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Energy Insider

Market structure aids oil crisis threat

by William Engdahl

From the standpoint of global strategy, the timing is very advantageous from the Soviet point of view for triggering a new world petroleum crisis.

World consumption remains several million barrels below the peak year of 1979. On average, for 1983, the world produced 57.9 million barrels per day (bpd) of crude oil. At the height of the 1979 Iran crisis, the world produced 62.7 million bpd. The decrease in output occurred because Mideast OPEC producers have averaged a severely reduced 12.0 million bpd for the past year, compared with an average 21.2 million bpd four years ago. Due to soft demand—a major indicator of the lack of industrial recovery in the West—the OPEC official benchmark price for Saudi light crude plummeted in 1983 by $5 a barrel to $29.00.

This "slack" market could tighten in minutes should the Iranians make good on threats to shut the Strait of Hormuz or possibly make a surgical missile hit on the principal Saudi oil port at Ras Tanura with the SS-12 Soviet missiles they are said to have recently obtained. Here is what is at stake.

Supply and prices

Every day, some 8.5 million barrels of crude, about 20 percent of the free world production, move aboard huge oil tankers from Iran, Iraq, Kuwait, Saudi Arabia, Qatar, and the United Arab Emirates. They all must pass through the 24-mile-wide Strait of Hormuz. Though recent engineering studies calculate it would be highly unlikely sufficient tonnage could be sunk to physically block the Strait, which is two to three hundred feet deep, a dramatic hit on a large tanker would prompt Lloyds and other major insurers of oil tankers to charge prohibitive war premiums.

What would be the effect of even a temporary loss of this 8 million bpd? For Japan and large parts of Western Europe, which are highly dependent on Gulf oil imports (Japan imports 100% of its oil needs) it would be catastrophic (see *EIR*, Feb. 28). Even though at this point, there is a certain smugness around Washington and New York that the United States is no longer heavily dependent on oil from the Persian Gulf, the price impact of such a crisis would be staggering to a world economy on the brink of complete crisis.

The Dallas Federal Reserve Board calculates that some 4 million bpd could be made up more or less immediately from alternate routes and untapped capacity in other producing regions. Such options include Nigeria, which could easily add another million barrels to its daily output, as well as Indonesia and Venezuela. In addition, over the past six months, Saudi Arabia has been pouring an immense stockpile into a "floating reserve" estimated at close to 70 million barrels.

Decentralized markets

The danger is not, then, the threat to supplies so much as the transformed nature of the international petroleum market since the 1979 "oil shock." While in 1978, only a tiny 2-3% of total world oil sales were taking place in the short-term so-called Rotterdam spot markets, today 40-50% of world oil trade is traded in spot. This means that the global market is vastly more open to panic bidding than ever before.

Added to this is the introduction of a major new element of pure speculation in paper with enormous panic potential in any perceived shortfall crisis. This is the creation of the New York Mercantile Exchange, known as NYMEX, and its London International Petroleum Exchange counterpart. Rather than selling actual cargoes of crude or refined petroleum products, these speculative boondoggles bloat paper prices based on "futures," anticipated future rise or fall in oil price. Almost overnight, the NYMEX daily trades an average of 9.5 million bpd. A short-term supply crisis could be magnified into a price panic through the combination of the new futures market and the high spot market dependence.

And the man heading this new NYMEX futures operation gives rise to additional concern. He is John Treat, the man who ran Carter Energy Secretary James Schlesinger's Iran Emergency Task Force in 1979. As this writer documented at the time, Schlesinger's deliberate supply manipulations during that crisis were a major factor to force panic when the actual shortage was non-existent. Treat is well primed to force a new price crisis this time around.

"The creation of the New York oil futures market," one West Texas oil trader told me, "allows a tiny handful of insiders with large funds to have enormous impact on manipulating price." Over recent weeks, Treat has made an attempt to persuade the Reagan administration to turn major portions of the almost 400 million barrels of government Strategic Petroleum Reserves now in underground storage in Texas and Louisiana over to NYMEX speculative control. The eruption of a new Mideast crisis could give Treat the lever he needs. A U.S. Department of Energy simulation last summer calculated the price of oil would soar to $95 per barrel from the present $29 per barrel within eight weeks of the closing of the Strait of Hormuz. Treat's NYMEX is one reason such a scenario is entirely possible.

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