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MEMORANDUM FOR: The Honorable Henry A. Kissinger
The Secretary of State

I believe you will find the attached Briefing Book useful in preparing for the 11 February Energy Conference.

Bill

W. E. Colby
Director

State Department review completed

MORI/CDF per C02912223 PAGES 2 & 4-132 PER C02912223

Attachment:
ER IB 74-3

4 FEB 1974
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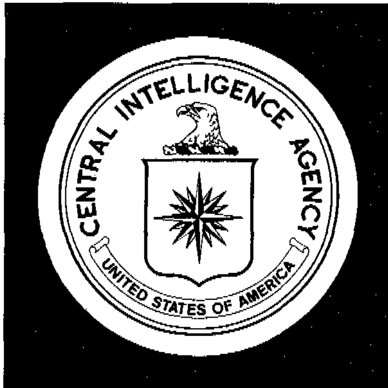

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A Briefing Book for The Washington Energy Conference

11 February 1974

State Department review completed

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ER IB 74-3
4 February 1974

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A BRIEFING BOOK FOR THE WASHINGTON ENERGY CONFERENCE

OVERVIEW

Most consumer countries will come to the Washington conference with a positive attitude toward some form of international cooperation on energy matters. Although some consumers have joined in the race to make bilateral deals with oil producers, they still support cooperation regarding oil prices and other issues. Even the Japanese, who are highly cautious toward joint consumer action, now believe that some form of cooperation between exporting and importing countries on oil prices is desirable.

The more receptive attitude toward cooperation that has developed recently does not mean that foreign participants will necessarily follow US initiatives. Still too shaken by recent events to risk antagonizing the oil-exporting countries, these representatives will avoid provocative words or actions. Some countries, notably France, will resist making any commitments on major policy issues.

Several countries believe that a Washington-led group is not the best forum for consumer cooperation. They view the Washington meeting only as an opportunity to exchange ideas and believe that the thornier problems will have to be hashed out at a consumer-producer conference. The French, unwilling to support any initiative that may strengthen US influence in Western Europe, have suggested a UN-sponsored world conference to deflect attention from the US-sponsored meeting. Several EC countries oppose this suggestion, preferring to avoid the bureaucratic clutches of the United Nations. Nevertheless, most countries would like to see either the Washington conference group or an OECD group of consumers join together with oil producers and representatives of the less developed countries to decide major policy issues.

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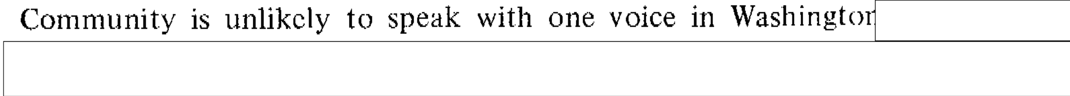
The European Community -- to be represented at Washington by EC Commission President Ortoli and by West German Foreign Minister Scheel, who is the current president of the EC Council -- has been unable to develop a common energy policy. Because disagreements among members probably will not be resolved at the 4-5 February meeting of the EC Council, the Community is unlikely to speak with one voice in Washington



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The EC Commission itself has long advocated consumer cooperation.

Several of the West European participants will favor cooperative action to make oil supplies more secure. The Netherlands, still embargoed and with little hope of arranging bilateral deals with Arab states, is likely to push hardest for a united consumer front on the matter of assuring adequate oil supplies. West Germany has been visibly irritated by its EC partners' unwillingness to cooperate in solving energy problems and will come to Washington hoping to find a common course of action. Other countries that are unable to compete with the major industrial nations in making bilateral agreements also will support cooperation in obtaining supplies.

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Most of the participants in the energy conference will favor discussion of a new oil pricing system and a non-provocative attempt to roll back the recent large price increases. For instance, most consumers would endorse a public statement emphasizing the potential of higher oil prices to cause a worldwide depression, damaging producers and LDCs as well as major consumers. Japan and several other countries favor postponing substantive work on a new oil pricing system until a joint consumer-producer task force can be formed.

Nearly all conference participants will favor discussion of oil company profits and of ways to channel massive Arab dollar holdings to consumer countries. All consumers, even the recalcitrant French and Japanese and the energy-rich Canadians and Norwegians, support cooperation in the development of new energy sources, in sharing energy technology, and in fostering energy conservation.

Although few countries now expect serious oil supply constraints, the extraordinary October and December oil price increases provide considerable motivation for international cooperation. The oil price increases will add between $2 billion and $6 billion to the import bills of most consumer countries. For Japan, the increase is $11 billion, threatening the first trade deficit in a decade. Because of the deterioration in their trade accounts, the main consumer nations now face large current account deficits in 1974 instead of the near balance most were forecasting in October (see Table 2).

Table 2

Changed Outlook for the Trade and Current Account Balances in 1974[1]

Billion US $

	Increase in Oil Import Bill	Trade Balance		Current Account	
	January 1974	October 1973	January 1974	October 1973	January 1974
Japan	11	5 to 7	-3 to 0	1 to 3	-7 to -4
West Germany	5½ to 6	10 to 12	7 to 8	3 to 4	0
France	5½	2	-3	0	-4
United Kingdom	5	-3½ to -2½	-9	-2 to 0	-7
Italy	4	-3	-7 to -6½	-1½	-5½
Netherlands	2	N.A.	N.A.	1	-½
Canada	2	2	1 to 1¼	-½	-1
Norway	¼ to ½	N.A.	N.A.	-½	-1

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The oil price increases also will slow economic growth and intensify inflation. The industrial nations were expecting slower growth and accelerating price increases in 1974 even before oil prices rose. With consumers facing the choice of curtailing living standards or escalating their wage demands to offset higher fuel bills, 1974 prospects for growth and prices are much dimmer now than before the oil crisis (see Table 3). Japan will be hard hit. The oil price increases will contribute to an expected 17% increase in consumer prices and to a decline in the economic growth rate to only about 4%, as against the 9% forecast earlier. The United Kingdom will come close to matching the Japanese rise in consumer prices and will probably experience a decline in overall output.

Table 3

Changed Outlook for Economic Growth and Inflation Rates in 1974[1]

Annual Growth Rates in Percent

	Economic Growth		Consumer Prices	
	October 1973	January 1974	October 1973	January 1974
Japan	9	3 to 4	10	17
West Germany	3½	0 to 2	6	10
France	5½	4	8	12
United Kingdom	3½	-2	12	15
Italy	6	1 to 2	8	15
Canada	5	3 to 4	8	10
Netherlands	4½	1	5	14
Norway	5½	4	7	10

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Canada

Background

Before the oil crisis, slackening consumer expenditures and export earnings were expected to reduce Canada's growth from 6-1/2% in 1973 to a more normal 5% in 1974. The Arab oil restrictions, which cut oil imports going to eastern Canada by an estimated 75,000 b/d (or 8%) in October-December, did not dampen this outlook. The loss in imports is being more than made up by 100,000-b/d shipments of west Canadian crude oil via the St. Lawrence River or the Panama Canal.

Current Outlook for Oil Supply and Costs

For the five importing provinces of eastern Canada, the oil problem is a matter of soaring cost, not physical shortages. For the three western producing provinces, the oil problem is a matter of the extent of domestic price controls and tax measures. For the nation as a whole, the oil problem raises serious issues of inter-provincial relations.

The staggering OPEC price increase will boost eastern Canada's crude oil import bill by $1.8 billion to a total of $3.1 billion in 1974 -- an increase equal to about 3% of total personal consumption expenditure in the five provinces. Even if the Arab supply restrictions are eased later this year, seaborne shipments of west Canadian oil will remain economic at the higher world prices and probably will be continued at about the present level. This will help to reduce demand for imported oil to 800,000 - 850,000 b/d for the remainder of 1974, compared with about 900,000 b/d in 1973.

Economic Prospects for 1974

While political difficulties over sharing of the cost of the OPEC price increase remain, Ottawa is successfully meeting the direct economic problem. Potential balance-of-payments strains in 1974 were averted by slapping on an oil export tax, which has raised the price charged US customers to approximately the OPEC level. Although the government has not yet decided what combination of domestic price and export tax should be established for the full year, the export price almost certainly will be kept near the OPEC price. Canadian oil export earnings would thus jump by about $1.8 billion to $3.5 billion -- an increase equal to the estimated rise in the oil import bill.

The Canadian economy still will be adversely affected by the price hikes. Ottawa plans to avoid the depressive effect of higher oil prices on

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the east Canadian economy by using the export tax proceeds to limit the rise in consumer prices for oil products. Nevertheless, the impact of the price hike on Canada's foreign customers -- especially the United States -- will hurt demand for Canadian exports, probably widen the current payments deficit a little, and possibly slow Canada's investment boom. Real economic growth in 1974 probably will not exceed 4%, and unemployment may rise from 5-1/2% in 1973 to 6% in 1974. Higher oil prices will increase the inflation rate to perhaps 10%, compared with 9% last year.

Positions on International Cooperation

Despite Canada's positive response to the US initiative, Trudeau's minority government will be reluctant to commit itself to any comprehensive consumer nation scheme for global or continental energy cooperation. Ottawa is prepared to discuss such cooperation on a case-by-case basis but will drive a hard bargain because of Canada's still favorable oil situation.

The most important influence on Ottawa's position is the necessity of ensuring that domestic energy resources first meet Canada's present and future needs before any international commitments are undertaken. With the strong rise of Canadian nationalism in recent years, Prime Minister Trudeau must move circumspectly. Above all, he would be unable to join in any agreement that left him vulnerable to charges that other nations are dictating the development and use of Canadian energy resources. The urge to act independently is tempered by recognition of Canada's close economic interdependence with the United States and its need for a healthy US economy to maintain its own prosperity.

As an energy-rich but capital-importing nation, Canada would be interested in proposals by the other conference participants on sharing of the costs of energy research and development. External Affairs Minister Sharp views such cost-sharing as an opportunity for involving oil-producing countries so as to avoid limiting cooperation to the consuming countries. The Trudeau government has hinted that it would be willing to consider creation of an international consortium -- controlled by Ottawa -- to develop the Alberta tar sands. Under such a scheme, consortium investors would provide the financial resources and be repaid in crude oil. The Trudeau government also has taken a strong stand in favor of the proposed MacKenzie Valley pipeline, which would transport natural gas from the Canadian Arctic and Alaska to US and Canadian markets.

Although Ottawa has recently announced plans -- including extension of the Alberta-Ontario pipeline to Montreal -- to achieve self-sufficiency in oil, eastern Canada will remain partly dependent on oil imports for some

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years to come. Consequently, the Trudeau government should be strongly interested in an international agreement to assure oil supplies to consumer nations. While the Canadians have not been directly hurt by skyrocketing oil prices, they are concerned about the worldwide economic impact. Ottawa might tacitly favor cooperative action to obtain a price rollback but would be hesitant to adopt a strong stand because of the desire to remain neutral in the Middle East conflict.

Canada: Energy Data

	Primary Energy Consumption by Source (Percent)	Consumption as a Percent of Domestic Production
Total	**100**	82
Oil	45	87
Natural gas	20	57
Coal	10	129
Hydro/nuclear	25	99

	Pattern of Energy Consumption (Percent)
Total	**100**
Transport	24
Households	20
Manufacturing	38
Commerce	14
Other	4

	Oil Trade 1973 (est.)	
	Thousand b/d	Percent
Total exports (all to the United States)	**1,260**	....
Total imports	**1,000**	**100**
Arab	220	22
Saudi Arabia	80	8
Abu Dhabi	60	6
Other Arab	80	8
Iran	180	18
Venezuela	470	47
Nigeria	80	8
Others	50	5

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West Germany

Background

Before the Arab oil supply cutbacks, West Germany's main concern was cooling off the overheated economy. As the rate of inflation approached 8% last spring, the government imposed restrictive policies that began to bite by September. Forecasts made prior to the oil crisis anticipated a slowing of economic growth from about 6% in 1973 to between 3% and 4% in 1974. Unemployment was expected to grow from 1% to 2% of the labor force. Most observers foresaw the trade surplus declining from an expected $15 billion in 1973 to between $10 billion and $12 billion in 1974 under the impact of continued appreciation of the mark and slower economic growth abroad.

Following the Arab announcements of restrictions on oil supply, German officials were very pessimistic about the energy situation, in part because of the country's heavy dependence on the embargoed port of Rotterdam. Early forecasts projected an oil supply shortfall of 20%-25% by the end of December.

On 9 November the Parliament gave the government emergency powers to impose conservation measures. The initial measures included reduced speed limits, a driving ban for the four Sundays before Christmas, and export licensing for both crude oil and refined products. Rationing was rejected in favor of a program to allocate supplies to industry and transportation at the expense of individual consumers. In addition, the government purchased a controlling interest in the oil firm Gelsenberg to gain more control over domestic refining and distribution. Under government encouragement, energy users began to save 85,000 b/d of oil by substituting coal.

By mid-December, Bonn was expecting recession by the spring of 1974 and a GNP for 1974 at or, more probably, below the 1973 level. Consumer demand was expected to be down about 10% in early 1974. Several major industries announced their intention to cut production by an average of 10%. Concerned over the prospects of widespread unemployment, the government in early December banned the entry of new foreign workers from non-EC countries and authorized the construction of additional housing units. Later in the month, it rescinded most of the anti-inflationary measures instituted earlier in 1973, including several that had inhibited investment. Monetary policy remained restrictive, however, because the oil price increases announced in October were expected to intensify inflationary pressures.

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Current Outlook for Oil Supply and Costs

Since the first of the year, German attention has largely shifted from the problems caused by short oil supplies to those expected to result from increased oil prices. December figures indicated that the shortfall in oil supply was much smaller than had been expected -- only 7% to 8% of anticipated demand. Deliveries of crude oil were reported as normal, with all the shortfall occurring in product imports, largely from the Netherlands. The oil import bill is expected to be about $6 billion higher in 1974 than in 1973, assuming a price of $10 per barrel and a 7%-10% reduction in demand because of conservation and slower economic growth. The volume of oil imports would in that case remain at approximately the 1973 level.

Economic Prospects for 1974

West Germany faces a year of little economic growth, continuing rapid inflation, and sharply increased unemployment. Real GNP is now expected to grow by 0% to 2%; the inflation rate probably will accelerate to about 10%; and unemployment will approach 3% of the labor force, compared with the usual 1% rate. Even with the large increase in oil import costs, Germany probably will be able to achieve a trade surplus of $7 billion to $8 billion, which should still offset its deficit on services. The higher oil prices will combine with the growth recession already in progress to present Bonn with serious short-term economic management problems.

Officials see difficult adjustments ahead, as the shock waves from oil price hikes are transmitted through the economy. Many government officials believe that the increased cost of oil will scuttle the fight against inflation and are focusing their attention primarily on preventing further large increases in unemployment. Officials of the Bundesbank nonetheless plan, for the present, to pursue anti-inflationary monetary policies.

The economic slowdown is resulting almost entirely from slower growth of private domestic demand, as foreign sales remain very strong. The slackening of private domestic demand is traceable to the restrictive economic policies of 1973, which hit hardest at the construction industry, and to structural problems in the textile and clothing industries. Only the decline in domestic demand for automobiles can be attributed directly to the oil shortage. Many firms seem hesitant to invest, even though removal of the 11% investment tax has made available an additional $2.5 billion for investment. Public spending shows no sign of slowing and may accelerate as the government takes up the fight against unemployment.

The balance of payments should come through the year reasonably well. Thus the trade account will again achieve a surplus, but one

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considerably smaller than the record achieved in 1973. The increased import bill probably will be largely offset by export growth of 6% to 8% as foreign buyers continue ordering from West German firms because of their ability to deliver high-quality goods quickly. Some impetus to German exports may come from US consumers' stampede toward smaller cars. Certain oil-producing countries have indicated that they want to use some of their increased revenues to import more West German capital goods.

Although foreign workers' remittances will be reduced, West Germans' travel expenditures abroad will stay near the 1973 level. The deficit on invisibles probably will more or less offset the trade surplus. A net outflow of capital from West Germany, primarily to the United States, is expected to put the official settlements balance into deficit.

Positions on International Cooperation

At the Washington conference, West Germany will seek common action to alleviate the oil supply and price problems. Minister of Foreign Affairs Scheel will have the dual role of speaking for the EC and for Bonn. He will push hard before, during, and after the conference for a common EC energy policy that includes cooperation with other oil-importing countries. French disregard for Community interests in breaking off from the joint float may make it easier to achieve agreement on such a policy among other EC members.

Bonn is vitally interested in securing a rollback of recent oil price increases and views the current race to strike bilateral deals with oil producers as possibly detrimental to this end. Nevertheless, it is under pressure to seek such arrangements itself because of the highly publicized deals of some of its EC partners and Japan. Bonn has tentatively agreed to finance a $1.2 billion refinery in Iran in exchange for oil supplies and reportedly is also considering a trilateral arrangement for natural gas with the USSR and Iran. In Washington, West German representatives will support proposals for cooperative efforts to acquire adequate oil supplies at reasonable prices but will be wary of joint moves that might trigger retaliatory action.

The West German government is convinced that alternative sources of energy must be developed. It is already planning to allocate more funds for deep drilling for domestic natural gas and for subsidizing the increased use of coal. In Washington, the West Germans will wish to discuss measures that consumer nations might take to protect large investments in these projects against a sudden turnaround in oil exporters' policies.

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Bonn is interested in discussing appropriate uses for the massive funds that will flow to oil-producing countries. In their own bilateral negotiations, the Germans are talking about long-term economic cooperation and assistance in industrializing Arab economies. Bonn undoubtedly would welcome consideration in Washington of proposals for channeling Arab surplus funds back into consumer countries without disrupting world money markets.

West Germany: Energy Data

	Primary Energy Consumption by Source (Percent)	Share Imported (Percent)
Total	**100**	**52**
Oil	56	95
Natural gas	11	37
Coal	30	-10[1]
Hydro/nuclear	3	36

	Pattern of Energy Consumption (Percent)
Residential, commercial, and agriculture	43
Industrial	41
Transportation	16

	Crude Oil Imports[2] 1973 (est.) Thousand b/d	Percent
Total	**2,200**	**100.0**
Arab	1,610	73.2
Libya	550	25.0
Saudi Arabia	480	21.8
Other Arab	580	26.4
Iran	270	12.3
Other	320	14.5

1. Exported.
2. Oil requirements are greater than crude oil imports. In 1972, net imports of petroleum products amounted to about 700,000 b/d.

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France

Background

Before the oil crisis the French government officially projected a 5.5% increase in real gross domestic product (GDP) for 1974, compared with an above-average rate of 6.6% estimated for 1973. Production bottlenecks, tightened monetary policy, and reduced export growth resulting from faltering economic activity elsewhere in Western Europe were the factors behind the expected decline. Unemployment would nudge above the 2% level, and the average rate of inflation would be about 8% in 1974.

France suffered only a small loss in oil supplies during the last quarter of 1973, but the international crisis nonetheless made businessmen more cautious, especially in view of difficult oil supply problems faced by France's major European trading partners. Capital spending plans were not reduced, but there may have been some reluctance to take on additional employees or to rebuild depleted inventories.

In a pre-Christmas forecast, the government saw the value of French exports increasing by only 5% in 1974, compared with a previously expected 15%. This decrease in foreign demand, based on the assumption of no West European economic growth in 1974, would cut the French GDP growth rate to an estimated 2.5%. Unemployment was seen as rising to a politically unpalatable rate of 3%-4%.

Current Outlook for Oil Supply and Costs

Paris does not believe that oil supply will be an important constraint on economic growth this year. France enjoys favored status with the Arabs and will not deviate from its pro-Arab policy. It has negotiated important bilateral oil deals with Saudi Arabia and Iraq already and is pressing for bilateral deals with other governments, offering armaments and industrial goods for oil.

The French are concerned, however, about the large price increases for imported oil. The oil import bill (on a c.i.f. basis) is now expected to run about $8 billion to $9 billion in 1974 -- more than $5 billion higher than in 1973.

Economic Prospects for 1974

Prospects for economic growth in 1974 are brighter in France than in most of the other EC countries. Sustained by strong domestic demand, the real increase in total output should approach 4%. Unemployment,

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however, will grow by about one-third, to a rate of about 2.5%, and inflation will accelerate, to an average of about 12%. The payments balance also will be cause for concern, with the current account probably registering a deficit of some $4 billion.

Because of the pressures on prices, the government is maintaining restrictive economic policies. At the same time, it appears to be alert to the danger of provoking a recession by waiting too long to reverse course. Floating of the franc has given the authorities freedom to use monetary policy without fear of a large loss of reserves. The government's strongest fiscal weapon would be reduction of the value-added tax rate -- a move that would immediately put more money into consumers' pockets. Easier financing for exports also could stimulate the economy.

As a result of the doubling of its outlays for oil and prospects of sluggish export growth, France faces a trade deficit of at least $3 billion this year. This deficit could exceed $3 billion if Paris does not succeed in substantially increasing exports to the petroleum-producing countries. Foreign Minister Jobert has expressed the hope that France will be able to sell up to $3 billion worth of arms to these countries annually.

To help the balance of payments, France began last month to reverse its policies concerning long-term capital movements. Outflows will now be discouraged unless they directly increase French exports, and both French borrowing abroad and foreign short-term and long-term investment in France will be encouraged.

Positions on International Cooperation

Paris is counting on the current visit of Foreign Minister Jobert to Arab capitals to result in favorable oil supply arrangements for France and will not risk accepting Washington's invitation until this mission is completed. If the French attend the Washington conference, they will try to dilute its importance and limit commitments to consumer cooperation. The French will pressure other participants to avoid offending the oil producers by any indication of confrontation and to resist developments that may strengthen US influence in Western Europe. They also will attempt to restrict the international companies' control in oil marketing.

Paris has made its own proposal for a world energy conference, to be held under UN auspices. Participants would include oil producers and LDC consumers as well as the industrialized nations. This proposal probably is a tactic to divert attention from the Washington-sponsored conference and to gain favor with oil-producing nations.

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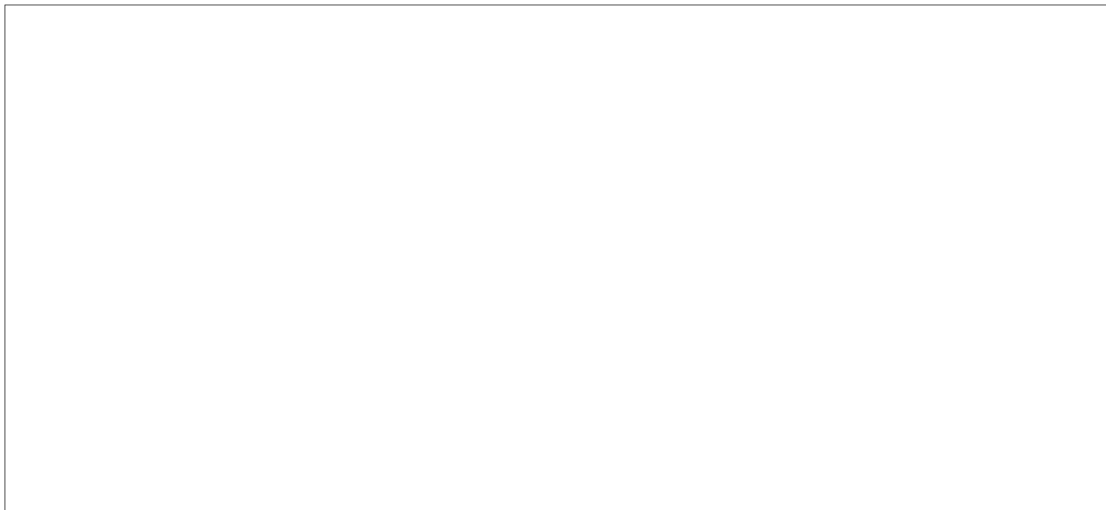
In a letter to the chairman of the EC Council, the French government urged that the Community retain total freedom of action to participate in energy discussions in other forums and to enter into bilateral agreements with Arab producers. The letter was ambiguous on whether bilateral arrangements should be concluded by the EC, as such, as well as by individual member states. The French have pressed for the Community to speak with one voice at the conference, thus giving Paris a veto over the EC position.



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France: Energy Data

	Primary Energy Consumption by Source (Percent)	Share Imported (Percent)
Total	**100**	74
Oil	71	98
Natural gas	7	46
Coal	15	32
Hydro/nuclear	7	-10[1]

	Pattern of Energy Consumption (Percent)
Residential, commercial, and agriculture	38
Industrial	44
Transportation	18

	Crude Oil Imports[2] 1973 (est.)	
	Thousand b/d	Percent
Total	**2,690**	**100.0**
Arab	2,070	76.9
Saudi Arabia	610	22.7
Iraq	350	13.0
Kuwait	310	11.5
Abu Dhabi	290	10.8
Other Arab	510	18.9
Iran	220	8.2
Other	400	14.9

1. Exported.
2. Oil requirements are less than crude oil imports. In 1972, net exports of petroleum products amounted to about 75,000 b/d.

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Italy

Background

As late as October 1973, the outlook for the Italian economy in 1974 remained good. Real growth of GNP was officially projected to accelerate to 6% or more, on the assumption that the strong 1973 recovery in consumer demand and industrial activity would continue. Stringent price controls, selective credit restrictions, and improved productivity gains promised a slowing of inflation to about 8% from the 12%-14% rate of mid-1973. Rising industrial production was expected to ease unemployment, recently running at about 3.5% of the labor force. A swing to a small trade surplus was expected as a delayed benefit from the 1973 lira devaluation.

The October-December oil production cutbacks for the Arab states threatened a 20% shortfall in Italian supplies in 1974. Government conservation measures adopted in October and November would have reduced the shortfall to an estimated 12%-14% of demand. Included in the conservation measures were a Sunday driving ban, imposition of speed limits, price increases for petroleum products, restricted business hours, and controls on exports of petroleum products.

Despite the conservation program, Italian economic prospects for 1974 were dim by mid-December. Even without further oil supply cutbacks, stagnant output and a worsening of the unemployment rate to at least 5% were predicted. Hopes of an export revival were laid to rest; the leading export industries were among those likely to suffer most from the oil shortages, and West European demand for Italian goods clearly would weaken.

Current Outlook for Oil Supply and Costs

By the end of December, increased oil prices supplanted the supply situation as Rome's major worry. Assuming oil consumption at the 1973 level and a cost of $10 per barrel, Italy's net oil import bill will swell by some $4 billion this year. Italian officials see little opportunity to avoid a corresponding deterioration in the current account balance. Furthermore, Italy's foreign exchange position is comparatively weak; the holdings of $5.8 billion equal only three months' imports.

The oil supply still is running about 10% below demand. Industrial needs are largely being met by reducing refinery stocks and cutting consumption by households and the service sector, although enterprises in some provinces have been experiencing fuel oil shortages. Failure to ease price controls for petroleum products could cause continuing diversion of

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crude oil supplies to more lucrative markets in Europe and the United States, holding 1974 oil imports below the 1973 level.

Economic Prospects for 1974

Forecasts of Italian economic activity in 1974 vary widely. The Bank of Italy, for example, estimates a 0.5% decline in real output while the OECD Secretariat forsees a 5% rise. A more realistic forecast we believe, is an increase of 1%-2% in GNP, together with a jump of about 15% in prices and a rise in the unemployment rate of at least one-half percentage point. The Embassy's estimate that the current account deficit will grow from $3 billion in 1973 to about $5.5 billion this year also seems reasonable.

High oil prices will raise major policy issues for the Rumor government. The automobile and tourist industries are being hit hard by weakened consumer demand. Although most industries will be able to avoid sizable layoffs of workers, retail price controls and an investment slowdown preclude much of an increase in production. Inflationary wage demands seem inevitable, despite price controls and rising unemployment.

The recent oil price hikes will severely weaken the balance of payments. Because demand is expected to be sluggish in Italy's major markets, exports are likely to show only moderate growth even if the lira remains at its present depressed level. Such gains as are made in export receipts will be swamped by the rising cost of oil and other raw materials, which bulk especially large in Italian imports.

At the same time, tourist receipts and worker remittances probably will stagnate as the West European economies turn downward. Pressures against the lira are likely to continue as the current account is thrown into growing deficit. The lira's weakness will again prompt large capital outflows in spite of stringent controls. As large foreign loans become increasingly difficult to obtain and the Bank of Italy attempts to support the lira, substantial drawdowns in Italy's already small foreign reserves will be necessary.

Despite the contractionary impact of the oil price hikes, Rome will be slow to take up expansionary measures. Monetary policy probably will remain slightly restrictive through much of 1974.

Positions on International Cooperation

Rome is likely to support, in principle, US initiatives aimed at international cooperation on energy matters. It will not enter into any new

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arrangements, however, without considering the attitudes of other EC countries and the effect on bilateral relations with the Arab states.

The Italians will be most receptive to proposals promising success in obtaining a price rollback. Among other things, the Minister of Foreign Trade has recommended that the 11 February meeting assign a high priority to finding ways of limiting auction prices for government-owned oil.

Rome is trying to develop alternative sources of energy and probably will approve international proposals with this purpose. Even Raffaele Girotti, director of the state oil company and a strong proponent of closer ties with the Arabs, has urged Italian participation in multilateral efforts to develop energy sources other than oil. The government recently earmarked $1 billion for construction of two nuclear powerplants before 1980. Rome is a major participant in EURODIF, one of the two consortiums organized to develop Europe's nuclear fuel capabilities, and advocates close cooperation with our Atomic Energy Commission.

The Italians will oppose any arrangements suggesting a consumer-producer confrontation. They will be wary of proposals that would undermine the state oil company's agreements with Libya and Iraq or interfere with current efforts to expand bilateral relations with Arab oil producers. Officials from the foreign ministry and President Leone's office recently visited Syria, Iraq, and Saudi Arabia, and Foreign Minister Moro began a trip through Saudi Arabia, Kuwait, and Iran on 29 January. Moro recently tried to improve the climate for his tour by moving beyond the EC declaration on the Arab-Israeli dispute, citing total Israeli withdrawal from the occupied territories as the most important element for peace.

These efforts have been mounted partly because of sharp domestic criticism of Rome's Middle East policy. The government has been accused of following a policy calculated to offend no one while other West European countries were concluding favorable bilateral deals. At the Washington meeting, the Italians will be careful not to endorse any arrangement that would renew this controversy.

Rome's approach to dealing with its energy problems is typified by the comments of Christian Democratic party chief Amintore Fanfani, probably the most powerful politician in Italy. He asserts that Rome can respond favorably to the Arab call for new forms of economic support, to the US call for international cooperation, and to the EC effort to settle on a common energy policy. Italian officials do not see these initiatives as mutually exclusive but rather are trying to devise a balance among them.

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Italy: Energy Data

	Primary Energy Consumption by Source (Percent)	Share Imported (Percent)
Total	**100**	**80**
Oil	76	99
Natural gas	10	9
Coal	6	97
Hydro/nuclear	8	Negl.

	Pattern of Energy Consumption (Percent)
Residential, commercial, and agriculture	36
Industrial	45
Transportation	19

Crude Oil Imports[1] 1973 (est.)	Thousand b/d	Percent
Total	**2,410**	**100.0**
Arab	1,930	80.1
Saudi Arabia	630	26.1
Libya	460	19.1
Iraq	390	16.2
Other Arab	450	18.7
Iran	330	13.7
Other	150	6.2

1. Oil requirements are less than crude oil imports. In 1972, net exports of petroleum products amounted to about 225,000 b/d.

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Japan

Background

Prior to the oil crisis, Japan's economic outlook was fairly bright. Although a slowdown in economic growth in 1974 was expected because of a cyclical downturn in private investment spending, real GNP still was projected to grow about 9%. Tokyo was confident it could bring under control the rapid inflation experienced in 1973, when wholesale prices jumped 30%. Some increase in the country's trade surplus, which had been more than halved in 1973 to $3.8 billion, was expected along with a reduction in the overall balance-of-payments deficit. All of these projections assumed that Japan would continue to buy steadily increasing amounts of oil at prices not too far above the 1973 average.

When the Arabs cut oil supplies beginning in October, Japan's economic prospects were altered dramatically. Oil deliveries to Japan began falling almost immediately, dropping by about 400,000 b/d between October and December. Not only were Arab oil deliveries being reduced, but also foreign-owned oil companies (which handle more than 70% of Japan's oil imports) began diverting substantial amounts of non-Arab oil away from Japan, primarily to Western Europe. Indeed, most of the supply shortfall during the last quarter of 1973 reflected diversion. If Arab oil cutbacks had continued much into 1974, Japan would have experienced a sharp decline in economic activity for the first time in the post-war period.

Current Outlook for Oil Supply and Costs

The price of oil, rather than the physical supply, is now the chief problem facing Japan. Although diversion is continuing, Japan's supply outlook has improved since it was placed on the "friendly country" list in late December and Arab oil production began increasing. As a result, oil import volume in 1974, rather than declining, will at least match last year's level of 5.4 million b/d. The cost for the same volume will increase enormously – by at least $11 billion to about $17 billion. Except for the United States, Japan's oil import bill this year will increase by more than that of any other country.

The supply shortfall during the early months of 1974 is expected to total several hundred thousand barrels per day, with the gap narrowing as the year progresses. To cope with the shortfall, Tokyo has implemented a wide-ranging energy conservation program aimed principally at cutting industrial use, which accounts for about 65% of Japan's energy consumption. The conservation measures are being administered flexibly and will be eased as the supply situation improves. In the meantime, drawdowns of stocks probably will be accelerated to avoid serious production bottlenecks.

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Economic Prospects for 1974

Energy-related problems have already disrupted normal growth patterns. Shortages have slowed the growth in industrial output, and higher oil prices will aggravate the situation in the months ahead. The $11 billion direct loss in purchasing power resulting from higher oil costs this year is equivalent to almost 3% of GNP and 8% of fixed investment. Because of shortages and less favorable terms of trade stemming from the energy problem, the real rate of growth in GNP in 1974 will slow to 3%-4%– the slowest rate since the 1950s.

Energy-related problems are aggravating Japan's inflationary spiral. Spurred by supply problems at home and higher import prices, wholesale prices rose 30% last year and consumer prices nearly 20%. Even before the latest oil price increase the outlook was for at least a 10% rise in wholesale prices in 1974. The price spiral already poses a serious political problem for the Tanaka government, and Finance Minister Fukuda has made clear his desire to bring inflation under control even at some cost in reduced economic growth and unemployment.

Higher oil prices also threaten Japan with its first trade deficit in a decade. With a slow rate of real growth, the physical volume of imports will decline, but higher prices will boost the import bill by about 30%, to at least $40 billion. A rapid expansion of exports in either volume or dollar value in 1974 is not in the cards. Most industrial countries will experience even slower growth than Japan, and their demand for Japanese as well as other foreign goods will not increase much. Moreover, competition for export markets will become more intense as countries attempt to offset inflated oil import bills by boosting sales abroad.

To help bolster its trade and payments position in the wake of the oil crisis, Tokyo has already allowed the yen to depreciate 11% relative to the dollar. The government is also considering measures to stimulate exports and restrain imports in an effort to slow the decline in foreign exchange reserves. Official reserves, which reached a peak of $19 billion in February 1973, now total only about $11 billion. In addition to official reserves, however, Tokyo can draw on $10 billion in reserves built up in non-official accounts during 1972 and early 1973. Even so, the huge balance-of-payments deficit expected in 1974 could reduce total reserves by at least one-third.

Positions on International Cooperation

Tokyo's view of the conference still is based mainly on its fear of antagonizing the oil producers. Although the Japanese are eager to see a reduction in oil prices, they oppose taking any action that might lead to

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a confrontation. They are therefore unlikely to agree to any but the most innocuous forms of cooperation.

Government leaders do not fully agree on oil policy. Finance Minister Fukuda is most concerned about the price question and, together with Foreign Minister Ohira, most inclined to move in the direction of international cooperation. Their hands are tied to some extent, however, by Minister of International Trade and Industry Nakasone and his supporters, including Deputy Prime Minister Miki. The chief concern of the latter two is ensuring supplies, preferably by dealing directly with the producing countries. Nakasone was among the strongest proponents of a pro-Arab policy when the energy crisis emerged and probably is in a position to veto Japanese involvement in any type of organization that might antagonize the oil producers.

Because of these policy differences, the Japanese will avoid taking any major initiatives at the February conference. Indeed, the Ministry of Foreign Affairs is delaying its preparation of position papers until it has a better idea of the attitudes of the European Community. Japan hopes to follow an EC lead in pushing for a statement by the conference giving approval in principle to bilateral arrangements between oil importers and exporters. Even without such sanction, however, the Japanese will continue to pursue bilateral deals. Since the start of this year, Japan has lined up additional large supplies of crude oil from Iraq for the next 10 years, arranged to import crude oil from Algeria for the first time, and offered to finance a $1 billion refinery in Iran in return for the output.

Stabilization of oil prices is an issue of prime concern to Japan. Nonetheless, Tokyo will oppose any move to force a price rollback by the producers. In order to avoid antagonizing the exporters, the Japanese will seek to have discussion of prices deferred until a joint producer-consumer conference can be held. At the first stage of international talks, Tokyo probably will try to steer any discussion of prices to those charged by the major oil companies, which it accuses of unduly raising profit margins.

Japan wants the conference to lay the groundwork for a meeting of producers and consumers and apparently prefers that such a meeting be held before any working groups are established. As Tokyo sees it, joint producer-consumer task forces should tackle the price issue as well as other matters, including ways to help the Arabs invest their money. The Japanese would be willing, however, to discuss less controversial issues, such as energy conservation and development of new energy sources, at the February meeting. In fact, Tokyo agreed last summer to cooperate with the United

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States on the latter. The signing of a formal R&D Agreement has been delayed by bureaucratic jealousies in Tokyo rather than by any major disagreements with Washington. Japan and the United States also agree that the United Nations energy conference proposed by France should not be convened until after the 11 February and any follow-up meetings have been held.

Japan: Energy Data

	Primary Energy Consumption by Source (Percent)	Share Imported (Percent)
Total	**100**	**86**
Oil	75	100
Natural gas	1	26
Coal	17	67
Hydro/nuclear	7	0

	Pattern of Energy Consumption (Percent)
Total	**100**
Households	10
Agriculture, mining, and construction	6
Manufacturing	61
Transportation	11
Other	12

	Oil Imports 1973 (est.)	
	Thousand b/d	Percent
Total	**5,400**	**100.0**
Arab	2,390	44.3
Saudi Arabia	1,240	23.0
Other Arab	1,150	21.3
Iran	1,730	32.0
Indonesia	840	15.6
Other	440	8.1

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Norway

Background

Prior to the oil crisis, Norway's economic outlook for this year was bright. The growth of real GNP was expected to accelerate from 4.3% in 1973 to 5.5% in 1974. The inflation rate promised to drop slightly, to 7%. Only a modest weakening in the country's trade and payments position was expected.

The Arab supply restrictions induced Norway to initiate a fairly effective conservation program. Net imports of oil satisfy about 45% of total energy requirements, with hydroelectric power meeting most of the remainder. The Arab cutbacks reduced Norway's oil imports by about 20% during the last quarter of 1973. Both direct shipments from the Arabs and deliveries of refined products, mainly from the Netherlands, were reduced. Exports of nearly all of the 40,000 b/d of oil domestically produced apparently have continued despite the loss of Arab oil.

Current Outlook for Oil Supply and Costs

Continuing supply constraints do not threaten serious problems for the economy. The government's conservation program has already resulted in a 20% saving in consumption of heavy oil, largely by switching some industries to use of hydroelectric power. Private consumption of heating oil and gasoline has also been reduced. With Arab oil production increasing, Norway expects to obtain as much as necessary during most of 1974. Total imports this year probably will at least match the 140,000 b/d imported in 1973. The cost of petroleum imports will rise in 1974, but by the end of the year Norway's oil exports should about equal imports.

Economic Prospects for 1974

Real growth of GNP in 1974 probably will about match last year's rate of 4%. Business confidence appears fairly strong, and industrial production will increase steadily. No appreciable increase is expected in the present low rate of unemployment.

The inflation rate probably will be pushed well above the 7% average of recent years by higher oil costs and sharply increased labor costs. Norwegian labor unions, for example, may demand wage increases of as much as 15%, compared with hikes averaging about 10% over the past several years. There is no sign so far that the government is moving to tighten fiscal and monetary policies.

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Higher prices for imported oil will hurt Norway's trade balance much less than those of most other developed countries. Much of the cost will be offset by increased earnings from Norway's exports of oil and natural gas. Most of the estimated rise in the current account deficit from $400 million in 1973 to $800 million in 1974 is attributable to import requirements associated with oil and gas development. Because earnings from oil and gas exports are expected to increase sharply in late 1974 and 1975, deterioration in the current account balance this year need not be viewed with alarm. In fact, because Norway stands to be hurt less than other industrial countries by the energy crisis, some funds have flowed into the country in anticipation of a currency revaluation.

Positions on International Cooperation

Although the Norwegian government has responded positively to US initiatives looking toward cooperation on energy matters, Foreign Minister Frydenlund has suggested that the OECD might be the best forum. Oslo fears that US sponsorship may squelch French cooperation and alienate Arab oil producers. In any case, Oslo was relieved that the conferee list was expanded to include all EC members. It hopes that subsequent meetings will include even more countries, including the USSR and Eastern Europe.

At the Washington conference, Oslo can be expected to endorse plans that would help assure stable oil supplies. It will support proposals aimed at helping producer countries invest their surplus funds. Because it wants to prolong the life of Norwegian oil fields and avoid overheating the economy through an oil boom, Oslo also will support consumer efforts to develop alternative energy sources. Norway may advocate greater public control over the international oil companies. Prime Minister Bratteli already has suggested formal cooperative arrangements between countries and oil companies to bring the industry under political control.

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Norway: Energy Data

	Primary Energy Consumption by Source (Percent)	Share Imported (Percent)
Total	**100**	**50**
Oil	58	81
Natural gas	....	....
Coal	6	50
Hydro/nuclear	36	-3[1]

	Pattern of Energy Consumption (Percent)
Residential, commercial, and agriculture	31
Industrial	52
Transportation	17

	Crude Oil Imports[2] 1973 (est.)	
	Thousand b/d	Percent
Total	**140**	**100.0**
Arab	64	45.7
Saudi Arabia	20	14.3
Abu Dhabi	7	5.0
Other Arab	37	26.4
Iran	55	39.3
Other	21	15.0

1. Exported.
2. Oil requirements are greater than crude oil imports. In 1972, net imports of petroleum products amount to about 25,000 b/d.

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The Netherlands

Background

Before the October oil crisis, the Netherlands expected in 1974 to achieve a 4.5% rise in real GNP, a slight reduction in unemployment from the present rate of 3.0%, and a current account surplus of about $1 billion. Oil consumption was expected to increase by about 10%. The government's primary concern was the 8% inflation rate. Tighter price controls, a restrictive monetary policy, and the revaluation of the guilder in September were expected to trim the rate of inflation to 5% in 1974.

The October embargo on Arab oil shipments to the Netherlands invalidated previous forecasts for 1974. Faced with the prospect of a 30% - 35% reduction in normal oil imports, the government adopted stringent measures to reduce domestic oil consumption and an export licensing system to cut off oil exports to non-EC countries. An allocation scheme favoring industry was developed to minimize the impact of oil shortages on output and employment. Stocks were to be drawn down during 1974 to the compulsory 65-day EC floor to limit the decrease in crude oil consumption to about 25%.

Mid-December forecasts for 1974 predicted no growth in real GNP, an unemployment rate approaching 4%, an inflation rate of 10.5%, and a sharp deterioration in the balance of payments. A $715 million government program to facilitate industries' conversion to natural gas was expected to stimulate business investment despite the depressing effects of the oil crisis on outlays in the metallurgy and chemical industries. Officials expected a 3% decrease in commodity exports because of supply constraints and weak foreign demand. The volume of Dutch imports was not expected to increase, because of production limitations in major trading partner countries. To adjust demand to production capacity, the government froze $250 million of planned highway, defense, and education expenditures, and indicated that curbs on private consumption might be forthcoming.

Current Outlook for Oil Supply and Costs

In January the focus of government concern shifted from supply shortages to the impact of the October and December price increases. If the physical volume of imports equals the 1973 level, the Dutch oil import bill will rise by $2 billion in 1974, further aggravating inflation and investment problems. Even so, the Dutch are in a strong position to pay the higher prices because sizable reserves have been accumulated.

Oil company diversions and increased imports from non-Arab sources have improved supply prospects and made possible a higher level of refinery

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throughput than first expected. The supply situation should continue to improve as the Arabs expand production. Oil shortages in other industrialized countries are smaller than expected; this should facilitate continued diversion of non-Arab crude oil to the Dutch market. The government's decision to end gasoline rationing on 5 February is evidence of the improved supply picture.

Economic Prospects for 1974

The Dutch economy simultaneously faces growing unemployment and stepped-up inflation in 1974, despite recently improved oil supply prospects. The outlook for major economic indicators is: GNP up 1%, prices up 14%, unemployment of 3.5% to 4%, and a current account deficit of $500 million.

Investment decisions, particularly in export industries, are likely to be postponed in anticipation of a squeeze on profits from rapidly rising production costs. Depressed investment and output will increase unemployment later in the year. An expected increase in private consumption demand will further strain production capacity and, combined with the higher cost of imported oil, aggravate the rampant domestic inflation.

The oil crisis, combined with the effects of the September guilder revaluation and overall import price trends, probably will change the substantial current account surplus of 1973 into a slight deficit in 1974. While the import price index is expected to rise 15% or more in 1974 -- including the nearly $2 billion increase for domestically consumed petroleum -- rising export prices will cushion the effect on the current account balance. Dutch officials estimate that, over two to three years, increases in the value of natural gas exports alone could more than compensate for higher crude oil costs. The primary concern is that the petroleum-intensive nature of Dutch export industries will hurt earnings in the longer term.

Inflation and unemployment pose problems for fiscal policy. To restrain price increases, the government needs to hold down budgetary expenditures. But to deal with rising unemployment, expenditures are needed for unemployment benefits and job-creating public works. Thus far, unemployment has been fought by reducing working hours and restricting the number of foreign workers. Emergency legislation passed in January will allow the government to restrict price and wage increases and to stimulate new employment, primarily in the building trades.

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Positions on International Cooperation

The government and people of the Netherlands welcomed the US initiative in calling the 11 February meeting. Their well-publicized bias toward Israel makes bilateral deals with Arab states much more difficult for the Dutch than for other EC members and turns them perforce toward cooperative action. Although the Netherlands is committed to the EC, it is disturbed by recent divisive trends, specifically:

- the failure of the EC members to stand by the Netherlands during the oil embargo,
- the failure of the EC to produce any semblance of unity on energy issues,
- French and British efforts to forge bilateral ties with the Arab states, and
- France's surprise move in breaking from the European joint float on 19 January.

The Dutch will seek a common EC position prior to the Washington conference but, faced with French intransigence, would rather see the EC divided in its response than uniformly negative.

The Dutch would like to see cooperation on oil sharing and on price reductions handled through existing institutions such as the OECD. Although not specifically averse to the United Nations as a forum, they would prefer to avoid unwieldy assemblies that would get bogged down in side issues. They are opposed to Communist participation. They will resist French attempts to denigrate constructive follow-ups to the Washington conference.

The Dutch are sensitive to the plight of less developed countries as oil consumers and are willing to help them solve their energy problems. They would like to see a tripartite conference among oil producers, major consumers, and less developed countries evolve from the Washington conference. They would prefer that these groups be represented by existing institutions – perhaps by OPEC, OECD, and the "Group of 77."

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The Netherlands: Energy Data

	Primary Energy Consumption by Source (Percent)	Share Imported (Percent)
Total	**100**	**16**
Oil	56	94
Natural gas	41	-71[1]
Coal	3	35
Hydro/nuclear	Negl.	-Negl.[1]

	Pattern of Energy Consumption (Percent)
Residential, commercial, and agriculture	50
Industrial	35
Transportation	15

	Crude Oil Imports[2] 1973 (est.)	
	Thousand b/d	Percent
Total	**2,070**	**100.0**
Arab	1,380	66.7
Saudi Arabia	690	33.3
Kuwait	380	18.4
Other Arab	310	15.0
Iran	440	21.3
Nigeria	220	10.6
Other	30	1.4

1. Exported.
2. Oil requirements are less than crude oil imports. In 1972, re-exports of crude oil and net exports of petroleum products amount to about one million b/d.

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United Kingdom

Background

Even before the oil crisis, the outlook was for a sharp economic slowdown in Britain during 1974. The growth rate was expected to drop to 3.5%, only half that achieved during the economy's rare sprint in 1973 but still a little above the long-term average. Consumer demand, which led the boom, seemed likely to cool in the face of rising prices and continued wage restraints. At the same time, export demand promised to remain strong and an investment upturn was in view because output was pressing against production capacity.

Expectations of a reduced supply of energy following the Arab oil cutback in October further depressed prospects for economic growth. Although Britain was a favored nation, its oil imports threatened to drop by about 10% during the first quarter of 1974 because of the Rotterdam embargo and company diversions of oil to countries harder hit than the United Kingdom. Early in November, moreover, Britain's energy situation took a sudden turn for the worse. A miners' ban on overtime cut coal output by more than 30%, preventing substitution of coal for oil. To adjust to lessened energy supplies, the government cut petroleum allocations for most economic sectors to 10% below November 1972 consumption, limited exports of petroleum products, and announced a drastically shortened workweek.

By mid-December, we were forecasting economic growth of only 1% and an inflation rate of 10% to 12% in 1974. The threatened shortfall in oil deliveries alone was expected to trim about 2 percentage points from industrial growth and 0.5 percentage points from the increase in GDP. Continuation of the short workweek through mid-January, it was estimated, would cost another 1 percentage point in economic growth. Prolongation of the short workweek would not only reduce output but also worsen the large trade deficit. To bring demand more into line with output expectations, the government tightened credit and introduced restrictive budgetary measures. Nevertheless, excess demand and rising world commodity prices presaged continuing rapid inflation and a shaky current account balance.

Current Outlook for Oil Supply and Costs

The easing of Arab oil supply restraints and the colossal oil price increases announced in late December altered the nature of Britain's energy problem. For 1974 as a whole, oil-supply constraints on economic growth probably will be slight, but high oil prices will intensify the country's economic woes. The United Kingdom is now paying about $10.00 per barrel,

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c.i.f., for oil. If some shortfall in supply occurs in early 1974 and conservation efforts continue to temper demand, oil imports will average about 2.5 million b/d this year, and their cost will jump by about $5 billion.

Dampened economic growth, high prices, and conservation measures have sharply reduced earlier forecasts of the demand for oil in 1974 in all countries. Nonetheless, oil deliveries to Britain during January and February are likely to fall 10% to 15% short of demand, which is being inflated by the coal shortage. But Britain should have little trouble filling its oil import needs by the end of the first quarter if the coal dispute is settled, particularly if Arab production is increased soon, as expected.

Economic Prospects for 1974

At best, Britain is unlikely to achieve any economic growth in 1974. If the dispute between the government and the coal miners drags on through March, a drop in GDP of at least 2% is possible. Unemployment will rise sharply, perhaps reaching 800,000 persons (3.2% of the labor force) by the end of 1974, compared with 500,000 persons in mid-December 1973.

Although the oil supply situation will ease as the year progresses, the price increases will both accelerate inflation and have a contractionary impact on some parts of the economy. The immediate effect of higher oil prices will be to raise the fuel bills of British consumers at a time of growing uncertainty about future incomes and prices. Consumers will be torn between increasing precautionary savings, which would further reduce their non-fuel purchases, and trying to maintain living standards. Reduced consumption would ease pressures on prices and imports, but British workers -- intent on maintaining or raising living standards -- probably would soon demand large wage increases, which would either shatter the government's Stage III wage goals or worsen the already bad state of industrial relations. Even under the Stage III restrictions, price-index clauses in many labor contracts are boosting money incomes.

Sizable wage hikes as well as higher fuel prices will raise production costs and curtail industry's ability to invest. The competitiveness of British goods would in turn be impaired and the trade balance worsened. Some purchasing power transferred to the Arabs may return to Britain through its well-developed financial markets. But with industrial relations in chaos and the pound floundering, Arab investors will shy away from direct investment in the United Kingdom.

The increased oil import bill will cause a substantial deterioration in Britain's trade and current account deficits, which already are at record levels. To offset some of the $5 billion added cost of oil, the United

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Kingdom has removed a ban on arms exports to belligerents in the Middle East and is trying to arrange barter deals with Iran and Saudi Arabia. In addition, the Arabs are being encouraged to use London's extensive financial facilities in investing their new wealth. These efforts will compensate for only a small part of the cost increase. Already floating at record lows, the pound is expected to remain weak this year.

The contractionary impact of oil-price increases is not an immediate problem for the economy, which already is afflicted with excess demand. With industrial growth constrained but incomes affected little by the short workweek, a switch from a restrictive to an expansionary policy would only aggravate inflation and boost imports. The increase in oil costs is expected to add 2% to 4% to retail prices, raising the inflation rate to about 15% for 1974. The trade and current account deficits probably will reach at least $9 billion and $7 billion, respectively, even without expansionary government policies.

These problems are so severe that the government is unlikely to stimulate economic activity even after industry goes back to normal hours. An expansionary policy would have to be accompanied by strict (probably unenforceable) price controls and severe import restrictions. Instead, Prime Minister Heath may opt for a restrictive spring budget to supplement the expenditure cuts announced in December. Monetary policy probably will stay tight, and inflation will push interest rates to all-time highs.

Positions on International Cooperation

Because of the expected large current account deficit, London probably favors low-key cooperative efforts to obtain an oil price rollback. It is skeptical about chances for success, however, and fears that any offense to Arab sensitivities could result in an even harder line. The British probably will argue against exerting direct pressure on the Arabs, recommending instead that the Washington conferees simply stress the damage to oil producers and consumers alike that would result from a worldwide depression. The British have suggested that private meetings be held with producer countries to explore the possibility of instituting a new pricing system.

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The United Kingdom already has moved to produce more energy from resources under its own control. Lord Carrington, head of the newly created energy ministry, has announced a speed-up in development of North Sea

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oil deposits, which are expected to satisfy about 80% of Britain's oil needs by 1980. By 1980 natural gas production is expected to double to some 5.5 billion cfd and fill about 15% of UK energy needs. At the same time, London is expected to restrict outside participation in the project, perhaps even by its EC partners. The British also hope to increase coal production.

The British probably will support multilateral efforts to help oil-exporting countries invest their surplus funds. London's first concern, however, will be to offset its increased import bill by bartering British goods for oil. A barter deal with Iran has been concluded and another with Saudi Arabia is well under way.

Because of Britain's unstable political and economic situation, the Heath government will strongly oppose any multilateral decisions not in keeping with its domestic concerns. It has said, for example, that it intends to continue pursuing bilateral deals – a course likely to be followed regardless of decisions made at the Washington conference.

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United Kingdom: Energy Data

	Primary Energy Consumption by Source (Percent)	Share Imported (Percent)
Total	**100**	**50**
Oil	52	100
Natural gas	14	3
Coal	30	3
Hydro/nuclear	4	1

	Pattern of Energy Consumption (Percent)
Residential, commercial, and agriculture	43
Industrial	41
Transportation	16

	Crude Oil Imports[1] 1973 (est.)	
	Thousand b/d	Percent
Total	**2,330**	**100.0**
Arab	1,480	63.5
Saudi Arabia	550	23.6
Kuwait	400	17.2
Libya	240	10.3
Other Arab	290	12.4
Iran	460	19.7
Other	390	16.8

1. Oil requirements are greater than crude oil imports. In 1972, net imports of petroleum products amounted to about 200,000 b/d.

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Attitudes of Other Countries

Belgium

Brussels generally supports Washington's initiative in calling a meeting of major oil-consuming nations. The Belgians delayed a public statement on the conference to permit EC coordination and will seek to act in concert with their partners in Washington as well. They will not hesitate, however, to speak out on matters that concern them.

Although the recent fall of the government was triggered by the failure of the Belgo-Iranian petroleum refinery agreement, the true roots of Belgian political troubles lie in domestic issues. The government continues to function in a caretaker capacity, and Minister of Foreign Affairs Van Elslande presumably will lead the delegation to Washington as planned. In any case, the major Belgian political parties differ little in their approach to international energy matters.

Belgium's resources preclude self-sufficiency in energy, and Brussels has little confidence in its ability to compete with larger European countries in arranging bilateral agreements with oil producers. The government thus should be receptive to plans for cooperative action to assure adequate oil supplies. Belgium also will support suggestions for coordinated action by consumer countries to develop alternative sources of energy.

The Belgian approach to the Washington meeting is likely to be shaped by two additional factors. As a country heavily dependent on trade, Belgium is particularly concerned about worldwide recession arising from the energy crisis. At the same time, Belgium wants to avoid offending the oil-producing countries, because petroleum imports provide about 60% of energy supplies and substitution possibilities are few. Brussels thus can be expected to advocate that consumers consult with oil producers as well as among themselves.

Belgium feels the LDCs should have a say in matters that seriously affect them and, for this reason, favors the French suggestion that the United Nations play a role as a forum on energy matters. Belgium perceives the need, however, to inform the LDCs that higher oil bills will reduce industrial countries' capabilities to furnish development aid.

Denmark

Copenhagen's new minority government of Moderate Liberals needs the support it might gain from effective handling of energy problems. Holding only 22 seats in the 179-seat parliament, the government is unlikely

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to last long but could benefit from new elections if it does creditably in the present crisis.

Prime Minister Hartling's response to the US initiative is enthusiastic even though Copenhagen has some of the same reservations as Oslo. Hartling views the Washington conference as a good "first step" toward solving the oil problem but has called for expanding the number of participants in subsequent meetings. In particular, he would like to see the LDCs included in future energy conferences.

Although the Danes reluctantly began bilateral oil negotiations in late January, they still favor a unified EC energy policy. Faced with nine opposition parties, Prime Minister Hartling apparently was forced to shift policies, at least temporarily. Earlier the Danes had strongly criticized bilateral oil deals by other members of the EC. Government spokesmen accused the UK, France, and West Germany of violating the spirit and perhaps the letter of the Rome Treaty by attempting such arrangements.

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Denmark will support a cooperative EC policy aimed at developing a coordinated consumer position for negotiations with producers. The Danes would support efforts to develop a framework in which producers and consumers can negotiate easily. Copenhagen can be expected to support pooling of research and development efforts and sharing of energy resources, even with countries outside the EC.

Ireland

Because of its worsening balance-of-payments problems, Dublin will be anxious to participate in cooperative action to obtain an oil price rollback. It also prefers a multilateral approach in trying to secure adequate oil supplies. The Irish press has been highly critical of French and British bilateral deals with oil producers. The view stems in large part, of course, from Dublin's limited bargaining power.

Dublin will resist any efforts to organize a consumers' cartel or other actions that would irritate Arab oil producers. The government traditionally has had a pro-Arab tilt, largely because 70% of Irish petroleum imports and nearly half of total energy supplies come from the Middle East.

Ireland does not have the resources to engage in a major program to develop alternative sources of energy. It would welcome international sharing of energy technology and joint research and development programs.

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Luxembourg

Luxembourg is enthusiastic about the Washington conference and flattered by the invitation to attend. Government officials, especially Prime Minister Pierre Werner and Minister of Foreign Affairs Gaston Thorn, see the meeting as an important opportunity to coordinate views on energy matters and as a step toward a realistic Atlantic partnership. They also hope that it will lay the groundwork for consultation with LDC consumers and with oil producers.

The Luxembourg government is eager to refute rumors that the Washington meeting's purpose is to set up a consumer bloc. It is wary of the French and worried that Arab states, supported by Paris, will initiate reprisals unless Washington participants broaden the scope of future oil consultations. [redacted] Luxembourg opposes the French proposal that the United Nations be used as a forum for energy consultations.

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The EC

EC political directors view Washington's convocation of the world's major oil consumers as an important initiative and are particularly pleased by inclusion of the Community as an entity. EC Commission President Ortoli and West German Minister of Foreign Affairs Scheel, in his role as Council president, will represent the Community. Their authority to speak for the EC will be circumscribed by the positions adopted by member states at the Council meeting of 4-5 February.

The objectives of the Commission itself are broadly similar to those of the United States. It would like to see progress at the Washington conference in the following areas:

- an assessment of world oil supply and price problems;
- a framework for cooperation among consumers on conservation, alternative energy sources, research and development, and limitations on competition for existing supplies;
- a basis for cooperation between consumers and producers; and
- plans for subsequent meetings that will include LDC consumers and oil producers.

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The Commission has been frustrated in its earlier efforts to guide the Community toward a common energy policy. To date, it has accomplished little more than to initiate information pooling on the energy situation within member states. Given the economic and political disarray within the Community, the Commission welcomes the Washington conference as a unique opportunity to move EC members toward the kind of cooperative action it has favored all along.

The OECD

OECD Secretary General Van Lennep has openly approved of the Washington conference and its objectives. He sees the OECD performing an important support function in the post-conference period.

The OECD secretariat supports joint action to assure adequate oil supplies for importing nations. It believes that present prices are higher than can be justified on the basis of medium-term costs of energy from alternative sources. Van Lennep favors multilateral attempts to persuade exporters to roll back prices or, at the least, to refrain from further increases. He recommends that meetings with oil producers also consider mutually beneficial means of channeling excess Arab funds back to consumer countries, particularly to the LDCs.

OECD is speeding up and restructuring its study of alternative sources of energy and of conservation possibilities. By this summer, it intends to provide a detailed analysis of mid- and long-term energy strategies that could be initiated in 1974.

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Belgium-Luxembourg: Energy Data

	Primary Energy Consumption by Source (Percent)	Share Imported (Percent)
Total	**100**	**86**
Oil	58	100
Natural gas	13	99
Coal	28	52
Hydro/nuclear	1	88

	Pattern of Energy Consumption (Percent)
Residential, commercial, and agriculture	38
Industrial	52
Transportation	10

	Crude Oil Imports[1] 1972	
	Thousand b/d	Percent
Total	**879**	**100.0**
Arab	424	48.2
Saudi Arabia	268	30.5
Kuwait	127	14.4
Other Arab	29	3.3
Iran	100	11.4
Other	355	40.4

1. Oil requirements are less than crude oil imports. In 1972, net exports of petroleum products amounted to about 250,000 b/d.

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