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DOLLAR SHORTAGE AND OIL SURPLUS IN 1949-1950

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BY HORST MENDERSHAUSEN*

I. SURVEY OF ISSUES

RECOVERY from the effects of World War II led the Western European countries on to a broad issue: Should they seek economic viability in a progressive integration of the non-Soviet world or in narrower frameworks implying some discrimination against United States commerce? Since their dollar needs showed a persistent tendency to exceed dollar availabilities during the recovery period and their dollar reserves proved either too small or too volatile, many countries, in particular Britain, found it necessary to make preparations for the latter alternative. During the postwar years, the United States exerted its influence in the direction of closer economic interdependence of countries throughout the world and effectively supported its persuasive efforts by grants and loans, particularly under the European Recovery Program (ERP). But, while relieving the foreign dollar needs inherent in the progress toward more effective cooperation with poorer nations, the United States was not able to still the fears abroad that within a few years—the year 1952 used to be considered as the critical break—the supply of American dollars might decline greatly and that such a decline might worsen the prospects of economic improvement and political stability in many parts of the world. Since 1941, Lend Lease, relief and recovery programs—amounting to forms of international redistribution—had given essential support to the livelihood of associated nations and strengthened the economic and political bonds between them. But the scope of redistributive measures seemed destined to shrink, perhaps excessively and prematurely in view of the world political situation. Market processes alone offered a frail substitute for the cumbersome yet resilient dual system of international economics that had developed since the war: foreign trade plus foreign aid. These fears encouraged discrimination against the United States trade in the name of dollar saving.

The economic developments of 1949, in particular during the first three quarters of the year, seemed to confirm the apprehensions. The dollar supply to the outside world declined as a result of a business

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recession in this country and other factors, and the British dollar position deteriorated rapidly. No major new foreign financing program from the United States was indicated, and the prospective decline of the existing ones was reaffirmed time and again. This hastened general provisions for restrictions of dollar expenditures over an indefinite period of time, in particular the British program of curtailing the dollar outlays of the entire sterling area by 25 per cent. It also led to specific measures against sales by American oil companies abroad. These sales cause foreign dollar expenditures although they come mostly from oil fields and refineries located outside the United States and do not constitute United States exports.

The foreign activities of American oil companies offered an obvious target for dollar saving efforts. Sales of American oil companies abroad constitute a major dollar expenditure to many countries. In 1949, the British Government estimated that more than half of the sterling area's current dollar deficit for fiscal 1950 would arise through the deficit on oil transactions. Transactions with American oil companies alone would account for more than a quarter of the deficit. Eleven per cent of the value of all Economic Cooperation Administration (ECA) shipments to participating countries up to the middle of 1950 consisted of oil.

During the ERP period, Britain, France and other countries felt it necessary to prepare for a lessening of their dollar outlays on oil. These preparations followed different lines: expansion of facilities to produce crude oil, refined oil, and oil industry equipment; limitation of civilian demand for oil products; and, finally, the restriction of oil purchases from American companies. Since no foreign country could afford an actual lessening of its oil consumption under the conditions of 1949, the last mentioned course was open only to those who had access to rapidly available supplies. Only Britain was in that position. Toward the end of 1949, Britain's major oil companies, which have been sharing the markets outside the United States with the American companies on a roughly half-and-half basis, became able to supply some additional oil in substitution for American company oil. Britain, therefore, took the lead in imposing discriminatory measures against the so-called dollar oil.

The measures taken by the British Government will be discussed below. Together they seem to have restricted the sale of refined oil products by American-controlled companies in the sterling area and elsewhere by about 6.75 million tons or 9 per cent of the overseas production of American companies.[1] (At least this may be said to have been

[1] Testimony of Assistant Secretary of State Willard L. Thorp before the House Inter-State and Foreign Commerce Sub-Committee on Petroleum, April 5, 1950, reprinted in *Effects of Foreign Oil Imports on Independent Domestic Producers*, Report

their potential effect by mid-1950; they never became fully effective in reality.) Further limitations on the sales of American oil companies abroad for dollars had to be expected in the course of time as new facilities were completed in the Middle East and Europe. France for instance has been aiming at eliminating all dollar expenditures on oil imports by 1952 and at relying thereafter on sterling and franc oil, chiefly crude oil from Iraq. But in 1949 more than half of France's oil imports were paid for in dollars, with the help of ECA, and no practical alternative was available.

Britain's measures took the form of stipulations in bilateral trade agreements with countries outside the sterling area (Egypt, Sweden, Brazil, Argentina, and others) providing for larger shipments of sterling oil to them, restrictions on the use of sterling owned by other countries for payments to American accounts, including those of the oil companies, and, finally, the partial substitution of sterling for dollar oil in the markets of the sterling area.[2]

The British measures were received with sharp opposition by the American oil companies and the State Department and led to protracted negotiations that seemed deadlocked up to the early summer of 1950. Then several compromise arrangements were made between the British government and individual American companies which reduced the effects of the restriction measures considerably and practically left not much more of them than the "whereases." These compromises were facilitated by the relative improvement of the dollar position of the sterling area following the devaluation of sterling as well as the renewed expansion of the American domestic market for oil following the general upswing of business in the early half of 1950. The outbreak of hostilities in Korea did not bring about the compromises, but it signaled the beginning of a new great economic effort in the western world that could not fail to increase greatly the effective demand for petroleum products and other fuels, and, more generally, signified a renewal and intensification of the community of interests. It is not likely that the positive restrictions against dollar oil will be tightened again unless general demand and dollar supply prospects take another turn for the worse.

of the Sub-Committee on Oil Imports to the Select Committee on Small Business, 81st Congress, 2nd Session, House Report No. 2344, Washington, D.C., 1950, p. 100. This committee report is henceforth referred to as: *Effects of Foreign Oil Imports.*

[2] The terms dollar oil and sterling oil mean different things to different people. The British government has used the word sterling oil to describe the oil offered by "British-controlled companies," and dollar oil that offered by "American-controlled companies." American oil men have stressed that dollar oil is oil that has to be produced at dollar cost, that most oil in the world has some dollar production cost, and that the distinction therefore is one of degree. In this study the British definition will be adhered to since it became operative in the British government's measures.

At home there developed simultaneously a conflict over imports of crude and fuel oil. While oil imports into the United States had been growing rapidly since the war, it happened only in 1949 that their growth was accompanied by a curtailment of domestic production—by about 8 per cent as compared with 1948—and the formation of a developed reserve capacity of about 50 million tons of crude oil per year—about 18 per cent of 1949 domestic production—that could be exploited in keeping with "sound conservation practices." The growth of the demand for oil had fallen behind the development of domestic production facilities. Strong efforts were exerted by oil and coal interests to restrict oil imports.

In the market, both of these phenomena—restrictions on dollar oil abroad and on production at home—appeared as expressions of an oil surplus.[3] It is the purpose of this essay to examine the causes of this apparent oil surplus of 1949, and the involvement of the domestic oil industry with its assets of $18 billion, the American oil industry abroad (assets over $3 billion) and the multi-billion dollar British oil enterprises. We shall also consider the involvement of certain countries of Latin America and the Middle East whose economic development depends so heavily on the operations of the British and American oil companies.

Part II of the essay is focused on the British-American conflict, part III on the controversy over oil imports into the United States and national oil policy. The fourth part of the study deals with the way in which the conflicts were resolved and aims to show how the troubles of this dynamic international industry reflected the difficulties of moving toward a more effective economic integration of the United States, Western Europe, and the areas of new development.

II. DOLLAR OIL ABROAD

1. Pattern of International Oil Industry

The larger part of the world oil market, 62 per cent in 1948, is in the United States. About 90 per cent of it is supplied from the domestic production of a variety of American oil companies including the Shell Oil Company, a subsidiary of the Royal Dutch Shell group.[4] The remainder is imported by the Standard Oil Company (N.J.), the Gulf

[3] Both were anticipated at the time of the conclusion of the as yet unratified Anglo-American petroleum agreement of 1945. See Herbert Feis, *Seen from E.A.*, New York, 1947, p. 181.

[4] Sixty-five per cent of the common stock of the Shell Oil Company, a Delaware corporation, is owned by Shell Caribbean, a New Jersey corporation, which in turn is owned 100 per cent by Batavian Oil Company, a Dutch corporation. The British/Dutch Shell group is referred to as British in this paper.

Oil Corporation, Socony-Vacuum, and about eight other large companies including the two British-controlled organizations, Shell Oil and Shell Caribbean.

Outside North America and Eastern Europe the oil industry is shared fairly evenly by a few large American and British company groups, with third groups holding a minor, although now increasing, share. The American share is somewhat greater in crude oil reserves and production, the British in refined products. (See Table 1.) The chief source of crude oil produced by American companies abroad is in Venezuela—where the American share is about twice as large as the British—followed by Saudi Arabia and other Middle East areas, where output has risen rapidly since the war. The British companies have their main sources of crude in the Middle East (particularly Iran) and the East Indies, where their share is greater than the American, and in the Caribbean area. (See Table 2.)

British and American oil interests throughout the world are interwoven in a very intricate manner. The major international company groups in the United States, in particular Standard of New Jersey, Caltex, Socony-Vacuum, Gulf, and the two British groups, Shell and Anglo-

TABLE 1

BRITISH AND AMERICAN COMPANY SHARE IN WORLD RESERVES AND AVAILABLE SUPPLIES OUTSIDE NORTH AMERICA AND EASTERN EUROPE

	Total (million metric tons)[a]	*American companies*	*British companies*	*Others*	*Total*
		(Percentage Shares)			
Proven crude oil reserves, January 1, 1950	6,236	50	46	4	100
Crude oil available, 1948, annual rate[b]	150	53	44	3	100
Refined products available, 1948, annual rate[b]	123	43	49	8	100

[a] Throughout this study the following conversion factors have been used: 1 metric ton = 7.3 barrels. 1 metric ton per year = 50 barrels per day.

[b] Including supplies obtained from North America. The difference between the availabilities of crude and refined oil is largely due to gross exports to North America and Eastern Europe and stock changes.

Sources: ECA, *Statistical Summary of Individual Plans for the Development of World Oil Production, Refining and Trade (Excluding North America and Eastern Europe), 1948 to 1953,* Washington, D.C., September 12, 1949, Tables 8 and 9. ECA, *Congressional Presentation Material,* March 10, 1950; published in *Petroleum Study,* Hearings before a subcommittee of the House Committee on Interstate and Foreign Commerce, February to May 1950, Washington, D.C., 1950, p. 118. These hearings are subsequently referred to as: *Petroleum Study.*

Iranian, are linked together by jointly held concessions, by joint ownership of wells, refineries, pipe lines and other facilities, and by the sharing of output and inter-company purchase agreements.[5] In the disposal of products, certain standard percentage shares of the companies have evolved in some markets and assumed a measure of stability; e.g., 28 1/2 and 7 per cent, respectively, for the shares of Jersey Standard and Caltex affiliates in the United Kingdom gasoline market. Market sharing has been encouraged by governments of importing countries through the allotment of import quotas to major suppliers.

Interlacement of production and market sharing seems to have superseded generally the acute struggle for supremacy between the British and American companies that was so pronounced in the 1920's and 1930's, although the emergence of Caltex as a major factor has invigorated competition. Such competition as does exist is often more pronounced between American companies than between the American and British companies as groups, largely as a consequence of exchange controls. On the whole, the two groups at present seem content to proceed with the orderly sharing of major existing markets and to limit their competition to marginal areas.[6] While the British restrictions of dollar oil sales have been explained by some domestic oil men as part of a major drive to conquer the international oil market for the British companies, neither the stated intentions of the British Government nor the timing of the restrictions, nor finally the nature of the settlements gives support to this explanation.[7] The preference of the British

[5] For example, Standard (N.J.) and Socony own the Iraq Petroleum Company jointly with Shell, Anglo-Iranian and a French government company, and share output in the same proportions as their capital. Gulf shares the Kuwait concession with Anglo-Iranian, is bound by contract not to sell in any marketing areas served by Anglo-Iranian, and regularly sells most of its crude oil from this source to Shell. Standard (N.J.) and Socony have a 20-year agreement with Anglo-Iranian for large purchases of Iranian oil. Standard (N.J.), Socony-Vacuum, and Anglo-Iranian jointly own the Middle East Pipeline Company. (Raymond F. Mikesell and Hollis B. Chenery, *Arabian Oil*, Chapel Hill, 1949.) Other joint Anglo-American oil ventures can be found in Canada, Germany, Austria, the East Indies and South America.

[6] In 1948, American companies had 39 per cent of the total refinery throughput of the world excluding North America and Eastern Europe, British companies 52 per cent, others 9 per cent. On the basis of independent company estimates for 1953, the share of American companies in that year has been put at 37 per cent, that of the British at 47 per cent, and that of others at 16 per cent. The ratio of American to British throughput volume remained constant at 1 to 1.3. Source: ECA, Petroleum Branch, *Statistical Summary of Individual Plans for the Development of World Oil Production, Refining and Trade, 1948 to 1953*, Washington, D.C., September 12, 1949 (mimeo.), Table 2.

[7] Herbert Feis, economic advisor of the State Department during the last war, judged similarly the view expressed by American oil companies in 1943 that the British were exerting themselves to oust or injure their American rivals in the Middle East. "They were imprints left by the earlier struggle to gain admission into a secluded and guarded area. Diligent questioning revealed little more than a state of mind." *Op. cit.*, p. 110.

government for a stable sharing of international oil markets appeared as no less definite than that of the American companies as a group. The intricate connection between government and oil companies in Britain, including the controlling share of the British government in the Anglo-Iranian group, is of course well known; but it is of no greater significance for Britain's conduct in the recent oil conflict than is the close cooperation existing on many issues between the major American oil companies and the United States Government.

In both countries, international oil matters are recognized as being of greatest importance to foreign commercial, political and strategic relations. Since World War I, both the British and American governments have frequently lent active support to the expansion of their nationals' interests in oil abroad;[8] and American and British commercial and political interests have clashed repeatedly in the process. But in the setting of 1949 that historic conflict hardly offered a satisfactory explanation of Anglo-American disagreement over oil. In both countries, companies and governments were drawn into a dispute over oil markets by tensions in broad demand and balance-of-payments developments that arose in the joint pursuit of greater over-all interdependence. These tensions produced the general problem of sterling inconvertibility as well as the particular and confusing division between dollar oil and sterling oil. To ascribe them primarily to a commercial or political imperialism was temptingly easy but deceptive.

2. Dollar Cost of Oil

Dollar outlays related to oil may appear in the purchase of oil products, or in their production, processing, transportation and distribution. Oil bought from American companies normally leads to a dollar claim on the foreign exchange supply of the buyer's country. American oil companies operating abroad, like domestic concerns, seek dollar earnings from their sales not only to remit profits and to amortize invested capital, but usually also to pay dollar salaries and buy dollar input supplies. The production and handling of oil costs dollars wherever royalties or taxes to concession-granting governments must be paid in dollars or some equivalent (e.g. gold) and whenever drilling, piping or refinery equipment must be bought from American firms, "dollar tankers" must be employed, or American patents or other services must be paid for. As far as the trade in oil is concerned, only American companies necessarily have to claim conversion of their earnings into dollars, at least

[8] For an account of policy developments, see *Hearings*, Special Senate Committee Investigating Petroleum Resources, *American Petroleum Interests in Foreign Countries*, Washington, D.C., 1946, *passim*; and Willard L. Thorp, *Effects of Foreign Oil Imports, op. cit.*, p. 95.

in part, while in production, refining, transportation and marketing an oil company controlled by nationals from any country may have to make dollar expenditures. When the impact of the oil trade on a country's balance of payments is to be established, dollar outlays on oil purchases and on oil production, etc., have to be considered.

Until 1949/1950, American international oil companies could be considered as dealing almost completely in dollar oil in both the trade and production sense. They claimed full payment in dollars for oil sold; they paid most of their royalties and taxes, e.g., to the Venezuelan and Saudi-Arabian governments, in dollars or instruments bought with dollars (gold sovereigns); they bought the bulk of their material, equipment, and commissary supplies from the United States and hired their non-native personnel there.

The British companies on the other hand were only partially engaged in dollar trade. A large part of production expenses in Iraq, Indonesia and other Eastern Hemisphere areas could be paid in sterling and related currencies. But in Venezuela, Shell had to pay royalties and taxes —recently upward of 50 per cent of profits—with dollars and, like American companies, buy all local currency needed with dollars—at a special and unfavorable exchange rate. Except for the profits remitted to owners in Britain, Holland, etc., and some salary payments, practically all the outlay of Venezuelan Shell took the form of dollars. Also, in Iran the British government had to convert a sizeable part of Anglo-Iranian royalty payments to the Shah's government into dollars to satisfy its requirements for imports from the United States. Much of the oil equipment needed for expansion and maintenance of facilities anywhere in the world had to be bought in the United States in the early postwar years, and American or Panamanian tankers had to be chartered. On the other hand, income from the oil sold by British companies in the sterling area and many other countries came in sterling form. Only in the United States, Canada and some Latin countries did they sell for dollars and, in the case of Shell, earn dollar profits through the domestic operations of American subsidiaries. These dollars had, of course, to be turned over to the British Government's dollar pool, which in turn provided the dollars for the companies' expenditure.

This difference between British and American-controlled companies with regard to dollar costs probably increased in 1949. Growing supplies of oil, transportation equipment, materials and shipping services became available outside the United States, particularly in Britain, and were sought by or allotted to British companies under their government's, if not ECA's, admonitions to save dollars. The British oil equipment industry more than doubled its export deliveries from 1946 to mid-1950

and broke the near-monopoly of the American industry that existed before the war. Since the fall of 1949, Iran's conversions of royalty earnings into dollars have probably declined, owing to the opening up of non-dollar sources of goods.[9] Thus, the British companies lowered the dollar component in the cost of their oil. This probably was not the case with the American companies operating in Latin America, the Middle East and Far East, partly owing to a lack of the pressures to which the British companies were subject, partly owing to British policies aimed at preventing the intrusion of American companies into the flow of sterling within the sterling area and between Britain and her trade agreement partners. This policy made it difficult for certain American companies to carry out a program of gradual shifts of input purchases from dollar to non-dollar sources that was conceived in the later part of 1949. Some American companies even shifted purchases from British and other foreign to United States sources in 1949 as the recession eased supplies and prices in this country.

Thus it came about that at the end of 1949 the dollar cost of British and American company oil to Britain differed very greatly. In an important memorandum issued in February 1950 to the American oil companies via the State Department, the British government provided data that made it possible to estimate the difference.[10] For 1950, Britain expected to pay about $535 million in dollars in connection with the production, marketing, etc., of 80 million tons of crude oil and oil products by British-controlled oil companies inside the sterling area and elsewhere.[11] She expected the operations of American companies in the sterling area to lead to dollar claims amounting to about $350 million (plus $12 million in other currencies) in return for about 13 million tons of oil. The *dollar* cost of oil operations of the British companies appears as $6.69 per ton (gross) or about 92 cents per barrel, that of the American-company oil sold in the entire sterling areas as $27.00 per ton—on the assumption of full conversion of sterling earnings into dollars—or about $3.69 per barrel, i.e. four times as much.[12]

These estimates refer to extremely complex commercial, financial and possibly transport transactions. Since their basis has not been published it is impossible to check their comparability in terms of inclusive-

[9] The monthly average of British exports to Iran in the first five months of 1950 was 5 per cent above, that of United States exports 48 per cent below, the 1949 average.

[10] This memorandum was published in the *Journal of Commerce* on February 14, 1950. It is henceforth called the *February Memorandum.*

[11] Thirty million tons in the United Kingdom and the sterling area, 50 million tons elsewhere.

[12] On the other hand, the British companies expected to earn $260 million in dollars through their trade with North America. The net dollar cost of their operations to Britain thus appeared as $3.44 per ton of oil handled.