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## The Weapondollar-Petrodollar Coalition

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# The Global Political Economy of Israel

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## 5

# The Weapondollar–Petrodollar Coalition

I warn you, that when the princes of this world start loving you, it means they're going to grind you up into battle sausage.

– Louis-Ferdinand Céline, *Journey to the End of the Night*

Although economically isolated from its neighbours in terms of trade and investment, Israel's political economy has nevertheless been deeply embedded in the larger saga of the Middle East. The twentieth century, with its endless thirst for energy, made the region crucial for its oil exports. Since the 1960s, however, oil outflows have been complemented by the newer and more precarious movement of arms imports. And as the 'petrodollar' earnings from oil and 'weapondollar' profits from arms grew increasingly intertwined, there emerged in the region a pattern of 'energy conflicts', a series of oil-related wars and revolutions which again and again rocked the Middle East, sending shock waves throughout the world.

### Enigmas

Unfortunately, most of those who tried to understand this link between oil and arms have willingly put themselves into the familiar straitjacket of aggregates. The theories are numerous, but their story is almost always about 'states', 'policy makers' and the 'national interest'. Economists writing in this vein, such as Chan (1980) and Snider (1984), for instance, tend to concentrate on the issue of 'recycling'. The problem, as they see it, concerns the balance of payment. Energy crises jack up the cost of imports for oil-consuming countries, while creating trade surpluses and accumulated reserves for the oil-producing ones. A relatively efficient way to 're-balance' these imbalances, they continue, is for oil importers, mostly developed countries, to sell weapons to oil exporters. Politically, this is easy to do. Consumers in the arms-exporting countries don't care much since the shipments do not require new taxes, whereas rulers in the oil-exporting countries like the trade since it boosts their

self-image and sense of security. The resulting arms race is perhaps unpleasant, but largely unavoidable; unless, of course, the producing countries agree to lower their oil prices.

The same universal language dominates the 'realist' literature of international relations. The underlying political anthropology here portrays a menacing Hobbesian environment, with each nation seeking to endure in a largely anarchic world. Survival and security in this context hinge on economic prosperity, national preponderance and military prowess, which are in turn critically dependent on the differential access to advanced technology, raw materials, and of course energy. According to the 'materialist' strand of this literature, such as Nordlinger (1981) and Waltz (1979), this dependency explains both why central decision makers insist on handling raw material and oil themselves, rather than leaving the matter to private business, and also why they seem almost trigger-happy whenever access to such resources is threatened. True, many conflicts cannot be easily explained by material interests. And yet even on such occasions, argue the realists, the national interest is usually paramount. One reason, they explain, is that the national interest could be 'ideal' as well as 'material'. And indeed, according to Krasner (1978a: Ch. 1), after the Second World War, U.S. state goals have become more 'ideological', emphasising broad aims such as 'competition' and 'communist containment' over strict access to resources (see also Lipschutz 1989). The other reason is that state officials can be wrong, misunderstand the true nature of the situation, or they can simply miscalculate the costs and benefits. But here too, even when policy seems 'nonlogical', the driving force is still – as always – the national interest (Krasner 1978a: Ch. 1).

Naturally, this type of theory can explain almost everything. The process is simple. Take any policy, and begin by looking for materialist explanations. If you find none, don't dismay. Look for ideal ones. And if that too fails, there are always errors, so you can never go wrong. Moreover, the national interest itself is a very strange concept. Since society is full of conflict, adherents of this concept argue it represents not the sum of individual interests, but rather the overall interest of the nation. In the language of Stephen Krasner, it is not the 'utility of the community' which matters, but rather the 'utility for the community', as determined by its central decision makers (1978a: 12, original emphases). However, since the decision makers themselves rarely agree on the matter, it is usually the *researcher* who ends up deciding the national interest for them (or for the reader). And the way this interest is phrased is often so loose, that it can be made consistent with virtually any line of action.

Now, to be fair, other grand narratives are also vulnerable to such ambiguities. Take the 'interest of the capitalist system', a notion often invoked by functionalist Marxism to rationalise developments which, on surface at least, appear contrary to the immediate interests of individual capitalists. A typical example for this is the welfare state. On the face of it, this institution undermines capitalist power. Yet, if we were to push this to the 'final analysis', the

conclusion would be the opposite: by making life more bearable for the workers, the welfare state ends up keeping capitalism as a whole viable. But is this really true? Or rather, can we *prove* it is true? Another example is green-field investment. Many Marxists consider such investment as synonymous with accumulation, and therefore good for capitalism. But if so, is the century long shift from building new capacity to mergers and acquisitions, illustrated in Chapter 2, bad for capitalism? And what about a high price of oil? Or war in the Middle East? Are they good or bad for capitalism 'as a whole'? The truth is that these questions cannot be answered, and for a simple reason. The 'capitalist system', much like the 'state', is an encompassing myth. It provides the broader framework for the discussion, and therefore cannot be simultaneously used for validating or refuting a specific hypothesis within that discussion.

The problem is illustrated in Bromley's otherwise insightful analysis of world oil. His conclusion in that study is that the post-war order, and particularly the emergence of OPEC and higher prices, have in fact helped strengthened the 'general preconditions of capitalist production' under the overall auspices of U.S. hegemony (1991: 59). But what exactly are these 'general preconditions'? And if OPEC and the oil crisis have indeed boosted the system of U.S.-dominated capitalism during the 1970s and 1980s, why haven't the cartel's disintegration and lower oil prices undermined this system during the 1990s? Or have they? Surely, the world has changed in the interim. But then, it always does, so how could we ever know?

The international flows of oil and arms have been examined also from the more disaggregate perspective of the underlying industries, but here, too, there is a considerable lack of unanimity, even on substantive issues. Writing from an implicit 'instrumentalist' view, Blair (1976) and Engler (1977), for example, contend that, intentionally or not, the energy policies of parent governments (particularly the United States, Great Britain and the Netherlands) have had the effect of assisting the international oligopoly of world oil. An almost opposite view is expressed by Turner (1983) and Yergin (1991), who, in line with a more realist perspective, argue that there was a gradual but systematic erosion in the primacy of international oil companies, and that, since the 1970s, these firms were in fact acting as 'agents', or intermediaries between their host and parent governments. Studies on the international arms trade have been equally controversial. According to Sampson (1977), the absence of any international consensus on disarmament created a void, which was then filled by the persistent sales effort of the large weapon makers. And since arms exports become particularly significant in peacetime as domestic defence budgets tend to drop, the end of U.S. involvement in Vietnam during the early 1970s redirected attention to the Middle East, causing military shipments into the region to rise. Other writers, however, such as Krause (1992), reject this interpretation. The impact of private producers on arms sales policies, he claims, should not be overstated, at least not in the case of the United States, where the

volume of arms exports is small relative to domestic military procurement and the contractors' civilian sales.

Whatever their insight, though, most writers tend to treat Middle East conflicts and energy crises as related though *distinct* phenomena. Wars are commonly seen as arising from a combination of local conflicts complicated by superpower interactions. Energy crises, on the other hand, are generally perceived as a consequence of changing global market conditions and institutional arrangements (such as OPEC). Some conflicts – for instance, the 1990–91 war between Iraq and the U.S.-led coalition – have been partly attributed to a struggle over the control of crude reserves, whereas others – specifically the Arab–Israeli wars of 1967 and 1973, and the Iran–Iraq conflict of 1980–88 – were seen as having aggravated ongoing energy crises. Yet, no one has so far offered a general explanation of 'energy conflicts' – that is, a framework which would *integrate* militarisation and conflict on the one hand, with global energy flows and oil prices on the other. Most significantly, existing writings on both oil and war in the region tend to deal rather inadequately, and often not at all, with the process which matters the most, namely the accumulation of capital.

As outlined in Chapter 2, during the 1970s and early 1980s the pendulum of differential accumulation swung from breadth to depth. While economic growth and corporate amalgamation receded, stagflation rose to fill the gap, contributing massively to the differential profit of dominant capital (Figures 2.6 and 2.9). A central facet of this new regime was the cycle of militarisation and energy conflicts in the Middle East, which helped both fuel inflation and aggravate stagnation the world over (Figure 2.10). Stated in this way, our argument may sound reminiscent of supply-shock theory, but the similarity is only superficial. For one, stagflation started to pick up in the early 1970s, *before* the increase in the price of oil. The oil boom certainly fuelled the process, but as a mechanism, not a cause. Second, and more importantly, to argue that oil prices were somehow a shock coming from 'outside' the system is to miss the point altogether. On the contrary, if there was indeed any 'system' here, it was one of differential accumulation. And at that particular historical juncture, its engine was running in depth mode fuelled by an atmosphere of crisis emanating from the Middle East. In other words, the region was very much an integral part of the 'system'.

The purpose in this chapter is to examine the global political economy of this process. In a nutshell, our argument is that, during the 1970s, there was a growing convergence of interests between the world's leading petroleum and armament corporations. Following rising nationalism and heightened industry competition during the 1950s and 1960s, the major international oil companies lost some of their earlier autonomy in the Middle East. At the same time, the region was penetrated by large U.S. and European-based manufacturing companies which, faced with mounting global competition in civilian markets, increased their reliance on military contracts and arms exports. The attendant *politicisation* of oil, together with the parallel *commercialisation* of arms exports,



helped shape an uneasy *Weapon-dollar–Petro-dollar Coalition* between these companies, making their differential profitability increasingly dependent on Middle East energy conflicts. Interestingly, when we look at the history of the region from this particular perspective, the lines separating state from capital, foreign policy from corporate strategy, and territorial conquest from differential profit, no longer seem very solid. Many conventional wisdoms are put on their head. State policies, ostensibly aimed at advancing the national interest, often appear to undermine it; company officers and government officials, moving through a perpetually revolving door, sometimes simultaneously cater to several masters; arms races are fuelled for the sake of ‘stability’; and peace is avoided for being ‘too expensive’. In contrast to these anomalies, the logic of differential accumulation seems remarkably robust. It helps us make sense of corporate strategies, of foreign policies and of the link between them – and all of that within the broader context of ‘energy conflicts’.

### **The Military Bias**

The first half of the nineteenth century in Europe was marked by rising hopes for progress. The Industrial Revolution was helping humanity harness nature. The French Revolution brought new ideas of freedom. Nationalism, liberalism and socialism were breaking new ground. And absolutism was on its way out. With these changes all taking place at once, many were tempted to believe that society was on its way to a better future, one in which military conflict and war were to be rooted out. The theoretical justification for these hopes owed much to the technological determinism of French philosopher Auguste Comte. War he argued, was mainly the consequence of scarcity. Scarcity, however, was alleviated by industrialisation and technical progress, and since these were expected to continue their forward march, conflict and war were bound for extinction. And initially, he seemed vindicated. The ‘bellicosity index’, devised by Pitirim Sorokin and charted in Figure 5.1, shows the intensity of European military conflicts, measured by a weighted average of various indicators, as it evolved since the twelfth century (Sorokin 1962, reported in Wright 1964: 56). This intensity roughly doubled every hundred years until the seventeenth century. During the eighteenth and nineteenth centuries, however, with technical change and industrialisation picking up speed, bellicosity fell sharply, much along the lines suggested by Comte.

And yet, the drop proved a false start. By the second half of the nineteenth century, with the European powers scrambling to complete their colonial acquisitions, conflict again flared up in and outside the Continent. Sorokin’s bellicosity index came back with a vengeance, soaring to record highs in the twentieth century, even without counting the Second World War and beyond. Comte was wrong. Industrialisation in general and capitalism in particular were

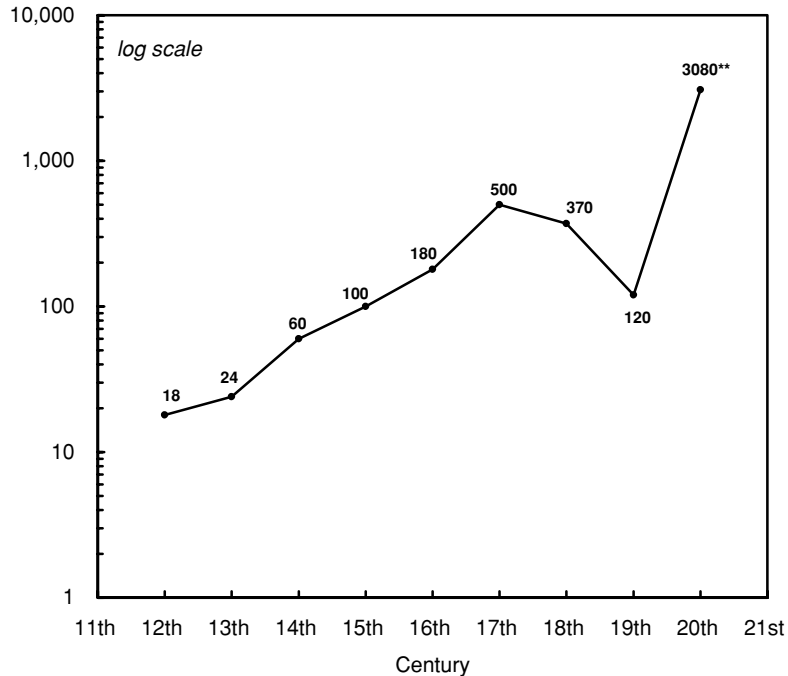


Figure 5.1 European Bellicosity Index\*

\* Number of wars weighted by duration, size of fighting force, number of casualties, number of countries involved, and proportion of combatants to total population.

\*\* Data for the twentieth century cover the period until 1938 only.

SOURCE: Sorokin (1962) reported in Wright (1964: 56).

compatible with war after all. And indeed, by the early twentieth century, a growing number of writers, mostly Marxist, started pondering the link between capitalism and imperialism.

### *Imperialism*

The seminal study on the issue, titled *Imperialism*, was written by a British left liberal, John Hobson (1902). Many of his themes have resurfaced again and again in subsequent works, so the argument is worth presenting, if only briefly. During the latter part of the nineteenth century, capitalism in the leading countries was moving from atomistic competition toward concentration and monopoly. According to Hobson, this transition tended to redistribute income from wages to profits, thus creating a chronic problem of 'oversavings' and

'underconsumption'. Monopoly profit, like any profit, was earmarked for green-field investment. With workers having less to spend, however, the need for such investment was much reduced. In order to avoid stagnation and crisis, the excess savings therefore had to find outlets *outside* the home country, hence the tendency toward imperialist expansion. The scramble for colonies was intense, and Africa, which in 1875 had only 10 per cent of its territory colonised, lost another 80 per cent to European powers within the next quarter of a century. And, yet, this was only ironic, since, according to Hobson, imperialism was in fact a *net loss* to society, and even to its capitalist class. A more sensible route would have been to redistribute income back from monopoly profit to wages, thereby reversing the entire causal chain from monopolisation to stagnation. So why had imperialism prevailed over redistribution? For Hobson, the reason was that state policy was conducted not by society at large, and not even by the capitalist class, but rather by a fairly narrow coalition for whom imperialism was indeed hugely profitable. The main profiteers were the arms producers, trading houses, the military and imperial apparatus, and above all, the financiers, whose foreign investments appreciated greatly from reduced risk premiums brought by imperial rule. The financiers, leading the pro-imperial coalition, were able to harness key politicians to their cause, enlist the possessing classes on threat of redistribution at home, and have the newspapers inflame for them the necessary atmosphere of nationalism and racism.

Marxist writers were greatly influenced by Hobson, although most tended to reject his belief that capitalism could be 'reformed'. According to Rosa Luxemburg, territorial expansion and takeover – in quest for both new markets and cheaper inputs – was in fact *inherent* in capitalism, 'the first mode of economy which is unable to exist by itself, which needs other economic systems as a medium and soil' (1913: 467). Moreover, the expansion was *necessarily violent*. 'Force is the only solution open to capital: the accumulation of capital, seen as a historical process, employs force as a permanent weapon, not only as its genesis, but further on down to the present day' (p. 371).

And indeed, according to Rudolf Hilferding (1910), imperialism projected its violence inward as much as outward, working to transform the economic, political and ideological face of the imperial countries themselves. In contrast to the classical stage, in which the various fractions of capital were politically divided, during the monopoly stage the leading elements among these fractions were fused into 'Finance Capital', an amalgamate of industry and finance controlled by the big banks. This newly welded power, argued Hilferding, drove finance capital into seeking an ever growing territory for its operations, but such expansion was meaningless unless protected by tariffs against outside competition. It was here, then, in the dual quest for territory and protection, that private capital discovered it actually needed a *strong state*:

The demand for an expansionary policy revolutionizes the whole world view of the bourgeoisie, which ceases to be peace-loving and humanitarian. The old free traders believed in free trade not only as the best economic policy but also as the beginning of an era of peace. Finance capital abandoned this belief long ago. It has no faith in the harmony of capitalist interests, and knows well that competition is becoming increasingly a political power struggle. The ideal of peace has lost its luster, and in place of the idea of humanity there emerges the glorification of the greatness of and power of the state.... The ideal now is to secure for one's own nation the domination of the world, an aspiration which is as unbounded as the capitalist lust for profit from which it springs.... Since the subjection of foreign nations takes place by force – that is, in a perfectly natural way – it appears to the ruling nation that this domination is due to some special natural qualities, in short to its racial characteristics. Thus there emerges a racist ideology, cloaked in the garb of natural science, a justification for finance capital's lust for power, which is thus shown to have the specificity and necessity of a natural phenomenon. An oligarchic ideal of domination has replaced the democratic ideal of equality. (Hilferding 1910: 335)

For Karl Kautsky, a Marxist contemporary of Hilferding, this portrayal was far too bleak. The conflict between industrial and financial capital, he argued, had not been decisively won by finance capital as Hilferding claimed. In fact, there was scope for labour opposition, in both the developed and periphery countries, to strengthen the hands of the industrial fraction. Such opposition, if successful, could redirect capitalism toward a more benign alternative, which Kautsky called 'ultra-imperialism' (1970; originally published in 1914). Exploitation would surely continue, but the exploiters, instead of locking horns in imperial destruction and inter-capitalist war, would vie for a common front. 'Hence, from a purely economic standpoint', he wrote, 'it is not impossible that capitalism may still live through another phase, the translation of cartelisation into foreign policy: a phase of *ultra-imperialism*, which of course we must struggle against as energetically as we do against imperialism, but whose perils lie in another direction, not in that of the arms race and the threat to world peace' (p. 46, original emphasis).

With hindsight, we can read here an early anticipation of the transnational corporation, of decolonisation, and of the shifting emphasis of imperialism from inter-capitalist rivalry to core–periphery struggles. But when Kautsky first articulated this view, before the First World War, he was greeted by great hostility from Lenin and Bukharin. Lenin in particular, having thrown his hopes on an imminent revolution, refused to see capitalism as culminating in anything less than Armageddon. Unequal development among the different capitalist powers, he argued, prevented any mutual cooperation among them: 'Finance capital and the trusts do not diminish but increase the differences in the rate of growth of the various parts of the world economy. Once the relation

of forces is changed, what other solution of the contradictions can be found *under capitalism* than that of *force?*' (Lenin 1917: 243–4; cited from Marxist Archives, at [www.marxists.org](http://www.marxists.org)). Furthermore, if workers were sufficiently powerful to bend finance capital as Kautsky suggested, what was to prevent them from moving all the way to socialism?

### *Military Spending*

After the Second World War, things changed drastically. In the periphery, colonialism came to an end, while in the developed core countries real wages soared and unemployment fell sharply. Was this a fundamental change, asked the Marxists? Was capitalism finally able, perhaps with the aid of government intervention, to resolve its earlier contradictions? And if so, was socialism irrelevant? According to contemporary adherents of the 'monopoly capital school', led by Baran and Sweezy, the answer to all three questions was negative. The post-war prosperity was certainly real; but it wasn't because of capitalism, but *despite* capitalism. The shift from small-scale production to big business, they argued, altered the functioning of the economy in two important respects. On the production side, large-scale undertakings, heavy R&D spending, and the incessant introduction of new technologies enabled the big oligopolies to cut cost as never before. At the same time, the strong oligopoly bias against price competition not only prevented these cost savings from being translated into lower prices, but actually introduced persistent inflation. And so, contrary to the view of classical Marxism, monopoly capitalism, by lowering cost and raising prices, created a *tendency for the surplus to rise*. For Marx, the chief menace to capitalism came from a rising organic composition of capital, leading to a tendency for the rate of profit to fall; here, on the other hand, the key issue was the rising rate of exploitation, or 'surplus' in the new terminology. But if so, what was the problem? Indeed, shouldn't a rising surplus bring *higher* profit, thus boosting capitalism even further? Not necessarily, argued Baran and Sweezy:

According to our model, the growth of monopoly generates a strong tendency for surplus to rise without at the same time providing adequate mechanisms of surplus absorption. But surplus that is not absorbed is also surplus that is not produced: it is merely potential surplus, and it leaves its statistical trace not in the figures of profits and investment but rather in the figures of unemployment and unutilised productive capacity. (Baran and Sweezy 1966: 218)

In short, Hobson's curse was still with us. Monopoly bred redistribution, under-consumption, and therefore *falling* surplus – that is, unless absorbed by *external* offsets to savings. Contrary to the early writings on the subject, however, the

most potent offsets according to Baran and Sweezy were created not by colonial expansion, but through the ‘institutionalised waste’ of state spending, a process first identified by Thorstein Veblen.

For external offsets to savings to be effective, the two writers argued, they needed, first, to absorb more surplus than they generated, and, second, to be available in large doses. Investment was no good here, since it usually generated more surplus than it absorbed, while exports were limited by foreign demand. Government expenditures, on the other hand, and particularly *military spending*, faced neither limitation. They were commonly ‘wasteful’ in the sense of absorbing but not generating surplus, and they could be extended almost at will. Technically speaking, *civilian* government spending could work in much the same way. Politically, though, it was unwelcome. The main reason was that such spending, as it pushed the economy toward full employment, undermined the social hegemony of business. According to Michal Kalecki,

‘discipline in the factories’ and ‘political stability’ are more appreciated by the business leaders than profits. Their class instinct tells them that lasting full employment is unsound from their point of view and that unemployment is an integral part of the normal capitalist system.... The workers would ‘get out of hand,’ and the ‘captains of industry’ would be anxious to ‘teach them a lesson’.... In this situation a powerful block is likely to be formed between big business and the *rentier* interests, and they would probably find more than one economist to declare that the situation was manifestly unsound. The pressure of all these forces, and in particular of big business would most probably induce the Government to return to the orthodox policy of cutting down the budget deficit. A slump would follow in which Government spending policy would come again into its own. (Kalecki 1943b: 141, 144)

Military spending did not pose a similar threat. It did not compete directly with private interests, and while it might have lessened the disciplinary impact of unemployment, the ‘shortfall’ was more than compensated for by the direct use of force and violence in the name national security. And so, capitalism, according to Kalecki, tended to oscillate between two ideal types. One extreme was a democratic model in which the government, torn between supporting and legitimising accumulation, ended up creating a ‘political business cycle’ by its stop-go policies. The other extreme was the fascist model, in which full employment was sustained by military spending in preparation for war, and where the concentration camp substituted for unemployment as a way of pacifying workers.

Since the Second World War, argued Baran and Sweezy, the United States used armaments to write its own ticket to prosperity. According to Gold (1977), the arrangement was supported by a powerful ‘Keynesian Coalition’ between big business and the large unions, which, since the 1950s, consistently preferred ‘military Keynesianism’ and aggressive foreign policy to the more benign use

of civilian spending. And the policy was not without consequences. Ten years before the publication of Baran and Sweezy's *Monopoly Capital*, Shigeto Tsuru, a Japanese political economist, wrote an article entitled 'Has Capitalism Changed' (Tsuru 1956). Having examined the sources and offsets of U.S. savings, his conclusion was that in order to maintain its prevailing growth rate, the country needed military spending equivalent to roughly 10 per cent of its GDP. However, if this proportion was to be maintained, he continued, the *absolute* level of military expenditures ten years down the road would become far too high to justify for a country in peace. And indeed, a decade later, in 1966, the United States was deeply involved in the Vietnam War, with military spending kept at close to 9 per cent of GDP.

### The U.S. Arma-Core

#### *The 'Angry Elements'*

During the 1970s, other writers, such as O'Connor (1973) and Griffin, Devine and Wallace (1982), have taken the argument a step further, suggesting that government involvement, and particularly military spending, were affected not by overall macroeconomic needs or the interest of capitalists in general, but rather by the specific requirements of dominant economic groups. More significantly, however, the Korean and Vietnam conflicts of the 1950s and 1960s indicated that military spending was not only a *consequence* of economic structure, but also an important force *shaping* that structure. One of the first writers to recognise this double-sided relationship was Michal Kalecki. Much of his early writings from the 1930s and 1940s were concerned with the effect on macroeconomic performance of the 'degree of monopoly' in the underlying industries. Toward the end of his life, during the 1960s, he closed the circle, pointing to the way in which macroeconomic policy, primarily military spending, could affect the economic and social structure. In his articles 'The Fascism of Our Times' (1964) and 'Vietnam and U.S. Big Business' (1967), Kalecki claimed that continued U.S. involvement in Vietnam would increase the dichotomy between the 'old', largely civilian industries located mainly on the East Coast, and the 'new' business groups, primarily the arms producers of the West Coast. The rise in military budgets, he predicted, would effect a redistribution of income from the old to the new groups. The 'angry elements' within the U.S. ruling class would be significantly strengthened, pushing for a more aggressive foreign policy, and propagating further what Melman (1974) would later call the 'permanent war economy'.

Was Kalecki right? Had the epicentre of the U.S. 'big economy', or dominant capital in our language, indeed shifted from 'civilian' to 'military' oriented corporations? Unfortunately, the question is not easy to answer. Corporate power, we argue in this book, is a matter of differential profit. And, yet, the link

between profit and production is elusive at best. If military contractors were producing only armaments and civilian firms only non-military items, the problem would have been less serious. But that is not the case in practice. Since the 1960s, most large U.S. firms have become conglomerates to a greater or lesser extent, with military contractors diversifying into civilian business and vice versa. The difficulty for our purpose is that conglomerate finance is inherently 'contaminated' by intra-firm transfer pricing, so although we may know how much a firm gets from the Pentagon in *sales revenues*, we cannot know for sure the impact this has on its *profit*.

The problem, though, is not insurmountable. In what follows, we identify the leading 'Arma-Core' of the U.S. economy, defined as the inner corporate cluster which appropriated the lion's share of defence-related contracts, and which was highly dependent on such contracts. Having identified the members of this 'Arma-Core', we then proceed to examine their combined profit relative to U.S. dominant capital as a whole. Now, although both groups derived their earnings from military as well as civilian business, and although the impact on their profit of each line of business cannot be determined with accuracy, it is safe to assume that the Arma-Core's profitability was much more sensitive to military contracts than that of dominant capital as a whole. A rise in the profit share of the Arma-Core would then indicate that Kalecki was right, and that the 'military bias' of the United States indeed enhanced the power of 'military oriented' firms. A decline in the ratio would of course suggest the opposite.

Who then was in the Arma-Core? A first approximation could be derived from data published by the U.S. Department of Defense (DoD), in its annual listing for the *100 Companies Receiving the Largest Dollar Volume of Prime Contract Awards*.<sup>1</sup> From this publication we can learn that military procurement was fairly concentrated, such that, over the period between 1966 and 1991, the largest 100 contractors accounted for between 62 and 72 per cent of the DoD's total prime contract awards. However, it is probably inappropriate to consider all of the leading 100 firms as members of the Arma-Core. Our tentative criterion for inclusion in this core is for the firm to be large enough to exercise political leverage, as well as significantly dependent on defence contracts, and not all of the leading 100 companies fit both characteristics. Some corporations – such as AT&T, IBM, IIT, Eastman Kodak, Ford, Chrysler, Exxon, Mobil and Texaco – were very large but depended only marginally on military contracts. Others, like Singer, Teledyne, E-Systems, Loral, FMC, Harsco and Gencorp, relied more heavily on defence sales, but were probably not big enough to exercise political leverage. Thus, concentrating only on *large, defence-dependent*

1 We ignore here parallel listings of subcontracting, foreign military sales, and contracts awarded by NASA and the Department of Energy. These contracts are significant, but their recipients tended to be the same as the DoD's prime contractors.



contractors, we end up with a more limited group of about 20 to 25 firms, which for our purpose here comprise the U.S. Arma-Core.

The precise choice of boundary between the Arma-Core and the remaining contractors is of course arbitrary to some extent, a problem which is further exacerbated by periodic changes in the ranking of firms. Given the attendant uncertainty and ambiguity, we focus on a more limited sample of only 16 corporations. These include, in alphabetical order: Boeing, General Dynamics, General Electric, Grumman, Honeywell, Litton Industries, Lockheed, McDonnell Douglas, Martin Marietta, Northrop, Raytheon, Rockwell International, Texas Instruments, Textron, United Technologies, and Westinghouse. This group is representative of the Arma-Core in that it consists of only large firms and, with only minor exceptions, it included the top ten DoD contractors in every year between 1966 and 1991.<sup>2</sup> During the 1966–91 period, these 16 firms received more domestic military contracts than any other comparable group of American corporations. On average, they accounted for 36 per cent of the DoD's total prime contract awards, with a floor of 30 per cent (in 1966) and a ceiling of 41 per cent (in 1985). As a group, the Arma-Core proved much more dependent on sales to the Pentagon than dominant capital as whole. For the latter, denoted here by the Fortune 500, military contracts ranged between 5 and 10 per cent of total sales. The comparable figure for the Arma-Core was 20 to 40 per cent (Nitzan and Bichler 1995: 460–1).

Turning to the crucial question of differential profitability, Figure 5.2 presents the net profit share of the Arma-Core within dominant capital. The data show that, following the Vietnam War, this share had doubled to 10 per cent by the mid-1980s, up from 5 per cent in the mid-1960s. In other words, if our interpretation here is correct, the 'permanent war economy' which existed in the United States pretty much until the end of Reagan's second presidency, seems to have indeed created an ongoing 'military bias' within the U.S. corporate sector, strengthening the relative power of military contractors. Kalecki was certainly prescient.

#### *Corporate Restructuring and 'Military Keynesianism'*

To a certain extent, this interaction between military expenditures and business realignment was also part of a broader, worldwide transformation affecting the relationships between nation states and transnational corporations. Following the Second World War, the global economic significance of the United States began to wane. The decline is evident in various indicators. For instance, whereas during the 1960s U.S. GDP measured one and half times

<sup>2</sup> Excluded from the sample is Hughes Aircraft which, as a privately held firm until 1986, did not publish financial reports. Also omitted are General Motors, which entered the Arma-Core only in 1986 after acquiring Hughes Aircraft; LTV, which filed for bankruptcy protection in 1986; and Tenneco, whose annual contract awards fluctuated widely.

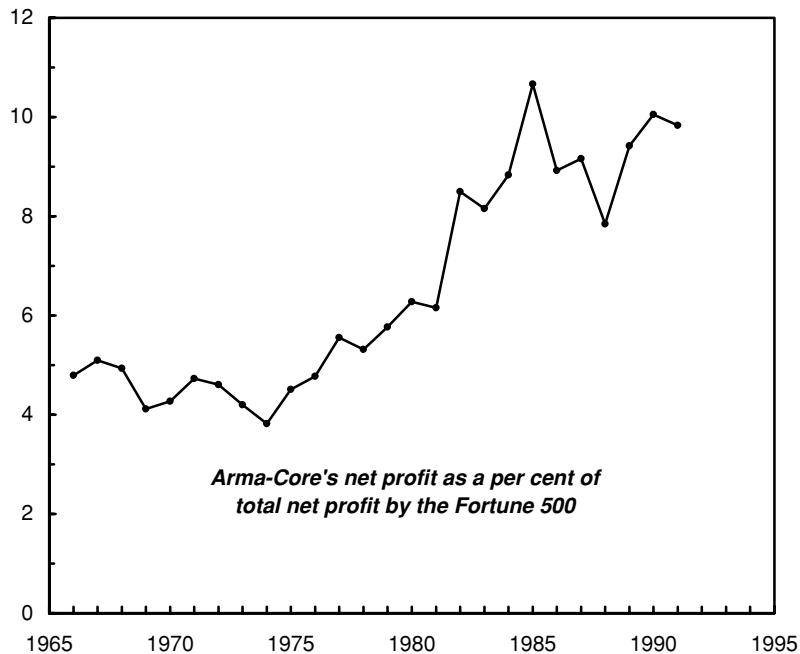


Figure 5.2 The Rise of the U.S. Arma-Core

SOURCE: Fortune; Standard & Poor's Compustat.

the combined total for the EEC's 12 countries plus Japan, by the early 1990s the ratio was only half as large. Also, as the country grew more economically open, its trade balance moved from surplus to deficit, requiring increasing doses of capital inflows to cover the shortfall. Under these circumstances, with the local market becoming relatively less important as well as increasingly contested by foreign competitors, U.S.-based firms naturally looked for further opportunities abroad. And indeed, by the early 1990s, roughly 25 per cent of their profits came from outside the country, up from less than 10 per cent in the 1960s. The foreign challenge, however, remained gruelling, and American-based firms continued their slide down the global rankings. In contrast to 1960, when the United States was home to 114 of the world's 174 largest firms, by the 1990 the number dropped to a mere 56 (figures in this paragraph are calculated from U.S. Department of Commerce through McGraw-Hill Online, and from Franko 1991).

These major transformations affected the choice of both corporate strategy and economic policy. Faced with mounting competitive pressures in civilian markets, many large U.S.-based firms found themselves increasingly drawn into the shelter of high-profit government contracts, particularly in areas such as

defence, nuclear energy, space, and medical technology.<sup>3</sup> On the policy side, this dependency got the U.S. administration entangled in a commitment to 'military Keynesianism', which, paradoxically, grew deeper as the big corporations became more global in scope. The reason was that, with a rising share of corporate profits coming from abroad, domestic government policies affected a *diminishing* portion of corporate earnings. Or to put it somewhat differently, all other things being equal, a given increase in the companies' overall profit required a larger increment of domestic military contracts. Under these circumstances, any attempt to eliminate the 'military bias' spelled a major blow to the credibility of macroeconomic policy, and of course serious injury to some of the country's most powerful firms.

Relying on domestic military spending, however, was always a tricky business. The main problem is the mismatch existing between the requirements of *arms making* and the reality of *arms selling*. From an industrial standpoint, the technology-intensive nature of weapon making requires continuous research and development and open production lines. Furthermore, military production is highly specialised, so it cannot be easily converted into civilian use when demand for weapons slackens. These industrial considerations call for a stable growth in demand for arms – and yet, that is not what usually happens in the armament business. Perceived as a drain on the country's resources, military expenditures need to be legitimised by external threats, and these tend to fluctuate with the ups and downs of international politics and the frequency of armed conflicts. The consequence is to make domestic weapon procurement *inherently* unstable, which is of course a serious headache for the large armament producers. Clearly, if these firms are to keep their production lines open, they can never rely solely on domestic procurement, and must constantly look for 'counter-cyclical' export markets.

3 In the electronics industry, for instance, General Electric embarked on a major restructuring programme which, over the 1981–87 period, saw the company acquire some 338 business and product lines, while divesting 232 others (*Business Week*, 16 March 1987). The process, whose main goal was to move away from markets dominated by the Japanese, included the 1985 acquisition of RCA, particularly for its defence business, and the 1986 swap of GE's consumer electronic lines for Thomson's medical equipment unit (*Time*, 23 December 1985; 3 August 1987). In 1992, General Electric sold its defence electronics unit to Martin Marietta, but in turn became a major shareholder of the latter company (*Business Week*, 7 December 1992). In the aircraft industry, Lockheed left commercial aviation altogether, after its entanglement with the L-1011 airliner brought it to near bankruptcy. Similarly, McDonnell Douglas, which was initially created in 1967 when McDonnell absorbed Douglas as a means of diversifying into non-defence activity, never made any money from civilian aircraft, and, in 1991, entered into a tentative agreement to sell 40 per cent of its civilian unit to Taiwan Aerospace (*Business Week*, 14 February 1983; 23 May 1988; 2 December 1991). The deal failed to go through, and McDonnell Douglas was eventually absorbed by Boeing, which sought to bolster its position against Europe's Airbus consortium. Similar retreats plagued the automobile industry, where pressures from Japanese competition pushed U.S.-based firms back into defence-related activity. The most publicised move here was General Motors' acquisition of EDS and Hughes Aircraft, which during the 1980s turned the 'car company' into one of the country's top ten defence contractors.

### Arms Exports

The perils of restricted demand are hardly new, of course. For example, during the Seven-Year War Frederick the Great found himself forced to import 32,000 rifles from abroad, and that because only a few years earlier he decided to cut down production capacity for lack of domestic demand (Frederick the Great 1979: 18). The simplest solution for this dilemma would have been to supplement the home market with foreign sales, but, initially, that was not at all obvious and for a very simple reason: weapons were usually produced by the state whose officials were hardly keen on selling them to potential enemies. Industrial advancement, however, increasingly shifted armament production into private hands, and it was this privatisation which eventually enabled the business to become truly international. The imperative of combining private ownership and foreign sales was succinctly elucidated in 1913, when, on the eve of the First World War, Krupp, the German weapon maker, got entangled in a corruption scandal. Answering his critics in the Reichstag, the Minister of War, Josias von Heeringen, defended this new system, arguing that in order to maintain sufficient capacity for wartime, military producers had to export in peacetime. This, he insisted, could be achieved only by private firms which were free from the patriotic scruples of state companies (Sampson 1977: 43). And indeed, by the end of the nineteenth century, the large armament firms – such as Krupp, Nobel, Armstrong, Vickers, Du-Pont, Electric Boat and Carnegie – were all privately owned, highly dependent on foreign markets, and most importantly, unregulated (*ibid.*, Chs 2–4).

This structure of the military industry first came under scrutiny during the 1920s and 1930s. After the First World War, the League of Nations accused the arms companies of fermenting international conflict, causing a flurry of official investigations into the arms business. Following the Nye Committee hearings in the United States, the isolationist congress passed the 1935 Neutrality Bill, with special provision for a National Munitions Control Board to supervise American arms exports. A few years later, the 1941 Lend Lease Act brought the U.S. government further into the centre-stage of the arms trade, and by the end of the Second World War it was commonly accepted that the export of weapons was no longer a private affair, but rather a matter of foreign policy.

After the war, the 'Truman Doctrine' conceived military exports, particularly to Europe, as part of the larger effort to contain communism, a goal which would be later extended to legitimise arms shipments to South East Asia. Yet this new emphasis on broader policy goals did little to resolve the problem of unstable demand. The continued military Keynesianism of the 1950s and 1960s created the basis for an Arma-Core of large military-dependent firms, and by the late 1960s, toward the end of the United States' direct involvement in Vietnam, these corporations appeared just as vulnerable to budget cuts as the Carnegies and Du-Ponts half a century earlier. Despite several decades of change, the weapon business remained predominantly private, and with the war effort

now receding, its owners were once again seeking to counteract excess capacity with foreign military sales.

#### *Arms Exports and Corporate Profit*

Interestingly, until the late 1980s most observers tended to doubt this 'economic' rationale for U.S. military exports. Such exports, they argued, were simply too small to make a difference (for instance, Krause 1992: 106). And on the surface they seemed to have a point. Domestic procurements, measured in constant 1995 prices, ranged from \$61 billion in 1974, after the end of the Vietnam conflict, to \$136 billion in 1987, at the peak of the Reagan build-up. The comparable figures for foreign military sales were much smaller: between \$5 billion in 1963, just before the Vietnam conflict started to pick up, and \$23 billion in 1987, at the height of the Iran–Iraq War (data sources in Figure 5.3). And yet the comparison is deceiving. The arms makers, like any other capitalist, are concerned not with sales but with *profits*, and these tend to be far higher in export sales. The basic reason is simple enough. The production of weapons, particularly major platforms such as tanks, aircraft and ships, involves very high research and development outlays. This fixed component is typically recovered through domestic sales, so by the time the company starts exporting, its average unit cost is far lower, and the profit per unit correspondingly higher. And indeed, an internal DoD study cited in Brzoska and Ohlson (1987: 120) estimated foreign military sales to be 2.5 times more profitable than those made to the U.S. government, while similar ratios – ranging from 2 to 2.3 – emerged from other industry sources (U.S. Congress 1991: 53).

Using these profitability indicators in conjunction with sales data, Figure 5.3 reassesses the relative importance of arms exports. The top series in the chart traces the value of domestic military shipments, measured in constant prices. The bottom series imputes the relative contribution of foreign military sales to overall military-related profit (domestic as well as foreign). The later computation is based on the conservative assumption that the export markup was twice as high as the local one, and that the ratio between the two markups remained stable over time.<sup>4</sup> Now, since actual markups do change over time, the ratio plotted in the chart is necessarily imprecise. Nevertheless, its overall magnitude and broad trajectory are telling. All in all, the chart suggests, first, that arms exports were probably far more important for U.S. military contractors than is commonly assumed, and, second, that this dependency has grown over

4 Symbolically, if (*MS*) is overall military sales, (*MS<sub>d</sub>*) is domestic sales, (*MSe*) is export sales, and (*v*) is the ratio between the export and domestic markups, then the relative contribution of military exports to military-related profit (*RC*) is given by the following expression:

$$RC = (v \cdot MSe) / (v \cdot MSe + MSd)$$

time. Export first became significant during the military build-down of the late 1960s and early 1970s. The United States was scaling back its direct involvement in Vietnam, and with military exports to the region continuing to rise, the ratio of export profit to total profit soared. Based on our imputation, in 1973, at the cyclical peak of the process, foreign sales accounted for up to one-third of all military-related profit. Subsequently, with President Carter reversing the spending downtrend, and with the Reagan Administration embarking on the country's largest military build-up in peacetime, arms exports became relatively less important. And yet, even in the late 1980s, when domestic spending reached record highs, exports still accounted for a sizeable one-quarter of all military-related profit. Ominously, during the 1990s, with military spending dropping and 'peace dividends' mushrooming the world over, foreign military

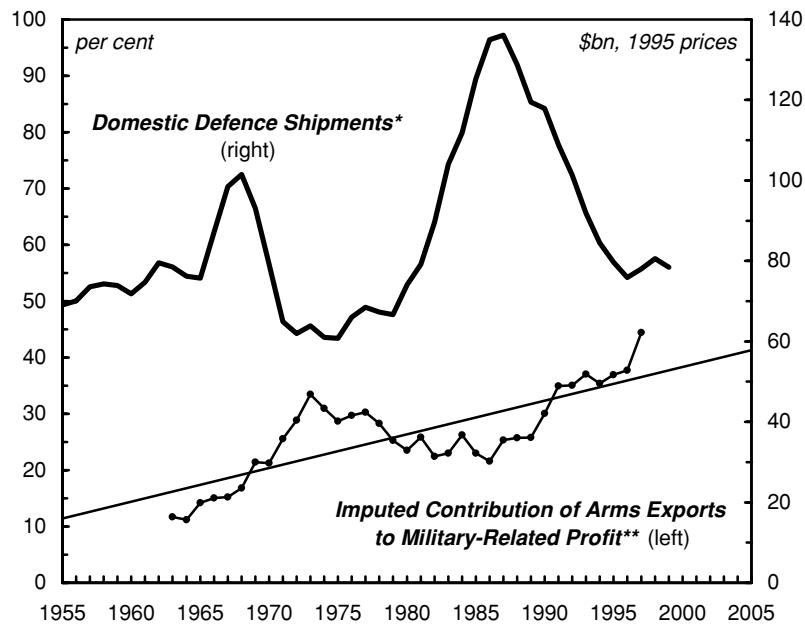


Figure 5.3 U.S. Military Business: Domestic and Foreign

\* Manufacturing shipments of defence products. Data prior to 1968 are estimated based on pro-rated splicing with overall U.S. military expenditure.

\*\* Based on comparison of arms export deliveries and domestic shipments of defence products, assuming the export markup is twice as high as the domestic markup. Arms exports prior to 1984 exclude military services, resulting in an estimated downward bias of 5 per cent.

SOURCE: U.S. Arms Controls and Disarmament Agency (Annual); U.S. Department of Commerce through McGraw-Hill (Online).

sales have become the profit life-line of U.S.-based contractors, accounting for an estimated 45 per cent of their total military-related earnings.

This focus on profit rather than sales helps explain why a single export deal can sometimes make or break even a large contractor. Grumman, for example, was saved from near-bankruptcy in 1974 by the sale of F-14 Tomcat fighter planes to Iran (Sampson 1977: 249–56). Similarly, during the early 1990s, the sale of 72 F-15 Eagle fighters to Saudi Arabia gave financially troubled McDonnell Douglas a temporary lease on life (*Business Week*, 16 March 1992; *Fortune*, 22 February 1993). Northrop, on the other hand, was seriously hampered by its F-20 debacle, a dedicated ‘fighter for export’ which the company spent \$1.4 billion to develop but never managed to sell (Ferrari et al. 1987: 27).

Contrary to received wisdom, then, the evidence, however tentative, suggests that the Arma-Core was in fact very much affected by U.S. military exports. And given the growing political leverage of this core, it should be hardly surprising that foreign policy has become increasingly bound up with private profit.

#### *Commercialising Arms Exports: From Aid to Sales*

The growing interaction between trade and the flag in this area was facilitated by two related developments. The first of these developments was the *commercialisation* of arms exports. During the 1950s, when arms exports were still seen as a matter of foreign policy, up to 95 per cent of U.S. foreign military deliveries were financed by government aid. Over time, though, with the line separating state from capital becoming less and less clear, the proportions changed, and by the 1990s only 30 per cent were given as aid. The rest, up to 70 per cent, were now paid for directly by the buyer (figures computed from U.S. Defense Security Assistance Agency 1989; 1992; and U.S. Department of Commerce. Bureau of the Census Annual).

The second development, which greatly facilitated this commercialisation, was the emergence of the Middle East as the world’s prime destination for exported arms. The process, illustrated in Table 5.1, shows the level of arms imports from all sources (expressed in 1987 prices), as well as their regional distribution during four distinct periods. During the first period, between 1963 and 1964, global arms imports amounted to \$11.7 billion annually, with about half going to Europe (earlier data are unavailable). In the aftermath of the Second World War, the Continent was still perceived as potentially unstable, and so until the mid-1960s, the United States sent most of its military assistance to its NATO allies primarily in the form of surplus stockpile grants. Since 1965, however, the emphasis began to change. The ‘hot spot’ of the West–East conflict moved to South East Asia, and with it came a rapid escalation in the global armament trade. Over the 1965–73 period, world arms import rose by 65 per cent, to an annual average of \$19.4 billion – with over one-third now going to East Asia. In the United States, the shift of focus from Europe to the outlying

areas of the Third World brought a redefinition of arms-export policies. Weapon deliveries to Vietnam and other South East Asian countries were still financed by aid, but the European countries were now increasingly requested to pay for their U.S.-made hardware.

Table 5.1 Arms Imports by Region (annual averages)

| Period  | World Total<br>(\$m/year,<br>1987 prices) <sup>(a)</sup> | Of Which (per cent of world total) |           |             |        |        |
|---------|--|------------------------------------|-----------|-------------|--------|--------|
|         |  | NATO &<br>Warsaw Pact              | East Asia | Middle East | Africa | Others |
| 1963–64 | 11,711   | 49.9                               | 17.3      | 9.9         | 4.3    | 18.7   |
| 1965–73 | 19,356   | 28.9                               | 35.2      | 16.8        | 3.8    | 15.3   |
| 1974–84 | 45,598   | 18.7                               | 11.3      | 36.3        | 16.3   | 17.4   |
| 1985–89 | 51,096   | 18.0                               | 12.4      | 32.9        | 9.5    | 27.1   |

(a) Constant price data are computed by dividing the original nominal figures by the U.S. implicit GDP deflator.

SOURCE: Original current-price data are from U.S. Arms Control and Disarmament Agency (Annual). (Because of repeated updates, data are from the last annual publication in which they appear.) Implicit GDP Deflator is from *Economic Report of the President* (Annual).

This change, which signalled a return to the pre-war commercial pattern of weapon sales, was to some extent inescapable. The post-war policy of containing communism through military aid was feasible as long as U.S. arms shipments were small and U.S. government finances solid. But as the arms race started picking up and the federal deficit ballooned, successive American administrations began to preach the merits of commercial sales. During the Eisenhower, Kennedy and Johnson governments, the trend was limited mainly to transactions with NATO, but the late-1960s entanglement in Vietnam hastened the final policy reversal. By 1969, the new 'Nixon Doctrine' stipulated that all transfers of weapons – including those going to the Third World – should, whenever possible, depend not on direct U.S. military involvement, but on the buyer's ability to pay.

#### *Global Redistribution and the Rise of the Middle East*

The single most important factor enabling this shift from aid to sales was the global income redistribution triggered by the 1973 oil crisis. The explosive growth of OPEC's revenues made the cartel's members ideal clients for weaponry, and in 1974, after the U.S. exit from Vietnam, the Middle East became the world's largest importer of armaments. As Table 5.1 shows, over the 1974–84 period, the annual arms trade rose to nearly \$46 billion, up 136 per cent from the previous period, with roughly 53 per cent of the total going to the Middle East and Africa (mainly Libya and Egypt). The pivotal role here of global redistribution can hardly be overstated. Indeed, as oil revenues



dropped during the latter half of the 1980s, the rapid rise in arms transfers was arrested. During 1985–89, world military imports rose only marginally, to an average annual level of \$51 billion, with much of the stagnation taking place in the Middle East and Africa, whose combined share dropped to 42 per cent. (During the 1990s, the global redistribution of income has taken a new turn with the rapid growth of ‘emerging markets’ in Latin America, South Asia and South East Asia. Interestingly, this shift has been accompanied by a ‘mini-boom’ of military imports flowing into their regions, with the initial takeoff already evident in the increasing share of ‘Others’ recorded in Table 5.1.)

To sum up, the post-war era was marked by several important changes affecting the nature of arms production and trade. In the United States, there emerged an Arma-Core of large defence contractors, whose rising power, particularly since the Vietnam conflict, enabled it to appropriate a growing share of the profit of dominant capital. The relative growth of these companies was influenced by the continuous ‘military bias’ of the U.S. economy, which was itself partly the consequence of mounting global competition in civilian markets. The consolidation of this powerful group of firms strengthened their political leverage – mostly in matters affecting the domestic budget, but increasingly also in the choice of foreign policy. This latter significance stemmed primarily from the intrinsic dependence of arms production on flexible foreign demand. After the Second World War, the U.S. Administration made military exports a tool of foreign policy; but, over time, the very menu of policy options became intertwined with the development of the Arma-Core. Initially, the need for foreign markets was both limited and easily financed by U.S. military aid. However, the continuous ascent of defence-dependent corporations eventually raised arms exports up to a level which could no longer be backed solely by U.S.-government grants. The dilemma was solved by a gradual return to the pre-war pattern of commercial trade in weaponry, and what made this transition feasible was the global redistribution of income triggered by the Middle East oil crisis.

With this latter development, the U.S. Arma-Core found itself entering the centre-stage of Middle Eastern ‘energy conflicts’. The consequences of this entry were far reaching. The large defence contractors which earlier depended mainly on the level of domestic military spending and foreign military aid, now found their financial fate increasingly correlated with the boom and bust of the oil business. And they were not alone. With them on the same stage were also the newly empowered OPEC governments, the governments of the imperilled Western countries, and the major petroleum companies whose dominant position in the oil world was now called into question. The emergence of the Middle East as the ‘hot spot’ of world conflict and the leading arms-importing region has altered the delicate relationships between these transnational corporations and both their parent and host governments. Furthermore, the seemingly circular sequence of regional wars and oil crises brought the petroleum companies into a new, and in some way unexpected

alliance with the arms makers. Before we can turn to examine this alliance, however, we must look more closely at the changing circumstances affecting the petroleum industry.

### **Middle East Oil and the Petro-Core**

#### *The 'Demise Thesis'*

The dominant view among students of the subject, is that the oil crisis of the 1970s signalled the final stage in a fundamental transformation, a transformation which started in the 1950s, and which eventually altered the structure of the oil industry. The first aspect of this transformation was the relative decline of the major oil companies vis-à-vis a growing number of lesser firms. After the Second World War, the 'Seven Sisters' – notably Exxon (then Standard Oil of New Jersey), Royal Dutch/Shell, British Petroleum (previously Anglo-Iranian), Texaco, Mobil, Chevron (then Socal) and Gulf – still dominated the relatively concentrated international oil arena. Gradually, however, the entrance of smaller independent companies, the growth of existing firms other than the seven largest, and the re-entry of the Soviet Union into Western energy markets, made the sector less concentrated, eroding the leading position of the oil majors. In just two decades, between 1953 and 1972, the share of the 'Seven Sisters' in the oil industry outside the United States fell from 64 per cent to 24 per cent of all concession areas; from 92 to 67 per cent of proven reserves; from 87 to 71 per cent of production; from 73 to 49 per cent of refining capacity; from 29 to 19 per cent of tanker capacity; and from 72 to 54 per cent in product marketing (Jacoby 1974: Table 9.12, p. 211).

A second and perhaps more important facet of this transformation was that the locus of control, which previously rested with the owners and officers of the large petroleum companies, had now apparently shifted into the hands of government officials, monarchs and dictators. At the 'upstream' part of the industry, the oil companies succumbed to the relentless nationalistic pressure of their host countries, and after a quarter-century of eroding autonomy eventually surrendered most of their crude oil concessions. Once begun, the transition was swift and decisive. The transnational companies, which as late as 1970 still owned about 90 per cent of all crude petroleum produced in the non-communist world, found their equity share drop sharply to only 37 per cent by 1982, most of it now concentrated in North America (figures cited in Penrose 1987: 15). A similar change occurred at the 'downstream' segment of the industry, particularly in the Western industrial countries. With the oil crisis, the cost of energy and its very availability became major policy issues with wide-ranging domestic and foreign implications; so that here, too, the firms found they had to comply with political dictates – in this case, those coming

from their own parent governments. Energy in general and petroleum in particular became *political* questions, and just 'as war was too important to be left for the generals', wrote Yergin (1991: 613), 'so oil was clearly too important to be left to the oil men'.

And so emerged the 'demise thesis'. According to Turner (1983: 118–24), after the Second World War the major oil companies have come to assume various roles, acting as 'governmental agents', as 'transmission belts' between host and parent governments, as occasional 'instigators', or simply as a 'complicating factor' – but, in his opinion, all of these roles have merely added some colour to the sphere of international political economy. In the final analysis, he argues, it was the diplomats who were making the crucial decisions. The multinational petroleum companies – particularly after the oil crisis – have been pushed aside, reduced to a status of 'interested bystanders' in the high politics of world oil (pp. 147–8).

#### *Whither the Oil Companies?*

At the time, the 'demise thesis' seemed persuasive, even fashionable. It was certainly the next logical step in a long theoretical sequence, which began with the 'bureaucratic revolution' of the 1930s, continued through the 'managerial revolution' of the 1940s, and from there led to the 'technostructure' of the 1950s and 1960s, and to 'statism' in the 1970s. There was only one little problem. The evidence used to support this thesis was strangely silent on the issue which mattered most, namely the accumulation of capital. In the final analysis, capitalism emerged and expanded not because it offered a new ethos, but because that ethos helped the rising bourgeoisie alter the distribution of income from landed rent to business profit. For that reason, those who argue in favour of bureaucratic-statist determinism, or believe in the demise of big business, must go to the essence of capitalism and demonstrate that these developments have fundamentally altered the distribution of income and the mechanism of accumulation.

In this particular case, if we are to conclude that the oil majors have indeed declined, we need to be first shown not only that they lost market shares and became dependent on government policies, but also that these structural and institutional changes affected their business performance, and, specifically, their *profits*. Assuming that the large petroleum companies were squeezed between rising competition and more demanding governments, the combined pressure must have caused their net earnings to wither – either absolutely, or at least relative to some broader aggregates. And yet, this has never been demonstrated in the literature. Most studies pertaining to the 'multinational debate' in the energy sector either gloss over the issue, or simply ignore it altogether; and even where profits are referred to, the data are often incomplete and rarely

analysed in a wider historical context.<sup>5</sup> Unfortunately, this neglect helps distort the overall picture, for while the institutional and structural indicators may imply that the major oil companies have indeed declined, the profit data seem to suggest the exact opposite!

Table 5.2 provides some long-term summary indices for the profit performance of the world's six largest petroleum companies in the early 1990s. This group – which we label here the 'Petro-Core' – consists of the original 'Seven Sisters', with the exception of Gulf which was acquired by Chevron in 1984. The comparison includes various differential accumulation indicators, relating the profit performance of the Petro-Core to corresponding figures for larger corporate groupings, including a wider international composite of petroleum firms, the Fortune 500, and the U.S. corporate sector as a whole.

The first column gives the average net rate of return for the Petro-Core (ratio of net profit to owners' equity). The overall impression from these data is that the oil crises of the 1970s and early 1980s in fact helped *boost* the profitability of the large oil companies, a notion to which we return later in the chapter. For our purpose here, though, the more interesting results are those obtained from the differential indices. In the second column, we present the rate-of-return ratio between the Petro-Core and the 'Petroleum 40–42' group of companies. This ratio is calculated by dividing the net rate of profit on equity obtained in the Petro-Core, by the matching rate attained by the Petroleum 40–42 – the latter being a broader cluster of the world's 40–42 largest non-governmental petroleum companies (including the Petro-Core firms). The results show that, during the late 1960s and 1970s, despite the competitive assaults from new entrants, the Petro-Core was able to maintain its net rate of return more or less in line with the other oil companies, and that during the 1980s it actually succeeded in surpassing them. A similar result is obtained in the third column, where we compare the net rate of return for the Petro-Core with that of U.S. dominant capital as a whole, approximated by the Fortune 500. Here, too, the large Petro-Core firms exhibit a remarkable staying power, even after the 'OPEC revolution' and the politicisation of oil in the industrialised countries. Indeed, despite the wholesale surrendering of concessions, the revoking of preferential U.S. foreign tax-credits, and a list of other adverse consequences of the new

5 Earlier pre-crisis studies are also not without fault. For example, in his work *Multinational Oil*, Jacoby (1974: 245–7) showed that the large oil companies suffered a significant decline in their foreign profitability, which he attributed to increased competition since the mid-1950s. Jacoby's methodology and implications are questionable, however. First, much of the decline of international profits in the 1950s was rooted not in more intense competition, but in higher royalties to host countries. Second, since the royalties were debited as foreign taxes against the oil companies' domestic operations, focusing only on foreign operations serves to conceal the compensating increase in domestic after-tax earnings. Indeed, as Blair (1976: 193–203, 294–320) demonstrated, the decrease in the companies' global rate of return was far smaller than the one recorded in their operations abroad. Furthermore, global profitability started to rise again in the early 1960s and, by the early 1970s, was already far higher than in the early 1950s.

oil order, the Petro-Core's rates of return in the 1970s, 1980s and early 1990s were higher than the comparable averages for U.S. dominant capital as a whole.

Table 5.2 The Petro-Core:<sup>(a)</sup> Differential Profitability Indicators (annual averages, %)

| Period  | Rate-of-Return Ratios |   |                                     | Net-Profit Ratios                          |  |  |
|---------|-----------------------|---|-------------------------------------|--|--|--|
|         | 1<br>Rate of Return   | 2<br>Petro-Core<br>÷<br>Petroleum<br>40–42 <sup>(b)</sup> | 3<br>Petro-Core<br>÷<br>Fortune 500 | 4<br>Petro-Core<br>÷<br>Petroleum<br>40–42 | 5<br>Petro-Core<br>÷<br>Fortune 502 <sup>(c)</sup> | 6<br>Petro-Core<br>÷<br>All U.S. Corps |
| 1930–39 |                       |   |                                     |  |  | 9.1 <sup>(d)</sup>                     |
| 1940–49 |                       |   |                                     |  |  | 3.3                                    |
| 1950–59 |                       |   |                                     |  | 18.2 <sup>(e)</sup>                                | 7.2                                    |
| 1960–69 | 11.5 <sup>(f)</sup>   | 1.01 <sup>(g)</sup>                                       | 1.00 <sup>(f)</sup>                 | 61.3 <sup>(g)</sup>                        | 17.1   | 8.1                                    |
| 1970–79 | 14.3                  | 0.99  | 1.12                                | 61.7                                       | 18.0   | 9.0                                    |
| 1980–89 | 13.1                  | 1.08  | 1.03                                | 73.2                                       | 17.8   | 10.5                                   |
| 1990–91 | 11.5                  | 1.03  | 1.20                                | 78.1                                       | 22.3   | 9.1                                    |

(a) The Petro-Core consists of British Petroleum, Chevron, Exxon, Mobil, Royal/Dutch Shell, and Texaco.

(b) The Petroleum 40–42 denote the Pforzheimer & Co. group of major non-governmental petroleum corporations, representing a composite of 40–42 major worldwide oil firms aggregated on a consolidated, total company basis.

(c) The "Fortune 502" comprise the Fortune 500 corporations, as well as British Petroleum and Royal/Dutch Shell.

(d) Excluding 1931–32 in which total U.S. net corporate profits were negative.

(e) For 1954–59.

(f) For 1966–69.

(g) For 1968–69.

SOURCE: Net profit and rate of return on equity of the Petro-Core are from O'Connor (1962), *Fortune* directories and Standard & Poor's *Compustat*. Net profit of all U.S. corporations is from U.S. Department of Commerce through McGraw-Hill (Online), and from U.S. Department of Commerce, Bureau of Economic Analysis, *Statistical Abstract of the United States* (1992), Table 871, p. 542. Net profit and rate of return on equity for the Fortune 500 are from various "The Fortune 500" listings. Net profits and rate of return on equity for the world's 40–42 leading petroleum firms are from Carl H. Pforzheimer & Co., *Comparative Oil Company Statements*, reported in the *Statistical Abstract of the United States* (Annual).

Another way to assess the differential earning power of the large oil companies is by looking at their relative share in the profit of a wider aggregate of companies. This we do in the last three columns, where we compute the share of the Petro-Core in the net profits of the Petroleum 40–42 group, the 'Fortune 502' (as defined below), and all U.S.-based corporations. Beginning with the first of these net-profit ratios (fourth column), we can see that despite the Core's relative decline in terms of economic activity (such as concessions, reserves, production, refining, transportation and marketing), its distributive share of the industry's net profit did not decrease at all. If we consider the world's largest 40–42 petroleum companies as a reasonable proxy for the international non-governmental petroleum industry, then it appears that the share of the Petro-Core in global oil profit in fact rose – from around three-fifths

during the late 1960 and 1970s, to almost three-quarters by the 1980s, and then further, reaching close to four-fifths by the early 1990s. A similar picture emerges when we examine the share of the Petro-Core in the net profit of U.S. dominant capital (fifth column). Taking the Fortune 500 group again as our tentative proxy for U.S. dominant capital, and adding to its ranks the European-based British Petroleum and Royal Dutch/Shell, we can see that the profit position of the large Petro-Core firms within this modified 'Fortune 502' group has remained surprisingly unassailable. Here we have a longer time series, extending from 1954 to 1991, so the comparison is even more telling. During the late 1950s, when the oil majors were still the undisputed leaders of the international oil industry, the Petro-Core accounted for nearly one-fifth of the net profits earned by the Fortune 502 group, but that has hardly changed in the subsequent period when these firms presumably lost their pre-eminence to new entrants and politicians. The final indication for the enduring power of the Petro-Core is given by their net-profit ratio with the U.S. corporate sector as a whole – an index for which data are available since 1930 (sixth column). Following the Achnacarry and Red Line agreements of 1928, in which the large international oil companies divided the world and the Middle East between them, the Petro-Core became so powerful that, even with the Great Depression and collapsing raw material prices, it still managed to appropriate over 9 per cent of all net profits earned by U.S. corporations. The economic revival of the Second World War raised overall corporate profits, thus causing this net-profit ratio to drop significantly. However, during the 1950s, the ratio began to climb again, rising more or less continuously until, in the 1980s, it topped 10 per cent – more than the earlier record of the 1930s.

Clearly, then, as we move from means to end – that is, from economic activity to differential profitability – the historical picture seems to change, and rather significantly. What appears as the Petro-Core's relative decline from the viewpoint of exploration, production, refining and marketing, is not at all what we see when we reach the 'bottom line'. On the contrary, once we focus on the ultimate business criteria of differential accumulation, the oil crisis seems to turn from a menace to a blessing. The Petro-Core, far from losing ground, has actually held and even consolidated its leading position – relative to other international oil firms, relative to the U.S. big economy, and relative to the U.S. corporate sector as a whole.

Now, these findings are admittedly puzzling. After all, competitive pressures from new entrants and demands from governments did increase since the 1950s, so how did the Petro-Core manage to nevertheless come on top with such a feat of differential accumulation? Alternatively, given the Petro-Core's remarkable staying power, why did it give up so much control to governments? The paradox, though, is only apparent, and disappears quickly once we shift our attention from the industry's *formal* institutions to its *effective* power structure. The 1970s indeed altered the formal control of oil. But following the line of analysis first anticipated in the wake of the crisis by Blair (1976), and

recently summarised by Bromley (1991), one may argue that the ultimate consequence of this transformation was to consolidate rather than undermine the relative earning power of the large petroleum companies.

*Politicising Oil: From 'Free Flow' to 'Limited Flow'*

Perhaps the most fundamental aspect of this transformation was the progressive *politicisation* of the oil business.<sup>6</sup> While this process was to a large extent continuous, it is nevertheless possible to distinguish between two qualitatively different phases. The first period, roughly until the early 1970s, could be labelled the 'free-flow' era in world oil – this in the sense that the control of oil was exercised through private ownership with state 'interference' assuming only a secondary role (Turner 1983: Chs 2–3). During the 1920s and 1930s, the international petroleum arena was practically run by the large companies, particularly British Petroleum, Royal Dutch/Shell and Exxon. In 1928, the three companies, meeting in the Scottish castle of Achnacarry, divided the world between them. In that year, the same firms also signed, together with other companies, the Red Line Agreement to coordinate their activities in the Middle East.<sup>7</sup> Over the following three decades, explicit collusion slowly evolved into a broader system of complex arrangements and understandings, partly overt but mostly tacit, which together enabled the large oil companies to maintain their control of production, transportation, refining and marketing around the world (cf. Blair 1976: Ch. 5). However, the Second World War and the ensuing economic boom made things more complicated. First, the substitution of the United States for Britain as the leading Western power shifted the internal balance among the Seven Sisters in favour of the U.S.-based companies, undermining to some extent the group's previous cohesion. And second, the growing number of independent producers exerted downward pressure on prices, precisely at a time when rising nationalism in the Middle East and Latin America called for higher royalties. Threatened with loss of control, the large

6 Our own notion of 'politicisation' here is completely different from the realist concept of 'petro-political cycles' developed by Wilson (1987). According to the latter, during a sellers' market, producing countries are able to politicise the market in order to raise prices. During a buyers' market, on the other hand, Western countries are content letting competition reign, so as to bring prices down. Clearly, this focus on states does not allow for a *transnational* political coalition between the U.S. government, OPEC, the oil majors and the large armament contractors, along the lines developed in this chapter.

7 The extent of the companies' control during that time is well illustrated by their ability to contain the threat of oil glut throughout the Great Depression. During the 1930s, the Iraqi Petroleum Company – a joint venture between British Petroleum, Royal Dutch/Shell, CFP, Exxon, Mobil, and 'Mr 5 per cent', Calouste Gulbenkian – exercised a Veblenian policy of 'watchful waiting' throughout much of its 1928 Red Line Agreement regions. In Iraq, for example, the company actively utilised only 1 per cent of its concession; in Qatar it delayed production until 1950, some 18 years after the first exploration; and in Syria, it drilled shallow holes in order to fulfil its concession charter without producing any output (Blair 1976: 80–6).

oil companies resorted to classic predatory market practices against the independents, but that wasn't enough. And as the problem continued, the companies turned to their governments for help.

Government assistance, particularly in the United States, assumed a variety of forms, including foreign tax-credits to offset royalty payments, restrictions on the importation of cheap oil into the United States, exemptions from antitrust prosecution, and a CIA-backed coup against the Mossadeq government in Iran, to name a few. The fact that the large petroleum companies were able to secure such services is of course not entirely surprising, given their 'special relations' with successive U.S. administrations (cf. Tanzer 1969; Engler 1977). Part of this capital–state symbiosis was surely rooted in the strategic nature of oil. And yet that could by no means be the whole story. The reason, on which we shall elaborate later in the chapter, is that, on many occasions, U.S. government actions in favour of the large oil companies were patently *contradictory* to the nation's material interest.<sup>8</sup> Staunch realists like Stephen Krasner solved the anomaly by blaming such policies on 'nonlogical' behaviour and the 'misconceptions' of policy makers (1978a: 13–17). But there could be a much simpler explanation, namely that the oil companies, along with other dominant capital groups, were increasingly seen as synonymous with the national interest. Perhaps the best summary of this union was given by U.S. Major-General Smedley Butler:

I spent thirty-three years and four months in active service as a member of our country's most agile military force – the Marine Corps.... And during that period I spent most of my time being a high-class muscle man for Big Business, for Wall Street, and for the bankers. In short, I was a racketeer for capitalism.... Thus, I helped make Mexico and especially Tampico safe for American oil interests in 1914. I helped make Haiti and Cuba a decent place for the National City Bank boys to collect revenues in.... I helped purify Nicaragua for the international banking house of Brown Brothers in 1909–1912. I brought light to the Dominican Republic for American sugar interests in 1916. I helped make Honduras 'right' for American fruit companies in 1903. In China in 1927 I helped see to it that Standard Oil went its way unmolested. During those years, I had, as the boys in the back room would say, a swell racket. I was rewarded with honors, medals,

8 Indeed, many policy initiatives were cancelled solely due to opposition from the large companies. For example, during the Second World War, the large firms objected to the Petroleum Reserve Corporation taking control over their joint Saudi holdings, much as they opposed the Anglo-American Oil Agreement and the Saudi Arabian Pipeline. The big companies also refused to allow independent companies more than a symbolic share in the 1953 Iranian Consortium; they objected the 1970 Shultz Report which suggested to substitute tariffs for the dated system of import quotas; and they ignored the Administration's request to accommodate Libyan demands for a higher price. As a result, none of these policies and suggestions came to fruition (see Blair 1976: 220–30; Krasner 1978a: 190–205; and Turner 1983: 40–7, 152–4).



promotion. Looking back on it, I feel I might have given Al Capone a few hints. The best *he* could do was to operate his racket in three city districts. We Marines operated on three *continents*. (cited in Huberman 1936: 265–6, original emphases)

Such blunt services, however, were too crude and certainly insufficient for the post-colonial era. They were unsuited for the more subtle ‘new imperialism’ of transnational companies, and wholly inadequate for dealing with new problems such as business competition and the management of technical change. Since the 1960s, therefore, there emerged an urgent need for some ‘external’ force, a qualitatively new institutional arrangement which would bring crude production back to what the ‘market can bear’ – yet without implicating the oil companies as ‘monopolies’ and the Western governments as ‘imperialists’. Historically, this institutional arrangement appeared in the form of OPEC and the upstream nationalisation of crude oil.

The broad causes for this transition have long been debated in the literature, but at least one of its consequences seems fairly clear. As Adelman (1987) rightly pointed out, the cartel achieved something which, for political reasons, the oil companies could never have pulled off on their own: a *dramatic* increase in prices. The eighteen-fold rise in the price of crude oil between 1972 and 1982 would have been inconceivable under the ‘free-flow’ system of private ownership. Rapid increases of such magnitude required not only a tight institutional framework, but also that oil appeared to be in short supply. The problem, though, was that oil was hardly scarce. In fact, it was abundant. The industry was plagued by chronic excess capacity (from the perspective of profit, that is), and the only way to bring this back to what the market could ‘bear’ was through an exogenously imposed ‘crisis’. Such crisis, though, necessitates a *new political realignment*, and that is precisely what happened. With the nationalisation of crude oil, production decisions now moved to the offices of OPEC, opening the way to a new, ‘limited-flow’ regime.

The ‘limited-flow’ era worked wonders for OPEC. There can be little doubt about that. But the bonanza hardly came at the expense of the Petro-Core. On the contrary, OPEC, by working closely if tacitly with the companies, was instrumental in boosting their relative performance. The converging interests of these two groups is clearly illustrated in Figure 5.4, which shows a tight positive correlation between the value of OPEC’s crude oil exports on the one hand, and the net profit of the Petro-Core on the other. A simple linear regression between the two series suggests that for every one dollar increase or decrease in export, there was a corresponding 6.7 cents change in the companies’ net profit, and, moreover, that changes in the value of exports accounted for almost three-quarters of the squared variations in profits. Causality, however, was also running in the other direction, from the companies to the oil-producing countries. Although OPEC was providing the pretext for the crisis, there was still the need to coordinate output – and that it couldn’t do on its own. As Blair

(1976: 289–93) and Turner (1983: 90–7) correctly indicated, managing the immense complexity of the oil arena required an overall knowledge which OPEC lacked, and which could be supplied only by the oil majors. The latter, of course, were no longer controlling output directly as producers, but they were now doing so indirectly, as the largest buyers, or ‘offtakers’ of crude petroleum. Interestingly, the rationale for this new alliance was delineated already in 1969 by the Saudi petroleum minister, Sheik Yamani. ‘For our part’, he stated, ‘we do not want the majors to lose their power and be forced to abandon their role as a buffer element between the producers and the consumers. We want the present setup to continue as long as possible and at all costs to avoid any disastrous clash of interests which would shake the foundations of the whole oil industry’ (cited in Barnett 1980: 61). There emerged, then, a new and more sophisticated realignment. The oil companies have indeed relinquished formal control, but that was largely in return for higher profits. Perhaps the most striking expression of this new ‘trade-off’ was provided by British Petroleum. The 1979 revolution in Iran deprived BP from access to 40 per cent of its global crude supplies; yet in that very year its profits soared

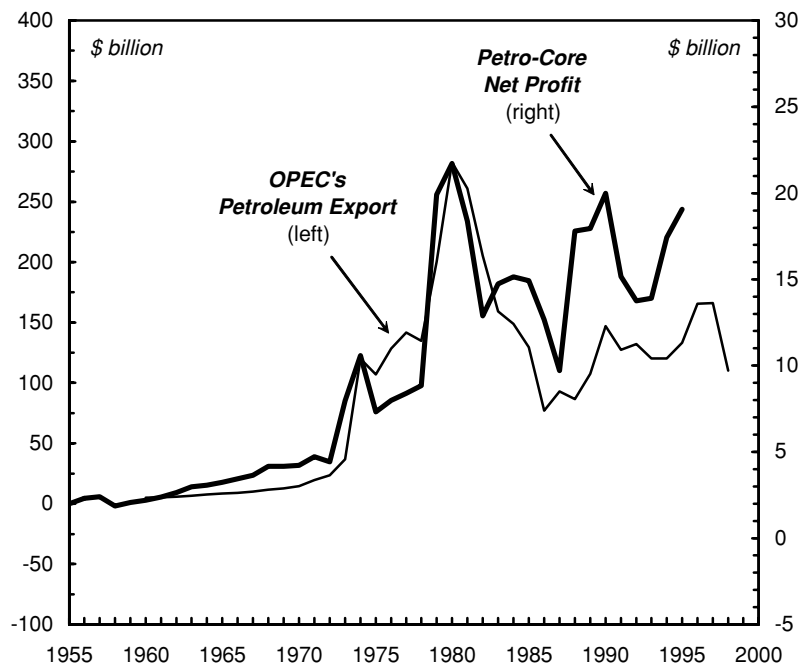


Figure 5.4 OPEC and the Petro-Core: Conflict or Convergence?

SOURCE: OPEC (Annual); Fortune.

by 296 per cent – more than those of any other major company (Turner 1983: 204; Yergin 1991: 684–7; and *Fortune*, ‘The Fortune 500’ 1978, 1979).

The convergence between OPEC and Western interests has long been suspected. On the eve of the first oil crisis, for example, Dan Smith suggested in *The Economist’s* survey titled ‘The Phony Oil Crisis’ (7 July 1973), that the U.S. Administration may have supported OPEC’s drive for higher prices as a way of slowing down the Japanese economy (see also Anderson and Boyd 1984: Chs 9–11; and Terzian 1985: 188–202). Another possible reason why the U.S. government ‘capitulated’ and accepted separate negotiations leading to the Tehran and Tripoli Agreements of 1971, was that the large oil firms saw this as a means of checking the ominous rise of independent companies (Blair 1976: Ch. 9). In the words of Odell (1979: 216), the 1970s brought an ‘unholy alliance’ between the large international oil companies, the United States, and OPEC, which together sought to use higher prices as a way of boosting company profits, undermining the growth of Japan and Europe, and fortifying the American position in the Middle East. To these, Sampson (1977: 307) also added the eventual support of the British government, the Texas oil lobby, the independents, investors in alternative sources of energy, and the conservationists – all with a clear stake in more expensive oil.

In a way, then, the oil arena has evolved in a direction opposite to that of the armament industry. While the military sphere of domestic spending and arms exports has been increasingly *commercialised*, the petroleum industry has grown more *politicised*. This politicisation, however, has by no means spelled the demise of the large oil companies. On the contrary, it became a *prerequisite* for their survival. The relentless search for new reserves, along with the incessant proliferation of new technology created a constant menace of excess capacity and falling prices. At the same time, with the number of actors on the scene growing rapidly, counteracting this threat solely through corporate collusion was impractical. For the large companies, the way to overcome these challenges was to integrate their private interests into a broader political framework.

### **The Weapondollar–Petrodollar Coalition and Middle East ‘Energy Conflicts’**

And so, toward the beginning of the 1970s, several groups of large U.S.-based firms saw their interests converging in the Middle East. To recap, the first of these groups included the large weapon makers of the Arma-Core which turned to the region in search of export markets. The second cluster comprised the leading oil companies of the Petro-Core, including those based in Europe, which were now driven toward a broader alliance with OPEC. These were also joined by a second tier of interested parties, including engineering companies such as Bechtel and Fluor with big construction projects in the oil regions, as well as large financial institutions with an appetite for petrodollars. Each of these groups stood to benefit from higher oil prices; and yet none could have done

so on its own. To push up the price of oil, they needed to act in concert, and this is how a 'Weapondollar–Petrodollar Coalition' between them came into being. In this section, we argue that, deliberately or not, the actions of these groups helped perpetuate an almost stylised interaction between energy crises and military conflicts. In this process of 'energy conflicts', the ongoing militarisation of the Middle East and periodical outbreaks of hostilities contributed toward an atmosphere of 'oil crisis', leading to higher prices and rising oil exports. Revenues from these exports then helped finance new weapon imports, thereby inducing a renewed cycle of tension, hostilities, and, again, rising energy prices.

#### *From Crisis to Prices*

Let's begin with prices. The common perception is that, one way or another, the price of crude oil depends on its underlying 'scarcity'. From this viewpoint, OPEC's early success is usually attributed to rapid Western growth during the 1960s and 1970s. This growth, it is argued, created 'excess demand' for oil, which in turn pushed up prices and made the cartel easy to manage. The same process, only in reverse, is said to have worked since the early 1980s. Lower industrial growth and improved energy efficiency, goes the argument, created 'excess supply', causing prices to fall and OPEC to disintegrate. Despite its popularity, however, this framework is vulnerable to both logic and fact.

From a long-term perspective, the relevant proxy for scarcity is the ratio of proven reserves to current production. Over the past three decades, due to extensive exploration, this ratio rose by a quarter – from about 30 production years in the mid-1960s, to over 40 production years during the 1990s (data from British Petroleum Annual). Now, according to the scarcity thesis, the increase should have brought crude oil prices down. And yet the exact opposite has happened. As Figure 5.5 shows, during the 1990s the real price of oil was not lower than in the 1960s, but *twice as high*. Whatever the cause for the long-term price appreciation, it was certainly *not* scarcity. And the concept is not much more useful in the short term. As we explained in Chapter 2, the argument that prices are affected by scarcity is meaningful only when such scarcity is set by natural or technical limitations. But that is by no means the case in the oil industry, which commonly operates well below its technical capacity. In this context, the impact on price of a 'shortfall' in supply is therefore a matter of sellers' collusion, not 'scarcity'.

The second problem with the scarcity thesis is that 'excess supply' and 'excess demand' reflect the difference between the *desires* of sellers and buyers; and desires, as we all know, cannot be directly observed, let alone quantified. A common way to bypass the problem, if only provisionally, is to use changes in inventories as a proxy for excess or shortage. But then the evidence from such exercise is often more embarrassing than revealing. The difficulty is illustrated

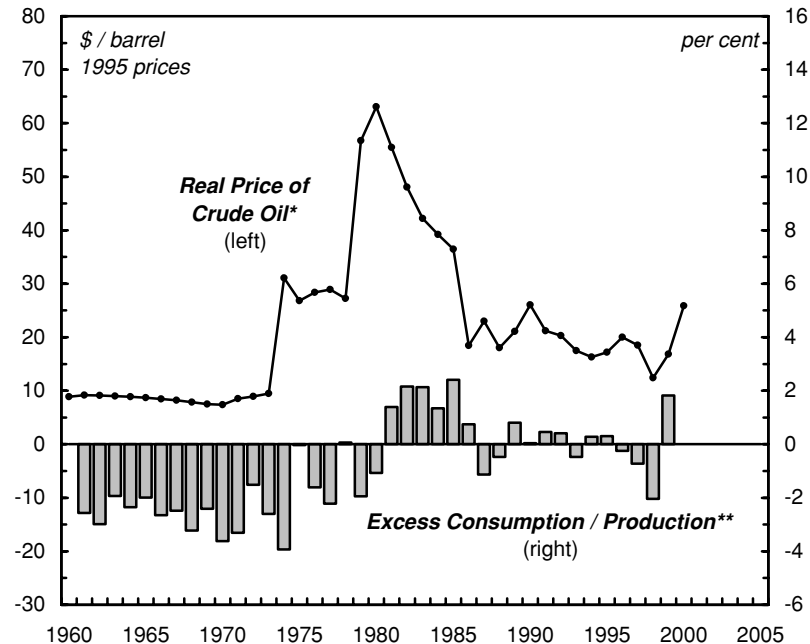


Figure 5.5 'Scarcity' and the Real Price of Oil

\* Spot \$ price divided by the U.S. Implicit GDP Deflator.

\*\* World consumption less production as a per cent of their average.

SOURCE: British Petroleum (Annual); IMF and U.S. Department of Commerce through McGraw-Hill (Online).

in Figure 5.5, where we contrast the real price of crude oil (denominated in constant 1995 dollars), with the excess of global consumption over global production (measured as a per cent of the average of the two). The latter variable reflects changes in inventories, with negative values representing build-up and positive ones denoting depletion. Now, if excess consumption indicates a 'shortage' (caused for example by unexpected rise in demand), and excess production represents a 'glut' (triggered for instance by the unforeseen arrival of 'distress oil'), then we should expect prices to rise in the former case and fall in the latter. The facts, however, tell a much more confused story. During the glut-plagued 1960s, the scarcity thesis seemed to be working, with inventories building up and prices falling. But then things started to go wrong. Although the inventory build-up continued through much of the early 1970s, the real price of oil *soared*, rising by 16 per cent in 1971, 4 per cent in 1972, 6 per cent in 1973, and 228 per cent in 1974. And indeed, according to Blair (1976: 266–8), the 1973/74 oil crisis had nothing to do with the 'oil shortage', simply because there wasn't any such shortage to begin with. Early in 1973, the ARAMCO

partners (Exxon, Mobil, Chevron and Texaco) were explicitly warned by the Saudis, both of the pending Egyptian attack on Israel, and of the possibility that oil would be used as a political weapon (see also Sampson 1975: 244–5). Anticipating the consequences, the companies raised production in the first three-quarters of the year, an increase which fully compensated for the eventual drop in the last quarter. All in all, OPEC production for 1973 amounted to 11.0 billion barrels, slightly higher than the 10.8 billion it should have been based on long-term growth projections (Blair 1976: 266fn). And the law of scarcity didn't seem to work much better in subsequent years. Between 1975 and 1980, inventories continued to accumulate, but the real price of oil, instead of remaining the same or falling, soared by a cumulative 135 per cent. During the first half of the 1980s, excess production gave way to excess consumption, and yet the real price of oil again refused to cooperate. Instead of rising, it fell by 71 per cent between 1980 and 1986. Even over the past 15 years, with the oil market presumably becoming more 'competitive' (notwithstanding the Gulf War of 1990–91), it is hard to see any clear relationship between excess demand and real price movements.

Last but not least, there is the issue of relative magnitudes. Indeed, even if we could ignore the direction of price movements, their amplitude seems completely out of line with the underlying mismatch between production and consumption. Over the past 40 years, world consumption was usually 2–3 per cent above or below world output. But then could such relatively insignificant discrepancies explain dramatic real-price fluctuations of tens or sometimes hundreds of per cent a year? And why are prices sometimes hyper sensitive to the mismatch, while at other times they hardly budge?

The solution for these perplexities is to broaden the notion of 'scarcity'. As a speculative commodity, the price of crude petroleum depends not only on the relationship between *current* production and consumption, but also – and often much more so – on *future* expectations. The prices buyers are willing to pay relate not only to present energy needs and the cost of alternative sources, but also to expected future prices. Similarly, sellers, both individually and as a group, are constantly weighing the trade-off between present incomes and anticipated but unknown future revenues. Moreover, these factors are not independent of each other. Indeed, buyers' willingness to pay is often affected by the apparent resolve of sellers; which is in turn influenced by the extent of consumers' anxiety. Once acknowledged, such intricacies imply that any given consumption/production ratio can be associated with a *host* of different prices, depending in a rather complex way on the nature of future expectations.

The significance of these considerations could hardly be overstated. To illustrate, consider the fact that after the emergence of OPEC, the number of primary industry players has grown appreciably – from less than a dozen in the 1960s to over 150 by the late 1970s, according to one estimate – and that still without counting governments (Odell 1979: 182). Such multiplicity should

have undermined the industry's ability to coordinate output, but that is not what the facts tell us. Indeed, if we were to judge on the basis of OPEC's revenues and the companies' profits as illustrated in Table 5.2 and Figure 5.4, it would appear that collective action was indeed more effective with hundreds of participants during the 1970s and 1980s, than with only a handful before the onset of the crisis! The reason for this apparent anomaly is that, in the final analysis, the price of oil – on the open market, but also between long-term partners – depends not only on the ability to limit current output to 'what the market can bear', but also on the nature of *perceived* scarcity associated with 'external' circumstances. And in our view, since the early 1970s, the single most important factor shaping these perceptions was the vulnerability of Middle East supplies.

The global importance of Middle East oil is of course hardly new, but its significance has increased substantially since the Second World War, and particularly since the 1960s. In 1972, on the eve of the first oil crisis, the region accounted for as much as 36 per cent of the world's total production and 62 per cent of its proven reserves, up from 12 per cent and 42 per cent, respectively, in 1948 (computed from Jacoby 1974: Table 5.1, pp. 68–9; Table 5.2, pp. 74–5). But as they became more crucial, the region's oil supplies were also growing more vulnerable. The oil 'prize' acted like a magnet, turning the Middle East into an arena of superpower confrontation. And this confrontation, combined with rising nationalism, growing class inequalities, and the ancient tensions of ethnicity and religion, helped stir up instability and armed conflict. The consequences for oil were twofold. First, the region's ongoing militarisation since the late 1960s created a constant threat for future energy supplies, helping maintain high prices even in the absence of tight producer coordination. Second, the occasional outbreak of a major conflict tended to trigger an atmosphere of immediate 'energy crisis', pushing confident sellers to charge higher prices and anxious buyers to foot up the bill. And, indeed, since the early 1970s it was regional wars which perhaps more than anything affected the course of oil prices. Despite the absence of any real shortage, the onset of such hostilities – the 1973 Israeli–Arab conflict, the 1979 Islamic Revolution in Iran, the 1980 launch of the Iran–Iraq War, and the 1990/91 Gulf War – invariably generated an atmosphere of 'crisis' and 'shortage', sending prices higher. Similarly, once the crisis atmosphere dissipated – either at the end of a war, or when conflict no longer seemed threatening to the flow of oil – prices began to stagnate and then fall. The importance of these features is attested by their incorporation into common jargon. The industry's 'price consensus', for example, now customarily incorporates, in addition to its 'peacetime' base, also such items as 'embargo effects' and 'war premiums' (*Fortune*, 5 November 1990). The precise magnitude of such 'premiums' and 'effects' cannot be determined, of course, but their significance seems beyond dispute.

*From Oil Revenues to Arms Imports*

The weapondollar–petrodollar link was also running in the other direction, with rising oil exports helping finance military imports to fuel the regional arms race. This side of the arms–oil interaction is examined in Figure 5.6, where we contrast the annual value of foreign arms deliveries to the Middle East, with the corresponding value of the region’s oil production three years earlier (both in constant dollars). The reason for the lag is that current oil revenues bear on the value of current military *contracts*, but the *delivery* of weapons, which is what we display in the chart, usually takes place later, with a lag of roughly three years.<sup>9</sup> We also express both the vertical and horizontal axes as logarithmic scales, in order to show the ‘responsiveness’ of arms imports to oil revenues. In this presentation, the slope of a trend line passing through the data indicates the per cent change of arms imports corresponding, on average, to a 1 per cent change in oil revenues three years earlier.

The first thing evident from the chart is the sharp ‘structural change’ affecting the relationship between the two variables. Around the early 1970s, as the oil regime shifted from ‘free flow’ to ‘limited flow’, the slope of the relationship tilted from a fairly steep position to a much flatter one. During the 1964–73 period, the trend line going through the observations had a slope of 3.3, indicating that for every 1 per cent change in oil revenues there was, three years later, a 3.3 per cent increase in arms imports. Despite this high ‘responsiveness’, though, the magnitudes involved were fairly small. Both superpowers were preoccupied with Europe and subsequently with East Asia, and since oil revenues increased only moderately, weapon shipments into the region, although responding eagerly, remained limited in size. By the early 1970s, however, things changed, and rather drastically. The slope of the trend line going through the 1973–97 data fell to 0.4, meaning that a 1 per cent rise in oil revenues during that period generated only 0.4 per cent increase in arms imports. And, indeed, in contrast to the 1960s, when the region’s export revenues were earmarked largely for weapon purchases, now they were allocated also to a range of civilian imports, as well as being accumulated as reserves in Western banks. But, then, with the flow of oil having been ‘limited’ by the high politics of government and companies, and with arms exports becoming increasingly commercialised, the dollar value of both oil income and military

9 Conceptually, we should have contrasted arms imports with the region’s *net income* from oil exports, rather than with the overall value of its oil output. The latter measure is broader, including, in addition to net export income, also production costs and the value of domestically consumed oil. Furthermore, our own measure here is imputed as the product of physical output multiplied by the average spot price, rather than measuring the actual revenues received. We use this proxy nonetheless because it is available consistently for the entire period, and since it correlates very closely with various net income series which are unfortunately available for only shorter sub-periods.



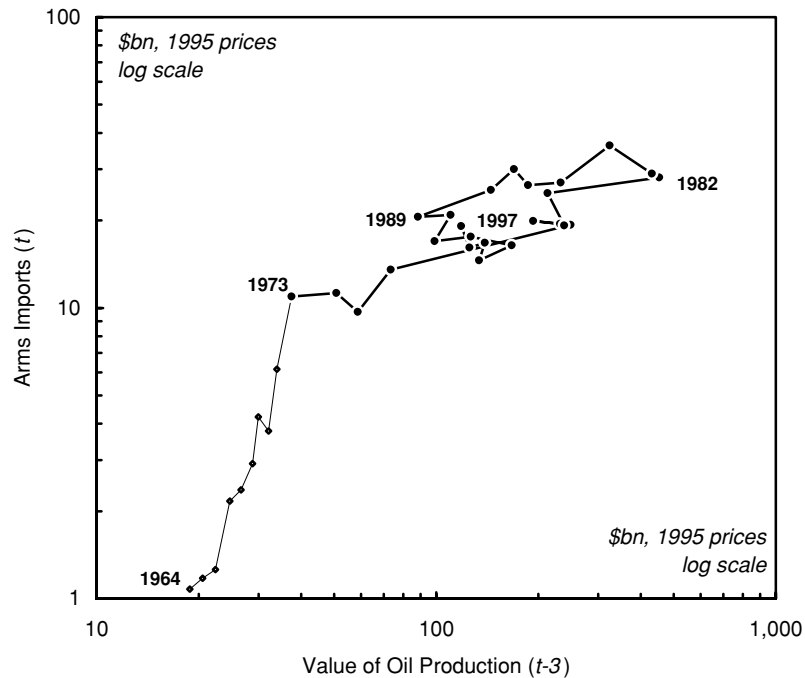


Figure 5.6 Middle East Oil Income and Arms Imports

NOTE: Value of oil production is computed as the multiple of output volume times the world spot price of crude oil. Current dollar figures for both oil production and arms imports are deflated by the U.S. implicit GDP deflator.  
SOURCE: British Petroleum (Annual); U.S. Arms Controls and Disarmament Agency (Annual); U.S. Department of Commerce through McGraw-Hill (Online).

imports soared to unprecedented levels toward the early 1980s – only to drop, again in tandem, when this order started to disintegrate since the mid-1980s.

The second, and perhaps more remarkable thing about Figure 5.6, is the extremely tight fit between the two series. Based on this chart, it appears that knowing the oil revenues of Middle Eastern countries was practically all that one needed in order to predict the overall value of arms deliveries three years later! Arms deliveries into the region were of course affected by numerous factors, including domestic tensions and inter-country conflicts, superpower policies to protect and enhance their sphere of influence, and the evolution of domestic arms production, to name a few. Furthermore, some arms deliveries were financed by aid or loans, so their import was not directly dependent on oil revenues. Yet, based on the chart, it would seem that these factors were either marginal, or themselves corollaries of the ebb and flow of the ‘great prize’ – oil.

*From Differential Accumulation to 'Energy Conflicts'*

We have now reached the final step of our brief statistical journey, ready to move from means to ends. Our method in this exploration was to progressively distil the interaction between oil and arms, moving from production, to sales, to profit, and, eventually, to the differential accumulation of the Weapondollar–Petrodollar Coalition. The task now is to identify the hidden links between this differential accumulation on the one hand, and Middle Eastern 'energy conflicts' on the other. Leaving the state and foreign policy for later in the chapter, and concentrating solely on the companies involved, our question is twofold. First, supposing that these firms acted in unison, how would their quest for differential accumulation relate to militarisation and conflict in the region? And, second, is this hypothetical relationship consistent with the facts?

Although the broader regime of tension and crisis was generally beneficial for the Weapondollar–Petrodollar Coalition, there were nevertheless certain differences between the interests of its armament and oil members. For the former, arms exports constituted a net addition to sales, so their gain from Middle Eastern militarisation and armed conflict was practically open ended. For the latter, however, the consequences of tension and hostilities were beneficial only up to a point, for two reasons. First, excessively high oil prices tended to encourage energy substitution, weaken profits in downstream operations, and lure entry from potential competitors. And, second, regional instability, if spun out of control, could undermine the close cooperation between the companies and oil-producing countries.

Hypothetically, then, we should expect the armament companies to have had little objection to ever-growing militarisation and conflict – this in contrast to the more qualified stance of the oil companies. Specifically, we speculate that as long as the Petro-Core companies managed to beat the 'big economy' average – that is, as long as they accumulated differentially relative to dominant capital as a whole – they judged their performance as satisfactory, and were generally content with having 'tension but not war'. However, when their rate of profit fell *below* that average, their position turned hawkish, seeking open hostilities in order to push up prices and boost their sagging performance. When that happened, the more aggressive stance of the large oil companies brought them into a temporary consensus with the leading armament firms. And it was at this point, we argue, when the Weapondollar–Petrodollar Coalition became united, that a Middle East 'energy conflict' was prone to erupt.

To see how well this hypothesis sits with the facts, consider Figures 5.7 and 5.8. The first of these charts contrasts the rate of return for the Petro-Core with the comparable rate for dominant capital as a whole, approximated here by the Fortune 500 group of companies. The second chart plots the difference between the two rates, expressed in percentage points. In both diagrams, dark areas denote a 'danger zone': a period of negative differential accumulation for

the Petro-Core, and a consequent risk of a new 'energy conflict'. The eruption of each such conflict is indicated in Figure 5.8 with a little explosion sign.

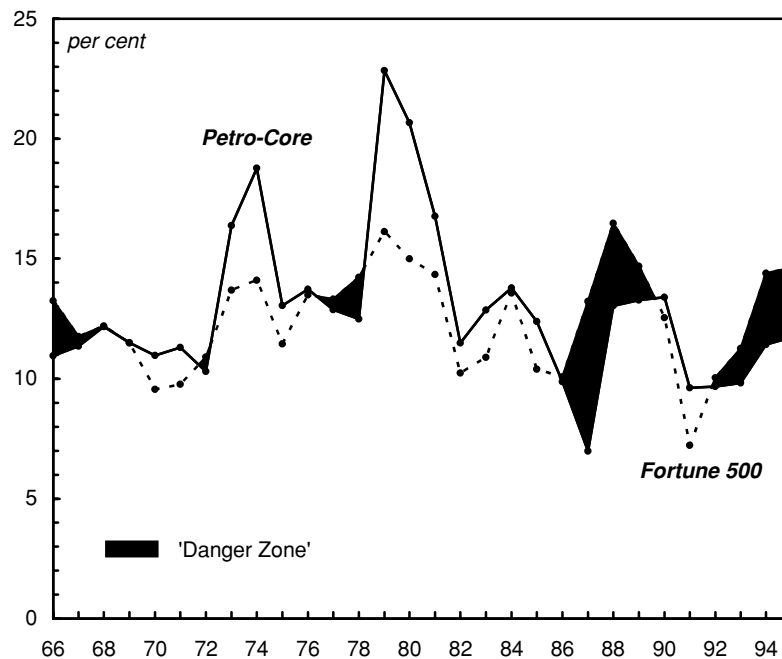


Figure 5.7 Return on Equity: The Petro-Core vs. the Fortune 500

NOTE: For 1992–93, data for Fortune 500 companies are reported without SFAS 106 special charge.

SOURCE: Fortune; Standard & Poor's Compustat.

The evidence arising from these charts is rather remarkable. First, until the early 1990s, *every single one* of these 'danger zones' was followed by the outbreak of an 'energy conflict' – the 1967 Arab–Israeli War, the 1973 Arab–Israeli War, the 1979 Islamic Revolution in Iran and the outbreak of the 1980–88 Iran–Iraq War and, recently, the 1990/91 Gulf War. Second, the onset of *each* of these crises was followed by a reversal of fortune, with the Petro-Core's rate of return rising above the comparable big-economy average. And finally, *none* of these 'energy conflicts' erupted without the Petro-Core first falling into the 'danger zone'. (The figures also make clear that the mechanism was by no means eternal. Indeed, after the 1990/91 Gulf War, a new 'danger zone' opened up – and yet this time there was no 'energy conflict' to close it. Even the 2001 war in Afghanistan has done little to prop up prices. The reasons for this change are dealt with at the end of the chapter.)

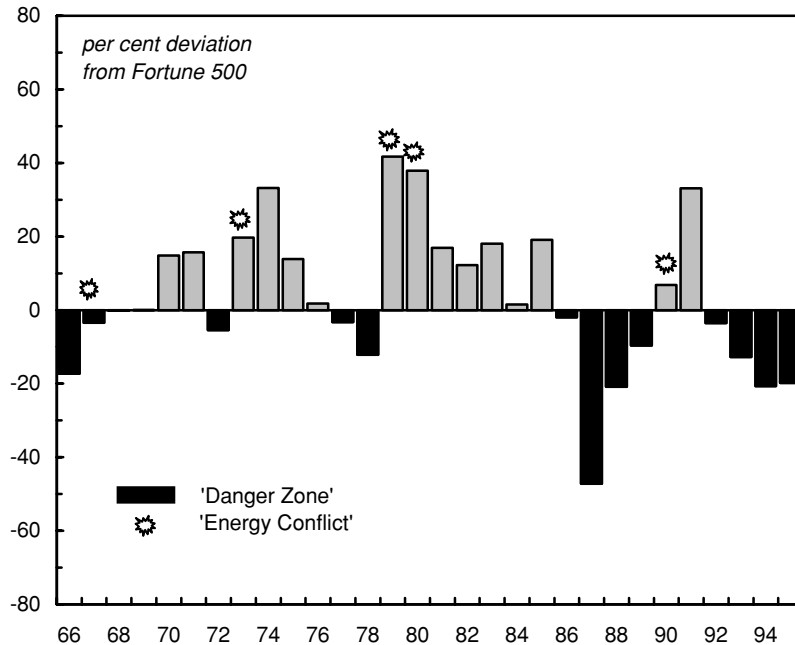


Figure 5.8 Petro-Core's Differential Accumulation and Middle East 'Energy Conflicts'

NOTE: For 1992–93, data for Fortune 500 companies are reported without SFAS 106 special charge.

SOURCE: Fortune; Standard & Poor's Compustat.

Given the complexity of Middle Eastern affairs, these three regularities seem almost too systematic to be true. Indeed, is it possible that the differential rate of return of six oil companies was all that we needed in order to predict such major upheavals as the June 1967 War, the Iran–Iraq conflict, or the Iraqi invasion to Kuwait? And what should we make of the notion that Middle East conflicts were the main factor 'regulating' the differential accumulation of the Petro-Core? Finally, are lower-than-normal earnings for the oil majors indeed a necessary condition for Middle East energy wars? Maybe the process pictured in Figures 5.7 and 5.8 is a statistical mirage? Perhaps the real causes of energy conflicts are totally different, only that by historical fluke they happened to coincide with differential profitability?

For instance, one simple alternative, still in the realm of business explanations, is that energy conflicts were triggered by movements in profitability rather than *differential* profitability. This, however, does not seem to be the case here. The figures show that the rate of profit of the Petro-Core fell in 1969–70, 1972, 1975, 1977–78, 1980–82, 1985–87 and 1991. Energy conflicts, on the other hand, erupted only in 1967 (after the Core's profits were rising),

in 1973 and 1979–80 (after they were falling) and in 1990 (after they were rising). Furthermore, despite falling profitability, no new energy conflict broke out in 1969–70, 1976, 1983 or 1988. Clearly, then, there is no straightforward connection between movements in the simple rate of profit for the Petro-Core and the occurrence of conflicts.

Another possible explanation is that energy conflicts were triggered not by setbacks for the Petro-Core, but by declining exports for the oil-producing countries. According to this argument, the destabilising impact of lower oil revenues would make governments more willing to engage in conflict in order to raise them up. The facts, however, don't seem to support this explanation either. For instance, Egyptian oil exports rose from \$35 million in 1970, to \$47 million in 1972, and to \$93 million in 1973 (United Nations Annual). If wars were indeed contingent on falling state revenues, this should have worked *against* the Arab–Israeli conflict in 1973. Similarly with the Iran–Iraq War. The conflict erupted in 1980, after oil revenues for the two countries were *climbing rapidly*, reaching \$18.4 billion for Iran and an all time high of \$26.9 for Iraq; and it ended in 1988, after revenues *fell sharply* to \$12.7 billion for Iran and to \$15.9 for Iraq, exactly the opposite of what we would expect based on the export logic (U.S. Department of Energy Annual). Finally, the 1990 Iraqi invasion of Kuwait occurred after several years of *stable* oil revenues, with Iraqi revenues during 1987–90 hovering around \$15 billion annually (*ibid.*). Of course, prior to his invasion to Kuwait, Saddam Hussain was under a growing financial strain accumulated during his years of fighting against Iran, so he needed much more than stable oil earnings to resolve his problems. Nevertheless, as we shall argue below, this rationale was hardly sufficient to outweigh a clear threat of forceful U.S. intervention – had there been one. Now, of course, every one of these conflicts could be explained by its own particular circumstances, many of which are related neither to oil nor arms. But recall that our purpose is to see if there was perhaps a broader logic to tie these conflicts together, and from this viewpoint, regional and local factors alone, although crucial, do not provide a picture nearly as consistent as the one offered by the Weapondollar–Petrodollar Coalition.

The corporate members of this Coalition, we argue, were not 'free riders' on the roller coaster of Middle East conflicts. Indeed, the evidence indicates not only that these companies *eventually* gained from militarisation and oil crises, but more fundamentally, that adverse drops in their differential profits have been a most effective *leading* indicator for upcoming 'energy conflicts'. This evidence cannot easily be dismissed as a chance occurrence. By the standards of empirical research, the links between differential accumulation on the one hand, and militarisation, 'energy conflicts' and oil crises on the other, are far too systematic and encompassing to be ignored. Clearly, there is need here for further exploration. How, for instance, was the weapon trade commercialised? What politicised the oil business? What role did the superpowers play in the process? How did Middle East governments, including Israel's, fit into the bigger

picture? Did the large corporations shape 'foreign policy' in the region, or were they themselves instruments of such policy? Can we actually draw a line between state and capital here? Should we? Let's turn then to look more closely at the actual history of the process.

### The 1967 Arab–Israeli War

Analyses of the June 1967 War are usually cast in terms of three regional processes, none of which is directly related to oil. The first process is of course the ethnic and cultural antagonism between Arabs and Jews, which began at the turn of the century, and which developed after 1948 into a nationalist clash between Israel on the one hand, and the Palestinians and the Arab states on the other (Safran 1978). The second process concerns the barriers on rapidly growing population imposed by an acute shortage of water. According to many writers this is the root cause of the conflict between Israel and its immediate neighbours, Jordan, Syria and Lebanon (Kelly 1986; Naff and Matson 1984; Rabinovitch 1983; and Sexton 1990). The third process, which received considerable attention in recent years, is the development since the 1950s of nuclear weapons by Israel (Hersh 1991). Some, such as Aronson (1992; 1994–95), see this development as crucial in determining Israel's foreign and security policies, and as a major force steering the region's recent history.

#### *Making America 'Aware of the Issue'*

Yet, the conflict was also related, even at that early stage, to the broader, *global* significance of the Middle East. The 'free-flow' era after the Second World War was marked by U.S. concerns regarding access to the region's oil fields. During the late 1940s and early 1950s, many at the State Department saw Israel as a destabilising factor. Military support to that country, argued the CIA, could provoke anti-American sentiments, weaken the U.S. position in Iran, Turkey and Greece, and possibly lead to a loss of control over the oil routes (Gazit, 1983a: 14). The Israelis, although formally non-aligned, were displeased with these negative attitudes, particularly since they had so much to offer. The sentiment of the country's elite in this matter was echoed by Gershon Schocken, editor of the daily *Ha'aretz*:

Israel had proven its military might in the War of Independence, so making it somewhat stronger could help the West keep the political balance in the Middle East. According to this view, Israel would act as a watchdog. It wouldn't become aggressive against the explicit wishes of America and Britain. But, if, for whatever reason, the latter were to turn a blind eye, Israel could be counted on to punish those neighbours whose attitude towards the

West had become a little too disrespectful.... (*Ha'aretz*, 30 September 1951, cited in Orr and Machover 1961: 158).

Until the mid-1950s, however, Britain still seemed to be doing a good job protecting the oil routes, and with its various positions in Iraq, the oil emirates, and the Suez Canal looking secure, the Israeli overtures were politely ignored. Ben-Gurion, though, was persistent. 'It's about time to make the defence of Israel part and parcel of defending the free world', he wrote to U.S. Secretary of State John Foster-Dulles (cited in Bar Zohar 1975: 1320). To demonstrate his commitment, he offered in 1951 to secretly dispatch an Israeli battalion in order to assist the U.S. war effort in Korea, while on another occasion he proposed that Washington finance a 250,000-strong Israeli military force, dedicated to defending the region against Soviet intrusions (Gazit 1983a: 16–19). 'There was something pathetic and shameful', wrote his biographer, 'in these repeated attempts to hold on to the U.S. skirt, particularly when the latter was trying, again and again, to get rid of the embarrassing nuisance....' (Bar Zohar 1975: 1320). And yet the efforts continued. Pinchas Lavon, who replaced Ben-Gurion as Defence Minister in 1953, tried a new, bolder direction. His intention was to set up a terrorist network in the Arab countries, with the purpose of attacking U.S. embassies and cultural centres. This, he hoped, would alienate the Americans against their Arab hosts, helping them realise that their only true ally in the region was Israel (Sharet 1978: Vols. II–III). The hasty plot was uncovered, and although the affair was never thoroughly investigated, Lavon had to resign, and eventually so did Ben-Gurion. The Israeli military, though, continued the escalation, using massive 'retaliations' against Palestinian guerrillas in the hope of warming up the conflict and pulling the United States into the fold (Sharet 1978: Vol. III; Cafafi 1994: 73).

The crowning achievement of this strategy was Israel's 1956 invasion of the Sinai peninsula, followed by Britain and France's attempt to take over the Suez Canal. *U.S. News and World Report* was quick to summarise the obvious: 'Why did Britain and France go to war against Egypt? In order to topple Nasser, to control the Suez Canal and save their oil' (9 November 1956, cited in Orr and Machover 1961: 297). The Israeli elite, on the other hand, denied any conspiracy. According to the official version, Ben-Gurion never went to France on the eve of the war to sign the Sèvres Treaty between the conspirators; there was no prior plan for France and Britain to take over the Canal in order to 'separate' the warring factions; and there was no intention to topple Nasser. The whole thing was an act of self-defence, pure and simple. Israel was threatened with annihilation, and so took a pre-emptive strike. Thirty years later, though, Shimon Peres, who participated in orchestrating the operation, presented a rather different version:

If it were not for the Suez Operation, the danger was that Britain and France would leave the Middle East before the Americans became aware of the issue,

therefore allowing the Russians to penetrate and shape the region without the U.S.A. Following the Suez Operation, the Americans became committed to a regional balance. It was this commitment which shaped the U.S. stance toward the Six Day War.... (cited in Evron 1986: 164)

In other words, Ben-Gurion and his clique managed to trick their allies as well as foes. Not only was there no threat of 'annihilation', but the 'eternal Franco-Israeli friendship', which Peres always took credit for cementing, was itself merely a temporary move. The real goal was to make the Americans 'aware of the issue'.

#### *Subcontracting*

And aware they became. Following the Suez debacle, the 'free flow' of oil no longer looked secure. The emergence of Pan-Arabism and increasing Soviet intrusion into the region presented a growing threat to the feudal regimes of Saudi Arabia and surrounding sheikdoms. In 1958, Faisal, the pro-American king of Iraq was assassinated, and the 1954 Baghdad Pact erected by the British fell apart. In that same year, Syria and Egypt merged into the United Arab Republic, prompting King Hussein of Jordan to request American aid and British paratroops for his protection, and the Maronite government in Beirut to invite the U.S. marines. These developments gave rise to the new 'Eisenhower Doctrine'. According to this doctrine, the United States itself would assume military responsibility for the Persian Gulf and the Arab Peninsula (Gold 1993: 35). However, the new realignment also required to fortify the perimeter surrounding the oil region, and here Israel came in handy. Valued for its stability, pro-Western characteristics and logistical potential, it was declared a 'strategic asset' for the West (Safran 1978: Ch. 20). With persistence and a dose of good luck, the dream had finally come true.

Initially, the State Department was careful to not openly support the Jewish state. The CIA, however, having fewer inhibitions, quickly started fashioning covert liaisons with local politicians and security officials. Many of these relations were built around a proposal by Ben-Gurion that Israel create a peripheral, pro-American alliance with non-Arab countries, such as Turkey, Iran and Ethiopia, in order to contain Arab radicalism. A central feature of this 'peripheral alliance' was a secret agreement, code-named *KK Mountain*. According to the agreement, the Israeli Mossad would become a permanent paid 'subcontractor' for the CIA, carrying out delicate operations which the U.S. legislator and judiciary would otherwise find difficult to stomach. Since the region's 'bastion of democracy' was much more lenient in these matters, the deal seemed only fair, and the Mossad quickly found itself involved in numerous proxy undertakings around the world. In the Middle East and Africa, these included military assistance to various groups and regimes, such as the royal



forces in Ethiopia and Yemen, the Kurds in Iraq, the army and secret service of the Iranian Shah, the secret police in Morocco, the security forces and military of South Africa, and the rulers of Uganda, Zaire and Nigeria. Later, the Israelis would also diversify into Latin America, providing their ware and knowledge to pro-American dictatorships such as Panama, Chile, Nicaragua, Honduras, El Salvador and Guatemala (Cockburn and Cockburn 1991: Chs 5, 9, 10).

Some of these operations were allegedly part of the CIA's effort to have the new Kennedy Administration pay more attention to the Middle East. The role of the CIA is especially noteworthy, because, after the Second World War, and particularly since the early 1950s, the Agency's Middle Eastern activities were almost exclusively handled by the ARAMCO partners and Bechtel (McCartney 1989: Ch. 10). Kennedy wasn't swayed. Despite his favourable attitude toward the petroleum industry and the close oil connections of some of his top officials,<sup>10</sup> he continued pursuing his policy of appeasement toward Nasser. However, his 'New Look' doctrine also permitted, for the first time, American military shipments to Israel. Contrary to the 'nuclear-containment' policy of his predecessors, Kennedy emphasised the use of conventional weapons and direct involvement against Soviet subversion. In 1960, he announced that he was not opposed to a 'military balance' between Israel and the Arab countries, and that in global matters the United States had 'special relations' with Israel, comparable only to its relations with Britain (Safran 1978: 581; and Gazit 1983a: 33).

#### *Breaking Nasser's Bones Asunder*

Initially, the change may have been partly motivated by Kennedy's desire to check Israel's nuclear development programme, and to prevent an out-of-control nuclear arms race between Israel and Egypt (Gazit 1983b: 49–56). Another possibility is that Kennedy was simply paying off the Jewish Lobby for financing his election campaign (Hersh 1991: Ch. 8). But toward the mid-1960s, when attempts to appease Nasser seemed to go nowhere, his successor, President Johnson, put Kennedy's 'special relations' into practice, and began sending Israel large military shipments. Despite his preoccupation with the intensifying conflict in Vietnam, Johnson was nevertheless worried about the fighting in Yemen, where Egyptian troops had on a number of occasions crossed the border into Saudi Arabia. After the end of its involvement in Libya and in the Congo, the United States ceased its economic support to Egypt altogether, and instead switched to overtly assisting the Jewish state. In 1966, at the height

10 Some of these connections involved the Texas oil associations of Vice-President Johnson, the southwestern and international oil affiliations of Secretary of the Navy Connally, the Rockefeller links of Secretary of State Dillon, and the long-term business partnership between CIA director McCone and the Bechtel family (Engler 1977: 57–8; McCartney 1989).

of its entanglement in Vietnam, Washington began giving Israel, for the first time, *heavy* assault weapons, including tanks, aircraft and missiles.

In that year, Soviet involvement in the region seemed more menacing than ever. First, Britain announced it would soon be leaving Aden, notwithstanding the ongoing Soviet-backed war in neighbouring Yemen, just south of the world's richest oil fields; then, the pro-Soviet Ba'ath party staged a coup in Syria; and finally, the Kremlin began to promote a socialist union between Egypt, Syria, Algeria and Iraq, threatening to engulf Saudi Arabia from the west and north. Given its difficulties in Vietnam, the United States was not prepared to counteract these developments directly, but Israel certainly was and did.

Toward the end of 1966, the Arab–Israeli dispute was again heating up. In November, Israel staged a massive raid into the Jordanian town of Samoua, officially in retaliation for guerrilla attacks. Then, in April 1967, an Israeli tractor, sent to cultivate a demilitarised zone just beneath the Golan Heights, sparked a border skirmish which ended with humiliating Syrian losses. Adding insult to injury, the Israelis went on to announce their intentions of forcibly dethroning the Damascus regime. Faced with mounting challenges to his Pan-Arab leadership, Nasser was more or less compelled to respond, moving two army divisions into the Sinai desert and closing the Straits of Tiran. There are, of course, other explanations. Aronson (1994–95), for instance, argues that the escalation was in fact an unintended consequence of Nasser trying to stop the development of nuclear weapons by Israel. One way or the other, it is clear that the Americans (like the French and British before them) hoped that Israel would use the opportunity to topple Nasser, and the closing of the Tiran Straits now offered the pretext for a pre-emptive strike.

Contrary to popular belief, the Israeli and American leaderships had little doubt about the outcome of the looming war. The certainty of Arab defeat was also known to Nasser – as well as to the other Arab participants – but given their internal disputes, they found it politically impossible to ignore Israeli provocations, and were thus increasingly drawn toward a point of no return.<sup>11</sup> Following the closure of the Straits of Tiran, Israel scheduled its attack for 25 May, but had to wait until 6 June, after Meir Amit, head of the Israeli Mossad, returned from an emergency trip to Washington with the 'green light' to 'break Nasser's bones asunder' (Haber 1987: 214–16). And so, by maintaining its loyalty to U.S. strategic interests in the region, Israel had finally succeeded in

11 According to former Israeli ambassador to the United States, Abba Eban, many in the State Department were convinced of Israel's military superiority and ability to win a 'crushing victory' already in the 1950s (Eban 1977: 185). After the 1967 War, IDF generals such as Ezer Weitzman, Benjamin Peled and Yitzhak Rabin, admitted quite openly that Nasser had presented no real danger. Ten days before the war, a secret CIA report delivered to Johnson accurately predicted an Israeli victory within six days. Some U.S. officials who hoped to avert a war communicated these assessments directly to Jordan and Egypt and, indeed, until the last moment, Nasser still hoped for a diplomatic resolution (Cockburn and Cockburn 1991: 140–54).

joining the U.S. orbit as an official satellite, a process which would further intensify during the 1970s and 1980s.

Preoccupied with the 'free flow' of oil, the Petro-Core may have viewed the war's outcome as highly favourable: Soviet aspirations were undermined and the cause of Pan-Arabism suffered a serious blow. However, the companies must have also noticed the positive effect the war had on their differential profitability (see Figures 5.7 and 5.8) – an ominous sign that their 'free-flow' system was itself coming to an end.<sup>12</sup> And as if to hasten the process, the aftermath of the war was marked by increasing arms exports. Rewarded for its victory, Israel began receiving F-4 Phantom aircraft made by McDonnell Douglas, which were previously sold only to Britain and Germany. With this, the door was now open for an arms race of sophisticated weapons, a race which would eventually help 'limit' the flow of oil and introduce the petroleum business into the new era of 'crisis'.

### The 1973 Arab–Israeli War

The 1968 U.S. presidential elections brought in an administration highly attuned to the coinciding interests of oil and arms. Nixon's campaigns were supported heavily, and sometimes illegally, by contributions from both defence contractors and oil companies, while his Secretary of State Kissinger enjoyed close connections with the Rockefellers, and proposed an aggressive realpolitik which on more than one occasion entertained the feasibility of 'limited' nuclear war.<sup>13</sup> In the eyes of this new administration, the 1967 War did little to secure U.S. interests in the Middle East. Qaddafi's 1969 showdown with the oil companies in Libya and the attempted coup in Saudi Arabia were disconcerting reminders of pending regional hazards. Washington, so it seemed, must pay more attention, not less, to this troubled area.

#### *The Realist View*

And yet, that was easier said than done. In 1969, the United States began withdrawing its troops from Vietnam, and with warmer relations with China

12 While official crude prices had not changed, fuel prices for Western consumers rose, thus boosting the profits of the oil companies while undermining them elsewhere in the economy.

13 On Nixon's campaigns, see Sampson (1975: 205–6) and Sampson (1977: 151–2, 195). On Kissinger, see Barnet (1983: 178–9). Representatives of Rockefeller's Chase Manhattan were involved in the network of activists around Nixon's career, and some of them accepted key posts in his administration. Paul Volker, for example, was made Under Secretary of the Treasury for Monetary Affairs; John Letty became Assistant Secretary of the Treasury; and Charles Fiero became Director of the Office of Foreign Direct Investment in the Commerce Department (Barnet and Müller 1974: 251; Turner 1983: 105).

and the declaration of Détente, the new 'Nixon Doctrine' called for a lower defence budget. Instead of Kennedy's strategy to prepare for '2½ wars', Nixon and Kissinger offered resources for only '1½ wars'. In 1969, the policy kicked in, and domestic military spending started to fall. From a statist viewpoint, the result was to weaken U.S. capabilities in the Middle East, this precisely when the region emerged as one of the world's most sensitive (Gold 1993: 40). Moreover, Britain's withdrawal from its last stronghold in the Persian Gulf, together with the United States losing its last strategic air base in Libya, created a military vacuum. The solution, stipulated by Kissinger, was for the United States to concentrate only on 'core conflicts', leaving 'peripheral conflicts' to be handled by local pro-American forces. The consequences for the region were twofold. First, Washington embarked on massive arms exports, initially to Israel and the 'twin pillars', Iran and Saudi Arabia, but later also to Egypt and other countries. Second, State Department attempts at settling the Arab–Israeli conflict were now frustrated by White House support for Israel (Safran 1978: Ch. 23). With Middle Eastern affairs increasingly handled by the Nixon–Kissinger duo rather than State Secretary Rogers, Israel was now used as a threat against anti-American Arab countries (Kissinger 1979: 1285, 1289). Kissinger was particularly intimidated by what he regarded as deliberate Soviet challenges, and in 1970 worked out, together with Yitzhak Rabin, then Israel's ambassador to Washington, a joint plan for military intervention in case Syria or Iraq attacked King Hussein of Jordan.

These observations do not sit well with the realist perspective. First, given the split between the conciliatory position of the State Department and the aggressive stance of the President, it is not clear what 'national interest' American policy makers were trying to achieve. Second, the type of cannon diplomacy entertained by Kissinger did not look particularly conducive to his goal of regional stability. Indeed, according to Safran (1978: Ch. 23), the United States continued to send arms to the region, this despite its own fears that an Israeli victory against Arab aggression would cause chaos and seriously disturb the flow of oil.

#### *The Coalition's View*

From the viewpoint of the Weapondollar–Petrodollar Coalition, however, U.S. foreign policy here seems pretty consistent. Declining military spending at home hurt the large defence contractors badly (Sampson 1977: 214–21), and with pressures from these contractors coinciding with his own strategic outlook, Nixon moved to further commercialise arms exports. His new doctrine stipulated that the burden of defending U.S. allies – financially as well as in manpower – should now be borne by those allies themselves (Ferrari et al. 1987: 21). In order to do that, explained military contractor David Packard (then acting as Deputy Secretary of Defense), the United States was ready to 'give or

sell [to these allies] the tools they need for this bigger load we are urging them to assume' (quoted in Sampson 1977: 243). In the Middle East, the Nixon Doctrine elevated the arms race to a new level. Commercialisation, to be sure, was not strictly enforced. Israel, for instance, was unable to pay for its rapidly rising military imports; and, yet, to its great surprise, Washington was willing to give them for free (Rabin 1979: Ch. 4).<sup>14</sup> Officials in Jerusalem celebrated this as a 'huge achievement' (Gazit, 1983a: 53), only that they failed to notice the even greater achievement of other states, who, unlike Israel, were both able and willing to pay.

The most 'successful' of the lot was Iran. On their visit to Tehran in 1972, Nixon and Kissinger reputedly agreed to sell Iran 'virtually any conventional arms it wanted' (cited in Sampson 1977: 252). And with this newly acquired freedom to sell, U.S. armament companies quickly started courting the country's Shah, whom Washington now appointed as 'policeman of the Gulf'. At the time, domestic sales to the Pentagon were hitting rock bottom, so military exports to Iran provided a much needed lifeline for many contractors (Figure 5.3). The extent of these exports, however, depended crucially on the petroleum revenues of the Peacock Throne, an important detail which both Nixon and Kissinger were most surely aware of.<sup>15</sup> And, indeed, the oil industry, too, was undergoing a profound transformation. With weakening prices and falling profitability, as illustrated in Figures 5.5 and 5.7, the large petroleum companies came to realise the potential benefit of a stronger OPEC. The cartel's apparent resolve to control output impressed the oil majors, and their London Oil Policy Group was now ready to accept a new revenue-sharing agreement (Odell 1979: 105, 215). But although the price of oil started to rise in 1971, the Petro-Core's rate of profit continued to linger and, in 1972, fell dangerously below the Fortune 500 'normal' (Figures 5.7 and 5.8).

And then came the October 1973 'energy conflict'. The war brought a sharp increase in prices, restoring the oil companies' differential profitability high above the big-economy's average. At the same time, it also generated dramatic increases in the oil revenues of Arab countries, with immediate consequences for the arms trade. In 1974, a year after the war, the Middle East surpassed South East Asia to become the world's largest market for imported weapons, with over one-third of the global trade.

14 During the 1962–66 period, Israel's annual weapon imports averaged \$107 million. After the 1967 War, with the United States replacing France as the main supplier, the average almost tripled to \$290 during 1967–69, and in 1970–72, with the Nixon Doctrine starting to kick in, it rose further to \$550 (unpublished data from Israel Central Bureau of Statistics, courtesy of Reuven Graff).

15 Allegations that the U.S. government was promoting higher prices as a primary means of funding U.S. arms deliveries to the Shah were put forward on the CBS programme *Sixty Minutes* (3 May 1980). Kissinger, though, declined to comment (Chan 1980: 244). Kissinger was also closely associated with Rockefeller's Chase Manhattan, and it is not far fetched to assume he also contemplated the benefit for the bank from higher petrodollar deposits (*Ha'aretz*, 2 January 1981).

While there is no evidence to implicate the U.S. Administration as instigator in the conflict, there is also little to indicate it keenly tried to prevent it. To be sure, the war didn't catch the Nixon government by surprise. Warned by King Faisal of Saudi Arabia already in the beginning of 1973, the ARAMCO partners were aware of what was coming, and they passed on the information to Washington (Blair 1976: 266–8; Sampson 1975: 243–8; and Yergin 1991: 593–7). A similar message came from a CIA study (incidentally co-authored by the same analyst who anticipated that the 1967 War would last only six days), which concluded that the Egyptians were planning to attack Israel (Cockburn and Cockburn 1991: 171). Indeed, Kissinger was directly informed of the pending assault, both by Jordan's King Hussein (who between 1957 and 1977 was a paid CIA agent), and by sources close to President Sadat of Egypt (Neff 1988: 105).

*The U.S. 'National Interest': What Price Stability?*

These observations seem perplexing. If Nixon and Kissinger were indeed concerned with maintaining regional stability as stipulated in the realist literature, why didn't they heed Saudi requests that Washington softened its support for Israel? To suggest that this was because the Administration was by then irrevocably committed to the Israeli cause is not persuasive; for if that was the case, why did it fail to warn the Israelis of the pending calamity? Indeed, why did Kissinger caution Israel not to fire the first shot when the latter finally realised that Egypt and Syria were about to attack? One common interpretation is that Kissinger wanted the Arabs to win their self-respect and some territory, which would then be traded for peace through his own mediation (Hersh 1991: 227). However, from a statist viewpoint, Kissinger was walking on a tightrope here. The problem, according to his own admission, was how to achieve a 'balanced' outcome – one in which the war would end after Israel had recovered some of its earlier losses, but before it had the chance to destroy its opponents. For Kissinger, this must have been a real problem. He had absolute confidence in Israel's military ability and feared that an Israeli victory would be devastating for U.S. regional interests (possibly by inciting leftist coups and encouraging Soviet intervention). Yet despite the obvious danger, he stuck to his plan, moving to broker a ceasefire only at the last moment, after Israel had threatened to use nuclear weapons (Safran 1978: Ch. 23).

Clearly, then, realist calculations alone do not tell the whole story. Attuned to the plight of the oil and armament companies, Kissinger must have also pondered how an oil crisis might boost their coinciding interests. And indeed, after the war, with petrodollars and weapondollars locked in an upward spiral, peace between Israel and the Arabs was put on the backburner. The more urgent task now was to keep the 'balance of power'; and sure enough, instead of preaching reconciliation, we find the U.S. ambassador to Cairo recommending military shipments to Egypt, while his colleagues in Kuwait and Saudi Arabia

explain the merit of American-made aircraft to local rulers (*New York Times*, 21 July 1975, cited in Frenkel 1991: 76). Working now for the new Ford Administration but still pursuing his original plan, Kissinger helped establish an 'interim agreement' between the warring factions. This time, though, the United States held the carrot as well as the stick; it could use Israel as a threat against pro-Soviet Arab regimes, but it could also force it to return occupied Arab land to those who promised to leave the Soviet orbit and cross the floor onto the American side (Safran 1978: Ch. 25). However, the U.S. Administration was also careful to insist that any interim agreement should not evolve into a comprehensive settlement. When in July of 1975 the Israeli government appeared willing to go to a peace conference in Geneva, President Ford threatened to withdraw American assistance (*New York Times*, 3 July 1975). The imperative of maintaining tension was spelled out clearly less than a year later. Appearing before the Jewish-American Congress in April of 1976, Henry Kissinger effectively asserted that a comprehensive Middle East peace depended not so much on the warring factions, but rather on the superpowers first agreeing on their respective spheres of influence (reported in Meyer 1976: 157).

These pursuits on the armament front also help shed some light on the Administration's energy policy. On the surface, Washington's view on the subject seemed confused, even contradictory. Based on his analysis of over one thousand State Department cables and papers obtained under the Freedom of Information Act, Yergin (1991: 84) concluded that, between 1974 and 1981, the U.S. government in fact objected to higher oil prices. But then he simultaneously inferred that the government didn't want to see those prices lowered either (p. 643). This indecisiveness, Yergin argued, was rooted in a conflicting quest for lower energy cost at home, coupled with a richer and thus more stable Middle East. And yet, if the goal was indeed stability, why send so much armament to the region, particularly when Washington itself doubted their contribution to peace? And what about the support of Kissinger and the International Energy Agency for a 'minimum safeguard price' as a means of protecting *Western* interests? (Sampson 1975: 306; and Turner 1983: 184). Perhaps the Administration, despite its declarations to the contrary, was in fact interested in *neither lower oil prices nor regional stability*? After all, representatives of the Weapon-dollar-Petro-dollar Coalition were now increasingly involved in 'state policy', so couldn't they have pushed things in that direction?

The realist failure to square the circle around oil prices is only understandable. The basic reason is that, by the 1970s, while the world was already well into the 'limited flow' era, realist theories were still stuck in the 'free flow' logic. Stephen Krasner, for example, claimed that there was a negative trade-off between the level and variability of petroleum prices (1978b: 39-40). The consequence, he concluded, was that policy makers had to choose between low but variable prices, or stable but high ones. Yet, when those lines were written, this menu had already become irrelevant, and in fact misleading. From the late 1960s onward, with oil shifting to a 'limited flow' footing, the rela-

tionship between the level and variability of prices became *positive*. The choice now was not between low and variable oil prices as opposed to high and stable ones, but rather between low and stable prices against high and volatile ones. Obviously, this transition fundamentally altered the relationship between the oil companies and the so-called ‘national interest’. During the early period, when the companies were concerned mainly with concessions, the Administration’s willingness to have higher prices in order to secure stability and access seemed sensible. It helped the companies, as well as the broader U.S. ‘national interest’. Since the late 1960s, however, harmony gave way to discord. The United States could no longer pay higher prices in order to achieve access and price stability; it couldn’t, simply because access was no longer negotiable, whereas higher prices were clearly causing *greater instability*. The oil companies, on the other hand, were now interested not in access but in higher prices. Contrary to the earlier situation, therefore, there was now clear conflict between the companies and the ‘national interest’, and the Administration’s pursuit of both instability and higher prices only indicates where its allegiances lay.

Initially, the coinciding interests of the Arma-Core and Petro-Core in regional turmoil were blurred by the imaginative use of language, which insisted on equating arms shipments with ‘stabilisation’. For example, Secretary of State Rogers, who would later become a retainer for the Iranian Shah and board member of the oil company Sohio, characterised U.S. military sales as having a ‘stabilising influence’ – this in contrast to the ‘invitation for trouble’ posed by similar Soviet shipments (Engler 1977: 242). Similarly, Kissinger (1981: 182), using a more academic lingo, explained that the ‘balance of power is a kind of policeman, whose responsibility is to prevent peaceful countries from feeling impotent and aggressors from becoming reckless’. Eventually, however, as the Orwellian identity of weapons and peace began to dissipate, the true forces at play came into focus.

The rising influence of the Weapondollar–Petrodollar Coalition coincided with the new policies of Jimmy Carter. Unlike Nixon’s, the ‘Carter Doctrine’ moved from emphasising loyal proxies – chiefly Israel and the ‘twin pillars’, Iran and Saudi Arabia – to direct military intervention. With growing nervousness on the part of the Saudi pillar – first in response to Soviet involvement in the Horn of Africa, and later as a consequence of Soviet participation in the Yemen conflict – Carter and his national security adviser, Zbigniew Brzezinski, decided to build a ‘Rapid Deployment Joint Task Force’, or RDJTF (Long 1985: 62). As they saw it, the lesson from Iran was that the United States should not count on local proxies, and must use its own forces to protect its own interests (Quandt 1979: 543). This fitted well with the broader strategic rethinking in Washington. According to Brzezinski (1983: 454), events and decisions in 1979–80 had fundamentally altered the U.S. global strategic position. The Middle East – which was previously seen as semi-neutral and protected from Soviet power by a defence belt comprising Turkey, Iran, Pakistan



and Afghanistan – no longer seemed invincible. As a consequence, U.S. dual commitments in Europe and the Far East were supplemented by a third strategic commitment toward what was now known as ‘West Asia’. The resources needed to support this new pledge, however, were unavailable, and so in order to bypass congressional objection, part of the military deployment was financed by Saudi petrodollars (Gold 1993: 51).

Thus, notwithstanding his desire to promote world peace, President Carter was subject to considerable pressures to act otherwise. At home, his was the first administration to raise domestic military spending after almost a decade of decline (Figure 5.3). On the international arena, Carter indeed announced a policy of restraints on arms exports, which, in its first 15 months, led to the cancellation of 614 requests from 92 countries, worth over \$1 billion (Ferrari et al. 1987: 25). Yet, despite these limitations, and contrary to the new statist stand on the principle of American ‘self-defence’, total U.S. arms exports continued to increase (albeit still slowly), particularly to the Middle East. Somewhat paradoxically, Carter, who was often perceived as a peacemaker and promoter of regional reconciliation, was also the president who contributed the most toward opening the Arab market to U.S. weaponry. In 1978, toward the Camp David Accord, he initiated the first ‘combination deal’, whereby U.S. armament producers *simultaneously* equipped several warring factions – a pattern which was then promptly institutionalised by other arms-exporting countries as a means of promoting peace through arms sales.<sup>16</sup>

### The 1979 Iranian Revolution and the 1980–88 Iran–Iraq War

#### *The Hostage Crisis*

Yet the ongoing rearmament during the mid-1970s was merely sufficient to keep oil prices from falling, and in the absence of a serious upheaval, the Petro-Core’s profitability in 1977 and 1978 again dropped into the ‘danger zone’, below the big-economy’s average (Figures 5.7 and 5.8). Fortunately for the Coalition, though, help was on the way, with turmoil again starting to build up. The Islamic Revolution which began in 1978 failed to have a significant effect on the oil market, although the potential was clearly there. In this light, the involvement of the U.S. Administration in the onset of the

16 Israel was compensated for its withdrawal from the Sinai peninsula with two new airfields in the Negev desert worth \$2.2 billion, and a ‘reorganisation’ package of 15 F-15 and 75 F-16 aircraft valued at \$1.9 billion. The Egyptians were allowed to purchase 50 F-5 fighter aircraft worth \$400 billion (with an option to buy more advanced ones later), and the Saudis bought another 60 F-15s worth \$2.5 billion (*Ha’aretz*, 3 April 1983). Cyrus Vance, who participated in the negotiations as Carter’s Secretary of State, was later nominated a director of General Dynamics, one of the deal’s principal winners.

1979 oil crisis is noteworthy. Despite the delicate situation in Iran, President Carter quickly granted asylum to the ousted Shah, thus triggering the hostage crisis. When Iran threatened to withdraw its U.S. banking deposits, the President immediately retaliated by seizing Iranian assets.

The background leading to the seizure was outlined by journalist Anthony Sampson (1981: Ch. 17; *Ha'aretz*, 2 January 1981). During the period from 1976 to 1978, Iran borrowed \$3.8 billion to finance arms purchases. On the eve of the Iranian Revolution, an outstanding debt of \$500 million was owed to a consortium headed by Chase Manhattan, which also held \$433 million in Iranian deposits. In theory, these deposits could have been withheld as a forced collateral, only that Chase had no legal right to do so – that is, unless instructed by the U.S. government for reasons of ‘national security’. And as it turns out, this is precisely what happened – although not without help from David Rockefeller, the bank’s chairman and one of its principal owners. Sampson reveals how Henry Kissinger, acting as a special adviser to Chase Manhattan at the time, and Jack McCloy, a former chairman of the bank, courted President Carter, who was himself closely associated with the Rockefellers through the Trilateral Commission, so that he granted asylum to the Shah despite the fragile political atmosphere. Kissinger later told Sampson that there was nothing subversive in these activities, arguing it was inconceivable that ‘a few private citizens’ could affect state policy. The Islamic government, in any event, was deeply offended. Turmoil ensued, and as the script unfolded, Tehran threatened to withdraw its U.S. deposits, to which Carter immediately retaliated by freezing them. The official justification was that the freeze was necessary to defend the integrity of the American banking system, although the real risk couldn’t be that serious. Iran had roughly \$8 billion dollars worth of deposits, but of these only \$1 billion were ‘call money’ available on demand – less than 1 per cent of the U.S. system’s outstanding cash balance. Moreover, most of these deposits were held in London, so even if drawn out, the only place for them to go was back into the Euro market. Clearly, the financial system as whole was not at threat. Certain institutions, however, particularly Chase and Citibank of the Rockefeller group, were vulnerable, and had much to gain by the freeze.

#### *The ‘Sting’*

The hostage crisis in Iran sparked panic, and the price of oil finally began to rise. Adding to the turmoil, the Soviet Union invaded Afghanistan in late 1979, and in 1980 the Iraqis attacked Iran. Oil prices were now climbing beyond \$35 per barrel, pulling the Petro-Core’s profitability safely out of the ‘danger zone’. And with Middle East oil revenues on the rise, the flow of imported weapons was also growing rapidly. To some extent, both the invasion of Afghanistan and Iraq’s assault on Iran were rooted in the rising threat of Islamic fundamentalism. Yet the U.S. government, although happy to see this threat being

checked, was not entirely antagonistic to the Khomeini regime. According to several sources analysed in Cockburn and Cockburn (1991: 317–18), during the last year of his administration, Carter embarked on a ‘sting operation’ which, if successful, would have both helped his re-election and caused Iran to renew its demand for American weapons. The underpinnings of his strategy were relatively straightforward. With much of their sophisticated arsenal made in the United States, the Iranians were crucially dependent on U.S. spare parts and ammunition. In this context, a major conflict, preferably starting before the 1980 elections, could convince Iran to release the embassy hostages in return for American military re-supply. The unsuspecting carrier of that plan was Iraq’s Saddam Hussein. With blessing from Jordan and Kuwait, promises of Saudi finances and, most importantly, a warm endorsement from Zbigniew Brzezinski, whose declared aim was to see Iran ‘punished from all sides’, Hussein swallowed the bait, and began advancing his forces into Iran (Cockburn and Cockburn 1991: 392). Unfortunately for Carter, the timing of the ‘sting’ was out of sync. Once Iraq launched its attack, his administration condemned it and began soliciting the Iranians to trade hostages for spare parts. But that was too late. Apparently, Iran already had a secret agreement with the U.S. Republican Party, according to which the hostages would be released only after the elections. And so although the weapons were ready to flow, Carter was no longer there to benefit from the deal.<sup>17</sup> For the Weapondollar–Petrodollar Coalition, of course, the deal was manna from heaven, regardless of who won the election – although naturally, it much preferred having Reagan on its side than Carter.

During Reagan’s presidency, the Middle East was defined – in some sense paradoxically – as being increasingly important for the U.S. ‘national interest’. In 1983, Reagan created a new military central command, or CENTCOM, to include the entire area of ‘West Asia’ from India to the Horn of Africa. CENTCOM’s mandate emphasised active defence over deterrence. Its capabilities, however, were very limited. It wasn’t able, for example, to counter a Soviet challenge against the oil zone in southern Iran, and certainly not to embark on a larger operation (Gold 1993: 69). Moreover, with funding being tight, the new focus on West Asia had to come at the expense of American military commitments in Europe and East Asia – this at a time when the significance to the U.S. of Middle East oil, as well as of the Soviet danger, were in fact *declining*, as we describe later in the chapter.

### *The Network*

While the importance of oil and Soviet power were apparently waning under Reagan, the political leverage of the Weapondollar–Petrodollar Coalition was

17 The allegations about a deal between Iran and the Reagan campaign headquarters were first made by Gary Sick and others (*New York Times*, 15 April 1991; Sick 1991).

soaring to new highs. Vice-President George Bush – a former Director of the CIA and an oil millionaire in his own right – had close acquaintance with the petroleum industry, and strong ties to ultra right-wing groups. As his first Secretary of State, the President nominated Alexander Haig, previously a director of Chase Manhattan and President and Chief Executive Officer of United Technology.<sup>18</sup> Reagan also nominated Donald Regan, a partner and chairman of Merrill Lynch, as his Treasury Secretary. Merrill Lynch, much like Chase Manhattan and United Technology, also had special links to the Middle East. In 1978, the company acquired White Weld, an international investment firm that advised the Saudi Arabian Monetary Agency (SAMA) on how to manage its \$100 billion portfolio and guided the investment of a daily inflow of about 450 million petrodollars. As his Assistant Secretary for International Affairs, Regan chose David Mulford, who until then was running White Weld's operations in Saudi Arabia (*Business Week*, 22 July 1985). Other oil-related appointments included the nomination of Paul Volker as chairman of the Federal Reserve Board, who was then succeeded by Alan Greenspan; the former was linked to the Rockefeller group, whereas the latter, besides being a groupie of Ayn Rand, was a director at both Mobil Oil and J.P. Morgan prior to his appointment.

However, the most important representatives of the Weapon-dollar–Petro-dollar Coalition who found their way into the Reagan Administration were the veterans of Bechtel Corporation, the world's largest contractor of military installations and energy-related projects.<sup>19</sup> Bechtel has had a long history of building political ties at home and abroad (cf. McCartney 1989). Among other things, the company was the driving force behind the election campaigns of Presidents Edgar Hoover, Dwight Eisenhower and Ronald Reagan; it had close associates in the CIA, including Agency Directors William Casey, Richard Helms and John McCone;<sup>20</sup> it courted special relations with the Dulles brothers; and it has dominated decision-making at the Atomic Energy

18 Earlier, Haig served as Nixon's Deputy Assistant for National Security Affairs, as well as the White House Chief of Staff, but his leverage was now much stronger. Shiff and Yaari (1984) allege that it was he who gave Israel's Defence Minister Sharon the 'green light' to invade Lebanon in 1982. United Technology, to which Haig later returned as a special consultant, exported helicopters and aircraft engines to the Middle East. Haig was able to persuade the Israeli government to install United Technology's engines in its proposed Lavi aircraft – although the IDF preferred the alternative engines made by General Electric. Eventually General Electric came out on top. While the Lavi got cancelled, the Israeli air force, with the help of hefty bribes to IDF Brigadier General Rami Dotan, decided to equip its F-16 fighters with GE engines.

19 During the 1980s, the Bechtel family owned about two-fifths of the company's shares, with the remainder spread among the firm's senior managers. The company had to be excluded from our statistical analysis due to lack of publicly available data.

20 Supplying arms and equipment to the U.S. army during the Second World War, John McCone and his partner Steven Bechtel Sr. managed to earn in only a few years over \$100 million on an investment of less than \$400,000; certainly a remarkable achievement, even by the loose standards of war profiteering (McCartney 1989: 70).

Commission and the Export-Import Bank. On the international scene, Bechtel acted simultaneously as an arm of the CIA, as well as the unofficial representative of foreign governments, particularly Saudi Arabia, in the United States. These and numerous other connections, often supplemented by substantial bribes and clandestine operations, helped win Bechtel some of the world's largest construction projects.<sup>21</sup> But what made these projects so valuable to begin with was the unfolding 'energy crisis' since the early 1970s.

Bechtel entered the Middle East after the Second World War as a major contractor for the ARAMCO partners, but until the consolidation of OPEC its activities in the region were relatively limited. It was only with the oil price explosion of the early 1970s, that the contracts began piling up. Among others, these included the construction of natural gas projects in Algeria and Abu Dhabi, power stations in Cairo, and refineries, airports and entire petrochemical cities in Saudi Arabia. In addition, many of the company's other energy-related projects – such as Quebec's hydroelectric James Bay complex, the Alaska oil pipeline, Indonesia's liquefied natural gas facilities, and nuclear reactor plants in the United States and elsewhere – were themselves partly the consequence of rising oil prices. The company also became a major constructor of military installations – mainly for U.S. forces, but also for other sovereigns, particularly in cash-rich Arab countries.

By the early 1980s, Bechtel's international operations had risen to over one-half of its business, and the person who guided this transition since the mid-1970s was the company's president, George Shultz. Toward the 1980 election, Shultz grew worried about candidate Ronald Reagan, whose fixation on *laissez faire* and small government threatened Bechtel's lifeline. However, after a series of re-educational meetings with Bechtel executives and associates of the Rockefeller group, the presidential hopeful came back to his senses, at least enough to make Shultz an avid supporter. Once in office, Reagan began drawing on the talent of Bechtel officials. As his initial Defense Secretary he chose Casper Weinberger, who until then was a Bechtel vice-president, and in 1982, he asked Shultz to replace Haig as Secretary of State. Other Bechtel veterans with key positions in the new administration included, National Security Adviser Richard Allen; Deputy Secretary of Energy Kenneth Davis; and Philip Habib, whom Reagan sent as his Special Envoy to the Middle East while still on Bechtel's payroll.

The convergence of oil and armament interests in the Reagan Administration was paralleled to some extent in their own corporate boardrooms, mainly through interlocking directorships which provide an informal setting for exchanging ideas and coordinating collective action. For example, during the 1980s, the chairman and chief executive officer of Standard Oil of Indiana

21 Perhaps the largest bribe was the \$200 million paid to Saudi officials in return for the \$3.4 billion contract to build the new airport in Riyadh. The earliest covert operation involved the Syrian coup of 1949, after the Syrian government raised obstacles to the construction by Bechtel of a Saudi-Syrian pipeline.

(Swearingen) was a director of both Chase Manhattan and Lockheed; the board of directors of McDonnell Douglas included a director of Phillips Petroleum (Chetkovich) and a director of Shell Canada (McDonald); the chairman and president of United Technologies (Gray) was a director of both Exxon and Citibank; Boeing shared one director with Mobil and three with Chevron, including the latter's chairman (Keller); and the Chevron board included a director from Allied Signal (Hills), as well as the president and chief executive of Hewlett Packard (Yound) (based on Moody's Annual; Adams 1982).

### *Nourishing the Conflict*

Whether the oil and armament companies indeed colluded to advance their common interests remains an open question, but the policies of the Reagan Administration certainly worked on their behalf. At home, Reagan helped consolidate the Weapon-dollar–Petro-dollar Coalition by embarking on the largest defence build-up in peacetime, while simultaneously reducing corporate taxes. The obvious result was a rapidly rising budget deficit, which horrified the economists but delighted the arms contractors and oil companies.<sup>22</sup> And in the Middle East, the new Administration continued the policies of its predecessors, though apparently with much greater vigour. Whereas for Carter arms exports were an 'exceptional foreign policy implement', Reagan took the view that they were 'an essential element of [U.S.] global defense posture and an indispensable component of its foreign policy', moving to eliminate many of their previously imposed restrictions (U.S. Congress 1991: 20). Of course, in order to enable buyers to pay for the outgoing weapons, Middle East 'energy conflicts' had to be continuously nourished, a task to which the new Administration turned with little delay.

Building on their earlier success, Washington and Tehran were now trading regularly in exotic commodities. The United States secretly supplied weapons to the Ayatollah Khomeini, for which the latter paid with released hostages held by Iranian-backed forces in Lebanon, plus hard cash which the Americans then used to finance the Contra rebels in Nicaragua. The elaborate scheme, popularly known as the 'Iran-Contra Affair', was conceived and approved at the highest echelons, including President Reagan, Vice-President Bush, Secretary of State Shultz, Secretary of Defense Weinberger, CIA Director William Casey, and National Security Advisers Robert McFarlane and John Poindexter (*New York Times*, 19 January 1994). The purpose of the scheme, though, involved more than hostages and rebels. Its other goal, less publicised though certainly

22 The petroleum sector was a double winner under Reagan. Whereas over the 1960–80 period its effective tax rate rose from 11 to 29 per cent on an average annual profit of less than \$7 billion, during the next five years earnings rose to \$27 billion annually, while effective taxation dropped to 18 per cent (computed from the U.S. Department of Commerce through McGraw-Hill Online).

no less important, was to enable Iran to hold out against Iraq – but just barely, so that the war could continue for as long as possible. According to retired IDF general Avraham Tamir, Defense Secretary Haig explained to his Israeli counterpart Sharon that ‘it was U.S. policy to prevent either side from winning’ (Cockburn and Cockburn 1991: 328). And indeed, as journalists Waas and Unger describe in their colourful language, the Administration “tilted” back and forth between support for Iran and support for Iraq, sometimes helping both countries simultaneously, sometimes covertly arming one side as a corrective to unanticipated consequences of having helped the other’ (1992: 65). Arms shipments to sustain the Iranian war effort – ranging from \$500 million to \$1 billion annually, depending on the source – were handled by Israel. At the same time, the Americans also kept promoting the Iraqi cause. This was done in a variety of ways: by renewing diplomatic relations; by providing military intelligence; by granting low-interest loans; by encouraging Saudi financial assistance; by asking the Gulf states and Egypt to deliver more than \$1.5 billion worth of arms and ammunition; and, finally, by allowing over \$5 billion of U.S. credit – partly guaranteed by the Agriculture Department – to be covertly (and possibly fraudulently) used for Iraqi purchases of U.S. machinery and technology with military and nuclear applications (*Business Week*, 13 July 1992; Waas and Unger 1992). To facilitate payments for the war effort, it was suggested in 1984 that Bechtel construct a multibillion dollar pipeline from Kirkuk to the Jordanian port of Aqaba, so that Iraqi oil exports could bypass the hazards of the Gulf. The undertaking was endorsed by CIA Director William Casey, but apparently that wasn’t enough. The main risk was Israel, whose war planes could have easily blown the project out of operation. And so Bechtel lined up an impressive battery of friends, including Swiss oil magnate Bruce Rappoport, U.S. Attorney General Edwin Meese, and National Security Adviser Robert McFarlane, whose role was to make sure such an attack wouldn’t happen. Rappoport, with his reputed CIA connections and long-term friendship with Israeli Prime Minister Shimon Peres, managed to obtain a written promise, signed by Peres, that Israel wouldn’t mess with the pipeline; this in return for an overall premium of about \$650 million, payable in ten equal annual instalments, which would then be partly diverted to Peres’ Labour Party. To further secure the arrangement, Peres was willing to freeze in a ‘salvage fund’ \$400 million out of the U.S. military aid to Israel, and Meese and McFarlane laboured to arrange that the scheme be approved by the Overseas Private Investment Corporation (*Business Week*, 22 February 1988; Frenkel 1991: 30–4).

#### *The Oil-Arms Bust*

The project, however, never took off, perhaps because the flows of petrodollars and weapondollars were themselves beginning to recede. In 1980, the volume of Middle East oil production started to decline, and in 1982 prices followed suit.

The combined result was a steep drop in the region's oil revenues – from \$197 billion in 1980 to a mere \$52 billion by 1986, according to UN data. And given the intimate link from oil exports to arms imports, the consequences for the weapon makers were dire. 'We're all down now to nibbling crumbs', professed a frustrated U.S. defence executive during the 1985 Paris air show: 'The damn oil boom has gone and there is not much money around any more' (cited in Ferrari et al. 1987: 4–5). As of themselves, these developments are not entirely surprising. First, high oil prices induced greater energy efficiency, substitution to alternative sources, and further exploration and output by non-OPEC producers. Second, diversification by Saudi Arabia and Kuwait into downstream operations brought them into conflict with the companies. And finally, the Iran–Iraq War, previously a major source of 'risk' and 'scarcity', was no longer viewed as a threat for Western oil supplies.

Indeed, in this sense, the situation during the early 1980s differed from the one prevailing after the 1973 Arab–Israeli War. In the earlier conflict, the anti-Israel alliance of the Arab countries lent credibility to their 'oil weapon' and the threat of future shortages. By the 1980s, however, the OPEC front was no longer united and two important members of the cartel were themselves military foes. The disturbances occurring in the Persian Gulf, particularly the so-called 'tanker war' and attacks on oil installations, made the oil market nervous and perhaps exerted a positive influence on prices. Yet rivalry prevailed instead of cooperation, and with no end in sight to the hostilities, the likelihood of restoring OPEC's earlier cohesion seemed remote. In this respect, the overriding need of both Iran and Iraq for new weapons and ammunition only made things worse, since it forced both to stretch production to the limit, creating a gushing flow of 'distress oil'.<sup>23</sup> And so, from a certain point onward, the Iran–Iraq War turned from a blessing to a curse. Instead of boosting prices, it now caused them to *fall*, creating a rather taxing environment for both OPEC and the Weapondollar–Petrodollar Coalition.

Given the gravity of the situation, Saudi Arabia agreed to provide a 'cushion' for OPEC's other members, selling its oil at the cartel's official price and absorbing the demand shortfall. The cost, though, mounted quickly. The kingdom had to reduce its output from 9.8 million barrels a day in 1981, to 6.5 million in 1982 and, finally, to a mere 3.2 million in 1985, but even that failed to stabilise spot prices (OPEC Annual). Eventually, the Saudis bailed out, and as their production rose, panic ensued and the price collapsed even further.

In 1986, with the price of crude oil heading below \$10 a barrel for the first time since 1973, the Petro-Core's rate of return once again dropped below the

23 Spending on the war was partly financed by foreign assistance, with Khomeini supported by both Syria and Libya, and Iraq allegedly receiving \$30–60 billion in cash and replacement oil from Saudi Arabia and other Gulf states (*Business Week*, 4 June 1985; Stockholm International Peace Research Institute 1987: 303). This aid, however, was hardly sufficient for the task at hand, leaving the two countries no choice but to prime the pump.



big economy's average (Figures 5.7 and 5.8). And as the Middle East found itself entering a new 'danger zone', Vice-President Bush found himself on a mission to Riyadh, with the task of *openly* asking the Saudis to reconsider their actions and reinstate lower levels of production. Bush insisted that the government of the United States was 'fundamentally, irrevocably committed' to maintaining the free flow of oil, and that 'the interest in the United States is bound to be cheap energy prices'. However, the Vice-President also emphasised that '[there] is some point at which the national security interests of the United States say, "Hey, we must have a strong, viable domestic interest"' (*New York Times*, 7 April 1986).

The other reason for the Administration's concern for oil was the armament market. Defence procurement at home started to level off after having soared for a decade. And yet, military shipments to the Middle East, which could have partly compensated for the shortfall, were now drying up for lack of petrodollars. Worse still, as Table 5.3 shows, competitors from other countries were now winning market share from American companies. In contrast to the period until the late 1970s, when the market was more or less under the thumb of the two superpowers, since the early 1980s suppliers from Europe and the developing world were making significant headway. By the end of the 1980s, these contenders saw their combined market share rise to more than 50 per cent, double its level a decade earlier; the share of U.S. suppliers, on the other hand, dropped to 18 per cent, down from 48 per cent.<sup>24</sup> A large part of this decline was due to the fact that U.S. arms shipments, despite considerable deregulation under Reagan, were still partly subjugated to 'foreign policy' considerations, whereas in other countries they were by now completely commercialised. And so, with the Iranian market having been lost to scandal, and with sales to Iraq forbidden by government decree, U.S.-based firms could only watch and see their competitors stepping in to fill the void. The lost opportunity was immense. The Iran–Iraq War, which dragged on for much of the 1980s, turned out to be the most expensive conflict since Vietnam, with the belligerent countries spending over \$400 billion to fight each other. And yet, save for covert shipments, the profits from this gold mine were going not to U.S. firms, but to their rivals.<sup>25</sup>

24 During the 1990s, U.S. producers recovered the lost ground, although according to realist thinking they should have done far better. Indeed, with their country being the world's sole hegemon now that the Soviet Union was no more, what was to prevent them from kicking their competitors completely out of the picture? But then, the question itself is misguided. By now, U.S., European and Japanese contractors have grown increasingly intertwined through complicated supply chains and transnational cross-ownership, so that their 'state' allegiance was not always obvious. Also, and as we shall see at the end of the chapter, the U.S. 'national interest' was itself starting to shift from weaponry to other business, making competition over Middle East arms contracts seem less important.

25 Some estimates suggest that Iraq imported about \$40 billion worth of arms during the period from 1980 to 1986, while Iran's foreign purchases amounted to \$30 billion. The overall stake of covert U.S. shipments in these totals must have been limited. The prime suppliers for the war were based in France, the United Kingdom,

Table 5.3 Arms Exports to the Middle East

| Period  | Total<br>(\$ million) | Supplier (per cent of total) <sup>(a)</sup> |                                    |        |
|---------|-----------------------|---|------------------------------------|--------|
|         |                       | United States                               | Soviet Union/Russia <sup>(b)</sup> | Others |
| 1964–73 | 9,447                 | 34.4 <sup>(c)</sup>                         | 50.2                               | 15.4   |
| 1974–78 | 29,000                | 47.6  | 25.9                               | 26.6   |
| 1979–83 | 65,355                | 21.7  | 31.2                               | 47.0   |
| 1984–88 | 89,065                | 18.3  | 29.9                               | 51.8   |
| 1989–93 | 83,600                | 38.3  | 11.4                               | 51.4   |
| 1994–97 | 67,300                | 47.1  | 3.9                                | 49.0   |

(a) Totals may not sum up to 100 per cent because of rounding.

(b) Russia from 1992 onward.

(c) Data for the United States are for fiscal years. Total does not include the re-supply effort to Israel following the 1973 Arab–Israeli War.

SOURCE: U.S. Arms Control and Disarmament Agency (1975 Edition, p. 70; 1980 Edition, p. 160; 1985 Edition, p. 134; 1998 Edition, p. 174); U.S. Department of Commerce, Bureau of Economic Analysis, *Statistical Abstract of the United States*, 1991, Table 550, p. 340.

### The 1990–91 Gulf War

With so much at stake, it was once again time for the U.S. Administration to hype the Persian Gulf as a ‘vital national interest’. In a speech given in 1987, Secretary of Defense Weinberger reminded his audience that the Middle East still contained 70 per cent of the world’s proven reserves. The role of the United States, he said, was to assure the region was secure, stable and, above all, free from Soviet influence and intervention. According to Weinberger’s strict guidelines, the American military was practically prevented from intervening in any conflict short of a world war. The only exception was the Middle East, where direct military intrusion was deemed warranted (Gold 1993: 76). From a realist perspective, though, this new emphasis sounded a bit odd. Indeed, according to the analysis laid out in Gold (1993: 75), during Reagan’s second term in office the region had become strategically *less* important to the U.S. ‘national interest’. For one, the Soviet Union, locked into a losing war of attrition in Afghanistan, was no longer perceived as marching toward the Strait of Hormuz. Furthermore, although the Middle East still contained much of the world’s reserves, the expansion of non-OPEC output, greater conservation, and

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West Germany, Italy, South Africa, the Soviet Union, China, North and South Korea, Vietnam, Israel, Taiwan and Brazil (*Business Week*, 29 December 1986; for a full list of the 52 known participating countries, see Stockholm International Peace Research Institute 1987: Table 7.8, pp. 204–5). According to *Jane’s Defence Weekly*, Iraq even supplied Iran, reselling to the latter through private dealers heavy weapons previously captured in the fighting (reported in Stockholm International Peace Research Institute 1987: 307). For detailed accounts of the arming of Iraq during and after the Iran–Iraq War, see Darwish and Alexander (1991: Chs 4–6) and Timmerman (1991).

new energy-saving technologies, have together made this oil less important than before. And, finally, the experience of the Iran–Iraq War suggested that regional conflicts could go on with oil supplies remaining cheap and plentiful. But then, these very developments, which from the viewpoint of the U.S. ‘national interest’ were supposedly all good, spelled serious trouble for the Weapondollar–Petrodollar Coalition. And so the escalation began.

### *Warming Up*

Attempts to bolster U.S. military presence in the region began in 1984, when Washington tried to persuade the Persian Gulf emirates to allow the installation of American bases on their soil. The latter refused, but in 1986, when an Iraqi Mirage fighter hit an American frigate, Washington responded by sending aircraft carriers into the region. The Iranians retaliated by littering the Gulf with naval mines, to which the United States answered with mine sweepers. And, so, in 1986, when Vice-President Bush was on his mission to Saudi Arabia in an effort to raise oil prices by peaceful means, the U.S. military was already well on its way toward direct involvement in the region, a trajectory which would four years later culminate in Operation Desert Storm.

The first direct target was Libya’s ruler, Muammar Qaddafi, who was increasingly blamed for fostering international terrorism. A Sixth Fleet armada of more than 45 warships, including three aircraft carriers with over 200 planes, was dispatched in March 1986 toward the renegade state. The official reason was to ‘enforce the principle of freedom of the seas’ against Qaddafi’s unwarranted extension of Libya’s territorial waters to the 32nd parallel. But as U.S. administration officials later acknowledged, the real purpose of the operation, code-named Prairie Fire, was rather different. The plan was to provoke a military response by Libya, against which U.S. forces would retaliate with escalating counter-strikes, including the destruction of the Libyan air force and bombing raids on the country’s oil fields. Qaddafi, however, failed to pick up the bait and did not respond in any meaningful way (*Montreal Gazette*, 29 March 1986; *Time*, 7 April 1986). A new opportunity arose a month later, after a terrorist attack on a West Berlin discotheque ended with numerous injuries and one dead American soldier. The blame for the attack was immediately put on Libya and the fleet was sent once again toward Qaddafi’s ‘line of death’. But the Libyan ruler, to whom Reagan referred as the ‘mad dog of the Middle East’, held his fire and the military exchange was limited (*Time*, 21 April 1986). Incidentally, the Syrians, who were also blamed for being involved in the West German bombing, came out against ‘U.S. aggression’ in Libya, and there were increasing reports about heightening Israeli–Syrian tensions (*Time*, 26 May 1986). The attempted escalation continued, when in August, information leaked by the Administration to the *Wall Street Journal* suggested that the United States and Libya were again ‘on a collision course’ (*Time*, 13 October 1986).

This policy of confrontation was presented as part of a new, stronger U.S. stand against radical Middle East regimes. In 1987, however, Reagan abruptly abandoned the Libyan cause, shifting his focus back to the Persian Gulf. The official reason was again the Soviets. The ‘tanker war’ in the Gulf, which since 1980 had already accounted for over 300 damaged oil vessels, was suddenly made into a top priority after the Kuwaitis requested U.S. protection for their tankers. Initially, the Administration appeared reluctant, but then quickly reversed its stance once the Kuwaitis turned to the Kremlin (Gold 1993: 79–104; Darwish and Alexander 1991: 244–5). The real story, however, was more complicated. Since the beginning of 1986, the Administration was voicing open concerns that Iran was getting the upper hand in its six-year war with Iraq. But, then, in November of that year, the Iran–Contra Affair began to unravel, suggesting that part of the credit for Iran’s success must go to the U.S. Administration itself. Revelations that Reagan was both condemning and supplying Tehran forced Washington to reiterate its anti-Khomeini stance, and the Kuwaiti request provided the right pretext. The Seventh Fleet assumed the role of protecting Kuwaiti tankers, and before long found itself attacking Iranian oil installations and exchanging fire with Iranian forces.

The intensified conflict and growing U.S. involvement drew the more moderate Gulf states deeper into the militarisation process. Countries such as Saudi Arabia, Kuwait, Oman and the United Arab Emirates were now looking to buy more U.S.-made weapons, which the White House was only too happy to supply.<sup>26</sup> The Congress, though, being far less forthcoming than the Administration, managed to block several large deals, forcing the Gulf states to look for alternative sources.<sup>27</sup> The biggest setback for the U.S. companies was the 1988 ‘deal of the century’, in which the United Kingdom agreed to supply Saudi Arabia with \$25 billion worth of military hardware, construction and technical support over the next two decades (*Business Week*, 12 September 1988). The end of the Iran–Iraq War in 1988 opened new business opportunities for companies which could help rebuild the war-shattered infrastructures of the two countries. The scope of the work was substantial – estimated at the time in excess of \$200 billion – but then here too U.S. corporations found themselves facing stiff competition from non-U.S. rivals (*Business Week*, 29 August 1988).

26 In 1988, the Administration suggested increasing U.S. arms exports by \$3.3 billion, to a level exceeding \$15 billion – with proposed shipments worth \$3.6 billion to Israel, \$2.7 billion to Egypt, \$950 million to Saudi Arabia, and \$1.3 billion to other Middle Eastern countries (*New York Times*, 2 May 1988). This proposal did not prevent Secretary of State Shultz from declaring in front of the U.N. General Assembly only a few weeks later that ‘developing countries must help reduce the international tension and ease the arms race’ (*New York Times*, 14 May 1988).

27 In 1985, the Congress refused to approve the sale to Saudi Arabia of 40 advanced McDonnell Douglas F-15 aircraft and, in 1986, blocked the sale of 800 General Dynamics Stinger missiles. In 1988, the U.S. Senate voted to deny a Kuwaiti request for Hughes (GM) Maverick missiles and also forbade the sale of Stinger missiles to Oman (*New York Times*, 13 May 1988; *Time*, 25 July 1988).

*'Danger Zone'*

The Bush presidency, which began in 1989, provided continuity for the Weapondollar–Petrodollar Coalition in Washington. Some of the Coalition's representatives were by now gone, but their successors were in most cases equally aware of the oil and armament interests at stake. These included, in addition to oil millionaire George Bush, people such as Nicolas Brady, who previously ran Dillon, Read & Company when it was controlled by Bechtel, and who was now nominated Treasury Secretary; Robert Mosbacher, an oil businessman who now became Secretary of Commerce; and James Baker, a lawyer with deep ties to the oil business, who previously served under Ford and Reagan, and was now made Secretary of State (during the 1990s, Mosbacher and Baker returned to the private sector as special consultants to the energy giant Enron). Bush also wanted John Tower to become Secretary of Defense, but the former senator, who acted as retainer for five defence contractors, failed the conformation hearings. Eventually, the post went to Richard Cheney, a strong supporter of 'Star Wars' and the Contra rebels, who would later become Vice President under George Bush's son.

The Middle East situation, however, remained precarious for the Coalition. Despite the Administration's loyalty and its greater military involvement in the region, the price of oil did not recover significantly, the Petro-Core's rate of return was still in the 'danger zone', and demand for foreign weapons was stuck in the doldrums. The gravity of the situation was succinctly summarised in February 1990 by the head of CENTCOM, General Norman Schwarzkopf. Appearing in front of the Senate Armed-Forces Committee, Schwarzkopf, whose father had previously set up the dreaded Iranian SAVAK, explained the crucial and growing significance of Middle East oil. The region, he warned his audience, had 13 ongoing conflicts, and if any one of them were to develop into a full-fledged war, the consequences for the West could be dire. Despite this danger, though, he strongly recommended that the United States increase its military exports to the region in order to match disturbing advances made by foreign competitors. On the day of Schwarzkopf's speech, a 'prime Pentagon source' suggested to the *Wall Street Journal* that the Administration, now that the East–West conflict was over, should divert funds from defending Europe to protecting Saudi Arabia (cited in Frenkel 1991: 9–13). The background for these pressures was succinctly summarised two months later by an unnamed Pentagon official:

No one knows what to do over here. The [Soviet] threat has melted down on us, and what else do we have? The navy's been going to the Hill to talk about the threat of the Indian navy in the Indian Ocean. Some people are talking about the threat of the Colombian drug cartels. But we can't keep a \$300

billion budget afloat on that stuff. There is only one place that will do us as a threat: Iraq. (cited in Cockburn and Cockburn 1991: 354–5).

And, indeed, a month later Saddam Hussein finally made his move, beginning to threaten his Gulf neighbours with the dire consequences of their oil policies.

After the end of the Iran–Iraq War, Hussein found himself between a rock and a hard place. His country was devastated, overburdened by \$80 billion in foreign debt, and deprived of petrodollars. In order to rebuild his economy and army, he demanded that the Gulf states, which in his view benefited from Iraq fighting the fundamentalist threat for them, should now foot up the bill, forgiving their Iraqi loans and providing him with even more funds (Darwish and Alexander 1991: Chs 9–11). In parallel, he also insisted that OPEC should get its act together by reducing output and raising prices. Needless to say, neither policy sat well with his neighbours. First, they had no desire to help re-fortify Iraq only to see its claws eventually turned against them (Darwish and Alexander 1991: 256–65; Frenkel 1991: 15–18). And, second, some of the Gulf states, particularly Saudi Arabia and Kuwait, were by now sufficiently diversified into downstream operations to benefit from more moderate prices (*Business Week*, 3 July 1988, 21 January 1991). Seeing that the differences could not be settled peacefully, Hussein eventually decided to take Kuwait over. On paper at least, this would have helped him kill two birds with one stone – enlarging his own fiefdom while simultaneously limiting overproduction by ‘merger’. The only problem was that there was a much bigger picture to consider, and here Hussein’s calculations proved fatally wrong.

By July, with the build-up of Iraqi forces along the Kuwaiti border becoming all too evident, the United States deployed several combat ships on joint manoeuvres with the United Arab Emirates. But except for these drills its message to Iraq was ambiguous and, at times, even encouraging. To learn more on the American position, Hussein summoned the U.S. ambassador, April Glaspie. In the interview which was held on 25 July, a week before the invasion, Hussein explained his grievances against Kuwait, noting quite explicitly that Iraq intended to ‘take one by one’ its disregarded rights. Glaspie replied that the dispute was an internal Arab matter on which the United States had ‘no position’, and that she had a ‘direct instruction from the President to seek better relations with Iraq’. When Hussein mentioned his demand that OPEC push the price of oil over \$25 per barrel, Glaspie chose to respond that there were also many Americans who would like to see the price go above that level. On 28 July, Bush reportedly sent a message to Hussein that the use of force against Kuwait was unacceptable, but three days later his Under-Secretary of State Kelly said to reporters that the United States had ‘no defence treaties with any Gulf countries’. On 1 August, despite the CIA’s conclusion that an Iraqi attack was imminent, the United States still failed to voice any explicit warning (Darwish and Alexander 1991: 267–75).

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The American stance changed drastically, however, once the Iraqis began crossing the Kuwaiti border on 2 August. Three days after the invasion, Defense Secretary Cheney and General Schwarzkopf convinced the Saudi royal family that their kingdom was Hussein's next target – a most implausible presumption by all counts as U.S. officials later admitted – persuading them to invite the deployment of 'infidel' forces on their land, something which until then the Saudis always managed to avoid (Woodward 1991: Ch. 19). During the following months, Hussein apparently attempted to seek a face-saving diplomatic solution, but to no avail. For the Americans, the opportunities offered by open confrontation were simply too great to give up.

And, indeed, the consequences of the war were highly beneficial for the Weapondollar–Petrodollar Coalition. The initial rise in the price of crude oil – from around \$14 per barrel in 1990 to near \$40 just before the onset of Operation Desert Storm – helped pull the Petro-Core's profitability above the big economy's average (see Figures 5.7 and 5.8). In 1991, the price per barrel declined to an average of \$22 (which, incidentally, was not much below what Hussein demanded on the eve of his invasion), but that was still sufficient to keep the Petro-Core out of the 'danger zone'.<sup>28</sup> The price revival raised Middle East oil revenues, and although their level was still far below that of the early 1980s, the anxiety created by the war, particularly in Saudi Arabia and the adjacent sheikdoms, caused them to nervously convert more of their petrodollars into weapondollars.

And this time, the main beneficiaries were U.S. firms, whose exports to the region in the two years following the war jumped by 45 per cent, according to the U.S. Department of Commerce. Part of the increase was in the export of civilian goods and services, mainly to Kuwait. During its short occupation, the Iraqi army engaged in systematic plunder, stealing according to some estimates \$20–50 billion worth of Kuwaiti property. In addition, it also left behind war damages whose repair cost was projected at \$100 billion. Perhaps not surprisingly, some of the largest reconstruction contracts went to Bechtel, beginning with a \$1 billion task of extinguishing the 650 oil fires ignited by the retreating Iraqi army, and continuing with the multibillion-dollar job of restoring oil production, repairing refineries and rebuilding damaged infrastructure (*Business Week*, 18 February 1991, 6 March 1991, 11 March 1991, 17 February 1992; *Fortune*, 25 March 1991). Most of the export increase, however, was in the category of military goods and services, which rose dramatically to reinstate the United States once again as the region's prime supplier (see Table 5.3).

28 Many oil executives actually felt relieved by the more moderate prices, which were high enough for differential profitability but not for 'conspiracy theory'. Just to be on the safe side, though, some oil companies decided during the last quarter of 1990 to write off part of their higher profits against the cost of 'future environmental regulations' (*Business Week*, 11 February 1991).

On 6 March 1991, while addressing a joint session of Congress after the Iraqi surrender, George Bush exclaimed that ‘it would be tragic if the nations of the Middle East and Persian Gulf were now, in the wake of the war, to embark on a new arms race’ (*New York Times*, 7 March 1991). Then, on 30 May, he went further, calling the major arms-exporting countries to establish guidelines ‘for restraints on destabilizing transfers of conventional arms’ to the Middle East (*New York Times*, 30 March 1991). In parallel, however, the President also insisted it was ‘time to put an end to micro-management of foreign and security assistance programs, micro-management that humiliates our friends and allies and hamstring our diplomacy’ (*New York Times*, 7 March 1991). To help erase some of the traces of such ‘micro-management’, in which both he and Ronald Reagan were explicitly implicated, Bush granted pardon in 1992 to six key figures in the Iran–Contra Affair, including a pre-emptive one to former Defense Secretary Casper Weinberger whose trial was just about to begin. Then, in line with the eternal principles of free enterprise, the Administration instructed American embassies to expand their assistance to U.S.-based military contractors, and even proposed to alter the 1968 Arms Exports Control Act, so that the Export-Import Bank could guarantee \$1 billion in loan-financing for U.S. arms exports (U.S. Congress 1991: 21; *New York Times* 18 March 1991).<sup>29</sup> True to the time-honoured strategy of ‘stabilisation through military exports’, Bush proposed in January of 1991, while the Gulf War was still going, that the United States sell Saudi Arabia over \$20 billion worth of armament – a deal so large that the Administration eventually had to ‘slice’ it into smaller pieces, for easier Congressional digestion (U.S. Congress 1991: 21).

And, so, by 1990, after a decade of losing ground to rival sellers, the United States, helped by falling exports from the former Soviet Union, was once more the largest weapon exporter to developing countries. The American comeback was especially pronounced in the Middle East – so much so that it prompted British officials to openly complain that the United States was ‘monopolizing’ the region’s arms trade (*The Independent*, 13 December 1992). The Gulf War also helped reinstate the primacy of petroleum companies vis-à-vis their host countries. The previous political arrangement, with OPEC in the spotlight and the oil in the background, no longer seemed to work. Despite the region’s militarisation, producing countries were increasingly acting at cross purposes, with Saudi Arabia, the companies’ principal ally, unable to bring them back into line. And so, here too the war helped put things back in order. The region’s most important suppliers – notably Saudi Arabia, Kuwait and surrounding sheikhdoms – were now signatories to defence treaties with the United States and

29 Government support was not limited to defence contracts, of course. For example, both President Bush and his Secretary of State Mosbacher did not hesitate to intervene personally on behalf of AT&T, when Saudi Arabia appeared to prefer European contractors for its \$8.1 billion plan to expand the kingdom’s telephone network (*Business Week*, 18 February 1991). The new Clinton Administration kept up the pressure and AT&T eventually won the contract.



Britain, which effectively subordinated their oil policies to U.S. dictates. Iraq was put out of circulation by UN sanctions, and with Iran still isolated, the risk of glut was significantly limited. On the surface, then, the Weapondollar–Petrodollar Coalition looked ready to roll. But in fact, this was to be its last victory, at least for the time being. After the Gulf War, the ‘danger zone’ opened up once more, with oil profits falling below the average. And yet, this time around there was no new energy conflict to pull these profits back up.

### **The Demise of the Weapondollar–Petrodollar Coalition**

#### *The New Breadth Order*

Compared with the 1970s and 1980s, the 1990s were far less hospitable to weapon dealers and oil profiteers. During the earlier period, dominant capital in the developed countries found itself well extended within its respective envelopes, its breadth potential being restricted by the post-war legacy of statism, by antitrust policies, and by capital controls. Given these barriers, differential accumulation concentrated mainly on stagflationary depth, whose main promulgators and principal beneficiaries were members of the Weapondollar–Petrodollar Coalition. But this constellation was inherently temporary. For most large firms, stagflation was a stopgap measure, to be abandoned once the pendulum swung back to breadth.

The basic conditions for renewed breadth were laid down in the late 1980s. Soviet economic liberalisation, the abandonment of import substitutions in much of the developing world, and the retreat of statism in the industrialised countries, worked to dismantle barriers on capital mobility and ease antitrust sentiments. And with controls falling apart, large firms were now more than eager to break their last, national ‘envelope’, moving toward integrated global ownership.<sup>30</sup> The differential prize was substantial. For the winners, gains from cross-border mergers and acquisitions, bolstered and replenished by green-field prospects in the developing countries, were far greater than the increasingly risky benefits from war profits and stagflationary redistribution. And as the world began shifting back to breadth, the symptoms of depth receded rapidly: world inflation fell to less than 5 per cent in 1999, down from over 30 per cent at the beginning of the decade; international hostilities were actively curtailed,

30 For instance, of the 599 regulatory changes recorded by the *World Investment Report* during the first half of the 1990s, 95 per cent were aimed at liberalising capital controls. Similarly, the number of bilateral investment treaties had risen to 1,330 by 1996, up from fewer than 400 in the early 1990s, with 88 per cent of the changes aimed at increased liberalisation and incentives for foreign investment (United Nations Conference on Trade and Development 1997: 18–19).

with the number of major conflicts falling to 25 in 1997, down from 36 in 1989; and military budgets the world over came under the axe, dropping by over one-third in real terms from their peak in the late 1980s.<sup>31</sup>

The Middle East, an epicentre for conflict and stagflation during the global depth phase, was greatly affected by this renewed breadth. The disintegration of the Soviet Union and the end of the Cold War robbed local wars of their international *raison d'être*. In parallel, the petrodollar boom, which earlier fuelled the region's military arsenals, turned into bust, making conflict difficult to sustain. The decline in oil prices and revenues also had dramatic domestic implications. Until the early 1980s, the oil bonanza helped local rulers tranquillise their domestic populations with a cocktail of large public spending and extensive internal security budgets. But with the peace blitz pulling the rug from under oil prices, the technique became expensive. According to World Bank data, GNP per capita in the Middle East and North Africa, measured in constant U.S. dollars, fell to 35 per cent of the world's average in 1998, down from 42 per cent in 1979, with the predicament being particularly severe in the Gulf countries, where per capita income, again measured in constant dollars, dropped by as much as 50–80 per cent. Starved of revenues, governments were forced to cut their budgets, and as spending declined, internal opposition, particularly from 'Islamic fundamentalism', intensified. The region's autocratic rulers were of course willing to fight such opposition nail and tooth, even with less resources. And yet, here too, global circumstances, particularly the ideological shift from statism to liberalism, put them on the defensive, weakening their self-confidence and compromising their resolve. And so, before long, many of them found themselves between a rock and a hard place. No longer awash with petrodollars, unable to pit one superpower against the other, and bogged down by domestic instability, their only way to survive was to accept U.S. protection. Those who refused, such as Libya and Iran, were doomed to isolation, whereas those opting for independent 'initiatives', such as Iraq with its invasion of Kuwait, risked severe punishment.

Israel, too, was caught largely off guard. Although its dominant capital was not directly dependent on oil, its domestic depth regime of militarised stagflation was intimately linked to the regional cycle of energy conflicts. Until the late 1980s, the local ruling class was still struggling to retain this regime, although its resolve, like that of other elites in the region, was severely weakened. The immediate reasons were the Palestinian *Intifada*, the collapse of the world market for arms exports, and increasing domestic macroeconomic instability, which, as we saw in Chapter 4, have together contributed to a massive differential accumulation crisis. The more fundamental reason, though, was the growing realisation that depth had come to an end. Global conditions

31 Data are calculated from International Monetary Fund (Annual), the Stockholm International Peace Research Institute (Annual), and the U.S. Arms Control and Disarmament Agency (Annual).

now required a new mechanism of accumulation, and possibly the restructuring of dominant capital itself.

The most important change in mechanism was a shift away from military conflict. On the surface, the transition seemed perplexing, even surreal. George Bush, a Weapondollar–Petrodollar loyalist, who only a few years earlier was busy promoting the Iran–Iraq conflict, and who had just completed a classic sting operation against Iraq, was now announcing in great fanfare the onset of a ‘new world order’ built on Middle East peace. Israeli and Arab leaders responded quickly, switching from bullets to business as if they had no animosity to overcome. And before the world could catch its breath, Prime Minister Rabin and Chairman Arafat were shaking hands on the White House lawn, celebrating the mutual recognition of their embattled nations.

The basic preconditions for this transition, though, were taking shape far from the troubled sands of the region, in the boardrooms of the world’s largest corporations. Much like during the earlier transition from breadth to depth, the current swing from depth back to breadth was also accompanied by a fundamental power shift *within* dominant capital. Whereas earlier, the transition strengthened the ‘angry elements’ of the Weapondollar–Petrodollar Coalition, this time, it was civilian business which took the lead.

#### *The Last Supper (Almost)*

The Weapondollar–Petrodollar Coalition of course didn’t give up easily. During the 1990s, it spent much time and effort trying to regroup and consolidate through corporate amalgamation, usually with full government backing. The consequence of this process was a massive centralisation in both the armament and oil sectors, culminating in the emergence of huge corporate ‘clusters’, illustrated in Table 5.4. In the armament sector, amalgamation was kick-started in 1993 when U.S. Defense Secretary Les Aspin invited the CEOs of the country’s leading contractors to their ‘Last Supper’. Military spending, he said, was poised for further declines, and with less orders to go around, the Clinton Administration wished to see its suppliers start merging. To speed up the process, the government relaxed its antitrust stance, and even reimbursed the merged firms for their amalgamation costs. It also declared that, when it came to military exports, foreign policy objectives would from now on take a back seat to profit considerations (Grant 1997). And so, over the next few years, the companies were busy buying each other out, until, in 2000, there emerged a clear pack of five leaders: Lockheed Martin (which now combined Lockheed, Martin Marietta, Loral, and much of the military lines of General Dynamics and General Electric); Boeing (which acquired McDonnell Douglas and Rockwell’s aerospace defence electronics); Raytheon (which added E-Systems and the military arms of Texas Instruments and Hughes); General Dynamics (which sold many of its original military lines only to buy others from Teledyne,

Table 5.4 The World's Largest Weaponry and Oil Companies, 1999 (with major acquisitions/mergers during the 1990s)

| Weaponry   |   |
|--|---|
| 1. <b>Lockheed Martin</b> ( <i>defence sales \$17.8bn, total sales \$25.5bn, net income \$382m</i> ) | 5. <b>General Dynamics</b> ( <i>defence sales \$8.9bn, total sales \$8.9bn, net income \$100m</i> ) |
| Lockheed   | General Dynamics  |
| General Dynamics Tactical Aircraft and Space Systems (1993-94)                                       | Teledyne Vehicle Systems (1996)   |
| Martin Marietta (1994)   | Lucent's Advanced Technology Systems (1997)   |
| Loral (1996)   | GTE Government Systems (1999)   |
| GE Aerospace (1997)  | Gulfstream (1999)   |
| 2. <b>Boeing</b> ( <i>defence sales \$16.3bn, total sales \$58bn, net income \$1.1bn</i> )           | 6. <b>EADS</b> ( <i>imputed defence sales \$6.1bn, total sales \$33.2bn, net income NA</i> )        |
| Boeing   | DASA (2000)   |
| Rockwell Aerospace and Defense Electronics (1996)  | Aerospaciale (2000)   |
| McDonnell Douglas (1997)   | Lagardère (2000)  |
| 3. <b>BAE Systems</b> ( <i>defence sales \$15.2bn, total sales \$19.4bn, net income \$491m</i> )     | Eurocopter (2000)   |
| BAE  | Dassault Aviation (45.8% joint venture with Dassault Industries, 2000)                              |
| Alenia Marconi (50% joint venture with Finmeccanica, 2000)   | Arianespace (22.6%, 2000)   |
| Saab (20% 2000)  | Airbus (80% joint venture with BAE, 2000)   |
| AES (2000)   | Matra BAE Dynamics (50% joint venture with BAE, 2000)   |
| Airbus (20% joint venture with EADS, 2000)   | Astrium (66% joint venture with BAE, 2000)  |
| Matra BAE Dynamics (50% joint venture with EADS, 2000)   | Eurofighter (44% joint venture with BAE and Finmeccanica, 2000)                                     |
| Astrium (34% joint venture with EADS, 2000)  | 7. <b>Northrop Grumman</b> ( <i>defence sales \$6.0bn, total sales \$9.0bn, net income \$467m</i> ) |
| Eurofighter (37% joint venture with EADS and Finmeccanica, 2000)                                     | Northrop  |
| 4. <b>Raytheon</b> ( <i>defence sales \$14.5bn, total sales \$19.8bn, net income \$404m</i> )        | LTV Aircraft (1992)   |
| Raytheon   | Grumman (1994)  |
| E-Systems (1995)   | Westinghouse Defense and Electronics (1996)   |
| Texas Instruments Defense Systems and Electronics (1997)   |   |
| Hughes (1997)  |   |
| Oil  |   |
| 1. <b>Exxon-Mobil</b> ( <i>sales \$163.9bn, net income \$7.9bn</i> )                                 | 4. <b>Total Fina Elf</b> ( <i>imputed sales \$82.9bn, net income \$3.9bn</i> )                      |
| Exxon  | Total   |
| Mobil (1998)   | Fina (1999)   |
| 2. <b>Royal-Dutch/Shell</b> ( <i>sales \$105.4bn, net income \$8.6bn</i> )                           | Elf Aquitaine (2000)  |
| Royal Dutch/Shell  | 5. <b>Sinopec</b> ( <i>sales \$41.9bn, net income \$448m</i> )                                      |
| Equilon (56% joint venture with Texaco, 1998)  | 6. <b>Texaco</b> ( <i>sales \$35.7bn, net income \$1.2bn</i> )                                      |
| Motiva (35% joint venture with Texaco and Saudi ARAMCO, 1998)  | Equilon (44% joint venture with Shell)  |
| 3. <b>BP-Amoco</b> ( <i>sales \$83.6bn, net income \$5.0bn</i> )                                     | Motiva (32.5% joint venture with Shell and Saudi ARAMCO)  |
| BP   | 7. <b>Eni</b> ( <i>sales \$34.1bn, net income \$3.1bn</i> )   |
| Amoco (1998)   | 8. <b>Chevron</b> ( <i>sales \$32.7bn, net income \$2.1bn</i> )                                     |
| Atlantic Richfield (2000)  |   |

SOURCE: Defense News (various issues); *Financial Times Survey of Aerospace*, 24 July 2000; *Fortune*; Moody's (Online); Charles Grant, 'A Survey of the Global Defence Industry', *The Economist*, 14 June 1997; newspaper clippings.

Lucent, GTE and Gulfstream); and Northrop Grumman (which combined Northrop and Grumman, along with the military lines of LTV and Westinghouse). Of the 16 companies which we used as a proxy for the Arma-Core, only 8 remained as independent contractors; the rest were either taken over or divested of defence holdings altogether.

And once centralisation had run its course in the U.S., the focus shifted to Europe, where in a matter of three years it gave rise to three Pan-European giants: BAE, EADS and Thomson. The European process was particularly noteworthy, since it involved cross-border amalgamation and significant privatisation in countries with strong statist traditions. The biggest amalgamate was created by UK-based British Aerospace (BAE), which took over Marconi from GEC plc., bought AES from U.S.-based Lockheed Martin, and acquired a minority stake in the Swedish-based Saab. In parallel, BAE also entered into various joint ventures with the newly formed European Aeronautic Defence and Space Company, or EADS. The latter conglomerate was created in 2000, by pooling together the various defence interests of DASA (formerly DaimlerChrysler Aerospace), France's Aerospaciale and Lagardère, and Spain's Ariespace. When EADS was formed, its largest shareholders were DaimlerChrysler, Lagardère, and the governments of France and Spain, but over 27 per cent of its stock were already publicly listed, with further privatisation to come. The third European giant, Thomson-CSF, was owned jointly by the French government, Alcatel, and Dassault Industries, with another one-third of the stocks trading freely on the market and additional privatisation in the pipeline.

The global oil sector went through similar centralisation. Unlike in defence, the process here was not openly promoted by governments, although few of the mergers faced any serious antitrust opposition. The major deals of the 1990s, listed in Table 5.4, included the acquisition of Mobil by Exxon to create Exxon-Mobil, of Amoco and Atlantic Richfield by BP, now named BP-Amoco, and of Fina and Elf Aquitaine by Total, now called Total Fina Elf.<sup>32</sup>

The differential financial consequences of these mergers were dramatic. The world's six largest oil firms listed in Table 5.4 had 1999 sales of \$513 billion, 25 per cent more than the six companies making the Petro-Core in its peak year of 1990; and \$27 billion in net profit, 24 per cent above the Petro-Core's record of 1980. In the armament sector the picture was more mixed. In 1999, the world's seven largest defence contractors listed in the table had \$84.4 billion in defence revenues, compared with \$61.3 billion for the 16 Arma-Core firms in their peak year of 1985. Their net profit, however, was only \$2.5 billion, compared with the Arma-Core's record of \$9.9 billion in 1989.

The problem for the large oil and armament companies here was that, by now, they controlled much of their universe, and that this universe was either

32 As these lines were written, Chevron and Texaco announced their intention to merge, a union which would create the world's fifth largest oil company in terms of sales.

growing slowly (as in the case of oil), or contracting (in the case of defence). Under these circumstances, internal breadth through amalgamation was inherently self-limiting, so that in this sense, government encouragement of greater centralisation merely pushed the Weapondollar–Petrodollar Coalition further toward its sectoral envelope. Beyond that point, continued differential accumulation for the Coalition depended on renewed conflict and stagflation boosting up overall profits. And yet, from the viewpoint of dominant capital *as a whole*, that route was unattractive, and in fact dangerous. By the early 1990s, civilian business offered much better ways to beat the average. Furthermore, the new civilian avenues required relative openness and stability, the very opposite of the conflict and stagflation with which the Weapondollar–Petrodollar Coalition fuelled the earlier depth regime.

The greater lure of civilian business is illustrated in Figure 5.9. The chart contrasts two series, each measuring the market capitalisation of a given corporate cluster, expressed as a share of the Standard & Poor's 500 (S&P 500), a widely used index for the largest firms listed in the United States.<sup>33</sup> The first series denotes the proportionate share of 26 leading aerospace and petroleum companies, a proxy for what earlier constituted the Weapondollar–Petrodollar Coalition. The second series, focusing on civilian business, measures the comparable share of 54 leading 'high-technology' companies. The focus on relative market capitalisation is indicative of how global investors view the *future* course of differential accumulation, and where profit growth is *expected* to be the fastest. From this perspective, the inverse movement of the two series points to a dramatic change occurring during the 1990s. Until the late 1980s, dominant capital was still under the fading eclipse of the Weapondollar–Petrodollar Coalition, with its representatives included in the chart accounting for close to 11 per cent of the S&P 500 total capitalisation. The 'high-technology' sector was relatively small, with less than 8 per cent of the total. Over the next decade, however, the situation has totally reversed. The armament and oil firms saw their relative share drop to about 5 per cent of the S&P 500, whereas that of the 'high-technology' companies soared to a peak of nearly 34 per cent. In 2000, 'high-technology' stocks collapsed, but even after the calamity, the sector's capitalisation was still three times larger than that of armament and oil combined. This picture is of course somewhat skewed by the much richer valuation of 'high-technology' companies, whose relative earning growth has so far lagged behind their differential capitalisation. Nonetheless, it seems evident that the Weapondollar–Petrodollar Coalition has lost its earlier primacy, and that the centre of gravity, at least for now, has shifted back to civilian business.

33 The index comprises leading companies listed on the New York Stock Exchange, American Stock Exchange and Nasdaq. Companies are usually leaders in their field and their contribution to the index are weighed by market value. In contrast to Fortune 500 companies whose 'home base' must be the United States, S&P 500 firms could be based anywhere, provided their shares are listed in the United States.

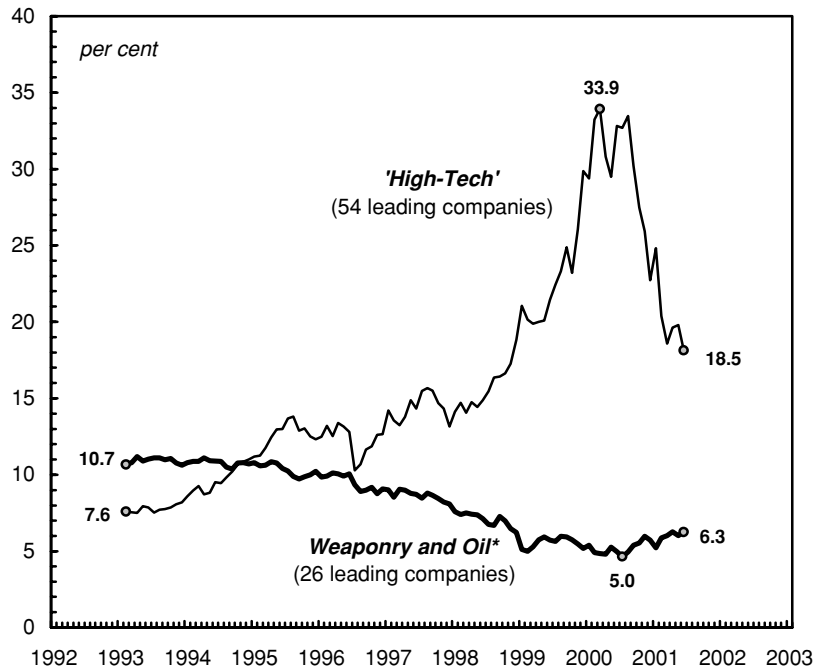


Figure 5.9 Share of Standard & Poor's 500 Market Capitalisation

\* Comprises 9 aerospace/defence companies, 11 domestic integrated oil companies and 6 international integrated oil companies.

SOURCE: McGraw-Hill (Online). DRI codes: SPAEROMV, SPOILDMV, SPOILIMV for Weaponry and Oil, SPHTECHMV for 'High-Tech'.

The fading power of the Weapondollar–Petrodollar Coalition was mirrored in the Middle East. During the 1990s, attempts to kick-start a new 'energy conflict' seemed to go nowhere. Every summer, tensions in the region would rise, sometimes pulling oil prices up with them, but never enough to build up momentum. During the early part of the decade, the main excuse were Iraqi ceasefire violations, to which the United States and Britain eagerly retaliated with aircraft and missile attacks. The situation again looked on the brink of war, when in September 1994, Washington announced that Saddam Hussein had dispatched an 80,000-strong force toward the Kuwaiti border, prompting President Clinton to send 60,000 soldiers and 600 aircraft back to the Gulf. But like Muammar Qaddafi before him, the Iraqi ruler preferred to ignore the 'smart' missiles and held his fire. Since then, numerous other enemies have appeared on the scene, from a nuclear Iran, to the Lebanese Shiites, to Islamic terrorism. And yet, despite the hyped rhetoric and ongoing hostilities – including the recent U.S.-led attack on Afghanistan – none of this has so far managed to significantly affect the price of oil.

The Gulf War was the Last Supper of the Weapondollar–Petrodollar Coalition, at least for the time being. During the 1990s, dominant capital as a whole was increasingly seeking cross-border expansion, a process which required tranquillity, not turmoil. Given that military conflict endangered such expansion, and that high energy prices threatened to choke the green-field potential of ‘emerging markets’, the Weapondollar–Petrodollar Coalition found itself increasingly isolated. And with depth giving way to breadth, it is perhaps not surprising that the ‘national interest’ itself was conveniently modified. As *Business Week* put it, ‘The President has recognised that, in the post-cold-war era, getting global contracts for U.S. business is a matter of national security’ (23 April 1994).

This neoliberal version of the national interest was eventually challenged by the 2001 attack on the Twin Towers and the Pentagon. Before turning to the present crossroad, however, we need to first travel through the transnational breadth phase of the 1990s.