THE CHALLENGE OF VENEZUELAN OIL

by Norman Gall

> Each year we, the countries which produce coffee, meat, tin, copper, iron or petroleum, have been handing over a larger amount of our products in order to obtain imports of machinery and other manufactured goods, and this has resulted in a constant and growing outflow of capital and an impoverishment of our countries. . . . To cite the particular case of Venezuela, petroleum prices showed a steady decline for many years, while our country was obliged to purchase goods from the United States at ever-higher prices, which, day after day, restricted even further the possibilities of development and well-being for Venezuelans. The establishment of the Organization of Petroleum Exporting Countries (OPEC) was a direct consequence of the developed countries' use of a policy of outrageously low prices for our raw materials as a weapon of economic oppression.
> —President Carlos Andrés Pérez of Venezuela, September 24, 1974.

With these words in an open letter to President Ford, published as a full-page advertisement in *The New York Times* last fall, the new President of America's leading foreign supplier of oil hurled a now familiar challenge to the United States. But the nation was not in the Middle East; the Israeli question was not remotely a consideration; and the nation in question, Venezuela, has traditionally been regarded by the U.S. and Latin-American Left as a strategically vital province of U.S. imperialism.

Within a few months, Venezuelans are expected to nationalize their oil industry. How successfully they do it—the exact details and the nature of the relationships which come into being after nationalization—may help decide the degree of future U.S. dependence on Middle East oil, the structure of the international petroleum industry, and the pros-

pects for democracy in Latin America.

For years, Venezuela has played an important role in the formation and growth of the oil cartel, OPEC. As an outsider, Venezuela was to play a leading role in unifying the squabbling states of the Middle East. Despite her backwardness in other respects, Venezuela had a far more sophisticated and progressive political leadership that the other states that formed OPEC.

A "Devilishly Difficult" Problem

It is one of the many ironies of the present oil panic that OPEC might never have come into being if the United States had protected Venezuela from the economic hardship resulting from the oil import quotas imposed by the Eisenhower Administration in 1959 to protect domestic producers and the oil majors against the flood of low-cost Middle East crude then glutting the world market. Venezuela was then emerging from a decade of military dictatorship in an economic slump that grew out of the U.S. recession of the late 1950's, aggravated by a loss of oil revenues due to the price-cutting in the Middle East. In this atmosphere Venezuela spent much of the 1960's pleading with Washington for "hemispheric preferences" for access to the U.S. market along lines similar to those given Canada. Indeed, at one point, President Rómulo Betancourt (1959-1964) thought that he and John F. Kennedy had worked things out. Kennedy "promised me that this Venezuelan aspiration for preferred entry to the U.S. market would be satisfied before the end of his mandate and mine," Betancourt recalled. "He told me the problem was 'devilishly difficult' because of the special interests involved. But he assured me that justice would be done to Venezuela."[1] The gunshots of Dallas left this explicit promise unfulfilled.

To the credit of Venezuela's young democracy, never has the public debate over nationalization of a great extractive indus-

[1] *Rómulo Betancourt, "Un recurso energético que no tiene igual,"* Visión, *February 12 & 26, 1972.*

try taken place in a more open and peaceful political climate. The possibility of nationalization, distantly contemplated for about 1984 when most of the concessions were due to expire, became an imminent reality with the October 1973 war. The discussion intensified greatly after the war and the landslide election, two months later, of Carlos Andrés Pérez as President of Venezuela. Since then, Venezuela has moved to nationalize its oil and iron industries and take a leading role in hemispheric politics.

The main question is no longer whether Venezuela will nationalize, but what the future modus operandi of the oil industry will be. The central issue of the nationalization debate is whether at least some of the 16 foreign companies—Exxon and Shell subsidiaries alone account for more than 80 per cent of Venezuelan production—will be allowed to remain in Venezuela as operating or marketing contractors to the new state holding company, Petroleos de Venezuela, in return for some share of future production, or whether the government will try to run the industry itself. Some companies have been quietly trying to play upon the percolating fears of mismanagement and to promote jobs for their employees in the future state marketing organization. This would give the present concessionaries more leverage in the future production of a nationalized industry. Expecting some kind of amicable dissolution of the old concessions, companies seem less interested in indemnification for installations already heavily amortized and depreciated than in some role in the Venezuelan industry's future.

At stake is the most important source of non-Arab oil for the United States, a source that becomes all the more critical during periods of threatened or actual embargo. And, as in the past, developments in Venezuela may affect events elsewhere.

Democratic Solidarity

Venezuela became the world's leading oil exporter in 1929, and held this position for

the next four decades. Since the end of the long dictatorship of Juan Vicente Gómez (1908-1935), oil and democracy have been closely linked in their development.[2] The flow of oil money into the cities has generated such enormous urban-rural income differentials that the countryside has been depopulated in one of the most intense internal migrations of this century, transforming Venezuela from a nation that was nearly 80 per cent rural in 1920 to one 80 per cent urban today. Meanwhile, Venezuela has moved fitfully toward creation of a complex and broadly based social democracy, with the economic leavening of oil revenues.

Venezuela received especially gentle and considerate attention in Washington after Mexico kicked out the foreign oil companies in 1938. Venezuela became a primary target for the Good Neighbor policy, and the State Department put heavy pressure on the oil companies to make their policies and personnel less offensive to Venezuelans, as well as to give in to Venezuela's demands for more oil money in order to avoid a repetition of the Mexican nationalization. By the 1960's, democratic solidarity had developed to the point where the Kennedy Administration viewed Venezuela as a test of its own hopes for the Alliance for Progress, and, later, as its only clear success in promoting reform, counterinsurgency, and private investment in Latin America.[3]

When Betancourt became the first popularly-elected ruler in Venezuela's 150-year republican history to finish his constitutional term of office, it was a triumph of his own

[2] *For a view of this relationship and of the structural weaknesses in Venezuelan society that have impaired the rational use of oil revenues, see my* Oil and Democracy in Venezuela, *American Universities Field Staff Reports, East Coast South America Series, Vol. XVII, Nos. 1 & 2, 1973.*

[3] *The Roosevelt and Kennedy policies toward Venezuela contrasted strongly to the official decoration given dictator Marcos Pérez Jiménez by Secretary of State John Foster Dulles in 1954 at the Caracas conference of the Organization of American States. However, the medal was awarded to the dictator over the objections of high State Department officials and only at the insistence of the U.S. military that anti-Communist rulers in Latin America must be given visible support.*

tenacity and of the people's awakening democratic vocation. To do this, Betancourt had to survive armed insurrections from the Left and the Right. He put down an outbreak of guerrilla warfare far more sustained and bitterly fought than Fidel Castro's Cuban insurrection. Two of his aides were killed and his own hand mangled in a 1960 assassination attempt by henchmen of Dominican dictator Rafael Trujillo, who rolled a car full of explosives into Betancourt's motorcade. This attempt was one of the considerations that led Washington to allow the CIA to supply arms to the men who killed Trujillo in May 1961.[4]

Venezuela Forms OPEC

As Venezuela's internal violence escalated, Betancourt's Minister of Mines and Hydrocarbons, Juan Pablo Pérez Alfonzo, was traveling in 1960 among the capitals of the Middle East to persuade the rulers of the oil-producing nations to form OPEC to defend their economies against the price-slashing being carried on by the companies and to find markets for the low-cost crude that was flooding the international oil trade in ever-increasing quantities. Pérez Alfonzo knew that only control of supply would enable Venezuela to influence price levels. If the oil-producing countries could unite, then the power of the integrated majors could be curbed. Later, a bargain could be struck with the United States and Canada to parcel out the hemispheric oil trade, giving Venezuela more security of access to its main markets.[5]

When Betancourt and his Acción Democrática (AD) party first ruled Venezuela in a reformist regime in the 1945-1948 period, the imaginative Pérez Alfonzo already had achieved much toward reversing the tendency of the oil companies to enrich rulers rather than governments. Under his leadership, Venezuela in 1947 pioneered establishment

[4] *See my "How Trujillo Died,"* The New Republic, *April 13, 1963.*

[5] *See Franklin Tugwell,* The Politics of Oil in Venezuela *(Stanford: Stanford University Press, 1975).*

of the 50-50 principle of profit sharing between companies and governments. AD governments in the 1940's and again in 1959 were the first among the oil-producing countries to formulate a policy of "no more concessions" to foreign companies. Trying to prevent her higher tax-paid costs from making her oil uncompetitive in world markets, Venezuela, in the late 1940's, began explaining to Middle East governments the terms of her new 50-50 deal with the companies, which led to the establishment of the 50-50 principle there as well.[6] By then, Venezuela had become so important to Jersey Standard (now Exxon) that half of its worldwide profits in 1948 were generated by Creole Petroleum, its Venezuelan subsidiary and the world's largest producing company, which supplied the crude for half of its worldwide refining capacity.[7]

The financial concessions that were wrung from the major companies by the host governments in the 1940's and 1950's, under Venezuela's leadership, did not disrupt the majors' cartel-like marketing arrangements, but only began a continuing escalation of the producing countries' share of the companies' profits. The next major mutation in the system came in 1960 with the formation of OPEC in response to the price erosion of the late 1950's. The U.S. import restrictions had created such an oil glut on the world market that British Petroleum (BP), with an oversupply of crude and rela-

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[6] *The Iranian Ambassador to Caracas, Manoucher Farmanfarmaian, who was Iran's Director-General of Mines in 1949, recently told a meeting of the Inter-American Press Association that the 1949 Venezuelan mission to Teheran "opened our eyes, showing us and discussing the contracts between Venezuela and the oil companies that were based on the 50-50 principle. This was the first time Iran got to know about these contracts. This shows how much influence the companies had. . . . In the following years, the Venezuelan system became our goal. The 50-50 was our objective but the resistance was so tenacious that finally there was no other solution but to nationalize."*

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[7] *See "Creole Petroleum: Business Embassy,"* Fortune, *February 1939, p. 180. The 87 cents per barrel earned by Creole in Venezuela compares with the return for the seven majors of 78 cents for lower-cost Middle East oil in 1957, during the post-Suez oil emergency.*

tively few marketing outlets of its own, unilaterally cut prices in 1959 for Iran, Kuwait, and Qatar production. Since the British government was then the majority shareholder in BP, the Venezuelan government addressed a memorandum on the price cuts to the British Embassy in Caracas, arguing:

> BP, the largest producer in the Middle East, has by this action brought prices below the 1953 level. Since that year, all the factors affecting production cost have increased substantially and the general level of prices in international trade has also risen. In the United States, the largest world producer, not only did costs rise, but the country also failed to discover sufficient oil in the past two years to replace the production of that period. The United States appears to have reached the depletion curve within a relatively short time, and other important producing centers of this irreplaceable natural resource will also reach a similar situation. In general, the costs of exploration and drilling are increasing throughout the world and the more widely dispersed the search to find new reserves for human needs, the more each new barrel will cost . . . the additional lowering of prices, by encouraging consumption, could very soon bring oil to the historic cycle of scarcity. This would force consumers to pay much higher prices to finance the exploration and discovery of new areas. It is evident that for the good of mankind, a stable situation would much better guarantee the interests of all concerned.[8]

Pérez and Oil

Since then, despite recurrent political crises, Venezuela has gone far toward consolidating her constitutional democracy. Today, flush with oil money and votes, President Carlos Andrés Pérez has embarked on a series of popular domestic reforms, including general wage increases, under special powers given him by his AD majority in Congress. A tough Andean politician who, as Betancourt's Interior Minister, had taken the lead in crushing the Castroite guerrilla insurrec-

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[8] *The memorandum was reproduced in* Venezuela and OPEC *(Caracas: Imprenta Nacional, 1961), p. 99.*

tion of the 1960's, Pérez became a prime mover behind the efforts to end the Organization of American States' diplomatic sanctions against Cuba last November. Failing to marshal the two-thirds majority needed to lift the sanctions, Venezuela then established diplomatic relations with Cuba, and, in other actions, championed higher prices for Latin-American primary products.

Venezuela is also trying to use her excess oil income to finance more rapid economic development in Latin America. After the tripling of her oil revenues between 1973 and 1974, Venezuela is recycling abroad more than one-third of her trade surplus, or about one-tenth of her whole GNP, in $500 million loans to both the World Bank and the Inter-American Development Bank, and in another $125 million distributed among the Andean, Central-American, and Caribbean development banks. Another $500 million was lent to the International Monetary Fund's oil recycling facility. Discussions are being held for lesser projects like financing a paper factory in Honduras, and an oil refinery in Costa Rica. This is more public money than the United States ever committed to the Alliance for Progress. In December, President Pérez met with the six Central-American presidents in the Venezuelan iron and steel center of Puerto Ordaz to announce that Venezuela would pay up to $80 million to Central-American coffee producers to enable them to withhold part of their crops from the market in an effort to support declining prices. Pérez announced that the six republics would only have to pay $6 of the $12 selling price of Venezuelan oil in dollars. The rest could be paid in local currencies into counterpart funds for soft loans such as those the United States made for decades to countries like India and Bolivia in the Food for Peace program.

In this way, Venezuela was able to advance her long-cherished ambitions for influence in Central America, and project her image throughout the Caribbean. A leading Dominican economist wrote recently that

"1974 probably represents the close of a period that began in 1961, of great dependence of our country on the United States, and unfortunately the beginning of another period of economic dependence on Venezuela and other nearby oil producers." [9]

Venezuela's oil power gave President Pérez center stage in Lima, at the December celebration of the 150th anniversary of the Battle of Ayacucho that won independence from Spain, where he urged the assembled military dictators of Bolivia, Panama, and Peru, and envoys of other Andean nations, to stop squabbling in ideological and border disputes. It also helped him in seeking to transform Venezuela into a democratic counterpoise to the influence of Brazil's military regime in Latin America and into a champion of economic justice for all underdeveloped countries.

Crisis of Democracy

But Pérez's trendy Third World rhetoric and some policy initiatives of his first year disguise much Venezuelan discomfort about how the oil revenues of the past two decades were wasted. How can they now absorb the much greater flood of oil money into what is essentially a rentier economy—some $10 billion in 1974, which is triple normal budgetary needs? Venezuela entered the 1973 election campaign in a mood of crisis due to the erosion of public faith in the parties that have run the country since the overthrow of dictator Marcos Pérez Jiménez (1948-1958).[10] The two big parties, AD and the Social Christian COPEI party of President Rafael Caldera (1969-1974), were able to dominate the election only through lavish advertising and by

[9] *Bernardo Vega, "1974: Año del Cambio en Nuestra Dependencia Económica Externa," in* Listín Diario, *November 22, 1974.*

[10] *The Kennedy Administration extradited Pérez Jiménez from his Miami exile in 1963 at the request of the Betancourt regime. He was finally released from jail in August 1968 and went to live in Madrid. Four months later, he ran, in absentia, for a Senate seat in Caracas, sweeping all but one of the city's 16 parishes. He gained the most votes in the poor workers' districts, where people had poured into the streets to overthrow him a decade earlier.*

changing the constitution a few months before the balloting to rule out a possible presidential candidacy of the ex-dictator, who had made a sensational political comeback in the five years since his release from jail for stealing public funds. The Yom Kippur war and the overthrow of Chilean democracy occurred within three weeks of each other at the height of Venezuela's election campaign, providing at once the economic impetus for oil nationalization and concern among Venezuelan leaders for the consequences of mismanagement of nationalized industries as under Allende. Many responsible Venezuelan politicians realize that their democracy could be washed overboard by incompetent handling of the nationalized oil industry or the tidal wave of oil money now pouring into the country. As Pérez himself said in a speech in Maracaibo three weeks after sending his public message to Ford:

> We have immense economic resources that the economy cannot absorb. We have the traditional and insatiable voracity of public spending, and the negligence with which the public and private sectors have used oil income. We are either at the beginning of an ascent toward consolidation of our nationality, or at a precipice that could leave us, not in catastrophe, but at a point back where we would have to start our development all over again.

In the same speech, Pérez attacked mismanagement of the state petrochemical industry, in which Venezuelan governments over the past two decades have invested roughly $2 billion, much of which has been squandered because of corruption and political interference. The new President said that, in its first six months of operation, the huge El Tablazo petrochemical complex near Maracaibo had some 50 breakdowns "from deficiencies in diligence and supervision." Previously, audits of the costs of building the $92 million El Tablazo complex found suppliers' and contractors' overcharges variously estimated at $20 million and $35 million. A few days after Pérez's speech, the head of the state petrochemical industry was fired amid

charges of price-rigging that allegedly cost the Venezuelan government $3 million in a deal with a U.S. firm.

Venezuela's difficulties in developing her state petrochemical industry, and in managing other state enterprises, have led to considerable self-doubt as she develops plans to nationalize oil, which before 1973 produced 90 per cent of her foreign exchange earnings and two-thirds of her government income, and today produces much more of both. While Venezuelan politicians have been talking for nearly four decades now about "sowing the petroleum" to diversify the economy, and despite widely publicized investments in modern infrastructure, heavy industry, agricultural development, and social programs, Venezuela has become more rather than less dependent on her oil revenues. The decision to immediately nationalize the oil and iron industries came in the weeks before and after the December 1973 elections, when the Arab oil boycott stimulated leaps in the posted price of Venezuelan crude to $14.08 per barrel, compared with the January 1973 price of $3.10. Although Venezuela's two big parties, AD and COPEI, had quietly agreed not to debate oil issues in the election, all but one of the 14 presidential candidates in the race had vaguely backed an "early reversion" of the industry to the state before the scheduled expiration of the concessions.

Doubts about Nationalization

Pérez began fulfilling this promise in May by appointing a 36-man Presidential Commission on Oil Reversion, representing the full range of political parties, professional associations, universities, and business and labor groups concerned with nationalization. As it was working on a draft nationalization bill last November, one member, Carlos Alberto Piñerua, president of the oil workers' union FEDEPETROL, expressed the growing nervousness of both politicians and the public over nationalization when he told me: "This is a kind of forced nationalization because of what is happening in the

Middle East. Without the rise in oil prices, Venezuela would not have moved so swiftly. The oil companies have started a campaign to frighten workers about the future. There is much more fear among the engineers and white-collar people than the workers, who want to conserve their social benefits, as well as technology and markets for Venezuelan oil production."

Pérez will be under great pressure to articulate policies in line with the conservative nature of his electoral mandate, with the feeling that Venezuela's rentier economy depends on one commodity that Venezuelans, lacking sufficient organizational and technological capacity, know they cannot produce and market alone. Many politicians privately say that the movement to nationalize comes not from any public clamor, but from pressures from within the smaller community of politicians, and from recent dramatic changes in the oil industry outside Venezuela.

Alternative to Middle East Oil?

One of the stakes is the degree of future U.S. dependence on Middle East oil. While Venezuela was overtaken in the ranking of oil exports by Iran in 1970 and Saudi Arabia in 1971, she remains the leading oil supplier to the United States. In 1973, Venezuela produced 35 per cent of net U.S. imports, mainly as heavy fuels for heating and electric utilities along the Eastern Seaboard.[11] However, Venezuelan production peaked at 3.7 million barrels daily (MBD) in 1971 and, according to both government and company projections, is expected to decline to below 2.0 MBD by 1984 from presently existing fields, mainly around Lake Maracaibo, many of which have been operating continuously for more than 50 years. This process of natural decline of the traditional producing areas has been temporarily obscured in 1974 by the conservationist production cutbacks of about 11 per cent of a government swim-

[11] *This includes the heavy oil exported by Venezuela to Canada's maritime provinces, offset by oil exported by Canada to the U.S. north central states.*

ming in oil revenues it cannot use. These cuts were made at the suggestion of the companies, which told the government that world demand had declined at the 1974 price.

If current predictions of rapid decline in Venezuelan oil production come true, then the United States will have to search elsewhere for supplies of heavy oil for her largest energy market, the Eastern Seaboard, or revert to greater use of coal. If the controversial conversion to coal is not made immediately, and the United States continues to rely on oil imports for its needs, then the international rivalries for access to Middle East oil may intensify. While world oil consumption continued its rapid rise over the past decade at an annual rate of 7.7 per cent, the volume of oil moving in world trade during the 1963-1973 period rose even faster, at 10.8 per cent annually. Because of steep rises in domestic demand, the role of U.S. oil imports since 1970 in world oil trade expanded even more dramatically, at more than twice the rate of international oil sales in the rest of the world. Between 1972 and 1973, U.S. imports rose by nearly one-third—to 6.2 MBD—while the volume of imports from Arab countries nearly doubled.

The relative immunity of the United States from the economic consequences of political convulsions in the Middle East has been based largely on U.S. domestic production and Venezuelan oil, both of which were taken for granted. Just as in the U.S. domestic oil industry, supplies from Venezuela are imperiled by the exhaustion of the reservoirs that have been producing now for several decades. Moreover, the anticipated production declines in Venezuela could be greatly accelerated by mismanagement of politicization of the nationalized industry. On the other hand, productivity could remain high if certain conditions are created. These are efficient management of the industry, and effective short-term investments in secondary recovery—gas and water

reinjection systems to maintain underground pressure in the older wells. These investments in high-cost recovery techniques have become more attractive after the tripling of Venezuela's oil prices during 1973. Moreover, any major exploration program probably could enable Venezuela to remain an important exporter at least for the rest of this century. To develop these new production possibilities soon, new tradeoffs will have to be devised to provide incentives for Venezuela, already overflowing with oil revenues, to at least maintain present production levels.

The strategic value of Venezuelan oil to the United States was again illustrated during the 1973 Arab oil boycott. Exxon's worldwide production of 6.3 MBD was cut by 20 per cent between the third and fourth quarters, but her 48 per cent share of Venezuela's 3.5 MBD production flowed normally to the United States. According to Exxon's 1973 annual report: "Supplies of heavy fuel oil . . . were not affected as seriously by the Arab embargo. Virtually all of Exxon USA's heavy fuel oil supplies are imported from refineries in Venezuela and the Netherlands Antilles operated by Exxon's affiliates. . . . Venezuelan crude supplies utilized in these refineries were maintained at normal levels." On the other hand, the tripling of the price of Venezuelan heavy fuel oil has had a major economic impact on the Eastern Seaboard.

Geologically speaking, there are promising prospects offshore in the Caribbean, in the 150-mile-wide delta of the Orinoco River, and in the Gulf of Venezuela, which is practically contiguous—separated only by a strait and some sandbars—to the great oil-producing basin of Lake Maracaibo. Apart from these conventional oil prospects, Venezuela contains one of the world's largest petroleum reserves in the Orinoco Tar Belt, estimated by geologists to contain 700 billion barrels of heavy oil. If only 10 per cent of the volume were recoverable, Venezuela could produce, from this basin alone, five

times her present reserves. Because this heavy Orinoco oil contains large amounts of nickel and vanadium, new technologies will have to be developed for large-scale lifting and refining operations by the 1990's. However, though the problems may be formidable, they may be less costly than producing oil from Colorado shale or Canada's Athabasca tar sands—the other major prospective sources of nonconventional oil in the Western Hemisphere.

The Future of the Majors

Beyond its role in determining the degree of future U.S. dependence on Middle East oil, the Venezuelan oil nationalization also may help shape the way the major oil companies will operate over the next few decades. Last November I talked with the government's chief economic negotiator, Manuel Pérez Guerrero, a soft-spoken, fragile-looking former Minister of Mines, who was one of OPEC's leaders in the mid-1960's. He said:

> We want this nationalization to be acceptable as an act of sovereignty within the law. Our greatest political problem is management capacity. We will need help from foreign technologies, but the reins of the business must be in our hands. We are not nationalizing buns and cakes, but important strategic commodities that cannot be left entirely in the baker's hands. We will be the owners and must make the basic decisions ourselves. We feel an obligation not to bring about any upheavals, nationally or internationally. . . . Under these new conditions, the major companies will be reduced to the role of traders, intermediaries, refiners, and providers of technical services. This is no small thing, but much less than before, when they had what seemed unlimited supplies of crude under their exclusive control. We must force the majors to be more aboveboard than secretive, and this will be good for the industry and the world.

In the worldwide wave of oil nationalizations that began in 1971 and is expected to reach its climax this year, two-thirds of the production of the seven major oil companies outside North America, or an amount

roughly equivalent to more than half of the 34.1 MBD that moved in world trade in 1973, will be taken from the proprietary control of these companies with the end of the old concession system. Although much of this oil will continue to move through the majors' marketing network as a result of new production and purchase agreements with the exporting countries, the security of abundant and low-cost supply that was the basis of an integrated industry now may be a thing of the past. Saudi Arabia, Venezuela, and the Persian Gulf sheikdoms, with a combined 1973 production of 15.8 MBD, are expected to announce the terms of their state takeovers this year. With the old structure of the international industry badly shaken, today's high prices and the insecurity of future supplies have made the oil contingencies less of a question of entrepreneurship and more of a question of state. The stresses caused by oil payments and supplies have led the governments of consuming as well as producing countries to consider taking a stronger hand in the management of the industry, just as the British government did on the eve of World War I, when Winston Churchill, First Lord of the Admiralty, told the House of Commons in 1914:

> Nobody cares in wartime how much they pay for a vital commodity, but in peace . . . price is rather an important matter. . . . I cannot feel that we are not justified . . . in considering how in years of peace, and in a long period of peace, we may acquire proper bargaining power and facilities with regard to the purchase of oil. The price of oil does not depend wholly, or even mainly, on the ordinary workings of supply and demand.

The occasion was the British government's purchase of a 51 per cent share of the Anglo-Persian Oil Company (now British Petroleum) as her navy's warships were converting from coal to liquid fuel. Today, consuming governments are pressed more urgently to reconcile the dual character of oil as both a strategic resource and a commodity traded throughout the world.

Through tax policies, Washington favored the oil companies with depletion allowances and credits for taxes paid governments of producing countries, and indirectly stimulated consumption by using a gasoline tax to finance the building of an interstate superhighway system. Now other tax policies are being discussed to limit oil imports. Going beyond this kind of fiscal improvisation, Walter J. Levy observed recently that "the problems of oil have become matters that in many key respects can only by handled directly between governments," adding that oil prices must remain high so as not to endanger the economic viability of expensive alternatives, such as development of tar sands, shale, and coal gasification as energy sources. Levy wrote that "avoiding dependence on foreign oil dictates public support and a substantial measure of price guarantees by individual countries, notably the United States . . . acting . . . in coordination."[12] During the Arab boycott another leading oil analyst, Edith Penrose, saw the possibility of the companies becoming "public utilities with appropriate public regulation," arguing that "it will no longer be possible for the governments of the oil-importing countries to leave the international companies as free a hand in the industry as they have had in the past in view of the fact that the governments of the exporting countries will be deciding the major issues affecting the terms on which oil is sold."[13]

A U.S. Government Share in Big Oil?

These arguments seem to provide strong reasons for U.S. government purchase of large minority stockholdings in one or more of the major American oil companies. First, the capital accumulation and reduced levels of consumption that will soon be

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[12] *See Walter J. Levy, "World Oil Cooperation or International Chaos,"* Foreign Affairs, *July 1974, p. 699.*

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[13] *From Edith Penrose, "Origins and Development of the International Oil Crisis,"* Millenium, *Vol. III, No. 1, 1974.*

needed in the energy field to lower oil imports and develop alternative sources of energy will require a strong public guarantee that the oil industry's "obscene profits" will actually fulfill the stated purpose of energy investment and not be diverted into unrelated activities (such as Mobil's attempted purchase last year of Montgomery Ward, as part of its efforts at corporate diversification, to relieve its dependence on an increasingly regulated yet unstable industry). Second, with the oil companies losing their control of foreign supplies of crude, their self-advertised role as buffers and intermediaries between producing and consuming governments has become less meaningful. What do remain important are their managerial and technological skills. Third, such direct government leverage in the industry would facilitate long-term government-to-government arrangements on price and supply that repeatedly have been urged by producing countries, especially Venezuela.

In the coming months, Venezuela will be faced with a choice between two kinds of nationalization: the Latin-American tradition of the operating state oil company, such as PEMEX of Mexico and PETROBRAS of Brazil, or the developing Middle East pattern, now working in Iran, by which the state owns the industry but foreign companies continue to operate under varying degrees of government control. The Iran formula may soon be applied, with modifications, in Saudi Arabia and the Persian Gulf sheikdoms, and the major concessionairies in Venezuela have expressed hope that they will be able to remain on similar terms. The Middle East formula is a variant of the "service contract" concept first formulated in Venezuela in 1959 but not applied there until 1970. In its 1973 annual report, Exxon said it was "optimistic that whatever changes may take place and whatever relationships may evolve, there will be a basis for continuing operations" in Venezuela.

While the state oil company has been the dominant operating entity in Chile, Argen-

tina, Uruguay, Bolivia, Peru, and Colombia as well as Mexico and Brazil, none of these countries has a major export industry like Venezuela's. Moreover, some repeatedly have called in foreign companies to find oil that their state enterprises have lacked the financial and technical resources to discover. While the producing countries agree that the technical and organizational services of the majors and large contractors will be needed for at least the near future, the Middle East formula remains an anathema to many Venezuelan nationalists.

In Venezuela, the draft law approved by the nationalization commission prohibits "creating mixed enterprises or participation in profits for activities reserved to the State." However, toward the end of 1974, the AD government showed many signs of moving away from this restricted definition of nationalization to allow itself much more flexibility in running the industry. In the final months of the commission's deliberations, the AD party and government representatives pointedly stayed away from the sessions to allow President Pérez and his advisers more room for maneuvering before presenting the final version of the nationalization bill to Congress. Pérez's attack on the management of the petrochemical industry has been seen as an effort to reinforce the public's fears that the government cannot directly manage the oil industry and that some deal with the companies should be made. Moreover, in December, when he announced the negotiated nationalization of the iron mining operations of U.S. Steel and Bethlehem Steel, Pérez called it "a magnificent solution that opens very favorable prospects for the more difficult and complex situation that will arise with the expiration of the oil concessions that will occur by Venezuela's sovereign decision in coming months."

The iron nationalization arrangement calls for the companies to run the mines during a transition period of one year, in exchange for a continuing supply of ore to U.S. steel mills, and leaves the way open for

future technical assistance in mining and joint ventures in intermediate stages of processing. Significantly, all the opposition parties refused to support the iron nationalization deal in Congress, arguing that it was too generous to the companies, and only AD's parliamentary majority and a small party sympathetic to ex-dictator Pérez Jiménez voted for approval. Since there were persistent rumors of oil company support for AD in the election campaign, the debate over oil nationalization may prove to be even more bitter if a formula is presented that would enable the companies to continue operating the industry.

Once nationalization is approved, difficulties are anticipated by conservatives and Jacobins alike. For one thing, automation and a sharp decline in exploratory drilling since Venezuela's "no more concessions" policy was announced in 1959 have resulted in a halving of the industry's work force over the past 15 years to 21,000, or less than 1 per cent of all persons employed in the country. The fact that so small a proportion of the labor force is employed in the capital-intensive industry on which the country is so dependent has permitted a pervasive ignorance of the oil business among even educated Venezuelans.

Scared Workers and Scarce Technicians

Automation and attrition have left the oil industry with a work force composed largely of middle-aged men (averaging 45 years old and 19 years on the job) who are economically privileged, politically conservative, and, on the whole, deeply worried about their future. Said a Marxist union leader, "both the iron and oil workers are against nationalization. They're afraid of what will happen to social benefits like company medical care and their retirement plans. The iron workers want all of their retirement payoff now, but if they were to get it they'd all leave the iron mines and never come back." The government has promised to place the retirement money of the oil and

iron workers in a special fund in the Central Bank. But unrest in the industry is likely to continue until the government provides strong proof that the nationalized industry will be effectively managed in the interests of both the workers and the country. Otherwise, both the iron and oil work forces will become hosts to agitation by opposition political parties that will make the transition to state ownership much more difficult.

While Venezuela proportionately has more of her own professionals in the oil industry than any other OPEC nation, she is still short of technicians to run the nationalized industry without outside help. Although the companies have made an effort in recent decades to put Venezuelans in high-level jobs, there are still 635 foreigners in key technical and executive positions. While many of these foreigners, if encouraged, would stay on after nationalization, many middle-level Venezuelans already have taken early retirement from the companies with the approach of a state take-over.

High Venezuelan officials have said many times that, after nationalization, they will maintain intact the organizations of the four largest concessionaires—Exxon, Shell, Gulf, and Mobil—and will gradually consolidate the operations of the smaller companies into larger production units. But there will be a continuing need for something like the logistical and technical support that always has been provided by the majors to their overseas subsidiaries. Moreover, most of Venezuela's oil has been sold abroad by the majors' marketing organizations outside Venezuela. While some of these limitations can be overcome with time, any attempt by Venezuelans to overreach these limitations now could prejudice their nationalized industry.

Curiously, some of the most important nationalizations since World War II[14]—Iran-

[14] *On the Chilean and Bolivian nationalizations, see my* Copper Is the Wage of Chile, *and* Bolivia: The Price of Tin: Part I, *American Universities Field Staff Reports, West Coast South America Series, Vol. XIX, No. 3, 1972, and Vol. XXI, Nos. 1 & 2, 1974.*

ian oil in 1951, Bolivian tin in 1952, and Chilean copper in 1969-1971—seem to have occurred when world prices for the commodity have peaked and begun to decline. Instabilities in the supply of oil can be anticipated from the wave of nationalizations now taking place throughout the world and from possible political conflict in the producing areas. Because of new oil from non-OPEC countries that probably will be available for marketing in the late 1970's, just as consumption restraints in the industrialized nations begin to take hold, it may be reasonable to expect dramatic fluctuations in the price and supply of oil for the rest of this decade. Despite their recent success in driving up oil prices, the OPEC countries have a long history of bickering among themselves, and, until 1974, have been especially unsuccessful in limiting production, as any cartel must, to protect prices. With most big producers now operating below capacity because of consumer response to high oil prices and the spreading world recession, coordinated production cuts by OPEC may be needed in the near future. Mexico's recent decision against joining OPEC indicates that new oil-producing areas may not be easily absorbed into the cartel.

Not that OPEC, of itself, is a bad thing. One of the most ardent advocates for primacy of the majors has argued persuasively that, in an inherently unstable industry given to boom and bust cycles and to gluts and scarcities of supply, "the oil industry, to exist at all, calls for concerted effort and, however often a cooperative structure may have been disturbed or broken up, it will soon begin to form again." [15] The problem is that OPEC has attempted to justify its 1974 price levels as being below competing sources of energy. This is a fallacious argument because, in the short term, there are no competing sources of energy, and OPEC could just as well charge $40 or $50 per barrel as $10 or $12. But many oil analysts in the consuming

[15] *P. H. Frankel,* Essentials of Petroleum *(London: Cass, 1969), second edition, p. 97.*

countries now believe it would be more tragic for humanity than for the OPEC countries for the price of a barrel of oil to fall back to the pre-1970 price of $2, thus stimulating a return to wanton consumption that would hasten the exhaustion of the world's limited petroleum reserves. A return to low oil prices also would undermine the shaky financial structure supporting worldwide oil exploration, into which consuming countries poured upward of $10 billion in 1974.

Given future market uncertainties, now may be a good time for Washington to enter into long-term price and supply arrangements with Venezuela, which could thus continue as a pioneer in developing new relations between producing and consuming countries. While Venezuela's unsuccessful quest for hemispheric preferences has been forgotten in the upward surge of prices over the past few years, such favored access to the U.S. market, coupled with price guarantees, could be extremely helpful to her should oil prices again become unstable. Extending preferences and guarantees to Venezuela, which could be done unilaterally by Washington, would be in the U.S. interest in that they would stimulate Venezuela to expand her oil production capacity despite worldwide economic uncertainty, and to remain an extremely valuable supplier. In addition, price and market guarantees could be coupled with technical and educational support to the nationalized oil industry to give Venezuela more economic autonomy and stability over the long term.

This kind of cooperation is certainly not going to be achieved through economically meaningless and politically counterproductive reprisals such as the denial to OPEC members of most-favored nation status under the new U.S. foreign trade statute, a provision that has led Venezuela and Ecuador, the two Latin-American OPEC members, to force cancellation of the Buenos Aires hemispheric foreign ministers' conference in March.

In the end, the United States must meet the challenge posed by President Pérez's

letter to President Ford. If not for reasons of sympathy or justice, then a decent respect for the future price and supply of a wide range of raw materials should dictate a new departure in U.S. policy toward nationalized industries. This would mean a reversal in U.S. economic diplomacy, since these industries traditionally have been treated as pariahs by international aid agencies. However, the stability of supplies of oil, copper, tin, iron, bauxite, and even bananas will depend, to a considerable degree, on the performance of nationalized industries in Latin America. To ensure a rational flow of these products into world markets, it may be in the self-interest of consuming countries to provide facilities in Latin America for the training of people from these nationalized enterprises in such varied skills as management, marketing, cost accounting, and specialized engineering operations. If the United States could provide continual training for more than a decade for police and counterinsurgency operatives in Latin America, then Washington surely could support, along with other industrialized countries, a public sector manpower training program implemented by some international agency. Beyond this kind of training, it may be advisable to provide design, engineering, and capital assistance to these industries to expand their capacities, especially in the processing of raw materials, and reduce the polarization between producing and consuming countries that is at the heart of the oil crisis. In this connection, perhaps as counterpoint if not refutation of former President Nixon's public expressions of support for the military dictatorship in Brazil, it might not be amiss for Ford to voice solidarity with Venezuela's democratic institutions and with her economic defense of the hemisphere's more vulnerable republics.