**ECONOMIC SANCTIONS**
**POLITICAL RATIONALE AND ECONOMIC EFFECT**

Middle East Institute
Petroleum Industry Research Foundation
Washington, 29/IV/1996

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**The Middle East Institute**
**and**
**The Petroleum Industry Research Foundation, Inc.**
**Present**
**"ECONOMIC SANCTIONS: POLITICAL RATIONALE AND ECONOMIC EFFECT"**
**National Press Club**
**Monday, April 29, 1996**

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| 8:00 am | COFFEE AND REGISTRATION |
| 8:30 am<br>WELCOMING REMARKS: | Roscoe Suddarth, The Middle East Institute<br>Lawrence Goldstein, The Petroleum Industry Research Foundation, Inc. |
| 8:45 am<br>KEYNOTE SPEAKER: | Gary Hufbauer, Institute for International Economics |
| 9:30 am<br>PANEL I | SANCTIONS: FOUR CASES<br>Moderator: Gary Sick, Gulf 2000<br><br>Iran: Patrick Clawson, National Defense University<br>Iraq: Ahmed Hashim, CSIS<br>Libya: Suleiman Bengharsa, Consultant<br>Nigeria: David Miller, Corporate Council on Africa |
| 11:15 am | COFFEE BREAK |
| 11:30 am<br>PANEL II | IMPACT OF SANCTIONS<br>Moderator: Cyrus Tahmassebi, Energy Trends<br><br>Market Analysis: John Lichtblau, Petroleum Industry Research Foundation, Inc.<br>Oil Company (US): J. Michael Stinson, Conoco<br>Trade Analysis: J. Daniel O'Flaherty, National Foreign Trade Council<br>Equipment Supplier: Larry Bowles, Halliburton/Brown & Root |
| 1:00 pm | LUNCH BREAK |
| 2:00 pm<br>PANEL III | THE POLITICS OF SANCTIONS<br>Moderator: Richard Murphy, The Middle East Institute<br><br>Congress: Gregg Rickman, Office of Senator Alfonse D'Amato<br>Administration: David Welch, Department of State<br>Europe: Eric Rouleau, French Journalist and Diplomat |
| 4:00 pm | CONFERENCE CONCLUDES |

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## PARTICIPANT BIOGRAPHIES

**Suleiman Bengharsa**

Suleiman Bengharsa is an international oil and gas industry consultant, who advises companies doing business in the Middle East and North Africa. Previously, Bengharsa held advisory positions with ARCO International Oil and Gas Company and Maxus Energy Corporation, where he conducted research and analyses of oil and natural gas sector/markets and policies, and country risk analyses. In 1992, he authored a paper on Egypt's natural gas industry and policy which was published in *The Journal of Energy and Development*. He presented a paper on Libya's oil and gas policy at a symposium sponsored by the Center for Strategic and International Studies in 1993. Bengharsa received an M.A. in international studies from Drew University.

**Larry Bowles**

Larry Bowles has represented Halliburton Co. on international trade, energy, environment, and tax policy issues to the US government. Prior to Halliburton company, he was an employee of Texas Instruments Inc., first as marketing and business manager of enviromental science services, then as strategic marketing and government affairs manager for the wholly owned subsidiary Geophysical Service Inc. He was on the teaching and research staff at Oklahoma State University. Bowles has undergraduate and graduate degrees in environmental science from the University of Tulsa, and Oklahoma State University. He studied international business managment at the University of Texas at Dallas.

**Patrick Clawson**

Dr. Clawson is a senior fellow at the Institute for National Strategic Studies of the National Defense University. In 1995 and 1996, he was the editor of the Institute's *Strategic Assessment,* a survey of US strategic interests and policy concerns. He is also a senior editor of *Middle East Quarterly,* a position he assumed in 1993 after four years as editor of *Orbis.* From 1981 to 1992, he was a senior economist respectively at the Foreign Policy Research Institute, the World Bank, and the International Monetary Fund. He is an adjunct scholar at the Washington Institute for Near East Policy, where he was previously a fellow in Economics. Clawson's most recent books are: *Energy Security in the Twenty-First Century; Iran's Strategic Intentions and Capabilities; How Has Saddam Hussein Survived? Economic Sanctions, 1990-93,* and *Iran's Challenge to the West: How, When, and Why.*

**Lawrence Goldstein**

Lawrence Goldstein is president and a member of the board of the Petroleum Industry Research Foundation Inc., an internationally known non-profit think tank. In addition, he is president of PIRA Energy Group, an energy consulting firm that is currently retained by 200 companies. He has been a member of the Petroleum Advisory Committee of the New York Mercantile Exchange and a steady contributor to studies by the National Petroleum Council (an industry advisory entity to the secretary of energy). He has written and made presentations to private companies, industry/government groups and has testified before Congressional committees and regulatory bodies. Goldstein currently serves as a board member of the US-Azerbaijan Council and board member and treasurer of the Scientists Institute for Public Information.

**Ahmed Hashim**

Dr. Hashim is a senior fellow at the Center of Strategic and International Studies. From October 1993- September 1994, he was research associate at the International Institute for Strategic Studies, London, where he worked on Iranian national security. He was a defense consultant to the US Department of Energy, September 1991-September 1993. In addition to his forthcoming book *Iraq Five Years After Desert Storm,* he is the co-author with Anthony Cordesman of *Iran: Beyond Dual Containment,* which will be published in the near future. Hashim received his Ph.D. from the Massachusetts Institute of Technology.

**Gary Hufbauer**

Dr. Hufbauer is the Reginald Jones Senior Fellow at the Institute for International Economics, and was formerly the Marcus Wallenberg professor of International Financial Diplomacy at Georgetown University. From 1977 to 1980 he served as deputy assistant secretary in the US Treasury, where he was responsible for trade and investment policy during the Tokyo round. Previously he was director of the International Tax Staff at the U.S. Treasury. A Harvard and Cambridge graduate in economics, and a Georgetown graduate in law, he has published books and articles on international trade, finance and tax policy, including *Economics Sanctions Reconsidered* (second edition, 1990).

**John Lichtblau**

John Lichtblau, a leading international expert on petroleum economics, has been head of the Petroleum Industry Research Foundation, Inc. since 1961, when he became executive director. He is now the chairman. He joined PIRINC in 1956 , a not-for-profit research organization that provides analyses of public policy matters affecting the US petroleum industry. From 1954 to 1955 he was an analyst with the petroleum consulting firm, Walter J. Levy Consulting Corp. He has written many articles on petroleum economics and has testified before Congressional hearings on energy policy. He has served on the National Petroleum Council since 1968. He is also chairman of the PIRA Energy Group. Mr. Lichtblau did his undergraduate work at the City College of New York and his graduate study at New York University.

**David Miller, Jr.**

Ambassador Miller is president and chief executive officer of ParEx, Inc. He was special assistant to the President for National Security Affairs at the White House from January 1989 to December 1990. During his diplomatic career he served as the ambassador to Tanzania (1981 to 1984) and to Zimbabwe (1984 to 1986). In 1985, he served briefly as director of the South Africa Working Group. From 1971 to 1980, he worked for the Westinghouse Electric Corporation and lived in Nigeria from 1976-1980. In 1968, after having been selected as a White House Fellow, Miller worked with the Attorney General and became his special assistant. From 1970 to 1971, he was director of the President's Commission on White House Fellows. Miller holds degrees from Harvard, Michigan Law School, and Lewis and Clark College.

**Richard Murphy**

Ambassador Murphy is chairman of the Board of Governors of the Middle East Institute and a senior fellow of the Middle East at the Council on Foreign Relations. A foreign service officer for 34 years, he spent most of his career in the Middle East and was ambassador to Mauritania, the Philippines, Saudi Arabia, and Syria. During 1983-89, he was assistant secretary of state for Near Eastern and South Asian Affairs, from which he retired with the rank of career ambassador, the most senior rank in the foreign service.

**J. Daniel O'Flaherty**

J. Daniel O'Flaherty has been vice president of the National Foreign Trade Council in Washington since 1987. He is also executive director of the US-South Africa Business Council. He has worked with the member companies of the NFTC on a range of trade policy issues, including US trade legislation and trade and investment relations with the former Soviet Union, China, Vietnam, and South Africa. He has been a senior associate of the Carnegie Endowment for International Peace, staff member of the Senate Select Committee on Intelligence, and assistant director of the Group of Thirty, a consultative group on international monetary and economic policy. He is a graduate of Williams College, Oxford University, and Harvard University, where he did graduate work in political science.

**Gregg Rickman**

Gregg Reckman is the legislative director for US senator Alfonse M. D'Amato (R-NY). Before assuming his present position in 1995, he was the legislative assistant for foreign affairs, terrorism, crime, narcotics, and immigration. He joined the D'Amato staff in 1991. Before that, he was a Ph.D. student in international affairs at the University of Florida. He received a M.A. and B.A. in history from John Carroll University.

**Eric Rouleau**

Eric Rouleau has been a journalist, editor, author, and diplomat. He has studied classical Arabic, French literature, Hebrew, and law. In the last two decades of a thirty-year career at *Le Monde,* he served as chief editorialist and head of the Middle East department, earning acclaim for his in-depth coverage of the Arab world, Cyprus, Greece, Iran, Israel, and Turkey. In 1985, he was appointed by French President François Mitterrand as ambassador to Tunisia, the Arab League, and the Palestine Liberation Organization. From 1988 through 1991, Rouleau was ambassador to Turkey. He now devotes his time to writing.

**Gary Sick**

Dr. Sick is a senior research scholar and adjunct professor of international affairs at Columbia University. He is a member of the board of Human Rights Watch, chairman of the advisory committee of Human Rights Watch/Middle East, and the executive director of Gulf/2000, an international research project focusing on political, economic and security developments in the Persian Gulf. Sick, a retired captain in the U.S. Navy, served on the National Security Council staff under presidents Ford, Carter and Reagan, and was the principal White House aide for Iran during the Iranian revolution and the hostage crisis. He served as the deputy director for International Affairs at the Ford Foundation from 1982 to 1987. He is the author of two books on U.S.-Iranian relations, as well as many articles on Middle East issues. Sick holds a Ph.D. in political science from Columbia University.

**J. Michael Stinson**

J. Michael Stinson is vice president of business development for Conoco Inc. He is also vice president for DuPont, Conoco's parent company. He joined Conoco in 1965; in 1982 he was named director and general manager of southern operations for Conoco (U.K.) Limited. He served as president of Conoco Norway Inc. from 1984 to 1988. He subsequently became vice president and general manager for exploration and production in Europe and Africa. In 1991 he returned to the United Kingdom as chairman and managing director of Conoco (U.K.) Limited. In 1993, he became vice president of business development and resources related to the company's exploration activities, based in Houston. He is a fellow of the Institute of Petroleum and a member of the American Petroleum Institute and the Society of Petroleum Engineers. Stinson holds a B.S. degree from Texas Tech University and a M.B.A. from Arizona State University.

**Roscoe Suddarth**

Ambassador Suddarth became the president of the Middle East Institute in July 1995. During his diplomatic career, he served in Mali, Lebanon, Yemen, Libya, Jordan, and Saudi Arabia. He was deputy assistant secretary of state for Near Eastern and South Asian Affairs from 1985-87, and was ambassador to Jordan from 1987-90. From 1991-94, he was deputy inspector general of the Department of State. In July 1994, he was assigned to the Naval War College as international affairs advisor, where he was a member of the teaching faculty. Suddarth has degrees from Yale, Oxford, and MIT, and is a graduate of the Beirut Foreign Service Arabic and Area Studies Program.

**Cyrus Tahmassebi**

Dr. Tahmassebi is the president of a newly established company called Energy Trends, Inc. He was previously the chief economist and director of market research for Ashland Inc. Before joining Ashland in 1981, he was a visiting fellow at Harvard University. Tahmassebi worked for the National Iranian Oil Company and the National Iranian Gas Company in senior management positions prior to the change in the country's government. He received his B.S. and M.S. from Brigham Young University and his Ph.D. from Indiana University in Bloomington. He has written extensively on oil, gas and energy markets. He served as a member of the National Academy of Science's workshop on the Strategic Petroleum Reserve, and the Office of Technology Assessments' workshop on US oil production.

**David Welch**

David Welch is principal deputy assistant secretary in the State Department's Bureau of Near Eastern Affairs. A career foreign service officer, he has had a number of assignments in the Middle East and South Asia, including to Saudi Arabia, Jordan, Syria, and Pakistan. Most recently, he was the deputy chief of mission at the US Embassy in Riyadh from 1992-95; in the absence of an ambassador, he was chargé d'affàires for two years (1992-94). He was member of the National Security Council staff at the White House from 1989-1991. Welch graduated from Georgetown University's School of Foreign Service. He also studied at the London School of Economics, and has an advanced degree from the Fletcher School of Law and Diplomacy .

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# Economic Sanctions: Political Rationale and Economic Effect

**Opening Remarks by**
**Lawrence J. Goldstein**
**President**

**At a Conference Sponsored by**
**The Petroleum Industry Research Foundation and**
**The Middle East Institute**

**April 29, 1996**

**National Press Club**
**Washington, DC**

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You're probably wondering why I've been given such a visible, prominent role in this conference. I too was curious, until I realized that I've also been given only five minutes. I guess it was concluded that how much damage can he do in only 5 minutes - well let's see.

## The Political Gravitational Pull Of Sanctions

I was invited to speak to a very distinguished gathering, and during a break a small group was discussing their academic achievements which included graduating with honors from such prestigious universities as Harvard, Yale, Oxford and Westpoint. Not wanting to be left out of this conversation I unintentionally blurted out that I had graduated university in only 3 terms. As soon as I said it I knew that I was in trouble and sure enough, each skeptically looked at me and in unison said, "Come on Larry, 3 terms?" "Absolutely, I said, "Johnson, Nixon and Ford".

Now, I can sense that some of your minds are working overtime here. Don't read too much into this, although I do admit that it's an interesting coincidence that none of these Presidents served a full elected second term. Strangely, six of our last seven Presidents fall into this category.

Speaking of politics, the issue of sanctions is likely to get caught up in the gravitational pull of the presidential election environment, and it will become increasingly difficult to distinguish between the parties. In what some have referred to as "political crossdressing," it's going to become increasingly difficult to tell the players - by the scorecard. We could get into a dangerous political game of leapfrogging with both the Congress and the Republican candidate trying to outdo the Administration. When examining the issue of sanctions it's important to be clear not only what it is you specifically want to achieve, but also how likely is it that you can achieve it and at what price. The dramatic growth in trade as a share of our economic activity makes sanctions an increasingly costly policy tool and will likely inflict more pain on us than the targeted country. Curiously the mere threat of sanctions may be more valuable than their implementation.

## Sanctions - Less Than Meets The Eye

It is not surprising that when measured in this context that sanctions -- particularly unilateral sanctions -- have simply not been effective. What is surprising is that this still comes as a surprise to anyone. First, sanctions are typically applied by large industrial democracies against non-democracies, where leaders control, if not the hearts, certainly the minds, the airwaves, the information flow and just as important, the purse strings.

In the one place where there is general agreement that sanctions have worked -- Iraq -- I would argue that it wasn't sanctions *per se* but sanctions plus two very unique additional ingredients found virtually nowhere else that have brought about whatever successes we've achieved there.

The first is a little thing I refer to as a war which helped not only to destroy Iraq's military capability but a substantial amount of its economic infrastructure as well, something that sanctions alone would have taken years if not a decade to achieve and secondly, the right to randomly send outside inspectors into Iraq. Without these additions the "success" of even these sanctions would have been severely limited.

## Sanctions And The Current Oil Environment

A cornerstone of U.S. energy policy is diversity of supply. Yet, we now have embargoes on Iraq, Iran and Libya. Who's next? Oil projects in newly emerging areas (Azerbaijan and Kazakhstan to name just two) are very capital intensive and have long gestation periods. They can require billions of dollars in up-front investment and take 5-10 years before substantial oil or gas starts to flow. Yet it is impossible to know over this time frame who your government's friends or enemies will be. Unfortunately, our government is showing an increasing propensity to use embargoes and sanctions as an everyday weapon in our foreign policy arsenal.

Any foreign project has to undergo market and country risk analysis. However, today, a new risk, unique to U.S. companies, must also be priced. A second country risk assessment: your own country. A proper pricing of this risk could render U.S. entities non-competitive in bidding for these foreign projects. Moreover, capital may not be as readily available to U.S. companies if lending institutions price this new risk as well. Accepting our government's assessment of who and what the foreign countries are, the question still remains: would our objectives be better served using private entities as buffers rather than bludgeoning tools of public policy?

Admittedly, if I have any expertise it's in the area of oil markets, so I'd like to say a few words about sanctions and oil before I turn the program to the people you've really come to listen to.

First, the oil markets are undergoing fundamental radical changes. As part of industry downsizing, global inventory management is moving towards a just-in-time inventory mind set. This is being led by the U.S. where commercial stocks are at record lows. The absence of a commercial cushion makes the market very vulnerable to "surprises." Secondly, spare productive capacity today is approximately half the level that existed during the 1980's.

The U.S. currently bans the imports of Iranian and Libyan oil and we've asked our allies to do the same. By coincidence Iranian production of 3.6 million b/d today matches our estimate of world spare capacity. Thus if we were successful in convincing our allies to embargo Iranian oil (forget Libya and possibly Nigeria for a moment) the entire spare capacity would be wiped out overnight even if all other producers with spare capacity agreed to immediately fully increase their output (an optimistic assumption). Under such a scenario you would get an instantaneous sharp increase in crude oil prices, as companies attempt to build up inventories' including a return to a speculative nature to inventory management followed by a small blip in inflation and a reduction in economic activity.

**Thus, under the heading of what I've referred to as "Be Careful What You Wish For..."**

## BE CAREFUL WHAT YOU WISH FOR....

Be careful what you wish for
I'm told the saying goes,
For you just might get your wish
And what you reap you'll sow.

Oil as a political weapon
Is not we're told P.C.
Yet, this type of legislation could result
In a ban on some VLCC's*.

At least that is the oil that
Comes to us from far off lands
Particularly the oil that flows
From Arab & Moslem sands.

A ban on Teheran
Sounds about right,
Yet, this would create an imbalance
and shortfall overnight.

Prices would jump at the retail pump
Creating a political fuss,
Forcing our Fed. Chairman
To do then what he must.

So be careful what you wish for,
For it just might come true.
And then the prospects of a soft landing
Would fall to less than one in two.

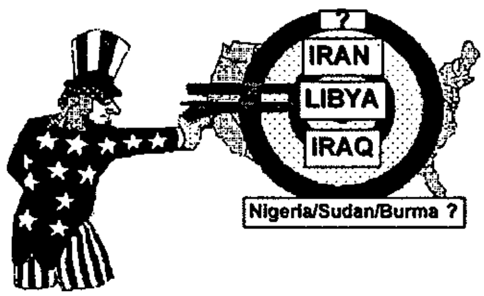
Who's next you ask?
I do not know,
But the answer will come with time.

Lagos, Algiers,
Beijing, Tangiers,
May one day queue the line!

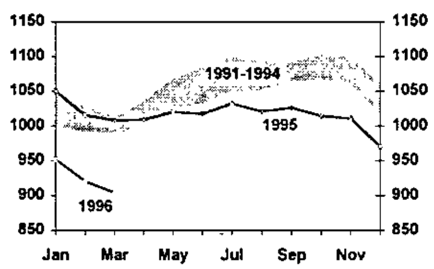
* Very large crude carriers

**LJG**

## Do Sanctions Hit the Mark?




## U.S. Commercial Stocks




## OPEC Spare Capacity
(MMB/D)

| | LATE 1980's | CURRENT |
|---|---|---|
| SPARE | 7.1 | 3.6 |

| | PRODUCTION - CURRENT |
|---|---|
| IRAN | 3.6 |
| LIBYA | 1.3 |
| NIGERIA | 2.0 |

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The Middle East Institute

and

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Conference:

"Economic Sanctions and the Middle East:

Political Rationale and Economic Effect"

National Press Club

April 29, 1996

Remarks by

Gary Clyde Hufbauer

Senior Fellow

Institute for International Economics

Conference on "Economic Sanctions and the Middle East:
Political Rationale and Economic Effects"
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April 29, 1996

# SANCTIONS AND THE MIDDLE EAST

Gary Hufbauer

Institute for International Economics

A flurry of new developments and an ambitious Congressional agenda have pushed the question of Middle East sanctions to the forefront. Iraq's ongoing discussions with the United Nations over oil sales, new information on Libya's chemical weapons program, and pending sanctions legislation aimed at Tehran and are all on the agenda. Harsh sanctions against Mideast rogue states are very popular with most Americans. Internationally, however, moves to extend the scope of US law has added a new, and potentially damaging element, to the policy discussion.

## Issues

The United States has employed sanctions in the Middle East since 1951 when, in conjunction with Great Britain, the United States imposed financial and trade controls against Mussadiq's Iran for nationalizing the country's oil industry. Since that time the United States has wielded the economic stick well over a dozen times: to counter the Arab boycott of Israel, to punish terrorist-supporting regimes, to prevent nuclear proliferation, to rein in Israeli adventurism, and to protect shipping in the

Persian Gulf. The region has also witnessed the most comprehensive sanctions effort to date anywhere: the UN embargo of Iraq.

Beginning with its sanctions against Iraq after the Gulf War and extending to recent and pending measures targeting Iran and Libya, the United States (coincident with the end of the Cold War) has expanded its objectives from changing specific policies – like proliferation and terrorism -- to ambitious attempts to overthrow entrenched governments or change the political character of Middle East states. The international community was originally sympathetic to US efforts aimed at Saddam, but has now begun to resist unilateral US attempts to topple regimes in the region. 1

To bypass the absence of international consensus, some advocates in Congress have turned to a relatively new weapon in the economic arsenal: the secondary sanction. The United States traditionally rejected the use of secondary embargoes as a tool of foreign policy. Indeed, it enacted its own tough anti-boycott measures to thwart the Arab League's attempts to sanction US companies trading with Israel. 2

Times change. Since the United States itself first employed secondary measures in 1982 – in an effort to stop the construction of the Soviet gas pipeline in Western Europe – secondary sanctions have gained popularity among policymakers impatient with reluctant US allies. The most striking examples of the US use of secondary measures is the recent Helms-Burton legislation, targeting Cuba. In this case, like the recent Middle East cases, US allies have protested vocally and introduced laws of their own to thwart US efforts (rather akin to the US anti-boycott measures twenty years ago). In addition to their adverse impact on US alliance relations, secondary measures may ultimately undermine the global trading rules which the United States has worked so hard to construct.

## The Effectiveness of Sanctions

The Institute for International Economics published a study of the efficacy of economic sanctions, based on an analysis of 116 cases that have arisen since 1914 (the study is currently being updated). From this study, my colleagues and I developed nine "commandments," guidelines aimed at maximizing the effectiveness of economic sanctions. Five of these would seem applicable to the current Middle East cases:

- Sanctions with modest goals are more likely to succeed than those with ambitious objectives. Efforts aimed at affecting modest changes in a target country's behavior have shown a greater propensity to succeed than those with grand designs, such as changing governments.
- The more support a goal has internationally, the better. While international support is not a prerequisite for success, it provides important moral support and helps avert a backlash among third countries. Antagonizing the international community tends to be counterproductive.
- The friendlier the target, the greater the chances for success. Friendly countries respond better to economic pressure than adversaries . In many cases, economic coercion by an antagonistic power has served to rally a people around its leaders, no matter how unpopular the leaders may have been previously.

- The faster the implementation, the greater the results. Incremental sanctions give a target country time to both adjust economically, by finding new suppliers and trading partners, and politically, by building public support for resisting foreign interference.
- Think ahead about goals and chances for success. The leaders of sanctioning countries should have a clear idea of their objectives when imposing punitive sanctions as well as the probability for successfully achieving them. Symbolic sanctions will often backfire if the costs they impose, either on the domestic economy or those of its allies, are too harsh.

## Assessment

It is obvious that many of these "commandments" have not been met by the recent initiatives targeting Iran, Iraq, and Libya. There is little chance that sanctions will succeed in meeting the goals implicitly wished or explicitly stated by their authors. Efforts that would extend US law to punish third countries will almost certainly strain US ties with its allies in Europe and Asia. If this line of policy is pushed hard, it will ultimately undermine the global trading system.

Policymakers in Congress and the administration should realize the limitations of economic sanctions. The almost airtight embargo enforced against Iraq has still failed to produce a new government in Baghdad. Proposed sanctions against Iran and Libya, for which there is much less international support, are doomed to meet a similar fate.

US policymakers should try a different approach, and attempt to find common ground with those among its allies. Many of them have greater influence, at this juncture, than the United States has on the regimes in Tripoli, Baghdad, and Tehran. At the very least, new legislation should give the President broad authority to waive secondary sanctions as he tries to build an international consensus for dealing with allies and adversaries in the Middle East.

Raymond Greene
April 15, 1996

## Status of Ongoing Middle East Sanctions Cases

US v. Arab League (anti-boycott): Anti-boycott measures have been relaxed as more Arab League countries begin formal and informal economic contacts with Israel.

US/UN v. Libya (terrorism): Libya continues to refuse to turn over the two suspects in the Pan Am 103 bombing prompting the United Nations to extend economic and travel sanctions against Tripoli. Libya has sought to increase pressure on its neighbors by expelling Palestinians and other foreign workers and attempting to open direct travel routes to Mecca. US Congress is poised to add Libya to its secondary sanctions legislation aimed at Iran. Libya's chemical weapons program has also raised concern within the foreign policy community.

US v. Iran (terrorism): US efforts to isolate Tehran remain strong despite the failure to win wide international acceptance of its strategy. Both the administration and Congress have enacted policies aimed at preventing proliferation and undermining the Iranian regime. As a result of US pressure, Iran has had difficulty attracting much-needed Western investment although it has enjoyed warming ties with both Russia and China, both of which are eager to expand economic and military cooperation with Tehran. China's sale of cruise missiles (and possibly chemical or nuclear weapon technology) to Iran has become a thorny issue in Sino-US relations.

US v. Syria (terrorism): Syria remains on the State Department terrorist list but bilateral relations with Washington have shown signs of warming, particularly if nascent talks between Damascus and Jerusalem succeed in ending hostilities between the two countries. However, the reconciliation process between the two countries remains vulnerable to recent terrorist incidents and Israeli moves into Lebanon. The United States has sought to facilitate a peace settlement through diplomatic initiatives, and perhaps, a direct peacekeeping role in the Golan Heights.

Arab League v. Israel (Palestine): Enforcement of the secondary boycott against companies which trade with Israel has become increasingly lax. Several Gulf states, along with Jordan and Morocco are moving toward full normalization with Jerusalem, sharply dividing the pan-Arab effort to isolate its long-time enemy.

US v. Sudan (human rights; civil war): Relations between Khartoum and Washington continue to deteriorate as Sudan continues to maintain close ties with Iran and Libya. Cairo and Washington have also accused Khartoum of involvement in the attempted assassination of President Hosni Mubarak in Addis Ababa and the abortive effort to blow up the United Nations and other sites in New York. The United States has withdrawn its diplomats from Sudan (citing lax security) and recently expelled two Sudanese diplomats accused of involvement in terrorist activities.

US/UN v. Iraq (proliferation et. al.): Efforts to negotiate the acceptance of a UN plan to allow limited oil sales potentially mark the first major easing of economic sanctions in place against Baghdad since 1990. Jordan's stronger role in enforcing the embargo, which had previously provided a critical loophole in the sanctions regime, likely has had a significant impact on the Iraqi regime.

# The Impact of U.S. Sanctions on Iran[*]

## by Patrick Clawson[**]

In March 1995 testimony before the Senate Committee on Banking, Housing and Urban Affairs (Sen. D'Amato, chair) , I said that comprehensive U.S. sanctions on Iran would reduce Iran's foreign exchange receipts by tens of millions of dollars a year. I was in a minority; many analysts argued that the sanctions would have no effect. Indeed, I was wrong. In fact, the U.S. sanctions have reduced Iran's foreign exchange receipts by at least several hundred millions of dollars. It can plausibly be argued that during their first year, sanctions will cost Iran two billion dollars, or ten percent of its foreign exchange receipts. The sanctions have been much more effective than anyone expected last spring.

**How the Sanctions Have Hurt Iran**

The sanctions have hurt Iran several ways:

- Oil exports. Iran had problems adjusting to the cut-off in sales to U.S.-owned oil firms. In the first three months after sanctions were imposed (May through July), Iran was not able to sell about 400,000 barrels a day. Plus on all its oil sales, Iran had to accept a lower price, said by *Petroleum Intelligence Weekly* and the *Financial Times* to be a discount of 30 to 80 cents per barrel. The events of those three months alone may have cost Iran $100 million to $200 million dollars. Nor did the problems end after July. The Islamic Republic News Agency admitted in August that Iran was still not able to market 200,000 barrels a day that had pre-sanctions been sold to U.S. firms. While Iran eventually found markets for all its oil, there is some evidence that Tehran continues to offer its oil at a small discount.

- Oil field renovation and expansion. Businessmen selling to Iran tell me that the National Iranian Oil Company (NIOC) is having to pay tens of millions of dollars a year more to get parts for its U.S.-built equipment. NIOC, which does not have enough capital to maintain (much less expand) its output, is having to offer particularly attractive terms to induce foreign firms to invest in its fields -- terms that bring Iran tens of millions of dollars a year less than what it could have expected in the absence of the U.S. sanctions. And the most important impact over time is that Iran has not been able to attract foreign investment into its oil industry -- investment Iran had counted on to increase its oil earnings. The November 1995 Tehran conference for

[*] The views expressed here are those of the author and do not reflect the official policy or position of the National Defense University, the Department of Defense, or the U.S. Government.

[**] Dr. Clawson is a senior fellow at the Institute for National Strategic Studies of the National Defense University. From 1981 through 1992, he was a research economist for four years each at the International Monetary Fund, the World Bank, and the Foreign Policy Research Institute. He is the author of, among other writings, *Iran's Strategic Intentions and Capabilities* (NDU Press, 1994) and *Iran's Challenge to the West: How, When, and Why* (The Washington Institute for Near East Policy, 1993). He is currently senior editor of *Middle East Quarterly*.

potential petrochemical investors was a bust, with not a single deal materializing. Even Lukoil, a Russian firm, backed out in reaction to the U.S. pressure. Total's development of the offshore Sirri field, taken over from Conoco, has run into serious problems, which may get worse if Dubai decides not to allow the import of gas from the project (the project will almost certainly proceed, simply because Total and the French government would not tolerate the public relations disaster of backing out, but without the gas to Dubai, it will probably be unprofitable).

- General imports. The sanctions appear to have caused Iran some problems doing business in U.S. dollars, that is, non-U.S. firms worry that sanctions may affect their ability to be paid in dollars. Businessmen and bankers dealing with Iran report to me that some Iranian firms have been going through middlemen, who charge a fee for their service. The extra cost may be as much as a hundred million dollars a year.

- Business confidence. I said in May to the House Committee on International Relations, "It is possible that comprehensive U.S. sanctions will trigger a run on the Iranian currency." Indeed the imposition of sanctions caused the Iranian currency to collapse, loosing a third its value in a week. Tehran responded by slapping on rigid controls. The controls caused the market to dry up. At the current artificial level, with only 3,000 rials to the dollar instead of 6,000, it is unattractive to export, and so non-oil exports have fallen by one billion dollars a year, or one-fourth, from their pre-sanctions trend. That only makes the foreign exchange shortage worse, and compels Tehran to impose more and more controls in a spiral downwards into a distorted and inefficient economy. To be conservative, I am not including the loss of export earnings in my calculations of the costs of sanctions. The export earnings loss can be attributed to inappropriate government policy as much as to the sanctions.

- Access to foreign capital. Foreign lenders, such as commercial bankers and government export credit agencies, are more cautious about lending to Iran because of the sanctions. Iran has only been able to arrange one large loan package (for $675 million from BHF, a German bank), and even that is conditional on uncertain access to coverage by the German official export credit agency. Some previously agreed loan deals, such as a ? large Italian official export credit agency credit line, are less than sure. It seems highly unlikely that Iran will raise anything like the two billion dollars in capital inflows it was counting on for this year. Meanwhile, Tehran has decided that it cannot be sure of continued access to foreign capital markets, so it has put top priority on repaying its foreign debt as quickly as it can. The Central Bank of Iran makes the implausible claim that it paid $9.4 billion dollars in interest and principal in 1995/96; the amount is probably more like five billion dollars. But even with that lower debt payment figure, the fact is that Iran has gone from being a net borrower of about $5 billion dollars a year during 1989/90-1992/93 to being a net repayer of about $5 billion dollars in the year 1995-6.[1] As foreign exchange is used to repay debt, less is available for importing

[1] Data on Iranian borrowing are at best approximate. The data reported by Iran to the IMF's *International Financial Statistics* are understatements, as can be seen by the fact that the sum total of borrowing over the years is less than the debt stock admitted by Iran's Central Bank. On debt service in 1995-6 and subsequent years, Vahe Petrossian of *Middle East Economic Digest* has

industrial equipment and materials, forcing factories to cut output.
The ten billion dollar turnaround in its foreign borrowing has forced Iran to cut its imports in half, from $24 billion in 1992/93 to $12 billion in 1995/96. Much of this change is due to the inappropriate Iranian policy which wasted so much of the borrowed money that the country would not have been able to make regular debt payments even in the absence of U.S. pressure. Still, the U.S. sanctions have pushed Iran's net borrowing by between one billion and two billion dollars below what Iran had counted on pre-sanctions.

**The Political Impact of the Sanctions**

Three goals can be posited for the sanctions: overthrow of the Islamic Republic, a change in its behavior, or weakening its ability to accomplish its aims.

There is no prospect that the first aim, the overthrow of the Islamic Republic, will occur because of sanctions. The fate of the Islamic Republic will be decided largely by internal factors. The U.S. does not have a major influence on Iranian domestic policy. Just as the U.S. cannot expect to shore up moderates, neither can Washington expect to directly bring about the Islamic Republic's downfall.

While the U.S. cannot cause the overthrow of the Islamic Republic, it can expect the clerical regime to fall apart. The Islamic Republic is in poor political, social, and economic shape. The current rulers in Tehran have made a mess of the economy, with per capita income about half of the pre-revolutionary level. Corruption is rampant, with a scandal last summer involving the diversion of $400 million. And the Islamic Republic has exacerbated social tensions, with the six million Afghans and Sunnis bitterly resenting Persian Shia chauvinism. It has alienated many of the devout and the senior clergy, who resent political interference in religious affairs. Tehran's rulers feel so nervous that five times in the last two years, they mobilized 200,000 troops to practice protecting public buildings against rioting mobs.

The reservoir of support for the current rulers, fed by the waters of hatred for the Shah, have run dry. It is quite possible that the Islamic Revolution will not last into a second generation. European experts on Iran are pessimistic about its prospects. The respected Paris newspaper *Le Monde* asked (December 24, 1994) if the Tehran regime was entering its last months. The Islamic Republic survives simply because there is no credible alternative. Like the Shah's regime, it could collapse quickly if any such alternative emerged. Unfortunately, it could also survive another decade or more if there is no good alternative.

The second goal, changing Iran's behavior, is the officially announced U.S. goal for the sanctions. Secretary of State Warren Christopher argues that Iran must be made to choose between its economic hopes and its unacceptable political behavior. This target is ambitious for two reasons. First, Iran harbors hopes that Europe and Japan will step in to replace any losses due to the U.S. sanctions. So far those hopes have only been partially realized -- the allies have traded with Iran while making few loans and essentially no investment. But the prospect of

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shown that the Central Bank has manipulated the data (MEED, *Iran Quarterly Report*, December 1995, pp. 31-35).

European and Japanese business ties has reduced Tehran's incentive to change its behavior. Second, the leaders of the Islamic Republic place great store on their radical foreign policy. It is one of the few remnants of the revolutionary ideology which has now been abandoned in some many aspects of domestic life. And the radical foreign policy does much to puff up Iranian nationalist pride, making more plausible Iran's claim to be a major force on the world scene (a player in Arab-Israeli matters and, to its mind, a leader of the world Muslim community).

The third goal, weakening Tehran's ability to accomplish its aims, has certainly been accomplished. The Iranian budget is already under tight constraints. Given the difficulties of making adjustments elsewhere, spending on the military may well go down because of the effects of sanctions. Indeed, one of the unsung accomplishments of U.S. policy towards Iran is its success in forcing Iran to curtail its ambitious 1989 plan for acquiring a large-scale modern military. Iran planned to buy $10 billion in arms in 1989-94, primarily from the Soviet Union. Iran's hard currency military expenditures, as Tehran reported them to the IMF, were $3.278 billion in the two year period 1990/91-91/92. Those hard currency military expenditures had to be cut in half (to $1.658 billion in the two year period 1992/93-93/94) when Iran was locked out of world capital markets, thanks both to its own inappropriate economic practices and to the U.S. pressure not to make politically-motivated loans to Iran.

### Allied Support on the Sanctions

Many in Europe and Japan argue that the West should woo Iran because it is the strategic prize in the Persian Gulf region. This view is outdated. Iran is no longer a country with a key economic and geostrategic position:

- Iran is not an oil superpower. Its oil fields are old, and its reserves are expensive to develop. Iran produces today less oil than it did in 1970, while production has soared in other parts of the world.

- Iran is not a lucrative market. Iran's imports in 1994/95 were $12 billion, which was less than it imported in 1977. The simple fact is that Iran's economic importance has faded along with its oil wealth.

- Iran does not have much influence with most of the world's Muslims. The differences between Shiites and Sunnis is an obvious limitation on Iran's ability to excite most Muslims. At least as important, the Islamic Republic of Iran is a failure; its experience does not inspire many others.

Many in Europe and Japan maintain that the West should support Iranian moderates in order to undercut the influence of Iranian radicals. This argument exaggerates the influence the West can have on domestic political developments in Iran. The argument also misreads the history of the last 15 years. The U.S. tried several times to support Iranian moderates. The Iran-contra affair began as an effort to reinforce the moderates. The bitter lesson from that experience was that Iranian moderates bite the hand of friendship, specifically, they took the arms shipped from the U.S. and then took more Americans hostages in Lebanon, including a colonel whom they killed. The principal reason that unilateral U.S. sanctions against Iran appear attractive is the singular failure of efforts to promote moderation.

The allies have every right, of course, to disagree with the U.S. on policy towards Iran. However, it is worth remembering that the allies benefit as much as the U.S. from a stable and secure supply of oil from the Persian Gulf. It is the U.S. which bears the brunt of the burden of guaranteeing Persian Gulf security. Germany and Japan made only token military contribution towards Desert Storm, and it is not their ships, planes, and troops, that would be looked to keep the Straits of Hormuz open. Because Bonn and Tokyo are getting a free ride at U.S. expense, it would seem fitting that they should let Washington take the lead on deciding what are the threats to security in the Gulf and how to respond to them. The Europeans insisted on a principle about the Bosnia affair that could well be applied to their own behavior with regard to Iran, namely, the principle that only those with troops at stake should decide what policies will be adopted.

While the allies are unlikely to join with the U.S. in adopting comprehensive economic sanctions on Iran, the U.S. has been successful in persuading them to adopt strict export controls on sales of arms and of militarily useful technologies, including a complete ban on nuclear-related technologies. Allied cooperation on these export controls has been, in general, better than the cooperation on exports of sensitive technology to the Soviet Union during the Cold War. Furthermore, allied governments have been rather cautious about making new loans to Iran, mindful that each such loan or loan guarantee would bring vigorous U.S. complaints. In other words, the allies have limited economic transactions with Iran in a manner which, it could well be argued, would not have been as vigorous had the U.S. sanctions not shown the seriousness with which Washington viewed the Iranian threat. The sanctions have therefore been successful at changing allied behavior.

European governments may adopt a tougher policy towards Iran in the near future. The key is the German government, which has been under pressure from several sources to abandon its policy of critical dialogue. Since late 1995, Norway, outraged about the attempted assassination of the translator of Rushdie's *Satanic Verses* has pushed for a tougher European policy. As public pressure mounted about Iranian official involvement in the 1992 murder of four Kurds in the Mykonos Restaurant in Berlin, the German federal prosecutor last month issued an arrest warrant for Iran's Information Minister Ali Fallahian. And the opposition Social Democratic Party broke with the government over Iran policy. Freimut Duye of the parliamentary foreign affairs committee said critical dialogue "has no future under the circumstances" (*Los Angeles Times*, March 27, 1996). After Iran refused to condemn terrorist bombings in Israel, the European Parliament approved a resolution condemning Iran and stating that critical dialogue had brought not useful results. European Union Foreign Ministers stated, "if critical dialogue is worth continuing, it must show some progress and convergences on such fundamental issues as the [Arab-Israeli] peace process and terrorism" (*Iran Times*, March 15, 1996).

Under these circumstances, the prospects are that the additional pressure on Iran's trading partners contained in the D'Amato-Gilman bill before Congress would have substantial effect. While European and Asian governments will undoubtably complain about what they see as a secondary boycott, few firms are likely to want to risk the legal consequences in the vast U.S. market in order to invest in Iran, given that its GNP is less than 1.5 percent that of the U.S.

In short, the U.S. sanctions on Iran have worked better than expected, and the prospects are good that they will be even more effective in the future.

4

"They Created A Wasteland And Called It Peace":

Sanctions and Iraq

Ahmed S. Hashim

for

"Economic Sanctions and The Middle East:
Rationale and Economic Impact"

Middle East Institute
Petroleum Industry Research Foundation

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**Introduction**

Iraq faces a growing economic crisis that is impoverishing the country and which threatens the social fabric of the country. This crisis is partly the result of:

- decades of mismanagement by the Iraqi government. The Ba`ath government has long indulged in extensive socialist central planning and has exercised heavy control over agriculture, foreign trade, and industrial production -- leaving only small industries, shops, and part of the service industry to the private sector.
- massive spending and foreign borrowing during the costly, and for Iraq, capital-intensive, war with Iran. The eight-year with Iran led the government to rapidly spend the $35 billion dollars in reserves it had built up during the oil boom of the 1970s, and make Iraq a massive borrower.
- gross over-extension of Iraqi credit between 1988 and 1990 in a simultaneous effort to fund wartime recovery, economic expansion, vast public works projects, major arms acquisitions, and a vast defense industrial complex whose dimensions became known only after Iraq's defeat in the Gulf War. In short, the Ba`ath government had effectively crippled Iraq's economy before the Gulf War and had forced devastating cuts in living standards. In fact, Iraq's average per capita income dropped from a peak of $8,161 in 1979 to $2,408 in 1989 -- a cut of 70%.[1]
- "authoritarian economics:" This is a different concept and practice from centralized planning in economics. While socialist centralized planning stemmed from the ideological standpoint that the best way to develop and modernize one's country is by means of the state sector, authoritarian economics is the use of the state's control of financial resources to reward its supporters and punish its enemies. Authoritarian economics is control pure and simple, and is an economic-based processs for the regime to establish and maintain legitimacy. After all, no state can build a formula for legitimacy based entirely on its control of the instruments of coercion. Long before the current crisis, Saddam used the state to subsidize and reward his supporters. His internal security strategy has always mixed *targhib* with *tarhib*, the stick with the carrot. Shortly after the 1968 coup which brought the Ba`ath to power, Saddam established a separate and independent (i.e. independent of official state control) channel for allocating state funds. He set up large

accounts inside and outside Iraq, and used these funds to pay or bribe cronies, potential allies, and large groups of the Iraqi population including ethno-sectarian minorities. For example, Saddam at one point ordered the distribution of thousands of TV sets to the poor following anti-government riots in the poor Shi'i suburb of Medinat al-Thawra. In the 1970s and 1980s, the regime went on a major land-buying spree by forcing owners to sell it lands at huge discounts. These lands were then parceled out to supporters of the regime, party officials, the military, and family members. At the same time, the state allocated housing, provided automobiles, university positions, foreign scholarships in order to build loyalty among the populace and the military.

**Sanctions and the Iraqi Economy After the Gulf War**

The distortions in the Iraqi economy described above are not by themselves sufficient to explain the country's current malaise and descent into extreme poverty. Even with these problems Iraq had achieved a high level of economic and social development in the late 1980s which had put it in the World Bank category of upper middle income countries like Venezuela, Greece, and Czechoslovakia. Further, the caloric intake of Iraqis in the late 1980s was just under 3,000 calories per day -- above average for an upper middle income country.[2]

**Iraq's current crisis is also the result of damage done during the Gulf War and of more than a half decade of UN sanctions. The title of my presentation refers to the international community's creation -- not without a little help from Saddam's regime -- of an economic, social, and cultural wasteland in what was once one of the most promising Arab countries. What is the nature of these sanctions and what are their objectives?**

These UN sanctions forbid member states, companies and individuals from undertaking any economic intercourse with the Iraqi government or with Iraqi firms, except in regard to goods deemed by the UN Sanctions Committee to be of a humanitarian nature. In particular, UNSCR 661 passed on August 6, 1990 imposed an economic and trade embargo on Iraq with the exception of the provision of medical supplies and in "humanitarian circumstances, foodstuffs." The resolution also called for the creation of a Special Sanctions Committee to monitor the embargo. UNSCR 665 passed on August 25, 1990 called upon specific measures to enforce the embargo against Iraq.

The UN embargo failed to get Saddam out of Kuwait; while the war itself failed to dislodge his hold on power in Iraq. At war's end the coalition decided to maintain the sanctions in order to get the Iraqi ruler out of Iraq. The economic embargo was to be supplemented by other instruments. Mindful of its failure to remove Saddam and well aware of the adverse impact this might have on George Bush's chances in the November 1992 presidential elections, the Republican Administration opted to maintain "excruciating pressure" on Saddam's regime by the constant threat of military action, continuation of diplomatic and political pressure to keep Iraq isolated internationally, and of course making it clear to the Iraqi people and military that sanctions will not be lifted until Saddam is overthrown. Bush had painted himself into a corner with his insistence that Saddam must go before sanctions are lifted, and it mattered to him not one whit if Saddam were replaced by a Saddam look-alike, down to the burly mustache.

Iraq hoped that the Clinton Administration would "depersonalize" the conflict and move toward better relations. Not only did the new administration fail to do that: it showed a virulent ideological hostility toward Baghdad that was actually unmatched by the previous administration. This was relfected in its policy of "dual containment," which was directed against both the Islamic Republic of Iran and Saddam's Iraq. Declaring Saddam's regime "irredeemable" and a threat to the US and its allies and friends in the Middle East, dual containment, in the case of Iraq, meant the continuation of the sanctions until the regime of Saddam fell from power. The policy also called upon Baghdad to comply with all UN Security Council resolutions, including those pertaining to missing Kuwaitis, return of Kuwaiti property, renunciation of terrorism, ending repression of its population and human rights abuses, and cooperation with international relief organizations. Last but not least, Iraq must convince the world of its "peaceful intentions." It rapidly became clear that these stringent requirements could not be fulfilled -- or more accurately, the United States would not allow Iraq to fulfill them -- without the regime falling from power. For example, the United States could define "peaceful intentions" any way it liked, making it impossible for Iraq to fulfill that condition.

Sanctions were also used to try to delegitimize the regime under the guise of expressing humanitarian concern for the Iraqi people. Several years Iraq considerably annoyed the West by not accepting UNSCR 706 (August 1991), which would have allowed it to sell $1.6 billion worth of oil over a six month period. The revenue from this limited oil sale would then be put in an escrow account controlled by the UN. Part of the revenue would then pay for Un activities in Iraq, in particular the elimination of Iraq's weapons of mass destruction (WMD) projects, while the bulk would be used to purchase food and medicines to be distributed under UN auspices. Iraq dismissede the resolution as an arrogation of its national sovereignty. In April 1995, Iraq also rejected out of hand the successor to UNSCR 706, UNSCR 986 for the same reason and because it objected to the stipulations that Iraq must export its oil through Turkey and that the UN was to be responsible for the distribution of aid in the three northern Kurdish governorates. By the end of 1995, Iraq began changing its tune because of the worsening socioeconomic conditions and because of hardening Western attitudes. The government stated that it would consider accepting 986 if its reservations were taken into consideration.

Sanctions are also being used to ensure Iraqi compliance with UNSCR 687 (April 1991) which demanded that Iraq eliminate its weapons of mass destruction, research into weapons of mass destruction, and any infrastructure associated with those programs. The resolution also stipulated in accordance with Section F, paragraph 22 the UN prohibitions against the export of commodities and products originating in Iraq would have no further force or effect. Iraq's record of lying about the size of its WMD programs and attempts to hide aspects of it have made it more difficult to justify the lifting of the sanctions.

**Impact of the War and Sanctions On Iraq**

Like the notorious gangster Willie Sutton, who when asked why he robbed banks, replied: "because that's where the money's at," Saddam sought to rob the world's biggest bank, namely Kuwait, in order to finance his way out of decades of mismanagement, fix the damage caused by the Iran-Iraq War, build-up Iraq's military, and continue rewarding his supporters both inside and outside of Iraq.

The issue of quantifying the damage that Iraq has suffered in the last 6 years is virtually impossible for a wide variety of reasons.

**First,** statistics are hard to come by because of the obsessive secrecy of a regime that views statistical and economic data on Iraq as state secrets. This problem has been compounded by the extreme state of uncertainty and abnormality within Iraq for the past six years. Even the best figures of the Economist Intelligence Unit, the OECD, the UN, or the Bank for International Settlements are "guestimates." In fact, as early as 1992, most analyses had given up attempts to put numbers on industrial and agricultural output, inflation, and wages.

**Second,** there is no easy way to quantify the relative impact the Gulf War itself has had on Iraq's economy since late 1990, as distinguished from the impact of the UN sanctions. There is no question that the war and the rebellions caused extensive damage. While there has been no official Western estimates of the impact of the wartime bombing, many independent estimates or immediate post-war assessments proved wildly off the mark.

**Third,** the Iraqi government has fluctuated between exaggerating wartime damage and the impact of sanctions and incredible claims about the speed and nature of recovery.

While accurate data are not readily available, what data there is can give some sense of the impact of the sanctions on Iraq's economy and its population. Iraq's per capita income has dropped from $2,408 in 1989 to around $600 a year in 1992-1995, a cut of another 75%.[3] To put it another way, Iraq's per capita income has shrunk from 60% of the OECD average in 1980 to to15% of the OECD average in 1989, and less than 4% of the OECD average in 1993. Oil exports are well under 5% of their pre-Gulf War levels , there are severe shortages of spare parts for industry and consumer prices have doubled annually since 1993.

The decline in Iraq's per capita income and caloric intake has meant that this country has plunged from the ranks of the very advanced states of the Third World through the levels common to poor states like Egypt, Yemen and Sudan, to the levels of the "Fourth World" states like Rwanda, Haiti, Zaire. Iraq now has an economy characterized by extreme poverty and a huge gap between a small parasitic class of nouveaux riches who have benefited from the sanctions and the rest of the population at large. Iraq's once solid and cohesive middle class has disintegrated and the society is marked by widespread corruption and endemic violence.

1. IMF International Financial Statistics, and International Energy Agency, *Middle East Oil and Gas*, Paris: IEA/OECD, 1995, p.247.

2. "Gulf Economies III: Iraq," *Gulf States Newsletter,* vol.19, no.498, October 31, 1994, p.8.

3. IMF International Financial Statistics, and International Energy Agency, *Middle East Oil and Gas,* Paris: IEA/OECD, 1995, p.247.

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# SANCTIONS IN THE MIDDLE EAST: THE LIBYA CASE

BY

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## SANCTIONS BACKGROUND

Libya has been the target of two sets of economic sanctions over the last 12 years. One set of sanctions was imposed unilaterally by United States to persuade the Geddafi regime to: a) stop its subversive behavior against various developing nations friendly to the West, especially the US; b) end its support of international terrorist organizations and acts of terrorism around the world by Libyan agents of the Geddafi regime; and perhaps c) do away with the production of chemical weapons.

The US sanctions, first imposed in March 1981 and renewed every six months since 1987, have included: a) a ban on the importation of Libyan crude oil into the US; b) the freezing of almost $1 billion of Libyan assets; c) a ban on all hydrocarbon imports from Libya; d) a ban on US oil companies operating in Libya; e) a ban on all US trade with Libya; f) a prohibition of travel and residence in Libya by US citizens; and g) the blacklisting of some 100 companies controlled by the Libyan government. Furthermore, in December 1995, the US engaged in some legislation to deny export licences, loans and credit guarantees to European and other oil companies investing in Libya.

The other set of sanctions were imposed by the United Nations Security Council in March, 1992, to persuade the Libyan regime to hand over, to either the US or the UK, two Libyan intelligence officers for their alleged involvement in the bombing of a PanAm plane over Lockerbie, Scotland, in 1988, which killed 270 people. The UN sanctions, which have been renewed every three or four months since they were imposed, have included: a) a total ban on civil aviation activity to and from Libya (including the lease of aircraft, the supply of spare parts and the provision of maintenance services); b) a ban on the export of military hardware and spare parts; c) a reduction of Libyan diplomatic representation abroad; d) a freeze on Libyan financial assets held abroad (excluding those derived from the sale of oil, gas, petroleum and agricultural products; and e) a ban on the export of downstream (transportation and refining) oil equipment to Libya.

## US SANCTIONS EFFECTS

The unilateral sanctions regime imposed by the US on Libya has had no major negative economic effects on that country. The reason is an obvious one: a unilateral sanctions regime cannot work if what has been sanctioned by one country can be purchased from another or a variety of other countries. This is precisely why unilateral sanctioning efforts almost never work, speaking strictly in terms of coercing a target country to comply with the sanctioning country's objectives/requirements, unless perhaps the sanctioning country is the only supplier of the sanctioned goods and services. This is not to say that unilateral sanctions regimes should not be pursued or that any compliance will result from negative effects on a target country. However, this is not the subject of this discussion.

Nevertheless, in terms of effects on Libya, an argument can be made that the US sanctions and general antagonistic posture toward Libya may have, indirectly, had beneficial long-term economic and political effects on that country. Since 1980, it has been the policy of the US to isolate Libya, which most of us are familiar with. Given the strong US influence on the international community and especially its allies, the Libyan government has engaged in a self defense effort to counter the US threat through its relatively vast and attractive hydrocarbon wealth. The Geddafi regime embarked on a successful campaign to gain the support of foreign governments (mainly European) by luring their national oil companies into large investments in Libya. I believe that the signing of new oil and gas exploration and production agreements, and oil development and re-development projects with foreign oil companies in the late 80s and early 90s is to some extent the result of the US antagonistic posture toward Libya.

Furthermore, also in the late 80s and early 90s, the Libyan government's Oil Investments International Company (Oilinvest) bought a majority interest in several refineries in Europe, and now controls 300,000 b/d of capacity and about 3,300 service stations. This was done to manipulate the European market for Libyan crude, which inevitably leads to some control of European policy towards Libya. It is not unlikely that the loss of the US market for Libyan crude provided the Geddafi regime with the incentive to buy some control over its only market -- Europe.

However, in terms of negative economic effects, only the US law that would deny export licences, loans and credit guarantees to European and other oil companies investing in Libya may have some potential. If this type of sanction can negatively affect non-US oil companies doing business in Libya, it may become an obstacle to expanding oil production capacity, and therefore truly affecting the country's oil based economy. But, it's to early to tell.

## UN SANCTIONS EFFECTS

The UN sanctions, although more threatening than the US sanctions to the Geddafi regime because of their multilateral nature, have not had a real serious effect on Libya. The claims that Libya has been suffering a great deal from the UN sanctions is an act to prevent further sanctions on the country, such as a ban on the purchase of Libyan crude oil. In other words, the Libyan regime's posture today is: if they think we are suffering they will not impose an oil embargo. In fact, prior to the UN sanctions, official information coming out of Libya was only about successes. Nothing negative about the economy was ever mentioned. Since the UN sanctions, information about economic problems is revealed on an official basis, especially if it can be pegged to the sanctions.

For Example, in August, 1992, Libyan leader Mu'ammar Geddafi himself, in a televised speech, announced that due to the UN sanctions the country was facing a liquidity crisis. During this period the Libyan government reported that it lost over $4.5 billion in the first three months after the UN imposed limited sanctions on the country. More recently, a Libyan delegate to the World Bank said that the sanctions had cost the country over $10 billion. Prior to the sanctions, the release of this type of information would have been considered highly unusual. But, since these economic problems can now be blamed on someone else, it is not only acceptable to officially announce them, but probably very much encouraged. We must understand that the Geddafi regime has become relatively sophisticated in the area of disinformation; not only as a result of experience, but also as a result of training from former Eastern Block security/intelligence advisors in Libya.

When considering economic problems in Libya one should understand that they are generally due to three main factors: corruption, mismanagement, and/or low oil prices. And, if the three are at work together, the country can become an economic basketcase. However, the truth of the matter is that in the absence of a total oil embargo or perhaps a huge drop in oil prices, Libya should not be experiencing the economic problems that exist today, when we consider that it has a very small population of around four million, and that the lowest GDP it experienced in the last 15 years was around $19 billion in 1988. (In 1994 the GDP stood at $32.9 billion, and the per capita GDP was about $7,300.) Also, Libya has been experiencing large trade surpluses, for a country its size, for many years (see table 1), and over the last 15 years the GDP has grown at an average of around 2% per year. Therefore, as mentioned above, Libya should not be affected by the limited UN sanctions. After all, they do not include a ban on the country's main source of income -- oil exports (currently around 95% of total export earnings).

One of the claims is that the imposition of UN sanctions caused prices for imported consumer goods to rise sharply, and in January 1995 the rate of inflation was reported to have reached 40%. This situation existed in Libya long before the UN sanctions were imposed on the country. First of all, no consumer goods are sanctioned by the UN. Secondly, these goods have mostly been imported into Libya through the maritime route, which unlike the civil aviation route has not been sanctioned. The truth of the matter, is that the importation of consumer goods is in the hands of government officials who for many years have mismanaged and/or abused the system much to their personal benefit. In general, the chaos due to the lack of accountability inherent in the Libyan system has given way to a great deal of mismanagement and corruption.

Another claim is that since the imposition of UN sanctions, the black market rate of the Libyan dinar (LD) against the dollar has plummeted. Once again, this has nothing to do with any sanctions. The black market rate of the dollar has been steadily increasing since 1988, when the government allowed the Libyan people to travel abroad with no restrictions, resulting in an increased demand for US dollars that went beyond the official supply. Hence, a huge growth of the dollar black market. The reason why the black market rate of the dollar has steadily increased since 1988 is strongly related to the fact that the Libyan dinar has steadily purchased less and less. Also, the demand of the dollar has increased due to the increase of private citizens purchasing all sorts of consumer goods abroad to return to sell them in the Libyan black market. It is considered common knowledge in Libya that the government is the major supplier of black market dollars, since it has the ability to buy them at the official price of about $3.30 for 1LD and sell at the black market rate of about $1.00 per 5LDs.

Since the UN sanctions include a ban on the supply of downstream oil equipment, I believe it is important to address the effect of the sanctions on the backbone of the Libyan economy -- the oil sector. Once again, the sanctions are not responsible for any negative impact. Firstly, according to some Libyan oil industry sources the Libyan government had stocked up on industry hardware and spare parts soon after the UN sanctions were imposed, at which time oil industry equipment was not banned. Secondly, also according to a reliable Libyan oil sector contact, Libya has purchased certain spare parts on the black market at no more than 60% above the normal price. Therefore, in the short-run (three to five years) perhaps, Libya should not experience any serious negative impacts on its oil sector. However, if the sanctions last beyond a five year period, the country may start experiencing crude oil refining and transportation problems, that can negatively affect the country's income.

Overall, the UN sanctions have helped to further ostracize and isolate the Geddafi regime. However, it cannot be said that the sanctions have had an impact on Libya's economy, particularly one that would make the regime comply with the objective of the UN sanctions.

## SANCTIONS AND THE FUTURE

In terms of the future, however, it is likely that both the UN and US sanctions will have a somewhat negative impact on Libya, particularly those sanctions aimed at having some effect on the country's oil sector. Here, I am mainly referring to the US legislation aimed at discouraging non-US oil companies (especially European) from investing in Libya (by denying US export licences, credit guarantees and loans to those companies), and the UN banning of certain oil refining and transportation equipment. As mentioned above, these particular sanctions have the potential for doing some damage to the Libyan oil sector in the long term, and therefore to the country's economy. This is primarily due to the fact that the country's oil industry is highly dependent on imported technology. However, they should not have an effect sooner than a five year period because, supposedly, Libya managed to stock up on a great deal of oil equipment before it was banned by the UN. Furthermore, they should not be expected to work at all if the

Libyan government manages to continue making purchases in the international black market. Therefore, the key to success here, speaking strictly in terms of economic effects, is serious implementation and monitoring.

Nevertheless, I believe that regardless of any sanctions effects, including those of an oil embargo, the Geddafi regime will never comply with the UN demands nor will it respond positively to any US expectations of civilized international behavior. It is not in the nature of this regime to bow to foreign demands and pressures. In fact, the Geddafi regime draws some of its legitimacy from defiance of the West, and belligerence towards it. In addition, and perhaps most importantly, any handing over to the West of the Libyan intelligence officers implicated in the bombing of the PanAm plane may give way to further evidence of the Geddafi regime's involvement in the Lockerbie affair, and perhaps other international terrorist activity. I believe that consequently the UN will probably continue adding to the sanctions, as it has done in the past, until it will find itself having to implement total sanctions on the country, including an oil embargo, much like the US approach. In turn, the regime will very likely collapse within months, given that its survival depends on the country's main source of income -- oil.

At this point, we can easily conclude that the sanctions on Libya have not and will not be successful, solely from the standpoint of effects that produce a desired change in behavior from the target government. However, all forms of sanctions that are designed and implemented to counter uncivilized behavior by any country, regardless of their effects, should be considered successful, simply because they send a message of intolerance of such behavior to the target country and to the rest of the world.

## Table 1

**Libyan Foreign Trade ($ million)**

| | 1988 | 1989 | 1990 | 1991 | 1992 | 1993 |
|---|---|---|---|---|---|---|
| Merchandise exports fob | 6,673 | 8,617 | 10,773 | 10,662 | 9,695 | 8,016 |
| of which: | | | | | | |
| crude oil | 6,397 | 7,500 | 9,800 | 10,025 | 9,200 | 7,607 |
| Merchandise imports cif | -5,869 | -4,923 | -5,336 | -6,546 | -6,711 | -7,208 |
| Trade balance | 804 | 3,694 | 5,437 | 4,116 | 2,984 | 808 |

Source: Economist Intelligence Unit.

**Table 2**

**1993 Main Trading Partners (% of total)**

| | Exports to: | Imports from: |
|---|---|---|
| Italy | 37.7 | 23.2 |
| Germany | 17.4 | 15.8 |
| Spain | 10.2 | 1.6 |
| Turkey | 5.6 | 5.4 |
| France | 4.8 | 7.3 |
| UK | 2.6 | 8.5 |

Source: IMF

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nb

argomenti a favore di
NO SANCTIONS ON NIGERIA
(es. prospettiva di partner on
failed state v. p. 2) valgono
x tutti i p. soggetti a
embargo. (Iran ...)

**Ambassador David C. Miller, Jr.**

**President,**
**Corporate Council on Africa**

Remarks Prepared for Delivery to:

The Middle East Institute
and
The Petroleum Industry Research Foundation, Inc.
Conference
"Economic Sanctions: Political Rationale and Economic Effect"
National Press Club
April 29, 1996

*The Corporate Council on Africa*

It is a great pleasure to have been invited as a representative of the Corporate Council on Africa to speak to you today about the situation in Nigeria. As you may know, the Corporate Council on Africa is a private, non-profit organization, composed of approximately 90 American corporations and individuals who came together in 1993 to promote the growth of the private sector in Africa. Our members hold a variety of views on most African issues, including Nigeria, but they all agree on the Corporate Council on Africa's guiding principle that the engine for economic growth in Africa must be the indigenous African private sector. It is the African private sector in a growing economy, not foreign assistance, which will create jobs, stimulate new enterprises, provide a local tax base for African governments, and improve the quality of life for all Africans.

This is not a unique concept. Indeed, the current Administration has been at the forefront of promoting international trade and commerce as a cornerstone of both political stability and progress toward democracy. The late Commerce Secretary Ron Brown -- a strong supporter of the Corporate Council on Africa -- was on such a mission when he met his untimely and tragic end. In a fitting comment about his late friend, Mickey Kantor aptly summarized the objectives of the Secretary's last mission: "He understood that we won't be able to build a functioning civil society there without a growing economy." Although the direct reference was to Bosnia, the lesson holds equally true for Africa.

Several months ago, a number of our members approached the Council to express their concerns about the course of events in Nigeria. They were concerned about the safety and well-being of their employees in Nigeria, both American and Nigerian, in the wake of possible political turmoil. They were also concerned that the domestic debate about Nigeria was being framed inaccurately and simplisticly as the struggle between democracy and human rights versus "evil and oil," as one columnist recently phrased it. They were very much concerned about the ongoing discussion about imposing various forms of economic sanctions against Nigeria. While there is general agreement about the need for progress toward democratic government and respect for human rights in Nigeria, the substance of much of the policy debate seemed focused more on punishing that country for past wrongs rather than on providing any incentives for future improvements.

In response to these requests, the Corporate Council on Africa established a "Working Group on Nigeria." The objective of the "Working Group on Nigeria" is not to usurp the role of international diplomats as they provide advice and pressure to keep the political process in Nigeria moving in a positive direction. Instead, this initiative was designed to facilitate a dialogue with policy-makers about the appropriate and constructive role the U.S. private sector can continue to play in Nigeria and to work in concert with the diplomatic process if at all possible. American companies work best in democratic environments, with stable political systems based on the rule of law. We believe American business can be most helpful during this process by strengthening of the Nigerian economy, the base upon which a "functioning civil society" and any new democratic government must inevitably rise.

*The current reality in Nigeria*

The image many Americans mistakenly hold of Nigeria is that of a rich nation, awash in revenues from oil pumped out of the ground, whose economic destiny could be easily reversed if only the benefits were shared more equitably. No one would deny that for too long, Nigeria's potential has been stalled due to domestic political turbulence and economic mismanagement by both military and civilian regimes.

However, the American companies which are operating in Nigeria tell us of another reality which they and their employees face on a daily basis. They tell us of a Nigeria which is struggling with the most basic of human needs. They tell us of a country where a once buoyant middle class is being squeezed out of existence, where per capita GDP has crashed from nearly $1200 in 1980 to only $300 in 1993, and where half of all children aged 2 to 5 show signs of persistent malnutrition. A recent study found Nigeria's population growing at 3%, the third highest national growth rate in the world. According to the World Bank, "basic social indicators place Nigeria among the 20 poorest countries" and "in real per capita terms, consumption and income are no higher than they were in the 1970s."

The prognosis for the future is no rosier. By the year 2020, according to U.S. Bureau of the Census estimates, the population of Nigeria will more than double, to over 215 million, concentrated primarily in the urban areas. I am reminded of the article, "The Coming Anarchy" by Robert Kaplan, which appeared in the February 1994 Atlantic Monthly. Kaplan's thesis, widely discussed at the time in academia as well as senior government circles, is that economic and environmental degradation, a product of under-development, tribalism, unchecked disease, over-population and war, threatens to create a category of "failed states" which would prove impossible to govern by anything resembling a democratic government. Kaplan astutely gave particular attention to Nigeria as a "bellwether for the region," the dominant economic and political power in West Africa.

The Corporate Council on Africa does not share Mr. Kaplan's pessimistic view that the course toward anarchy in Africa is inevitable. To the contrary, we are encouraged by numerous developments which indicate that countries of Africa -- South Africa, Ghana, Uganda, and others -- understand the promise of democracy and the private sector to encourage development and empower their peoples. Nevertheless, Mr. Kaplan's argument does raise a salient point about how we formulate our political and economic policies toward Nigeria, as well as other developing nations.

*The political problem*

America has a massive stake in Nigeria's ultimate success. Politically and economically, Nigeria is the linchpin of West Africa. One of every five Africans is Nigerian and goods originating in Nigeria account for approximately 80% of the goods sold in the West African region. Nigeria is also America's largest trading partner in all of Africa and direct U.S. investment exceeds $4 billion, with contracts and other commitments which will account for billions more. Nigeria is the source of approximately 9% of U.S. oil imports and represents an annual market of over $1 billion for American goods and services, ranging from sophisticated technical equipment to wheat, and thousands of jobs for American workers. New major projects are underway which could represent additional exports and opportunities.

Nigeria's economic potential, however, has been stymied by domestic political turbulence and economic mismanagement and characterized by a nearly unbroken string of military governments that have ruled the country since independence. National elections in 1993 were to have returned Nigeria to civilian rule, but the results were annulled and a new interim military regime was put in place, headed by General Sani Abacha. Domestic opponents were arrested and political activity has been restricted, leading to international criticism of human rights violations and calls for a speedy transition to democracy. In October 1995, Gen. Abacha announced a three year transition plan, to culminate in new national elections and the installation of a civilian president by October 1998. However, the government's decision the following month to execute several political activists, including a well-known local leader, catalyzed international criticism and accelerated calls for economic sanctions to force more rapid political change.

The United States government has responded to these and other events in Nigeria by terminating official development assistance, restricting the travel of senior Nigerian officials, sharply limiting military-to-military relations, and opposing new World Bank loans. There is legislation before both the House and the Senate which would impose economic sanctions on Nigeria, including a freeze on all new investment to that country.

The Administration has also commenced a series of high-level discussions with European and other governments about imposing a package of multilateral economic sanctions on Nigeria to demonstrate the seriousness with which the international community views the situation and to pressure the Abacha government to turn over the reins of power to an elected civilian government as quickly as possible. Spokesmen for the Administration acknowledge that multilateral sanctions would be far more "effective," but assert that the U.S. would be willing to impose unilateral sanctions if necessary to make its point.

*Economic Sanctions: Are they appropriate? Would they be effective?*

In my view, there is no question that international economic sanctions can be a legitimate foreign policy tool against rogue regimes which threaten international peace and security. In some cases, economic sanctions may be the only real mechanism, short of military action, which any Administration has at its disposal to respond to clear threats to America's national interests. However, Nigeria is not a threat to its neighbors. Nigeria is not seeking to acquire nuclear or biological weapons. Nor does Nigeria support international terrorism. On the contrary, Nigeria is an leader in regional peacekeeping efforts, as in Liberia where Nigerian troops constitute the largest component of the African peacekeeping force. Instead, our problem with Nigeria is a function of its internal politics and practices. As problematic as they may be, it is difficult to argue that these practices constitute a threat to the international peace as outlined in the UN Charter.

There is also a serious question about whether economic sanctions will have any impact on the segment of Nigerian society we are trying to influence. The Nigerian elite is relatively small, predominantly military, and generally wealthy enough -- as was the case in Haiti -- to take advantage of porous borders and other avenues to insulate itself from the effects of economic sanctions. This contrasts with the South African case, where 4 1/2 million white voters watched their economic prospects deteriorate before their eyes and chafed under the isolation through the travel and sports bans. In South Africa, international economic pressure -- coupled with a strong internal opposition movement -- clearly did compel the enfranchised whites to institute the necessary political changes. However, most of these elements are clearly missing from the Nigerian equation.

While the Nigerian ruling elite may be relatively insulated from the effects of economic sanctions. not so with the U.S. companies which have valuable equities in and just offshore Nigeria. It is difficult to imagine how the Nigerian government would tolerate the international humiliation of economic sanctions without some reprisals against the companies belonging to the countries concerned. There is no guarantee that the Nigerian response will be what we might consider proportionate nor is there reason to believe that the international competitors of these American enterprises would not attempt to exploit the situation. In short, Nigeria would likely be able to find other international partners to fill whatever gaps might emerge, while American leverage and influence over future events would be marginalized. In this regard, it is significant that Nigeria has, over recent months, initiated very public accommodations with China, Iran, Poland, and Iraq, while solidifying its trading relationships with its West African neighbors, including Senegal.

*Sanctions are not the answer*

The members of the Corporate Council on Africa strongly believe that the policies we pursue toward Nigeria should be carefully crafted to move us toward the goals we seek, not propel us toward the fate we are trying to avoid. Simply put, it hard to imagine how measures, such as economic sanctions, which further stifle economic growth and drive one of the world's 20 poorest countries deeper into poverty and hopelessness can be a stimulus for a successful political transition to democracy and prosperity. To the contrary, I believe that the late Commerce Secretary Brown was exactly right in his assessment: A viable economy is crucial to any new government's stability and its ability to meet the real needs of its people. It is one thing to say that we want to see an elected civilian government replace a military regime. It is quite another to ensure that any new Nigerian government has the capacity and the means to cope with the complexities of managing a society of over 100 million people, split with ethnic, religious, and tribal animosities and burgeoning demands for basic human needs.

*Responsible engagement, not isolation.*

Instead of isolating the Nigerian government through sanctions, we believe that American policies toward Nigeria should be designed to encourage positive development, raising the standard of living for the Nigerian people and demonstrating the promise of our democratic values. The members of the Corporate Council do not claim to have any precise prescriptions for a problem which remains essentially one the Nigerian people must ultimately solve for themselves. We look to our highly capable cadre of diplomats and other experts to define bilateral and multilateral policies which are designed to help Nigeria along the democratic path. At the same time, it seems clear to members of the Corporate Council that the key role for the U.S. at this critical time is responsible engagement, not isolation.

In our conversations with key policy-makers in Washington and with our contacts in Nigeria, members of the Corporate Council have stressed the need for more intensive dialogue between the two governments. Events over the last three years have reinforced on each side serious questions about the intentions and the reliability of the other. In some cases, the issues are fundamental and would obviously be subject of prolonged negotiations, but in others it appears that faulty perceptions and miscommunication are the main culprits. A crucial element in this process would be the establishment of a mutually-recognized set of benchmarks which could provide a goal for the Nigerian government and a standard for the international community to judge the pace of any progress toward stable and democratic government.

It is also important to establish a package of support and incentives to encourage the Nigerian government to avoid provocative actions and to make diligent progress toward its self-proclaimed goals, on both the political and the economic fronts. At the minimum, this list of options could range from "no new sanctions" to the phased elimination of sanctions already in place. The list of incentives could include direct linkages with new loans and debt rescheduling negotiations, as well as some assistance for the elections process.

*What can be done now?*

Sanctions will not solve the problem of developing a functioning civil society in Nigeria, nor will they provide for the well-being of 100 million Nigerians. Instead, we believe the U.S. private sector -- doing what it does best -- can perform an invaluable function in helping Nigerians create the confidence and economic wherewithal to develop and maintain a new pattern of government. Members of the Corporate Council on Africa have made it clear to both the Nigerian and American governments that we are willing to assist in any way we can in working toward both our objectives: democratic government and economic progress.

American companies have already taken the initiative in working directly with Nigerian communities themselves to improve their basic conditions and build potential for the future. What began, in many cases, as ad hoc decisions by local company management to ameliorate the worst of the local problems -- supplying clean water or helping build small local schools for the children of their employees -- have burgeoned into major community relations programs, which rival the foreign assistance efforts of Western governments. American companies are providing direct financial and other support -- focused on the communities in the vicinity of their ongoing operations and employment centers -- easily in excess of $20 million per year. Assistance is being provided in education, health, water supply, electricity, agriculture, sports, arts and culture through yearly budgetary allocations. Working in close collaboration with local community leadership, U.S. companies have provided direct support for projects that would not otherwise exist, such as a $225,000 hospital at Uquo Ibeno, an eight room schoolhouse at Onne Creek, a $182,000 library at Eket, and an array of smaller clinics, school buildings, and water systems.

U.S. companies on all levels maintain active training programs, keyed to employee development and technical skills. As a result, Nigerians numbering in the tens of thousands have not only learned entry-level industrial skills, but many have graduated to advanced training and moved on to other productive contributions to the Nigerian economy. Beyond basic or company-specific training, one American company has invested over $4.5 million in what is easily the most advance technical training institution in the region, where it offers 2 years of tuition-paid training to several hundred young Nigerians a year in an array of technical and professional fields. American companies have active programs for support of local universities, and a positive record for hiring Nigerian graduates for responsible positions within their companies, including leadership positions in operations outside Nigeria.

As members of the private sector, we are convinced that a policy of responsible engagement offers the best prospects for helping Nigeria move through this traumatic period. To impose economic sanctions on Nigeria at this time would be tantamount to acknowledging an inability or unwillingness to make that process succeed. We believe the stakes are much too high, not just for Americans but for the people of Nigeria and for their neighbors in West Africa, to accept that self-defeating conclusion. Instead, the members of the Corporate Council believe there is much that can be done to assist Nigeria in making a difficult transition to democracy. We have already begun the process, and hope that the example will encourage others to join the Nigerian people in building a better future for themselves.

Thank you.

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## Oil Sanctions:
## Their Effectiveness and Long-Term Ramifications

By

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Economic Sanctions: Political Rationale And Economic Effect
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**Oil Sanctions: Their Effectiveness and Long-Term Ramifications**
**By: Dr. Cyrus H. Tahmassebi**
**Energy Trends, Inc.**

The U.S. government currently has in force, either unilaterally or in conjunction with U.N. resolutions, oil embargoes/sanctions of one kind or another against Iran, Iraq and Libya. With the current political situation in Nigeria, its addition to the list of embargoed nations cannot be ruled out. Moreover, the U.S. government also has a variety of non-oil sanctions/embargoes in place against a number of other countries. For example, Cuba has been under U.S. trade embargo for decades. Furthermore, some officials have recently suggested sanctions to fight trade-related corruption in foreign countries. Our discussion, however, will focus only on oil embargoes/sanctions, because they are the most important and most frequently used form of economic punishment deployed by the U.S. government.

Oil embargoes/sanctions are not new. Their use in the past, however, was limited primarily to wartime or severe political crises where the national interest of the imposing nation was clearly at stake. In the 1970's, oil was also used unwisely by a number of producing countries as a political weapon against certain consuming countries. Most oil exporting countries welcomed the resulting higher oil prices at the time and celebrated this decision as a sign of their newly emerging economic and political power. However, in retrospect, most observers now believe that the use of oil by these countries as a political weapon was a mistake. The resulting higher oil prices did not last for too long; they suppressed demand growth and encouraged more drilling and increased production outside of OPEC. In the process, not only OPEC lost a huge market share, but was also stamped as an organization that would not hesitate to use its oil at the detriment of the industrialized countries-- a very negative publicity that still lingers on. Today, the situation is reversed. The glut in the world oil markets allows governments in major consuming countries to use oil as a foreign policy weapon. It is worth noting, however, that with the exception of United States, oil is rarely used unilaterally as a foreign policy tool by other industrialized countries.

To be sure, the U.S. government has had, at least from its own perspective, compelling reasons for resorting to oil sanctions as a foreign policy measure. After all, it is the only remaining superpower with vast responsibilities around the globe. Moreover, given its huge oil markets and the colossal size of its oil and oil service companies and their technological and financial resources, it would seem that the United States could be the only country in the world that can use oil as a political weapon effectively.

However, the use of oil sanctions as a political weapon has proven to be controversial. While some have vehemently supported them, others have expressed reservations about their efficacy or the government's justification for using them. Citizens of the country being sanctioned (particularly those who reside in the United States) have also been quite vocal in expressing their emotions for or against such measures. However, the purpose here is not to discuss those emotional sentiments. What this paper attempts to accomplish is to find an answer to the following questions:

- Have oil embargoes/sanctions been successful in achieving their political objectives?
- If not, what factors have contributed to their failure?
- What are the long-term ramifications of such policies for the U.S. oil industry?

## Have Oil Sanctions Been Successful?

Generally speaking, economic/trade sanctions are imposed either to exact commercial concessions or to achieve political objectives. By and large, sanctions seeking commercial or trade concessions have been successful. However, the story with oil or non-oil sanctions pursuing political objectives is quite different. With the exception of South Africa, sanctions have had very little success in affecting political changes. For example, a close analysis of numerous oil sanctions imposed for political purposes over the last few years indicates these measures have been successful in slowing growth, creating economic dislocations and financial hardships. However, these results cannot be construed as a sign of success because none of them by themselves are the ultimate objectives in politically motivated sanctions. The prime objective behind political sanctions is to force political changes, be it in certain internal affairs (e.g., human rights abuses) or foreign policy issues (e.g., territorial ambitions, nuclear proliferation, etc.). If political sanctions had been successful, Fiedel Castro and Saddam Hussein would have long changed their behavior or fallen from power. South Africa, often mentioned as an example of effectiveness of political sanctions, was a very exceptional case where a small minority was ruling a huge majority in the African continent and the sanction was truly a multilateral effort. Moreover, the economic sanction was augmented by a significant amount of political pressure. Still, it took decades for the measure to force the apartheid regime to yield to international pressures.

It seems the main underlying premise in the use of sanctions by the U.S. government as a foreign policy tool is a notion that the resulting financial pressure would make the governments in the sanctioned countries unpopular with their own people and subject them to such strong domestic criticism that they would be forced to accept the changes demanded of them. Although the ouster of the regime is rarely mentioned explicitly as a goal in defining the objectives of these sanctions, it is assumed that a protracted public discontent would eventually lead to it. However, the survival of Castro in Cuba and Saddam Hussein in Iraq, despite years of embargo, is a testament to the fact that the basic premise behind the U.S. sanction policy may be severely flawed.

## Factors Contributing To The Failure Of Sanctions Policy

If sanctions can create financial hardships and weaken the economies in targeted countries, why do they fail in achieving their primary goal of bringing about the desired political changes? Although there may be no consensus on the answer(s), the followings seem plausible:

- Economic sanctions are probably more effective as a threat than as an action to bring about political changes. Governments in targeted countries may be willing to yield to political pressures prior to the public announcement and/or implementation of sanctions. Once publicly announced or implemented, any yield to the sanctioning government's demands is normally deemed as nothing short of capitulation, which may make these governments even more unpopular with their people and vulnerable to internal criticism.

- Sanctions would be much more effective if applied multilaterally and if they enjoy the sincere support of other nations (e.g., the case of South Africa); but this is seldom the case. Most U.S. oil sanctions are unilateral and have little genuine support from other countries, including U.S. allies. Lack of sincere support could be due to economic and/or political considerations. Attracting the support of other countries becomes even more difficult when the dispute is primarily due to philosophical differences that might be less important or detrimental to the other countries' national interests. Some observers believe that a recent bill introduced by Senator Alfonse D'Amato (R-NY) may put teeth in the U.S. sanctions policy. The bill seeks to bar any foreign company that conducts a material amount of sanctioned activity with the targeted country from undertaking trade and other business activities in the United States. However, some experts believe this measure, if enacted, will be challenged in international courts and the World Trade Organization and could seriously damage U.S. relations with its allies.

- Sanctions usually take a long time to inflict tangible damage to the economy of the targeted country and bring about enough pressure to bear on its government. Unfortunately in the process, the country's inhabitants begin to feel the pain much earlier than the rulers who are supposedly the real target of the sanction. Moreover, these countries are often run by autocratic or despotic governments. Short of a popular uprising, the populace has no effective means of forcing their government to change or bringing it down. As a result, sanctions often become a protracted pain-inflicting drama whose real victims turn out to be the very people sanctions are intended to help. Thus, it is not uncommon to hear even staunch opponents of the regime in the targeted countries express their frustration with sanctions that are dragged on for too long with no discernible effect on the rulers. Strange as it may sound, some in embargoed countries have likened protracted sanctions to weapons of mass destruction in the sense that they both entail huge economic losses and indiscriminately inflict harm and misery on a very large number of people. In a war, these critics would say, the ruling elite would be equally exposed to the danger; however, under most sanctions they remain in power unscathed.

- Given the nature of the regimes in these countries, the governments have complete control of the mass media. They can use it very effectively to portray the sanction as an evil policy of a foreign government whose ultimate goal is to exploit the country's people or its resources. The rulers may also blame the sanctions for their own failures and all of the country's economic shortcomings. Such propaganda may cause the sanction to actually unite a nation behind its government rather than encourage the populace to revolt against it.

- Governments in sanctioned countries often try to break up the coalition behind sanctions by offering lucrative business deals to countries opposed to the sanction policy or that have a propensity to leave the coalition. Such an action not only may reduce the sanction's effectiveness, but also could gradually weaken the position of the leading government in the coalition vis-a-vis its own business community.

## Ramifications Of Oil Sanctions For The U.S. Petroleum Industry

Oil sanctions inflict financial hardship on the targeted country, but they are also bad for the economy of the imposing country because they constrain trade, create uncertainty and economic dislocations, and constitute yet another form of government interference in the private sector. Thus, unless they are used quite selectively in cases of over-riding national interest, the oil industry is not likely to support them.

Sanctions affect the U.S. oil industry in many ways--both in the short-and long-run. If the sanction prohibits oil purchases from a certain country, the resulting curtailment in supply may lower competition and undermine the price negotiating position of the oil purchasing company vis-a-vis other suppliers. Sanctions may also result in costly dislocations--particularly for refiners who cannot run crude oils of different grades or replace the lost oil with supply of similar quality. Replacing sanctioned barrels may sometimes require securing the needed supplies from sources at greater distances and at much higher shipping costs. Ironically, while the companies will have to face these additional costs and the cumbersome dislocations for many years, the targeted country may quickly find new customers for its oil with little or no long-term adverse consequences.

The recent sharp increases in oil and gasoline prices is a good example of the detrimental effects of sanctions on the U.S. economy and oil companies. The uncertainty created by the prospects of a partial lifting of the Iraqi sanction has forced most oil companies to reduce their inventories significantly. Oil companies may suffer large losses in the value of their inventories if the Iraqi return would force oil prices down precipitously. As the UN-Iraq negotiations concerning the issues surrounding this partial lifting of sanctions continue, oil companies are forced to pay much higher prices for the prompt barrels to meet the demand of their customers. As a result, crude oil prices for delivery in the immediate months were at times $5-$7 per barrel higher than the price for the outer months. This market "backwardation" has also resulted in higher gasoline prices that in turn is partially blamed for the renewed fear of inflation, higher interest rates and the stock market volatility.

Sanctions could entail the most enduring and damaging adverse effects when they are applied to overseas exploration and production ( E&P) or the so-called upstream activities of oil companies operating in foreign countries. Oil companies who venture into upstream activities overseas face many risks and uncertainties, ranging from dry holes to revolutions and nationalization. Economic sanctions imposed on these companies by their own government add a new element to the risks historically and technically inherent in the E&P business. Actual or potential financial losses could be huge by any standards. The investment already committed may be lost forever without any compensation. Alternatively, the opportunity to earn an attractive return on future investments may be forfeited to competition from other countries. Obviously, if oil companies from other countries do not move in, the sanctioned country will feel more pressure. However, this is seldom the case. Moreover, by delaying the E&P activities, such sanctions are also likely to result in lower supply, higher world oil prices, inflation and thus adversely impact the global economy and particularly the current account balance of the sanctioning country.

As mentioned earlier, the U.S. oil and oil-service companies are endowed with superb technological know-how and vast amounts of financial resources. Therefore, oil exporting nations are likely to remain dependent on American expertise and money for many decades to come. But major oil companies in Europe, Asia, Canada, and elsewhere are also well prepared--technically and financially--to move in where American companies are barred from doing business. The swift move by the French oil company Total to replace Conoco in the Iranian offshore deal last year is a good example. Some observers have suggested that the Total project may progress very slowly as long as the U.S.-Iran relations remain hostile. These observers believe that Senator D'Amato's proposed bill will also discourage Total and other companies from moving in where U.S. companies are barred to invest and operate. But the outcome of that bill and its impact remain to be seen. Even if Senator D'Amato's bill would indeed discourage other companies from moving in immediately, it is not likely to erase the long-term damages that sanctions could inflicted on the commercial relations between the U.S. companies and the sanctioned countries. For example, according to recent news reports, French and Russian oil companies have already signed major E.&P. agreements in Iraq pending the lifting of U.N. sanctions.

There seems to be a growing concern among oil industry observers that widespread use of sanctions could be very costly to the U.S. oil companies and detrimental to the American interest in the long run. Some fear that because it is the only superpower in the world, the United States may become engaged in many international conflicts and use the sanction card too often to the detriment of its oil companies. This solo-superpower status of the United States coincides with its growing need for imported oil and a rising probability of political problems in oil producing countries. This does not imply that the world is running out of oil or that the United States may become unable to secure the oil it needs. It does imply, however, that more and more oil fields that are denied to the U.S. companies by their own government are likely to be run by non-American concerns. Consequently, American companies, rather than produce the oils they import into the United States, may become more and more the buyers and importers of oils produced by others.

## Concluding Remarks

From our discussions here, it is evident that sanctions imposed to achieve political objectives are not likely to be successful. There are many reasons for their failure or ineffectiveness. First and foremost, *unilateral* sanctions are unlikely to succeed. This is because they often drag on for too long, gradually become less and less popular nationally and internationally and eventually lose their effectiveness. To avoid such an outcome, the sanctioning country would be better off if it would form a strong and dedicated coalition *before* it imposes the sanction. However, such a coalition would often require an international consensus on the merits of and justifications for the sanction. Obviously, the more controversial the issues in the conflict, the less likely the chances for forging such a consensus. It follows, therefore, that economic sanctions should be used very selectively, the issues in conflict should be serious and of global concern to attract support from the international community. If such a consensus is achievable, the sanction may be imposed through an international body such as the United Nations rather than a single country. Obviously, sanctions imposed in this fashion could be much more effective and less criticized. Some observers have mentioned President Bush's approach in countering the Iraqi invasion of Kuwait and his skillfulness in building an international coalition behind the use of force to eject Iraq as an excellent example of how a superpower may handle a major international dispute.

Moreover, in applying sanctions, the imposing country or the international body could prevent a lot of criticism and allegations of double standards and hypocrisy by being consistent. The leaders in the sanctioned countries can easily detect these inconsistencies and use them to their own advantage and drum up support nationally and internationally for their own cause.

Also, it has been suggested that since the United State is now the only superpower in the world, it should be more tolerant of political disagreements with other countries if such disagreements pose no real threats to its national interest or security. "Respect begets respect," some observers have asserted. These observers have suggested the U.S. government's foreign policy should be a mirror image of the democratic policies it follows domestically. Otherwise, given the growing multi-polarity of world political and economic powers, the growing diversity and independent-mindedness of other nations, the U.S. government may find itself tangled in too many disputes around the world.

Finally, some observers have suggested that if sanctions are imposed for truly a good cause but they become ineffective, for whatever reason, then such sanctions should be augmented by additional punitive measures. What has made economic sanctions unpopular and ineffective, according to these observers, is that they are used too often, that they take too long to work and that in the process they inflict a lot of hardship on innocent people. If sanctions are augmented by other measures, not only do they become more effective, but also the fear of the follow-up measures could by itself be a powerful force to bring about the desired political changes even before they are actually implemented.

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# Oil Markets and Economic Sanctions

A Presentation by
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Chairman

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I would like to present a brief analysis of the impact of the current and proposed US oil sanctions policy on domestic and world markets which is, of course, different from evaluating the pros and cons of this policy.

## Sanctions Have a History

Oil trade sanctions or embargoes have been a frequent policy tool in the post World War II period, both by importing and exporting countries. The first post-war embargo was imposed in 1951 by the British Navy on Iranian exports during the crisis over the nationalization of the Anglo-Persian Oil Company. The next embargo was initiated by several major Arab producers who refused to export oil to the US, the UK and Germany from June to Sept. 1967 because of these countries' support of Israel during the Second Arab-Israeli War. Neither of these embargoes had much of an impact on the world market which had enough spare capacity to cope with both disruptions.

The third embargo, imposed by most Arab oil producers in October 1973 at the start of the 3rd Arab-Israeli War, took place at a time when there was virtually no spare capacity in any oil producing country. It lasted only 5 months but it triggered a historic change in the world oil market, economically and politically. The next embargo was imposed by the US on imports from Iran during the 1979-81 hostage crisis.

## Current Sanctions

Currently, the US has oil sanctions against three countries: It is a participant in, and the strongest supporter of, the UN sanctions on Iraq oil exports since August 1990; it has imposed sanctions on imports from Libya since 1982 and on investments in Libya since 1986; and it has had an embargo on Iranian oil imports since 1987 which was expanded in 1995 to include all US business transactions with Iran.

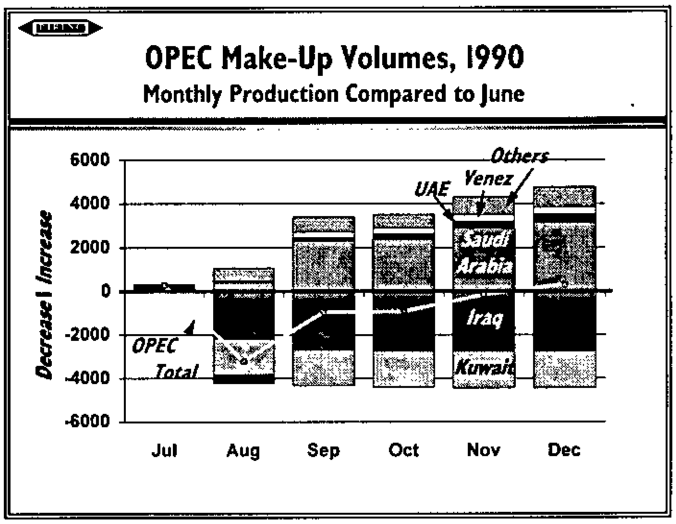
Both the Administration and the Congress now want other countries to join in the US embargoes on Iranian and Libyan oil exports or, at least, cease investing in the two countries' oil and gas sectors to reduce their export potential over time. The proposed legislation is an acknowledgment that our unilateral sanctions policy had very little effect on the sanctioned countries but put US firms at a competitive disadvantage by denying them access to these countries' oil production and trade.

Since all of these sanctions affect the same market, even though each has its own rationale, let us briefly examine each as part of a proposed comprehensive US policy.

## Iraq: Multilateral and Effective

First, let's look at Iraq, where sanctions on oil exports are multilateral, fully implemented and in existence for nearly 6 years. When these sanctions were first imposed by the UN on Iraq and occupied Kuwait in August 1990, they represented a loss of 4.5 million B/D or 7% of world oil supplies. Prices of course soared in the face of these reductions and also the fear of additional disruptions by military actions in the Gulf region. However, as we now know, the actual and potential excess capacity in Saudi Arabia, and, to a lesser but still significant extent, in several other OPEC countries, soon replaced all lost exports from Iraq and Kuwait. By December 1990 OPEC production was back to its July level and once the fighting stopped prices dropped almost immediately to their pre-invasion level even while Kuwait wells were still burning and sanctions on Iraq were fully implemented. The market reacted rationally to the restored flow of oil, the perceived end of military threats on existing production and the assumption that Kuwait exports would be restored fairly quickly.

Figure 1

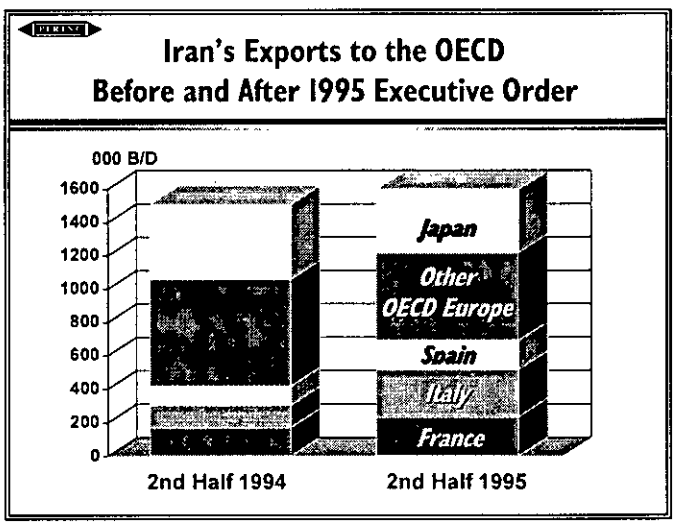



However, as long as the UN sanctions continue to keep Iraqi oil off the market OPEC's available spare capacity remains much lower than it was in 1990. It is currently around 3.5 million B/D. About 200,000 B/D of this total is located in Iran, currently the prime target of US advocates for multilateral sanctions.

## Iran: Unilateral Ineffective; Multilateral Coerced?

Let us look at Iran. While neither current government policy nor the proposed Congressional legislation contains any direct measures to block Iranian oil exports to markets other than the US, the Congressional advocates of Iranian sanctions would clearly welcome such a development. The Administration is reserved in its support but has frequently expressed

Figure 2



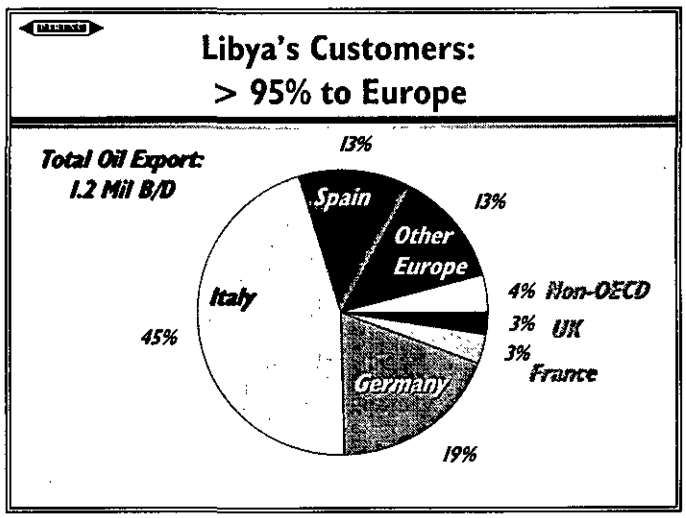
the hope that other countries will join the US embargo of Iranian oil exports to render it more effective by making it multilateral. Also, under H.R. 3107 currently under consideration in the House, any foreign company making significant future investments in the Iranian oil and gas sector may thereby be precluded from selling any oil or gas (or any other product) from anywhere to the US This could first and foremost affect TOTAL, the largest French oil company, which is currently investing in Iran and has large operations in the US The French government is unlikely to remain indifferent if this were to happen.

## Libya: Interdependence with Europe

Libya, which was added to both the Senate and the House bill this year, currently exports about 1.2 million B/D. US companies played a major role in developing the Libyan oil industry from the 1950's until 1986 when they were barred by the US government from operating in Libya. Libyan imports into the US have been banned since 1982 as part of a US policy to isolate Libya because of its support of international terrorism. However, other countries did not go along with this US policy, then or now.

Because of its Mediterranean location, Libya has become Italy's largest and nearest oil supplier, currently accounting for 30% of Italy's total oil imports. Similarly, Italy is Libya's largest oil export market, while AGIP, Italy's national oil company, is a large producer in Libya as are the major French company Elf Aquitaine and several large German firms. AGIP also has an undersea natural gas pipeline project from Libya to Sicily under active consideration. These investments are currently slightly hampered for all companies in Libya by the UN Security Council's sanctions on air traffic to and from Libya and on shipments of certain oil pumping equipment to Libya.

Figure 3

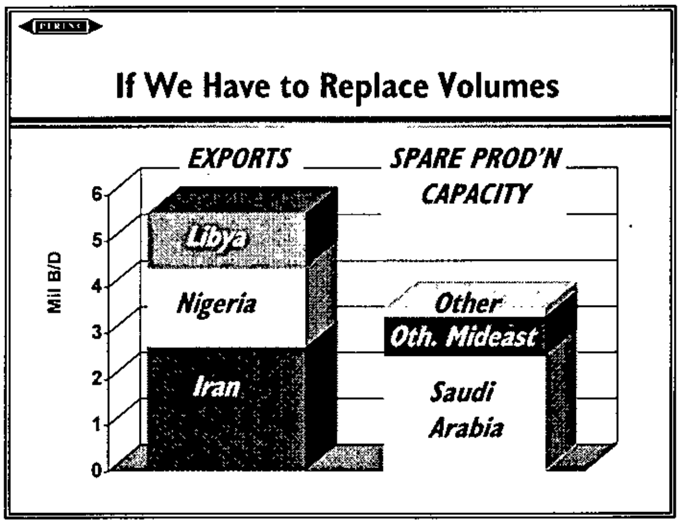



Economics and logistics clearly favor continuation of Italian investment in Libya's energy sector, and Italy and its European Union *confreres* have vociferously protested the US's planned imposition of secondary sanctions.

## The Cost of Multilateral Sanctions

If exports from both Iran and Libya, which together total nearly 4 million B/D, were substantially curtailed by US legislation coercing our allies into a multilateral embargo-by-proxy while the Iraq sanctions are still on, it would take most of OPEC's remaining spare capacity (70% of which is in Saudi Arabia and 13% in Kuwait) to offset the loss. Even then there would probably be a sharp price increase with all the attendant negative impacts on the balance of trade and inflation in the US and other oil importing countries, particularly in the developing world.

**Figure 4**




Yet, it is by no means certain that Saudi Arabia, Kuwait and the other OPEC members with spare capacity (there is virtually none outside OPEC) will actually make their capacity readily available to offset the loss in Iranian or Libyan exports. In 1990, the basis for the sanctions on Iraq was a UN Security Council resolution, as was the military action against Iraq. Saudi Arabia was part of the UN coalition and had good reason to belong to it because it felt threatened by Iraq's invasion of Kuwait. Saudi Arabia's and Kuwait's response to US-imposed sanctions on Iranian oil exports could be quite different, given the fact that Iran has not been charged with violating any UN convention nor is it viewed as a political "pariah" by most other countries, and is a member in good standing of OPEC. It should be recalled in this connection that even in 1990, several OPEC members initially opposed the idea of suspending production quotas to offset the loss of Iraq/Kuwait oil.

Thus, cumulatively, these sanctions could create supply constraints even if their impact on each targeted country is limited. This would certainly be the case under current and near-term market conditions. With oil stocks in the US and abroad exceptionally low and projected world demand rising about 2.5%, or 1.8 million B/D, for the remainder of this year as well as next year, according to the IEA, any significant extraneous supply reduction would have a disproportionate impact on prices. Such a development could also strengthen support for Iraq's position on the removal of sanctions. Any success in restraining Iranian and Libyan oil exports could generate pressure from importing countries to lift the sanctions on Iraqi exports as those consuming countries with no stomach for continued sanctions feel the pinch of increased oil prices.

Furthermore, under current market conditions any significant enforced export reduction will cause a disproportionate price increase. Hence, Iran's and Libya's loss in export revenue would likely be considerably less than their loss in export volume.

Of course, if and when the UN sanctions on Iraq are fully removed, Iraqi exports could offset almost any likely loss of Iranian and Libyan exports for several years. However, if the pace of the two-year negotiations over UN Resolution 986 (Humanitarian Aid) to export just 700 MB/D—about one-fifth of Iraq's export potential—is any indication, the removal of sanctions is a long way off. Thus, anyone advocating further constraints on oil exports must realize that for the time being, it would be additive to the embargo on Iraqi exports.

As I mentioned before, the proposed current sanctions legislation would not directly affect Iranian and Libyan oil exports but would aim to reduce future foreign *investments* in their oil and gas sectors. If passed in this form, the legislation would have little impact in the short term, i.e. the next several years, on the export levels and earnings of the two countries. Hence, they are unlikely to be coerced into changing their policies as a result of this legislation. However, world oil demand will continue to rise well into the next century. The latest EIA long-term forecast has in its Reference Case an increase of over 14 million B/D, a 2% annual growth rate, in world oil supply between 1995 and 2005. Thus, any effective externally-imposed restriction on production in these major exporting countries is likely to cause a tightening of *world* oil supplies, starting at the beginning of the next century, leading to disproportionate price increases. It should be pointed out in this connection that while the impact of the proposed investment constraints would take several years to make itself felt, it would also take several years to reverse it. Thus, there are long-term consequences of the oil sanctions policy currently under consideration in Congress. Eventually, if producer prices rise as a result of the imposed investment constraints, consumers will have to pay more for their oil products.

## Nigeria: A Potential Candidate

I have put Nigeria last because, so far, there is no official US policy or proposal that would affect imports from, or investments in, Nigeria. But, as we have heard, there are loud exhortations from a number of activist groups in the US and Europe for sanctions on Nigerian oil exports.

If any form of oil sanctions are imposed on Nigeria, the impact on the US market and the US oil industry would be quite different from that on Iran or Libya. There are no US companies in these two countries and we have not imported any oil from them since the 1980s. By contrast, there are some 10 US oil companies in Nigeria, 5 of them field operators. Last year, Nigeria's total oil exports amounted to about 1.7 million B/D of which 750 MB/D, or 44% came to the US (including shipments to the US Virgin Islands), much of it to the East Coast. The reason is the quality of Nigerian crude. Its uniquely high yield of middle distillate is an important factor in meeting the region's heating oil and diesel fuel requirements. If it became unavailable it would cause a sharp temporary regional price rise.

**Figure 5**

**US Crude Oil Imports from Nigeria, 1995**

| Importer | East Coast | Gulf Coast | Total |
|---|---|---|---|
| | Volume, in 000 B/D | | |
| BP Oil Supply Company | 125 | 60 | 185 |
| Sun Company, Inc. | 134 | - | 134 |
| Phillips 66 Company | - | 53 | 53 |
| Shell Oil Company | - | 41 | 41 |
| Amoco Oil Company | 3 | 38 | 41 |
| Add'l Co's | 31 | 135 | 166 |
| Total to Continental US | 292 | 327 | 620 |
| Hess Oil Virgin Islands | | | 130 |
| Total US Imports | | | 750 |

An effective *multi*lateral embargo on Nigerian oil exports, if it did take place, would cause sharp price increases worldwide for an extended period. A consideration in weighing a US embargo is that Nigeria might retaliate by expropriating US oil properties and incorporate them into its national oil company.

As I said at the beginning of my talk, I am addressing here only the economic aspects of the sanctions debate. The economic casualties of US sanctions on Nigerian oil could well be the US oil companies rather than the Nigerian government.

## Diversify Supply Sources

In conclusion I would like to reiterate the widely accepted precept that diversification of supply sources and peak maintenance of their productive capacity is good for importers since it reduces the risk and impact of supply disruptions. If this is so, is it really in our interest as the world's largest oil importer to actively pursue a policy of curtailing some of these supply sources?

9

# Unilateral Economic Sanctions
# Effects on Service and Supply Sector

Larry G. Bowles
Halliburton/Brown & Root
April 29, 1996

Economic sanctions have emerged as the number one barrier to trade and investment for our company and many other US companies. Existing and threatened sanctions have increased in frequency coincidentally with the increasing importance of markets we serve as an exporting employer.

The direct and indirect effects of sanctions, especially unilateral and narrowly multilateral sanctions, are pervasive, long term, and are exploited aggressively by our competitors whose home economies usually do not align with the USA on the sanctions. Unilateral sanctions threaten near-term strength of exporting employers as competitors supplant USA firms' market presence, and the long-term strength as well by eroding market share and the technology leads we have in many critical sectors. Those leads in technology and exports are also where the majority of higher paying jobs are otherwise being created. The use, or consideration of use, of unilateral sanctions also threatens the gains made in world trade order, and cooperation on international security issues.

US business leaders and our employees share the concerns expressed by many members of the Congress and the Administration about national and international security implications of the actions of rogue governments. The questions must be answered, though, are unilateral sanctions effective of their intended purpose, and what are the costs of imposing them? Congressman Lee Hamilton (D-IN), ranking minority member of the International Relations Committee, Toby Roth (R-WI), chairman of the trade subcommittee of the International Relations Committee, and Douglas Bereuter, (R-NE), expressed concern at the mark-up of the Iran/Libya boycott legislation about the need for an assessment of the jobs and economics consequences of that proposed law.

There are numerous reasons why especially unilateral and narrowly multilateral economic sanctions are not in the long-term economic and security interests of the USA. There are also increasingly numerous reasons economic sanctions are being sought - drug trafficking, weapons proliferation, democratic values, human rights, species protection, pollution control, ecosystem protection, labor rights, moral and cultural values, territorial assertiveness, and remnants of the cold war era policies.

As our nations economy and ability to maintain employment strength is strongly rooted in our global competitiveness, the political risk climate for taking the challenge of serving numerous markets in that global market place is greatly increasing. It is almost as if we should tell our new employees that their job is subject to government conscription in economic sanctions.

Politicians believe that economic sanctions are "off-budget" but they are among the most insidious unfunded mandates because politicians do not disclose their ineffectiveness, nor their adverse effect to their constituents. The proposed Iran/Libya boycott legislation would put at risk, in the US petroleum equipment sector alone, over $600 million in export sales, and over 12,000 export related jobs, as well as the technology lead gained over decades of investment, and invention and engineering.

There are international concerns about the use and reach of US economic sanctions.
For example, with respect to the recent action on the Iran/Libya boycott legislation, the EU, and some of it's member's, have expressed a concern about the behavior of the governments of targeted economies, Libya and Iran, but call for multilateral actions, for example through the UN, and express a concern that such actions as contained in that bill would be counterproductive toward the achievement of multilateral actions against the targeted economies.

Besides the technical jurisdiction of economic sanctions laws are the response to them by participants in the market place. For example, EU, and member nations, such as the Netherlands, and some of the companies in their home markets, e.g. Agip, of Italy, have expressed great concern about the reach of the Iran/Libya bill - the Netherlands even suggesting they would retaliate.

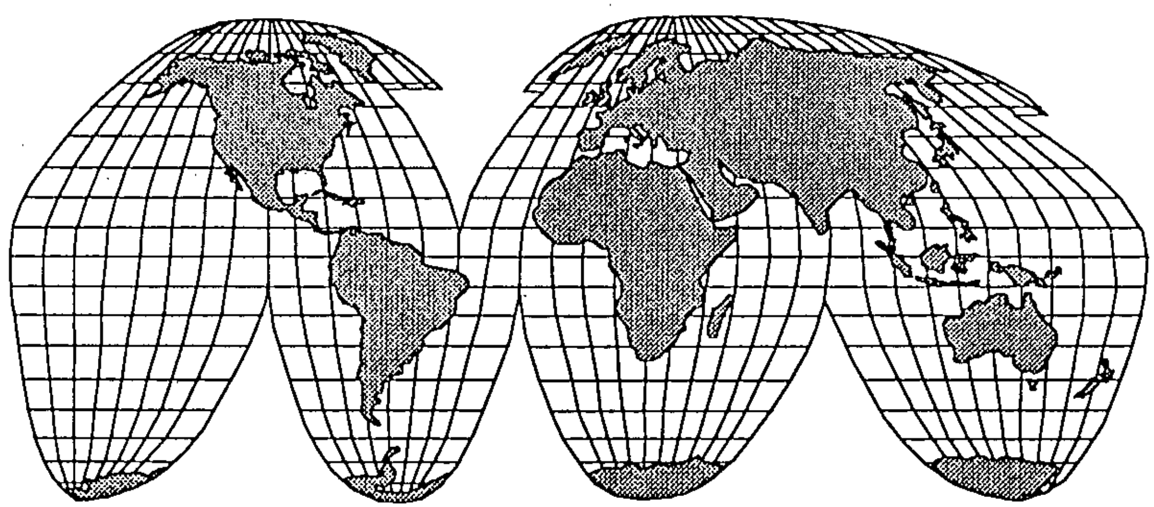
Another example of the functions of the market place is the likely market chaos, and supplanting of US suppliers in markets beyond the targeted economies of Iran/Libya, that would occur through the implementation of blocking statutes by US trading partners (similar to those provided in US law - the Export Administration Act, and the Treasury Reform Act, for such actions by foreign governments that is now being proposed in the Iran/Libya bill. The UK. and France took such blocking actions in the case of the US Russian pipeline embargo in the early 1980's, resulting in loss of US market share not only with respect to Russia, but with respect to other markets serviced by the European clients of US companies - when the US was finally forced to withdraw the boycott, it was already too late, and US firms are still being adversely effected as some EU based firms design-out US suppliers and substitute non-US suppliers who gained dominance during the boycott.

Market chaos and supplanting of US suppliers would also result from retaliation actions by trading partners - not limited to products and services like those targeted by a given US boycott. For example, the redirecting of defense procurements to non-US firms, which was done by the Netherlands, prompted by claimed unfair US trading practices).

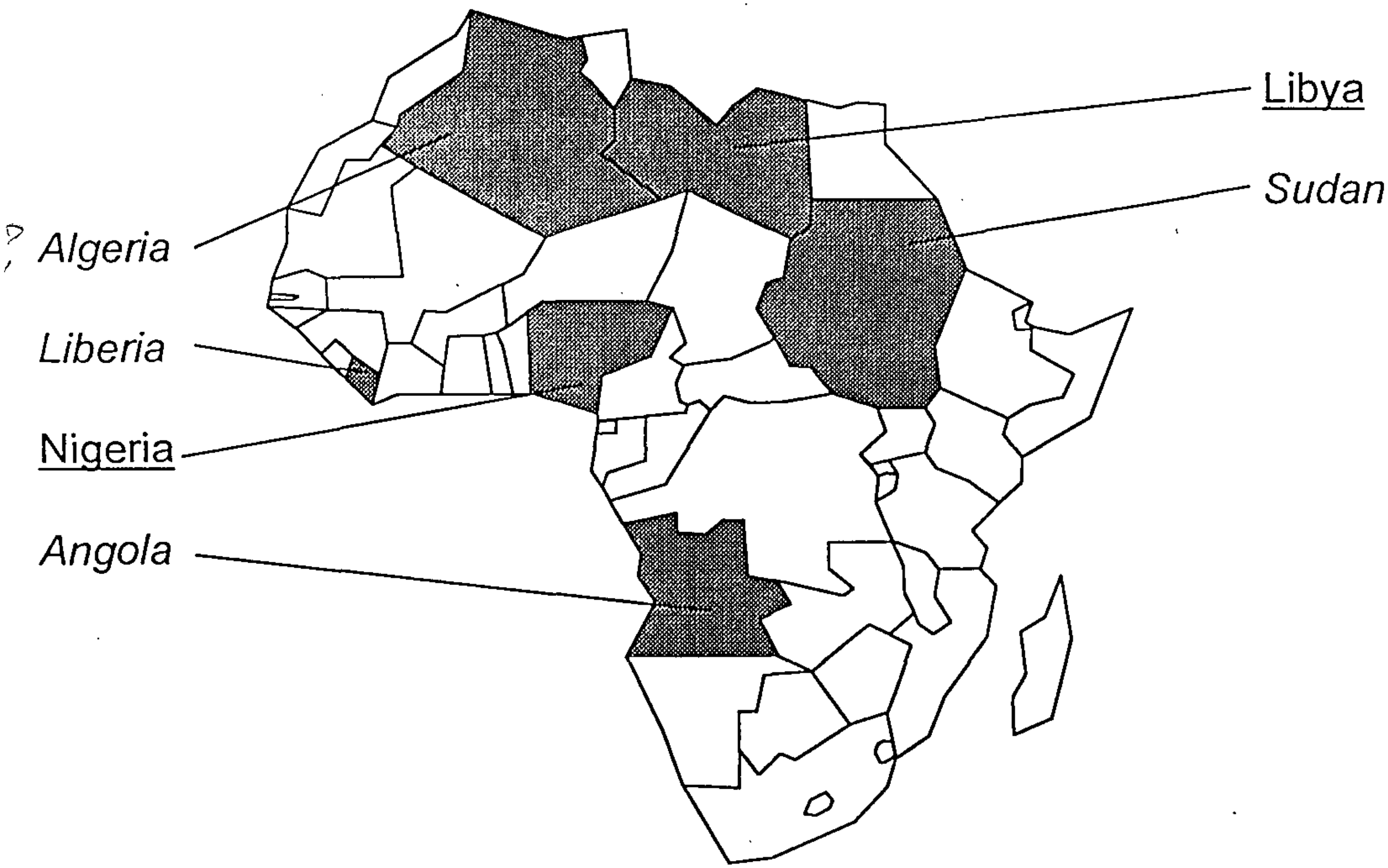
In the spirit of landmark legislation passed by the 104th Congress, such as the unfunded mandate and the regulatory flexibility acts, economic sanctions legislation, that has the potential to effect adversely US jobs and the US economy, should be deliberated carefully at the committee level and time be allowed to make sure all interested and affected elements of the US economy make an accounting of the potential consequences. Further, there should be a public disclosure of the US jobs and economic consequences of the sanctions, and when enacted, the effects, both on the targeted economy, and on US jobs and economy, should be monitored, measured and evaluated as to the efficacy of the policy. The, impacts should be carefully assessed, and serious consideration should be given, within a time-frame certain, to removing the economic sanctions that are not productive or are counterproductive.

(Text accompanied with view foils.)

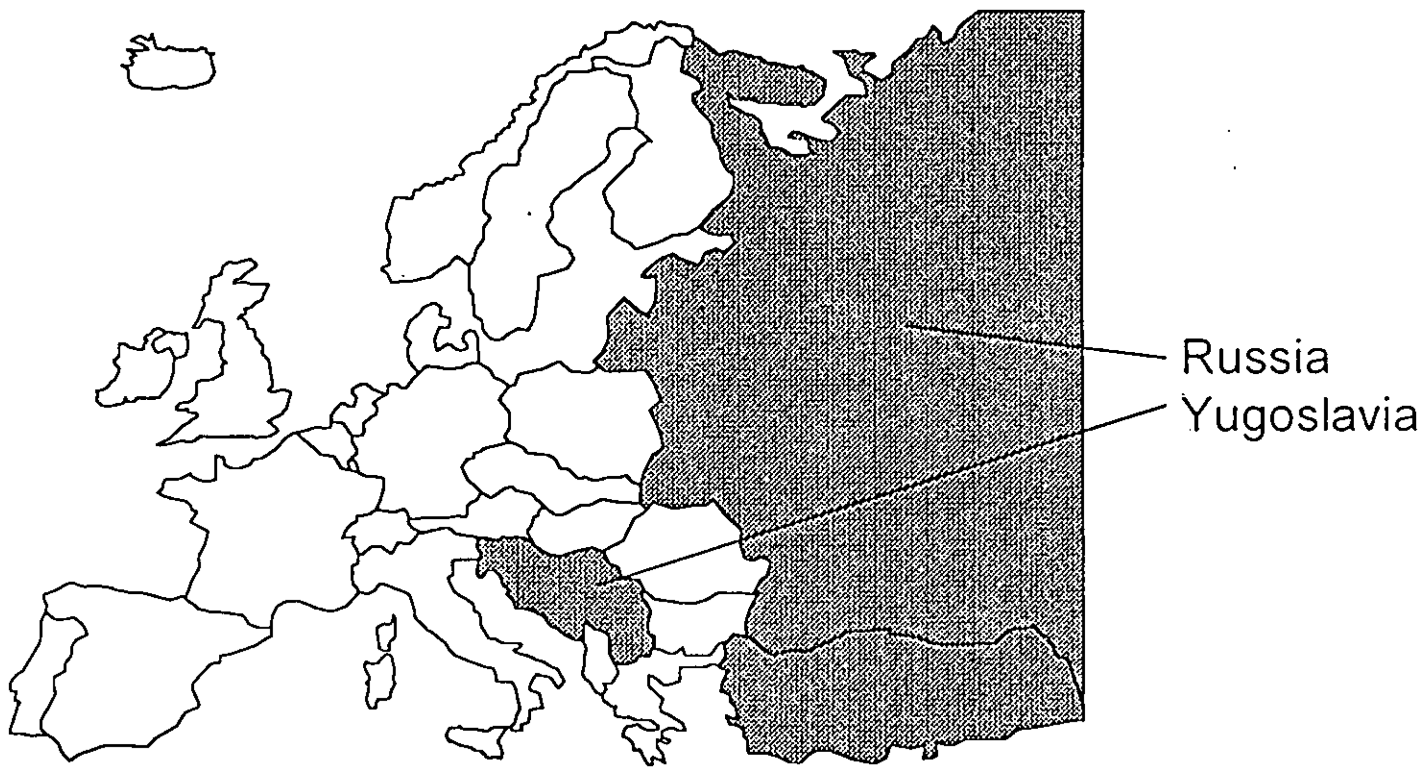
# World Map



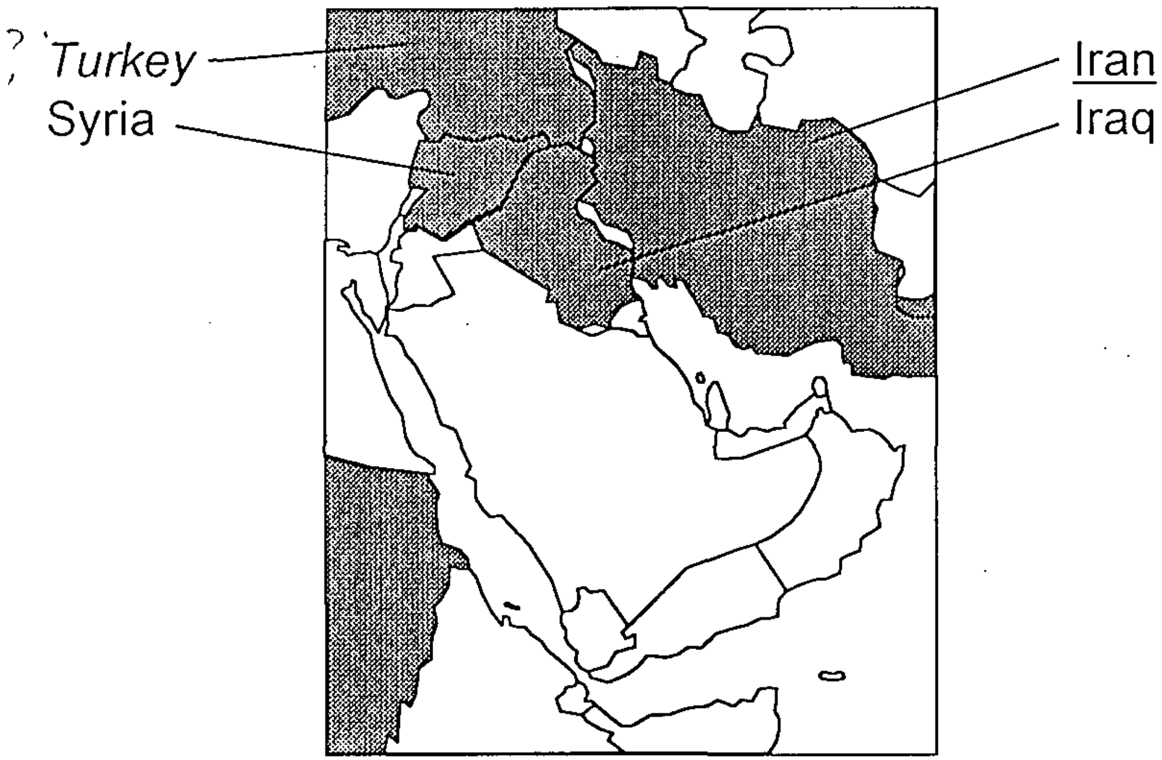
# U.S. Economic Sanctions in Africa



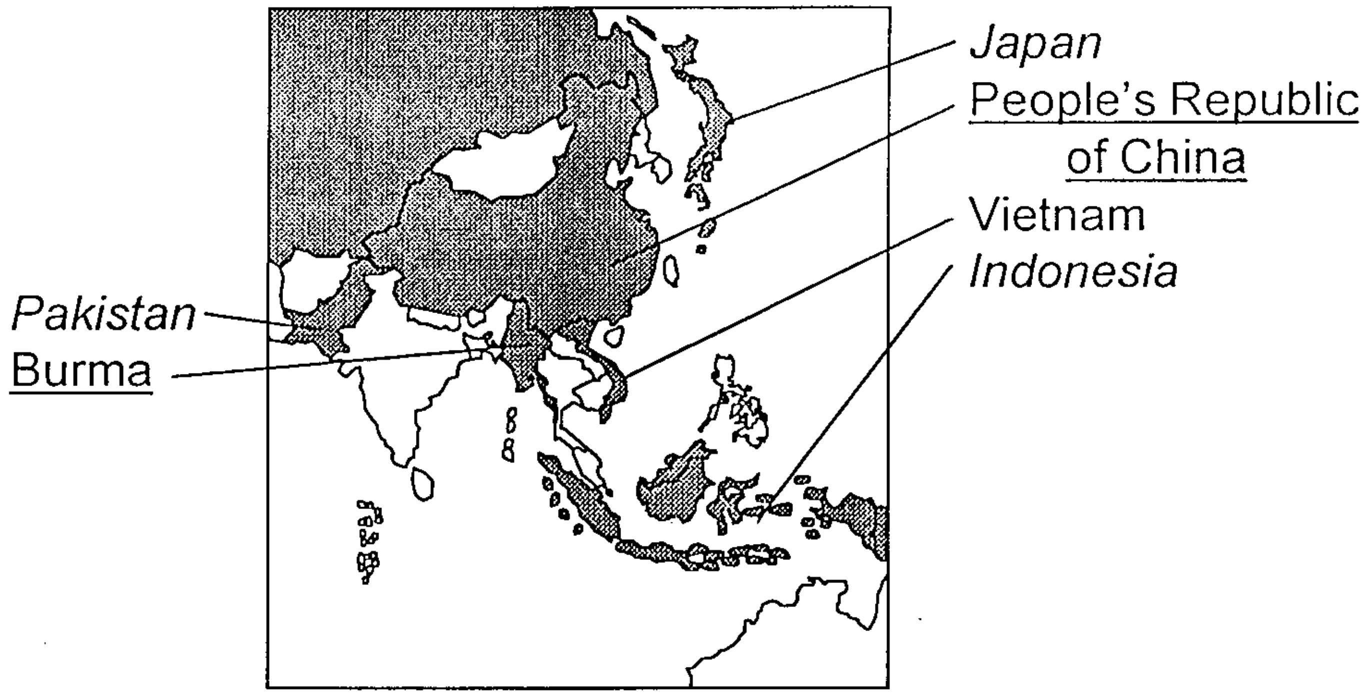
# U.S. Economic Sanctions in Europe



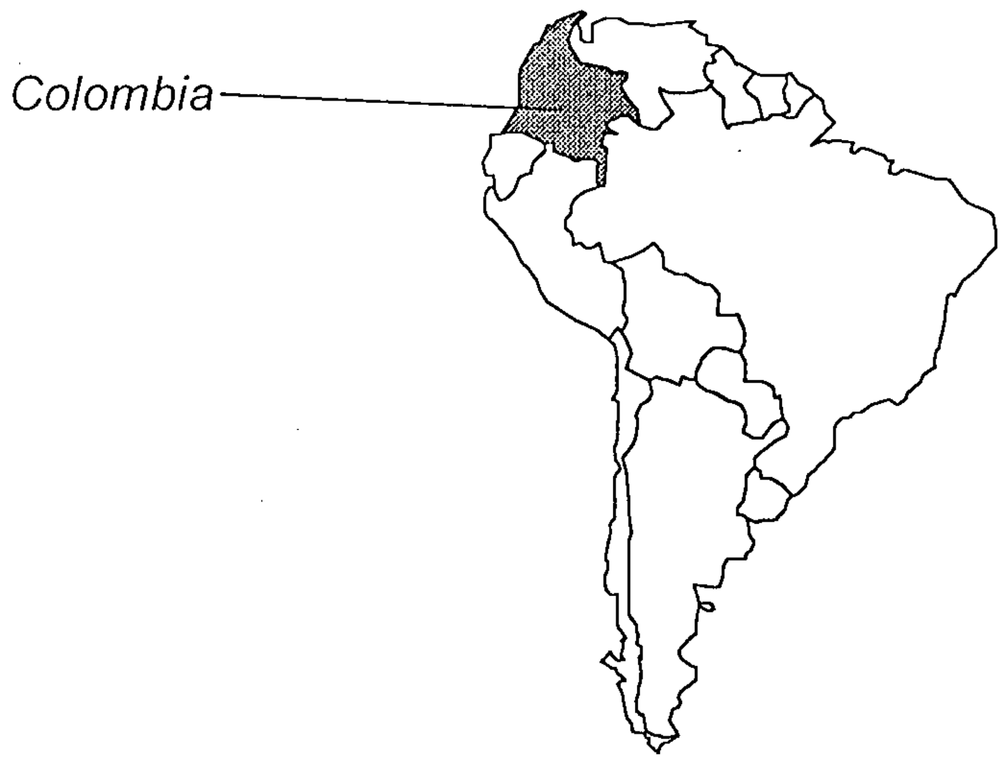
## U.S. Economic Sanctions in the Middle East



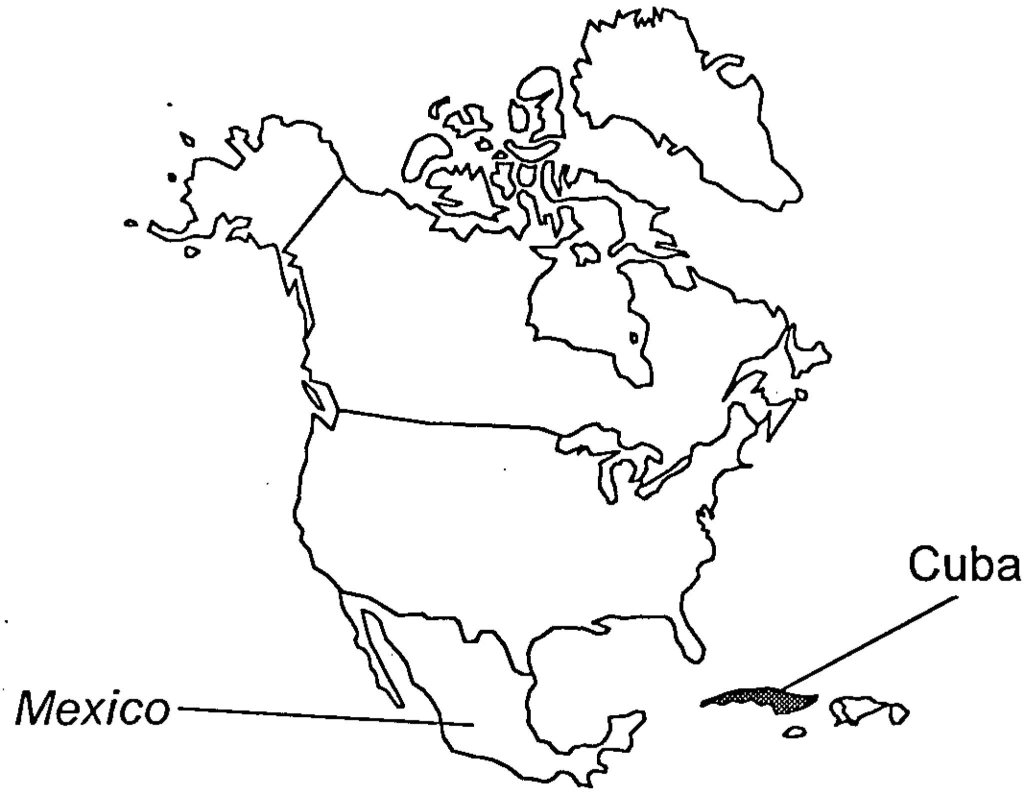
# U.S. Economic Sanctions in Southeast Asia



## U.S. Economic Sanctions in South America



# U.S. Economic Sanctions in North America



## US Foreign Policy Economic Sanctions

**Nations whose economies are of interest to some US suppliers that have been mentioned as possible targets of economic sanctions by either the Congress or the Administration include:**

| | |
|---|---|
| **Indonesia** | **human rights, worker rights** |
| **Burma** | **human rights, worker rights, drug trafficking (existing sanction)** |
| **Nigeria** | **human rights, drug trafficking (existing sanction)** |
| **Pakistan** | **human rights, drug trafficking, weapons proliferation** |
| **Angola** | **human rights** |
| **Algeria** | **human rights** |
| **Japan** | **unfair trade practices** |
| **Sudan** | **human rights, terrorist sponsor** |
| **Turkey** | **human rights** |
| **Mexico** | **drug trafficking** |
| **Liberia** | **human rights** |

**In the aggregate, these economies represent significant parts of the world market in which US suppliers are challenged as unreliable suppliers, and have significant and unpredictable home country political risk to deal with, as well as the usual consideration of host country risks.**

# US Foreign Policy Economic Sanctions

**Nations whose economies are of interest to some US suppliers, and which are targets of existing US foreign policy economic sanctions include:**

| | | |
|---|---|---|
| **Vietnam** | **unilateral** | **human rights** |
| **Iran** | **nearly unilateral/ unilateral pending** | **terrorist sponsor** |
| **Iraq** | **UN, thus multilateral** | **terrorist sponsor, territorial adventurism** |
| **Libya** | **UN/unilateral pending** | **terrorist sponsor** |
| **Syria** | **limited unilateral** | **terrorist sponsor** |
| **Peoples Republic of China** | **limited but effectively unilateral** | **unfair trading practices, human rights, weapons proliferation,** |
| **Azerbaijan** | **limited, but unilateral** | **human rights, territorial dispute (Armenia)** |
| **Cuba** | **effectively unilateral** | **human rights** |
| **Russia** | **unilateral** | **human rights, weapons proliferation** |
| **Yugoslavia** | **UN, thus multilateral** | **human rights, territorial adventurism** |
| | **(suspended, except for major weapons embargo)** | |
| **Colombia** | **unilateral** | **drug trafficking** |

(10)

Gregg Rickman

Middle East Institute
Petroleum Industry Research Foundation
Conference: The Politics of Sanctions
Monday, April 29, 1996

The views stated here do not necessarily reflect the views or position of Senator D'Amato.

During the week of November 11-14, 1995, the Iranian government held an investment conference in Teheran in which it invited 123 foreign energy development companies to attend. The conference failed horribly to meet Iran's expectations, attracting only 40-60 companies, and most of the representatives that came were already based in Iran. In the words of one State Department official, the conference was "a bust." This was the case because of an effort by the United States Congress, and I must add with all due modesty, my boss, Senator Alfonse M. D'Amato, that pushed the Clinton Administration to get tough with Iran. After the imposition of the sanctions, the White House publicly admitted this much.

For far too long the United States had been subsidizing Iranian terrorism through our trade with Iran until the President's Executive Order on May 6, 1995, banning all trade with Iran ended this practice. Unfortunately, the other nations of the world have failed to join us in this embargo. While Iran is racing to obtain weapons of mass destruction, many other countries of the world are subsidizing them through their development of the Iranian oil fields, the chief source of income for the Iranians, as well as through the provision of concessionary credits on the rescheduling of Iran's debt to each of its creditors. These practices give Iran hard currency to fund terrorism and its quest for nuclear weapons and in the case of credits, a tacit subsidy, freeing up funds to do the same.

Undersecretary of State Peter Tarnoff explained the danger of this, when at a Senate Banking Committee hearing in November 1995 he stated,

> "A straight line links Iran's oil income and its ability to sponsor terrorism, build weapons of mass destruction, and acquire sophisticated armaments. Any government or private company that helps Iran to expand its oil [production] must accept that it is ...contributing to this menace."

This could not continue and this is why Senator D'Amato introduced S.1228, the Iran Oil Sanctions Act, which passed the U.S. Senate by unanimous consent on December 20, 1995.

As for credits, Secretary of State Warren Christopher commented on May 1, 1995, that, "Concessionary credits...allow Iran to divert scarce resources to military programs and to sponsor terrorism."

Yet, despite its good intentions, the Clinton Administration has not yet been able to persuade the international community to support a sanctions regime against Iran. I think that the problem is not that the Administration is not trying, but that the rest of the world is not listening.

When I speak with staff at allied embassies, invariably I hear that they believe that our approach is wrong. They believe that by talking to Iran, the policy otherwise known as "critical dialogue," they can moderate Iran's behavior.

When I ask in return, what has critical dialogue done, for example, to lift the fatwa on Salman Rushdie, all they can answer is that they are still talking with them on the issue. This no doubt provides little comfort to Mr. Rushdie.

I must say, that their is no sympathy in Congress for critical dialogue and that the patience of Congress has worn thin for those nations that continue to stick to this position. Simply put, we believe that Iran must be economically isolated until it forgoes its policies of terrorism and aggression. Iran's aggressive policies impose a clear and present danger to the vital security interests of our own nation and those of our allies.

We don't have to go much farther back than just a few weeks to prove this. Hezbollah's ongoing campaign of Katyusha attacks on northern Israel is being supplied by Iran, through Syria. This is surely not a sign of a "moderate Iran." For that matter, nor was Iran's January testing of a sea-skimming cruise missile, the C-802. Clearly this missile poses a threat to U.S. ships in the Persian Gulf.

Without stauncher policies there is no doubt that Iran will continue to get the benefit of doing business with companies that put their own desire for profits ahead of the interests of the international community in preventing Iranian aggression. Furthermore, the continued provision of concessionary credits by Western governments, will only free up more money for Iran's military and terrorist use.

However, with such a policy, there can still be a chance of convincing Iran that its aggressive policies are entirely counterproductive. We must avoid, at all costs, another case like that of Iraq. We cannot allow Iran to grow into a monster that we will one day have to fight.

Foreign companies and foreign governments must understand that they are subsidizing Iranian aggression. If they don't, they should heed the words of Secretary of State Christopher before the United Nations General Assembly on October 25, 1995, when he stated,

> "Every dollar that goes into the coffers of a state sponsor of terrorism makes its secret quest for weapons of mass destruction even more alarming. We must stand together to prevent Iran from acquiring such threatening capabilities."

No one could have said it better. I hope that our friends overseas understand this as well, but if they fail to do so, this legislation will serve as a reminder.