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Norwegian Gas in the New Europe

How Politics Shape Markets

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Norwegian Energy Policy in an International Context: The U.S. Embargo of Soviet Gas in 1982

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International energy markets are more politicized than most other commodity markets, where governments extensively interfere with taxes, subsidies, regulations and even pure warfare. One important reason is that the oil price and the availability of energy are central factors, directly and indirectly, for the development of all nations' economic and political stability. This is true whether the country is a net exporter or net importer of energy. The conflict in the Persian Gulf after the Iraqi invasion of Kuwait in 1990 has emphasized this fact.

Scarcity of oil and gas will characterize international energy markets, either in an economic, physical or political sense, over shorter or longer time. With a constantly increasing Norwegian petroleum production, the international community will closely observe the development in Norway. Apart from security policy, petroleum issues may become the most central single factor in Norwegian foreign policy, simply because the outside world defines it so.¹

Norwegian oil and gas have already been the focus of international conflict. As late as in the spring of 1990, the Soviet Union halted considerable parts of its gas supplies to Lithuania. Norway was then requested to substitute these in order to alleviate the pressure from the superpower. Similarly, the question of oil supplies to Israel, the relationship to OPEC and various gas negotiations (Troll, Sleipner) have all had elements involving central international political aspects.

As an example of how Norwegian petroleum policy may be influenced from the outside world also in the political sense, I will in this article analyse the case

when Norwegian energy policy first became an explicit element in a larger political game. In order to prevent Western European countries from completing a notable gas contract with the Soviet Union in 1982, the U.S. introduced a ban on all American exports to firms supporting the project. Also European firms supplying equipment were boycotted by the U.S. The Americans claimed that if Western Europe became too dependent on Soviet gas, it might come under pressure in a future political crisis if the Soviets turned off the taps to stop the energy supply. The U.S. urged Norway to increase her gas exports as a substitute for Soviet gas.

Norway, on the other hand, maintained that the gas production could not be increased as quickly as desired. This was due to the long time lags between a field development decision until actual production can take place. The Norwegians also wanted, in case a development should be accelerated, a "price premium" to justify an act that otherwise would have been different.

The U.S. boycott of the equipment was all in all futile. Norwegian total gas production did not increase noteworthy during the 80's and prices have not been higher than those of other exporters either. The expected increase in production in the nineties is a result of the Troll agreements of 1986 which were signed for other reasons than the U.S. wishes.

This article will discuss central issues in this conflict. Was the argument regarding the risk of supply disruption the sole American concern? Was the policy realistic as to what was acceptable to buyers and sellers in the market? Did Norway play her cards right when responding to the American requests or could gains have been achieved by some other strategy? Can anything be learned if Norwegian petroleum again should be linked with international conflict?

Soviet gas export and American interests in 1982

The background of the conflict in the early eighties was that the Soviet Union planned to construct a pipeline with a capacity of 40 billion cubic metres (BCM) per year. The pipeline was to transport gas from the Urengoy field on the Yamal peninsula in Western Siberia to Western Europe. Yamal is about 4000 km from Western Europe, with permafrost and difficult weather conditions. In Western economies the project would probably not have paid off. But since it would bring the Soviet Union considerable revenues in convertible currency, while the expenditures were paid for in rubles, the project was assessed as profitable from a Soviet point of view.

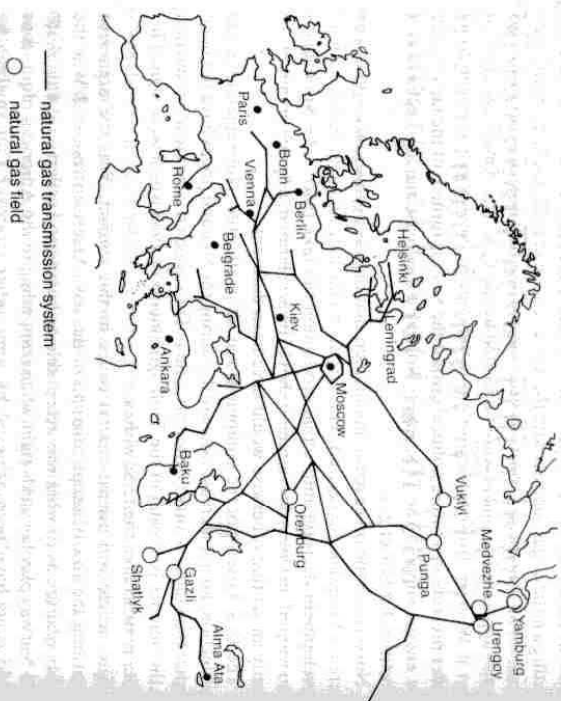


Fig. 1. Soviet pipeline systems for gas to Western Europe.

The purchasing countries were Western Germany, France and Italy. At one stage, the Netherlands and Belgium too were about to buy Soviet gas. While the initial volume was set to 40 BCM, it was later reduced to 25-30 BCM. This represented a Soviet share of 30% of the German and French and 40% of the Italians' gas import.

The Carter administration was sceptical to such a gas agreement already in the late 70's. The view was that Western Europe would become to dependent on energy supplies from the Soviet Union as well. Assistant Secretary of Defense in the Reagan administration, Richard Perle, made the arguments more clear in November 1981 ("Defense", February 1982) as a threat to Western security. First, the exports gave the Soviets vast revenues in hard currency. This enabled them to import technology for military use. It would also release civilian resources which in its turn could be used for military purposes. Secondly, Perle

thought the project would result in the formation of economic bonds between Western Europe and the Soviet Union. This could widen Soviet influence on U.S. allies, and could, over time, contribute to a Soviet-desired division between the U.S. and Western Europe. Thirdly, in a crisis the Soviet Union could disrupt the gas supplies to injure the West. A fourth argument, which was put forward later, implied that parts of the equipment delivered for the construction of the pipeline itself could be used for military purposes. Thus, the fear of a supply disruption was only one of several U.S. arguments to stop the Soviet gas supplies.

The Soviet Union was, and still is, very dependant on energy exports to earn convertible currency. In 1970, the country earned \$ 444 million from its energy exports, which represented 18.3% of its hard currency revenues. In 1980 these revenues amounted to \$ 14.7 billion, or 62.3% of hard currency revenues (Jentleson, 1986). In 1986 the energy share of Soviet hard currency exports had increased to 80% (Austvik, 1987b). There are very few other products of interest to Western Europe. Consequently, for the Soviets, the gas export deal became an important target in improving foreign trade balances.

Thus, if the U.S. should influence the Soviet economic situation, the gas agreement became an attractive target. Besides, the Soviet Union is in great need of Western technology in its energy production. Therefore, the technology transfer through the shipment of equipment for the pipeline construction had a double economic significance. New technology could make the Soviet Union more efficient. This strengthened the Reagan administration's conviction that the pipeline had to be stopped: an economically strong Soviet Union would be more dangerous than a weak one.

The American policy was to a large extent a result of the relationship between the superpowers after the invasion of Afghanistan in 1980. The U.S. assumed that the Soviet Union would face a difficult economic situation, with a deficit in foreign trade and lack of hard currency. This situation could be worsened by not only limiting the access to Western technology and credits, but also by curtailing Soviet trade with the West as such. An anarchic state usually exploits its resources less efficiently than a trading state.

As both an economic and a military superpower it seemed logical for the Americans to link economics with politics in order to promote their interests. This is in particular valid vis-à-vis an opponent which, more or less exclusively, is a military superpower and must be regarded as rather under-developed in economic terms.

Therefore, the Polish state of emergency in 1981 became a convenient reason for the American measures. The Polish situation gave the U.S. a concrete reason for introducing sanctions against the pipeline (Jentleson, 1986). "The

Evil Empire', as Reagan called the Soviet Union in his first presidential term, had to be punished for the treatment of Poland.

Economic pressure as a foreign policy instrument

The use of economic pressure to change other countries' policies is not unknown. Economic sanctions were undertaken by the United Nations against Rhodesia and South Africa with rather limited success. The U.S. has undertaken grain embargoes against the Soviet Union, also with limited achievements. The first time international economic sanctions were undertaken in an effective manner (with a substantial majority of countries participating) was evidenced with the U.N. sanctions against Iraq after the invasion of Kuwait in 1990. However, in general, sanctions have proved rather ineffective in obtaining political goals.² This has mainly been due to three factors:

- Individuals, businessmen and others who have to endure the burdens of an economic boycott are not willing to do so. This was for example expressed by American farmers who put pressure on president Reagan to cancel the grain embargo imposed on the Soviet Union by the Carter administration in 1978.
- Countries representing alternative sources for the boycotted country have refused to cooperate. This may be due to diverging views as to the purpose of the penalty. Or they find that an undue share of the burden by the sanctions falls on them. During the grain embargo, Argentina did not only allow sales to the Soviet Union, but diverted export to some extent away from her former markets towards the Soviet Union (Mastandano, 1984).
- It has not always been easy to predict the reaction of the country subjected to economic pressure. It may be mild, but can also get harder. Besides, countries depend on trade in varying degree. This puts limits (as well as it creates potentials) as to what may be achieved through a boycott.

Here, I shall distinguish between three ways of using economic pressure to reach political goals: economic warfare, tactical linkage and strategic embargo.

Economic warfare

Economic warfare implies, in short, to weaken another country's military potential by hurting its economy. This presupposes linkages between the country's trade and economic development as well as between its economy and

the military. Improved technology, a better qualified labour force and a more sophisticated civilian sector will strengthen the military beyond the effect of the imported goods as such.

Such a strategy does not necessarily have to be applied to all goods. In principle, it may be selective by picking those indispensable to the penalized country, while of less economic importance to the sanctioning one. Goods must be found where the demand in the target country is very inelastic, where the costs of indigenous production are unreasonably high and where it is (made) impossible to retrieve them from other contractors.

Highly developed technological commodities will very often be such an objective. Apart from being important for the military, technology is also a bottleneck for economic development. Because the gas contracts represent significant Soviet income in hard currency, they will also be a suitable goal under a policy of economic warfare.

Tactical linkage

Tactical linkage is a systematic junction of economic and political/military elements aimed at influencing the *politics* of the target country, rather than weakening its military capability through a weakening of the economy. If trade can impart the opponent's benefit from the military apparatus, even when this is still being built up, the net result regarding one's own security may well be positive. A country's security is not only dependant on the military capability of its opponent, but also on the costs involved for the opponent of using this capability.

In such a strategy the trade policy will be adjusted according to how content one is with the policy of the opponent. The trade may be extended if this policy is seen as positive and reduced if not. The adversary will then actually be inhibited in his actions in the sense that a political action may imply a loss of an important trade agreement. If the contract is sufficiently extensive and important, the dominant country may gain political influence in the target country through the economic dependence which has arisen and the personal ties that have been established.³ An economic interdependence has been developed which reduces the interest in waging war against each other.⁴ The influence will, however, in varying degrees, go both ways, positively as well as negatively.

The reason why the U.S. embargo of 1982 usually is not regarded as a linkage policy is that it was linked with Soviet policy at large, rather than with any singular aspect of it. And it aimed at *reducing* trade and relations, rather than increasing them.

Strategic embargo

By a strategic embargo the concern of the sanctioning country is not to weaken the opponent economically. It merely wishes to strike goods that can be of direct military use. The prohibition of contraband in wartime is the most typical example of a strategic embargo.

During a strategic embargo, export of goods that reduce economic bottlenecks in the target country is allowed as long it does not affect military ones. Raw materials have historically often been such goods, while technology may be more predominant today. As long as equipment for the gas turbines is of no military relevance, a boycott of the Soviet gas supplies will not be included in such a strategy. Limitation of technology export under the Consultation Group Coordinating Committee (COCOM) rules, however, must be characterized as a part of a strategic embargo.

Why did the U.S. boycott fail?

In 1982, a delegation under the auspices of the U.S. State Department went to induce the Western Europeans not to buy Soviet gas. Western Europe should rather choose alternatives to meet their increasing energy demand. The arguments in favour of such diversion were close to our notion of economic warfare, even though the whole range of arguments was actually used (cf Perle's list). An economically strong Soviet Union is more dangerous than a weak one. The U.S. compensation package contained two main components (Jentleson, 1986, pp. 185-187): American coal and Norwegian gas were presented as alternatives to Soviet gas.

The proposal concerning American coal was somewhat vague as the capacity needed for such an export was not obtainable in the U.S. at the time. Besides, coal entails an environmental problem and may be seen as inferior to gas as a source of energy. Complete solutions as to transportation across the Atlantic were also omitted.

The proposal of Norwegian gas implied problems the Americans obviously had not been aware of. Jentleson (1986) claims that the Americans found that the Norwegian government lacked the will to increase production above existing plans. But for Norway it was technically impossible to increase production as fast and as much as desired.

Apart from putting forward these rather unrealistic alternatives, the U.S. failed to include a proposal of compensation for the loss of export contracts for

equipment to the pipeline. The basic conditions of a "just" burden-sharing when a boycott is introduced were consequently broken in the proposal.

Apart from differing economic interests in the burden-sharing, there was a political divergence between Western Europe and the U.S. on the desirability of an embargo, as well. First, Western Europe had, partly with strong internal opposition, just been deploying Pershing and Cruise missiles. This complicated an acceptance of another Western initiative against the Soviet Union.

Secondly, most countries thought the gas supplies would result in a lesser degree of dependence than maintained by the U.S. Much of the risk of such a dependence could be counteracted by enlarging storage facilities for gas, increasing the flexibility of the national distribution systems and securing the supply of Dutch and Norwegian gas in the long term. Even though the Western European countries did not reject the possibility of a Soviet stop in supply in a worst case scenario, they did not see themselves as vulnerable as the Americans did.

A third divergence occurred as the Europeans thought the Americans overestimated the strategic Soviet advantages of the agreement. It was argued that the Soviets would benefit from high technology import, i.e. the importance of a *strategic embargo*. The views, however, differed as to what degree hard currency incomes would increase Soviet military capability. There was, in other words, no consensus on the effect of *economic warfare*.⁵

When the supplies of compressors and other equipment commenced at the end of August 1982, President Reagan banned all American export to those firms that supplied the project. Despite the ban, however, supplies of the European equipment continued. When President Reagan, the same fall, increased U.S. grain exports to the Soviet Union, the European countries became even less willing to break the contracts.

The tension was eased on November 13, 1982, as the U.S. terminated the sanctions. No European return services were agreed upon, but it was settled (Jentleson, 1986) that Western Europe should close no further gas contracts with the Soviet Union until (a) The International Energy Agency (IEA) had completed a study on the danger of becoming (too) dependent on Soviet gas; (b) the OECD had concluded a study on the effects of export credits to the Soviet Union; (c) a COCOM agreement was reached on limitation of high tech export to the Soviet Union and (d) a NATO study of the significance of trade in general between the WP and NATO countries was completed.

The volumes were reduced as compared to the original 40 BCM per year. The U.S. claimed that this was a result of the pressure put on the Western European countries. The countries themselves declared that the market situation had led to this reduction. Decreasing oil prices and a weaker economic growth were the

main reasons, and most central suppliers of gas to the Western European market had to reduce their quantities according to expectations.

Though the joint economic warfare against the Soviet Union failed in 1982, an agreement was reached on revising and updating the COCOM rules; in other words, on a strategic embargo. The U.S. wanted a somewhat longer list of commodities on the COCOM list than her allies, while these accepted a more consistent enforcement of the rules and control with Soviet agents involved in technological espionage in Western countries. Western European and U.S. economic interests diverged to some extent, as more trade with data equipment takes place between Western and Eastern European countries than between the U.S. and Eastern Europe. In June 1984, however, an agreement was signed imposing a strategic embargo on the Soviet Union through the COCOM rules.

Politics shape markets and markets shape politics

Norway expressed, in response to the American initiative, that it would be impossible to accelerate production, for instance from the Troll field, sufficiently to make Norwegian gas a real substitute for Soviet gas in the short and medium run. Even though the U.S. appeared to have difficulties in accepting this, the reaction seems correct enough. It does take a long time to develop a gas field in the North Sea, often as much as 5–10 years.

Furthermore, Norway stated that if production was to be accelerated compared to existing plans in the long term, Norway should get an additional price to justify the increase. There would be no reason for Norway to increase gas production if profit was not increased as compared to existing expectations. By this strategy, Norway put forward wishes for a higher price than her competitors for security policy reasons. This line was pursued until the fall of the Willoch government in 1986, without any gas contracts of significance having been signed. When the Harlem Brundtland government adopted a form of market pricing in 1986, the Troll negotiations were eventually speeded up.⁶

Views may diverge about what should have been the aim of Norwegian strategy in 1982. Even though higher prices in new contracts were chosen, implicitly a volume increase, Norwegian interests would also have been promoted through price guarantees, securing access to the markets and flexibility in the contracts, to mention a few.

Should the goal, however, be limited to desire for more profits by new gas sales compared to previously expected profits, it is vital to have an opinion of how the market functions. An increased price *may* be obtained by being preferred to competing exporters. But is it possible to be preferred to other

exporters in terms of price? If the answer is yes, one has to establish whether this is a result of commercial calculation only or, as in this case, whether it can be made on political grounds as well. Or can higher prices only be achieved when prices in the market in general are increasing? If so, is there anything Norway can do to make this happen? And is it desirable?

If the objective is modified from aiming at higher prices to promoting Norwegian gas interests in general, an increase in volume could also be a goal in and by itself. An increased volume will be important, partly because production and transmission of gas is an industry with obvious elements of economies of scale. A large production usually implies lower costs per unit than a smaller one. But will volumes increase primarily due to a growing total market where all exporters increase their export? If so, is there anything that can be done in order to expand consumption of natural gas in Europe? Or is it so, that Norway had the potential for enlarging her market shares at Soviet expense when parts of the central framework of the market changed in 1982?

A totally different objective could have been to improve Norway's economic and political relations with the outside world in general. As a significant exporter of petroleum in a strongly politicized market, this is, of course, a relevant aspect to be considered in a total strategy. The importance of considering such aspects was clearly demonstrated in connection with the signing of the Troll agreement. In order to accept this commercial agreement the French government required an improvement in a series of fields in the Franco-Norwegian relations. An important aspect of such type of national linkages is that parts of the deal cannot be negotiated on the commercial level only, but directly involves governmental bodies and politicians.

The purpose of the discussion above is to point out that the choice of objective and strategy has to be made according to how prices and volumes are formed endogenously in the market and the exogenous factors influencing the market. This equilibrium is very hard to find. But it is, in one way or another, being created by techno-economic barriers; structures of production, transmission and distribution; diversification wishes on commercial, competitive and security grounds; as well as by overall economic and political assessments. Equilibrium can be changed over time, as capacity is being increased, management capability (political and commercial) enhanced, political and commercial positions changed, demand and overarching political structures develop, new pipelines constructed, etc.

Did the situation in 1982 *per se* alter the functioning of the market, or the strategies of the actors, in such a way that Norway's situation as a gas exporter was significantly improved? Could the situation be used to influence and improve the frameworks or the functioning of the market in the interest of

Norway? Clearly, a "free market" does not exist anywhere. There may be no real long-run development of the market based on pure economics. Politics may well, from time to time, overthrow any of the expectations based on purely economic analyses. Therefore, perhaps Norway should more actively play her own "cards" into the formulation of the outcome?

Why did the demand for higher prices fail?

At the time the U.S. put forward the wish for increased Norwegian gas sales to substitute Soviet gas, oil prices, and consequently gas prices in Western Europe, were high. In the market there were expectations that new large gas contracts would be signed at high prices. The Statfjord contract of 1980/81, which until then represented the highest prices of natural gas in Europe, underlined these expectations. The U.S. pressure on the purchasing countries to buy Norwegian instead of Soviet gas was added to this favourable market situation. In the early 80's the prospects for the Norwegian gas trade seemed bright, both in a commercial as well as in a political perspective.

The Norwegian "price premium" policy has mainly rested on the ground that prices, first, certainly must cover all expenses attached to the development of fields and pipelines. Secondly, gas production was put up against crude oil production. If gas production was less profitable than oil production, there would be no reason for Norway to increase sales, at least not in such a degree that would have been necessary if Soviet gas should be replaced. Consequently, the reason for the Norwegian price demand had its basis in production economic considerations.⁷

In Norway, much attention was paid to the U.S. argument that the Soviets, in a crisis, could turn off the tap. But the disruption scenario was only one of the American arguments for halting the supplies. And, as discussed above, even though Western Europe had considered the risk of a supply disruption, it was only one part of their overall risk assessment. For them, in an overall evaluation, it was desirable and beneficial to pursue the import deal with the Soviets. In a crisis, common Western security and/or American interests would eventually be jeopardized, not only the interests of individual European consuming countries. Thus, the Norwegian price premium policy can not be defended as well from a market point of view as it can be argued from a production point of view.

It was the American, and not primarily Western European governments, that wanted the Soviets to sell as little gas as possible. A price premium on Norwegian gas should, consequently, be invoiced to the U.S. or, for instance,

NATO. Whether it would be possible to make the U.S. pay such a premium is doubtful, when regarding American administrations' previous reluctance to cover the expenses of others when economic sanctions against the Soviet Union are imposed (of the grain embargo and the reaction of American farmers). It also seems most unlikely that NATO, as an organization, could agree upon such an arrangement, when taking the conflicting interests across the Atlantic into account. The conclusion is that it would be difficult to achieve a price premium, whether paid by the consuming countries, the U.S. and/or NATO.

Of course, security against disruption in energy supplies is vital to all importers. Then again, this attitude, both concerning economic pressure and supply disruption/reduction, whether for technical or political reasons, is the main cause why most countries want to reduce their dependence on oil imports (and, thus, supplies from the volatile Gulf region) and increase the use of alternative energy sources. Such a philosophy of risk aversion is to be found in all international trade and division of labour.⁸ There must be a mutual trust to make the international system work, which is only partially the case.

Each importing country must have an opinion about the costs of maintaining high self-sufficiency (if gas is produced domestically) vs the (short-term) benefits of basing much consumption on (basically cheaper) imports with the risk of supply disruption. Similarly, the (short-term) benefits of relying on few energies and suppliers in the import balance must be gauged against the risk and costs involved in such one-sided reliance if it is possible to (more costly) diversify imports.

This security-of-supply situation is different for Western European countries when assessing the sensitivity to imported gas as opposed to imported oil. The infrastructure in the European gas market makes the rigid *physical* linkages between countries important for security. For oil dependence, the *price* of oil, for most countries, is the variable to be concerned with. Oil can, in a crisis, still be imported from any producing country, but at an unacceptable high price involving unemployment, inflation and possibly recession. Gas, on the other hand, cannot be imported from another country if pipelines or LNG terminals are not built. In the short and medium term, a one-sided dependence on one single exporter makes an importer vulnerable to economic exploitation as well.⁹

The probability of a disruption and the damage it may cause must be large enough to offset the costs in non-disruption periods to diversify more than (short-term) economic considerations dictate. Faced with the disruption scenario as a motive, Western Europe and the U.S. had diverging views on how to define security of supply in 1982. The Soviet Union benefited by the Western European perception of the situation.

In fact, the argument of supply disruption could be turned *against* Norway. In a scenario where one supposes that the Soviets would turn off the tap, in an extreme state of tension between East and West, they will also lose their currency revenues. What if they, instead, could reduce Norwegian supplies? Then they would reduce the supply of energy to Western Europe at the same time as they (most likely) maintained their currency incomes. Western Europe would then be even more dependent on the Soviet supplies. Possibly, the likelihood that the Soviets should turn off their own taps, is such a dramatic scenario that the political climate can make such a pressure on Norway likely, too. This clearly demonstrates that the evaluation of risk as to a supply disruption must be put into a wider context in order to prove meaningful at all.

Could alternative strategies have been implemented more successfully?

To illustrate some alternative strategies to the price premium policy, I will mention some options below which possibly would fit better with the way the market works combined with how the interests were positioned in the conflict.

— With the huge costs of developing Norwegian fields, it would have been important to Norway if she was guaranteed a certain price for a long period of time. Such a price *guarantee* would perhaps have been obtainable in a good market situation, as in 1982–85, simply because it seemed improbable that it would ever be effective. In a weak market with low prices, such a guarantee would function as a price premium. If prices will be low in the nineties, Norway could have profited considerably from such an arrangement (such a contractual arrangement would, however, not have had much effect on active contracts in the eighties).

— It may seem as if the Western European gas prices, to a large extent, are being determined by a market equilibrium. Studies have shown that prices for all exporters tend to be quite similar when corrected for varying quality (Austvik, 1987a). Perhaps the encouragement of using Norwegian gas should be used to increase market shares at this common price. Various marginal improvements of normal contracts at that time could (from Norway's point of view) have been implemented as well. Furthermore, signing the Troll contract in this period would, most likely, have resulted in better contractual conditions than in 1986, when it was actually signed.

— The preference for one exporter may be expressed through more favourable take-or-pay or deliver-or-pay clauses than what other exporters get.¹⁰ This can also be done through more favourable *force majeure* conditions or, generally, by giving one seller more security against variations in quantity demanded than other suppliers, or that compensation systems favour particular sellers.

— The transmission companies (the pipelines) for gas are the third actor in the market, in addition to seller (producer) and purchaser (distribution companies, large industrial consumers and electricity plants). In the case of the Austro-Norwegian gas agreement of 1986 Norway witnessed how the pipeline company (Ruhrgas) for a long time was able to impede the fulfilment of the contract.¹¹ Perhaps a more reliable access to the continental pipeline systems, at a reasonable tariff, should have been contemplated as an element of the negotiations in order to improve the conditions of future Norwegian gas sales.

A weak development of the Western European gas market was observed during the eighties. Seeing this in retrospect, the unexpected "support" that Norway received from the U.S. regarding purchase of Norwegian gas, could have been used to improve positions in one or more of the ways mentioned above, rather than pursuing the price premium policy. But then again one should not totally reject the possibility that the weak market development successively became too weak to make this achievable, as well.

In fact, the Western European gas market can be interpreted as if Norway had corresponding interests with the *Soviets* regarding prices. With a group of importing countries organized in a consortium on the European continent and selling countries divided, a market structure that, to some extent, is created by a political situation where East and West is divided, may be characterized as an oligopoly on the selling side and as a monopsony on the purchasing side. Given that a monopsony, more than an oligopoly, has greater possibilities of influencing prices, the political situation may have led to lower gas prices than what otherwise could have been realized. And it is in the interest of the purchasers to maintain this situation. Thus, the real political price premium may favour consumers (or more correctly the importers) at the expense of producers, rather than one producer at the expense of another.

If Norway should intend to take advantage of this possible joint interest with the *Soviets* by coordinating price policies, its potential profit has to be gauged against the economic and political costs such coordination imposes vs other Western countries.¹² Such an approach to the Soviet Union in the gas market would probably be politically much more problematic to implement than the

Norwegian approach to OPEC in the oil market (Austvik, 1989), even though the security policy aspect of it may be reduced as the Soviet Union may open up to the West. The U.S. wanted (at least previously) Norway to sell her gas at the expense of the Soviet Union. But the Americans have not wanted the Soviets to get higher prices.

Can a similar situation occur again?

The fact that Norway was driven into the discussion of the Siberian gas pipeline illustrates that the content of Norwegian energy policy is important to both superpowers. Just as the Americans have been engaged in preventing exorbitant Soviet hard currency incomes, the Soviets are correspondingly eager to get such revenues. To the Soviets, Norway is an economic competitor as a gas seller. At least, in many situations, Norway is limiting Soviet chances of gaining western currencies. Even if the two countries have common interests in terms of prices, they still are competitors as to volume. Consequently, Norwegian gas strategy will be of major economic and strategic significance, also to the Soviet Union, partly independent of the political development between East and West.

A similar community of joint and conflicting interests that Norway faces towards the Soviet Union in the Western European gas market is to be found within OPEC. In the global oil market, all oil producing states share the interest that the public good, the oil price (within certain limits and in varying degree) should be at a higher level than most consuming countries want and that the market should be as large as possible.

OPEC member states have conflicting interests as to who is to pay to keep such high prices if they are not a result of a genuinely tight market, and production reductions are necessary in order to realize these prices. This is demonstrated in the recurring discussions on production and quota sharing within the organization. All OPEC countries wish to urge other producers to reduce output and keep prices up, as that is the least cost approach to maintain their own price goals. The Iraqi invasion of Kuwait is maybe the most extreme expression of an "influence" of one producing country towards another.¹³

Norway is an increasingly more significant oil producer. By this, Norway has an impact on the welfare of other oil producers. Norwegian production contributes in keeping oil prices at a lower level than they otherwise would have been. This has already proved to inhibit the potential for conflict, when Norwegian interplay with OPEC, introduced in 1986, was introduced as a result of pressure. Such type of pressure has the potential to occur again, in line with increasing

Norwegian oil exports, market conditions and international relations. Correspondingly, Norwegian gas exports are politically and economically important to both importers (principally the EC) and exporters (mainly the Soviet Union and Algeria) of gas.

Consequently, Norwegian international petroleum strategy has to be moulded in the awareness that each of the two superpowers, and petroleum exporting and importing countries in general, are preoccupied with its content. As an energy exporter, Norway has no overall joint interests with any other country, even though such interests exist within certain singular areas. Therefore, "the policy packages" that Norway will compose in the energy area have to be defined by Norwegian national interests and must be flexible in relation to the status of the market and the political situation.

In a tight energy market and/or tense political situation, the energy importing countries will give preference to supply security and a moderate price development. Norway could be put under pressure to increase Norwegian supplies and to moderate the prices, which may, to some extent, be in Norwegian self-interest. In a weak market and/or in a situation of détente, however, Norwegian supply possibilities and the price development for gas may be threatened. A subsequent pressure may occur from other exporters (especially of oil) towards production limitations and coordinated actions to stabilize the prices. In such a situation this too may be in Norwegian self-interest. Norwegian interests will, therefore, as an energy-exporting western industrialized country, be found somewhere in between those of the sheer energy importing and sheer energy exporting countries.

Of course, this discussion does not mean that Norway should adapt to all pressure coming from other countries in various situations. It should independently assess any requirement coming from other countries on a national interest basis. But the discussion indicates that Norway's interest partners, in the energy field, may change, depending on the state of the market and political situation.

As to credibility, Norway is, therefore, facing somewhat different problems in her international energy policy than in, for instance, her security policy. In the energy area the conditions change rapidly and some times dramatically, in a closely integrated interaction of economics, politics and even purely military movements. The formulation of Norwegian international petroleum strategy should therefore be rather flexible. On the contrary, her national interests indicate that it is the dynamics and the independence of the policy that may be the decisive factor whether a given policy is to prove successful or not. There is no such thing as an "entirely free market" in international economics or relations, where politics and economics are closely intertwined.

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Notes

- ¹ By the end of 1990, Norwegian oil production amounted to as much as 1.9 million barrels per day (mb/d). This is more than the Kuwaiti production

before the Iraqi invasion. In addition, Norway has produced natural gas at a stable level of around 30 billion cubic metres (BCM) over a decade. Thus, as a combined oil and gas producer, Norway is already significantly larger than Kuwait. Furthermore, the production of both oil and gas is expected to increase in the nineties.

² This sub-chapter is mainly based on Allison & Cornesale (1988).

³ Norway experienced a coupling between trade and politics when the French part of the Troll contract was signed. In order to accept the contract, France required a general agreement with Norway about increased political, scientific, trade, cultural and industrial cooperation. Ref. i.e. Austvik (1990a).

⁴ This is an important reason why another war between France and Germany seems quite unlikely today. Both countries will have more to lose than to gain by destroying the other. Before this economic (and political) interdependence was established, these two countries had fought wars regularly over centuries. Such a linkage philosophy is also a major element in the German "Ost-Politik" from the sixties. Making East and West economically interdependent, the blocks would gradually be worn down.

⁵ The Western European governments acted rather similarly despite different ideological make-up. The EC protested against unacceptable interference in sovereign decisions in member countries. Margaret Thatcher used British economic interests as an argument to pursue with the suppliers of the equipment. The Western European joint reactions may have improved their positions at the expense of the U.S.

⁶ However, another important reason for the lack of new contracts was a weak market development in the first half of the eighties. In the second half demand increased again.

⁷ The "price premium policy" contributed to the formulation of an "oil option policy". In short, the latter formulated that if the higher gas prices were not accepted, oil fields would rather be developed and the gas will remain in the ground. This policy has contributed to the doubling of Norwegian oil production in the period 1986-90.

⁸ In Norway, the agricultural policy over the last 20 years has partly been argued for on the basis of an as large as possible self-sufficiency of food.

⁹ This may be the situation for some East European countries and Soviet republics throughout the nineties, being one-sidedly reliant on Soviet gas supplies. Many of these countries are even one-sided physically dependent on Soviet oil supplies, with no access to the sea and costly development of oil pipelines.

¹⁰ "Take-or-pay" clauses involve that the buyer either has to purchase the contracted quantity or pay an economic compensation to the seller. "Deliver-

to pay an economic compensation to the purchaser.

¹¹ This problem is an important reason for the EC Commission to consider some sort of "Open Access" system for the transportation of natural gas. A introduction of the Single Market approaches in 1993. See Austvik (1990a) and another article in this book reviewing some of the main issues of these ideas.

¹² It is important to be aware that the potential for price changes by such action is much less than OPEC's potential for changing prices. But even though administered changes of gas prices are taken within more narrow limits than for oil prices, small margins constitute large amounts of money. For example a 10 per cent change of gas prices will, for Norway, represent some 300 million dollars annually at the volumes now exported (1990).

¹³ Austvik (1990b) discussed the oil side of the conflict in the Persian Gulf in 1990.