
<td>US</td>
<td>3.2</td>
<td>949</td>
<td>2,185</td>
<td>2,209</td>
<td>43</td>
<td>43</td>
<td></td>
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<tr>
<td>Arco</td>
<td>US</td>
<td>3.0</td>
<td>732</td>
<td>521</td>
<td>529</td>
<td>140</td>
<td>138</td>
<td></td>
</tr>
<tr>
<td>Petrobras*</td>
<td>Brazil</td>
<td>2.9</td>
<td>617</td>
<td>1,377</td>
<td>1,182</td>
<td>45</td>
<td>52</td>
<td></td>
</tr>
<tr>
<td>ENI*</td>
<td>Italy</td>
<td>2.6</td>
<td>432</td>
<td>740</td>
<td>898</td>
<td>58</td>
<td>48</td>
<td></td>
</tr>
<tr>
<td>Texaco</td>
<td>US</td>
<td>2.7</td>
<td>833</td>
<td>1,525</td>
<td>2,391</td>
<td>55</td>
<td>35</td>
<td></td>
</tr>
<tr>
<td>Amoco</td>
<td>US</td>
<td>2.7</td>
<td>811</td>
<td>1,055</td>
<td>1,222</td>
<td>77</td>
<td>66</td>
<td></td>
</tr>
</tbody>
</table>

†Production, refining and marketing arms of state-owned companies presented as single entity, though technically separate units in some cases.

*State-owned companies. **Partially state-owned (40 percent).

Saudi Arabia’s unique position: even the total boycott of Iraqi and Kuwaiti oil was of little consequence to the world economy as long as the Saudis boosted their output to compensate for the supply loss. Leaving Iraq in a position to influence the Gulf monarchies, though, might have jeopardized Riyadh’s ability to moderate prices.

The war against Iraq needs to be seen in the context of the shifting oil politics in the Gulf region. During the 1970s, Iran under the shah protected the political status quo. When Khomeini’s Iran turned against the West, the US moved closer to Iraq and shored up Baghdad’s staying power in its war against Iran. When the war ended in 1988, the monarchies confronted a well-armed and economically hungry Iraq. Determined to maintain the existing political order in the Gulf, but now shorn of proxy forces, the United States felt compelled to intervene directly.

Oil companies—some more than others—were clear winners of the events following the Iraqi invasion of Kuwait. Robert Horton of British Petroleum commented that “every dollar increase in the price of a barrel of crude adds $200 million to my bottom line.” More important than the crude price itself are the price differentials between crude oil and oil products and between wholesale and retail markets. Thus oil companies reported more spectacular profits in the 4th quarter of 1990 and the 1st quarter of 1991, when crude prices declined gradually, than in the 3rd when they surged upwards.

This may have been a one-time bonanza. When the war started in January, oil prices on the futures market dropped by $10, the largest-ever one-day decrease. When Iraq and Kuwait re-enter the market, the result may well be an oil glut, depressing prices.

Three major factors determine corporate profits. The first concerns the extent to which a company is able to supply its refining facilities and marketing networks with its own crude production (see Table 3), and the degree to which it operates in low-tax areas. Some 54 percent of BP’s net income stems from crude production, and its “self-sufficiency” rate is higher than that of most other major firms. Oil production in Alaska, taxed at the comparatively low marginal rate of 34 percent, is a boon for BP and also for Arco, Unocal, and Amerada Hess.

Companies that enjoy very high self-sufficiency rates include Amoco and the French firm, Elf-Aquitaine. The operations of other majors, including Royal Dutch/Shell, one of the largest, are subject to marginal tax rates as high as 64 percent.

The second consideration relates to the “downstream” refineries and distribution networks. During the early 1980s, rising crude oil prices depressed refinery profit margins, while falling crude prices allowed refiners greater margins. Because the Iraqi invasion led to the withdrawal of roughly 750,000 barrels per day (b/d) of petroleum products (and another 500,000 b/d of refinery output went to the allied forces in Saudi Arabia), refining profits have jumped. During the second oil crisis in 1979-80, US refiners used 74 percent of their capacity; now they are running at 92 percent. Those companies that are more strongly involved in refining than in distribution—Ultramar, Diamond Shamrock and Ashland Oil, for example—have reaped the greatest windfall. More specifically, those companies whose refineries are configured to process the heavier Saudi crude that is replacing lighter Kuwaiti and Iraqi oil—Chevron, Shell, Unocal, and Amoco—have (literally) a built-in advantage. Those selling jet fuel—in particular, companies supplying Saudi Arabia during the war—fared much better than those selling gasoline. The situation is less opportune for companies that market their products via long-term supply contracts.

A third factor concerns the degree to which oil companies have invested in the petrochemical industry. Overcapacities in this industry make it impossible to pass through higher costs for the most important petrochemical feedstock, naphtha. In the US, recession compounds these difficulties.

With the obvious exceptions of Iraq and Kuwait, all oil exporting countries have benefited from the upsurge in oil prices since August 1990. The biggest gainers were Saudi Arabia, the United Arab Emirates, Libya, Gabon, and Venezuela: they were best able to respond by increasing their own production. Saudi Aramco went from 5.3 million b/d in July 1990 to 8.35 million b/d five months later. Production capacity is to rise to 10 million b/d in three years.

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### Table IV. Control of Oil Reserves, Production and Sales, 1989

<table>
<thead>
<tr>
<th>Oil Reserves</th>
<th>Oil Production</th>
<th>Oil Product Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>(bn bbls)²</td>
<td>(m b/d)²</td>
<td>(m b/d)²</td>
</tr>
<tr>
<td>Majors³</td>
<td>38.8</td>
<td>45.9</td>
</tr>
<tr>
<td>National Oil Companies⁴</td>
<td>799.0</td>
<td>93.1</td>
</tr>
<tr>
<td>All Other Companies⁵</td>
<td>20.1</td>
<td>2.3</td>
</tr>
<tr>
<td>TOTAL⁶</td>
<td>857.8</td>
<td>100.0</td>
</tr>
</tbody>
</table>

¹Billions of barrels. ²Millions of barrels per day. ³The “Seven Sisters” minus Gulf Oil (acquired by Chevron plus Amoco and Arco). ⁴525 companies from major oil producing nations. ⁵32 companies, mostly smaller private firms but also some partially or wholly state-owned enterprises whose operations are not primarily based on domestic oil reserve holdings. ⁶Encompasses the 65 leading companies outside the Soviet Union and China. Totals may not add up due to rounding.


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### Structural Aspects

The nationalization of oil resources by OPEC governments in the 1970s led to a sharp drop of the crude oil availability for the international oil companies. “Vertical integration”—the balance between upstream and downstream operations or, to put it differently, a corporation’s control over sufficient quantities of crude oil production to supply its refining and marketing outlets—came to an abrupt end. The companies subsequently sought to replace lost reserves by exploring in a variety of non-OPEC countries and, during the mid-1980s, by acquiring other firms with proven reserves—“prospecting on Wall Street.” But most still purchase substantial amounts of crude or refined oil, through contractual relationships or in the open market, to balance their operations. During the
1980s, the global oversupply of oil allowed the companies to put pressure on producer governments to lower prices and gradually to abandon them in favor of prices set in spot and futures markets.23

In the last few years, growing numbers of oil-producing countries have felt compelled by shortages of capital, skills or technology to invite exploration ventures by private oil companies after excluding them for decades. Nations that have already welcomed back foreign firms include the Soviet Union, China, Vietnam, Venezuela, and Algeria, and others in Eastern Europe. Together they represent one third of current world oil output. As the Petroleum Intelligence Weekly commented: "In the Middle East... a dramatic move away from resource nationalism is providing opportunities for oil companies to move back into that corner of the world."

The international oil companies may thus find a new avenue toward vertical reintegration. Before its Kuwait adventure, cash-strapped Iraq was the first state in the Gulf region to invite international oil firms to develop known oil fields.24 The Financial Times subsequently reported that "the crisis in the Gulf may force Kuwait to consider allowing foreign ownership of petroleum assets as a means of enhancing its future security..."25

The national oil companies are facing the opposite situation: they control huge oil deposits but lack sufficient outlets. OPEC governments have tried to boost the share of their crude production that is sold in the form of products by constructing refineries and acquiring gasoline stations in Western Europe and North America. Kuwait Petroleum Corporation has been at the leading edge of this move downstream, followed by Venezuela's PDV and Saudi Aramco.26

Tables 3 and 4 portray the upstream/downstream disparities between state oil companies and private international companies. Both are trying to (re-)build vertically integrated structures, from opposite vantage points. It seems the world oil industry is entering a new era. In the absence of serious efforts to enhance energy efficiency and to develop renewable sources of energy, oil demand is set to grow; only the Gulf states seem able to satisfy that demand. With both sides heavily investing capital and technology—the private firms investing in exploration and production in the oil-rich countries, and the state companies in refining and marketing in the major markets—both have an overriding interest in stable prices and stable politics as well. Edward Morse of Petroleum Intelligence Weekly presented the case for condominium recently, arguing that "it is no longer a case of 'us versus them.' It is now much more an issue of how differing endowments of geology, capital, technology and human resources complement one another."27

Iraq, by invading Kuwait, was moving to augment its endowments of geology and capital, and in the process to redefine the political relationships that have linked the OPEC producers, the companies, and the governments of the industrial consuming countries. Saudi Arabia identifies itself closely with the economic and political interests of the US and the major European states. But in "representing" these interests in OPEC and Arab politics, the Saudis have had to take account of the balance of forces in the region. It was this balance that Iraq attempted to restructure, and the US was determined to re impose.

The arrangements that will follow the US defeat of Iraq will likely produce a kind of joint "oil dominion" between major consumer countries and a core of oil exporters which will override the interests of the poorer oil importers and exporters alike. At the center of this new alignment will no longer be the "seven sisters"—the major private companies that dominated the industry before the 1970s—but what South magazine has dubbed the "four stepsisters"—Saudi Aramco, PDV, and Exxon and Shell, the two largest private firms.28 But OPEC will have to confront some serious conflicts within its ranks which may well split the organization. Producers like Saudi Arabia, Iran and Venezuela are investing huge amounts of capital to expand their production capacity: will they be ready to scale back their market share once Iraq and Kuwait resume production?29 The new world order of oil could bring unprecedented producer-consumer cooperation for the privileged states and companies, and increasingly harder times for the rest.

Footnotes

1 Time, August 20, 1990.


4 Reserve trends from BP Statistical Review of Energy (London: British Petroleum Co., July 1989), p. 3. During 1975-1982, three quarters of oil exploration money was expended in the Western industrial countries, with the United States receiving the lion's share, while only 3.4 percent went to the Middle East. Between 1973 and 1981, about 90 percent of worldwide exploration wells were drilled in industrial countries, again most of them in the United States. See Renner, "Stabilizing the World Oil Market," p. 51.


12 On July 27, 1990, just before the takeover of Kuwait, Iraq's intimidation tactics led OPEC to raise its target price from $18 to $21 per barrel. US Ambassador April Glaspie reportedly told Saddam Hussein on July 25 that "We have many Americans who would like to see the price [of oil per barrel] go above $25 because they come from oil-producing states." See "The Quiet Campaign to Export Alaska's Oil," Earth Island Journal, Fall 1990, p. 6. On October 21, 1990, article in the Observer (London) speculated that Saddam Hussein's and Bush's interests overlapped at least partially.

13 When oil prices collapsed in 1986, then-Vice President Bush urged the Saudi government to stabilize prices.


15 The monthly average of oil prices rose from $12.80 in June 1990 to $35.32 in September. Adjusting for inflation and exchange rate variations, however, Japan paid only 32.49 and Germany 33.71. By November, the United States paid $39.65 for a barrel of imported oil, but at $34.75 and $22.86, respectively, Japan and Germany still paid less. See "Falling Dollar Takes Sting Out of Oil Price Spike," PW, December 10, 1990, pp. 4-5.

16 Derek Bamber, "Profit Surge on the Way?", Petroleum Economist, September 1990, p. 23. Prices remained high until the US launched the war against Iraq; even though the oil shortfall arising from the boycott of Iraq and Kuwaiti oil was compensated by October 1990. See "OPEC 1990 Output Hits

See Aarts, page 47


Ian Black and Benny Morris, Israel's Secret Wars: The Untold History of Israeli Intelligence (New York: Grove Weidenfield, 1991). $24.95.


"Stabilizing."


Venezuela has already raised its production capacity to 2.8 million b/d and is planning to go to 3.3 million b/d by 1996, a move estimated to cost $12 billion. Venezuela is known to consider leaving OPEC. Iran has announced plans to increase its capacity by 50 percent to 5 million b/d. See Wald, "Assessing the Damage to OPEC," op. cit.