THE POLITICS OF

OIL

A SURVEY
Foreword

*The Politics of Oil* aims to provide up-to-date information on and analysis of essential aspects of oil politics, with the intention that it should serve as a reference book.

The volume is divided into four parts. The first consists of essays which endeavour to present some of the latest research findings, and in this way to initiate further enquiry into the topic. An Introduction, followed by a piece on oil and the global political economy by Darrell Whitman, set the scene for the subsequent essays. The second essay, by Emre Iseri, provides an account of the geopolitics of oil and pipelines in the Eurasian Heartland. Erin Mofford, in the third contribution, examines oil and power in the Caspian Sea region, focusing on supermajor oil companies and geopolitics. Production Sharing Agreements and oil nationalism in the context of Iraq are the subject of the fourth essay, by Vassilis Fouskas. Øystein Noreng’s essay focuses on the subject of oil and Islam, and the section concludes with Chukwumerije Okereke’s examination of oil politics and environmental conflict in Nigeria.

The second part of the book provides an extensive A–Z glossary section, prepared by Bülent Gökay. This glossary provides essential factual and analytical information on relevant terms, issues and personalities in the area of world oil politics. Entries are cross-referenced for ease of use.

The third section consists of a number of maps and statistical tables, which furnish the reader with an important guide to understanding the politics of oil in relation to various production regions and key issues.

The final section contains a select bibliography organized into specific fields of interest. This bibliography is not in any respect comprehensive—a select bibliography is, by definition, limited. The aim of the bibliography is to guide those who are interested in studying the politics of oil towards the main books and articles, which, it is hoped, will both inform and entertain them. It is dedicated to those who have an interest in the subject but who do not know precise bibliographic details of the key sources.

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Abbreviations

b/d  barrels per day
bbl  barrels of oil
c.   circa
Cent. Central
DC   District of Columbia
Dr   Doctor
Ed   Editor
Edn  Edition
Gen. General
m.   million
OECD Organisation for Economic Co-operation and Development
OPEC Organization of the Petroleum Exporting Countries
Rep. Republic
Rev. Revenue
S.   South
UK   United Kingdom
UN   United Nations
US   United States
USA  United States of America
Essays
Introduction: How Oil Fuels World Politics

BÜLENT GÖKAY

‘Standard Oil (now ExxonMobil) and Shell seat and unseat kings and presidents, finance palace plots and coups d’états, have innumerable generals, ministers and James Bonds at their command … make decisions about peace or war in every field and every language.’ (Eduardo Galeano, Open Veins of Latin America)\(^1\)

Oil is the most strategic raw material. It can hardly be overstated how crucial petroleum is to our modern industrial society. Virtually every aspect of modern industrial life requires oil, gas and—largely created from these fossil fuels—electricity. The economic history of the last 200 years has been a succession of technological transformations in the way of finding and delivering energy to production, transport and communications—first based on coal and steam, then on petroleum, then on electricity and electronic communications—which is also based on a mixture of fossil fuels (oil, gas and coal) and nuclear power. This is the story of how our modern system of production has evolved essential material characteristics, most critically those of the carbon economy. How have we become so dependent upon oil?

The story starts in AD 347 in China, where the first oil wells were drilled. These wells were 240 m deep and bamboo poles were used to extract the oil. The first modern oil well, however, was drilled in the Tsarist Russian Empire in 1848. According to the Azerbaijan Academy of Science, this well was prepared in what is now known as the giant Bibi-Eibat field in Baku. This was not even intentional! Oil was discovered during drilling for water. However, mechanical drilling did not substitute digging by hand until drilling machinery was imported to Baku in 1871, which was followed by the opening of large flowing wells in 1873.

The modern history of the oil industry began in 1853, with the discovery of the process of oil distillation. Crude oil was first distilled into kerosene by Ignacy Łukasiewicz, a Polish pharmacist. He also invented the petroleum kerosene lamp, which he used in 1853 to light a local hospital in Lvov so that an emergency surgical operation could be performed. As a result, the first ‘rock

ESSAYS

Oil’ mine was opened in Bóbrka (near Krosno) in southern Poland in the following year and the first oil refinery was constructed in Ulaszowice, also by Łukasiewicz. Six years after Łukasiewicz’s refinery was constructed, Edwin L. Drake drilled the first modern technological oil well, which was about 21 m deep, near Titusville in north-western Pennsylvania. The invention of the kerosene lamp, by Łukasiewicz in Poland, had ignited strong demand for oil world-wide. By drilling an oil well, Drake was keen to profit from the growing demand in the USA for oil for lighting and industrial lubrication. His business quickly made huge profits. Drake’s success encouraged hundreds of entrepreneurs and small companies to search for oil in the USA. As a result, in 1860, world oil production reached 500,000 barrels; and by the 1870s oil production had climbed to 20m. barrels annually.

The distinguished Russian chemist Dimitri Mendeleyev, who was commissioned to analyse technological development in the Caspian-Caucasus oil region, attended the US Centennial Exposition at Philadelphia in 1876 as a member of the official Russian delegation. This offered him the opportunity to visit the Pennsylvanian oil-producing region. He was impressed by the fact that the Pennsylvania oil belt and the principal axes of the Alleghany mountains bore a remarkable resemblance to the Baku fields and the Caucasus mountains. After this visit, more collaboration between the Russian oil industry and its US counterpart took place in the field of technological know-how.2

As oil production exploded, prices fell and oil industry profits dropped—basic economics. In 1882, John D. Rockefeller, the US industrialist who set up the Standard Oil company, worked out a solution to the problem of unrestrained competition in the oilfields: he managed to establish a kind of monopolistic control, and the Standard Oil trust was born, which brought together 40 of the USA’s foremost refiners. Through its control of refining, Standard Oil trust was temporarily able to regulate the price of oil and restore high profits.

Up until the 1910s, it was the USA which produced 60%–70% of the world’s oil supply. As fear intensified that US oil reserves were becoming depleted, the search for oil turned to the rest of the world. Oil was discovered in Mexico at the beginning of the 20th century, in Iran in 1908, in Venezuela during the First World War, and in Iraq in 1927. Many of the new oil discoveries took place in areas controlled by the British and Dutch empires. Indeed, in the early years of the 20th century, when Great Britain had converted its naval fleet from coal to oil propulsion, the relationship between oil and military power had become the central driver of imperial policies. Lacking any petroleum reserves of its own, the British Empire found itself dependent on rich oil resources in the Middle East. During the First World War, keeping those oil-rich lands under British control became a crucial war goal for Britain. As a result, by 1919, Britain found itself practically controlling 50% of the world’s proven oil reserves. Therefore, it was not surprising to see the start of a bitter battle for control of world oil reserves in the aftermath of the the First World War. Britain, Holland and France disallowed

US companies from purchasing (or operating in) oilfields in territories under their domination. The US Congress struck back in 1920 by introducing the Mineral Leasing Act, which denied right of entry to US oil reserves to any foreign country that limited US access to oil reserves under its control. The quarrel was partly resolved during the 1920s when some US oil companies were finally permitted to drill in the British Middle East and the Dutch East Indies.

In the USA, during the early 20th century, despite earlier fears, oil production continued to climb. By 1920, it had reached 450m. barrels, which again prompted fears that the nation was about to run out of oil. Government officials predicted that US oil reserves would not even last for another 10 years. However, the discovery of enormous new oilfields in Texas, Oklahoma, and California in 1924 ended the fear that US oil reserves were nearly exhausted. As a result of these discoveries, together with production from new fields outside the USA, most importantly in Mexico, the Soviet Union and Venezuela, oil prices again declined drastically. By 1931, with crude oil selling for 10 US cents a barrel, US oil producers were calling for restrictions on production in order to raise prices to a profitable level. In response, Texas and Oklahoma passed state laws and stationed militia units at oilfields to prevent drillers from exceeding production quotas. Despite these measures, prices continued to fall.

During the Second World War, however, the oil surpluses of the 1930s quickly disappeared. The heavy war machine of the Allied forces was consuming huge quantities. Six thousand million of the seven thousand million barrels of petroleum used by the Western allies during the war came from the USA. In the 1940s, the USA began to rely on foreign oil to fulfil rising energy demand. There emerged serious worries once again that the USA was running out of oil.

After the war, it seemed imperative that the USA secure access to foreign oil reserves. Energy security became an essential dimension of state security. Increasingly, policy-makers and the oil industry focused their attention on the Middle East, particularly the Persian (Arabian) Gulf, which they rightly believed would become the centre of post-war oil production. As early as the 1930s, Britain had gained control over Iran’s oilfields and the US companies discovered oil reserves in Kuwait and Saudi Arabia. After the war ended, Middle Eastern oil production maintained its upward surge. From that point on, gradually, US dependence on Middle Eastern oil increased.

During the 1950s, a mixture of cheap fuel and a rapidly increasing consumer culture led to frantic indulgence in consumption. With only 6% of the world’s population, the USA accounted for one-third of global oil consumption. Foreign oil was so cheap that coal-burning utilities led the expensive shift to oil and natural gas. But this optimism based on readily available cheap oil did not last. Initially, in 1960, low oil prices pushed Iran, Venezuela, and Arab oil producers to group together to form the Organization of Petroleum Exporting Countries (OPEC), a producers’ cartel, to negotiate higher oil prices. OPEC was fashioned after the thinking of Argentinian economist Raúl Prebisch, who chaired the UN Economic Commission for Latin America and promoted the idea that national sovereignty over natural resources was essential for successful development.
OPEC was organized as a producers’ bloc that could collectively bargain for the price of oil and thus enhance oil’s value for the producing countries. Several large oil-producing countries, however, including the Soviet Union and the USA, remained outside of OPEC and actively worked to undermine its power to control oil prices.

By the early 1970s, the USA depended on the Middle East for one-third of its oil. Foreign oil producers were finally in a position to raise world oil prices. The oil embargo of 1973 and 1974, during which oil prices quadrupled, and the oil crisis of 1978 and 1979, when oil prices doubled, graphically demonstrated how vulnerable the USA (and Europe) had become to foreign producers. In response to this situation, US President Jimmy Carter introduced the so-called ‘Carter Doctrine’, labelling access to Middle Eastern oil resources as a vital US security interest. In order to implement this doctrine, Carter established the Rapid Deployment Joint Task Force and initiated a web of US military and intelligence base arrangements in the Middle East oil region.

The oil crises of the 1970s were a painful reminder of the critical role that oil plays in the global political economy. These crises had also an unanticipated side effect. Rising oil prices stimulated conservation and exploration for new oil sources. As a result of increasing supplies and declining demand, oil prices fell from US $35 a barrel in 1981 to US $9 a barrel in 1986. The sharp slide in world oil prices was one of the factors that led Iraq to invade neighbouring Kuwait in 1990, in a miscalculated attempt to secure control over 40% of Middle Eastern oil reserves. The expulsion of Iraqi forces from Kuwait in February 1991 produced a degree of stability, for about 10 years, in this strategic oil region. The same events, however, underlined once more the growing reliance of the Western industrialized economies on foreign oil.

Despite these ups and downs in oil prices, it is an unquestionable fact that the petroleum industry is among the most rewarding and most important in the world, and its impact on international politics is colossal. We live in a petroleum landscape, in the sense that the advance made in industry and technology over the last 150 years and the luxury we enjoy every day have been made possible by one thing and one thing only: cheap energy, in the form of oil. The whole success of the world economic system, the so-called prosperity of the 20th century, was driven by cheap, oil-based energy. Oil fuels the economy. If gold was the standard for currency and economic progress for much of the 19th and early 20th centuries, it has now been replaced by oil. The ability to set the price of gold against a particular currency, as happened with the post-Second World War dollar, has now been replaced by the ability to set the price of oil against a particular currency. But, unlike gold, oil has the added power of being central to the industrial processes of modern economies: it does not rely on a perception of value, but on its actual instrumental value as an essential commodity. Thus, holding the power of setting oil’s value against a currency means that transactions in oil will naturally gravitate toward that currency as the most stable indicator of its value. This logic is fully played out when oil contracts are required to be valued in a particular currency, whose strength is then reinforced by the demand.
Introduction: How Oil Fuels World Politics

for the currency created by the contracting parties. Since 1975, when the USA concluded an agreement with Saudi Arabia (OPEC's most powerful member), OPEC has been committed to pricing oil exclusively in dollars. This understanding, much of it never publicized and little understood by the public, provided the Saudi ruling family the security it craved in a dangerous neighbourhood while ensuring that the USA had a reliable and very important ally in OPEC. Since then, practically all oil has been traded in US dollars. Hence the oil standard became the dollar standard. In 2002, a former US ambassador to Saudi Arabia told a committee of the US Congress: ‘One of the major things the Saudis have historically done, in part out of friendship with the US, is to insist that oil continues to be priced in dollars. Therefore the US Treasury can print money and buy oil, which is an advantage no other country has.'

Oil is also a determinant of national security. Today's modern armies are entirely dependent on oil-powered ships, planes, helicopters and armoured vehicles. A defining characteristic of the second half of the 20th century was very swift, accelerating, inescapable technological change. At the same time, rapid societal change and organizational adaptations by military forces were also taking place. The military establishments of the industrialised countries are making the most of the new technology that they are introducing, and have energetically exploited and experimented with it in military campaigns since the end of the Cold War. All of this new technology, including high-tech precision weaponry and new information systems, however, is exclusively based on oil-based energy. Modern military technology is exclusively dependent on oil. Oil has become the pivot upon which the axis of war and peace rests. This is consistent with a historical pattern in which control of precious minerals has directly or indirectly led to war. In the last century alone, oil played a key role in at least 10 of the 12 major conflicts. It seems that of all the resources that are critical to modern industrial society in the 21st century, none is more likely to provoke a major war between states than oil, and as oil reserves decline its importance will only grow in the decades ahead.

As a result, over the last century, the demand for oil has risen dramatically and the physical structure of our society is organized around the assumption that there will always be plenty of it. What makes it possible that we do what we do? What makes us have jobs? How can we buy anything we want? What powers all the conveniences we enjoy in our houses? What fuels our cars and airplanes? What makes the water flow? Why are the supermarkets always full of food? What is this magical thing?

It is energy. Massively available, cheap energy. Cheap energy is essential for the world economic system. Even to produce food we need to burn oil: 17% of our energy is used for producing food. Modern agriculture makes heavy use of oil

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in a variety of ways. We use oil for fertilizers, pesticides, and for the packaging and distribution of food. Since the beginning of the 20th century, global trade and a global economy have developed, and our population has grown in size from 1,000m. to 6,000m. by drawing down a massive natural gift of energy in the form of cheap crude oil. Indeed, all economies are energy-dependent. There are no exceptions.

Up until early modern times, miners, scientists, natural philosophers and other 'experts' believed that gold, silver and other minerals were vegetable-like in that, when mined, they would literally grow back like mown grass. This belief was not wrong in principle in the case of coal and its hydrocarbon cousins in gaseous and liquid form, because they are the remains of ancient organisms. As a practical maxim, however, it was completely mistaken, because the time it would take normal geological processes to transform organic matter into coal, natural gas and petroleum is of the order of millions of years. Therefore, for all practical purposes, these fuels are finite, non-renewable energy resources.

In 1956, much to the surprise of most oil experts and industry executives, M. King Hubbert, a geophysicist working as an oil consultant to Shell Oil Company, developed a simple model of US oil production which predicted that the USA would peak in its oil production in the next 10–15 years (i.e. in 1966–71) and enter a permanent decline. This model was considered highly contentious for that era, and most economists and other experts, who thought the analysis failed to take the effects of market prices into consideration, rejected Hubbert's results. Many others, including Shell executives, also thought Hubbert's analysis was invalid and defeatist and would damage support for the home-based, US oil industry. Just before the time that the real price for petroleum inflated following the attempted oil embargo related to the October 1973 Arab–Israeli War, US oil production did indeed peak and entered a permanent decline. Hubbert was proved right. Since then many petroleum experts and economists have used Hubbert's method to predict the timing of the oil peak world-wide.

More than a quarter of a century later, similar questions to those asked earlier about the USA are now being asked about oil production world-wide. Is world production of so-called 'easy oil' approaching its peak? If world oil production does reach a peak, will it straight away begin to trend downwards, and, if so, how does this affect oil prices? Most predictions made in advance of the peak are likely to be highly unreliable, mainly because production and resource figures from many countries are not reliable. Both oil companies and countries have financial and political incentives to either over- or underestimate the amount of oil reserves under their control. The real world peak point can only be empirically visible when world oil production passes its highest point. Once the world-wide peak takes place, how steep will the curve of decline be thereafter? These questions, whose answers are at present all perplexing, are seriously worrying. Oil-producing countries that have peaked already are the United Kingdom, Norway, China, Mexico, Venezuela, Indonesia, Russia, Syria, Libya, Nigeria, Qatar and many others. Only part of the Middle East and the Caspian Sea region have spare capacity, and their reserve figures are not very transparent.
Introduction: How Oil Fuels World Politics

Today, it seems that the idea that the world may have hit ‘peak oil’ seems to be taking hold; and oil and gas experts around the world are growing alarmed not just at future scarcity, but also at who is in control of the remaining ‘black gold’. As demand for energy explodes worldwide, there is less of it available and, it seems, less exploration for it. According to many estimates, world oil production will peak between 2004 and 2008, which means that the world is depleting oil reserves at an annual rate of 6%. At the same time, growth in demand is rising at an annual rate of 2%. All this means that the world’s oil industry would have to find the equivalent of 8% a year in newly discovered oil reserves to maintain an orderly oil market. Unfortunately, discoveries are lagging behind, primarily because new large oil deposits are not being found, but also because even if they were there is a considerable time lag between a discovery and turning the oil into a usable energy product. While conservation and renewable energy are much in the news, the reality is that neither of these factors are likely to have any significant impact on the steadily growing demand for oil products. As an essential energy source, oil is still hard to beat.

During the last 10–12 years 3,000m. people from China and India have entered what we call the global economy. Currently, the economic power of China and India is growing at three to five times the gross domestic product (GDP) rate of Western states, which is the main reason for fast-growing demands for oil. China was the world’s second largest consumer of petroleum products in 2004, having surpassed Japan for the first time in 2003, with total demand of 6.5m. barrels per day (b/d). China’s oil demand is projected by the US Energy Information Administration to reach 14.2m. b/d by 2025, with net imports of 10.9m. b/d. China is currently seeking oil security through multiple channels, buying shares or making investments in various oil construction projects all over the world. In this atmosphere, competition for existing proven and prospective reserves is increasing sharply and dangerously.

In the century-and-a-half since Edwin L. Drake drilled the first modern oil well in Pennsylvania, the history of the oil industry has been a story of gigantic swings between times of over-production, when low prices and profits led oil producers to create ways to limit output and raise prices, and times when oil supplies were feared to be on the brink of exhaustion, initiating a world-wide search for new oil sources. At stake are thousands of millions of dollars in oil and natural gas revenues and the vast geopolitical and military advantages that fall to the power or powers that secure a dominant position in the oil regions. Two basic questions are key to understanding oil politics in the 21st century: who owns the remaining oil resources, and who will control the transportation of this oil to world markets? The answers to these questions will strongly influence how the world economy evolves in this century. In a world that runs on oil, the power that keeps the flow of oil under control has that key strategic authority.

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At the beginning of the new millennium, this cycle may now be approaching an end, simply because soon there may not be enough oil left. It appears that world oil supplies may truly be reaching the natural limits imposed on them by the laws of physics. With proven world oil reserves anticipated to last less than 40 years, the age of the modern oil industry may be coming to an end. There are already some indications that, in the years to come, the search for new sources of oil may be transformed into a quest for entirely new sources of energy. Oil politics is no longer just an industrial matter or a regional matter, but a world-wide security issue. Today, more than ever, oil politics is at the core of security and world politics. Many international conflicts in the world today are rooted in oil politics. That is why, in the first decade of the 21st century, oil politics represents world politics more than anything else.
As Good as Gold: Oil and the Global Political Economy

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