

# OPEC IN THE CONTEXT OF THE GLOBAL POWER EQUATION

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## I. INTRODUCTION

The name of the Organization of Petroleum Exporting Countries has been on thousands of lips around the globe in recent months. The Organization's initials—OPEC—have filled thousands of newspaper pages the world over. To the people in the oil-importing countries, the word OPEC is a frightening one, reminding them of high oil prices, gas station lines and fuel shortages. OPEC has been called many names, the nicest of them being "international cartel;" it has been accused of many things, the mildest of them being "monopoly pricing."<sup>1</sup> Yet few of OPEC's critics, and fewer of its followers, know what OPEC really is or what its purposes are. Briefly, OPEC is an association of twelve full-member plus one associate-member countries, dedicated to the protection of their national interests in the production and export of oil. OPEC was originally established by five oil-producing countries as a "mouvement de resistance" (defense league) against arbitrary and unilateral decisions of the major oil companies.

At this point, a bit of oil price history is highly illuminating. In 1947 the "posted price," or the price on which royalties and taxes are based, of a barrel of Persian crude was \$2.17. During the 1950's, while other prices were rising, the oil price was stable or on the decline. In February 1959, the "posted price" of Persian Gulf crude was officially lowered by the major oil companies, who gave as their reason a glut in world oil supply, to \$1.90 a barrel. The oil exporters, who were economically poor and politically divided, could not and did not do anything to stop these losses per barrel. Instead, the exporters strove for increased output to maintain their total income. The companies, in turn, lowered the price to \$1.80 in August 1960. Of this, 80 cents was the exporter's share.<sup>2</sup> Since most of the exporters were depending principally on oil income for their foreign exchange needs, the companies' disregard of these needs and the exporters' other aspirations resulting from repeated reduction of oil prices served as the turning point in the history of OPEC.

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1. For the history and background of OPEC see Z. MIKDASHI, *THE COMMUNITY OF OIL EXPORTING COUNTRIES* (1972).

2. *Hearings on S. Res. 40 Before the Senate Subcomm. on Antitrust and Monopoly*, 91st Cong., 1st Sess., pt.1, at 437 (1969). Another source puts oil prices at \$2.22 per barrel for 1947. H. FRANK, *CRUDE OIL PRICES IN THE MIDDLE EAST* 30 (1966).

The five countries involved (Iran, Iraq, Kuwait, Saudi Arabia and Venezuela) formed OPEC in September 1960. Later, Algeria, Ecuador, Indonesia, Libya, Nigeria, Qatar and the United Arab Emirates joined the group. Gabon was recently accepted as an associate member. OPEC's victories were hard and long in coming. Despite the members' resolve to prevent an oil price decline, the countries' policy of unrestrained production to obtain larger revenues and foreign exchange kept pushing prices down. These policies were imposed on the countries by the companies against the exporters long-term interests, and against technical requirements for prudent and efficient exploitation. Although the official posted price, under OPEC pressure, remained at \$1.80 a barrel throughout the 1960's, significant discounts (of 40 cents to 55 cents a barrel from the posted price on the producers' own offtake) were not unusual. A barrel of offtake crude was often sold by the Persian Gulf producers at \$1.25 in the world markets—with the prospects of the blissful "\$1.00 a barrel" gleefully contemplated by the companies and net oil-importers.<sup>3</sup>

Then, success came suddenly. Following the Caracas Resolution of December 1970,<sup>4</sup> a conference was held in Tehran between OPEC representatives and those of the oil majors in February 1971. After a series of long and difficult negotiations, an agreement was reached whereby the posted price was increased to \$2.30, and provisions were made for (a) small annual increases in that price, and (b) allowance for inflation in the major oil importing countries.<sup>5</sup> With this significant triumph in hand, other successes followed. In January 1972, a new concession was obtained by the oil exporters in terms of adjustment allowances in their incomes (received in U.S. dollars) against dollar devaluations.<sup>6</sup> In March 1972, the principle of "participation" by producer-governments in the operation of the oil companies was accepted.<sup>7</sup> In October 1973, after weeks of unsuccessful negotiations with the companies, the oil-exporting governments declared their intention to establish oil prices among themselves, free from the obstructionist tactics of the companies in bilateral bargaining.<sup>8</sup> The

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3. FRANK, *supra* note 2, at 116.

4. OPEC Resolution XXI. 120 Calling for Negotiations and Forming Three-Member Negotiating Committees, Dec. 1970, 10 INT'L LEGAL MATERIALS 240-42 (1971).

5. Tehran Agreement Between Six Gulf States and Oil Companies Operating in Their Territories, Feb. 14, 1971, 10 INT'L LEGAL MATERIALS 247-54 (1971). Thus between 1947 and 1972 the posted price of crude oil in the Middle East rose only from \$2.17 to \$2.30. When inflation is taken into account, the real price was actually fifteen percent lower over twenty-five years.

6. Organization of Petroleum Exporting Countries: Agreement Between Oil Companies and Six Persian Gulf States on Increased Payments, Jan. 20, 1972, 11 INT'L LEGAL MATERIALS 554-60 (1972).

7. See L. MOSLEY, *POWER PLAY: OIL IN THE MIDDLE EAST* 388-411 (1973).

8. N. Y. Times, Oct. 17, 1973, at 16, col. 1.

posted price was raised to \$5.11,<sup>9</sup> and finally, in December 1973, when the crude oil auction price in the free market had risen to over \$22 a barrel, the posted price in the Persian Gulf was raised to \$11.65 a barrel.<sup>10</sup>

## II. REASONS FOR THE RISE OF OPEC

The intriguing question is: How could OPEC, which for ten long years had been largely helpless in promoting the interests of its members, suddenly succeed in bringing the oil majors to their senses, so to speak, and in making the whole world take notice of the Organization's aims and strengths? The answer lies in a multitude of forces, long in the making, which have suddenly converged on the scene. Eight interrelated factors can be distinguished as contributing to OPEC's recent rise in prominence.

The first factor relates to a change in the world's basic balance of politico-economic power. The nature and source of OPEC's bargaining strength in dealing with the major oil consuming nations and the oil majors are a part of this change in the global power equation—a reflection of the growing power and independence of the Third World. The essence of world power in the last two decades has undergone two fundamental changes: (a) away from originally bipolar, and later triangular, hegemony of the Super Powers; and (b) in favor of the less-developed countries (LDC's). International bargaining, a dynamic process, has thus undergone significant changes in its participants, its scope, and its dimensions. The bargaining leverage possessed by OPEC is a manifestation of the emergence of the Third World as a Third Force.<sup>11</sup>

Several basic features of this new global power equation can be easily underlined. The new U.S.-U.S.S.R. detente, for example, has ushered in greater tolerance by both major powers of neutralism, non-alignment, and the pursuit of political independence; non-alignment no longer necessarily connotes hostility toward the left or the right. Then, there has been a multilateralization of power bases, following the rise of Japan and the EEC to the position of Super Powers in the world. Furthermore, new international politico-economic alliances have been formed on the basis of functional and geographical rather than political and ideological considerations. For example, the Soviet Union and the United States have entered into a number of technical, cultural, scientific and even economic treaties and relationships with countries possessing different political ideologies. The membership

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9. N. Y. Times, Oct. 19, 1973, at 61, col. 1.

10. N. Y. Times, Dec. 24, 1973, at 1, col. 8.

11. For a succinct analysis of the new developments see S. BROWN, *THE CHANGING ESSENCE OF POWER* (1973) and G. BERGSTEN, *THE THREAT FROM THE THIRD WORLD* (1973).

composition of such international bodies as UNCTAD, GATT, the Arab League, and the Organization of African States, groupings in the International Monetary Fund and the World Bank, and other similar mixtures present vivid examples of pragmatic and apolitical coalitions.

These criss-cross coalitions have been stimulated and fostered by the Super Powers' need for votes in various international forums which, in turn, have stimulated and nurtured the emergence of the Third World as a significant force favoring cooperation rather than coercion in international relations. "Gunboat diplomacy" has been gradually replaced by relatively polite official debates and skillful informal lobbying in the corridors of international agencies. Finally, the emergence of the People's Republic of China as the new champion of the Third World has significantly strengthened the LDC's hand in their bargaining with the richer countries.

The second factor responsible for OPEC's rising power and influence has been the geopolitical strength of the OPEC members. For example, six major OPEC countries are located around the Persian Gulf, a strategic area for all Super Powers. The Soviet Union's historic desire for access to the warm waters of the Gulf and the Indian Ocean,<sup>12</sup> the United States' special commitments to the State of Israel plus her vast investments in the Middle East oil fields, and Sino-Soviet rivalry in this part of the world for its own sake and as a gateway to Africa—all have given the Persian Gulf region its geopolitical significance.

The third factor operating in OPEC's favor has been the Organization's control over oil reserves and exports on the one hand, and the industrial countries' dependence upon imported petroleum on the other. By 1985, more than half of world energy consumption (estimated at 145 million b/d of oil equivalent) will be supplied by crude petroleum. Considering that more than sixty per cent of the world's proven oil reserves and about eighty-five per cent of world oil exports are in OPEC's hands, the Organization's actual and potential clout is not difficult to recognize.<sup>13</sup>

The fourth factor accounting for OPEC's mounting significance and power is solidarity among the exporting countries. History records many exporting organizations of bygone days which faded away in a short span of time due to short-sightedness, secretive competition, and the pursuit of "beggar-my-neighbor" policies. In the case of OPEC, however, in spite of differences in ideology and political

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12. In this connection see L. LANDIS, *POLITICS AND OIL: MOSCOW IN THE MIDDLE EAST* (1973).

13. R. MILLER, *THE ECONOMICS OF ENERGY: WHAT WENT WRONG AND HOW WE CAN FIX IT* (1974).

philosophy among member countries, there has been a strong harmony of economic action among members, a harmony which has remained largely immune to countervailing maneuvers of both the big oil companies and the consuming nations.<sup>14</sup> Above all, OPEC's leadership has remained in the hands of moderate countries which have succeeded in avoiding useless and unproductive confrontations with the consuming nations.

The fifth element underlying OPEC's success has been the existence of conflicting interests among certain major consuming countries, despite their similar political philosophies and orientations. OPEC members, notwithstanding their dissimilar political regimes, have found it advantageous to follow certain common economic goals. Western Europe, the United States, and Japan, on the other hand, continue to follow what they themselves call "cannibalistic competition" in the economic arena. The United States, primarily relying on its own relatively rich domestic oil resources,<sup>15</sup> has recently vowed to follow a policy aimed at self-sufficiency by 1980. The United States' policies and prospects are thus vastly different from Japan's, a country which is totally dependent on foreign oil. In case of an emergency, the United States can maintain her levels of employment, income, and living reasonably well by adopting energy-saving policies which might necessitate only small sacrifices on the part of her people. But without foreign oil the Japanese economy would be in total chaos. The economic interests of EEC members also vary. England hopes to attain self-sufficiency and an exporting position in oil by 1980, a hope which cannot be shared by her other partners in the Community. Italy, France and Germany have thus found it necessary to follow their own national self-interest in attempting to obtain long-term supplies of foreign petroleum.<sup>16</sup>

The sixth element contributing to OPEC's strength has been the greater self-confidence among members as a result of a series of consecutive successes in the international economic scene. The expression "nothing succeeds like success" has never been more clearly manifested than in this case. OPEC members had endeavored to

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14. See MOSLEY, *supra* note 7, at 388-411; Mikdashi, *Cooperation Among Oil Exporting Countries with Special Reference to Arab Countries*, 28 INT'L ORG. 1, 9-10 (1974). For examples of discord among OPEC countries see Mikdashi, *supra* note 1, at 12-17 and Note, *From Concession to Participation: Restricting the Middle East Oil Industry*, 48 N. Y. U. L. REV. 774, 791-93 (1973).

15. Even during the economic boom of 1972-73, only one-third of the United States' oil consumption was imported, but the figure for Japan was close to 100 percent.

16. The virtual abandonment of the Netherlands by other EEC countries in the face of the Arab oil embargo after October 1973 is another example of European disunity when national interests are at stake.

obtain their due shares since 1960, but their early setbacks in negotiations with oil companies repeatedly weakened their hand. Then they had their first success in February 1971 under the guidance and leadership of Iran's Shahanshah. From then on, one success led to another. The 1971 victory provided not only the psychological self-confidence needed by OPEC negotiators, but also the politico-economic underpinnings for future bargains. Once assured of their annual foreign exchange needs, the oil producers could negotiate from a position of financial strength and ultimately political power.

The seventh factor leading to OPEC's successful negotiations with the oil companies' skilled and sophisticated negotiators has been the ample supply of indigenous talent from the oil-producing countries. The exporter's representatives today are a group of well-informed and experienced individuals who fully match their Western counterparts in political skill and bargaining ability. They are equipped not only with their own courage and their governments' full support, but with reams of statistics and a number of arguments carefully selected and meticulously worked out by their technical and professional deputies. Oil bargaining sessions are no longer an exercise in favors humbly requested by the producers and magnanimously bestowed on them by the oil majors. The relationships are now conditioned by sovereign states bent on optimizing returns from their exhaustible resources and their customers. The West and the oil companies have come to understand these facts, and their relations with the Third World and the oil producers have significantly changed.<sup>17</sup>

The eighth factor responsible for OPEC's remarkable recent achievements has been the developing governments' success in following independent national policies free from the insidious influences of the oil companies or their governments. The majority of the people in the Third World have obtained greater confidence in their leaders now, and are willing to endure greater sacrifices to ensure the attainment of their national goals. At the same time, the political and administrative influence of the oil majors over both their own governments and those of the producing countries has considerably diminished.<sup>18</sup>

The success in oil negotiations and the acquisition of substantially vast sums of revenues have enabled national leaders in the oil-producing nations not only to give their people greater material amenities and increased economic welfare, but to prove to them their leadership ability and governing capacity. The rank and file, in turn, have not only become relatively more comfortable and thus more

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17. R. VICKER, *THE KINGDOM OF OIL/THE MIDDLE EAST: ITS PEOPLE AND ITS POWER* (1974).

18. MOSLEY, *supra* note 7.

content; they have come to believe, more and more, their leaders' promises of higher material standards of living and enhanced national political prestige for their countries. This increased popular support has, in turn, strengthened the leadership's hand, allowing them to stand up to foreign politico-economic pressures and to resist oil company dictates.

### III. THE WEAPONS OF OPEC

Having discussed the foundations of OPEC's economic strength and political power, we may consider the means through which this politico-economic power can be used in negotiating with international oil companies and Western consuming countries. The so-called "weapons" in OPEC's hands can be classified into two categories: (1) negative sanctions, and (2) positive stimuli, which can be used alternatively vis-a-vis foreign interests. In resisting intolerable demands or intransigences of the oil-importing countries or companies, OPEC members may retaliate by resorting to such negative sanctions as:

1. Withholding part or all of the oil supply from all or selected customers through (a) nationalization or threat of take-over of oil and/or other foreign investments, and (b) temporary embargoes on exports;

2. Using its "embargo" power to demand and receive increasingly higher prices for crude oil—naturally to the extent that consumer resistance, the development of substitutes, and retaliatory measures by the oil importing countries (e.g., import quotas, foreign investment restrictions, denial of aid, and other retaliation) may permit;

3. Regulating domestic operation by foreign oil companies through such requirements as greater local participation in production and/or distribution; further changes in internal "value-added" in oil production and marketing; and increased local purchases, restricted company imports, etc.;

4. Switching huge export earnings from some foreign currencies and countries to others depending on type of cooperation and attitude, or denying foreign investment in "hostile" countries;

5. Making discriminatory price concessions, or engaging in unfavorable price discrimination vis-a-vis selected customers, or dumping other export products in "unfriendly" countries;

6. Retaliating against industrialized creditors by the repudiation or re-scheduling of foreign debts; and

7. Shifting alliances and coalitions in trade, investment and military agreements between cooperative and

non-cooperative nations (including threats of withdrawing from membership of regional pacts or closing military bases).

The possibility of using these negative sanctions is only part of OPEC's strength. Part of its power also resides in the offer of positive stimuli or incentives for cooperation. These incentives may include such things as:

1. Giving special concessions to foreign private investors for the purpose of exploiting domestic national resources which are outside the scope of existing contracts;
2. Promising cooperation in the reform of international monetary, fiscal and trade systems; and
3. Investing in joint ventures for the development of energy sources and/or other investment projects with cooperative and accommodating partners.

These positive and negative "weapons" have been used in the past and are more likely to be used in the future when circumstances warrant. Like all destructive weapons, however, the significance of the negative sanctions lies, partly at least, in their potential deterrence rather than actual use.

#### IV. CONCLUSION

In the final analysis, the very existence and occasional use of these weapons—even those which are retaliatory in nature—are not only in the interest of the Third World, but also to the advantage of the whole international community. The possibility of using the negative weapons will ensure greater economic justice among the rich and poor; reduce inferiority complexes of the developing nations (particularly the previous colonies) when dealing with the industrial countries; enhance their self-reliance and self-confidence; narrow existing political, psychological and economic gaps between the large and small countries; and pave the way for a better world. The productivity and beneficial prospects of the positive stimuli, in turn, open up vast horizons of cooperative endeavors between oil producers and oil consumers in efficient use of fuel supplies and in the search for newer sources of energy.