The Role of the Middle East Producers in the Global Oil Market

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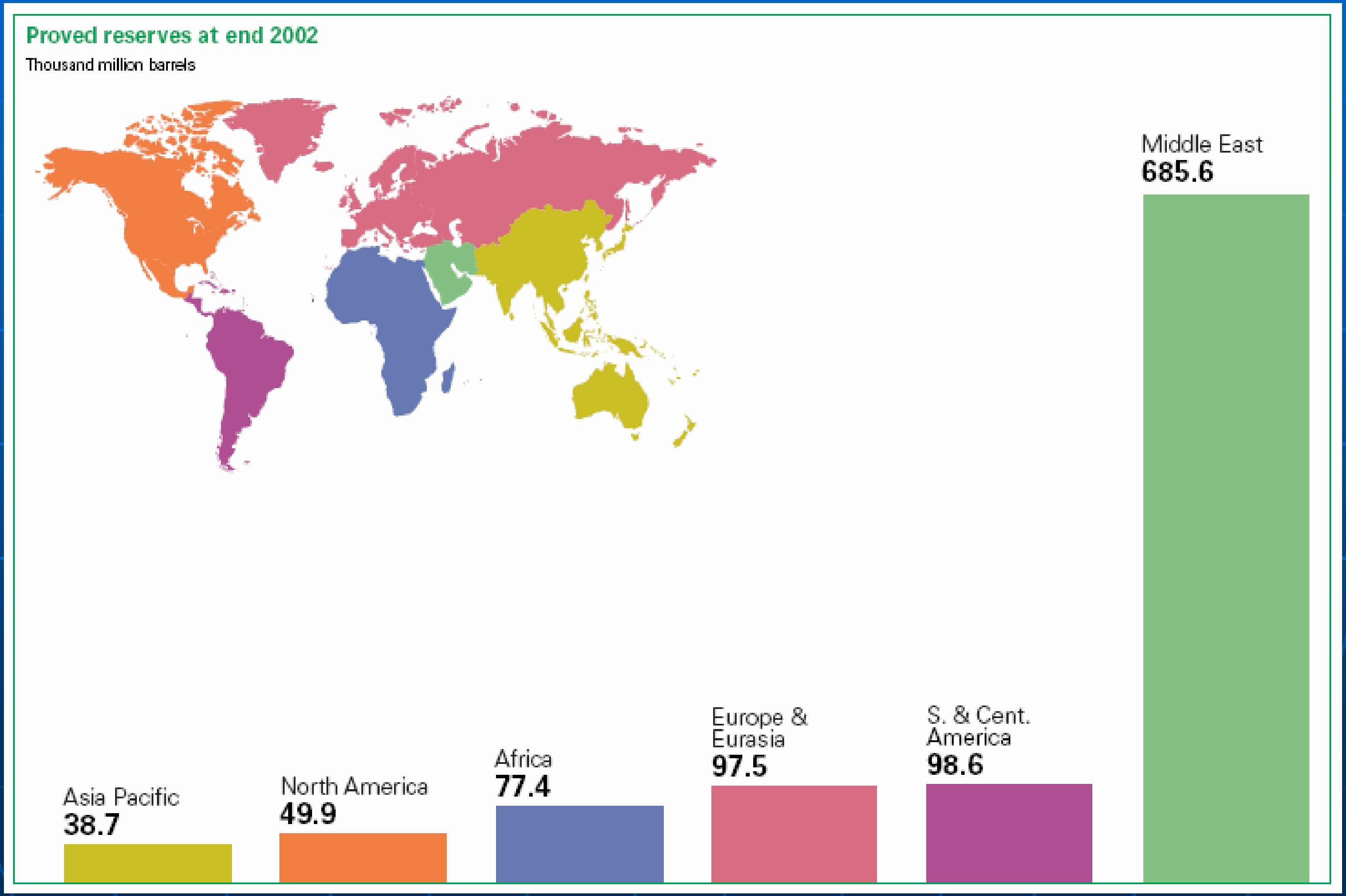
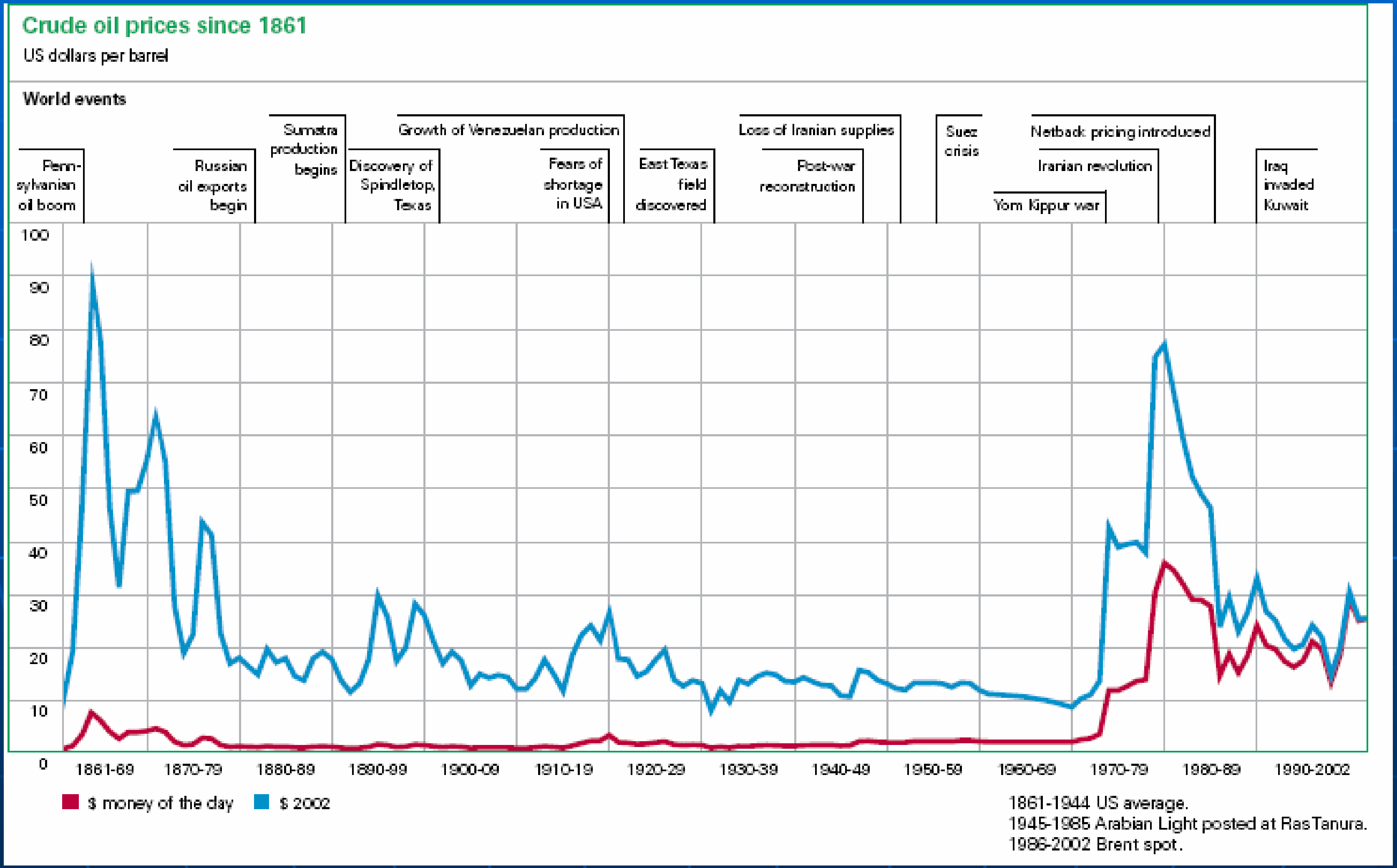
Agenda

- Evolution of the global oil market
- Future “dependence’ and the role of the Middle East
- Oil exporters’ economic development

Middle East oil reserves dominate



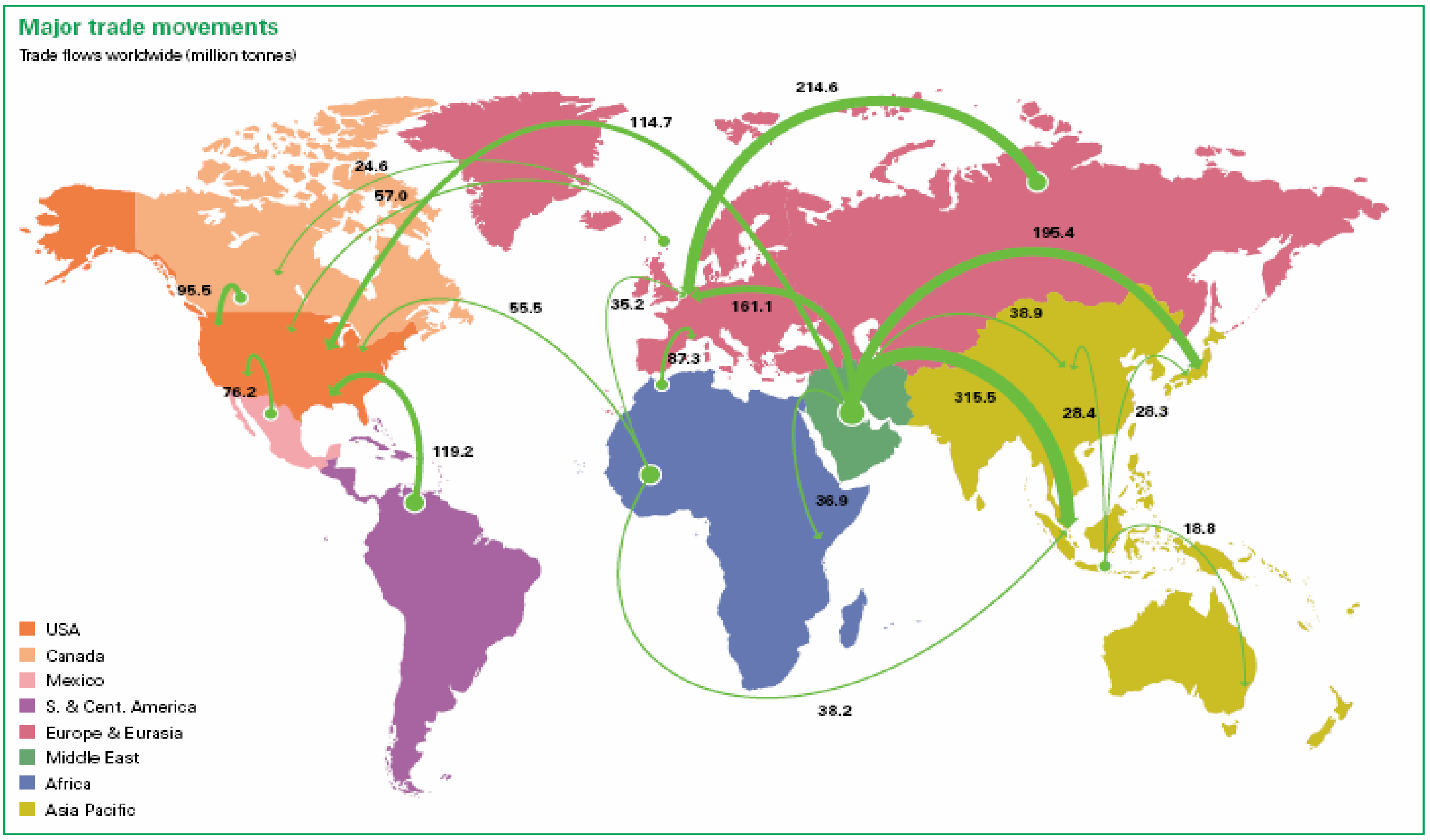
Post – 1973 is different



Crude oil reserves and production - 2002

	Reserves	Production	Reserves	Production
	Gb	MB/d	Shares	
Saudi Arabia	262	8	25%	12%
Iraq	113	2	11%	2%
United Arab Em	98	2	9%	2%
Kuwait	97	2	9%	2%
Iran	90	3	9%	5%
Qatar	15	1	1%	1%
Gulf OPEC	***674***	***17***	***64%***	***24%***
Venezuela	78	3	7%	4%
Libya	30	1	3%	2%
Nigeria	24	2	2%	3%
Algeria	9	2	1%	2%
Indonesia	5	1	0%	2%
Other OPEC	***146***	***9***	***14%***	***13%***
Russia	60	8	6%	11%
No America	37	10	4%	14%
China	18	3	2%	5%
Other FSU	18	2	2%	2%
North Sea	16	6	2%	8%
Mexico	13	3	1%	5%
ROW	66	13	6%	18%
Non-OPEC	***229***	***44***	***22%***	***63%***
		-		
World	**1,048**	**71**	100%	100%

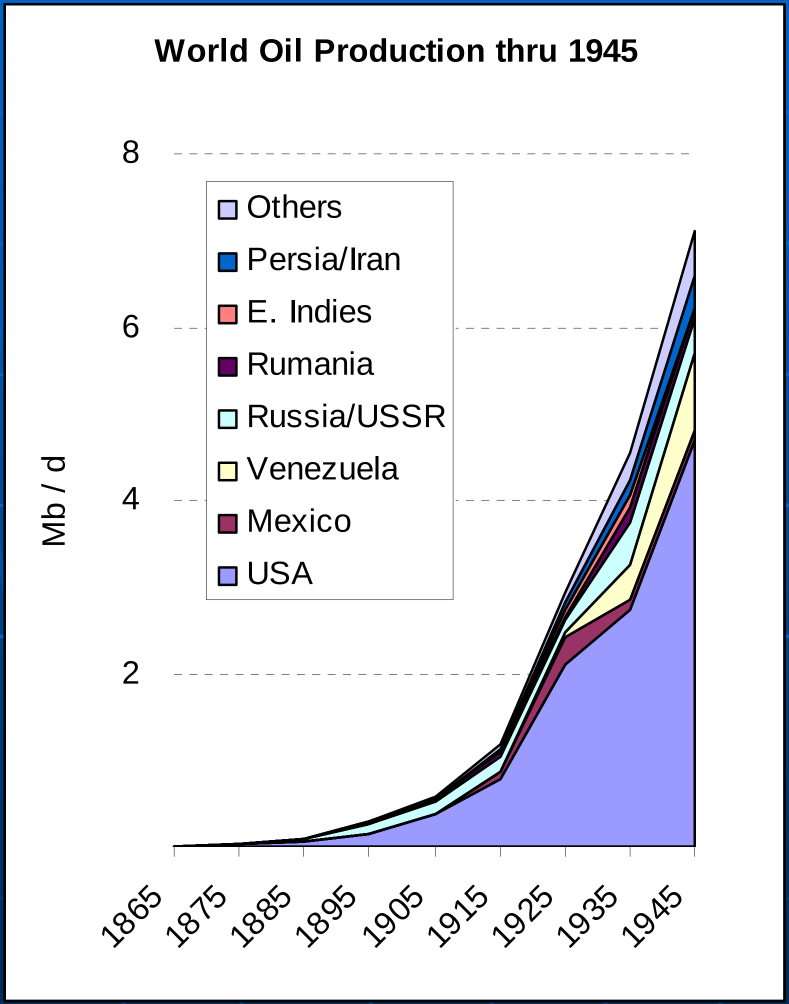
Oil trade -- 2002

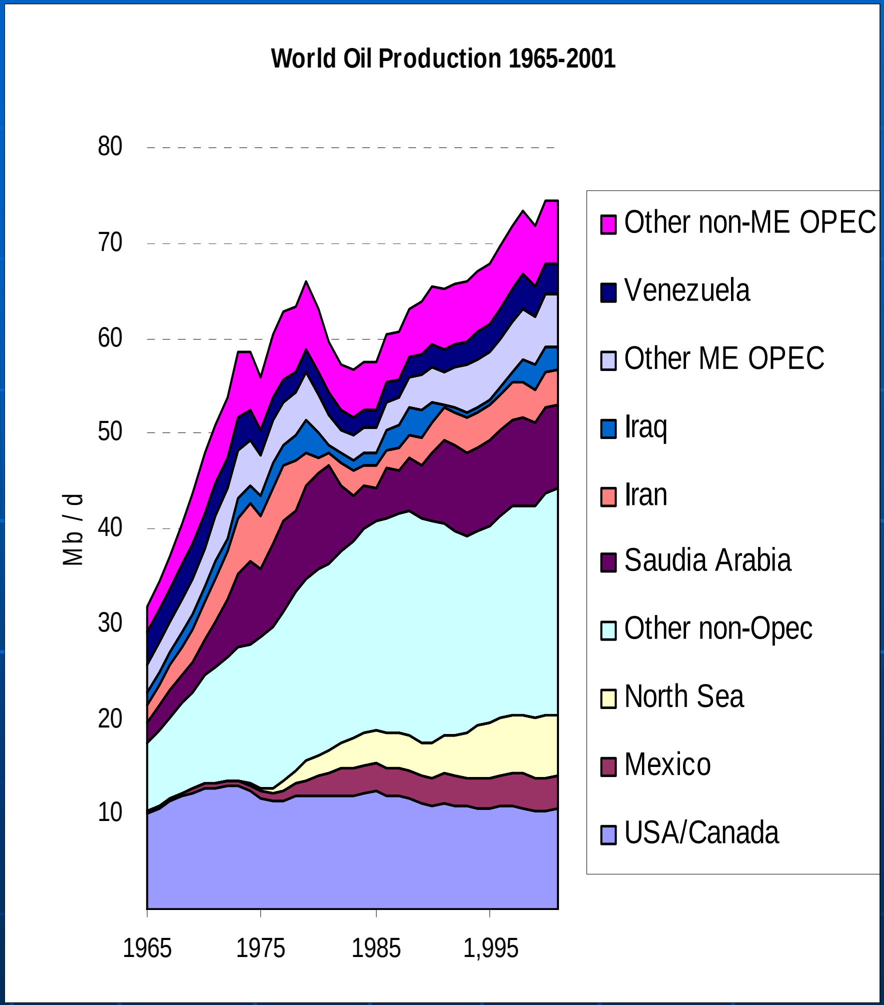


Most oil is found in big, cheap chunks

- Always an issues of market power -- tension between glut and monopoly control
- Trade dependence implies geopolitical significance

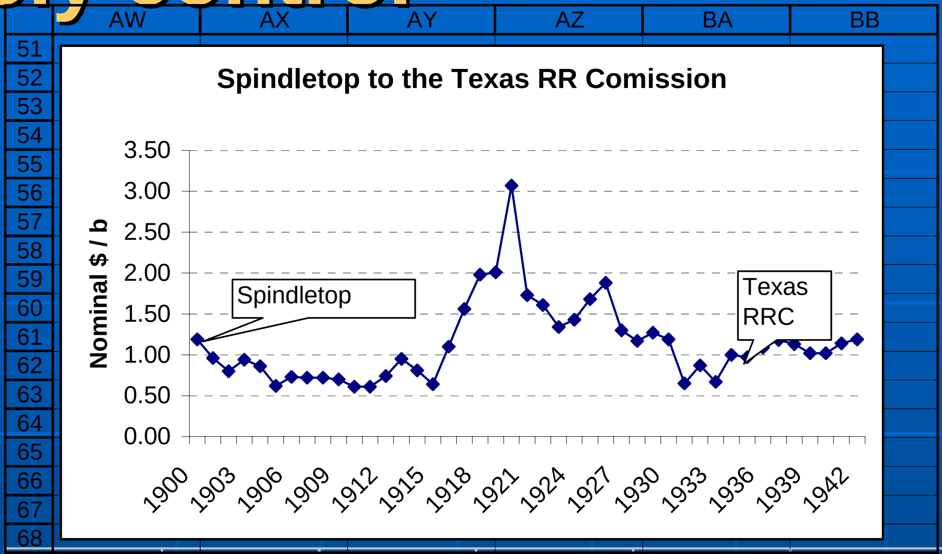
World Oil Supply

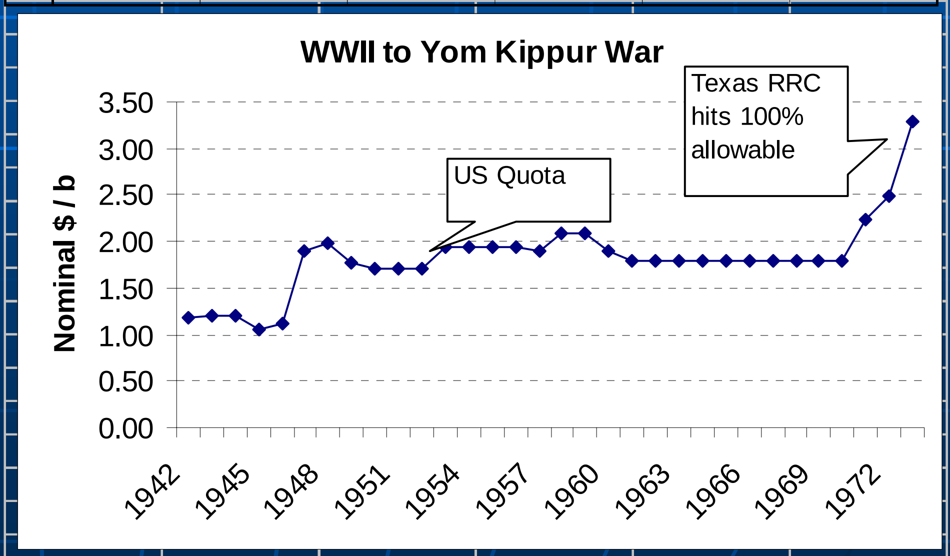




The oil market is almost always under monopoly control

- 1870 – 1911 Standard Oil
- 1911 – 1928 International co-operation / wars
- 1935 – 1971 Texas RR Commission, US Quotas
- 1971 –OPEC, more or less





1860 – 1945: US dominates, but Europeans "colonize" the rest of the world

1859 -- Oil discovered in Pennsylvania

1870 – Rockefeller forms Standard Oil

1873 -- Nobels enter Russia at Baku

1885 – Rothschilds enter Russia
Royal Dutch finds oil in Sumatra

1892 – S. Marcus send *Murex* thru Suez

1896 – Ford builds first car

1901 – concession in Persia,
Spindletop in USA

1907 – Shell and Royal Dutch combine

1908 – Anglo Persian formed

1911 – Standard Oil Trust dissolved

1914 – UK gets 51% of Anglo-Persian

1922 – oil discovered in Venezuela

1928 – (Gulbenkian) Turkish Petroleum negotiate "Red Line" agreement splitting ME (except Kuwait) between French (CFP), BP, and Rd/Shell

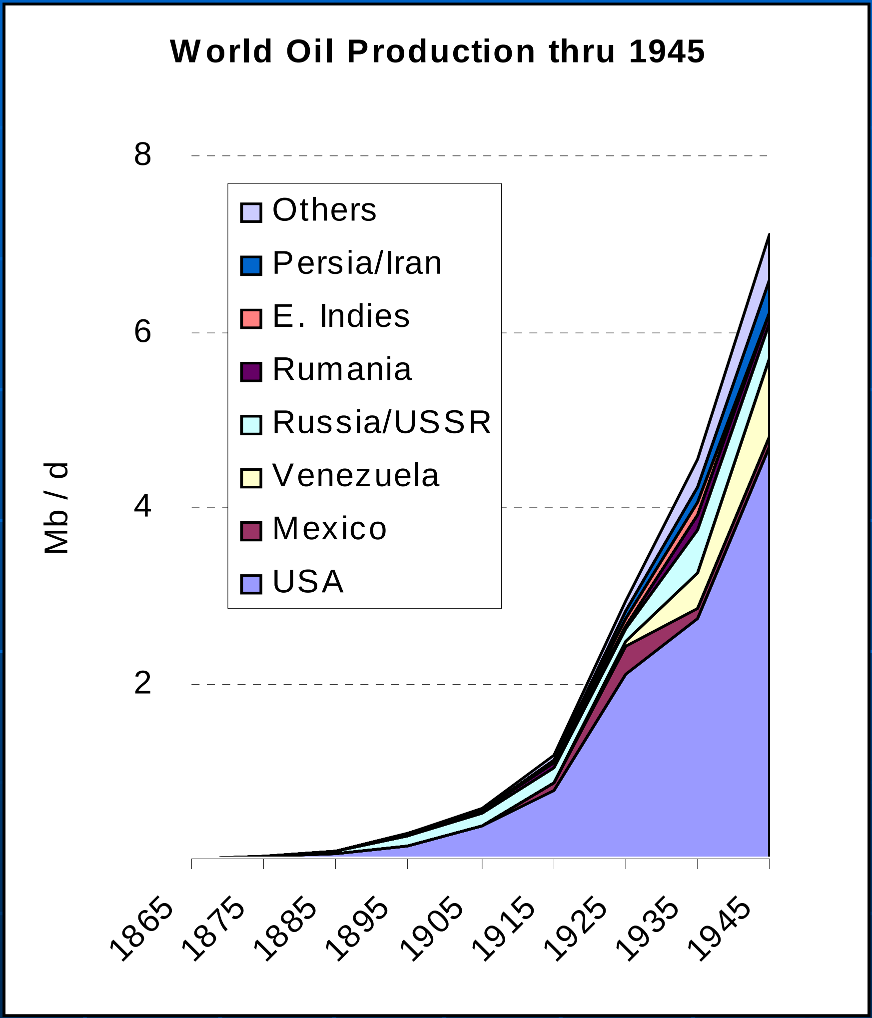
Achnacarry "As is" agreement

1930 – East Texas fields come in in time for recession

1935 – Texas RailRoad Commission formed

1938 – Mexico nationalizes oil

1939 – 45 WWII, Japan grabs SE Asia oil
Hitler invades Russia to get Baku



1950 – 1975: Producers' power emerges

1950 – US invited into Saudi Arabia,
Aramco is Standard, Texaco, Chevron, Mobil

1952-55 Buyers' embargo of Iranian production

1956 – Suez war, canal closed;
founding of independent tanker and FOB crude oil market

1959 –MidEast and Russian production grow,
US import quotas to sustain US price

1960 – OPEC founded (Venezuela, Saudi Arabia, Iraq, Iran,

1967 – 6-day war, Suez closed again

1968/69 – North Slope and Alaska discovered

1970 – Libya raises price and share

1971 – Texas RR Commission "allowable" hits 100%

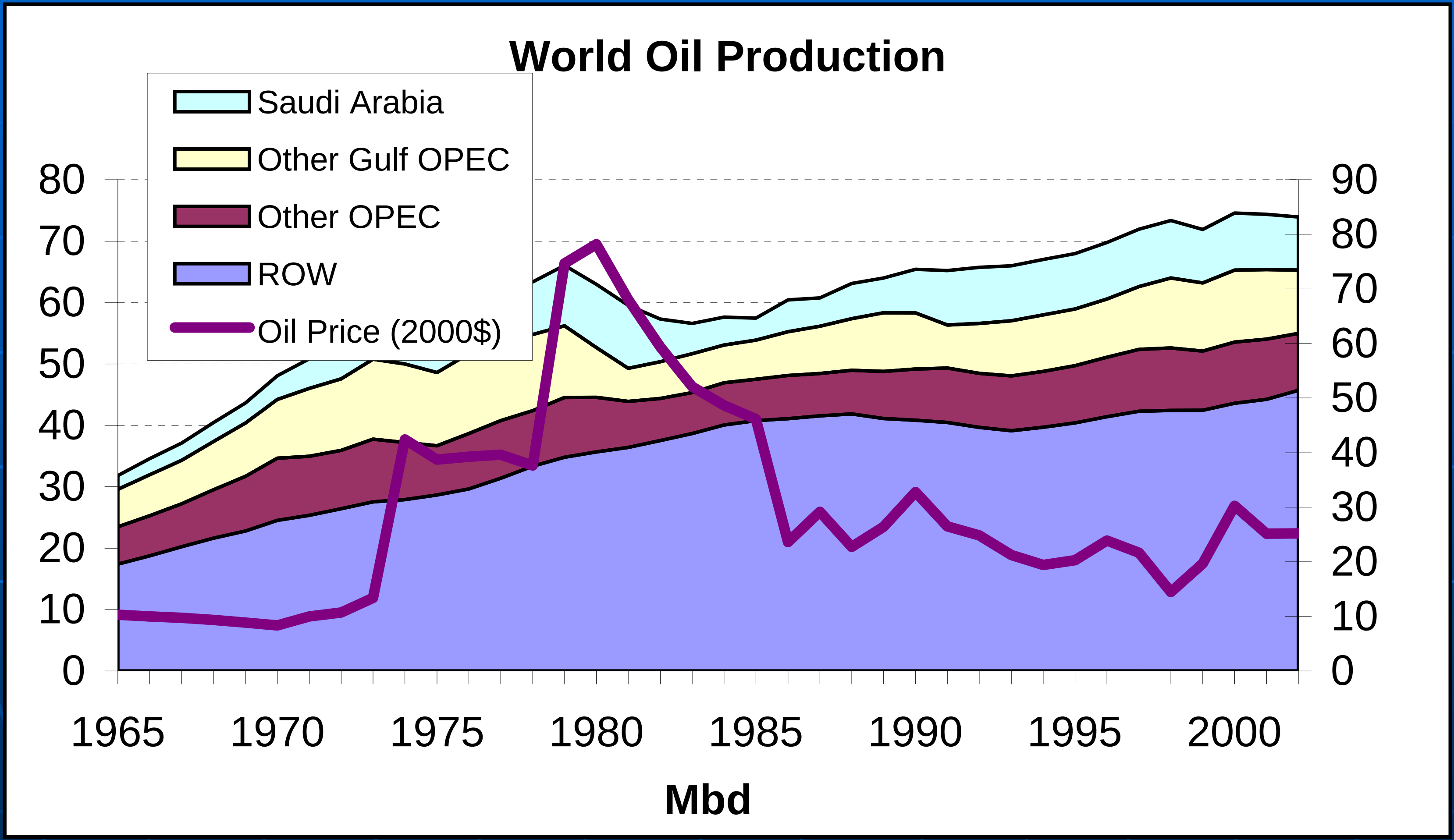
1973 – Yom Kipper war and embargo, oil price shock ($3/b to $11/b)

1975 – Concessions end in Saudi, Kuwait, and Venezuela

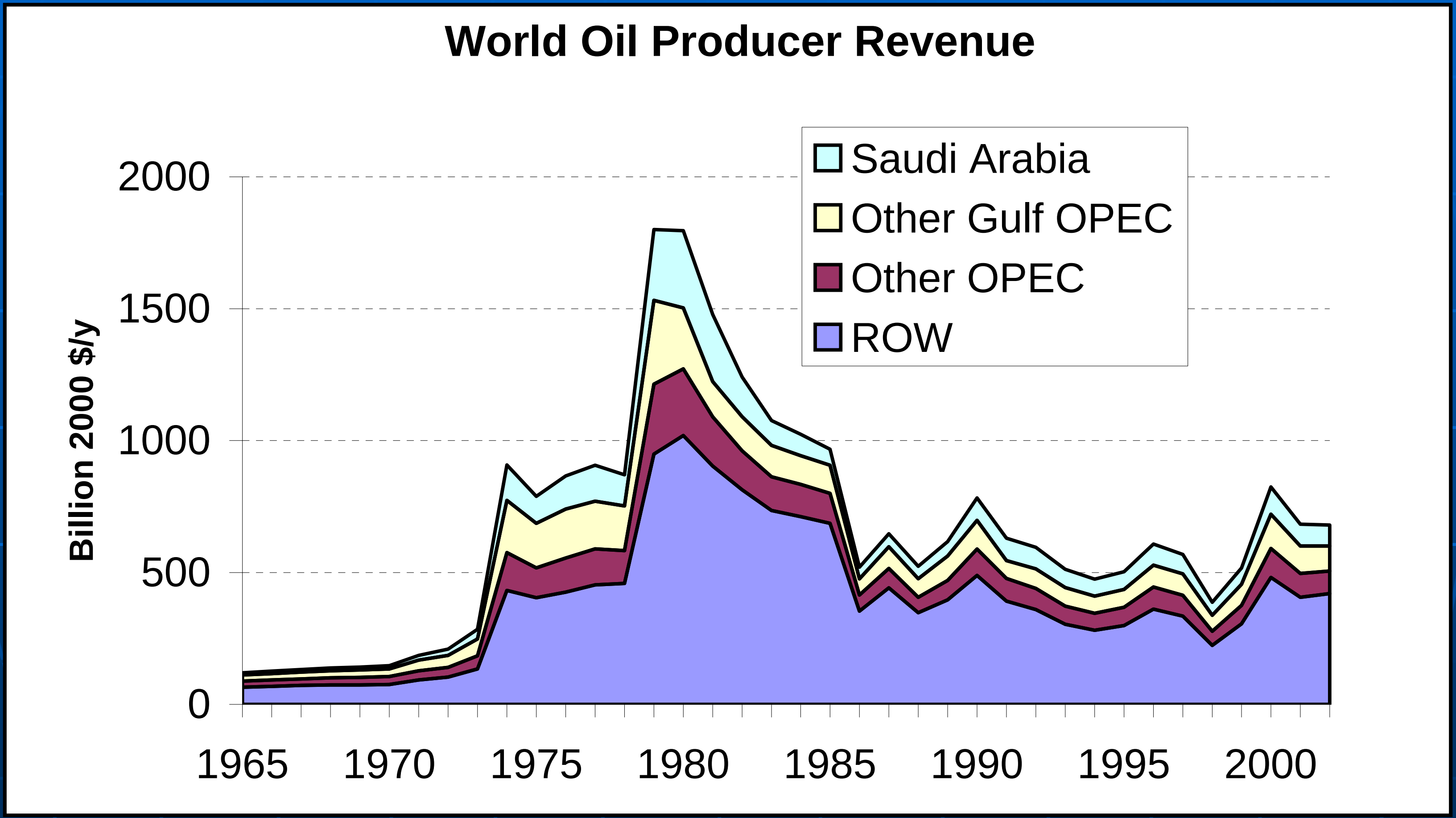
OPEC takes control and learns that greed is not rewarded

- 1973 – Yom Kipper war and embargo, oil price shock ($3/b to $11/b)
- 1975 – Concession end in Saudia, Kuwait, and Venezuela
- 1979 – Iran crisis, second oil price shock (#13/b to $34/b)
- 1981 – Saddam goes to war on Iran
- 1985 – Saudi (at about 3 Mb/d) sells “netback” oil
- 1986 – Oil price collapse to $8/b,OPEC switches from controlling prices to allocating quantities
- 1991 – Kuwait price spike broken by SPR release
- 1998 – “Asian flu” causes $10/b glut
- 2001 – OPEC discipline -$22 - $28/b
- 2003/4 – no Iraq-war spike, but prices stays in mid-$30s

OPEC and Oil Pricing



OPEC and Oil Revenue



Lessons

- **Producers' pricing powr is limited by the response of demand and competing supply**
- **Saudia Arabia has been the stabilizing force after 1973**

Projections of oil market dependence

- Volume
- Inter-regional trade and dependency

Projected regional trade grows by 26 Mb/d to 50%

- **Imports**
  - Industrial regions grow 15 Mb/d
  - China and Other Asia grow 11 Mb/d
- **Exports**
  - Mexico down 1 Mbd
  - Russia, Caspian, West Africa add 9 Mb/d
  - Non-Middle East OPEC adds 3 Mb/d
  - Middle East OPEC adds 15 Mb/d

	Trade		
Mb/d	2001	2025	*Change*
Regional imports			
Industrial	23	38	*15*
Non-OPEC So Amer	1	1	*0*
Other Asia	6	11	*5*
China	2	8	*6*
	32	57	*26*
Regional exports			
Mexico	2	1	*-1*
Non-OPEC Africa	1	5	*4*
Russia/Caspian/EE	4	9	*5*
OPEC-nonME	7	10	*3*
OPEC-ME	18	33	*15*
	32	57	*26*
Regional trade share			
	41%	50%	

US Energy Information Agency, 2004 Annual Energy Outlook

US EIA projected world oil volume grows 37 Mb/d

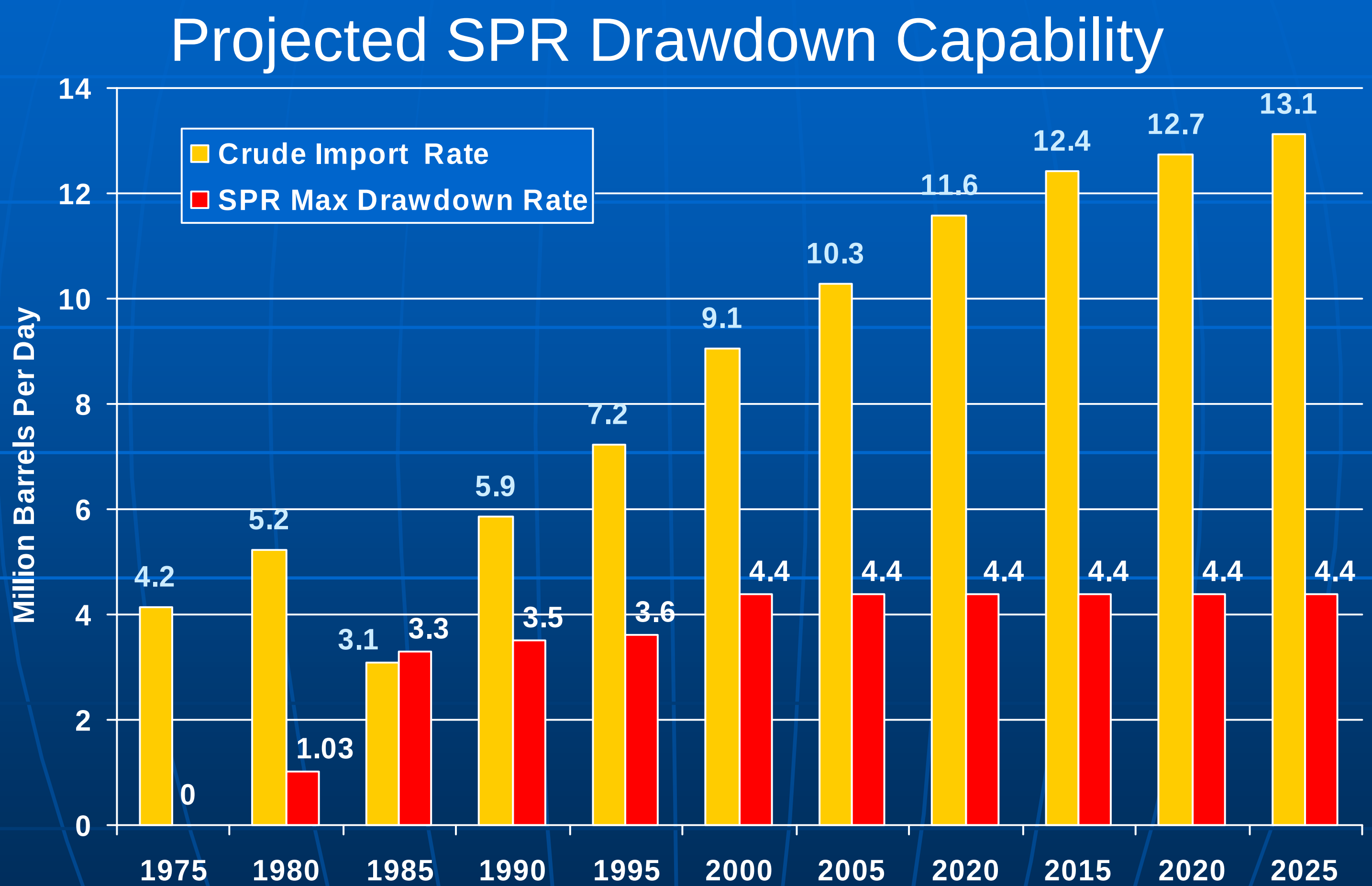
- Real oil price about flat at $25/b
- World oil market volume grows 37 Mb/d
  - Non-OPEC 14 Mb/d
  - OPEC 23 Mb/d
- Industrial countries' supply drops 3 Mb/d
- Outside OPEC, big increases
  - South America 4 Mb/d
  - West Africa 4 Mb/d
  - Russia/Caspian/EE 8 Mb/d
- OPEC
  - Non-Middle East 4 Mb/d
  - Middle East 19 Mb/d

	Supply		
Mb/d	2001	2025	*Change*
Importers			
Industrial	19	16	*-3*
Non-OPEC So America	4	7	*3*
Other Asia	4	5	*1*
China	3	3	*0*
Exporters			
Mexico	4	5	*1*
Non-OPEC Africa	3	7	*4*
Russia/Caspian/EE	9	17	*8*
OPEC-non ME	10	14	*4*
OPEC-ME	21	40	*19*
World*	77	114	*37*
of which:			
Non-OPEC supply	46	60	*14*
OPEC supply	31	54	*23*

** includes non-conventional production*

US Energy Information Agency, 2004 Annual Energy Outlook

How much can Strategic Storage do in a world with shrinking inventories?



A parallel Washington universe -- "Neocon" policy

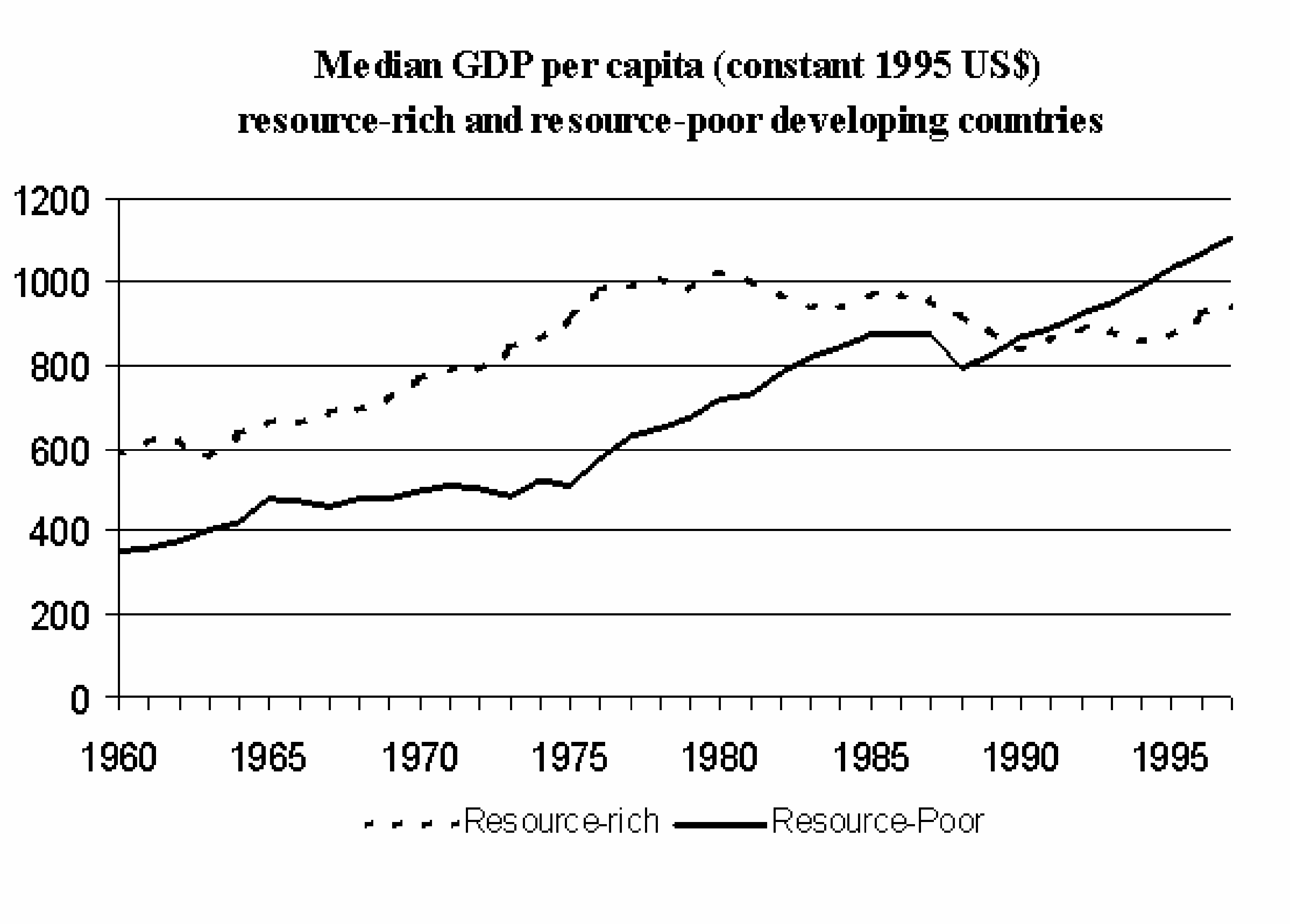
- *Supply diversification -- Russia, Caspian, Iraq, Iran(?)*
  - **Can break the power of OPEC**
  - **Reduce prices**
  - **Deprive "terrorist" states of revenue**
- *None of this makes any sense*
  - **Low prices not in the interests of new, costly, privatized suppliers**
  - **Not enough new volume**
  - **New supplies are more unstable – costly oil, difficult access to world markets, political immaturity Oil policy can't starve "terrorism revenue"**

Conclusions

- The Middle East will increase in importance
- Only Saudi Arabia (with Kuwait and UAE) has the capability of maintaining spare capacity
  - Low cost capacity
  - National oil company
  - Sovereign interest in stability

Oil exporters’ economic development

Oil exports don't foster economic development



“Resource curse”

- Countries with large resource exports
  - Have stifled agriculture and manufacturing sectors
  - Incur massive debt
  - Develop “clients” political systems
    - Gulf
      Venezuela
    - Indonesia – controlled corruption
    - Nigeria -- pervasive corruption

- Why
  - “Dutch disease” raises prices of non-traded factors
  - Rent-seeking corrupts institutions

“Rent seeking”

- **Impact on governance incentives**
  - *Surplus* => no necessity for efficient performance
  - *Sovereign governance* => rent-sharing,
    not maximization of value added
  - *Political “rent-seeking”*
    – participation, procurement, employment, pricing
  - *Personal “rent-seeking”* – “corruption”

- **Leads to**
  - **economic inefficiency**
  - **stultified institutional development**
  - **smothered political and economic growth**

Remedies

- Corporatized and competitive oil company
- Development and non-oil sector independent and competitively financed
- Transparent revenues
- Transparent procurement
- Key international security issue going forward