“Follow the money” is the advice routinely offered to detectives in low-budget thrillers. For anyone attempting to understand the ebbs and flows of international politics, I offer a variant of that old line: “Follow the oil”.1

This book grew out of the need for a comprehensive examination of the interaction of politics and oil in all dimensions at both the national and international levels. Its chapters capture the diversity and complexity of the global oil system, as well as those of many key oil-consuming and producing countries.

The volume’s various themes are intended to provide a deeper understanding of the forces that have led to a series of booms and busts in oil prices, instability in the global economic system, economic nationalism, growing concern over climate, and, most recently, regime change in the Middle East. The forces described in the chapters that follow will no doubt also serve as catalysts for many future developments as well.

The global energy dilemma that the world currently faces serves as the book’s unifying focus. Can we have secure, reliable and affordable supplies of energy and, at the same time, manage the transition to a low-carbon energy system? What policies are needed to make this transition and what factors impede it? Do we, either nationally or internationally, have the political will to make the hard decisions required?

To this end, the volume is divided into five main sections. The chapters in the first section examine the problems surrounding the continued availability of oil at reasonable prices. Those unfamiliar with the workings of the oil industry may be surprised to learn that experts are less concerned over oil’s physical availability than with a broad spectrum of uncertainties that surround the petroleum industry.

Paul Sullivan’s excellent overview in Chapter 2 looks at these uncertainties, as well as at many of the themes in the chapters that follow. He points out that it is unclear how politics, political instability and war will affect future oil exploration and production. It is also impossible to predict how changing attitudes toward technologies, like transportation, that contribute to climate change will combine with increased energy demand by developing countries to affect the demand for oil and overall conditions in the petroleum industry. Sullivan suggests that such potential conflicts between oil producers, consumers, environmentalists and other concerned...
groups cannot be resolved simply through reliance on the market price incentives and disincentives of the past, but will require political action.

Michael Klare’s discussion of the politics of oil in Chapter 3 expands the uncertainty theme. Klare notes that geopolitics and oil have been closely intertwined for a very long time. Given oil’s strategic importance to the efficient functioning of modern economies and military organizations, it is not surprising that the geopolitical picture has often been dominated by the efforts of the major oil-consuming economies to gain and retain influence in the major oil regions. Similarly, because key oil suppliers are often located far from the major sites of consumption, control over oil transportation routes is another source of geopolitical contention. As long as oil remains a critical commodity, oil-related conflicts are likely to be part of the geopolitical equation.

It is often assumed that the increasing share of world oil produced by national oil companies (NOCs), as opposed to profit-maximizing private international oil companies, (IOCs) provides an additional source of uncertainty. This assumption is based on the fact the ultimate goals of the NOCs are to maximize long-term economic benefits to their respective countries, whereas the IOCs attempt to maximize short-term benefits to their shareholders. Jean-Francois Seznec, however, comes to a different conclusion in his detailed assessment of NOCs and IOCs in Chapter 4, arguing that the 10-year lead time from decision to refining requires the IOCs to similarly engage in long-term planning. Based on this, he concludes that it is not surprising that many NOCs, like Total, Sinopec, Rosneft and Lukoil, have moved to private portions in their shareholding and predicts that NOCs may increasingly come to be owned by the public at large.

One area of uncertainty that has captured the imagination is peak oil, which is the point at which the world’s petroleum output can no longer increase and production begins to level off or decline. Popular commentators often use the concept as a jumping-off point for speculation that the world is facing a painful and even catastrophic adjustment period. While peak oil makes intuitive sense, Laural Graefe’s examination (Chapter 5) suggests the concept itself is imprecise and sheds little light on future uncertainties. For example, on the supply side, how much will companies invest in capacity? How will extraction and refining technology advance? How many hurricanes or wars will occur in oil producing regions? Similar unknowns exist on the demand side. In the end, Graefe concludes that the time at which peak oil occurs is at least partially under our control and that, by acting with foresight, it is possible to accomplish a smooth transition to fewer hydrocarbons and increased usage of other forms of energy.

A very different form of uncertainty over future oil supplies comes from the instability associated with many of the oil-producing countries, especially those in the developing world. In Chapter 6, Michael Ross associates this instability with the oil curse, a combination of factors that includes overvalued exchange rates (the so-called Dutch Disease), wasted revenues during boom times, and the increased corruption which high oil revenues facilitate. These factors often combine to produce stagnating economies ruled by authoritarians with little interest in the public good that eventually degenerate into high levels of violence, instability and reduced levels of oil production. As Ross notes, however the situation isn’t hopeless, pointing to Canada and Norway as examples of countries that overcame the oil curse to become reliable suppliers. Hopefully, such examples will provide inspiration and instruction to new leaders and regimes wishing to develop their economies.

One way to increase the certainty of future oil supplies and prices is through improved cooperation between the producers and consumers, which in the past has been marred by mistrust and deceit on both sides. Paul Stevens explores the outlook for a more constructive dialogue between the two groups in Chapter 7. As in seemingly all group situations, the call of
“why can’t everyone just get along” becomes more imperative than ever with increased instability in the producing countries and slack growth in the major consuming nations. Sadly, after exploring possible avenues of co-operation, Stevens finds it unlikely that much progress will be made. As he notes, “… the fundamental self-interest of the marketplace will always provide a cold dose of reality to dampen desire for dialogue or co-operation.”

In Chapter 8, the final paper in this section, Giacomo Luciani examines the uncertainty factor stemming from the structural instability of crude oil prices – the result of a series of rigidities in supply, demand, costs and associated short-term factors. Luciani, however, finds room for optimism, pointing to the willingness of Gulf countries to assume the role of swing producers, coupled with the increased storage capacity of consuming countries. In addition, he cites a number of exciting new financial instruments that have a great potential for reducing oil market uncertainties.

All in all, the papers in this section document the dramatic changes taking place in the oil industry and associated institutions. Unfortunately, with so many degrees of freedom, scenarios ranging from the highly optimistic to the catastrophic are possible. The next section attempts to shed further light on future developments in the industry by focusing on political responses to many of the problems identified above. Are there adequate policies that can be put in place to dampen instability stemming from the oil markets? Will governments have the will and courage to confront problems before they spiral out of control? All political solutions are complicated by two increasingly pervasive forces: climate change and the need for increased security.

Energy security clearly means different things to different people and countries, but, as Dan Moran observes in Chapter 9, at its center lies a basic concern about access to energy resources. Security concerns began with Churchill’s decision in the early 1900s to diversify suppliers to avoid over-dependence on Persian oil and grew dramatically in the early 1970s with the rise of OPEC and the oil embargo. While energy security has a nice political ring to it, Moran reminds us that energy security is not an absolute value, but rather exists in varying degrees. It cannot be achieved without some proportional sacrifice of other social goods. “Sound policies to sustain it must be based on realistic expectations of what is possible, a fair accounting and equitable distribution of the sacrifices involved.” Viewed in this light, Alan Reynolds’ assessment of US policymaking (Chapter 17) becomes even less reassuring.

As James Russell notes in Chapter 10, American presidents in the post World War II era have been reluctantly drawn into the maze of Middle Eastern politics and security. Future American foreign policy in the region will be further complicated by “the myriad and cumulative challenges from climate change.” While the Middle Eastern countries are not among the major contributors to the factors underlying climate change, they will become its victims as climate change accelerates a series of already negative trends in the region. Such trends include decreased precipitation and resulting crop failures, as well as flooding in highly populated low-lying coastal areas. Clearly these changes will create even more instability in an already unsettled part of the world. As with several other authors in this volume Russell is skeptical the USA will be willing and able to provide the leadership necessary to reverse many of the forces leading to a warmer planet. “Only if and when this happens can the Middle Eastern states and the international community begin to start building policies that will address the systemic challenge posed by climate change in the region.”

A popular notion, especially on many of the web’s conspiracy sites, is that the USA deals with its energy security directly – by going to war and taking over oil fields in countries such as Iraq. As David Henderson notes in Chapter 11, even a sophisticated thinker like Alan Greenspan has argued from time to time that wars for oil make a certain amount of sense. Henderson
refutes this argument by demonstrating that the case for “war for oil” is profoundly weak, whereas the case against it rests on sound economic analysis. In stark terms, our oil supply is secure, not because our government threatens to use force against those who would make it insecure, but because the world’s oil suppliers want to make money.

The chapters in the section illustrate that there exists in the major oil-consuming countries a large body of sophisticated analysis capable of providing straightforward policy solutions to most of the world’s energy problems, even those closely intertwined with climate and security considerations. Unfortunately, this analysis has little effect on actual policy-making. There is plenty of oil in the world, yet policy-makers fret over self-inflicted oil shortages while doing little to expand supply. The planet is rapidly warming, yet policymakers do not feel immediate pressure to take action and, instead, pursue policies that speed up the warming. Even countries that hate the West are willing to sell large volumes of oil on a regular basis, yet military action and a large defense presence in the Gulf is felt necessary for energy security.

The chapters in the next section demonstrate that policymaking in many of the producing countries, while admittedly focused on a different set of issues, has been even more flawed, inept and even self-destructive. There is something about oil that seems to prevent people from applying logic and common sense to the issues that arise from its continued production and use. Clearly, oil rents corrupt, but their corrosive effects often go much deeper.

Jessica Piombo (Chapter 12) notes that, based on generous human and natural resource endowments, Africans possess the means to become among the wealthiest people in the world. Instead, they tend to rank lowest in most economic and human development indicators, and their political systems are often among the most corrupt and authoritarian. The worst performance occurs in the countries with the largest mineral resource endowments, and of these, the petroleum-rich countries have the most dismal records in governance, inequality and human development. Plimbo’s analysis clearly makes the link between oil and deprivation in sub-Saharan Africa. The causal mechanism is straightforward: regime concerns with maintaining control over oil rents undermine government accountability and increase authoritarian tendencies, while access to oil rents increases regime stability even as it attenuates the link between rulers and citizens.

Oil has created a somewhat different set of political and policy problems in Latin America. While oil rents have not been as detrimental to governance structures, Sidney Weintraub (Chapter 13) observes the region’s policymakers have failed to design programmes to transform oil wealth into the basis for strong, dynamic economies. Most often short-term political gains have trumped sound energy policies that emphasize a long-term viewpoint. Policies lack coherence because they have alternated between market-friendly and nationalistic orientations. Instead, they have focused on increasing domestic political support by limiting exports to ensure a cheap domestic supply, providing generous subsidies to ensure cheap domestic energy, and expanding the state in production to increase government revenues. Weintraub warns that: “These policies will ultimately backfire, as the statist energy policies from the 1950s-1980s did, and their successors will be left with the cleanup.”

Energy politics and resource policymaking have not fared much better in the oil-abundant countries of the Middle East. As Hossein Askari notes (Chapter 14), in the oil-exporting countries of the Persian Gulf, economic and social policies have been largely designed to support the royal families (Kuwait, Qatar, Saudi Arabia and UAE) or ruling elites (Iran, Iraq). As a result, corruption is commonplace. Askari charges that the current policy-making mix verges on criminality in that “viable institutions have not been nurtured because effective institutions would reduce the role and importance of ruling families and illegitimate governments and prevent them from capturing the oil rent that rightfully belongs to the citizenry.” His solution,
which is increasingly gaining acceptance, is the development of an oil fund that takes revenues away from the state and invests them on behalf of all generations of citizens. No doubt in the years to come many of the region’s deposed rulers will look back and rue the day they did not take this sound advice.

Many of the mistakes of the Middle East resource experience have been replicated in Kazakhstan, Azerbaijan, and Turkmenistan, where poor governance and authoritarian political structures are the norm. Richard Pomfret (Chapter 15) notes that in all three countries power is concentrated in the hands of the president. As in the Middle East, oil rents strengthen the incumbent’s position and free him from the need to seek the population’s support in order to raise state revenue. Pomfret warns that in the Caspian Region “… the dependence of economic and political decisions on the wisdom and health of the leader may be a source of future instability.”

The final chapter of this section sounds a more optimistic note. Benjamin Smith’s (Chapter 16) empirical examination of Southeast Asian oil producers, both old and new, reveals a strikingly broad set of oil-influenced political trajectories. From Brunei’s archetypical oil monarchy to Indonesia’s uneasy transition out of major exporter status to Malaysia’s surprising economic transformation, the older producers in Southeast Asia have put their oil wealth to a wide variety of political uses. Even more impressive, the region’s new group of oil exporters—Cambodia, Timor-Leste and Vietnam—illustrate both how potentially transformative and how modest a sizeable oil sector can be.

Benjamin Smith’s chapter provides an excellent transition to the next section of country case studies. While looking at broad regional patterns has some distinct benefits, Smith’s sound advice is that we should be careful in making blunt assessments that assume uniform relationships across all oil-producers. The chapters in this section provide detailed accounts of the unique political decisions that inform energy policy in six key countries: The United States, Iraq, Iran, Saudi Arabia, Egypt, Russia and Brazil. Their experiences confirm Smith’s assessment by illustrating how truly conditional the effects of resource wealth can be.

Alternative energy would seem to be the obvious solution to many of the world’s oil problems. In Chapter 17, Alan Reynolds notes that US alternative energy proponents with two quite different policy goals—reducing energy dependence and improving climate stability—share a common presumption that US passenger cars and the fuels they use are the single largest cause of both problems. As a result, US policies have centered on a series of tax credits, subsidies, and mandates to reduce automobile gasoline consumption and emissions. Focusing on the campaign to mandate and subsidize ethanol and also to subsidize the producers and buyers of hybrid and/or electrical cars, Reynolds’ painstaking analysis shows that these policies unfortunately have little merit as a cost-effective means of dealing with global warming or even the high volumes of imported oil. Instead, the evidence suggests that these policies were designed by energy interest groups to reward politically influential coalitions of industrial, financial and ideological interests. “In other words, realists would be well advised to not view valuable subsidies and mandates for alternative fuels and vehicles as a means to an end, but rather as the end itself.”

In Chapter 18, Abbas Kadhim looks at the destructive effects of oil in Iraq. There, oil facilitated policies that ultimately depleted the country’s infrastructure, exhausted its human capital and retarded its economic potential through wars, political oppression, and the prohibition of modern technology and the free flow of information. With the overthrow of Saddam Hussein, the country has the opportunity to make a new start, and there are indications that its leaders may this time use oil revenues to compensate for the missed opportunities of the past.
The misuse of oil revenues also underlies many of the problems confronting present day Iran. Rather than dwell on the standard litany of oil-enabled policy failures, Farrokh Najmabadi’s (Chapter 19) fascinating account of the country’s oil industry illustrates how rentier state environments impede wealth creation, even in industries critical to regime survival. He notes that, from a technical perspective, the country’s oil industry could possibly double its rate of production in the medium-term. Unfortunately under the present regime such a scenario is highly unlikely. Najmabadi concludes that, even in the absence of today’s political and ideological interference, unless Iran’s oil and gas sector becomes more accountable and transparent the best it can do is muddle through.

Given its history, the role of its royal family and its enormous reserves of oil and gas, Saudi Arabia may be a very unique case. The kingdom has not abused its oil revenues as in Iraq, nor has it descended into the stagnation and inefficiencies so prevalent in Iran. While those countries have experienced falling rates of production and export over the years, Joseph Kéchichian (Chapter 20) documents the responsible way in which oil policy has enabled the country to stabilize oil markets. He concludes that the country’s willingness and ability to expand production should ensure it an enduring role as a contributor to world supplies for the foreseeable future.

Because Egypt is not a major oil producer, certainly by MENA standards, its economy is not typically described as being driven or even heavily influenced by hydrocarbons. In recent years, however, the situation has changed. As Robert Springborg notes in Chapter 21, nearly three-quarters of the country’s merchandise exports were comprised of oil and gas in 2007. Unfortunately, despite being a relatively new hydrocarbon producer, Egypt appears to have learned little from the failed oil policies of its neighbors. As a result, Egypt’s hydrocarbon-based development strategy is not sustainable nor does it lay the foundation for an alternative mode. As Springborg characterizes it, the “… authoritarianism once associated with state capitalism was reinvented within what was nominally a privatizing economy, but which in reality was an economy whose commanding heights were controlled by regime cronies.” After reading Springborg’s analysis, the reader comes away with a much clearer understanding of the forces that eventually resulted in the overthrow of the Mubarak administration.

In Chapter 22, Philip Hanson observes that if Russia is a petro-state, it is a rather unusual one. Its economy is moderately developed and diversified. It exports metals, nuclear reactors, weapons systems and, in most recent years, grain, as well as hydrocarbons. It is clearly an exception among major oil exporters in that around 60% of its oil is produced by private firms. On the other hand, the country shares many negative traits of oil economies. Energy rents account for a large share of government revenues and exports and have enabled the regime to retain many of its authoritarian tendencies. While there is no national oil monopoly, the government exerts undue political pressure on Russian oil firms, and international oil companies are restricted. Given the government’s opaque and informal involvement in the industry, Hanson is not optimistic about the future development of the country’s vast hydrocarbon resources or the constructive use of the revenues they generate.

This section on country experiences ends on an optimistic note as Flavia Carvalho documents the creation and rise of the giant Brazilian oil company Petrobras in Chapter 23. Petrobras is a rare success story coming out of the import substitution process common throughout Latin America in the 1950s, 60s and 70s. Of particular relevance are the strategic and political motivations for setting up a strong national oil industry. Import substitution should be looked at as an investment in the future, and that is how the Brazilian government approached the development of Petrobras. In contrast to other oil-based developing countries, the Brazilian government has played a positive role by providing the resources and human capital necessary to
foster technological excellence and efficiency. Petrobras demonstrates the potential of objective, farsighted policies and the proper use of oil rents to expand the productive capabilities of a hydrocarbon rich economy.

The papers in the final section of this volume revisit some of the main themes developed previously and speculate on how they may play out in the future. Will the oil curse continue to plague many hydrocarbon based economies (Richard Auty, Chapter 24)? What will the main challenges be in global oil governance (Andreas Goldthau, Chapter 25)? What does the future hold for sovereign wealth funds (Gawdat Bahgat, Chapter 26)? Will the dollar maintain its role in oil trading or will the international monetary system undergo a major transformation in the years to come (Eckart Woertz, Chapter 27)? How will China’s rise impact oil markets (John Calabrese, Chapter 28)? Finally, Daniel Johansson, Fredrik Hedenus and Thomas Sterner (Chapter 29) take on the question of the day: what is the future of oil in a carbon-constrained world?

While various chapters in this volume clearly document past mistakes in the critical area of national energy policy-making, many chapters also offer hope for oil policy-making in the future. One can only hope that governments will have the wisdom to learn from past errors and the foresight to take a longer term approach in both their management and use of the world’s remaining hydrocarbon resources.

Note