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ENERGY AND NATIONAL SECURITY

Good afternoon. It is a pleasure to join you at this Twenty-Seventh Annual Student Conference on U.S. Affairs.

The topic of this conference -- "The Politics of a Changing Global Economy" -- has many facets, each one a fit topic for dozens of dissertations. You can analyze politics, for example, at any number of levels, from the county court house to the United Nations. And the global economy today involves such a dynamic process that it is, in fact, always changing.

But perhaps the one major characteristic of the global economy is interdependence. The term global economy implies interdependence: We depend heavily on the rest of the world for certain goods, and they, in turn, depend on us. And politics can be defined as the effort to develop predictable relationships that take the insecurity -- and hence the fear -- out of interdependence.

Politics -- if successful -- enables people and nations to accept that condition of interdependence, confident that it will not evolve into dependence, and then into subservience.

This afternoon, I would like to reflect on that concept in the context of energy -- specifically oil -- and on the implications it has for the domestic and international relationships that the United States has developed over the last thirty years. And I would like to begin by looking at some of the history of international oil.

Clearly, the most dominant factors in the development of Middle Eastern oil between the two world wars were the large, integrated international oil companies. British dominance in the Mideast assured a stable political and economic climate allowing the oil companies to explore, develop, produce, transport, refine, and market oil in growing quantities.

It was the companies -- and only the companies -- which had enough expertise and experience with petroleum to make the key decisions vital to the industry and therefore to the countries of the Middle East -- decisions on price and supply.

In the years following World War II, colonialism around the globe began to disintegrate. The process had its effect on the Middle East, but because the oil producing nations had little internal political cohesion, and no experience in the oil industry, control of production remained in the hands of the companies.

That same post-war period saw the United States as the single most influential nation in world affairs. Our economic and military power was second to none. Through the Marshall Plan, we had declared our intention to see Western Europe returned to economic health and political strength. We were the prime mover in establishing the International Monetary Fund and the General Agreement on Tariffs and Trade.

As a result, Western Europe and Japan stabilized, rebuilt and recovered. Under American military, political and economic guarantees, world trade began to grow at an unparalleled rate.

But underlying that economic growth was the assumption that vast amounts of oil would be available at reasonable prices. The only area of the world capable of providing that oil quickly and cheaply was the Middle East.

Many of you already know that that area contains some sixty percent of the world's crude oil reserves. But consider this fact: In the past 40 years of global oil exploration, well over half the significant discoveries have been in the Middle East. In fact, if the United States alone had to supply the world's oil needs, our reserves would last for two and a half to three years; the Middle East oil producing nations, on the other hand, could supply the world for twenty to twenty-five years.

For a quarter of a century, through the instrument of the international oil companies, those reserves were available to the industrialized west on acceptable terms. So heavily dependent were the industrial economies on oil that between 1950 and 1973, free world oil production rose from 10 million to 45 million barrels a day -- an increase of 450 percent. Two-thirds of that increase came -- as it had to -- from the Middle East.

But it is also important to remember that during the post-war period, the flow of Middle Eastern oil was repeatedly interrupted.

After the 1949 war in the Middle East, supplies of oil were curtailed, as they were after the Suez Crisis of 1956, and the Six Day War of 1967. In all three instances, the effort to accomplish political ends through the use of petroleum was unsuccessful -- primarily because of excess oil production capacity in the United States.

Nevertheless, these curtailments of oil supplies were clear evidence of rising nationalism among the Middle East oil producers, and of their desire to control the oil they were exporting to the rest of the world. That determination was manifested in a cooperative fashion in 1960 when Saudi Arabia, Iraq, Iran, Kuwait and Venezuela established the Organization of Petroleum Exporting Countries.

By 1973, the Middle East oil producing countries had developed enough technical and managerial ability to make workable decisions on price and production. And when the October War overcame -- at least temporarily -- the traditional distrust among Arab states, they united to impose the oil embargo of 1973-74.

By that time American oil fields no longer had excess capacity. Thus, the fourth interruption of supply was effective -- both in pursuit of political ends and the attainment of economic objectives. The price of oil since that time has more than quadrupled -- from $3 to $12 a barrel -- or from 8 cents to 30 cents a gallon.

Now most of us in the United States measured the effectiveness of the embargo by the length of the lines at service stations and the price of a gallon of gas. But look at it another way. The embargo was successful enough to cost the U.S. economy from $10-20 billion, and a half million jobs.

And by comparison, most of our allies were even worse off.

Together, Western Europe and Japan make up a far larger part of OPEC's market than the United States. For all practical purposes, Japan, the United Kingdom, the Netherlands, France, Belgium, Luxembourg, Italy and Spain are one hundred percent dependent on OPEC oil, while West Germany fills seventy percent of its needs with OPEC oil. And most of the European countries in that group can be spelled with four letters -- N-A-T-O.

Norway and the United Kingdom will eventually be self-sufficient. But for now the economies of our traditional allies in Europe are, in a very real sense, hostage to the supply of oil from the nations that make up OPEC, the major members of which have clearly defined political and economic objectives.

One of those objectives -- maximizing their profits -- was realized when they successfully increased world oil prices. And, when that happened, the shock waves in Europe reverberated throughout the alliance.

The strength of those shock waves can be measured in money. Italy, for example -- already running a trade deficit -- was forced to the edge of national bankruptcy by the price increases. Every single nation was hurt. Some ran drastic deficits. Others -- very few -- saw once healthy trade surpluses reduced to insignificance. As a result, those nations which make up the Organization for Economic Cooperation and Development -- NATO, most of the rest of Western Europe, as well as Australia, New Zealand and Japan -- ran a cumulative deficit of almost $30 billion. At old oil prices, they would have run a surplus of more than $35 billion.

The reaction in some international financial circles bordered on hysteria. Though they gradually adjusted to the initial shock, there was talk of imminent economic collapse and the end of western civilization as we had known it. Obviously, neither has happened. The international financial system has -- so far -- successfully coped with huge transfers of funds between oil producing and oil consuming countries.

But we have to remember that our ability to cope was enhanced by world-wide recession caused, in part, by exorbitant world oil prices. As the world recovers from the recession, there is no guarantee that the international financial system will be able to manage increasing transfers of funds successfully. And there is no guarantee, in the cases of those countries with the weakest economies, that economic recovery is possible with the new high cost of oil.

And that uncertainty could persist, unless the world economy -- particularly the United States --permits an adjustment to these prices.

Nor is there a guarantee against future embargoes, and that possibility will remain a very large and unpredictable element in world economic and political calculations from now on.

The implications of this situation for our allies, and consequently for us, are enormous.

The embargo of 1973-74 strained our whole system of alliances more than any single event since the end of World War II. There was confusion and panic among many of our allies who were caught in the scramble for favorable treatment by the oil producing countries. For example, there was considerable apprehension over whether the United States would be allowed to re-supply Israel from certain NATO bases in Europe.

Aside from the economic and strategic implications of this dependence on Middle Eastern oil, we also have to consider its impact on U.S. military guarantees. In short, how much does our reliance on foreign oil producers undermine the credibility of our military commitments around the world, and, consequently, the balance of power?

The nuclear stalemate makes it extremely likely that any future disputes will be characterized by limited wars, confrontations that stop short of violence or localized disturbances. Those conditions require prompt and flexible responses, all of which depend on adequate energy supplies for use by the military.

But in 1973, the embargo introduced new problems into American military logistics. For instance, commanders of ships and planes in the Mediterranean, which often have to be fueled from the continental United States, had to begin wondering about supply reliability.

Luckily, it was reliable. But without secure supplies in the future, the range of our responses would be limited. And what is more to the point, the very perception of those limitations encourages more disturbances, more confrontations, and a more dangerous world.

Of course, the American military needs a strong industrial base. Our armed forces depend on a strong industrial capacity to provide material support. That is why we must regard our dependence on OPEC oil with such alarm. We could, in any protracted conflict, find our industrial ability to support the operations of our military restricted either by an embargo, or the destruction of supplies in transit.

And it is that situation of growing dependence, regardless of what we do in the short term, that still faces us.

Let's look at where we stand now -- two years after the embargo.

-- Domestic oil production is at a nine-year low, down eight percent this year from 1973.

-- Dependence on foreign oil has actually risen from 35 percent before the embargo to 38 percent now -- despite curtailed consumption due to the recession and conservation efforts.

-- And dependence on OPEC oil -- the oil that led to quadrupled world prices -- has increased from 49 to 60 percent of imports over the same period.

-- And, during that same time, the cost of our dependence on OPEC and other foreign oil has more than tripled -- to 27 billion dollars a year.

So far, perhaps, the most meaningful step that has been taken to assure the security of world energy supplies has been the International Energy Agency, and the arrangements for emergency sharing of energy supplies. But the only way that kind of progress can be consolidated and continued is if the United States assumes the leadership of the free world by establishing its own domestic energy policy.

And this, I think, is where much of the debate on energy policy has faltered. At home we have refused to adopt policies which are consistent with our long-term domestic interests. And our refusal to do so has further jeopardized our long-term strategic goals.

By refusing to allow prices to rise, we have abdicated our responsibilities as a major power with unprecedented responsibilities throughout the world. Those obligations -- which have become ours not by choice but from necessity -- involve the maintenance of stable economic and political relationships for our good and that of our allies.

From 1945 until 1973, we were able to meet those responsibilities because of unequaled industrial might, and unprecedented military power, all of which presupposed secure supplies of energy. But in these new circumstances, with energy supplies -- especially oil -- uncertain, and its availability unpredictable, will we be able to meet our commitments in the future?

That question has yet to be answered definitively. And the answer will not be forthcoming as long as we persist in refusing to deal with the new economics of energy.

The energy crisis -- or problem, if you will -- is not just a question of automobiles and utility bills, though they are indeed urgent matters. There is a direct and unavoidable link between our domestic energy problem and global economic and political stability.

And as Secretary Kissinger has said: "The days when the United States could overwhelm its problems are gone." But nevertheless, that does not absolve us from the responsibility of taking a leading role in establishing a new equilibrium between resource producers and consumers -- a role we cannot play without a national energy policy.

Energy is the most immediate and urgent area where we must begin to seek stability. And by stability, I do not mean a static relationship which benefits only the oil consuming nations, but an arrangement which guarantees the legitimate interests of both sides, as well as the security of the United States and its allies.

Only then -- with the interests of all sides secure -- can we feel confident that interdependence will be a relationship among equals.

Thank you.

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