

The 1970s Arab-OPEC Oil Embargo and Latin America

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In October 1973 in retaliation for U.S. support of Israel against Egyptian and Syrian forces in the Yom Kippur War, the Arab members of OPEC, plus Syria, Tunisia and Egypt, embargoed oil sales and shipments to the United States and ultimately to other countries seen to be assisting Israel. Neither Venezuela nor Ecuador, the two Latin American members of OPEC, joined in the embargo, which lasted until mid-1974. The embargo and the OPEC driven price increases dramatically altered the world balance of economic power in the 1970s, impacting not only the major producing nations but also the less developed nations, especially those which were dependent on imported energy. The crisis also intensified the debate between less developed countries and the major western industrial powers. Perhaps for the first time the former had found not only such strong supportive voices as Venezuelan President Carlos Andrés Pérez but also the economic power to make those voices heard in the corridors of political power in the industrial nations. The increases in the price of oil in 1973-74 were sudden and dramatic. Between 1960 and 1971 international oil prices, posted by the oil companies, were held stable at \$1.80 a barrel. By mid 1973 this had risen to a negotiated \$3.29 a barrel. But with the onset of the war OPEC unilaterally raised the price of oil to \$5.12 a barrel; Iran auctioned some oil to the highest bidder for as much as \$17 a barrel, and some OPEC members raised their prices again in January 1974 to \$11.65 a barrel.¹ Thereafter prices rose only slowly, reaching \$12.70 in 1978. In December 1976 Saudi Arabia split the cartel by refusing to raise its price more than 5%, although it did so while warning that they expected more acceptable Western policies in the Middle East specifically and toward the developing world more generally.²

Much of the literature on the oil shock has focused on the Middle East, United States policy, relations among OPEC members and the relationship among the western industrial powers in responding to the crisis. With the possible exception of Venezuela, in part because of its status as a founding member of OPEC and an aggressive advocate of higher oil prices, little attention has been devoted to an understanding of the ways in which the energy crisis impacted Latin America as a region. This paper examines the impact on and response of select Latin American countries to the oil embargo in the period 1973 through 1978, prior to the onset of the second oil shock brought about by the Iranian Revolution in 1979. It was impractical to attempt a review of the experience of every country in the region, with the result that the paper focuses on two categories of countries: the main oil producing and exporting countries, and the major countries which relied heavily on imported oil for energy needs.

The impact on Latin America of the first energy shock in the 1970s needs to be understood in a larger context of evolving national energy policies, the role of the state and private sectors, especially foreign capital, in exploration and production, and overall economic development strategies. In the decade prior to the 1973 crisis the import-substitution industrialization model advocated by Argentinean economist Raul Prebisch and the Economic Commission for Latin America (CEPAL) had prevailed, but increasingly Latin American planners had begun to question the effectiveness of the approach and move toward a focus on export driven models. Throughout the region there was increased political sensitivity to economic dependency on Western developed countries, in particular the United States, and an intensified desire to control natural resource development for the benefit of the producing nation. Regardless of the overall development approach, what increasingly dominated natural resource policies in the region from the late 1930s were nationalism and state control. All of the producing countries had state energy companies. Mexico had nationalized its oil industry in the late 1930s. Venezuela did so in 1976. Bolivia expropriated the subsidiary of Standard Oil in 1937. It was rare to find economic liberalism in the region in the early 1970s, just as a significant number of major

countries were characterized by military and/or authoritarian civilian governments, in particular the three major countries of the Southern Cone, Argentina, Brazil and Chile. For the most part, nationalism and state control aside, the Latin American region, with few exceptions, continued to depend on foreign capital investment and technology to develop its energy resources. The consequence of this reliance on foreign capital and technology was to temper nationalism to some extent and in the course of the 1970s and 1980s to move a number of countries toward more neo-liberal economic regimes. Chile was the leading example of this shift in the 1970s. After September 1973 and the coup against Salvador Allende the authoritarian government of General Augusto Pinochet pursued aggressive neo-liberal economic policies. The most politically democratic of the Latin American oil producing countries, Colombia, moved toward trade liberalization and export promotion but it did so slowly while at the same time strengthening the controls of the state oil company, Ecopetrol, as well as nationalizing foreign banks.³

At the time of the price increases and embargo two-thirds of Latin American countries had an energy deficit and had to import some form of energy; oil represented 65% of that energy import. Only Mexico, Chile and Colombia were considered to have a fairly diversified pattern of energy supply, but even in those countries oil was the dominant source of energy. Argentina for instance, relied on oil for 89% of its energy in 1969, Mexico 70%, Chile 57%, and Brazil 45%.⁴ In spite of that dependency Latin America as a region, primarily because of Venezuela, was second only to the Middle East as a supplier of oil to other areas of the world.⁵ The embargo and the resulting oil price spike was both a blessing and potential curse for Latin American oil exporting countries, two of which, Venezuela and Ecuador, were members of OPEC.⁶ Much of the region, however, depended on imported energy, and the sudden and sharp increases in oil prices significantly impacted balance of payments challenges. For most countries it increased external debts and served as prologue to the debt crises of the last decade of the 1980s. For the region as a whole, again primarily because of Venezuela, Latin American had a balance of payments surplus in the order of \$9 billion by early 1974, but that general figure masked the huge deficits which

major importing countries experienced. Even in those countries which reaped the windfall profits from oil exports, controlling inflation proved to be a monumental task. A report prepared in April 1974 by the U.S. Agency for International Development identified the countries which would be most seriously impacted by the energy crisis. In Latin America the list included Chile, Costa Rica, El Salvador, Honduras and Uruguay. The report noted that Chile (along with India and Pakistan outside the Western Hemisphere) would face one of the largest financing difficulties and would need a debt restructuring program in the course of the year. The Central American countries, none of which produced its own oil and were especially hard hit by the rapid price increases, were fortunate to receive financial assistance from Venezuela through the IDB. The only major energy deficit country in Latin America which seemed able to weather the storm of the steep increase in the price of its imported oil was Brazil since it had strong foreign exchange reserves and access to private capital markets.⁷

It was indicative of the growing concern among Latin American countries about energy resources that prior to the 1973-74 energy crisis they sought some degree of collaboration. Only a few weeks after the price increase in late 1973 twenty-one countries in the region signed the Lima Agreement establishing OLADE, the Latin American Energy Organization. The formation of OLADE reflected regional concern over the fact that in spite of major production and export of oil from Venezuela and lesser levels from Bolivia and Ecuador, 45% of Latin America's oil requirements had to be met by imports, and eleven countries had to import over 95% of their hydrocarbon requirements. In 1974, Latin America as an economic entity paid 23% of its export revenues just to cover the cost of oil imports.⁸ The sharp price increases in 1973-74 clearly posed a significant challenge for countries seeking to modernize infrastructure, encourage industrialization, and address challenges of economic disparity. During and in the immediate aftermath of the OPEC actions it became quickly apparent that the sharp increase in world oil prices was hampering development and economic growth. The Economic Commission for Latin America reported at the end of 1975 that except for the exporting countries

regional production had only grown 4% in 1975 in contrast to 7.2% in 1973 and that per capita growth of product was less than 1% in 24 countries in the region. CEPAL observed that major South American countries- Argentina, Brazil, Peru and Chile – were experiencing inflation levels ranging from 30% in Brazil to 300% in Argentina and Chile.⁹

The problems identified by CEPAL in late 1975 persisted through the decade. Juan de Onís reported in a feature article in the *New York Times* in February 1978 that inflation and foreign debt constituted the dual “Latin curse.” High import costs combined with a soft market for Latin American exports along with high levels of foreign borrowing to meet project requirements hit the region very hard in the course of the decade. Onís noted that Peru, for instance, had exhausted its reserves of foreign currencies and was seeking ways to refinance its foreign debt in spite of the more than \$210 million which had been lent to Peru by U.S. banks in 1976. He observed that “the fight against inflation in Argentina, Chile, Brazil, Peru and other countries has involved wage controls and suspension of the right to strike. Labor has lost political influence under the military regimes in power in most Latin American countries. Balanced budgets are back in style under the orthodox anti-inflation policies being applied, so there has been a reduction of public spending and easy government credit. This contributes further to austerity, and has led to recession in some countries.”¹⁰

The economic problems which Onís identified toward the end of the first oil shock deteriorated further in the course of the next ten years after the Iranian revolution and the continued massive foreign borrowing that contributed to the “lost decade” of the 1980s in Latin America. Nonetheless, the first oil shock impacted countries in the region in different ways. The following sections examine first the Latin American oil producing countries, some of which were net exporters of oil, including the two OPEC members Venezuela and Ecuador, and then turns to a consideration of the net energy importers.

The OPEC Members: Venezuela and Ecuador:

In 1960 Venezuela took the lead in the establishment of OPEC. In that same year the Venezuelan government, led by the visionary energy minister Juan Pablo Pérez Alfonso, ended the granting of oil concessions to foreign companies (existing ones were to expire in 1983) and set up a state oil company, CVP (Corporación Venezolana del Petróleo). By decree and against strong private sector opposition in 1964 the administration provided that CVP would take 33% of the domestic market by 1970, and Congress followed with legislation giving CVP 100% of the domestic market by 1971.¹¹ In spite of this evident move toward a more nationalistic policy, by 1973 oil exploration and production was still dominated by major foreign companies, in particular Creole, Shell, Gulf, Texaco, Mobil and Exxon. Exxon and Shell subsidiaries alone accounted for approximately 80% of the country's production.¹² In 1973 its rich oil fields were producing 3.3 million b/d, its significance in the region reflected in the fact that all of the other Latin American countries combined were only producing 1.8 million b/d. By 1973 and the implementation of the Arab-OPEC embargo Venezuela had become a major international player as one of the world's leading exporters of crude oil.

The 1973-74 oil crisis coincided with a shift in Venezuelan politics toward a more nationalistic stance on the oil industry. During the presidency of Rafael Caldera (1969-73) there was little initial support for nationalization or for OPEC, including from President Caldera, but that changed by the end of his administration for a variety of reasons. One factor was the impact of the Libyan decision in 1970 to obtain a major tax increase from the oil producers. A second factor was Caldera's revenue problems, which necessitated legislation increasing the oil profits tax from 52% to 60%. A third consideration by the time of the 1973 election, which preceded the embargo, was a widely held concern that the foreign oil companies, given both the impending end of their concessions in 1983 and the lack of appeal of service contracts, were not investing in new exploration, development and infrastructure.¹³ The result was that by the time of the 1973 election both the outgoing Caldera administration and Acción Democrática President-elect Carlos Andrés Pérez were supportive of nationalizing the oil industry. With

the onset of the Arab-OPEC embargo in late 1973 the outgoing Caldera administration raised the price for Venezuelan oil by 56%, an action that would clearly have a major impact on United States fuel oil prices, particularly in East Coast states.¹⁴ What Venezuela did not do was follow the Arab nations' embargo of oil shipments to pro-Israel countries. Both the outgoing Caldera administration and the incoming government of Carlos Andrés Pérez assured the international market that the country would honour its commitments, although they would not increase production even if the industry had the technical capacity to do so. In the course of the crisis EXXON's global production declined an estimated 20%, but because of the Venezuelan commitment EXXON's 48% share in Venezuelan production continued to flow to the United States without interruption.¹⁵

Once in office the Pérez administration (1974-79) pursued an economic development policy of rapid modernization, with policy fueled by the dramatic increase in the price of oil after 1973. The country's oil revenues tripled in the short term. In June 1974 with the end of the Arab-OPEC embargo Venezuela announced its intention to raise oil prices and taxes on the oil companies, thus declining to comply with an OPEC decision to freeze the posted price of crude oil at its present level. The goal was to cut into oil company profits and erase a difference between prices for Venezuelan and Middle East light crude exported to the eastern United States. The price increase would raise Venezuela's revenue to over \$9 a barrel.¹⁶ The government viewed the oil industry as a tool for development. Under the slogan "la Gran Venezuela" the administration nationalized the iron industry, invested in large scale industrial projects in the aluminum industry, in hydroelectricity and also invested in expanded social welfare programs. In January 1976 the administration nationalized the oil industry and established PDVSA, *Petróleos de Venezuela*.

The Pérez government moved quickly to employ the country's oil wealth to advance its regional leadership, setting a trend that would later characterize the presidency of Hugo Chavez. Venezuela

extended loans to the World Bank and the Inter-American Development Bank as well as to regional development banks and in late 1974 even provided funding for Central American oil imports, support for development programs and credits to Central American coffee producers to withhold coffee from the market for two years until coffee prices improved.¹⁷ In concert with Mexico in 1975 Venezuela led in the establishment of SELA, the Latin American Economic System, which included twenty-five Latin American states, including Cuba. Venezuela also joined the Andean Pact and on the whole took a more engaged role in supporting the economies of developing nations. At the same time Venezuela's new wealth did not trickle down in any significant way to the majority of the country's people. It was estimated that the lowest 1/5th of the Venezuelan population received only 3% of the national income in spite of the fact that Venezuela had one of the highest per capita incomes in Latin America in the mid-1970s (approximately \$2000). In addition Venezuelan government policies did little to alleviate the country's chronic unemployment. The oil price spike and increased revenues in the mid-1970s (Venezuela's revenues in 1974 increased by more than \$7 billion) exacerbated the condition of the poor and working class as the country fought to deal with the overheated economy and sharp increases in consumer prices. Illustrative of the price increase for basic staples in Venezuela the price of black beans increased from 44 cents a kilo in 1973 to 99 cents by May 1974.¹⁸

The Richard Nixon administration paid comparatively little attention to Venezuela, or to the rest of Latin America except Chile, during the first phase of the energy crisis (1973-74), understandably preoccupied as it was with the Yom Kippur war in the Middle East and the Arab-OPEC embargo and oil price increases. The February 1974 Washington Energy Conference was attended by 13 countries; none from Latin America. The crisis did, nonetheless, reinforce the need to seek secure sources of supply outside the Middle East. A 1975 Department of State memorandum, "A Contingent Energy Strategy," stressed the need for the United States to reduce its energy dependence on the Persian Gulf and to maximize imports from Mexico, Venezuela, and Canada.¹⁹ The U.S. Congress late in the Nixon

administration also responded to the Arab-OPEC embargo with threatened retaliation against OPEC members. Section 301 of the United States Trade Bill passed in 1974 authorized the President “to take all appropriate action, including retaliation, to obtain the removal of any act, policy, or practice of a foreign government that violates an international trade agreement or is unjustified, unreasonable, or discriminatory, and that burdens or restricts U.S. commerce.” Neither Venezuela nor Ecuador adhered to the embargo provisions of the Arab members of OPEC, but the 1974 U.S. legislation provided no recognition of that fact and in its application excluded both countries from the U.S. General System of Preferences for their imports.²⁰

The relative lack of attention to Latin America in the Nixon and the brief Gerald Ford Presidency changed somewhat with the election of Jimmy Carter in 1976. Carter and Carlos Andrés Pérez appear to have had positive working relations on energy issues yet they had different, and to a considerable extent, irreconcilable goals. The Carter administration wanted more Venezuelan leadership within OPEC on price controls, although it also wanted security of supply. Pérez sought US financial and technical assistance with the expensive development of the Orinoco tar belt, in which Japan had expressed some interest, as well as with OLADE, which Venezuela led. He also sought US assurances of a long term market for Venezuelan residual fuel oil, which represented approximately 40% of U.S. imports in 1978. For the Carter administration the critical goal was to contain oil prices, with the result that the administration was only interested in supply agreements if the impact was to lower prices. As far as development of the Orinoco tar belt was concerned the administration stressed that investment would have to come from the private sector. In late November Secretary of State Cyrus Vance met with Pérez in Caracas to press the Venezuelan government on the need for leadership on an oil price freeze.²¹

Consistent with the developmentalist and nationalistic approach which his administration pursued, Pérez consistently stressed that there needed to be a more equitable relationship between

developed and developing nations. In his address to the U.N. General Assembly in November 1976 he stressed that oil price increases resulted from the decision to “dignify the terms of trade to confer true value to the raw materials and other primary commodities of the nations of the third world.” He echoed those sentiments in New York in July 1977 when he indicated that he anticipated oil prices would continue to rise and that prices would be closely linked to progress in the dialogue between developed and underdeveloped nations over a new distribution of world resources.²²

Ecuador:

More nationalistic policies in Ecuador also preceded the 1973 crisis. In 1972 a military government led by Rodriguez Lara took power and pursued economically nationalistic policies in the energy sector. The previous civilian administration had already established a state energy company, CEPE (*Corporación Estatal Petrolera Ecuatoriana*) and under the direction of the new Minister of Natural Resources Captain Gustavo Jarrin, the military government sought to improve the management of petroleum resources and enhance the financial benefits of oil production for the state. In 1972 the Gulf-Texaco consortium which operated the Oriente fields began large scale export of oil. In June that year the government by decree specified that oil concessions granted prior to 1971 would have to be renegotiated. The agreement reached with the companies also required the companies to increase both investment and production levels and stipulated that 25% of production would be controlled by CEPE. Gradually CEPE took control of the domestic market during the years the military government was in power (1972-79). In contrast to Venezuela, however, the Ecuador government shied away from nationalization. In 1974 the government did not pursue plans for a 51% share in the consortium. On the issue of nationalization Oil Minister Luis Salazar argued, rightly, that CEPE lacked the capital and the technology to run the consortium’s operations. Ecuador’s position in the context of the embargo was

also further complicated by the presence of an Israeli military mission in 1974, in addition to which in the following year Ecuador voted against the UN Zionist resolution.²³

In 1973 Ecuador joined OPEC, a decision that was far more controversial in Ecuador than it had been in Venezuela, primarily because of concerns over the impact membership would have on relations with the United States. Concerns aside, over the next few years as the world oil markets became saturated and prices declined, Ecuador faced similar problems to other producing countries where production levels were controlled more by the companies operating the concessions than by the state. The result was that the government in 1975 made some tax concessions to the consortium but ordered the companies to maintain a 250,000 b/d level of production, from which CEPE would take its 25%. Still, the consortium did not increase its investments or production, with the result that in the first half of 1975 the value of exports dropped from \$430 million to \$213 million, contributing to a larger budget deficit, growing balance of payments deficit and an upsurge in popular unrest.²⁴

As elsewhere inflation was a serious problem for most Ecuadorans. The price of rice doubled between 1972 and 1974 as did the price of a loaf of bread. Milk rose from 12 to 20 cents a quart. The price of sugar increased 40% in the same period.²⁵ Given a high level of dissatisfaction with the Lara government he was pressured to resign by the three military service chiefs in early 1976 to be replaced by another military regime under Admiral Ernesto Poveda Burbano, whose government shifted away from the previous nationalistic policies toward the neo-liberal policies being pursued in Chile under Pinochet.

The Other Oil Producing and Exporting Countries

Mexico:

Mexico was in a transitional period economically when the oil crisis hit in 1973. Although an important oil producer since the 1910s, by the 1950s production was absorbed by domestic demand. On the eve of the oil crisis Mexico was producing approximately 180 million b/d for the domestic market, but major discoveries in 1974 in Veracruz, Chiapas, Tabasco and Baja California changed its position significantly, with the result that the impact of the oil shock on Mexico was less than on Brazil, for instance. In contrast to Brazil, which in 1974 had to pay over 34% of its export earnings to cover the increased cost of imported oil, Mexico paid out only 2.5%.²⁶ In 1974 Mexico produced 238 million barrels and exported only 6 million. By 1979 it produced 590 million barrels and exported 303 million.²⁷

Mexico's strengthened energy and economic situation derived from the new oil discoveries did not save the country from economic challenges which were largely independent of the 1973-74 energy crisis. During the Luis Echevarría presidency (1970-76) high levels of foreign borrowing and low levels of direct foreign investment nonetheless placed Mexico in a serious financial situation by the end of the 1970s. Indeed, the domestic spending and foreign borrowing policies pursued under President Echevarría's ambitious infrastructure projects and social programs had at least as significant an impact on the Mexican economy as the international energy crisis. Under Echevarría foreign borrowing increased from only \$0.8 billion in 1972 to \$3.1 billion in 1974 and \$4.9 billion in 1975. Mexican non-energy exports also suffered in the context of the energy crisis because of dependency on the U.S. market, which declined sharply in the context of the energy crisis. The country's economic growth rate was only 1.4% of GNP in 1976, in contrast to Brazil, which had an average annual growth rate of 6.9% of GNP between 1974 and 1980, and Mexico faced added challenges of labour unrest and land seizures in mid-decade.

In 1977 the Echevarría government gave way to that of José López Portillo (1977-83). During his administration the situation improved somewhat as the result of lowering the budgetary deficit and re-

introducing export subsidies, at the same time that the country enjoyed significantly increased revenues from oil exports. Oil exports in 1977 added \$1 billion to the country's foreign exchange earnings and another \$1.8 billion in 1978. Foreign borrowing, however, did not abate, resulting in a gross external debt of more than \$32 billion by the end of 1978. A decline of agricultural exports in the 1970s further exacerbated Mexico's economic situation and even after the peso devaluation in 1976 the peso was still overvalued. López Portillo did shift PEMEX development strategy in a more aggressive direction, in part to generate more revenue to address Mexico's pressing social problems.²⁸

U.S.-Mexican Energy Relations:

The 1970s energy crisis intensified the need for the United States to build effective working relationships on energy issues with key Latin American countries. For the Carter administration this meant a particular focus on Mexico as well as Venezuela. Carter personally placed high priority on good relations with Mexico and worked closely with the López Portillo administration on oil and natural gas issues. To that end in late 1978 Carter's Assistant for National Security Affairs Zbigniew Brzezinski requested Energy Secretary James Schlesinger to prepare an energy strategy for relations with Mexico.²⁹ The development of significant new resources in Mexico in 1977 made this initiative especially timely, since the expansion of Mexican production was viewed as an important contribution to world supply, which could in turn have a restraining impact on prices. The U.S. National Security Council concluded that even a conservative estimate of Mexico's proven and probable oil reserves of 40 billion barrels placed Mexico behind only the USSR, Iran and Saudi Arabia. It was projected that Mexico would within a decade "be at the forefront of the world's oil nations, placing it on a par with Iran." U.S. officials also perceived opportunities in the expansion of production and import of Mexican natural gas into the United States, possibly replacing imported oil from the Middle East. Such a development would also benefit the Mexican economy since it would direct an estimated \$5-\$6 billion in US payments for energy

imports to Mexico rather than the Middle East. From a U.S. perspective Mexico had the added advantage of not being a member of OPEC and not inclined to become a member, although it did follow OPEC leadership on prices.³⁰

In his September 1979 meeting with Carter López Portillo predicted that the world was living at the end of the petroleum area and that objectives of energy policy should be to introduce the use of other resources and in the meantime to rationalize use of petroleum. He was particularly concerned, he suggested, with the plight of developing countries which were dependent on imported energy, citing the example of Costa Rica which used almost 30% of its GNP to purchase oil. Echoing the sentiments of Carlos Andrés Pérez in Venezuela, López Portillo argued that economic hardship weakened democracy and that the oil exporting countries needed to recognize that they had a responsibility to assist such countries.³¹

Bolivia:

By the time of the Arab-OPEC embargo Bolivia had a well established record of nationalism in the oil sector having expropriated Standard Oil's subsidiary in 1937, establishing a state oil company, YPFB, and nationalizing Gulf Oil in October 1969. In contrast to the other Latin American oil producing countries, however, and in spite of the strong nationalist tradition, the Bolivian government during the oil price increases did not pursue any vigorous effort to increase its "take" from the increased revenues or develop a strategy to recapitalize YPFB. Nor did it attempt to redistribute the profits beyond the producing province of Santa Cruz, already the wealthiest area of the country. The lack of effective policies was extremely short-sighted, since the country lost a major opportunity for broader social and economic development. Bolivia continued to attract foreign investment. The natural gas pipeline to Argentina opened the year before the OPEC embargo, and revenue from the 19% profits tax shot up from \$5.49 million in 1972 to \$51.39 million in 1974. During the same period royalties which accrued to

Santa Cruz increased from \$3.88 million to \$21.0 million, all of this in spite of the fact that oil production in the country reached a peak in 1973 and then declined for the rest of the decade. By 1979 Bolivia was producing only 32,000 b/d.³²

Colombia:

Colombia had a far more balanced and diversified economy than neighbouring Venezuela at the onset of the 1973 energy crisis. It depended on oil for 44% of its energy needs by 1969,³³ similar to the Brazilian level, but in contrast to Brazil Colombian production was adequate to meet domestic demand. There had been considerable foreign investment in the Colombian oil sector under favourable investment terms in the 1960s with the result that until 1973 Colombia was a net exporter. In 1970 it produced 226,000 barrels a day. In 1973 the level of production was down to 183,000 b/d and to 160,000 in 1974. One result of the decline in production in the midst of the energy crisis was that Ecopetrol had to import oil and gasoline to meet domestic demand at a time of increased world prices, and it continued to import through 1978. Colombian policy under the Alfonso López Michelsen Liberal government was designed to stimulate investment in energy resources, not only in oil and natural gas but also in coal and hydroelectricity, but the policies were largely ineffective. In an effort to strengthen the control of Ecopetrol the government issued two decrees in 1974 and 1975 stipulating that except for existing contracts only the state company Ecopetrol could explore for and exploit oil either on its own or under an association contract with a private firm. This move reflected the more nationalistic trend in the region on energy policy in the 1970s occasioned by the 1973 energy crisis, but it was clearly misguided since it was a significant impediment to badly needed foreign investment. The one new major discovery at Chuchupa in 1973 did not significantly improve the energy situation in the short term in large part because the tightening of the terms of the Association Contract to increase the state take from production made the oil sector less attractive to the foreign companies. One clear result was the

decline in exploration and production until well into the 1980s. As in the case of Brazil, however, the impact of the energy crisis on Colombia was buffered somewhat by the favourable world market for coffee by the mid-1970s. As a result Colombia was able to accumulate nearly \$2 billion in reserves between 1975 and 1978, thus reducing its external debt ratio from 13% to 4%.³⁴ Consistent with trends throughout the region Colombia continued to be plagued with inflation, public discontent and labour disturbances during the period 1974-78, capped by a short general strike in 1977 which shook the López administration. Inflation ran at 28% in 1974, declined slightly to 18% in 1975 only to rise again in 1976 to 26%.³⁵

The major importing nations: Brazil:

Brazil was controlled by military governments from 1964, when the military came to power in a coup against President Goulart, until 1985. The government of General Emilio Garrastazu Medici (1969-74) was particularly repressive, but like its successor under General Ernesto Geisel (1974-79) there was a focus on development, with major investments in infrastructure – highways, telecommunications, hydroelectric dams, mineral extraction, and atomic energy development. The Brazil-West Germany collaboration on nuclear power development proved to be a source of conflict with the Carter administration. The administration also initiated a longer term ethanol development to reduce the reliance on hydro-carbon resources.³⁶ Brazil had impressive economic growth rates in the late 1960s and early 1970s prior to the oil crisis, with average growth rates of 10% of GDP. Between 1969 and 1973 there was an increasing focus on export promotion, and there was strong performance in the export of manufactured and semi-processed goods. Economic growth was particularly impressive in the 1967-74 years, with a 60% increase in per capita income, a 130% increase in manufacturing output and a 350% increase in the value of exports.³⁷ Imports, however, were growing at an even more rapid rate, with the result that the impact of the 1973-73 oil crisis was especially sharp.³⁸ The government's National

Development Plan called for large investments in pulp and paper, petrochemicals, fertilizer, steel and nonferrous metals, with a goal of reaching a high level of self-sufficiency by 1979.³⁹ As well, in an effort to promote domestic oil exploration and development the military governments opened Brazilian oil exploration to foreign firms for the first time since the 1950s and pursued a development policy which combined export expansion with import substitution.

The oil crisis of 1973-74 threatened to stall this impressive growth. An increase in the price of imported oil could have had a particularly severe impact on Brazil, since the country depended on oil for approximately 45% of its entire energy requirements, and 80% of its oil requirements were met by imports. Analysts at the time estimated that Brazil would have the largest oil deficit of all Latin American countries, approximately 200 million barrels. Given the increased cost of imported oil, 76% of which came from the Middle East and Asia and 15% from Africa, Brazil had little choice except to increase domestic exploration and production. The cost of oil imports shot up from \$469.4 million in 1972 to \$2.89 billion in 1974 and \$4.06 billion in 1977.⁴⁰ In 1974 Brazil had to pay 34.5% of its export revenues just to cover the cost of imported oil.⁴¹ The country's resource gap increased dramatically in the context and as a result of the oil embargo and price increases, from approximately \$1 billion in 1972 to \$6.3 billion in 1974. \$2.4 billion of that increase was attributed to the increased cost of fuel and \$3.1 billion to a deterioration in the terms of trade.⁴²

A World Bank report in mid-1974 recommended increased emphasis on oil exploration and the involvement of foreign oil companies to work with Petrobras. Petrobras had originally been established to refine imported oil, but that role underwent significant evolution in the aftermath of the oil crisis. Although Brazil had a high level of foreign exchange reserves when the oil crisis hit in late 1973,⁴³ in order to maintain its development goals the Geisel government chose to borrow heavily to see it through the oil crisis, with the result that the country ran up a massive current account deficit and its

debt service ratio increased from 43% to 68% between 1973 and 1978.⁴⁴ The country was nonetheless able to maintain reasonably positive economic growth in the aftermath of the oil crisis, with GNP growing in 1976 by 8.7% and in 1977 by 4.5%. Brazil, like Colombia, benefitted in the mid-1970s from strong world prices for coffee, and like Mexico Brazil also benefitted from the relatively high export share of manufactured goods, at least in 1974 when demand was still reasonably strong.⁴⁵

An internal World Bank memorandum on Brazil reported that three years after the energy crisis Brazil was still struggling with the challenge of adjusting to the new world economic realities. As in most of the region inflation posed a serious problem. In each of 1974 and 1975 prices had risen approximately 28% and 1976 prices were 41% above the average level in 1975. Financial measures introduced in 1974 did slow inflation somewhat, and industrial production also declined along with the demand for consumer durables. The Geisel administration also introduced higher import duties to improve the balance of payments problem.⁴⁶ Brazil weathered the oil crisis storm as well as any Latin American country, but even in the case of the economic giant of the region it was not until 1977 that for the first time since the energy crisis Brazil's merchandise account for balance of payments registered a small surplus.

Argentina, Chile and Uruguay:

In 1969 Argentina depended on oil for 89% of its energy needs, Chile for 57%. As one of the most diversified and developed economies in Latin America Argentina had the highest per capita energy use in the region, yet its sources of energy lacked diversity. The country derived only 1% of its energy requirements from hydroelectricity and 3% from coal. By contrast Chile derived 15% of its energy supply from hydroelectricity and 16% from coal. Uruguay had no oil production and was significantly less developed than neighbouring Argentina and Brazil. All three countries on the eve of the energy crisis had a dependence on imported energy, although much less so than Brazil. In 1971 the net

imported energy dependence of Argentina was 2.61 million tons oil equivalent, Chile 3.85 million tons and Uruguay only 1.68.⁴⁷ Argentina had two large producing oil fields, the oldest at Comodoro Rivadavia and a second, Puesto Hernandez, in Neuquén province. By the late 1970s the country was producing slightly less than 500,000 barrels of crude oil a day. Juan Peron's brief return to power (October 1973-July 1974) resulted in an expansion of the state oil company YPF, but the oil shock added \$470 million in oil import costs, with the result that the country experienced considerable inflation during the energy crisis, significant decline in its foreign exchange reserves, as well as in exports. The government which took office in March 1976 sought to stimulate exports by reducing export taxes on traditional primary exports. It also pursued deflationary monetary policies, increased interest rates and introduced wage controls. The policies made only a minor impact on inflation, and economic growth was very weak through the decade, averaging only 1.2% per annum between 1973 and 1979.⁴⁸

Chile's situation underwent perhaps the most significant policy shift in the region since the military coup by General Augusto Pinochet in September 1973 preceded by only a few months the onset of the Arab-OPEC inspired energy crisis. The Allende government had pursued highly nationalistic and inward-looking economic policies. The military government which followed the coup shifted to export oriented economic policies, privatization, market liberalization, abolishing price controls and raising interest rates. At the end of the Allende government inflation had reached as high as 500% and it was still as high as 341% in 1975. The Pinochet government did require external financing but it nonetheless made progress in manufacturing exports and in reducing the deficit, although the new policies hit the unemployed particularly hard. Unemployment in the Santiago area at the end of December 1975 was at 14% and a year later it was still 10%.⁴⁹

Uruguay, on the other hand, was considerably less industrialized and urbanized and was consuming only 2.11 million tons of energy in oil equivalent at the time of the crisis.⁵⁰ The country's

comparatively low level of energy requirements did not spare it from financial challenges. As with many Latin American countries Uruguay relied primarily on foreign borrowing to finance its resource gap, with the result that the country's external debt increased from \$369 million at the end of 1973 to approximately \$866 million by the end of 1978. Uruguay was also impacted in the 1970s by a decline in foreign demand for wool as well as the slump in beef prices for much of the period 1974-78 resulting from European Common market restrictions on beef imports.⁵¹ At the same time the military government which took power in 1973 engaged in considerable liberalization of the economy, shifting resources from the public to the private sector, reducing the budget deficit, and engaging in export promoted economic policy, which contributed to a modest acceleration of economic growth, 3.9% of GNP in 1974 and 2.5% in 1975. The military government concentrated in the export sector on the promotion of non-traditional exports, that is industrial goods which were produced from Uruguayan raw materials using low wage, low skilled labour. Policies introduced in July 1974 ended domestic price controls, reduced both tariffs and import restrictions, eliminated existing minimum foreign financing requirements for imports, and liberalized foreign capital movement.⁵²

Conclusions:

This brief review of the impact of the first oil shock on selected countries in Latin America underlines both the diversity and the areas of commonality of experience. Not surprisingly, a major oil producing and exporting country such as Venezuela gained economically as well as in terms of regional political and diplomatic power through the calculated use of its dramatically increased revenues to support less developed countries in the region. The awareness on the part of United States officials that at last something had to be done to reduce reliance on Persian Gulf oil imports further enhanced the economic and strategic importance of Venezuela and Mexico. Yet, even Venezuela and then Mexico with its expanded oil production in the later 1970s were confronted with the challenges of inflation,

social and economic disparity and, at least in the case of Mexico, ill-advised and massive over borrowing in foreign capital markets. That major increase in foreign indebtedness could not be attributed in any direct way to the oil shock of 1973-74 and yet it was the prevailing characteristic of the region by the 1980s, by which time the western world had experience the second oil shock following the Iranian revolution. The experience of countries such as Uruguay, which suffered economically from weak markets in both wool and beef reinforced the fact that the oil shock was not solely responsible for the economic woes of the region. The energy deficit countries which most effectively weathered the storm of the oil shock were countries such as Brazil which had substantial foreign reserves and which began in the course of the crisis to pursue in an aggressive way alternative energy development. A common feature throughout the region was a continued focus on state enterprise as the vehicle for resource development, although degrees of commitment varied from Venezuela's nationalization of foreign companies in 1976 to Brazil's expansion of the role played by Petrobras in the oil sector. Other countries moved with varying degrees of enthusiasm and success toward a greater degree of market liberalization and openness to foreign investment, the most dramatic example that of Chile, but the Chilean shift had virtually nothing to do with the energy shock. Perhaps above all the oil shock demonstrated not so much the dependence of less developed countries on the developed industrial countries but the growing interdependence of the world's economies.

Endnotes:

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- ² "Two Decades of OPEC Price Moves," *New York Times*, June 29, 1979, p. D4. *New York Times* (December 17, 1978), p. E2.
- ³ James Petras and Morris Morley, "The Rise and Fall of Regional Economic Nationalism in the Andean Countries, 1969-1977," *Social and Economic Studies*, 27, no. 2 (June 1978), 159-166.
- ⁴ Bernardo Grossling, *Latin America's Petroleum Prospects in the Energy Crisis* (Washington, D.C.: Geological Survey Bulletin, 1975), pp. 1-2.
- ⁵ Grossling, *Latin America's Petroleum Prospects*, pp. 1-2.
- ⁶ Venezuela was a charter member; Ecuador did not join until 1973.
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- ⁸ Christopher Joyner, "Latin America's Communal Response to the Energy Crisis," *Lawyer of the Americas*, vol. 6, no. 3 (October 1974), pp. 637, 644.
- ⁹ *New York Times* (December 24, 1975), p. 31
- ¹⁰ *New York Times* (February 5, 1978), p. IES23.
- ¹¹ George Philip, *Oil and Politics in Latin America* (1982), pp. 297-99.
- ¹² Norman Gall, "The Challenge of Venezuelan Oil," *Foreign Policy*, no. 18 (Spring, 1975), 46. Robert Stobaugh, "The Oil Companies in the Crisis," *Daedalus*, vol. 104, no. 4 (Fall 1975), 181.
- ¹³ Philip, *Oil and Politics*, pp. 300-306.
- ¹⁴ *New York Times* (October 27, 1973), p. 41.
- ¹⁵ *New York Times* (December 13, 1973), p. 2; Gall, "Challenge of Venezuelan Oil," p. 57.
- ¹⁶ *Washington Post* (June 28, 1974), p. A6.
- ¹⁷ Gall, "Venezuelan Oil," p. 51. *Washington Post* (December 15, 1974), p. A1.
- ¹⁸ Gregory F. Treverton, "Venezuela's New Role in World Affairs," *The World Today*, vol. 32, no. 8 (August 1976), 310-15.
- Consumer prices are from the *Washington Post* (May 5, 1974), p. G3.
- ¹⁹ U.S. FRUS, *The Energy Crisis, 1969-1976*, vol. 37, pp. 135ff.
- ²⁰ On the general application of US trade law to Latin America and the Latin American reaction to the 1974 Trade Act see John S. Odell, "Latin American Trade Negotiations with the United States," *International Organization*, vol. 34 (Spring 1980), 207-28.
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- ²² *New York Times*, July 1, 1977, p. 1; November 17, 1976, p. 9.
- ²³ Philip, *Oil and Politics*, p. 284.
- ²⁴ Christopher Brogan, "The Retreat from Oil Nationalism in Ecuador, 1976-1983," p. 2. <http://sas-space.sas.ac.uk/3401/1/B51 - The Retreat from Oil Nationalism in Ecuador 1976-1983.pdf>. Accessed April 5, 2013. Philip, *Oil and Politics*, pp. 274-285.
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- ²⁶ Joyner, "Latin America's Communal Response to the Energy Crisis," p. 644.
- ²⁷ John D. Wirth, ed., *Latin American Oil Companies and the Politics of Energy* (Lincoln: University of Nebraska Press, 1985), p.264.
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- ²⁹ November 8, 1978, FRUS, vol. 37, 536.
- ³⁰ Memorandum, November 22, 1978, FRUS, 543-44.
- ³¹ Meeting of September 28, 1979, FRUS, vol. 37, 753-57.
- ³² Philip, *Oil and Politics*, pp. 269, 272, 462-65.
- ³³ Bernardo Grossling, *Latin American Petroleum Prospects* (Washington: Geological Survey, 1975), p. 9.

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- ³⁴ Bela Balassa, "Newly-Industrializing Developing Countries After the Oil Crisis," Working Paper No. 437 (Johns Hopkins University, October 1980), p. 34.
- ³⁵ Stephen J. Randall, *Alfonso López Michelsen, Su vida, su época* (Bogotá: Villegas, 2007), p. 400.
- ³⁶ In 1975 Brazil was producing only 165,000 barrels of oil a day. U.S. Library of Congress, , Energy, Country Studies, Brazil.
- ³⁷ World Bank, Memorandum on Brazil, Report No. 812-BR (Washington D.C., July 7, 1975), p. i.
- ³⁸ World Bank, *Economic Memorandum on Brazil* (Washington D.C., October 13, 1977), pp. 1-4.
- ³⁹ Bela Balassa, "Policy Responses to External Shocks in Selected Latin American Countries," in Werner Baer and Malcolm Gillis, eds., *Export Diversification and the New Protectionism* (Champaign-Urbana: University of Illinois Press, 1981), pp. 131-167. Brazil's pursuit of a nuclear program with the aid of West Germany brought its government into conflict with the Carter administration, with the result that the Geisel government renounced its military alliance with the United States in 1977.
- ⁴⁰ Philip, *Oil and Politics*, p.p. 388-89.
- ⁴¹ Joyner, p. 644.
- ⁴² Grossling, *Latin America's Petroleum Prospects*, p. 25.
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- ⁴⁴ Balassa, "Newly-Industrializing Developing Countries After the Oil Crisis," p. 49.
- ⁴⁵ Balassa, Policy Responses, p. 149.
- ⁴⁶ World Bank, *Economic Memorandum on Brazil*, Report No. 812-BR (Washington D.C., July 7, 1975), p. 14.
- ⁴⁷ Grossling, *Latin America's Petroleum Prospects*, p. 8.
- ⁴⁸ Balassa, "Newly-Industrializing Developing Countries," p. 36.
- ⁴⁹ Balassa, "Newly-Industrializing Developing Countries," pp. 42-46.
- ⁵⁰ Data from UN, Economic Commission for Latin America (1973), p. 11, cited in Grossling, *Latin American Petroleum Prospects*, pp. 7, 9.
- ⁵¹ Balassa, "Newly-Industrializing Developing Countries," p. 19-20.
- ⁵² Balassa, "Policy Responses", pp. 139, 154-55, 159.