

THE OIL COMPANIES AND THE ARAB WORLD

Giacomo Luciani

ROUTLEDGE LIBRARY EDITIONS:
THE ECONOMICS AND POLITICS
OF OIL AND GAS



ROUTLEDGE LIBRARY EDITIONS:
THE ECONOMICS AND POLITICS OF OIL
AND GAS

Volume 9

THE OIL COMPANIES AND
THE ARAB WORLD

This page intentionally left blank

THE OIL COMPANIES AND THE ARAB WORLD

GIACOMO LUCIANI

 **Routledge**
Taylor & Francis Group
LONDON AND NEW YORK

First published in 1984 by Croom Helm Ltd

This edition first published in 2016

by Routledge

2 Park Square, Milton Park, Abingdon, Oxon OX14 4RN

and by Routledge

711 Third Avenue, New York, NY 10017

Routledge is an imprint of the Taylor & Francis Group, an informa business

© 1984 Giacomo Luciani

All rights reserved. No part of this book may be reprinted or reproduced or utilised in any form or by any electronic, mechanical, or other means, now known or hereafter invented, including photocopying and recording, or in any information storage or retrieval system, without permission in writing from the publishers.

Trademark notice: Product or corporate names may be trademarks or registered trademarks, and are used only for identification and explanation without intent to infringe.

British Library Cataloguing in Publication Data

A catalogue record for this book is available from the British Library

ISBN: 978-1-138-64127-3 (Set)

ISBN: 978-1-315-62232-3 (Set) (ebk)

ISBN: 978-1-138-64781-7 (Volume 9) (hbk)

ISBN: 978-1-138-64782-4 (Volume 9) (pbk)

ISBN: 978-1-315-62685-7 (Volume 9) (ebk)

Publisher's Note

The publisher has gone to great lengths to ensure the quality of this reprint but points out that some imperfections in the original copies may be apparent.

Disclaimer

The publisher has made every effort to trace copyright holders and would welcome correspondence from those they have been unable to trace.

The Oil Companies and the Arab World

GIACOMO LUCIANI

CROOM HELM
London & Canberra

©1984 Giacomo Luciani
Croom Helm Ltd, Provident House, Burrell Row,
Beckenham, Kent BR3 1AT

Croom Helm Australia Pty Ltd,
28 Kembla Street, Fyshwick,
ACT 2609, Australia

British Library Cataloguing in Publication Data

Luciani, Giacomo

The oil companies and the Arab world.

1. International business enterprises
2. Petroleum industry and trade
3. Petroleum industry and trade – Near East

I. Title

338.8'87 HD9560.5

ISBN 0-7099-1619-1

All rights reserved. For information, write:
St. Martin's Press, Inc., 175 Fifth Avenue, New York, NY 10010
Printed in Great Britain
First published in the United States of America in 1984

Library of Congress Cataloging in Publication Data

Luciani, Giacomo, 1948-

The oil companies and the Arab world.

Rev. translation of: Compagnie petrolifere a paesi
arabi.

Includes bibliographical references and index.

1. Petroleum industry and trade—Arab countries.
 2. International business enterprises—Arab countries.
- I. Title.

HD9578.A55L813 1984 338.8'87 83-42536
ISBN 0-312-58276-5

Printed and bound in Great Britain

For Albertina

CONTENTS

List of Abbreviations

Note on Company Names

Conversion Factors

Preface	1
Introduction	3
1. The Disintegration of the International Oil Industry	8
2. The Evolution of the Crude Supply Position of Ten International Companies	34
3. The Companies without Vertical Integration?	63
4. The Policy of the Producing Countries on Relations with the International Oil Companies	97
5. The Policies of the Oil Importing Countries	124
6. The Global Strategies of the International Oil Companies and their Attitude Towards the Arab Countries	146
7. Evolutionary Trends in the Structure of the International Oil Market	160
8. The Political Impact of the Reintegration Process	179
Index	192

ABBREVIATIONS

ADGLC	Abu Dhabi Gas Liquefaction Company
ADGIL	Abu Dhabi Gas
ADMA	Abu Dhabi Marine Areas
ADNOC	Abu Dhabi National Oil Company
ADPC	Abu Dhabi Petroleum Company (also ADCOPO or ADPC-OPCO)
AIOC	Anglo-Iranian Oil Company
Aramco	Arabian American Oil Company
BAPCO	Bahrain Petroleum Company
BNOC	British National Oil Company
BP	British Petroleum
BPC	Basrah Petroleum Company
Caltex	a 50-50 joint venture of Chevron (California Standard and Texaco
CFP	Compagnie Française des Pétroles
ENI	Ente Nazionale Idrocarburi
IEDC	International Energy Development Corporation
IEOC	International Egyptian Oil Company (a subsidiary of Agip)
INOC	Iraqi National Oil Company
IPC	Iraq Petroleum Company
JNOC	Japan National Oil Corporation (formerly JPDC)
JPDC	Japan Petroleum Development Corporation
KNPC	Kuwait National Petroleum Company
KOC	Kuwait Oil Company
KPC	Kuwait Petroleum Corporation
MPC	Mosul Petroleum Company
NIOC	National Iranian Oil Company
OECD	Organization for Economic Cooperation and Development
OAPEC	Organization of Arab Petroleum Exporting Countries
OPEC	Organization of Petroleum Exporting Countries
PDO	Petroleum Development Oman
Pemex	Petroleos Mexicanos
QPC	Qatar Petroleum Company
SABIC	Saudi Arabian Basic Industry Corporation
SNEA	Société Nationale Elf-Aquitaine
ZADCO	Zakum Development Corporation

NOTE ON COMPANY NAMES

International oil companies have remarkable vitality, and deceases are an exception; however, they seem to have a certain tendency to change their identities, or at least their names. To avoid unnecessary mental stress to the reader, we have adopted a single denomination for each company, even if this is not always entirely accurate.

The record of name changes is probably held by the company which is today known mostly as Exxon, the name used in this book. Exxon was initially a part of the Standard Oil Company; when this was broken up in 1911 it became the Standard Oil Company of New Jersey (also variously called Jersey Standard, or SONJ). Later it came increasingly to be identified as Esso, its main brand name, which it still uses in some countries. This was changed into Exxon for marketing reasons, and the latter is presently the most commonly used denomination for it.

Other companies that derive from the original Standard Oil are Mobil, Amoco and Chevron. The first was initially called the Standard Oil Company of New York, or SOCONY; it was later known also as SOCONY-Vacuum, then SOCONY Mobil, and finally Mobil. The use of the latter name is today widespread. On the other hand, the Standard Oil Company of Indiana has increasingly utilized the Amoco brand name to designate the entire company, or specific subsidiaries, but is still often known as Indiana Standard. The same applies to the Standard Oil Company of California, which has increasingly been using the brand name of Chevron to designate both subsidiaries and the company as a whole, but is still often called by its full name or by various abbreviations, most frequently Socal.

Among the European companies, British Petroleum (BP) was initially known as the Anglo-Persian Oil Company, then as the Anglo-Iranian Oil Company (or AIOC), until it changed its name after the Iranian nationalization. We call Shell the entire complex group that results from the interlocking of Royal Dutch and Shell Transport and Trading. CFP (Compagnie Française des Pétroles), although it has never changed its name, has increasingly been using its brand name, Total; we have opted for the use of the original name because this is by far the most widespread solution in the trade literature. The official name of the company that we call Elf is SNEA, standing for Société Nationale Elf-Aquitaine: I doubt that this official designation will ever become

popular among English-speaking people. In the past the same company has also been identified as ERAP, or Elf-ERAP.

Three cheers for Texaco and Gulf, which have always been faithful to their original names!

CONVERSION FACTORS

In this book statistics related to volumes of oil have been uniformly expressed in barrels per day, or b/d. The data in tons per year (t/y), which are widespread in the literature outside the Anglo-Saxon countries, were converted into b/d by using the standard conversion factor: 0.0201. The Japanese data are expressed in kilolitres: these were converted into b/d by using the factor: 0.0173.

PREFACE

This book is the result of research conducted in the spring of 1980. At the time the international oil market was still dominated by fears of severe shortcomings; but since then a state of equilibrium has been reached, and this has undoubtedly affected the way in which I now look at the evidence which I gathered at the time. My focus has shifted from the question of how the international oil companies intended to stabilize their crude supplies in the long term, to the somewhat broader issuer of whether a vertically disintegrated international oil market is a stable proposition over time. I have made an effort to update continually my evidence, and the core of the empirical material on the international oil companies was assembled in the course of interviews with numerous company officials. I was fortunate enough to be able to interview all the companies included in my sample, with the exception of BP, who answered a questionnaire which I had submitted by telling me that I evidently already knew much more about their business than they would have liked and thus saw no need to help me further! In fact, it emerges that much of the information about the companies is available in published form and can be gathered without great difficulty. Interviews seldom added to my knowledge in terms of hard facts, but they were invaluable in so far as they provided a clearer insight into company strategy. Unfortunately, these interviews were arranged with the understanding that specific sources would not be named. This I found reasonable, because individuals change or move, while companies endure. However, I thought it would not be very useful to include notes referring to interviews with 'Exxon' or 'Mobil', and thus notes and references, where included, only pertain to information for which there is a public source available.

One particular area in which interviews were of little use concerned data on company crude flows. The insufficiencies of these data is highlighted in Chapter 2, but company executives were generally unable or unwilling to explain the reason for some of the puzzling anomalies. This reflects the basic fact that sometimes inconsistency or lack of clarity is in fact deliberate, and the interviewer therefore has little bargaining power. I have not attempted to work from the other angle, i.e. interview officials of the oil-producing countries, because they are generally even more secretive, as is evident from the fact that they pub-

lish no data whatsoever, which is even worse than publishing bad data. Sometimes company data are bad because countries require that the exact origin of supplies should not be identified. In any case, not even the OECD manages to reconcile statistics on exports to statistics on imports.

As I approached the subject of the companies' strategies towards the Arab world I had no preconceived thesis that I wished to demonstrate. The main points made in this book genuinely emerged from an analysis of the empirical evidence. This is why it took three years to write the book in its present form. Since events move fast in the oil business, and in the contemporary world in general, it is almost inevitable that the factual basis of a study like this will become outdated: yet this has little importance if, from an analysis of the situation as it was at a certain moment in time, an author has managed to understand the relevant evolutionary laws. If the main theses are right, the book will be of relevance for some time to come.

This objective may or may not have been achieved. If it has, much of the merit belongs to the very many people who on various occasions discussed earlier drafts, or partial presentations at conferences and seminars. Since it is impossible to thank them all individually, I wish to single out my debt to Marcello Colitti, Domenico Tantillo and Vittorio Jucker. I greatly benefited from the discussion that took place around an earlier draft on the occasion of a joint meeting between the Royal Institute of International Affairs (Chatham House, London) and the Istituto Affari Internazionali in July 1981; and in the context of a conference organized by the Hellenic Centre for Islamic and Arab Studies in Rhodes, in September of the same year. In January 1982 I was kindly invited to introduce and discuss some of my points at a seminar held by the Rand Corporation in Santa Monica, California. I also wish to express gratitude to the Japan Centre for International Exchange, which kindly supplies a wealth of useful material on Japan on a regular basis, and specifically helped in updating the data for Table 5.1, p. 137.

A considerably different version of this book was published in Italian at the beginning of 1982. The preparation of the English version took a long time because I felt I had to rewrite extensively. I was also able to improve the statistical evidence, and wish to acknowledge the help which I received in this respect from Raffaello Pezzoli and Gabriele Marruzzo.

Neither the Istituto Affari Internazionali nor any of the people mentioned above are responsible for errors and shortcomings which, I fear will still be found in this work.

INTRODUCTION

Since 1973 most analysts of oil affairs have concentrated their attention on the attitudes and strategies of the oil producing countries. Attention has been paid to the large international oil companies mainly in order to discuss whether they are victims or accomplices of OPEC actions; whether they are monopolizing and/or slowing down the development of alternative energy sources; and from where they derived the exceptionally high profits they recorded throughout the 1970s. In this way the debate has implicitly oscillated between two extremes: on the one hand, there are those who believe that the fate of the international oil industry since 1973 has been decided almost unilaterally by the producing countries, leaving no power to the oil companies; on the other hand, there are those who see a continuing and unrelenting alliance between companies and producing countries. Needless to say, both visions are ill-founded.

The present study is based on the conviction that in recent years excessive attention has been devoted to the exporting and importing countries, and too little to the companies. Too much has been said on prices, long-term equilibria and the politics of oil, and too little on the structure of the industry. While no one would claim that the former are unimportant, the latter is important as well. Thus we propose a discussion of the structure of the international oil industry which is based, in particular, on an in-depth study of the relations between a group of ten international oil companies (six American: Amoco, Exxon, Gulf, Mobil, Chevron, Texaco; four European: BP, CFP, Elf, Shell) and the Arab countries. There are, of course, many more companies (a special discussion is devoted to the Japanese and Italian experiences), and there are also non-Arab exporters. Yet, for reasons which are explicit in the book, the relationship between these two main groups of actors will potentially determine the future structure of the industry at the international level.

The fact that the structure of the industry changed fundamentally during the 1970s, when a process of vertical disintegration took place, has already been underlined in the literature; it is, indeed, a very evident fact. However, all authors of whom I am aware have concentrated their attention on a general description of the phenomenon: a list of nationalizations and a few aggregate figures on the share of oil traded by the companies in, say, 1970 and 1979 immediately prove

that the structure of the industry has changed. Yet a more careful analysis, which we propose, will show that the change has affected individual companies very unevenly, and each is responding to the new situation in a different way. Thus in a sense the structure may have changed either more or less than the aggregate figures would lead us to think: it depends on how a few crucial situations are assessed.

On this basis, we propose a discussion of how the structure of the industry might evolve. Here, as well, little more than isolated hints are to be found in the literature.

Some of the authors who mention the problem seem to believe that the process of vertical disintegration is irreversible, and that it constitutes no problem: things may and will stay as they are. Thus the well-known and reputed scholar Yusif Sayigh, in a recent book, deals extensively with what he calls 'the policy of control',¹ and I call vertical disintegration; but he sees little problem in another policy area that he identifies, namely marketing, except to the extent that 'there is a substantial shortage in aggregate supply, in which case there will have to be a deliberate adjustment of the various shares of the customers'.² The opposite situation, in which there is excess supply, and the national oil companies of the Arab countries find themselves unable to market the volume of oil that they targeted, is not raised.

Another eminent analyst and protagonist of oil affairs, Fadil al-Chalabi, sees some problems related to the process of vertical disintegration, but never to the point that one should raise the question of a possible process of reintegration. The national oil companies limiting operations to the territory of their respective country is seen as a limit, but not for marketing:

The impact of this change on the oil industry in the producing countries could be tremendous, as the nature of the strict concept of territoriality (excessive localism) prevents the realization of as high a profit return for the group of producing nations as the companies used to achieve when they divided the investment risk among themselves on the basis of the region as a whole.³

In other words, the problem is seen to be more in the decline of concentration or horizontal integration at the stage of oil production, than in vertical disintegration, meaning separation of production from marketing.

Some doubts are raised by Ian Seymour, but not greatly developed:

An industry which has hitherto been characterized by an abnormally high degree of integration, right from the production of the raw material to the sale of the final processed product, is now in the process of disintegration. This could mean that oil will in time begin to exhibit more of the features of other raw material industries (even with futures markets and things like that). On the other hand, one should not underestimate the centripetal drive towards integration in an industry as closely-knit and strategic as oil. The OPEC producers are themselves engaging in a certain degree of downstream integration . . . For the majors themselves, as functioning organizations, the change will be hard to digest . . . There are numerous ways in which the big oil companies can make use of the technological, managerial and financial trump cards at their disposal to improve their prospects in the OPEC countries or at least ensure that their positions are not undermined any further.⁴

These are brilliant intuitions, and the present study is essentially an attempt to spell these points out in detail, and look at the consequences.

In recent years other studies have addressed the question of the role of the oil companies, but little attempt has been made to connect the discussion on the companies to its inevitable implications for the international oil market. An example of this is the work of Louis Turner, who argues against the notion that the national oil companies of the producing countries should expand abroad. He believes that 'the assumption that national oil companies should base themselves on the integrated model of the majors' is a 'drawback', because 'times have changed'.⁵ Further on he sees that:

the national oil companies have two main strategies for which they can opt. First they can ape the majors by building up their expertise in all stages of the oil industry . . . [or they] can opt for a second strategy, playing a marginal role in the international industry but becoming leading industrial conglomerates in their own economies.⁶

While his reasons for favouring the second strategy are not to be rejected, the question is: if the national oil companies do so, what will the implications be for the international oil market? The answer is clearly that it will continue to be disintegrated, with grievous consequences on price and income stability for the oil producing countries. Thus one sees that the first strategy is not an alternative to, but a pre-

condition for, the second.

The issue has recently been touched upon by Morris Adelman, in a fashion that raises the question of political prejudice. Adelman's reasoning starts with recording the demise of vertical integration:

The oil companies stood at the centre of the stage in 1962. The largest eight still accounted for nearly all of the oil shipped in international trade. They owned the oil reserves from which they produced a growing flow, partly for resale but mostly for their own refineries. This integrated system no longer exists.⁷

Adelman believes that the situation of vertical disintegration will persist, essentially because the producing countries are structurally in bad faith:

In the 1970s a company buying at official prices did better during tight markets, when spot prices and product prices went above the official price. They did worse during gluts, when spot and product prices were lower. But now, when the OPEC nations make the market tight, companies will be charged the higher spot prices, contract or no contract. When spot prices drop below contract, companies with contracts must pay the higher contract prices. Hence contracts no longer benefit companies.⁸

As to the possibility of further exploration for oil in the developing countries, Adelman believes that companies are not interested: 'They know that if they make a profitable find, the host government will unilaterally change the terms of the bargain, to take more of the profit.'⁹

These things have certainly happened: but to generalize and believe that therefore only arm's-length relations are possible, with a short-term validity and in a vertically disintegrated context, seems irrational and unacceptable. This may be my prejudice: I believe that the oil producing countries are not stupid – they make mistakes, but in the long run should be assumed to be capable of serving their own interests.

Finally, I wish to recall the work of Peter Cowhey, which is very close to my own. I will not attempt to summarize the three scenarios that he proposes in an interesting paper,¹⁰ for fear of not appropriately conveying his thought. Cowhey addresses many of the same questions that I do, but lays relatively more emphasis on the companies (considering their activities outside the oil sector, and globally) than on the oil market specifically. The scenarios that I propose in Chapter Seven of

this book may be combined with those proposed by Cowhey, and this may be done in various combinations, excluding a biunivocal link.

The foregoing reflects the fact that the degree of vertical integration, disintegration and reintegration are not the only characteristic features of the structure of the international oil market. I simply believe that they are very important, and this is what this book attempts to prove.

Notes

1. Yusif A. Sayigh, *Arab Oil Policies in the 1970s* (Croom Helm, London, 1983), Ch. 2.
2. *Ibid.*, p. 13.
3. Fadhil J. Al-Chalabi, *OPEC and the International Oil Industry: a Changing Structure* (Oxford University Press, Oxford, 1980), p. 30.
4. Ian Seymour, *OPEC, Instrument of Change* (Macmillan, London, 1980), pp. 233-4.
5. Louis Turner, *Oil Companies in the International System* (Allen & Unwin, London, 1978), p. 206.
6. *Ibid.*, pp. 213-14.
7. Morris, A. Adelman, 'Oil Prices: the Protagonists', paper delivered to the Memorial for Enrico Mattei (organized by ENI, Rome, Oct. 1982), p. 2.
8. *Ibid.*, p. 3.
9. *Ibid.*, p. 5.
10. Peter F. Cowhey, 'The Future of the International Oil Companies and the Probable Evolution of the World Energy System in the Eighties', paper prepared for the 'International Workshop on Prospects for the World Hydrocarbon Markets for the 1980s' (El Colegio de Mexico, Mexico, 31 March-2 April 1982, mimeo).

1 THE DISINTEGRATION OF THE INTERNATIONAL OIL INDUSTRY

Among the dramatic changes that occurred in the international oil industry in the 1970s, the increase in the price of crude attracted by far the greatest attention. Understandably so: after all, most people see oil only in terms of whether there is cheap petrol to fill the tanks of their cars and heating oil to keep a comfortable temperature in their homes. Yet the international oil industry has seen far greater changes than in the price system alone.

Our concern in this book is not with the price increases but with the change in the 'structure' (or 'organization')¹ of the industry itself, in other words, the degree and pattern of vertical integration and horizontal concentration that characterize it. These aspects are normally of little interest to the man in the street, but to anyone connected to the oil industry they are probably much more important than the price itself. Because — to put it bluntly and in an extremely simplified way — what is bad about price increases if I am in a position to increase my profits as well? What is good if I am not?

Furthermore, corporate power attracts the attention and imagination of the wider public. From the very beginning of the oil industry itself, in the latter part of the nineteenth century, the industry has come to be identified as the Leviathan of corporate power. *Ex post facto*, one cannot avoid the impression that this perception was never truly warranted, not even at the time when the Seven Sisters² defeated Mossadeq's nationalization in Iran. It is even less warranted today, after they have lost substantial ground, and very rapidly so in the last decade. Thus the issue is of more general importance to the wider field of political economy.

But history is not linear, nor is it unambiguous. Many people will deny that the international oil majors have indeed lost as much ground as I will argue that they have. Moreover, lost ground may be recovered, and we cannot rule out the possibility that, after a long cyclical phase of vertical disintegration, a new phase has begun or will soon begin in which some kind of vertical reintegration processes will take place.

What is most striking is that companies themselves have very diverse understandings of their own fortunes, and react with widely differing strategies.