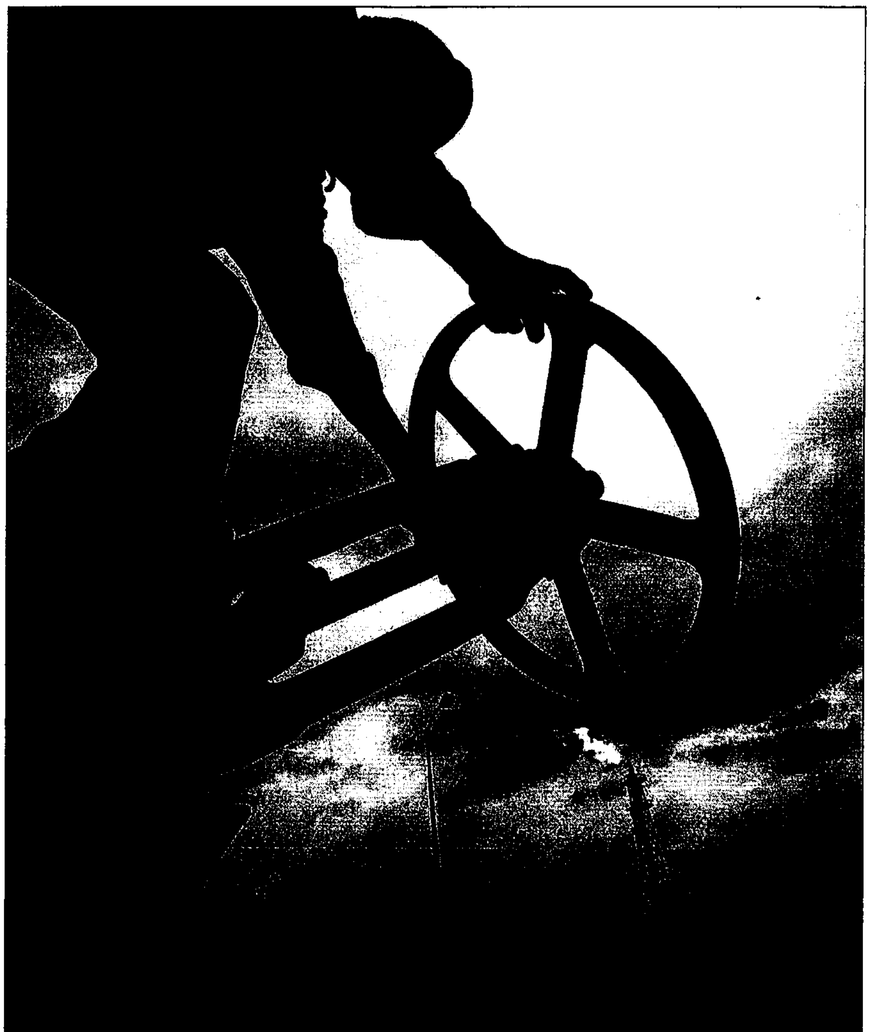
THE WORLD: Restraining Trade

How to Break The OPEC Cartel

BY J. MICHAEL WALLER

With the defeat of Saddam Hussein, the Bush team is taking aim at another entity that plays a prominent role in supporting global terrorism – the OPEC oil cabal.



Open up: *On the supply side, increasing Iraqi oil production to 8 million barrels per day could reduce the cost of a barrel of oil to less than $20.*

KARIM SAHIB/AFP

Oil-producing titans Kuwait, Qatar and Saudi Arabia may have passively helped the United States and its allies to topple Saddam Hussein, but they stabbed Uncle Sam in the back before the gunfire subsided in Baghdad. With the world economy in a slump, they easily could have repaid the United States and others for destroying the threat the Iraqi regime posed to their oil fields and their regimes. Instead, they met in Vienna on April 23 with some of the most notorious state sponsors of terrorism, Iran and Libya, as well as the fanatically anti-Western regime of Hugo Chavez in Venezuela and a vegetable soup of other countries that might or might not be "with us" in the war on terrorism. In what promised to continue a crushing burden upon the working people of their benefactor nations, they agreed sharply to cut back oil production to keep prices artificially high.

That meeting of the member states of the Organization of the Petroleum Exporting Countries (OPEC) brought together an almost-humorous collection of medieval dictatorships and kleptocracies. Weeks before, Saudi Arabia boasted that OPEC's decision to increase production during the war in Iraq helped prevent a spike in oil prices. Indeed, oil analysts say, it did. But the April 23 decision, in effect, declared economic warfare on the rest of the world, including the United States.

With the end of Saddam's regime and the shadow it cast upon much of the oil-producing Middle East, say administration insiders, the United States is reassessing its relationships in the region — particularly with regimes such as Saudi Arabia that financial records show to have been playing both sides in the terrorism war. And with the world evermore conscious about state sponsorship of terrorism, and of how fossil-fuel-dependent countries inadvertently finance such regimes, U.S. policymakers are taking a new, hard look at OPEC as an illegal syndicate in restraint of trade.

Founded in 1960, OPEC's aims, according to its founding statutes, are "the coordination and unification of petroleum policies of the member-countries and the determination of the best means for safeguarding their interests individually and collectively." It was created literally as a cartel or, to use its own words, "The Organization shall devise ways and means of ensuring the stabilization of prices in international oil markets with a view to eliminating harmful and unnecessary fluctuations." Its main "stabilization-of-prices" strategy has been to prevent the free market from keeping prices generally low.

OPEC allies: *Venezuelan strongman Chavez, right, and his oil minister, Rodriguez, center and Kuwaiti oil minister Saud Nasser al-Sabah are all smiles after colluding to manipulate the oil market.*

ANDREW WINNING/REUTERS

The OPEC members control more than three-fourths of the world's proven oil reserves and supply more than 40 percent of the world's oil, according to the U.S. Department of Energy (DOE). The cartel cannot afford to allow prices to rise too sharply, as sustained higher prices would give others greater incentive to develop new oil fields outside OPEC's control. Industry analysts say that OPEC has tried to keep prices at about $25 per barrel since 2000, and that recently the price has been fluctuating between $22 and $28 per barrel — just low enough to discourage other countries from exploiting new fields.

Sen. Charles Grassley (R-Iowa), a longtime critic of OPEC, has sought action against what he calls the cartel's "stranglehold on the U.S. economy." He says OPEC "distorts" the gasoline and diesel market and has had a harmful effect on farmers, truckers and ordinary Americans. Grassley has proposed pressuring OPEC members (see sidebar, p. 26) that receive U.S. military backing and foreign aid. Indonesia and Nigeria are among the recipients of this U.S.-taxpayer assistance; Saudi Arabia, Kuwait and the United Arab Emirates among others are beneficiaries of the U.S. Armed Forces.

Regimes hostile to the United States have sought to use OPEC as a tool of political and economic warfare. The Arab oil embargo of the 1970s caused the first sustained price spike, and the Islamic Republic of Iran has been one of the hard-line members arguing for higher prices. More recently, another anti-American force has arrived on the scene: Venezuelan strongman Hugo Chavez. In 2000, the former paratrooper-turned-president hosted OPEC's first summit in 25 years to strengthen the cartel. He tried to cement OPEC support for his regime by tightly enforcing cartel quotas. Prior to his taking power in 1999, Venezuela was considered a renegade within OPEC, ignoring quotas in an attempt to double production by 2007. But Chavez promised to turn OPEC around and to slash Venezuelan oil production to raise the world market price. In turn, OPEC appointed his oil minister, a former communist guerrilla named Ali Rodriguez Araque, as its secretary-general.

OPEC leaders flatly refused to keep prices down, saying instead that wealthier industrialized nations should cut prices at the pumps by lowering their taxes on energy, while starting a new image-making campaign of its own, pledging to fight to protect the world's environment and safeguard the rights of developing nations. Chavez then worked to develop strategic collusion among the often-fractious OPEC members and to invite independent major oil-producing states such as Angola, Mexico, Norway, Oman and Russia to join the cartel.

"I am one of the many who think that what is happening in Iraq is very dangerous for the world," Chavez told journalists on April 11. He voiced alarm that the successful U.S.-led ouster of Saddam threatened the unity of OPEC. Even more, OPEC is worried that a pro-U.S. Iraq, along with oil producers outside the cartel, might allow world market forces to work by increasing supply and lowering prices. According to a new DOE report, Venezuela's cut in production was keeping post-Saddam prices from "falling too low." Now the OPECers have met once again, like any other band of robber barons, to restrict supply and raise prices.

And this, American strategists say, is the time for the United States to finish off OPEC once and for all. There is no shortage of ways to do it, says John McCormack, head of energy practice at Stern Stewart & Co. in New York. All that's needed, he tells *INSIGHT*, is a strategy and commitment. Some of the options have the added value of denying revenue to state sponsors of terrorism [see "Economic Warfare Can Win Terror War," Nov. 12-25, 2002]. Options

Member States of OPEC

Iran	Libya
Iraq	Indonesia
Kuwait	United Arab Emirates
Saudi Arabia	Algeria
Venezuela	Nigeria
Qatar	

(Source: Saudi Arabian Information Resource)

worth considering include the following:

• **Make it a priority to construct and safeguard a pipeline to deliver Caspian crude oil from Azerbaijan and Kazakhstan on a route that avoids transit through Iran and Russia.** The pipeline, called Baku-Tblisi-Ceyhan, would begin in Azerbaijan, transit Georgia and end in Turkey, strengthening three pro-U.S. countries in the region and undermining the petropower of Iran and Russia. Former national-security adviser Zbigniew Brzezinski and others have been strong proponents of development of Caspian Sea oil and gas, and construction of secure pipelines that would bypass Azerbaijan's large neighbors.

Azerbaijan and Kazakhstan do not coordinate with OPEC, and their immense reserves promise to supply international oil needs for decades to come and help keep prices low. A Muslim state that consistently is friendly toward the United States, Azerbaijan finds itself sandwiched between hostile Russia and Iran and has yet to receive the special treatment that geostrategist Brzezinski and others say it merits. The problem, say industry analysts, is getting the resources to market. Economists such as McCormack, who has worked with many energy companies around the world, offer another reason for avoiding Russia: "stupid Russian oil-company managements."

• **Promote the growing democracy movement in Iran.** Ripe for regime change of a peaceful kind, Iran needs more creative and strategic attention from the United States. Unrest in Iran continues to grow among a population that is considered the most pro-U.S. in the Muslim Middle East. A democratic revolution in Iran would eliminate another terrorist-sponsoring government that keeps power through Western petro dollars.

• **Promote freedom and justice in the rest of the Middle East.** Part of this campaign already is under way with the new Palestinian-Israeli "road map," even though it has little to do with oil per se. However, the United States must start telling the truth about the other regimes in the region, beginning with diplomatic and public-diplomacy efforts to highlight the systematic human-rights violations, institutionalized corruption, support for terrorism and decades of economic warfare against the United States by regimes such as those of Saudi Arabia and Syria. A big question with such an effort is what would come after those regimes.

• **Promote regime change in Venezuela.** As the fifth-largest oil producer, Venezuela is key to U.S. security and vital to OPEC's cohesion. Chavez has broken the independent unions of the state-owned PDVSA oil company and is bringing it under his political control. Purging the senior management of the once-autonomous company, Chavez tapped a longtime confidant, a former communist guerrilla once known as Comandante Fausto, to run the enterprise. Fausto, whose real name is Ali Rodriguez Araque, served as secretary-general of OPEC from 2000 until recently, and has excellent relations with some of OPEC's radical member-states. PDVSA owns the Citgo Petroleum Corp., reported to be the third-largest gasoline supplier in the United States.

• **Quickly ramp up Iraqi oil production.** Modernization of Iraqi oil exploration, refining and shipping facilities will allow the new post-Saddam government in Baghdad to benefit from a huge inflow of hard currency to rebuild the country and boost the economy. A quick recovery and modernization of the Iraqi energy sector, experts reason, would lessen internal political and economic pressures that otherwise would fan militant anti-Americanism in the country. It also would help strengthen the new, pro-U.S. government.

"By far the most effective way would be to encourage Iraq to reach its potential production capacity of 8 million barrels per day versus the 1 million to 1.5 million barrels per day they have done over the past few years," says McCormack. After Saudi Arabia, Iraq has the second-greatest reserves within the cartel, and its oil is among the cheapest in the world to bring to the surface. Iraq might find it in its interest to discontinue coordination with the rest of OPEC.

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10 Ways to Break the OPEC Cartel

Demand Side (reducing consumption of products refined from oil):

1. Impose European-style sales taxes on gasoline, and perhaps also on diesel fuel and home-heating oil. This would cut U.S. consumption by several million barrels per day (bpd). OPEC would find it extremely difficult to cut back production this much and avoid a price collapse. Such a move dramatically would lower the standard of living of most Americans and cause a recession. This is not the way to go.

Supply Side (increasing production of fossil fuels):

2. Help Iraq reach its 8 million bpd production capacity, up from its current 1 million to 1.5 million bpd production. OPEC either would have to let prices go back down to below $20 per barrel or the Saudis would have to cut production and revenues by at least one-half.
3. Provide special tax credits to U.S. companies to develop oil reserves in countries that are not members of OPEC. This would include several in South America, Africa and the former Soviet Union and would both add to supply and reward countries for not joining OPEC.
4. Encourage Canada to reject the Kyoto accords, as Alberta premier Ralph Klein has urged. Such a policy would lift an obstacle to further exploitation of the Alberta oil sands, a virtually unlimited resource geologically (if not economically).
5. Encourage investment in onshore U.S. production by allowing faster cost recovery (perhaps through faster depletion tax credits, the petroleum equivalent of depreciation) in the United States. Such investment would stimulate secondary and tertiary projects in old oil fields. Meanwhile, open the Arctic National Wildlife Refuge oil reserve to environmentally sound development.
6. Encourage more offshore drilling. The federal government could drop royalty percentages in deepwater sites. States such as California and Florida have discouraged development offshore through onerous regulations.
7. Encourage expansion of pipelines bringing oil out of the Caspian region (except for routes through Iran and Russia). Pipeline export capacity probably is the biggest constraint on Caspian exports right now.
8. Put diplomatic weight behind projects to develop oil and gas reserves in those Caspian countries with which the United States has the best relations — Kazakhstan and Azerbaijan. Assist (militarily if necessary) any Caspian countries being bullied by the Iranians or intimidated by the Russians over territorial disputes.
9. Encourage gas-to-liquids projects, perhaps through special tax credits. This technology allows companies to transform natural gas into an especially clean diesel fuel or home-heating oil. It would make some part of the world's natural-gas reserves a substitute for crude oil.
10. Provide major financial inducements for the use of natural gas as a transportation fuel, as President George W. Bush and Energy Secretary Spencer Abraham are trying to do.

— *JMW*