

## OIL EMBARGO OF 1973 AND ITS IMPACT ON TARGET COUNTRIES

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### INTRODUCTION

The economic state craft is a political act which utilizes economic instruments to achieve compliant behavior from a target actor. The economic state craft may appropriately be regarded as an umbrella term covering all instances where international actors use economic instruments for political ends.<sup>1</sup> The economic sanctions are a form of economic state craft which involves the use of economic capability by an actor or a group of actors (imposer/imposers) in a deliberately coercive manner to pursue certain policy goals. The essence of the sanctions attempt is to compel the target country to behave in a more civilized way. The means used to secure this compliance involve denying the target country an access to certain goods and services that are controlled by the imposer. When reference is made economic sanctions the punitive measures such as the embargo, the boycott, the withdrawal of most favoured nation's status are envisaged. The success of economic sanctions depends on following factors:

1. The more actors involved in the sanctions policy, the greater its chances of actually causing the target some deprivation;
2. The imposer should be in a monopoly position, vis-a-vis the target; and
3. The goods and services denied to the target country should supply key sectors of its economy.

Thus, keeping above factors in view the oil can be considered as one of the strategic commodities in sanctions context.

This paper presents a critical study of oil embargo imposed by the Organization of Petroleum Exporting Countries (OPEC) and the Organization of Arab Petroleum Exporting Countries (OAPEC) against the United States of

America, Japan and West European countries during 1973 and 1974. The paper will further analyse the impact of embargo upon the economies of sanctioned countries.

#### **BACKGROUND**

The Territorial disputes between Israel and its Arab neighbours originated with the creation of the state of Israel in 1948 which had been the cause of three wars i.e. the War of Independence in 1948, the Suez Conflict of 1956 and the six-day war of 1967 followed by the Yomkippur war that began in October 1973. An addition to continuing the quest for a national homeland for the Palestinians who had been uprooted from their homes during the 1948 and 1967 wars, a number of Arab states sought in 1973 to redress their own particular territorial grievances against Israel.<sup>2</sup> The month of October 1973 brought with it Arab coercion in two forms: the first was the military attack against Israeli forces begun on October 6<sup>th</sup>, the second was the of economic coercion against countries that Arab eyes, either supported Israel or did not support the Arabs in their present quest which include the retrun of claimed Arab lands, favourable settlements of the palestinian people's claim for self-determination and other political and military objectives.<sup>3</sup>

#### **THE ROLE OF OPEC**

The Organization of Petroleum Exporting Countries (OPEC) was established in 1960 by five states, Iraq, Kuwait, Saudi Arabia and Venezuela. In 1973 OPEC had increased its membership from the founding five to include Abu Dhabi, Algeria, Equador, Gabon, Indonesia, Libya, Qatar and Sharjah. (Abu Dhabi, Dubai and Sharjah later became the United Arab Emirates (UAE). In economic terms its intension was to establish a cartel arrangement between the commodity producer in the oil industry to maintain a price structure that would reflect the percieved interests of its member states rather than

the oil companies which had set prices and production level hitherto. Indeed it was not OPEC but OAPEC which consisted of the Arab OPEC group plus Egypt and Syria that launched oil embargo.

Similar tactics to impose oil embargo were, however, tried by the Arab oil ministers during the 1967 war but could not apply sufficient pressure on Western countries to convert them to the Arab cause. The Arabs felt more confident in 1973, however, given the industrialized world's increasing thrust for oil. Shortly before the outbreak of hostilities in October 1973, officials of Saudi Arabia, the largest Arab oil producer, were revealing plans to check the increase of their crude oil production if the United States did not take a more impartial position in the Middle East conflict.<sup>4</sup> Twenty days after the outbreak of 1973 war, OAPEC members cut off oil exports from Arab states to the United States in retaliation for American arms shipment to Israel. Shortly thereafter, embargo was extended to the Netherlands due to its strong support of Israel and later in November to other countries, which had also taken strong pro-Israeli positions. Some six weeks later, the use and impact of this form of economic coercion had broadened and intensified. Amid an aura of proclaimed unity, Arab leaders adopted a joint resolution calling for the continued use of oil as an economic weapon.<sup>5</sup>

#### **IMPACT OF OIL EMBARGO**

The less developed countries had increasingly become key sources of world crude oil productions with the Middle East countries in particular. At the same time, the major industrialized countries particularly in Western Europe and Japan had become increasingly dependent on oil imports to meet oil consumption needs but their overall energy requirements, with Middle East oil alone filling almost half (47%) of Western Europe's aggregate

energy needs and over half (57%) of Japan's aggregate energy needs by 1972.

The most glaring statistics were the West European and Japanese dependence on imports for 99 percent of European and Japanese dependence on imports for 99 percent of their total oil consumption, mostly supplied by the Middle East.<sup>6</sup> The West European countries had practically no oil and gas resources of their own. The Middle Eastern states had over 62 percent of the non-communist world's developed oil reserves and 28 percent of the natural gas. In 1970 exactly half of Western Europe's oil requirements were met by imports from the Middle East. In 1972 the Middle East covered 60 percent of Western Europe's oil consumption. West Europe was thus naturally more anxious to see a lasting or at least a stable peace returning to Middle East as early as possible. According to an international oil consultant, the United States could survive in some fashion without Arab oil but that the economies of most West European and Japan might collapse.<sup>7</sup>

United States of America, due to its own indigenous oil production capabilities and more varied energy alternatives was least affected by the oil crisis. But its demand for oil and reliance on foreign sources had increased by 1972. Between 1962 to 1972, US oil imports had increased from 2 million barrels to 5 million barrels a day, with the import share of total US oil consumption jumping from roughly 20 percent to 30 percent. On the eve of oil embargo in October 1973, this figure had reached close to 35 percent.<sup>8</sup>

The most important factor which enhanced the bargaining power of the oil producers was the increasing dependence of the Advanced Industrial Countries (AICS) including the United States upon Middle Eastern oil. This

meant that any significant interruption in supply and rise in prices would have a most damaging multiplier impact upon the economies of these developed states. In October 1973 the OPEC acted for the first time to raise oil prices unilaterally. The increase in crude oil posted prices by the OPEC from about 3 dollars a barrel to five dollars a barrel on October 16 and then again to 11.6 dollars a barrel effective from January 1<sup>st</sup> 1974, shook the entire world.<sup>9</sup>

The fourfold increase in oil prices to more than eleven dollars per barrel as of January 1974 is often referred to as the first "OIL SHOCK" experienced by the world system during the 1970s.<sup>10</sup> It was a virtually unprecedented exercise of power by a group of less developed countries. In many ways this act of defiance was a more significant aspect of the 1973 oil crisis than the embargo itself. Its repercussions were obviously world wide in the shape of mounting oil import bills and a sudden spurt in prices of manufactured goods. In sympathy prices of other commodities also started looking up. The U.S. supplied 90 percent of its energy requirements from its own sources and barring Canada, was the least affected among the industrialized countries by the consequences of a rise in the import bill. On the other hand, other advanced countries depended on indigenous sources to a much smaller extent. United Kingdom and Germany about 50 percent, France 22 percent, Italy 15 percent and Japan 11 percent. The impact of the oil price increase on the balance of payments was greater in the case of these countries which were quite heavily dependent on oil imports, than in that of the United States.<sup>11</sup> Hobart Rowan wrote in *Washington Post* that soaring oil costs threaten to swamp the world's economy. <sup>12</sup> The price rises were said to present a radical turning point in the outlook for the world economy.<sup>13</sup>

The greatest economic damage from the OPEC initiative on prices was felt by the oil importing Third World. The outlook for less developed countries was described as being "nearly disastrous", while the situation for many industrialized nations was difficult if not unmanageable. The basic problem was that the world will fast run out of money to pay for the oil it needs.

The Arab states already pledged to reduce their oil production by at least 25 percent compared with the September 1973 level, decided to go on making additional five percent cuts. In addition, periodic cuts in the oil trade were threatened with targeted countries that did not change their policies or engage in certain pro-Arab conduct. Interrelated with these threats were additional Saudi Arabians claims to cut oil production by 80 percent if the United States, Europe or Japan took measures to counter current Arab oil boycotts and reductions in production.<sup>14</sup>

West Germany, Switzerland, Denmark, Luxembourg and Italy joined Holland and Belgium in banning a total of nearly 25 million motor vehicles from their highways on Sundays to save fuel stocks and Holland announced the introduction of petrol rationing from January 1974. West Germany had been affected directly by the Arab oil boycott of Holland because the majority of West German oil supplies had been coming by way of Rotterdam. Gasoline prices in West Germany had already risen by 10 percent and heating oil price had almost doubled.

As a first step to meet the energy crisis, all government departments and owned industries in Britain were ordered to cut their fuel consumption by 10 percent. The government also decreed a 10 percent across the broad general cuts in the delivery of all oil supplies. Many

gasoline stations started rationing sales to customers.<sup>15</sup>

Eighty percent of Japan's fuel imports consisted of oil from the Persian Gulf, of which 37 percent had come from Iran. The Japanese Ministry of Trade and Industry expected the country's economic growth rate to be reduced to zero during the last four months of the fiscal year which was to end in March 1974. In the wake of a record balance of payments deficit (1.7 billion dollars) for November 1973, there were forecasts of a possible collapse of the Japanese economy, if inflation and oil cuts were to continue. It was said that higher prices for crude oil could wipe out Japan's foreign exchange reserves at that time standing around 13,000 million dollars. In view of the progressive oil shortage, the Japanese government had planned to announce tough restriction on oil consumption to protect the nations dwindling oil reserves. In this way oil weapon was successful in creating a global depression.<sup>16</sup>

#### INITIATIVES TO COUNTER THE ARAB STAND

The consumer governments attempted to counter the power of the producers. But the consumers, unlike the producers were unable to agree on a common policy. The United States sought to form a counter cartel to destroy OPEC. To this end, the United States pressed Western Europe and Japan to attend a consumer conference and develop a united policy. The US President Nixon warned that world stability and prosperity could be permanently damaged unless there is international co-operation to deal with oil shortages. The conference held in Washington in February 1974, demonstrated the inability of the consumers to agree on a common strategy. While the Americans argued for unity and resistance, the Europeans and Japan far more dependent on foreign sources of oil, far less interested in support for Israel, opposed a counter cartel and argued for cooperation with the producers.

After the Washington conference, the United States, the Europeans and the Japanese went their own ways.<sup>17</sup> Previously on 6<sup>th</sup> January 1974, Britain, France and Spain were declared as most favoured nations by Arab States. The most favoured list was able to import all the Arab oil they required, under the easing of Arab restrictions announced on 25<sup>th</sup> December 1973.<sup>18</sup> The Arab States also exempted Japan and EEC countries except Holland from the effects of December 1973 and January 1974 cuts of 5 percent each in appreciation of the political stand taken by Japan and the common market countries on the Middle East.<sup>19</sup>

#### **A MAJOR POLICY SHIFT**

The European countries sought bilateral political and economic arrangements with the oil producers and resisted consumer bloc strategies. France the strongest opponent of the American approach, refused to join International Energy Agency IEA (the oil sharing scheme of Washington conference) and urged instead for a producer-consumer dialogue.<sup>20</sup> The Japanese government, hard-pressed by the Arab oil embargo, declared that it was grateful for the Arab decision exempting Japan from a five percent cutback in oil supplies. The new Japanese Middle East policy breaks away from its traditional dependence on the United States. A United States that can self supply the bulk of its energy factors and a Japan that must depend on imports for the greater part of them, are entirely different in their circumstances and conditions. Japan has its own way to go.<sup>21</sup>

France, Britain and to a lesser extent West Germany had shown interest in securing the oil, they needed an exchange for weapons. Undeterred by United States warnings, France had gone ahead with bilateral agreements with oil producing countries such as Saudi Arabia, Iran and some of the Gulf States. The French

Government confirmed a 20-year agreement with Saudi Arabia, under which Saudi Arabia was to deliver 800 million tons of crude oil in exchange for arms and close co-operation in the development of petrochemical and other industries. This agreement also included the delivery of 38 Mirage III, interceptor air crafts, AMX-30 tanks, light armoured cars, amphibious crafts and tactical air-to-air and ground-to-air missiles. The arms supply was in exchange for guaranteed supplies of petroleum. France also made a similar contract with Abu Dhabi. West Germany was to supply its Leopard tanks to Iran. Britain entered into a contract with Saudi Arabia which was to provide an assured supply of 30 million tons of oil a year for ten years in exchange for arms and machinery. Britain was reported to be interested in seeking similar agreements with Kuwait, Abu Dhabi and Qatar.<sup>22</sup>

On 18<sup>th</sup> March 1974, seven countries, Algeria, Bahrain, Egypt, Kuwait, Qatar, Saudi Arabia and United Arab Emirates approved to raise the embargo on deliveries to the United States. Shaikh Ahmad Zaki Yamanni, the then Saudi Arabian oil minister told the United States that Arab oil producing states, which lifted the ban on oil deliveries to United States, would re-impose it if there was reason to believe that the United States was no more serious to exert its influence on Israel to make peace with the Arabia.<sup>23</sup>

## CONCLUSION

The winding down of the Yomkippur war in early 1974 with the help of the United Nations, combined with Arab satisfaction over economic victories and over West European and Japanese revision of their Middle East policies, led OAPEC to lift the oil embargo against the United States in March 1974 and to restore production levels. In terms of Arab political demands, the oil weapon ultimately worked more effectively against Britain,

France West Germany and Japan, the most vulnerable countries. Despite the embargo, the United States did not abandon its support to Israel.

In case of the countries that submitted to Arab political demands, it was really more the threat of massive oil shortages than actual shortages that accounted for their tilt towards the Arabs. In 1967 most of them were either committed to Israel or at best unsympathetic to the Arabs. This time it had been different. Some industrial nations had shown positive appreciation of the Arab stand. Some others had at least adopted an impartial position. In the words of U. A. E. Oil Minister Oteiba "A certain change has taken place in United State's attitude towards the Middle East problem. The former total incomprehension of the Arab position had yielded place to a desire to contribute to a solution which is acceptable to the Arabs as well as Israel."<sup>24</sup>

As far as the adoption of policy of flexible response by the Arabs is concerned, it was not a sign of weakness. It was a sign of strength and realism. It is noteworthy that the Arabs had chosen their own time for lifting the embargo and had not taken the decision under duress. And there is no doubt that the oil weapon had been used with telling effect. The impact the Arab oil strategy had exerted on the industrial nations of the world was there for all to see.

The Arab oil squeeze had destroyed the myth of European unity. The common Market had been forced to deny its existence as a single trading area. It had been turned into two separate oil markets because of preferentially treated countries like Britain and France and neutrals like Belgium, West Germany, Denmark and Italy leaving aside Holland which was deemed hostile to the Arabs. The oil producers were helped by the experience of over a decade of co-operation. OPEC encouraged what one analyst described as 'solidarity and a

sense of community'. In 1973, the oil producers tested their power, saw tangible results from common action and acquired the confidence to pursue such action.

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