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Libya: Impact of Economic Sanctions

Special National Intelligence Estimate

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LIBYA: IMPACT OF ECONOMIC SANCTIONS

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THE NATIONAL FOREIGN INTELLIGENCE BOARD CONCURS.

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Also Participating:

The Assistant Chief of Staff for Intelligence, Department of the Army

The Director of Naval Intelligence, Department of the Navy

The Assistant Chief of Staff, Intelligence, Department of the Air Force

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SCOPE NOTE

This Special National Intelligence Estimate considers the near-term impact on Libya of the call by the United States for a withdrawal of US citizens from Libya and the possibility of other US economic sanctions. It discusses the economic and political implications of these moves and, where possible, speculates on Libya's likely reaction. In formulating judgments, it takes account of the hostile relationship between the United States and Libya and assumes that successively applied economic sanctions would be played out in an increasingly charged political context.

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KEY JUDGMENTS

None of the unilateral economic levers against Libya available to the United States would have appreciable short- or long-term effects on that country. This judgment applies to sanctions such as withdrawal of personnel, a pullout of operating companies, a blocking of Libyan assets in the United States, a unilateral embargo against imports of Libyan oil, and an embargo of exports to Libya.

If the United States were joined by other countries in imposing comprehensive economic sanctions, Libya's economy would be disrupted within several months. In the longer run, however, even these sanctions—impossible to obtain under current circumstances—would have only a minimal impact.

An effective blockade or quarantine [1] of Libyan ports—which would be legally unprecedented, unlikely to garner the support of the international community, and difficult to implement—would have the most serious disruptive effect on the economy. Libya's basic import requirements could still be met via land and air routes, however. A quarantine would be interpreted as an act of war and would risk major escalation and a broadening of the dispute to involve third parties.

World reaction to US imposition of economic sanctions against Libya would vary according to their severity. In any case, the United States would be unable to obtain West European support and would incur the opposition even of the friendly Arab states. Moscow could utilize the confrontation to enhance its economic and military relationship with Libya.

[1] The term "quarantine" was coined in an attempt to appear less belligerent and to avoid the accepted international legal restrictions on naval "blockades." The difference between the "quarantine" concept and a naval "blockade" was never spelled out, nor has the concept of "quarantine" been applied since the 1962 Cuban missile crisis. It has no precise meaning or standing under international law, and force used in applying a "quarantine" could be justified only if it occurred in legitimate self-defense or pursuant to a United Nations decision taken under the UN Charter. The country subject to a "quarantine" might consider it an act of war.

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DISCUSSION

The Setting

1. Oil is the mainstay of Libya's economy and the ultimate source of its international political and economic influence. Oil revenues account for virtually all export earnings, for half of gross domestic product (GDP), and 85 percent of government revenues. Despite Libya's heavy reliance on oil, it is not especially vulnerable to actions directed against the oil sector. The majority of the country's small population is relatively undemanding in economic terms and has been conditioned by Colonel Qadhafi's chaotic revolutionizing of the private sector to endure prolonged dislocations in the availability of goods and services. The government's grandiose development schemes are largely irrelevant to the life of the average Libyan and cutbacks in spending in this area are not likely to have any serious ramifications. Moreover, Qadhafi's security services and his ability to manipulate internal propaganda would allow him to control domestic reactions to a US economic program directed against him.

2. Libya, which produces a premium crude of high gasoline yield, accounts for about 2.5 percent of oil supplies outside the Communist world. In the current soft market, other suppliers have the potential readily to make up for a loss of Libyan oil.

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also have equity interests in Libya. Production by US companies has recovered from a low of 398,000 barrels a day in September to between 765,000 and 815,000 b/d currently, the result almost entirely of Libya's belated willingness to cut its oil prices. [redacted] is the 25X1 largest single producer, with production currently running 500,000 b/d. As a result of the increase in production [redacted] total Libyan production 25X1 probably is running just under 1.2 million b/d. (See [redacted] 25X1

4. This increase in production, if maintained in the wake of the withdrawal of US personnel, will substantially lessen the cash flow problems Libya has been facing in recent months. Tripoli's current account fell into deficit in July, and despite substantial foreign exchange reserves, cash flow problems began to develop. Tripoli began to delay payments to foreign firms, to cut back on luxury imports, and to trim its ambitious five-year development plan. These cuts had minimal impact on imports in 1981 and net cash outflows peaked at $1.1 billion in October. If imports of goods and services remain at the October level, cash

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outflows will be $500 million by January given the recent increase in oil exports. Foreign official reserves are sufficient to cover this level of outflows for two years.

5. Libya is considering further price discounts of around $0.50 to $1.00 per barrel for January in order to boost production further. It needs a production level of around 1.6 million b/d to meet its current foreign exchange expenditures. With the end of the inventory drawdown and increased worldwide demand for OPEC oil likely to occur in mid-1982, Libya should be able to boost production to its capacity of around 2.0 million b/d if it implements the January price cut.

Economic Sanctions

6. The potential economic levers available to the United States to bring pressure on Libya are:

— The already ordered withdrawal of US personnel in Libya.

— The withdrawal of US oil companies.

— A partial or complete unilateral trade embargo against Libya.

— The blocking of Libyan assets.

— A collective embargo by the United States and its major allies.

— A quarantine or blockade of Libyan imports and exports.

As sanctions became more severe, the greater the impact on Libya; but also greater would be the possibility of escalation and reprisal and of adverse reaction from third parties.

Withdrawal of US Personnel From Libya

7. The vast majority of the [redacted] US citizens estimated to be in Libya during the second week of December 1981 were associated with the oil sector. [redacted] staff of foreign personnel to the Libyan petroleum sector, but most of these technical supervisors and

[redacted]

workers are non-US citizens—largely from Western Europe and Canada. In most cases, Libyan personnel back up this staff. [redacted] Although the overall capability of Libyans does not match in quality that of Western workers, Libyans probably are readily able to substitute for foreign personnel in most daily operational assignments, except for some specialized jobs in areas such as oil well completions. The Libyan National Oil Company itself is one of the largest operators in the country, operating oilfields with a capacity of roughly 500,000 b/d. 25X1

9. The impact of the departure of US personnel will be largely psychological. If a stable work environment is maintained, other foreign workers could be brought in to fill these jobs. Under normal operating conditions, oil companies have some difficulty recruiting and retaining US workers in Libya. Therefore, many of the most important functions are already performed by non-US personnel.

10. Libya has thus far responded to the US call for the withdrawal of US citizens by facilitating their departure. We have no evidence to suggest that the withdrawal is disrupting the work environment or that the Libyan Government is encountering any difficulties in arranging for the replacement of US technicians. Europeans and Canadians appear to be the Libyans' first choice for taking over from Americans. For a variety of reasons, the withdrawal of Americans is likely to take weeks if not months; this should allow the replacement process to proceed relatively smoothly. Moreover, to speed up the process, Libya has waived its visa requirements for third-country workers who will replace outgoing US personnel. 25X1

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Pullout of US Firms

11. Should the US companies be pulled out of Libya, Tripoli initially would have problems maintain-

ing operations, and exports probably could not be brought up to current capacity levels. In the event of a complete pullout by US oil companies, not supported by other governments, Libya would be able to negotiate to substitute European companies as operators or as contractors for a variety of services. US oil company officials believe that French and Italian integrated oil companies have already approached Libya about taking over US-operated oilfields. The Soviet Union and other Bloc countries that provide assistance in other oil-exporting countries such as Iraq could also step in. Among the critical factors influencing foreign oil companies' decisions to replace US firms would be guaranteed access to crude, Libyan oil prices, legal aspects of such turnovers, stability of the work environment, and international political considerations.

12. A shift to non-US companies in the petroleum sector would have its biggest impact in the area of marketing. It can be assumed that the US companies would lose their access to Libyan oil and would not regain their current privileged position. Those foreign companies replacing US firms would not necessarily have the same markets into which to move oil. Given the current world oil market, Libya probably would have to settle on a lower price for its oil unless demand rebounds significantly more than we now expect.

13. On the technical side, as long as Libya can obtain replacement skills and services, it should be able to maintain production at or above current production levels once the initial confusion associated with the pullout were overcome. Even without access to US technical expertise, Libya could maintain a relatively high productive capacity level.

14. Allowing for serious unanticipated problems in a transition period, a worst case for initial operational capacity would be in the range of 1.0-1.4 million b/d. We assign a relatively low probability, however, to this range. In the unlikely event that production were held to this range, Libya would be forced to draw down its foreign exchange reserves and reduce spending on white elephant development projects. Projects and imports that directly affected the daily lives of Libyans could be continued. The last areas to be cut would be military-related expenditures. A more reasonable range for initial capacity would be around 1.4-1.8 million b/d. This level of production is sufficient to cover Libya's current financial requirements.

15. A complete absence of Western support would result in a degradation of capacity over time, but this would not be crippling. One [redacted] estimated 25X1 that if the 1,800 Europeans working for US firms were withdrawn, maximum possible production would be roughly 1.4 million b/d until new foreign workers were brought in. While such estimates are conjectural, they still imply that Libya would be able to increase production about 20 percent above current levels. Denial of Western expertise in areas such as reservoir engineering, development planning, and well-test analysis could result in less than optimal efficiency. But most of the impact of a withdrawal of services would be long-term. The denial would be an inconvenience more related to future development and capacity than to current operational production performance.

16. The foregoing analysis assumes a reasonable technical adjustment but does not incorporate the possible psychological and internal political effects of a withdrawal. Moreover, Libya could face a major problem in the event of serious unanticipated physical damage to critical elements in the petroleum facilities network. US-manufactured equipment and services would be required to expedite repairs in such a contingency.

17. The Libyans value their longstanding relationship with US companies, which they have used as an unofficial means for communicating with US government and industrial leaders and for demonstrating their "friendship" with the American people, if not their government. A US demand that the companies withdraw from Libya would thus be interpreted by the Libyans as a signal of dangerous US intentions toward them—a final break that might be a prelude to more hostile actions. Since such action would have been preceded by the withdrawal of American citizens, the Libyans almost surely would assume that the United States wanted to strip Libya of any "protective" US presence. In such circumstances Colonel Qadhafi might consider a variety of actions, which could include asking for Soviet protection from further US actions, efforts to mobilize a serious anti-US effort among other Arabs, particularly oil producers, and prevailing on European countries to block the US "campaign" against Libya.

18. This reaction might also include expropriation of oil company assets with an estimated replacement value of $2.5 billion. Although current book value is substantially lower—probably less than $900 million—the companies also would lose their equity interests in Libyan oil reserves. The withdrawal of US firms or workers could lead Libya to declare breaches of contracts, enabling it to avoid paying for work already done and to draw down performance bonds posted by US contractors.

19. We do not anticipate that any strong economic actions will be taken by the other Arab producers against the United States as a result of a US Government–ordered withdrawal of US firms. During the recent OPEC meeting in Abu Dhabi, Libya sought an OPEC boycott of American oil and oil-related companies leaving Libya. The Libyan proposal was reportedly supported by the United Arab Emirates, Algeria, Iraq, and Iran. The Saudis argued that the US-Libyan dispute was a political matter and therefore not a legitimate topic for discussion at the OPEC conference. The Saudi position was supported by Kuwait and Qatar. OPEC, however, reportedly is examining the feasibility of providing technical assistance to Libya in the event of a US pullout and, according to press reports, Iran, Kuwait, and the UAE have already offered Libya such assistance. Because of severe manpower limitations, such assistance would be minimal.

A Unilateral US Oil Boycott

20. A US prohibition against imports of Libyan oil is likely to have little economic effect on Libya beyond a short-term disruption of its export patterns. In the event of a US boycott of Libyan oil, Tripoli would seek out alternate oil markets. This could be accomplished rather easily if Libya were willing to lower its oil prices to competitive levels. US efforts to prevent West European countries from purchasing Libyan oil would probably not succeed, given these countries' interest in maintaining their ties with Libya and their reluctance to disrupt their own trade unnecessarily. Provided the price is right, Libya could also find a ready market in the less developed and the Communist countries. Moreover, it would be difficult to prevent Libyan oil from entering the United States through Caribbean oil refineries.

21. Tripoli would respond to a US boycott of Libyan oil by trying to prevent US buyers from replacing the low-sulfur oil with purchases from Algeria, Nigeria, and the North Sea. The Libyans could achieve a fair amount of cooperation from Algeria, a fellow member of the Steadfastness Front. Libya reportedly has already asked Nigeria not to increase production. Nigeria would be eager to increase sales to the United States, but its response would be tempered by the political risks involved in angering Libya and other Arab producers.

22. Libya would play on the fears of Arab and other oil-producing countries in an effort to create a common cause in the face of the US "threat," presumably in hopes of engineering an embargo against the United States. The chances that such a ploy would succeed are slim, but oil producers not normally sympathetic to Libya are nervous at the prospect of revolt on the part of a leading consumer country and might consider applying some kind of leverage against the United States.

An Embargo of US Exports

23. Libya imported $500 million worth of goods from the United States in 1980. This represents less than 5 percent of Libya's total imports. Most of this was machinery and transportation equipment. The US exports nothing to Libya that could not be replaced by imports from other sources. Washington has already banned the export of military equipment and high-technology items with military applications.

24. Oil equipment is available from a wide variety of sources and it is unlikely that a denial of US equipment would cripple Libyan production capabilities. Libya probably could circumvent the sanctions, moreover, and gain access to US equipment. While Libya could turn to European manufacturers for most or all of the equipment needed, it would lose its place in the manufacturers' queue, so that some time delays might be experienced.

Blocking of Libyan Assets

25. Washington has very little leverage over Libya's investment and financial needs. An insignificant amount of Libya's estimated $12 billion in official foreign reserves is in the United States, mostly in

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government securities and short-term bank accounts sufficient to facilitate trade and other financial transactions. As of May 1981, Libya had official foreign reserves of around $15 billion, of which 85 percent—$13.1 billion—was held in foreign exchange accounts. In addition, Libya held $1.7 billion in gold and about $300 million in liquid IMF reserve accounts.

26. We know very little about the location of Libya's official assets outside the United States. We assume about three-fourths are in European and Japanese bank accounts. As occurred in US attempts to block Iranian assets, these banks would be extremely unlikely to join the United States in blocking Libyan assets. Deposits with overseas branches of US banks have been reduced sharply since mid-1981, and Libyan accounts with these banks have occasionally been overdrawn since August.

27. An attempt to block Libyan assets probably would lead to the nationalization of US company assets. A US blocking move, moreover, would probably trigger a storm of protest from US allies and Libya's fellow Arab countries and would reinforce doubts surfaced during the Iranian episode about the reliability of the United States as a safehaven for foreign depositors. Blocking Libyan assets could precipitate some short-term movement of Arab funds from the United States, and would slow future placements.

Multilateral Economic Sanctions

28. Comprehensive economic sanctions involving a trade embargo strictly adhered to, a blocking of Libyan financial assets, and a total embargo of Libyan oil exports would begin to disrupt Libya's economy within several months. International cooperation on such a range of sanctions seems out of the question, however. We need only look at the US efforts to impose sanctions on Iran to find a case history of the difficulties associated with gaining international support for sanctions and of the ease with which such sanctions can be circumvented.

29. A handful of developed countries, led by Italy and West Germany, supply about 36 percent of Libya's imports. As Libya's major source of imported food and other goods in 1980, Italy provided over $2.5 billion or 23 percent of total imports. West Germany, Libya's next largest supplier provided almost $1.3 billion in goods. While trade with individual countries drops off sharply thereafter, the OECD countries as a whole provided over 70 percent of Libya's 1980 imports. The Communist Bloc provided 20 percent, half of which was military goods.

30. Libya probably would be most vulnerable to a disruption in supplies of imported foodstuffs, which provide about 50 percent of domestic consumption.[2] In 1978 the OECD supplied slightly more than 60 percent of total Libyan food imports; Italy was the largest food supplier, providing 16 percent. Other important OECD suppliers were Turkey and Greece. The remainder of Libya's 1978 food imports came from the Communist Bloc—mainly Romania and East Germany—and developing countries.

31. Almost all of Libya's imports of manufactured goods come from the OECD. Italy again is the largest supplier among the OECD 19, having supplied 25 percent of total manufactured goods imported by Libya in 1978. While Libya prefers Western technology, substitutes for many manufactured goods could be obtained from the Communist Bloc. In response to current cash flow problems, Libya has already restricted the import of some luxury consumer goods, including cars, and has postponed some development projects that require imported manufactured goods.

32. Assuming—however unrealistically—that the United States could convince the OECD countries to go along with a trade embargo, we believe the impact on Libya would be minimal. Sanctions would cause delays in the receipt of needed imports, increase the cost and complexity of import trade, and hamper economic development. Trade sanctions would entail little belt tightening in the short run, however, if food were excluded from the embargo—as has traditionally been done for humanitarian reasons when sanctions have been imposed on other countries. An embargo of manufactured goods could serve to relieve Tripoli of the responsibility for shortages and delayed development plans, shifting the focus of any popular discontent to foreign powers.

33. Furthermore, after some initial confusion and delay, Libya should be able to overcome the sanctions. It could turn to Third World countries to act as third-

[2] The latest comprehensive data available are for 1978, but no major shifts in trade patterns have occurred.

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party purchasers of Western goods. The altering of ship manifests is another easy means of circumventing trade sanctions. In addition, the Libyans would readily turn to Soviet Bloc countries for help in overcoming sanctions.

34. Widespread West European support of a Libyan oil boycott would severely limit Libya's short-term ability to export oil. It is highly unlikely, however, that a significant number of Libya's West European trading partners could be convinced to join such a boycott; probably the most that could be expected would be a general agreement to discourage such imports.

35. Even in the event of a boycott, Libya could find other markets for its crude, particularly if it further lowers its price. Libya could increase direct sales to developing countries and to some East European countries. Alternatively, it could have these countries act as intermediaries in marketing Libyan crude in the West, as the Soviets and others have done in the past.

36. Because relatively large volumes of high-quality Libyan crude would be easily identifiable, however, Tripoli would have to arrange to refine much of the crude to disguise its origins and circumvent a boycott. Sufficient excess refinery capacity currently exists in a number of developing countries, notably the Caribbean, and in Eastern Europe to carry out such arrangements. Several of the OPEC countries might even be willing to assist Libya in such refining and marketing arrangements.

Military Quarantine/Blockade

37. An effective maritime quarantine [3] of Libyan ports would have the most serious disruptive effect on the economy. Libya probably could import basic requirements by air and through established highway links with Algeria, Tunisia, and other neighboring countries. Such an action by the United States would, however, be unprecedented and would require justification beyond the legal rationale used during the Cuban quarantine of 1962. During the Cuban missile crisis, the United States had photographic evidence that Soviet offensive missiles had been introduced, thereby enabling it to garner the backing of the Organization of American States for the maritime action. The current Libyan situation lacks both hard evidence of a significant offensive threat to the United States and support by the international community.

38. The establishment of a US naval quarantine, moreover, would pose a significant challenge for US naval forces; the 6th Fleet has already been reduced in order to meet Arabian Sea commitments. If sufficient forces were made available, the Navy could detect and intercept virtually all Libya-bound merchant ships as they approached Libyan ports. In the event of a naval quarantine, US and Libyan units would be operating in close proximity, and we could anticipate a hostile engagement, with the potential for subsequent air and naval attacks by either side.

39. Although a quarantine would have the greatest impact on Libya's economy, it would be interpreted as an act of war and is the most likely of the options to result in a broadening of the dispute to third parties. In response to a blockade, the USSR could augment its naval forces in the Mediterranean, provide the Libyans with information on US naval activity, and use Soviet vessels to trail and intermingle with US combatants. It is possible that some Soviet ships would enter Libyan waters or visit Libyan ports, or that Soviet reconnaissance or combat aircraft would deploy to Libya. This activity would serve Moscow's efforts to deter the United States by keeping it uncertain of Soviet intentions. Moreover, if the Soviets were willing to risk direct confrontation with the United States, they could attempt to escort Soviet or Warsaw Pact merchant ships through the blockade.

Political Repercussions

Regional Reactions

40. The Qadhafi regime is attempting to exploit the US-Libyan confrontation to rally support. It will use the United States as a scapegoat for any economic dislocations, and direct popular anger against Washington. The success of this tactic will depend on the severity of the US actions. Should sanctions against Libya progress to quarantine—let alone a military strike—the result will be the generation of significantly greater popular support for what is, at this point, an increasingly unpopular regime.

[3] This Estimate does not consider the impact of an overall air blockage, as the extensive military activity requisite to implementing such a move places it outside the sphere of economic sanctions.

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41. Most measures short of these extremes, however, may fail to elicit much response unless Qadhafi pulls out all propaganda stops and whips up anti-US sentiment. It is possible that some of the milder US options could stir up resentment among the Libyan people toward Qadhafi and his policies for having brought the country to such a pass. It is more likely that only those already opposed to Qadhafi—the remnants of the better informed, sophisticated middle classes, who have suffered most from his "reforms"—will react in this fashion.

42. Most of the proposed US moves, even the mild ones already undertaken, will generate some criticism on the part of friendly Arab states—particularly oil producers. As the US moves grow more severe, criticism will sharpen. Saudi Arabia has already demonstrated uneasiness at the prospect of a potential consumer boycott against an OPEC state, however unpopular, viewing it as a dangerous precedent. Blocking Libyan assets would make all the oil producers extremely nervous, complicating relations not only with the Saudis but also with the Algerians. The oil states never approved of the US blocking of Iranian assets, even though provocation was clear. The reaction would be even sharper in the case of Libya, a fellow Arab state, against which the US case is not clear. Indeed, in many quarters the confrontation is perceived as one of a superpower bullying a small, defenseless country.

43. Although many friendly Arab states would like to see Qadhafi vanish from the scene, they view the current highly publicized US campaign against a fellow Arab state as serving to strengthen the radical Arab bloc, engender anti-US sentiment within a broad Arab constituency, and seriously complicate efforts to be cooperative with the United States on far more important security issues. The friendly Arabs' predicament would be significantly intensified now that US moves against Libya would follow on the heels of the Israeli annexation of the Golan Heights.

44. Virtually all regional states would view the US moves, particularly any steps beyond those already taken, as a prelude to military action. One recipient of the fallout would be Egypt, which would be perceived as in collusion with Washington—adding a further burden to the Camp David process. The Syrians especially will seek to rally Arab support for Libya and probably will offer Qadhafi military aid and troops.

Importers of Libyan Oil
(1,000 barrels a day)

	1980	Fourth Quarter 1981 (estimated)
Total	**1,735**	**710-815**
United States	715	150
Western Europe	895	515
West Germany	310	150
Italy	250	105
Spain	95	65
Turkey	45	100
France	40	40
Switzerland	20	25
Greece	55	15
Austria	20	15
Other	60	—
Other countries	125	45-150

West European Response

45. The major West European allies have been trying in recent months to improve their relations with Libya, and have resisted US requests for more stringent restrictions on sales other than weapons. They are not likely to cooperate with further restrictions because they see no overriding political reason to change their policies and damage their energy and other commercial interests. In fact, they believe that political imperatives point the other way: although they see Qadhafi as influenced by the Soviets, they believe that Libya would be more dangerous if it were isolated from the West and "forced" into the Soviet Bloc. If an effort were made to blockade imports and/or exports to Libya, not only would the allies decline to cooperate, but they also would protest vehemently a policy that would strike at their own commerce. [redacted] 25X1 Unless the Libyans initiate some violent and apparently unprovoked action, the increased tensions between the United States and Libya are unlikely to alter the desire of the allies for a more stable relationship with Libya.

The Soviet Perspective

46. No matter what the eventual mix of US economic pressures on Libya, the USSR will point to it as "imperialist" bullying of a Third World nation and will attempt to exploit the tensions to increase its influence in Tripoli. The Soviets would readily respond to Libyan requests for economic assistance in overcoming sanctions. Their assistance, however, would be more

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symbolic than real. The USSR's grain shortage would prevent it from helping Libya much in the area where it would be hurt most by a complete trade embargo—food supplies. Moscow could mount a highly publicized "relief mission" designed to portray the USSR as a reliable friend in a time of need. It also would be likely to sign new economic agreements with Tripoli, possibly providing for Soviet technicians and machinery to be sent to assist in the Libyan oil sector. In return for whatever aid they provided, the Soviets would attempt to encourage Libya to supply oil on a barter basis to their East European allies.

47. If Washington should attempt to impose a quarantine on Libya, Moscow would try to avoid a military confrontation with the United States. Moscow would concentrate its efforts on providing political and diplomatic support to Tripoli and would seek to orchestrate widespread international condemnation of the US action—particularly in Western Europe and the Third World.

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