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Oil Gates Remain Ajar But Not Open

by Professor Gustav Schachter, Boston *

For the past century, the United States Government has strived to remain independent with regard to its sources of energy requirements for industry and transportation. The transition from water to steam did not create any problems in this respect; coal of good caloric content is abundant in the United States. With the discovery of oil in Pennsylvania a century ago, this situation did not seem to change. By 1914 half of the energy needs in industry was still derived from steam and in transportation the steam locomotive still reigned. Petroleum, however, made steady inroads in the American economy, reaching supremacy well before World War II.

Development of Automobile Industry

The automobile has been for the last two generations the *modus operandi* in the United States. Here, the gasoline propelled vehicle which had a glorious start at the beginning of this century in Europe, expanded beyond any prediction. In the United States there are about 100 mn cars on the road, and over the last decade, annual sales of cars averaged 10 mn. In 1967, these cars together with airplanes have consumed about 80 bn gallons of gasoline (1,846 mn barrels). The total United States production of petroleum for the last few years averaged 3 bn barrels annually. United States oil reserves (including the new discoveries in Alaska) are about 45 bn barrels. Assuming that gasoline consumption will stabilize to about 3 bn barrels per annum and with the same ratio of domestic to net oil imports (80 p.c. — 20 p.c.), the United States is secure in its oil supply for the next 15 years. This is why it is ridiculous to have restrictive trade policies for oil imports.

The Domestic Scene

In the past, this country wanted to induce entrepreneurs to search for oil. At the time it was understandably justified to subsidize them under the guise of depletion allowances to encourage

optimal production and to satisfy the growing need for petroleum products. Today, granting these subsidies to the already extremely lucrative oil extraction industries seems outrageous. Oil companies with total profits of about \$7.5 bn in 1968, paid 8 p.c. of their incomes in taxes while other corporations paid about 40 p.c. Therefore, now the depletion allowance is, in reality, just a giveaway program. This program is detrimental to other corporations and to the public at large who have to make up the gap in taxation. But this is only one side of the story. The other side is a nightmare of political manipulation.

Allegedly, for security reasons, about 80 p.c. of the oil consumed in the United States must come from the domestic producers. The remaining 20 p.c. is allocated under a special quota system to other friendly oil-producing countries. The United States prohibits outright oil importation over and above the quotas. This constitutes a windfall for domestic oil producers and a great loss for the American consumer. The price per barrel of United States produced oil is \$3; one barrel of Middle East produced oil FOB New York is about \$1.50¹. Erwin Knoll, quotes John M. Blair, the Senate Subcommittee Chief Economist, that oil quotas "cost the American public \$40 bn to \$70 bn in the last 10 years"².

All this shows that businessmen and the public at large are penalized by

☐ having to pay more taxes to replace the possible oil tariff which could bring the Treasury over a billion dollars a year and thus reduce the burden on taxpayers,

☐ must pay higher prices for gasoline³, and

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¹ True, with the closing of the Suez Canal, oil from the Persian Gulf, because of the roundabout way tankers must take, could cost twice as much FOB, New York.

² Erwin Knoll, The Oil Lobby is not Depleted, The New York Times Magazine, March 8, 1970.

³ The differential paid by petroleum users (gasoline and heating oil is about 8 cents per gallon, this is 50 p.c. of net dealer yield per gallon at 16.31 cents excluding taxes in 1967) or about \$100 per family.

☐ suffering because of the inflationary basis brought about by these prices.

US Policies

In February 1970, a United States Presidential Task Force completed a study on oil policies. Their recommendation included replacing the quota system by tariffs. Even at a high tariff, foreign oil could compete with US oil producers by supplying only a small share of the US oil requirements. This, of course, did not please the oil industry in the United States. They were worried about losing their monopolistic control and thus high monopolistic profits. They put strong pressure on the United States Government not to tamper with the entrenched quotas. In fact the President, after receiving the Task Force Report and recommendation, decided to just file it away. But Congress thought otherwise. In the tariff bill now before the House and Senate, the quota provision is retained for oil and extended to other commodities.

This retention of oil quotas (President Nixon promised to veto a trade bill containing quotas, but he is more concerned with other commodities rather than oil) baffles economists and laymen alike. US oil known reserves are expected to run out around 1985, and then the dependency on foreign producers will be complete and disastrous. Since for US oil companies (or for any profit-oriented oligopoly) high returns outweigh any future gains, it seems that a quota should be imposed on US production to lengthen the process of exhaustion of domestic resources.

Shifts to Other Energy Sources

It is often also claimed that the worry about oil is exaggerated because of the shifts in the sources of energy. Gas is one of them, and it is rapidly becoming a major contributor. Between 1950 and 1965, gas for industrial use increased its share of the market from 30 to 45 p.c. At the same time, the share of oil fell by as much. Also, 55 p.c. of fuel to generate electricity is provided by coal. Until now, nuclear energy has not fulfilled the hopes of the 1950s; it was found to be too expensive and too polluting as compared with other sources of energy. In the 1960s, oil, natural gas, and coal (in this order), had been the main energy source (about 96 p.c.⁴) for all uses. The highest oil user is, and will remain, the automobile. Indeed, in the 1960s, more than 50 p.c. of all petroleum demand energy was used for transportation.

⁴ The remaining 4 p.c. energy source is derived from water power mainly for generating electricity.

It seems that for the 1970s, the US energy policy is, in the last analysis, a petroleum policy⁵. This is so in terms of uses as well as resources. Coal does not present problems for the United States. It is plentiful; about 600 mn tons are consumed per year with known reserves of about 800 bn tons. In terms of oil, the known reserves would hardly last for two decades⁶.

Oil Companies Claims

The major claim of the oil lobby against oil imports is that the United States cannot rely on foreign supplies. They cite the volatile situation in the Middle East. True enough, the Middle East, with oil reserves of 311 bn barrels, accounts for three-quarters of all "free world" oil reserves and produces annually an amount equal to that of the United States. The political situation in each Middle East country has been precarious since World War II. However, during the 1967 Six-Day War, the major oil producers—Kuwait, Libya, Saudi Arabia, and Iran—(two-thirds of area oil production) were willing to supply Western Europe but were hampered by the closure of the Suez Canal. The Soviet Union, allegedly the friend of the Arabs, filled in the gap by selling Soviet oil to Western Europe.

A volatile international oil market can, at times, disturb normal activities in the importing country. Still, US could double its imports without much peril in time of crisis. This is so because industrial uses could be easily satisfied at a reduced domestic production. Industry accounts for only about 25 p.c. of total oil consumption in the United States. The only one affected for the very short run (the time lapse between stoppage of deliveries from abroad and enlarging again domestic production) would not be the industry which could continue to get domestic oil, but the pleasure cars for which gasoline can be rationed. Cryptically, this would be a great bonanza for the US air breathers. It is even doubtful that such a situation would arise because alternative foreign producers (e.g., Canada, Venezuela, West Africa) could easily fill the gap almost in a day's notice.

It must be recognized that being an oil producer and being able to sell are two different propositions. The major oil consumers in the world today are the United States, Japan, and Western Europe. The rest of the world accounts just for an insignificant fraction of the total. The USSR

⁵ While apparent natural gas reserves are also only for about 15 years, importation of liquified gas is more difficult and also, Canadian natural gas is easily transportable to the US by pipe.

⁶ Domestic shale oil might add to total output.

consumes today about 2 bn barrels (almost equal to the amount it produces) mainly for uses other than the car which even in the 1970s is projected to be a minor user. The USSR does not have the potential to be an oil trade partner (either as a seller or a buyer) in the foreseeable future. The Middle East producers, therefore, have no alternative than to cultivate outlets in the West.

Dichotomy in Argumentation

Considering this situation, it seems strange that American oil companies and others (e.g., David Rockefeller of Chase Manhattan Bank) get upset about US "commercial position" in that area. Moreover, these same oil companies are the ones who have been putting pressure successfully on the United States Government to prohibit oil imports. On the other hand, these corporations want the United States to protect their foreign oil revenues.

United States oil companies (at times together with Western European companies) control most of the Middle East oil production and distribution, but this is of little benefit to the United States in terms of obtaining cheaper energy supply or enriching the United States population at large. Much of the odd 1 bn dollars of foreign oil revenues is reinvested abroad with only a marginal positive effect on US balance of payments. Also, it is true that dividends of these companies tend at times to be higher than those paid by other corporations. But what is paid in dividends, as noted, is extracted back through higher prices on sales of domestic oil in the United States.

Necessary Amendments

The concern in the use of any energy source must be to satisfy both the individual and the nation. This suggests that

☐ the oil depletion allowance should be completely eliminated, thus avoiding inequities for other businesses and individuals;

☐ the quota system should be abolished—at an interim stage, a light tariff might be introduced to protect United States producers who are burdened with higher labor costs than abroad and also generate added revenue for the United States Treasury;

☐ more rigid price control for oil products must be introduced since we deal with oligopolistic (few large sellers often in collusion) practices⁷.

⁷ The case is sometimes made to decrease the net price and to increase the gasoline tax to limit the use of the car and finance other modes of transportation. This, however, penalizes the poor. The upper income groups could easily absorb the extra burden.

It is unrealistic to expect the present US Administration to follow these policies. The US oil gates will not be flung open (i.e., no quotas or tariffs), nor even ajar by the replacement of quotas with tariffs. The oil lobby in the US is too strong and the present Administration too business oriented to allow such "revolutionary" steps. A good indication is evident from the new quotas imposed on Canadian oil, the favorite fuel partner; when Canada attempted to sell more oil to the United States, the administration clamped down immediately. Moreover, the depressed economic conditions in the United States combined with the political atmosphere of neo-isolation inspires legislation for more restrictive trade practices on all commodities, oil included.

Selected Countries' Energy Production 1967

	Oil (1000 barrels)	Gas (mn cubic meters)	Coal (1000 short tons)
World	13,169,000	822,400	2,116,200
Canada	350,707	48,081	9,387
Mexico	132,916	16,223	1,570
USA	3,215,736	514,558	514,558
Venezuela	1,295,762	7,510	—
Australia	7,604	—	38,872
China	41,186	?	462,966
Czechoslovakia	1,352	—	28,600
France	19,794	5,563	52,496
India	42,431	—	75,202
Indonesia	187,285	2,776	—
Japan	5,510	1,859	52,339
Nigeria	115,342	—	—
Poland	3,327	1,463	136,554
Romania	98,882	20,502	5,635
South Africa	—	—	54,343
UK	668	—	192,790
USSR	2,157,011	157,445	456,448
Middle East+Magreb	4,487,783	—	—
Arab Middle East	3,562,698	—	—
Iran	958,208	1,466	—

	Oil (bn tons)	Gas (bn cubic meters)
World	485,377	28,293
USA	31,377	9,755
Other W. Hemis.	50,000	—
Africa	30,000	8,985
Middle East	314,000	—
USSR	30,000	3,699
Other E. Hemis.	30,000	5,854

Sources: The Middle East & North Africa. 1964-65, 11th edition, Europa Publications, Limited, London. United Nations Statistical Year Book. 1968, 1966, New York, 1966 and 1968. 1967 World Trade Annual, Prepared by the Statistical Office of the UN, Vol. II, Walker & Company, New York. Oil & Gas Journal, December 28, 1965. Compendium of Social Statistics: 1963. UN, New York. The Handbook of Africa edited by Junod, Violaine I. Assisted by Resnick, Idrain N. New York University Press, 1963. The Europa Yearbook — 1968, Vol. I & II, London: Europa Publications Limited. US Statistical Abstract, 1969. American Enterprise Institute; G. Leucowski, ed. "United States Interests in the Middle East", Washington, D.C., 1968.