Chapter 6

Conclusion
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OPEC has passed through different stages since its inception in 1960. During first decade of its formation, the organisation was acquiring shape and cohesion by defining the rules of the games among its members as well as was engaged in negotiating with the oil companies. In the seventies OPEC emerged as an effective organisation to influence the global oil prices. It acquired near monopoly control over prices, but in retrospects, it appeared to have ignored the parallel developments that were taking place in the oil market. Infact it was the so called 'first oil shock' that triggered these changes but the OPEC failed to take notice of them in deciding its price strategy. Consequently by the end of the seventies, OPEC overshot the prices. Thus creating more than enough market space for the rise of non-OPEC suppliers. Shaikh Yamani, former Petroleum minister of Saudi Arabia has very aptly put it, that a sense of excessive euphoria created a "false sense of omnipotence. In turn this arrogance of power, with the inavitability of an ancient Greek tragedy, led finally to namesis and a serious weaken-
The oil wells became cost effective all over the globe once the prices touched the figure of $39/b. No wonder that by the beginning of the eighties, the non-OPEC supply became critical enough to defy the oil prices determined by OPEC. It is pointed out that "During six years (1979-85) of very high prices OPEC was forced to shut in almost 10 mb/d of production market of OPEC was being eaten away at the rate of 2.5 mb/d in each year. That trend if continued, the price might still have been $28-29/b but OPEC's revenue would have been much reduced since output would have dwindled". OPEC lost control over prices and its share as well. Its share in production share came down to 30% from 50%, and export share from 60% to 50%. OPEC thus in the eighties had to face a different market, a market where oil was flowing outside the OPEC channel, where technological innovations had brought some basic changes in the industry, where the leading consumer from the West had prepared a more

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1. MEES, 10-4-94.

comprehensive and co-ordinated strategy under the auspicious of the IEA. In short, the oil market witnessed coming up of many new players.

Alongwith the changes in the global oil scenes, the power structure within the OPEC also underwent a shift following the structural changes initiated by the member states in their respective economies. As pointed out by Ian Seymour that "There was a time when the barrelage weight of Saudi Arabia was balanced or even overridden by the political clouts of other regional players such as Iraq, Algeria, Iran and even Libya. In early 1980s Saudi Arabia became the swing producer.³ Though the Saudi Arabia had to bear the cost of being swing producer but it did require a distinct leverage within the OPEC on price determination. Moreover the OPEC members got divided in their oil strategy between the Price seekers and volume chasers. This divide had decisive impact on OPEC's functioning. In other words, OPEC in eighties had to function in a global market when it did not have much leverage, and had to respond to competing and conflicting demands of its members in formulating its

³. MEES, 25-4-94.
strategy addressing to the global changes. In the preceding pages an attempt has been made to analyse and examine OPEC behaviour against the above context.

The issues dominating the organisation functioning in the eighties clearly show that OPEC had to change its strategy in favour of defending the market share to maximum oil revenue. This was the departure from the earlier of price maximisation. But not being able to control, leading to massive loss of revenue. OPEC decided for production restraint. It set-up production ceiling and quotas in compliance of its objective to maintain price stability in the global oil market. But revenue needs of the members varied, most often, the members did not comply with the OPEC discipline. Consequently, it could achieve neither. So OPEC in eighties lost both market share and prices. As pointed out by Sheikh Yamani, "OPEC did not learn much from 1985 episode, leaving oil prices to find their own level, or it can set government selling prices. It is self evident that OPEC cannot rigidly regulate both volume and prices, it lacks the degree of monopoly power to achieve the level of market control." (MEES 18-4-1994). The point is that the
changed market conditions led to decline in the initial power of OPEC. Basically, the member state did not recognise stark reality. The divide between 'price seekers' and 'volume chaser' quite often led to defeating moves made by the OPEC. Thus OPEC agenda in eighties was dictated by the changing nature of oil market, differences among the member states as well as pressure from the rising non-OPEC exporters. It was more at the receiving end than on dictating terms.

The market share strategy pursued by OPEC though failed to earn larger volume despite high production but did help in achieving objective of eliminating the non-OPEC competitors.

Table No.1

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<tr>
<td>The Cost of Policy Reversal</td>
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<tr>
<td>Petroleum Products (bn/B)</td>
<td>57.1</td>
<td>60.8</td>
</tr>
<tr>
<td>Local Consumption (bn/B)</td>
<td>7.3</td>
<td>9.6</td>
</tr>
<tr>
<td>Petroleum Exports (bn/B)</td>
<td>49.8</td>
<td>51.2</td>
</tr>
<tr>
<td>Petroleum Export Revenue ($ bn)</td>
<td>1385.0</td>
<td>829.0</td>
</tr>
<tr>
<td>Average Price ($/b)</td>
<td>27.8</td>
<td>16.2</td>
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Source: N. Ait Laoussine, 'OPEC from within a Non-Gulf Market's Point of View' (MEES 25.4.1994).
The above table makes it clear that OPEC exported more during the market share regime i.e. 51.2 bn/b as against 49.8 bn/b in price maximisation regime but could earn only $829 bn, as against $1385 bn. But as Stauffer has argued the strategy it did help OPEC to eliminate most of the competitors except Norway. According to his findings:4

I. Non-OPEC competition has been almost eliminated: under high prices non-OPEC took some 9 mb/d away from OPEC; since 1985 net changes in non-OPEC production have been essentially zero. Declines in some areas offset increases elsewhere.

II. OPEC production has grown steadily since 1985 by more than 1 mb/d per year thanks to the elimination of net competition from non-OPEC producers.

III. Growth since 1985 contrasts sharply with the period of high prices. Then OPEC production was either stagnant (1973-79) a falling rapidly by more than 2 mb/d per year (1979-85).

IV. Low prices have created 'victims'. They forced cutback in production in several areas. In the USA 2.5 m b/d of price-sensitive production has been lost, plus another 400,000 b/d in Alaska. In Australia and Canada unsubsidized production has also fallen Slowly, unable to compete at prices of $ 16-18/b.

V. Casualties of low prices were important competitors such as Mexico and the U.K. Their erosion of OPEC's market was halted. Previously Mexico and the U.K. had captured almost 5 mb/d from OPEC; further inroads stopped totally after 1985. Increased output from smaller competitors such as Brazil, Egypt and India was also halted.

VI. Smaller low cost competitors have survived - Angola, Malaysia, Oman and Syria have added 2 m b/d since 1985 in spite of low prices. Prices would need to fall below $10 to deter that development.

VII. Norway is anomalous important 'survivor'. Norway added more production after 1985 than it had under the protection of high oil prices. Most of those fields had been discovered when oil prices were high and new fields pay no royal-
ties, but nonetheless total costs in Norway are known to be high and sustained developments is surprising, even allowing for the inertial effects.

Low oil prices crippled at new competition from non-OPEC. They have had other favourable consequences. Some additional nuclear and coal plants have doubtless been deterred and expansion of competing sources of natural gas has been slowed, overall it is clear that low prices were indispensable to OPEC's recovery from the downhill slopes of mid 1980's.

The manifestation of crisis in the form of price and output had direct bearing on intra-OPEC conflict. The change in the nature of crisis had a corresponding impact on the conflict. The intra-OPEC conflict had sharpened on price and quota issues during the eighties. There was complete lack of discipline among OPEC members on the important agreements especially on price and production ceiling or quota. The basic element of the price lies in OPEC's failure to agree on pricing and production rates for much of the years in 1980's. It had become a difficult task for the organisation to determine the output ceiling for each member
states and price rate for crude oil. The members do not want to lose their output share as their economies unable to permit to go beyond a point. On the demand side, OPEC oil had declined throughout eighties from its 1979 level. OPEC had a long coordinated policies of their production and pricing before 1980 when there was tight demand. But in the eighties, they had started infighting on these two issues in the most of the years in eighties. In fact, the consistent violation of past OPEC production guidelines by some member-states contributed to the oil glut which had pushed the price at their low level.

As it is evident from Chapter III that there were broadly two groups: one group advocating lower prices led by Saudi Arabia, Kuwait and UAE and the group two led by Iran, Algeria, Iraq and Venezuela for higher oil price. It is therefore obvious that long-term conflict will then arise when Saudi Arabia and Kuwait advocate lower price than other member's desire. A simple composition is diagrammatically represented in the figure 1.

In this figure, where group (1)'s marginal cost is shown as $u_1$ and other member's marginal cost is designated
Figure 1. The Limit to Coalition Between Two (or Two Groups of) Producers
as \( u_2 \). The figure shows the upper limit to consensus. That is when \( u_2 \) shifts up to the position shown in this figure, Saudi Arabia, Kuwait and UAE to move out of OPEC alliance. These countries have major influence in OPEC because of their very high oil reserves than that of other members of OPEC. This will then charge their own desirable price, one at which other members cannot produce profitably. The very existence of OPEC depends on these member’s move. Thus, Intra-OPEC conflict will adversely affect to vary survival of OPEC.

The emergence of non-OPEC producers was one of the foremost source of uncertainty for OPEC’s ability to operate as a Cartel. At the March 1983 conference, for the first time in its history OPEC was forced not only to seek cooperation from non-OPEC producers on the issue of pricing but also to ponder the need for sustained cooperation with them. Though it is one of the important objective of OPEC to have a cooperation with other producers for the stability of oil market, OPEC made attempts to seek their cooperation in eighties when OPEC failed to bring stability in the global oil market on its own strength. But OPEC’s production programming was threatened by volume maximising and price
under-cutting activities of non-OPEC producers. The October 1984 production programming arrangement as well as January 1985 price reduction decision of OPEC were result of continued volume maximisation by north sea producers. The action of north sea producers became increasingly significant in OPEC as well as oil companies between 1983 and 1985. For OPEC, their significance stemmed from the fact that since 1983, Nigerian oil pricing policy had been determined not by OPEC decision but how British and Norway were responding to OPEC decisions. Throughout January 1985, it was becoming increasingly clear that in view of very large volume of oil coming on spot market from North Sea producers, "The price of oil destined to go down further" oil traders seemed to have found new leverages in Britain and Norway to sustain downward pressure on OPEC prices. Non-OPEC producers decided to follow-up their volume maximisation with aggressive pricing and marketing policies. This policy of non-OPEC was one of the major factor for creating glut in the global oil market in the eighties. Summing up, it can be said that the attitude of non-OPEC, especially U.K., was remained in-cooperative throughout the eighties.
The International Energy Agency was formed to counter the moves of OPEC. Though its main objective is responding to oil crisis and providing oil security to member-states. But it is evident from chapter V that IEA basically adopted strategies to counter OPEC moves more than providing oil security to its member-states. The basic aim is to reduce oil consumption and encourage fuel switching measures - through its International Energy programme contained short-term as well as long range policies. The short term programmes were aimed at protecting oil consumers, discouraging them from bidding competitively for available oil supplies. The purpose of long-range policies were: to develop among all importers long-term cooperative mechanisms aimed at reducing dependency on imported oil, to create an oil market information system aimed at improving knowledge of the functioning of global oil market.

The study makes it clear that an organisation like the OPEC can be effective only under certain conditions. It does not work in vacuum; so in the eighties when the global oil environment underwent change and the member states found divergence of interests, OPEC found it difficult to perform its role as it did in the seventies. Nevertheless, despite
various constraints, it did contribute in influencing the oil market from the margin. It is clear that as the oil market has evolved over the years many new players have come and the market has become more sophisticated. OPEC cannot and ought not to be expected play the role in the seventies. The experience of eighties suggest that OPEC has to redefine its role to the emerging market realities. It will be able to do so only if members states become more sensitised to it.