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**Secret**

# *The Current State of the Arab Oil Embargo*

State Department review completed

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## The Current State of the Arab Oil Embargo

### Summary

1. Arab oil ministers meeting in Kuwait last night announced a 25% production cutback based on September's production figures. Saudi Arabia and Kuwait, with the 10% limitation announced in mid-October and the additional embargoes of shipments to the United States and the Netherlands, had already reached the 25% level, and the new formulation appears to strengthen King Faysal's leadership role by committing the other producers to match his cutback. The move may be designed to bring countries such as Libya, Algeria, and Iraq, which have not been rigorously enforcing the earlier limitation, into line. If adhered to, it will increase the overall Arab cutback in November by 5% over that already in effect. Saudi Arabia and Kuwait, which account for 60% of Arab oil exports, had been holding firm. There had been some shippage in Algeria, Libya, Abu Dhabi, and possibly Iraq. The rest of the world's oil-producing countries are expanding their production at normal rates.

2. Arab oil exports have been cut from a mid-October level of 19.5 million barrels per day (b/d) to about 15 million b/d. By the end of November, the net loss of Arab oil exports to the United States, Western Europe, and Japan will be (in million b/d) 2.1, 1.4, and 0.5, respectively. This would amount to 12% of US consumption, 8% of Western Europe's, and 9% of Japan's. Because of the vast amounts of oil already on the high seas, however, the full impact on the consumers will be delayed several weeks.

3. Prior to the 4 November announcement, some Arab countries were not implementing the cutbacks rigorously. We cannot be certain how the announcement will change their implementation.

- Abu Dhabi is enforcing an embargo against the United States and the Netherlands, but has not cut production.
- Algeria's cutbacks appear to have been forced by technical problems in the producing fields, rather than by political decisions.
- Iraq, the only major Arab producer not signing the Kuwait agreement to reduce production, has cut back only because of pipeline problems.
- Libya is loosely interpreting the 5% cut and is not rigorously enforcing the embargo.

25X1 4. Although the major oil companies are taking measures to spread the impact of the Arab actions, all consuming nations will be hard hit if the cutbacks continue for some months and especially if they are increased beyond the present schedule.

25X1 Note: Comments and queries regarding this publication are welcomed. They may be directed to [redacted] of the Office of Economic Research, [redacted]



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The United States and the Netherlands have been embargoed by most Arab producers, and will – at least in theory – receive no Arab oil once the shipments already at sea are delivered. A number of nations, mostly in the Third World but also including France, Spain, and the United Kingdom, are considered friends of the Arabs and have been promised supplies equal to their average imports during the first nine months of this year. No mechanism has been set up to implement this policy, however, and these countries apparently will have to forgo any increases in imports to meet growing consumption needs. Most other countries, including such important consumers as West Germany, Italy, Japan, and Canada, will have their Arab oil imports cut by roughly the amount of Arab production cutbacks.

5. The reaction of most of the major consuming countries has been to assume a low profile and try to cut their losses without alienating either the Arabs or the United States.

- West Germany is preparing an emergency rationing bill and is pressing for measures to share the shortage among members of the European Community.

- The Netherlands is restricting oil exports and limiting nonessential use of automobiles. The Hague is also pushing for a Europe-wide oil-sharing plan.

- France, presently favored by some Arab producers, is resisting most moves toward intra-European sharing of available oil.

- The United Kingdom, also favored by some Arabs, hopes to obtain a degree of consumer country cooperation while expanding diplomatic contacts with the Arab producers.

- Japan hopes to improve its position by making cautious moves toward the Arab camp.

6. The chances of an early end to the embargo are slight. King Faysal is continuing to take a very tough stand, and Kuwait will likely follow his lead. Most countries of Western Europe as well as Japan and Canada are under increasing pressure to take pronounced pro-Arab stands. The United States, because of its domestic production and its potential for obtaining savings from its relatively large amount of nonessential energy consumption, is in a somewhat better position than most other major consumers. Nevertheless, the US import shortfall could reach 2.5 million b/d – 13% of consumption – by mid-winter.

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Discussion

**Implementing the Cutbacks**

7. While no Arab oil producer will ignore the decisions by the Organization of Arab Petroleum Exporting Countries (OAPEC) to reduce production progressively, some are more committed than others to making the cutback work. For various reasons, the vocally radical states – Libya, Iraq, and Algeria – are supporting the program with much less energy than states such as Saudi Arabia and Kuwait. [redacted]

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**Worldwide Impact**

***The United States***

9. We estimate that by mid-winter the US oil import deficit will be running at about 2.5 million b/d if the cutbacks and embargoes are

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reasonably strictly enforced. The United States will be short about 1 million b/d of crude oil and 1.5 million b/d of products, mostly heating oil. Even if the United States were able to obtain enough non-Arab crude oil to keep its domestic refineries running at capacity, it is highly unlikely that anything like the volume of products needed to make up the deficit could be imported. Western Europe not only will be unable to supply us with products, but also will be competing vigorously with the United States for the output of Caribbean refineries.

10. Recent Canadian actions are worrisome because the United States can no longer depend on Canada for the full amount of its usual imports of 1.2 million b/d of crude oil. Even before the Arab-Israeli war, Canada feared an energy shortfall and had restricted exports of certain petroleum products. Now, Ottawa apparently plans to make up east Canadian supply shortfalls caused by the Arab-Israeli war and its aftermath by diverting some west Canadian oil that would normally be exported to the US market. Canadian plans, however, will be hampered by a lack of a transcontinental pipeline, a shortage of railroad tankcars, and the winter freezeup of the Great Lakes and the Saint Lawrence. Given all of these difficulties, Canada probably will not be able to divert more than 200,000 b/d of crude to its eastern provinces. The estimates in Table 1 assume that the United States loses all of its inputs of products from eastern Canada – nearly 200,000 b/d.

11. The United States can offset some of the effects of the shortfall by opening up the Elk Hills naval reserve and encouraging surge production elsewhere, by drawing down stocks at a faster than normal winter rate, and by taking measures to reduce demand. Elk Hills and surge production would soon yield 250,000 b/d and eventually 500,000 b/d. Although the country has 500 million barrels of available stocks[1] – the equivalent of

**Table 1**

**United States: Estimated Oil Supply and Demand**
**Winter 1973/74**

| | Million Barrels per Day |
|---|---|
| Demand | 19.0 |
| Total supply | 16.5 |
| Domestic production | 11.1 |
| Crude oil | 9.3 |
| Natural gas liquids | 1.8 |
| Non-Arab imports | 4.4 |
| Normal winter stock drawdown | 1.0 |
| **Potential supply deficit** | **2.5** |

1. According to the American Petroleum Institute, which receives periodic reports from all US oil companies, US crude oil and product stocks were 850 million barrels on 5 October. We have adjusted this figure downward to 500 million barrels to arrive at an estimate of usable stocks.

80 days of imports from all sources and 240 days of imports from Arab sources – the product breakdown and geographical distribution of these stocks will prevent their full utilization. During a normal winter, stocks are drawn down at a rate of about 1 million b/d. Doubtless this rate could be increased substantially, but we have no basis on which to make an estimate. There are a variety of ways of reducing energy demand, which if very rigorously enforced, some US officials believe might save the equivalent of 2 million b/d or more. Despite demand reduction and stock drawdowns, the Northeast and Midwest will probably be moderately hard hit this winter. Local shortages around the country could be severe.

### *Other Consumers*

12. Unlike the United States, which has already lost all of its Arab oil supply, Western Europe and Japan will continue to be hurt by additional Arab cutbacks. The timing of the Arab cutback hit Europe and Japan at a most inopportune time. Western Europe consumes about 30% more oil in winter than in summer. Japan's seasonal boost in demand is about 15%. This swing in demand is more pronounced than in the United States. Western Europe and Japan normally meet their high winter demand by stock drawdowns as well as increased imports.

#### *Western Europe*

13. By mid-winter the West European deficit will be on the order of 3 million b/d – about 15% of consumption. Individual countries will be affected differently, with the Netherlands likely to be hardest hit if the selective embargo is not circumvented. West Germany, which receives nearly 20% of its oil supply through Rotterdam, will also be seriously affected. The Europeans can lessen the impact by drawing down stocks built up earlier for just such a contingency and by reducing demand. We estimate that Western Europe has about 880 million barrels of available stocks which we calculate are the equivalent of 55 days of imports from all sources and about 80 days of imports from Arab sources. Europe's stock drawdown in a normal winter is probably larger than in the United States, perhaps 1.5 million b/d. However, Western Europe's capability for reducing demand is probably much less than that of the United States. Western Europe consumes only 20% of its oil as gasoline, compared with 45% in the United States. Despite demand reduction and extra large stock drawdowns, Western Europe probably will have shortages this winter – some of which will doubtless be severe.

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Table 2

**Western Europe: Estimated Oil Supply and Demand**
**Winter 1973/74**

| | Million Barrels per Day |
|---|---|
| Demand | 19.5 |
| Total supply | 16.5 |
| Domestic production | 0.4 |
| Imports | |
| Arab | 10.1 |
| Non-Arab | 4.5 |
| Normal winter stock drawdown | 1.5 |
| **Potential supply deficit** | **3.0** |

*Japan*

14. Japan stands to lose roughly 500,000 b/d of oil imports, or about 9% of consumption, as a result of the initial Arab cutback. The major international oil firms, which supply most of Japan's oil, have already notified Tokyo of impending delivery cuts, and Gulf Oil, which supplies about 10% of Japan's imports, will reduce shipments from Kuwait by 35% retroactive to 1 October. We believe that Japan's import losses by mid-winter will be nearly 15% of consumption, assuming further Arab cutbacks of 5% per month after November.

15. For the moment, Japan's supply situtation is good, and refineries are operating normally. Stocks are now about 280 million barrels -- a 50-day supply. Partly because of the 20 days it takes to move Persian Gulf oil to Japan, the flow of crude oil has not yet been affected.

16. Japan can stave off any serious impact on economic activity for many months by drawing on stocks. Even with continuing Arab cutbacks, present consumption levels could be maintained well into early summer before stocks would be depleted. If consumption were constrained 10% by rationing, the Japanese could maintain this reduced rate of consumption for several additional months However, severe shortages could occur in coming months in some areas and in some sectors of the economy because of the mix of stocks and distribution problems.

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**Table 3**

**Japan: Estimated Oil Supply and Demand**
**Winter 1973/74**

| | Million Barrels per Day |
|---|---|
| Demand | 6.2 |
| Total supply | 5.4 |
| Imports | |
| Arab | 1.8 |
| Non-Arab | 3.3 |
| Normal winter stock drawdown | 0.3 |
| **Potential supply deficit** | **0.8** |

## Foreign Consumer Country Reactions

### *European Community*

17. The Arab policy of hitting some EC countries harder than others works against an early and effective EC effort to combat the oil crisis. There are signs, however, that pressures for a more united response are building. Thus far the EC has agreed only to establish a unified reporting system covering exports and stock levels. The Netherlands, singled out for an embargo by some Arab states, has requested urgent consideration of its oil situation at this week's Council of Ministers meeting and is pressing for Community-wide action on oil sharing and demand reduction. Because of their dependence on Dutch refineries, West Germany and Belgium may side with The Hague on pooling supplies. However, the French and British who have been singled out by the Arabs for favorable treatment, plus the Italians who would like to be, will resist such action, fearing that it might spark new Arab cutbacks.

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19. An emergency rationing bill had already been prepared and will probably soon be submitted to the Bundestag for priority treatment. With about 65 days of stocks on hand, the country will probably impose at least limited rationing, but will be able to make it through a normal winter without great difficulty.

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*United Kingdom*

20. The United Kingdom has been given assurances by some Arab producing countries that it will continue to receive oil in the same quantities as during the first nine months of 1973. Even so, London is preparing contingency plans and implementing regulations designed to prevent or to limit the effects of shortages. For example, a set of controls on exports of crude oil and oil products to non- EC countries, effective 12 November, will limit export volume to the November-December levels of 1972. If, within this limitation, UK companies continue to supply regular customers in Scandinavia, little will be left for export to the United States.

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*Netherlands*

22. An Arab embargo of the Netherlands threatens to reduce Dutch crude oil imports by 70%. State Secretary Kooijmans told the US Embassy that Arab threats and pressures on the Dutch would be counter-productive and that the Netherlands would not change its Middle East policy even if it meant doing without oil.

23. Exports to EC countries have continued thus far, but exports to the United States, Norway, and Sweden have been curtailed. The government has also been given powers to introduce rationing. The petroleum industry has been instructed to reduce the distribution of kerosine, heating oil, and fuel oil by about 10%. Pleasure driving on Sundays is now prohibited. The government has also called on the public to exercise economy in its use of gasoline and electricity. The Netherlands, with 65 days of oil stocks on hand, should be able to weather the oil embargo for several months.

*Japan*

24. Tokyo is under increasing pressure to abandon its neutral stance on the Middle East in favor of open support for the Arabs. Vice Foreign Minister Hogen, hoping that a political settlement can be arranged before the country's oil supply situation becomes tight, has thus far held to the line that Japan should not go beyond supporting Security Council

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Resolution 242. The goverment may face a major policy decision by late November, however, in view of the Arab's announced intention to make further cuts in the oil supply.

25. Japanese diplomats have already offered to underwrite previously rejected aid projects in Arab countries, and a new soft line on Egyptian debt rescheduling is being considered. A Japanese Foreign Ministry official has told the US Embassy, however, that working-level officials do not believe such representations will be sufficient to restore oil deliveries to previous levels. Consideration is now being given to sending International Trade Minister Nakasone, or even Prime Minister Tanaka, to visit Arab capitals if the Middle East situation has not improved by December. The working-level officials envision that such a trip might be accompanied by a drastic change in Japan's Middle East policy, possibly including a break in diplomatic relations with Israel. Thus far, senior Foreign Ministry officials have talked to the US Embassy only about Arab demands that Japan support them on the territorial issue.

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