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Texas

Mr. Georges Blondel
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Mr. Chairman, Ladies and Gentlemen,

May I begin by saying that I very much appreciate the honour of being invited by your Association to speak at your annual luncheon meeting. I believe this is the first time that you have called upon someone who is not only foreign to the industry but also to your country to give his views on some of the outstanding questions regarding international oil to day.

I was delighted to accept the invitation by your Chairman, which I trust was been made with a particular view to my present duties in the Commission of the European Communities. You are probably all aware of the ideas implicit in the concept of an unification for Europe, which would not only enable the countries involved to benefit from the economies of scale of modern industrial society, but also make it possible to avoid the antagonisms of the past which have often led to painful and sterile conflicts.

It is encouraging to find that there is a growing awareness in your country of the contribution that the nine member countries of the European Community can make towards a solution of the problems we are all facing in the energy field.

Assuming that economic growth will continue its present trend, world energy requirements are very likely to be at twice their present level by 1985 and to have increased fourfold by the year 2000.

The share of oil in total energy consumption will continue to go up, from some 45% in 1970 to about 50% by 1985; in the year 2000 it is expected that the share of oil will vary between 40 and 50%, depending on the assumptions made regarding the development of nuclear energy.

The United States and the European Community will be the two largest oil consuming areas in the world representing 25% and 20% of the total. The share of imports in total US requirements will not be lower than 50% by 1985, notwithstanding the availability of substantial inland resources. The European Community will remain the largest single importer of crude oil in terms of volume, with a dependance on imports that will not be less than 80%.

These figures are sufficient to illustrate what is at stake in the oil sector for all consuming countries. The world of oil is in a state of rapid evolution and questions regarding the conditions of supply for a substantially bigger volume of oil are being raised in many quarters.

Concession agreements with producers are being renegotiated in the majority of producing countries. Although complete nationalization of oil resources is likely to remain rather an exception, various types of new agreements, referred to as participation or association agreements, will place the management decisions in the hands of the national companies in the producing countries. The task of the integrated foreign companies will gradually be reduced to that of operators of nationally controlled concessions.

The international companies will continue to control part of the resources, but the cost of this oil is bound to be much higher as a larger share of the profits will be retained by the producing countries. Another part of the oil produced will be disposed of by the national companies, which may either endeavour to build up their own outlets in consumer markets, or sell the oil to independent companies for refining and distribution.

In addition to the traditional exporting countries of South America, the Middle East and Africa, new areas of supply, where exploration efforts have led to the discovery of major fields in recent years, will make their appearance. The North Sea basin is one of these areas and in a not too distant future Europe will be able to count for at least 15% of its requirements on resources located on its doorstep and offering greater security of supply. Although a considerable investment effort will be required, the development of the fields will be justified by their closeness to markets.

In view of the change in underlying conditions, the cost of oil will go up significantly, and a higher level of oil prices seems to be inevitable in the years to come. However, I feel we should not necessarily conclude, as some people are inclined to do, that the price of oil is inevitably going to reach the cost level of alternative sources of energy which are developed. In the U. S. and Canada vast resources of non-conventional fuels, such as oil shales or coal for gasification, can be brought into production; but, in other parts of the world, resources, which could rapidly be developed as a replacement for oil, are not now available in large volume. Nuclear energy will undoubtedly provide the long-term solution to our problem of potential energy shortage, but apart from the fact that its contribution will be essentially in the production of electricity, many years will go by before it can contribute substantially to the supply of energy: according to the most optimistic estimates available, nuclear energy will not cover more than 15% of energy needs by 1985.

On the other hand I believe it is correct to say that even present-day oil reserves in the world are large, particularly in the Middle East, sufficient, in fact, to meet rapidly increasing needs. In the absence of concerted efforts to limit supplies, prices should continue to be influenced by competition amongst the producers, as in the past, only situations of artifically created shortage would warrant an exception to this basic principle.

If competitive conditions cannot be assured on the supply side, the danger of bilateral agreements between producer and consumer governments becomes a real one; alternatively a world wide organisation of the market might appear to be unavoidable. It would be difficult to predict who in the end would reap the greater benefit from it, the producer or the consumer.

The fact that the United States will have to rely more heavily on imported energy to make up for the deficit in domestic supply is a source of concern, and it is understandable that the federal authorities are trying to encourage the indigenous production of all sources of energy.

Europe and Japan have always been in a situation of very considerable dependence on imports, and they are less inclined to be apprehensive in this respect. They are more inclined to rely on the diversification of sources as the mean of safeguarding the security of their supplies.

Under present circumstances, all consuming countries will have to secure a volume of supplies sufficiently large to meet requirements in the longer run, including a sufficient margin of flexibility to overcome possible emergency situations.

Over the years to come, exploration efforts will have to be greatly expanded in comparison with the past. Producer countries will not contribute more than a small fraction of exploration effort, the majority of them will prefer to use their oil production revenue for the development of their own economies, rather than invest in industrial operations which would not provide a great deal of employment for their populations. The major part of the investment in exploration will therefore have to be made by the oil industry. Both financing out of retained earnings and from external sources will make it necessary for profit margins to be sufficiently high. Consumer prices will have to be such that the total cost of exploration activities can be recovered.

Experience in the United States has clearly shown that exploration diminishes when profit margins at the production level are insufficient. This, in turn, over the longer run leads to a deficit in supply sources. A similar development as regards world resources should be avoided, as it would be difficult to remedy and prices would start on an upward sprial with no end in sight.

In order to solve the intricate problems of access to energy resources and the supply of consumer markets, the steps to be taken by the public authorities and the industry will have to be carefully concerted.

As we have seen, the industry finds it increasingly difficult to plan its traditional role. Caught between the demands put forward by the producing countries and the obligations of the consumer markets, it cannot always find sufficient room for developing its activities. Without the necessary support from consuming governments, the industry may no longer be able to carry its full responsibilities. Governments and industry should co-ordinate ways and means in this respect.

In view of this situation of growing concern for all the consumer countries, the necessity to define an energy policy appears today clearly. In this respect many actions will be required. It is generally considered that the following headings should be considered with priority: co-operation among consumer countries, improved relations between producer and consumer countries, the development of new resources and the improvement of market conditions.

In view of the conditions which govern the world oil market today there is a definite need for all consuming countries to coordinate their efforts when trying to define the appropriate solutions. It is undeniable that actions in the energy policy field would be far more effective if a greater number of countries would take part in them. The increase in emergency stocks and the arrangements made for allocating available supplies in a situation of shortage, which for the time being apply only to the European countries, are good examples of actions that could usefully be extented to other regions. Further areas for coordination would seem to be an additional exploration effort for new resources, a more rational use of energy, and the development of new techniques both in the production and in the consumption field.

The solidarity that exists between consumer countries is evident in the regular meetings that take place in the Organization for Economic Cooperation and Development in Paris. There is no doubt that it could be further developed.

Member countries of the European Community would welcome a closer cooperation with the United States and possibly Japan, with a view to coordinating energy policies. One has still to explore possible areas of application.

As far as the producer countries are concerned, nobody would find any benefit in the longer run in establishing a preferential relationship with some producing area. Normal market forces should continue to determine developments at world level and the security of supply should not be put in jeopardy by depending too heavily on certain areas. On the other hand, oil is only one of the components of international trade and the creation of more favorable conditions for the international exchange of goods in general would have a far reaching stabilizing effect on the relations between consumer and producer countries.

The industrial countries should consider ways in which they can assist the developing coutries, including the oil producing states, in the development and gradual diversification of their economies. The Community's development policy should aim at establishing economic, social and cultural links with those countries by way of cooperation agreements.

The Third and probably most important problem over the longer term is the development of new resources of oil. There are vast areas of sedimentary basin in the world where exploration for oil has not even started. Parts of the so-called shelf bordering the earth's continents, parts of the deep sea and certain arctic regions are a few of the more likely areas for exploration in the years to come. Technical difficulties will have to be overcome, but in this domain progress over the last ten years has been very rapid.

Fiscal legislation in the United States provides for a number of incentives in favour of oil exploration. The European Community could follow the example of the United States with a view to fostering its own industry. The Community also intends to create the possibility of direct financial incentives for industrial projects which are of particular importance for the supply of oil to the Community, and would not be undertaken by industry, in view of the risk involved or the uncertain profitability. A proposal to this effect, put forward by tha Brussels Commission, envisages the setting-up of "common enterprises" or "Community projects" which would be open to all oil companies without discrimination. The characteristics of each project would be the sole criterion for determining the extent of the financial support.

Last but not least, in view of the economics of oil marketing, the industry should be enabled to improve the profitability of its investments.

For many years in the past, profit margins in the oil industry were higher than the average for other branches of industry. Higher profitability in oil is justified by the higher risk involved in oil exploration and overseas production. More recently profits have come down to levels which in certain countries in Europe are disconcertingly low. Taking account of the greater uncertainity involved in new investments in some of the producing countries, it is understandable that the industry hesitates to make new investments at a rate commensurate with the increase in demand. There are already the first signs of a tendency on behalf of the industry to withdraw from some of the least profitable markets.

The countries of the European Community are very much aware of the risks involved and the necessity to find an appropriate solution. Measures to control market conditions, such as imposing maximum price levels which tend to lower profit margins in the industry, should be avoided. The burden of excise taxes on oil products, both on motor fuels and on fuel oils, is very heavy in Europe, and an effort could be made to bring it down to more reasonable levels.

Measures of this kind however might not be sufficient to halt the phenomenon of price erosion which is implicit in a situation of sometimes disorderly competition. Quantitative limits of any kind are unknown in the European market and any short term surplus supplies is likely to find its way to that market. Will the industry itself be able to find some form of self-discipline or will the alternative of more far-reaching interventions be unavailable? There has been some improvement over the last few months, but it is probably too early to say that all has turned for the better.

A further problem to industry is to ensure the necessary equilibrium between supply and demand for each product and at any point in time, maintaining product specifications at the level required by consumers. There is today a deficit of refining capacity not only in this country, but also in Europe. Recent experience in the United States has shown, that a lowering of import barriers - in order to encourage imports of the quantities and qualities of products which are in short supply on the internal market - is not sufficient. Relatively small additional supplies of low sulfur crude oil and finished products - such as heavy fuel oil and light distillate - for which the traditional import restrictions were partly reduced, have been secured at very high and rather speculative prices.

There is no doubt that crude oil producers or refiners from other areas would have been able to meet additional United States demand, if they had been told sufficiently in advance and not been obliged to respond to last minute calls for supplies that had to be found on an emergency basis in other markets.

Europe is certainly in a position to increase its exports to the United States, but the increase in refinery capacities which this implies will of necessity have to be planned some time in advance. Whereas existing capacities would no doubt make it possible to face normal cyclinal fluctuations in demand - for which they have been laid out -, they are not sufficient to take care of new export movements at short notice. Governments - including the United States - should therefore define clearly the orientations of their import policies and indicate what limitations a product specifications they will impose with a view to their environment policy. Industry, on the other hand, should be aware of the necessity to program its supply conditions both in the short and the long term sufficiently in advance.

There certainly is a great deal of uncertainty about the future which would make it hazardous to take decisions which bear upon too long a period ahead, but it is equally important to avoid the return to a situation of extreme tension in the market, such as was apparent during the winter of 1971-1972, when consumers on both sides of the Atlantic came to feel the consequences.

I admit that my presentation of the state of the world oil market is fairly gloomy, and I should like to finish with some more friendly perspectives for the future.

Over the years to come the equilibrium between supply and demand for oil in the world will no doubt be precarious. The oil industry, however, has been able to adapt itself to new situations on many occasions in the past and it has often been stated that it could stand as an example of a branch of industry with considerable flexibility.

We should only recall how a number of emergency situations, such as the Iranian situation in 54/55, and two Suez crises, have been met without major difficulties for the consumer. Prices have gone up over relatively short periods, but there has not been an actual shortage of availabilities and the return to normal conditions has always been very rapid.

The developments which have taken place more recently and led to the so-called Teheran and Tripoli agreements, followed by the agreements on participation, have had a far-reaching effect on the bargaining positions of both countries and the oil industry. If, however, the basic entente which underlies the agreements continues to prevail with both parties, the implication is certainly not that we will have a situation of shortage.

A fair deal of trust in the future seems to be justified. I feel that the oil industry should again reaffirm our conviction that it has great powers of flexibility and efficiency.