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WITHDRAWAL SHEET

Ronald Reagan Library

Collection Name EXECUTIVE SECRETARIAT, NSC: COUNTRY FILE

Withdrawer

LOJ 9/26/2006

File Folder IRAN-IRAQ WAR (5/24/84)(2)

FOIA

F1718

Box Number 36

BATTLE

43

ID	Doc Type	Document Description	No of Pages	Doc Date	Restrictions
27792	PAPER	ENERGY IMPLICATIONS OF CURRENT PERSIAN GULF SITUATION <i>R 5/1/2007 F1718</i>	3	5/24/1984	B1
27793	MEMO	MCFARLANE TO THE PRESIDENT, RE PLANNING (DIFFERENT DRAFT THAN 27770)	5	ND	B1
27796	PAPER	SAME AS 27792 <i>R 5/1/2007 F1718</i>	3	5/24/1984	B1
27797	MEMO	MCFARLANE TO THE PRESIDENT, PERSIAN GULF ENERGY <i>R 12/19/2011 F1718/1</i>	2	6/4/1984	B1
27798	MEMO	WILLIAM F. MARTIN TO MCFARLANE, RE ENERGY <i>R 12/19/2011 F1718/1</i>	2	5/31/1984	B1
27801	MEMO	OIL FACILITIES... <i>D 1/8/2008 NLRRF1718</i>	1	5/24/1984	B1 B3
27802	MAP	PERSIAN GULF AREA <i>PAR 1/8/2008 NLRRF1718</i>	1	3/1/1978	B1 B3

Freedom of Information Act - [5 U.S.C. 552(b)]

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B-3 Release would violate a Federal statute [(b)(3) of the FOIA]

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DRAFT

SECRETARY HODEL PRESENTATION
ENERGY IMPLICATIONS OF CURRENT PERSIAN GULF SITUATION
NSPG MEETING
Thursday, May 24, 1984

CURRENT OIL SITUATION

- ° Energy implications of situation in Persian Gulf have not changed fundamentally since you were last briefed.
- ° As result of recent escalation of air raids on tankers in Persian Gulf:
 - Spot market has firmed; apprehension in the market has produced some upward pressure on spot crude and product prices, causing world prices to fluctuate in response to these incidents; at this point, there is no evidence of upward trend in prices
 - Oil tanker/cargo insurance rates for Persian Gulf have increased; for example:

Kharg Island Premiums on Top of Normal Insurance Charges for Typical VLCC of 1.7 Million Barrels

	<u>3/30/84</u>	<u>5/22/84</u>
War risk premium (% value of hull) (dollars)	.75% \$60,000	3% \$240,000
Cargo insurance premium (% value of cargo) (dollars)	.5% \$253,750	3% \$1,522,500
Total added insurance premium per voyage	\$313,750	\$1,762,500

- ° Frequently, these premiums are subject of negotiations between buyer and seller
- According to industry sources, lifting operations south of Ras Tanura area (Saudi Arabia) appear to be continuing; however, in northern portion of the Gulf, oil companies are modifying tanker operations and assessing liftings on case-by-case basis

EXCESS PRODUCTION CAPACITY

- ° Excess production capacity in Free World is estimated at 10-12 MMBD in 1984; about 3 MMBD are outside the Gulf.
- As shown below if Strait were closed:
 - ° Complete loss 8.6 - 9.6 MMBD
 - ° Offset from Saudi-Yanbu pipeline (incr. thruput) (1.0 - 1.5)
 - ° Offset outside Persian Gulf region (2.6 - 3.1)
 - ° Net loss after avail. excess prod. 5.0 MMBD

DECLASSIFIED

NLS FL718 #27792

BY LOI NARA, DATE 5/1/07

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DRAFT

Page Two

- ° Two important points regarding excess available production capacity:
 - World has far more excess available capacity now than in prior disruptions in 1970's, when there was scant, if any, surplus
 - Not all excess available capacity will come to market immediately
 - ° Some will be delayed for technical reasons (30 - 90 days)
 - ° Some may be delayed for political or economic reasons (e.g., Saudi Arabia's reported 60 - 75 MMB contingency floating storage)

IMPACTS OF DISRUPTION

- ° Two possible scenarios illustrate potential economic impacts (these figures are without regard to drawdown of SPR or allies' strategic stocks):
 - 3 MMBD net world loss (after available excess production) for 3 months could mean price increases from present \$29 per barrel to level of \$35 - 75 per barrel in 2nd quarter 1984; \$35 - 55 average over 12 months following the disruption
 - 5 MMBD net world loss (after available excess production) for 6 months could mean \$50 - 95 per barrel in 2nd quarter 1984; \$40-70 average over 12 months following the disruption
 - ° Economic impacts for this scenario (12-month average): GNP loss in range of 3.2%; inflation rate (CPI) increase in range of 4.8%; unemployment rate increase in range of 1.3%; industrial production decrease in range of 6.9%
- ° For third quarter 1984, the net disruptions shown above could increase by approximately 1 MMBD as a result of seasonal increases in demand, adding \$5-35 per barrel to world crude oil prices

STRATEGIC STOCKS

- ° SPR today contains approximately 400 million barrels
 - Can be drawn for 5 months at peak rate of 1.7 MMBD or 3 months at 2.1 MMBD; thereafter remainder can be drawn down at lesser rates
- ° Allies' strategic stocks much lower than ours
 - Only Japan and Germany have significant government-owned strategic stocks
 - Japan has only about 27 days of import coverage in its strategic reserve and Germany about 68 days, compared to about 90 days for U.S.

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Page Three

- ° Not clear whether world's commercial stocks would be drawn down in event of disruption
 - Risk that, given uncertainties about length of disruption and past history, commercial inventories actually will build at beginning of disruption
- ° Administration publicly has announced that, ordinarily, best policy in major disruption is to engage in early draw of SPR in large volumes
 - Actual decision is President's at time of supply emergency
 - Depending on magnitude of disruption, SPR can be major offset against world supply loss and, therefore, dampen price rises
 - ° E.g., even if we assume net loss of 5 MMBD from closure of Strait of Hormuz, SPR draw of 2.1 MMBD is 1/3 of the net loss
 - ° SPR alone could limit the increase in world crude prices by as much as \$5-20 per barrel, depending on how fast used; coordinated allied stock draw could limit the increase even further.
- ° Administration publicly has stated that SPR will not be used to manage fluctuations in world prices not attributable to a net loss of supply.

CONSULTATION WITH ALLIES

- ° Bilateral and multi-lateral discussions with selected IEA/OECD partners concerning coordinated stock policies, including special emphasis on: need to increase strategic stocks; need to engage in such coordinated drawdown as appears appropriate in light of circumstances at time of emergency; need to avert overreaction to emergency by governments; and need to coordinate public statements of governments to calm unnecessary panic behavior of marketplace.

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BY ADJ, NARA, DATE 5/1/07

SECRETARY MODEL PRESENTATION
ENERGY IMPLICATIONS OF CURRENT PERSIAN GULF SITUATION
NSPG MEETING
Thursday, May 24, 1984

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DRAFT

4
9/26/86

NSC/S PROFILE

ID 8404239

RECEIVED 25 MAY 84 10

TO MCFARLANE FROM MARTIN
MARTIN

DOCDATE 24 MAY 84

31 MAY 84

KEYWORDS: ENERGY

LONDON SUMMIT

IRAN

IRAQ

PERSIAN GULF

OIL

SUBJECT. ENERGY BRIEFING BOOK FOR PRES / LONDON SUMMIT

ACTION: FWD TO PRES FOR INFO

DUE: 02 JUN 84 STATUS X FILES PA

FOR ACTION

FOR CONCURRENCE

FOR INFO

MCFARLANE

V N

COMMENTS

REF#

LOG

NSC/FID

(HW)

ACTION OFFICER (S)	ASSIGNED	ACTION REQUIRED	DUE	COPIES TO
	5/24	Mcfarlane Commented		
Martin	S 5/24	further action		
Mcfarlane	X 6/01	Pres for info		
Pres	P 6/04	information via PPB		
	C 6/11	Pres notes		WMV

DISPATCH

W/ATTCH FILE PA (Chm)

4239 5

THE WHITE HOUSE
WASHINGTON

6/6/84

Brunson McKinley

Attached is energy security
language approved by the President
for use in the Summit communique

Bob Kinnitt

V N

6

Recognizing the importance of global energy security and noting the relationship to the well being of our nations' economies of Middle East oil flows, we agree to continue present efforts, through the IEA/OECD, to assure energy emergency preparedness by establishing effective strategic stock levels and adopting mutually supportive actions^{V N} early in a crisis, including a coordinated stock draw if circumstances warrant.

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4239

7

MEMORANDUM

THE WHITE HOUSE
WASHINGTON

June 4, 1984

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ACTION

MEMORANDUM FOR THE PRESIDENT

FROM: ROBERT C. MCFARLANE *RCM*
SUBJECT: Persian Gulf Energy Threat and the London Summit

Issue

Based on the current situation in the Persian Gulf, it is increasingly likely that energy emergency preparedness will emerge as a key issue at the London Summit.

Facts

Over the last few months, we have been leading an international effort on energy emergency preparedness based on your guidance at the March 20 NSC meeting as embodied in NSDD-134.

Our international energy emergency policy is based on the principle of equitable burden sharing through strong and continued cooperation with other consuming countries. Special emphasis has been placed on the need for coordinated oil stock policies while recognizing that each country will have to respond through measures appropriate to its own situation.

Domestically, we will rely on market forces, supplemented by oil from the Strategic Petroleum Reserve, and will continue to oppose price and allocation controls.

Discussion

Consultations over the past few months have resulted in a growing consensus with the allies on the need to coordinate oil stock policy, including general support for an early stock draw if circumstances warrant. Those countries without adequate stocks have said that they could share the burden of a disruption by relying on demand restraint, however, this approach, in our view, is less effective and harder to quantify.

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NLRRF1718#27797

BY RW NARA DATE 12/14/11

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Our main objective is to get the allies to equitably share the burden of a major oil supply disruption. Congress and the public will not support our policies if it appears that we are carrying an inordinate share of the burden of an interruption despite our relatively low dependence on Persian Gulf oil.

To further this objective, we believe it would be useful to include text in the London economic communique which would embody these principles and serve to reassure the oil market in the event of an emergency. State, DOE and NSC have all agreed on the following language:

"Recognizing the importance of global energy security and noting the relationship to the well being of our nations' economies of Middle East oil flows, we agree to continue present efforts, through the IEA/OECD, to assure energy emergency preparedness by establishing effective strategic stock levels and adopting mutually supportive actions early in a crisis, including a coordinated stock draw if circumstances warrant."

Nakasone reportedly wants to raise this issue at London. Since we want to create a situation in which others will be coming to you on this (rather than we being seen to need something from them), I suggest that you raise the issue with him at your bilateral and, if he confirms his interest, then urge that he take the lead at the lunch the next day. (Talking points have been included in your materials.) If Nakasone agrees to raise the issue (e.g. at the June 8 Summit lunch), you could then ask the others you will see bilaterally on June 7 (Kohl, Craxi, Mitterrand) for their views and how they propose to cope with a major disruption. This too will provide you the opportunity to state your position and give us a good shot at getting the outcome we want (i.e., calming communique language).

I have attached at Tab A for your review an update on the Iran-Iraq threat to world oil flows and a 3x5 card of general talking points on energy.

Recommendation:

OK No

✓ QR

That you approve the above language on energy for the London Summit economic communique and agree to raise the issue in your bilaterals.

Prepared by:
William F. Martin
Ben L. Bonk

Attachment
Tab A - Energy Briefing Book

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4239

MEMORANDUM

NATIONAL SECURITY COUNCIL

~~SECRET~~

May 31, 1984

ACTION

MEMORANDUM FOR ROBERT C. MCFARLANE

FROM: WILLIAM F. MARTIN *WFM*

SUBJECT: Energy and the London Summit

Status. We have been working extensively with Allen Wallis, Don Pearlman at DOE and others to prepare a package on energy for the London Summit. We have jointly developed talking points on energy emergency preparedness for use in discussions on the Persian Gulf. These points have been incorporated by the Sherpa team in the latest draft of the President's Summit briefing book. As you will recall Secretary Shultz said at the NSC preparatory meeting that while energy emergency preparedness will be raised during the political discussions, it should also be included in the economic communique.

Energy Briefing Package. We attach for your transmission to the President the following material:

- o A memorandum (Tab I) summarizing our strategy on energy emergency preparedness, including draft language for the communique approved by State, NSC and DOE.
- o A revised energy briefing book (Tab A) incorporating some useful suggestions from John Poindexter, DOE and State. Our product is now the officially cleared briefing book.
- o A 3x5 card of general talking points on energy.

Contingency Planning. In the event the Persian Gulf situation does not worsen, the short statement on energy included in the memo to the President should be sufficient. Bob Morris and I have worked out some tactics which are incorporated in the President's memo, namely to have the President urge Nakasone at their bilateral to raise the issue at the June 8 Summit lunch. The President could then chime in with his views, and we could get a consensus rolling.

In the event the situation deteriorates, we may need a longer statement to calm the market. We are in the process of coordinating more detailed language with State and DOE which could be used in the final statement if conditions in the Persian Gulf warrant a fuller treatment. I will also bring to London extensive background material prepared by DOE and State, including a sanitized technical paper, which

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MLR/F1718#27798

BY RW
NARA DATE 1/19/11

Allen Wallis and I have agreed could be used as the basis for more thorough energy negotiations.

Don Fortier^{DF}, Roger Robinson^{RWR} and Doug McMinn^{DM} concur.

RECOMMENDATION:

That you sign the memorandum at Tab I transmitting our energy strategy and briefing book to the President.

Approve m

Disapprove _____

Attachments

Tab I

Memo to President

Tab A

Energy Briefing Book

V N

(1)

PERSIAN GULF OIL (GENERAL POINTS)

- DESPITE IMPROVEMENTS, WORLD REMAINS DEPENDENT ON PERSIAN GULF OIL
- DISRUPTION COULD THREATEN ECONOMIC RECOVERY
- I STAND READY TO USE U.S. SPR, TO EVERYONE'S BENEFIT
- CANNOT DRAW UNLESS OTHERS VISIBLY SHARING BURDEN OF COPING WITH DISRUPTION. NEED COMPARABLE ACTION BY ALL PARTNERS. DEMAND RESTRAINT LESS EFFECTIVE THAN OIL STOCKS.
- COORDINATED STOCK POLICY/OTHER MUTUALLY SUPPORTIVE POLICIES REQUIRED
- WORK THROUGH IEA/OECD
- NEED COMMUNIQUE LANGUAGE (OVER)

Summit Countries: Dependence on PG

<u>Country</u>	<u>% of Total Oil Consumption</u>	<u>Comment</u>
U.S.	3%	High SPR
Canada	4	Oil exporter
UK	12	Oil exporter
Germany	13	Reluctant to use stocks
France	32	No gov. stocks
Italy	43	Low stocks
Japan	61	Low stocks/ reluctant to use

Kathleen
Field

THE IRAN-IRAQ
THREAT TO WORLD
OIL FLOWS

DECLASSIFIED

Authority F96-120/3 #4284 SMF 7/14/06

BY NOI NARA DATE 9/28/06

NOI HAS SEEN

5/22/84

PREPARED BY

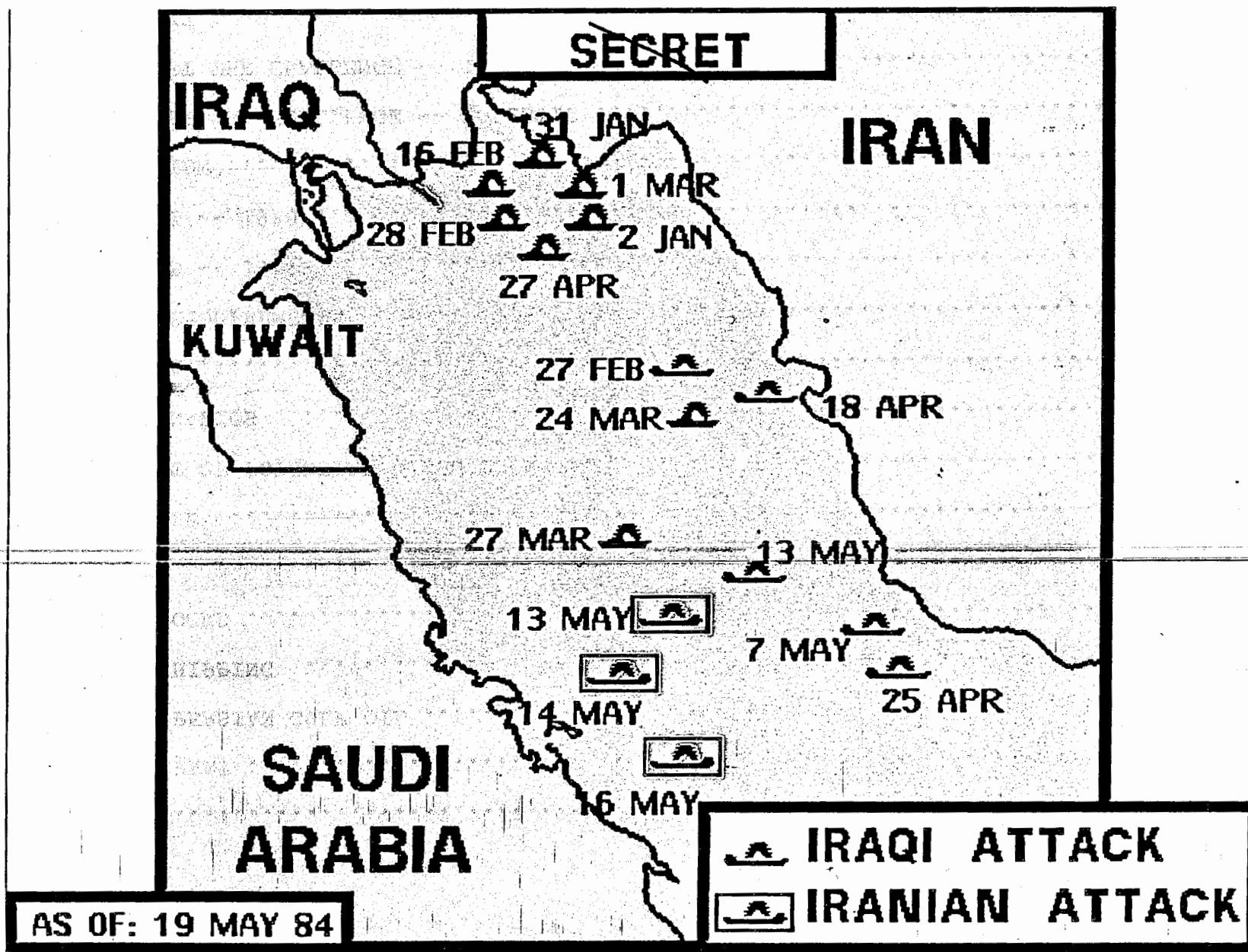
WILLIAM F. MARTIN
ROGER W. ROBINSON
BEN L. BONK
CRISIS MANAGEMENT CENTER

5/22/84

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SUMMARY

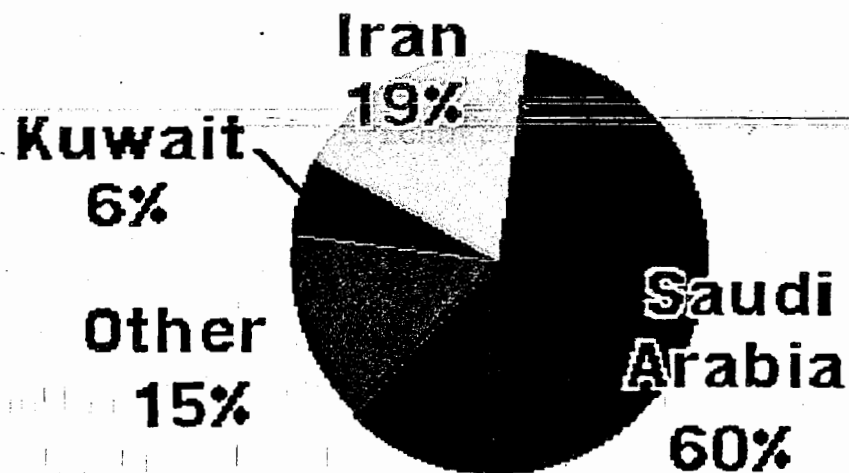
28-B

- o Past oil disruptions in 1973-74 and again in 1979-80 had serious impacts on the world economy. In both cases the rapid increase in energy prices helped initiate new recessions and higher inflation.
- o The new round of Iranian and Iraqi attacks on oil tankers threatens to disrupt the flow of Persian Gulf oil. There is an increasing risk that the fighting could involve Saudi Arabia and Kuwait. Tehran continues to threaten oil facilities and the Strait of Hormuz.
- o Under the worst circumstances, oil prices could triple, triggering a new recession, increased unemployment, higher inflation, and a further deterioration of the debt crisis.
- o The energy policy of the United States is defined by NSDD-87 and NSDD-134.
 - oo Domestically, we will continue to rely on free market forces and the Strategic Petroleum Reserve.
 - oo We cannot, however, insulate ourselves from the international economic impact as oil prices rise and available supplies are redistributed. If we are to win public support for our policies, we must not let it appear that the US is paying all the costs and making all the sacrifices. We are currently consulting with our allies to forge commitments to policies that will fairly share the burden of a major oil supply disruption, with particular emphasis on the adequacy and coordination of stock policy.

Free World: Surplus Oil Productive Capacity

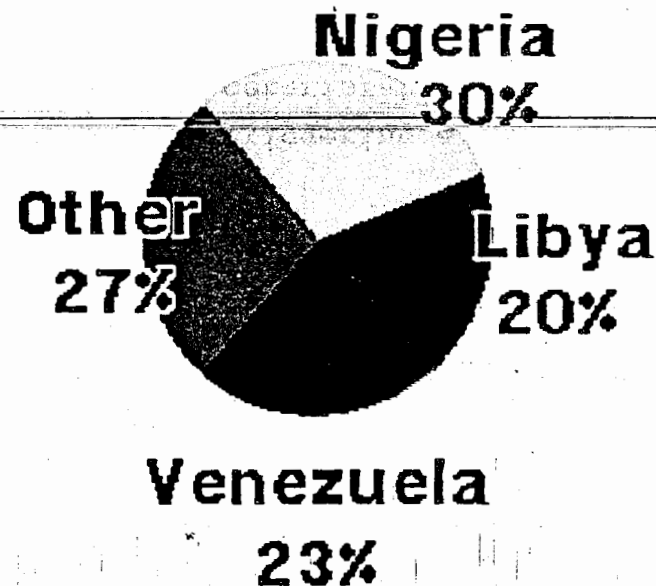
Persian Gulf

Total: 5.2 Million B/D



Non-Persian Gulf

Total: 2 Million B/D



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5/22/84

CURRENT OIL MARKET

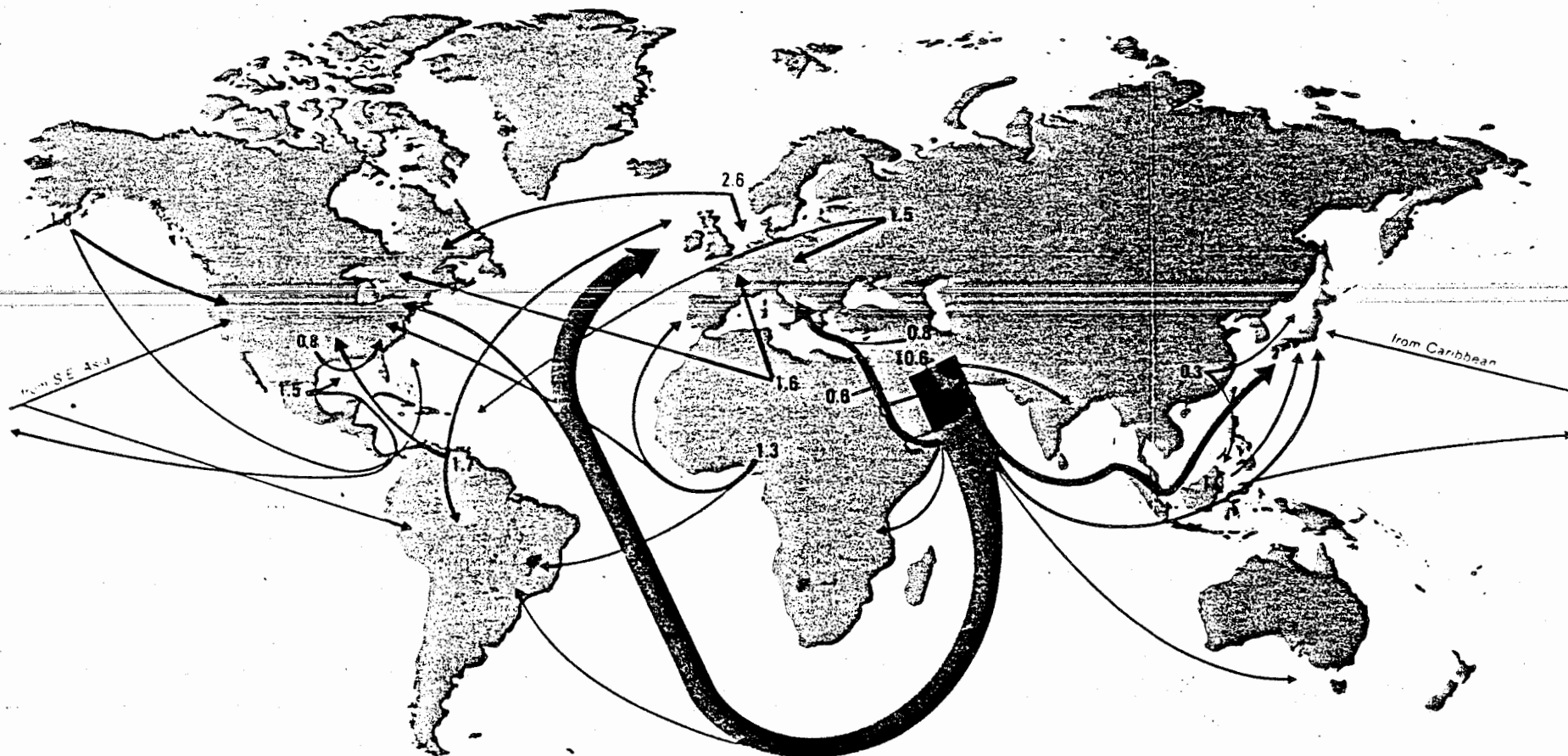
27-B

- o Persian Gulf countries are producing about 12 million barrels per day (b/d) of oil, this accounts for about 25% of total Free World output.
- o Surplus capacity available to help offset a disruption totals about 8 million b/d in the second quarter of 1984.*
 - oo Only 3 million b/d is outside the Persian Gulf, with 20% of the non-Persian Gulf total in Libya.
- o As a result of the recent series of attacks on tankers, insurance rates in the Persian Gulf have increased sharply.
- o After some initial nervousness, the spot oil market has adopted a "wait-and-see" attitude.

*NOTE: The unclassified estimate of surplus capacity is 9-10 million b/d.

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Main Oil Movement by Sea—1982*



1 2 Number indicates oil supply (million b/d) at point of origin.

Unclassified

637969 4-83

* First-half 1982 data.

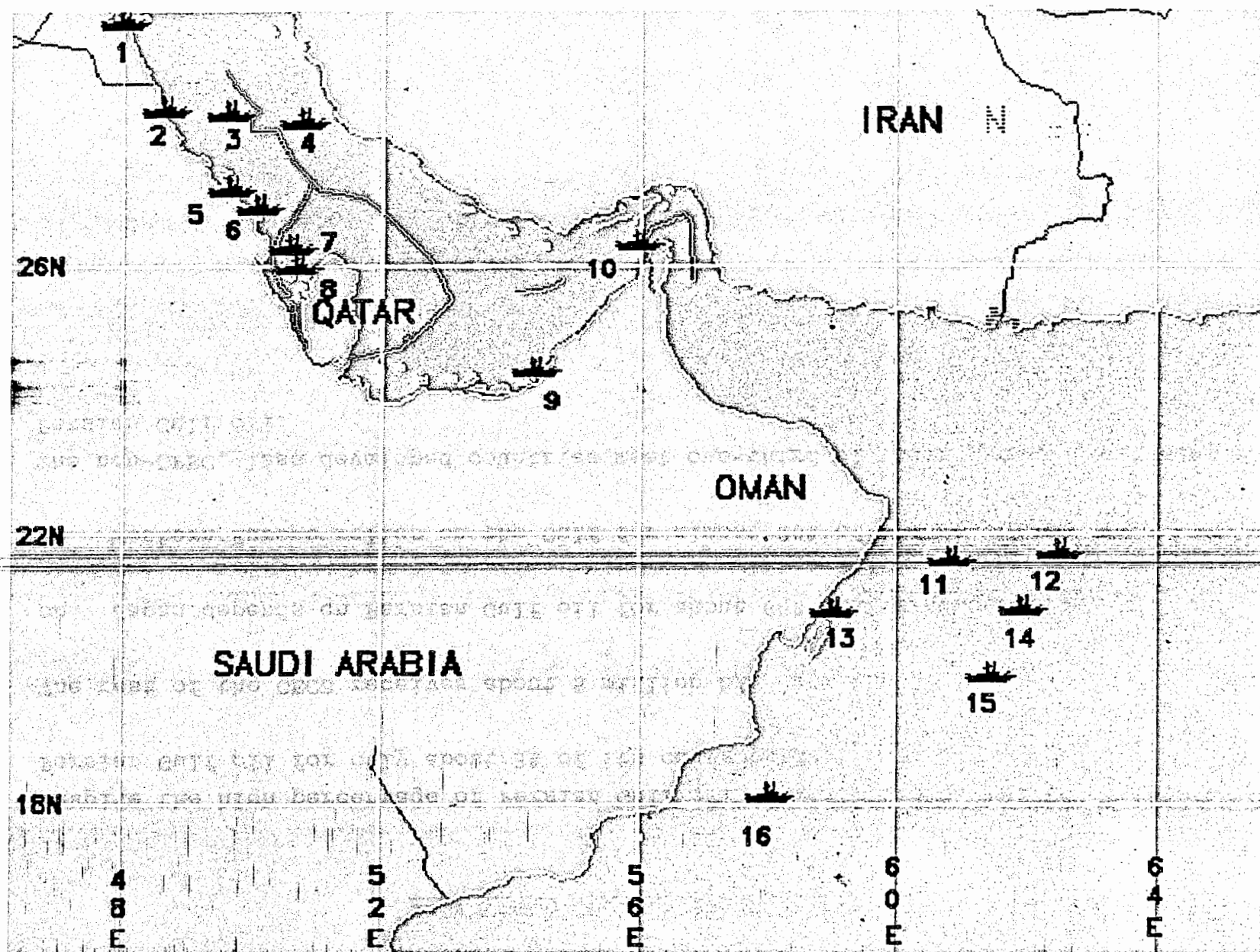
27

DEPENDENCE ON PERSIAN GULF OIL

26-B

- o Despite the high percentage of Persian Gulf oil in world trade, the US relies on Persian Gulf oil for only about 3% of its consumption.
- o The rest of the OECD receives about 5 million b/d from the Gulf.
 - oo Japan depends on Persian Gulf oil for about 60% of its consumption.
 - oo Western Europe relies on the Gulf for almost 20% of its consumption.
- o The non-OPEC, less developed countries meet one-third of their consumption needs with Persian Gulf oil.

LOCATION OF US OWNED OR CONTROLLED SHIPS (22 MAY 1984)

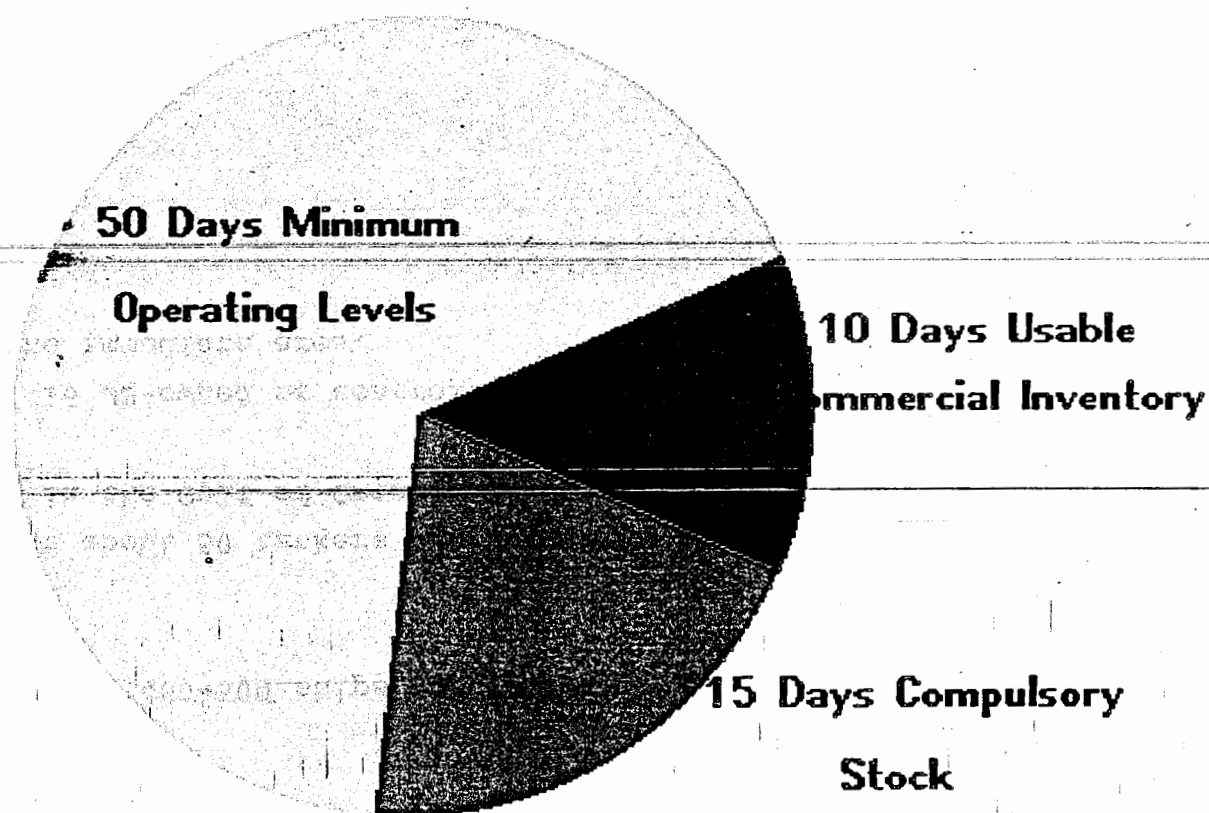


25-B

PERSIAN GULF SHIPPING

- o Under normal circumstances 400-500 ships are active in the Persian Gulf at any one time.
- o The Navy estimates that about 50 tankers are currently in the Persian Gulf, with an additional 80 waiting in the Gulf of Oman.
- o As of noon on 22 May, 16 US-owned or controlled ships, including 6 tankers, were in the Persian Gulf or the immediate area.

IEA: Primary Commercial Oil Stocks



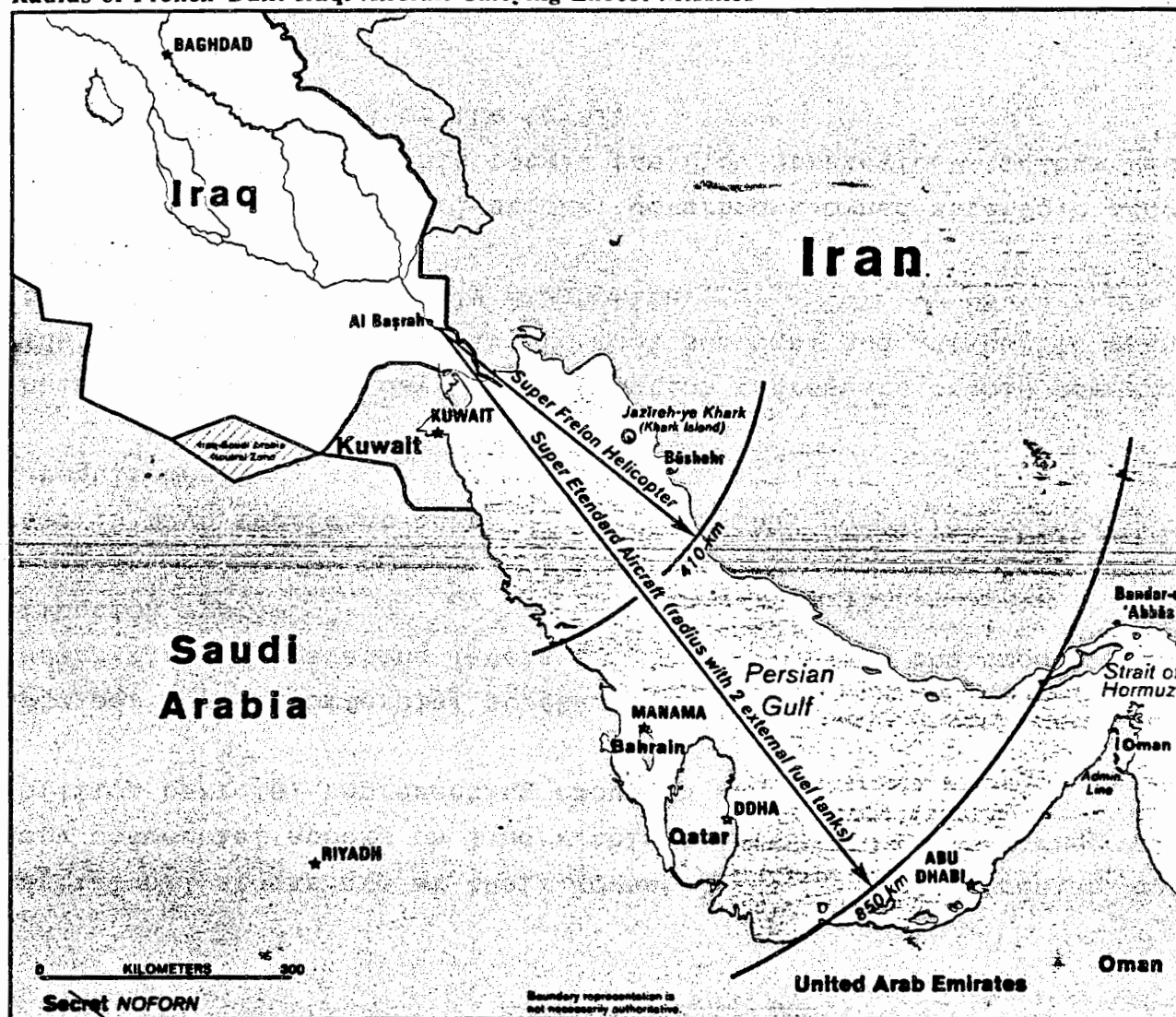
**75 Days of Consumption
(2.2 Billion Barrels)**

CURRENT OIL STOCKS

24-B

- o Commercial oil stocks are at their lowest level since the Iranian Revolution. Primary commercial stocks on land within the International Energy Agency total about 2.2 billion barrels, representing about 75 days of consumption.
- o A large portion of commercial stocks -- on average about 50 days of consumption -- represent minimum operating levels required to ensure the smooth functioning of the distribution system.
- o Another 15 days represent compulsory stocks that companies maintain to meet government requirements.
- o The balance of about 10 days of consumption represents usable commercial stocks that provide industry the flexibility to meet seasonal and unexpected changes in demand and to help cope with a supply disruption.
- o In addition to commercial oil stocks, government owned strategic stocks total about 585 million barrels. Of this total, the U.S. Strategic Petroleum Reserve contains 400 million barrels, 70% of the total.

Figure 1
Radius of French-Built Iraqi Aircraft Carrying Exocet Missiles



IRAQI STRATEGY

- o Despite the weak market, the war in the Persian Gulf poses a clear threat to the flow of oil. Iraqi and Iranian attacks against oil tankers threaten to expand the war to the rest of the Gulf, disrupting oil flows from non-belligerent countries on the Arabian Peninsula.
- o Iraqi objectives in attacking Iran's oil lifeline include:
 - oo Impairing Iran's warmaking capacity by reducing oil revenues.
 - oo Forcing Iran to begin negotiations.
 - oo Forcing Western powers to intervene, guaranteeing the safety of all oil exports.
- o In attacking tankers calling at Iran's main oil export terminal on Kharg Island, Iraqi has been relying on Super Etendard aircraft equipped with Exocet anti-ship missiles.
- o Iraq also has the option of using Super Frelon Helicopters equipped with Exocet missiles, Soviet-supplied surface-to-surface missiles or conventional air strikes.

23-B

Table 1
Persian Gulf Air Order of Battle

	Iraq	Iran	Saudi Arabia	Qatar	Kuwait	UAE	Bahrain	Oman
Personnel	30,000	50,000	17,000	300	4,000	3,000	100	2,500
Fighters	500	260 *	180	NA	50	30	NA	30
Attack helicopters	125	100	NA	2	23	6	NA	NA
SAM launchers	345	300	90	18	27	21	NA	24

* Less than one-third of these are operational.

This table is ~~Secret~~ NoFORN.

Table 2
Persian Gulf Naval
Order of Battle

	Iraq	Iran	Saudi Arabia	Qatar	Kuwait	UAE	Bahrain	Oman
Personnel	4,500	15,000	5,500	700	600	1,500	100	1,500
Major combatants	NA	7	NA	NA	NA	NA	NA	NA
Missile boats	10	11	6	3	NA	6	NA	3
Coastal patrol boats	21	34	100	35	40	44	19	24

This table is ~~Secret~~ NoFORN.

IRANIAN RESPONSE

22-B

- o Iranian officials have threatened to interfere with Arab oil exports from the Gulf to the same extent that Iraqi attacks impair Iranian oil exports.
- o Iran has responded to the Iraqi escalation by attacking Saudi and Kuwaiti tankers.
- o Tehran also has the capability to retaliate by:
 - oo Attacking targets in Iraq.
 - oo Striking out at oil facilities on the Arabian Peninsula via direct military attacks, or by sponsoring sabotage or terrorism by local Shia sympathizers.
 - oo Temporarily closing the Strait of Hormuz, prior to Western intervention, by using mines or declaring a blockade.
- o In order to avoid a Western military response and keep its own remaining exports and imports moving, Iran's response will probably remain at the lower end of the escalatory ladder for a time. Should Iraq significantly impair Iranian oil exports, Ayatollah Khomeini, supported by hardliners in Tehran, might force the most extreme military reaction.

Factors Influencing Economic Impact

- **Expectations**
- **Nature of Disruption**
- **Petroleum Stock Level and Behavior**
- **Availability of Alternate Fuels**
- **Government Initiatives**

21-B

ECONOMIC IMPACT OF POTENTIAL DISRUPTIONS

- o So far, escalation of the fighting in the Persian Gulf has disrupted relatively insignificant amounts of oil.
- o Should the disruption spread further, the oil market might not be able to cope.
- o One of the most important variables influencing the size of the economic impact of an interruption of oil flows is the actual duration and magnitude of the disruption. At the outset, however, the actual nature of the disruption is unknown. As a result, expectations play a central role. Owners of petroleum stocks base their decisions on current stock levels and their perceptions of future market conditions. Government initiatives to calm the market could aid in reducing the size of an oil price increase and subsequent economic dislocations.
- o Our effectiveness in handling the market reaction will depend on our ability to demonstrate that an interruption will be of limited duration and that it will not be repeated. In the absence of such perceptions, companies will respond by building inventories.
- o If a disruption were resolved and the flow of oil restored without the removal of the Iranian threat, inventories would probably be increased in the expectation of future disruptions.

CASE

LOW MED HIGH

NET PRODUCTION
LOSS (MILLION B/D) 0 3 5

OIL PRICES
(\$ / BARREL) 30-40 35-75 50-95

MAXIMUM US GNP
GROWTH REDUCTION
(% POINTS) 0.8 2.5 3.2

INFLATION RATE
INCREASE (% POINTS) 0-1.2 .9-3.8 2-4.8

UNEMPLOYMENT RATE
INCREASE (% POINTS) 0-0.3 .2-1.0 .5-1.3

DISRUPTIONS SCENARIOS

- o Although the probability of a major disruption of extended duration is low, we need to recognize the potential economic consequences and be prepared to deal with the unlikely. The above table summarizes the potentially disastrous economic consequence that could result from oil shortfalls of various size and duration.*
- o LOW: Loss of Iraqi and Iranian oil exports. Although there would be no net production loss since surplus available capacity could easily replace the output reduction, oil prices could begin rising from their current level of about \$29 per barrel if it were feared the conflict might spread.
- o MEDIUM: Complete loss of Iraqi, Iranian and Kuwait oil exports, as well as a partial disruption of Saudi exports for 6 months. As a result of higher oil prices, the economic progress of the past three years would be threatened. Economic growth would stagnate and inflation would increase.
- o HIGH: Complete disruption of Persian Gulf oil flows for 6 months. It is unlikely that Iran could close the Strait of Hormuz for this length of time. A serious long-term problem could develop, however, if an expansion of the war resulted in the destruction of key oil facilities on the Arabian Peninsula and the creation of an environment which would not permit meaningful exports for several months. Oil prices might have to triple to balance supply and demand, triggering a new recession, increased unemployment and higher inflation.

*These scenarios are drawn from interagency projections and assume countries outside the Gulf produce at capacity.

TOP DEBTOR COUNTRIES

BRAZIL *

\$420 BILLION

MEXICO

TOTAL DEBT

SOUTH KOREA *

ARGENTINA

VENEZUELA

INDONESIA

INDIA *

CHILE *

PHILIPPINES *

* SEVERELY AFFECTED BY
OIL PRICE INCREASE

IMPACT ON LDC'S

- o As serious as the consequences would be for the U.S. and OECD countries, a sustained increase in oil prices would have an even more serious impact on LDC debtor countries and the stability of the international financial and banking systems.
- o Should we experience higher oil prices for any extended period, several heavily indebted LDCs:
 - oo Would be increasingly unable to finance oil imports and
 - oo Barring new rescheduling, could be forced to increasingly delay or declare moratoriums on repayments. This, in turn, could result in a breakdown in increasingly strained debtor-creditor cooperation.
- o To give you an idea of the dimensions of the debt crisis at year end 1983, 52 LDCs and East European nations were behind on their debt repayments, with arrearages in the neighborhood of \$35 billion.
 - oo That figure has undoubtedly increased in 1984
 - oo Bankers Trust Chief Economist Lawrence Brainard estimates that over 90 day arrearages on the books of U.S. banks at the end of the first quarter could be as high as \$10 billion.

**KEY OIL-IMPORTING LDC DEBTORS:
IMPACT OF \$5/BARREL INCREASE**

NATION	\$ BILLION (US)
BRAZIL	1.2
CHILE	0.1
KENYA	0.1
MOROCCO	0.2
PAKISTAN	0.2
PANAMA	0.1
PHILIPPINES	0.3
S. KOREA	0.9
SUDAN	0.1
THAILAND	0.5
TOTAL	3.7

18-B

LDC FINANCING REQUIREMENTS

- o For every \$1 increase in the price of a barrel of oil, the total annual oil import bill of the 10 countries listed above would increase by an estimated \$750 million.
 - oo A \$5 increase would mean an estimated \$3.7 billion in additional costs to maintain current oil imports.
- o It is important to note that this is the first time we have had the prospect of a major new round of oil price increases running parallel with an international debt crisis. As a result, we could be faced with a new and more perilous wave of international economic dislocations, with substantial national security implications.
- o Increasing oil prices, combined with rising interest rates, could lend impetus to calls for a politicized debtor cartel.

1979 -- Iranian Revolution

- **Oil Production Shortfall:
1-2 million b/d**
- **Low Stocks**
- **Agreement to:**
 - **Reduce Demand 5% (IEA)**
 - **Oil Import Targets (Tokyo Summit)**
- **Highly Competitive Market**
- **Prices Double**
- **Principal Cause of Last Recession**

PAST EXPERIENCE -- 1979

17-B

- o The Iranian Revolution resulted in a complete halt of Iranian crude oil exports for three months. Uncertainty over future supplies and fear of a spreading Islamic revival subsequently caused a massive stock build.
- o Weak or vague international agreements calling for oil import ceilings (Tokyo Summit) and demand restraint (IEA) did not prevent a scramble for oil. Foreign companies, with the support and at the initiative of their governments, greatly contributed to this bidding war.
- o As a result, oil prices rose from less than \$13 per barrel in 1978 to over \$32 by the end of 1980. This triggered a major, worldwide recession.
 - oo Real GNP in the US, which had been growing at about 5%, stagnated.
 - oo Unemployment increased from less than 6% to nearly 9%.
 - oo The inflation rate rose from 9% to over 13%.

1980 -- Iran-Iraq War

- Oil Production Shortfall:
1-2 million b/d
- High Stocks
- IEA Agreement to:
 - Reduce Stocks
 - Price Restraint
 - Share Burden
- Japan and Europe Jawbone Companies
- Prices Increase 10%

PAST EXPERIENCE -- 1980

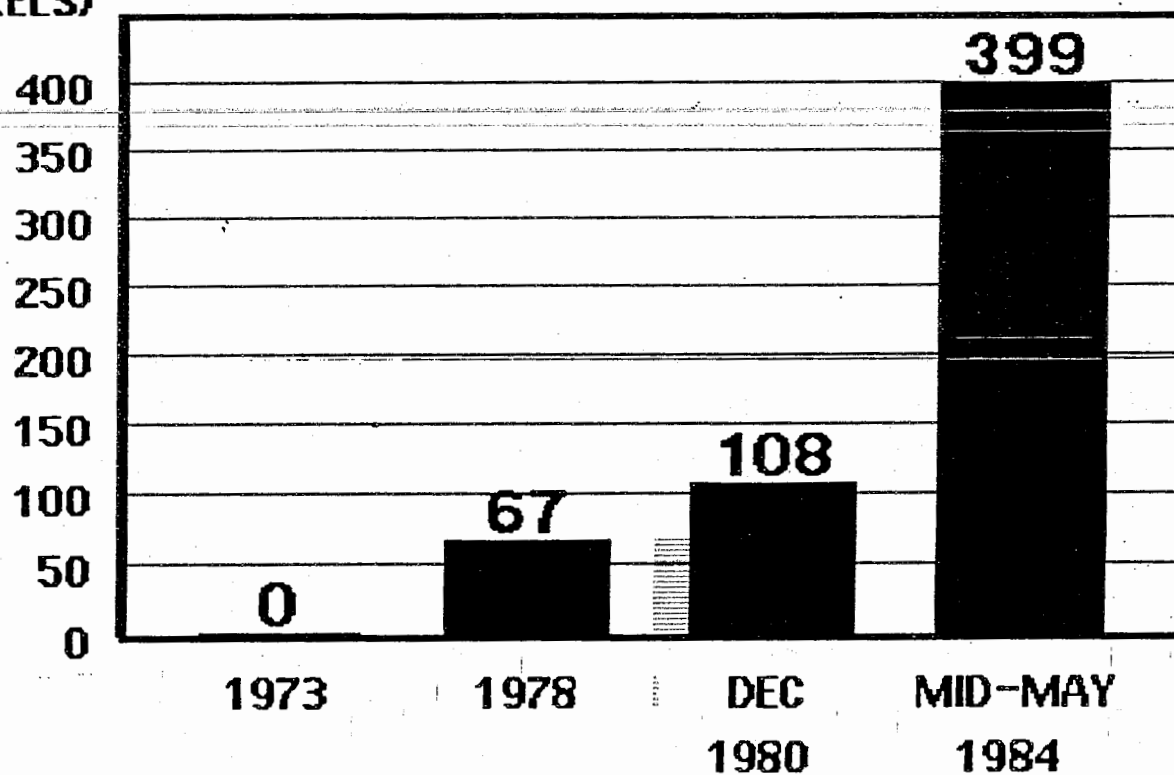
- o The Iran-Iraq war disrupted oil production from both countries. The size of the net production disruption was similar to the one after the Iranian Revolution.
- o Declining consumption and the large increase in oil inventories accumulated after the Iranian Revolution, however, provided us with a cushion.
- o The response in the international community was also different because the experience of 1979 was still fresh in everyone's mind. The IEA reached a firm agreement to lower stocks and avoid abnormal spot market purchases. These agreements encouraged Japanese and European restraint.
- o As a result, price increases were all but avoided.

CURRENT SITUATION

- o The current situation is very similar to 1979. Oil stocks are low, except in the US which has built up the SPR to 400 million barrels -- almost 6 times the level on hand in 1978 prior to the Iranian Revolution.
- o The current slack market, combined with excess productive capacity, has encouraged complacency. As a result, the stage is set for a bidding war which will significantly drive the price of oil upward.

US STRATEGIC PETROLEUM RESERVE

(MILLIONS
BARRELS)



POLICIES TO MEET THE CHALLENGE -- DOMESTIC

- o Reliance on market forces and opposition to price and allocation controls remains the cornerstone of our domestic policy response to an oil supply interruption.
- o The Strategic Petroleum Reserve is our most effective tool for reducing the economic dislocations of an oil disruption. In order to maintain flexibility, we continue to oppose any legislation that would require specific triggers, detailed criteria, or specific scenarios for SPR use. We are, however, on record supporting, under most circumstances, the early sale of SPR oil in the event of a major disruption. Early use of the SPR could reduce price increases by \$5-40 per barrel depending on the size of the disruption and demand response.
- o We also realize that federal, state and/or local economic response programs are necessary for those least able to cope with adverse economic consequences of major oil supply disruptions, such as low and fixed income groups.
- o DOE and State have developed and implemented mechanisms for coordination of the information which is disseminated to Congress and to the media concerning Persian Gulf developments and the ability of free world nations, including the U.S., to cope with such developments, thereby avoiding panic behavior.
- o DOE has instituted a dialogue with various groups concerned about energy emergency preparedness (including States, producers and various industrial and agricultural consumers) so they will have better understanding of Administration policies and efforts.
- o The Administration has also actively supported a legislative effort to facilitate use of energy emergency manpower reserve from the private sector.

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International Response

- **Stock Drawdown**
- **Demand Restraint**
- **Use of Spare Capacity**
- **Assistance to Strategic Countries**
- **Consultations**
- **IEA Trigger**

POLICIES TO MEET THE CHALLENGE -- INTERNATIONAL

- o United States international energy policy is based on the guidelines established in NSDD-87 and NSDD-134 which called for strong and continued cooperation with other consuming countries, equitable burden sharing and reliance on market forces.
- o If our policy of reliance on free market forces is to be successful in the domestic arena, we must ensure that the international market functions well enough to prevent the US from having additional problems at home. The Congress and the public will be very concerned if Europe and Japan are not carrying their fair share of the burden.
- o In order to develop a firm basis for international cooperation, we have conducted an extensive series of consultations with our allies.
 - oo We have engaged the International Energy Agency (IEA) in a major review of international energy emergency preparedness, primarily focusing on the adequacy and coordination of stock policy.
 - oo We have conducted bilateral consultations with the British, Germans, French, Italians, Japanese and Canadians.
- o In all these consultations our representatives highlighted the need for appropriate international policies in order to fairly share the burden of an oil supply disruption among the allies. Special emphasis was placed on the need for increased strategic stocks, coordinated stock policies and the usefulness of an effective public information strategy. It was recognized that each country would have to respond through measures appropriate to its own situation, including means to reduce demand on the world oil market in an emergency. Our allies all responded favorably and, in principle, indicated that they would be supportive of the U.S. approach.
- o In addition, we must be prepared to provide allied assistance to strategic countries in meeting their oil or financial needs, especially those countries where basing rights would be vital to military efforts in the Persian Gulf.
- o As a last resort we must be prepared to meet our commitments to the IEA emergency sharing program.

PUBLIC DIPLOMACY

- o An effective public information strategy will be essential to our efforts. If we can calm the market, we can better contain the economic impact and buy ourselves some time to assess the situation.
- o The following talking points may be used when discussing this issue:
 - oo We support UN Security Council resolution 540 which calls for freedom of navigation and an end to hostilities in the Gulf.
 - oo We and our allies will not stand by an permit an interruption in the oil flows necessary for maintaining the world's economic well being.
 - oo Due to this Administration's early efforts to decontrol oil prices, we have spurred domestic production and cut our imports. At the 1977 peak we imported 8.6 million barrels per day. Today our imports are only 5 million barrels per day and oil from the Persian Gulf accounts for only 3 percent of our consumption.
 - oo As long as we are dependent on any imported oil, we need to have sufficient reserves for use in times of disruption. Our Strategic Petroleum Reserve (SPR) has been increased to 400 million barrels, nearly 4 times the amount on hand when this Administration took office in January 1981. This represents the equivalent of 80 days of our net oil imports and is in addition to commercial stocks which can also be used to cushion the effects of a disruption.
 - oo We are willing and intend to use the SPR to optimum advantage early in a major supply disruption.
 - oo Surplus capacity available to offset a disruption is greater than ever before, totaling about 9 million barrels per day worldwide.
 - oo Because the oil market is international, we could not isolate ourselves from the effects of a temporary interruption of Persian Gulf oil flows.
 - oo Our allies remain very dependent on Persian Gulf oil. Europe depends on imports to meet nearly two-thirds of its consumption needs, while Japan imports nearly all of its oil.
 - oo We are engaged in an extensive new round of consultations with our allies on ways to prevent or deal with a disruption.

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KEYWORDS PERSIAN GULF

CENTRAL AMERICA

MCGOVERN, JIM

MEDIA

TOWER, JOHN

SUBJECT SLN TOWER APPEARANCE ON FACE THE NATION / GULF & CENTRAL AMERICA
ISSUES

ACTION: PREPARE MEMO FOR KIMMITT DUE: 26 MAY 84 STATUS S FILES PA

FOR ACTION

FOR CONCURRENCE

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COMMENTS *No further action required*

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White House Guidelines, August 28, 1997

By 101 NARA, Date 9/26/06

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To: NSRA --CPUA

05/24/84 19:47:51

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NOTE FROM: Robert M. Kimmitt

Subject: Forwarding Note 05/24/84 17:30 Note to Don Fortier
print

* * * F O R W A R D E D N O T E * * *

To: NSPBT --CPUA

~~SECRET~~

NOTE FROM: ROBERT MCFARLANE

SUBJECT: Note to Don Fortier

You may get a call from Jim McGovern (SASC Staff Director). Tower has agreed (at my urging) to go on Face the Nation this Sunday. I have volunteered us to provide him our themes on the Gulf and Central America for him to carry the flag. Jim may ask you to come up tomorrow or to talk to Tower on the phone at least before he goes on Sunday morning to give him any late breaking events. Could you please be prepared to do that, taking Ollie along for Central America? Many thanks.

copy to Small, North

cc: NSJMP --CPUA

7 N

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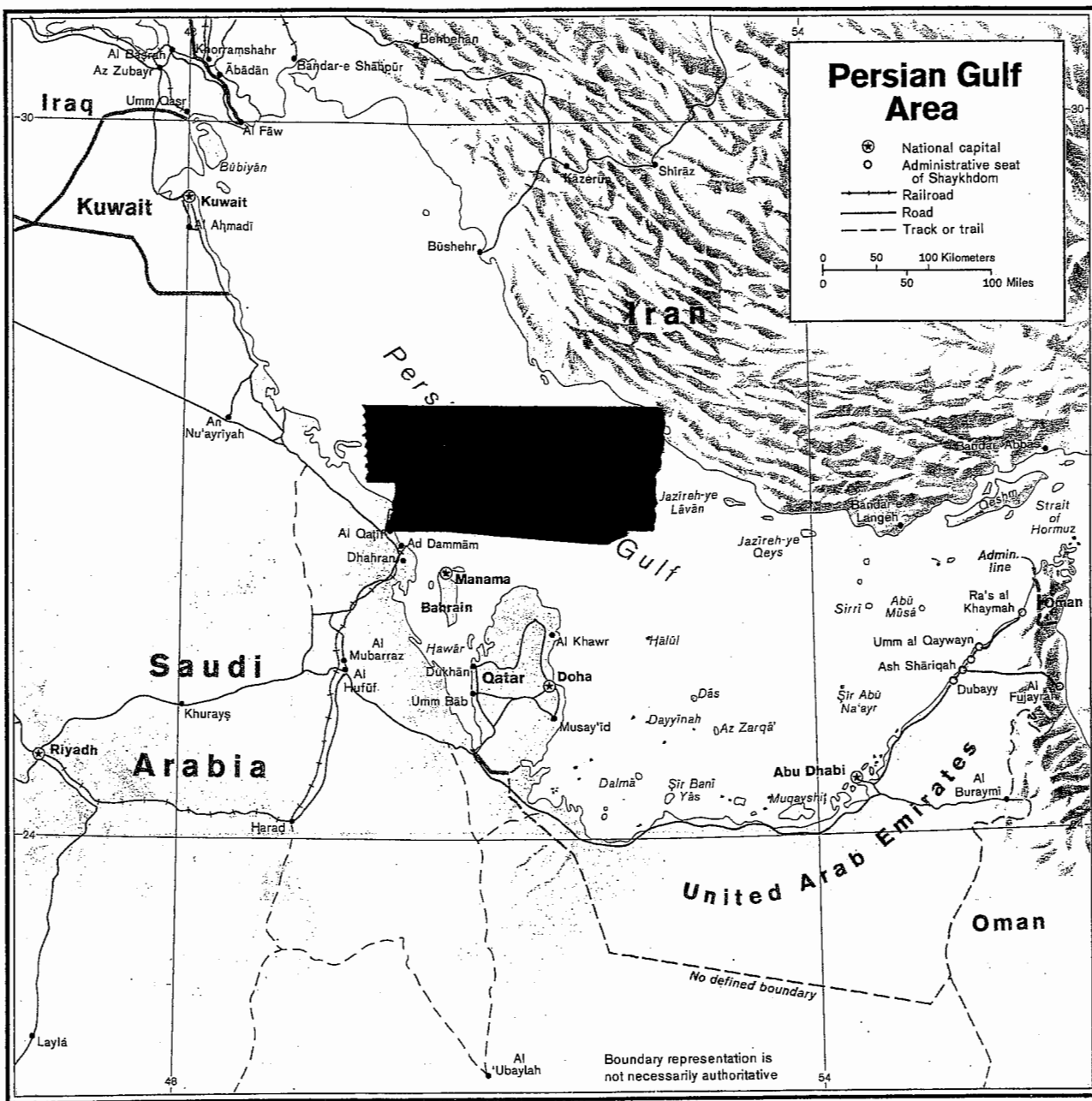
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27801	MEMO OIL FACILITIES...	1	5/24/1984	B1

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- B-1 National security classified information [(b)(1) of the FOIA]
- B-2 Release would disclose internal personnel rules and practices of an agency [(b)(2) of the FOIA]
- B-3 Release would violate a Federal statute [(b)(3) of the FOIA]
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- B-9 Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA]

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