

## GULF ANALYSIS PAPER



## SUMMARY

An energy revolution fueled by the rapidly growing production of unconventional oil and gas is under way in the United States today, but its effects so far on the Gulf Cooperation Council (GCC)—which still produces nearly a quarter of the world's oil—have so far been strikingly limited. Nonetheless, it would be simplistic to claim that new North American production will barely affect the region. The U.S. boom has a profound strategic impact on the GCC. It feeds an existing narrative of a coming U.S. abandonment of the Gulf and a need to find alternatives to U.S. security partnerships. For the Gulf states, no ready alternatives are apparent. In part as a consequence, the Gulf states are increasingly proactive in the economics and politics of the surrounding states, which has its own impact on U.S. diplomatic and security policy in the Middle East. ■

## The New Energy Revolution and the Gulf

By Carolyn Barnett

.....

A half century ago, huts lined the water in cities like Doha and Abu Dhabi. Riyadh and Kuwait were little more than villages. The countries that now make up the Gulf Cooperation Council (GCC) were desert backwaters then, but they were well placed to benefit from an impending upheaval.

In the 1960s and 1970s, global energy markets underwent major changes, and oil-producing governments decisively shifted the rules governing oil earnings in their own favor. In most cases, they were able to leverage their resources to boost national power. Since then, sleepy fishing towns, trading ports, and caravan stops in the Gulf have transformed into gleaming cities with subways, megamalls, and iconic skyscrapers. The GCC countries have become central players in international security arrangements, trade, and finance—all as a result of policies and ambitions built on their role in global energy markets. The United States has put special focus on the Gulf for many decades. This is in part because the United States replaced the United Kingdom in 1971 as the dominant great power in the Gulf, as part of its global role as a guarantor of global security. In addition, as U.S. fuel consumption grew, the United States grew increasingly tied to global energy markets in which Gulf states were dominant, creating an even more pointed U.S. interest in Gulf security.

Today, a revolution in energy production is under way in the United States, one that could lead to a new turning point in energy dynamics globally. In a reversal of the events a half century ago, U.S. energy demand growth is flattening, and after decades of lower output, U.S. production is soaring, though the United States remains a net oil importer. The rapid and dramatic growth

### GULF ANALYSIS PAPERS

In conjunction with its Gulf Roundtable series, the CSIS Middle East Program issues periodic policy papers addressing key economic and security issues in the Gulf region. Launched in April 2007, the Gulf Roundtable series convenes monthly and assembles a diverse group of regional experts, policymakers, academics, and business leaders seeking to build a greater understanding of the complexities of the region and identify opportunities for constructive U.S. engagement. Topics for discussion include the role of Islamist movements in politics, the war on terror, democratization and the limits of civil society, the strategic importance of Gulf energy, media trends, trade liberalization, and prospects for regional integration. The roundtable defines the Gulf as the United Arab Emirates, Saudi Arabia, Oman, Qatar, Bahrain, Kuwait, Iraq, and Iran and is made possible in part through the generous support of the Embassy of the United Arab Emirates. ■

in North American unconventional energy production has completely changed the conversation about energy in the United States, from one about how to secure import needs to one about how to manage export desires. Producers and industry analysts in the United States sometimes struggle to convey to laypeople just how dramatic the change has been.

Yet this energy revolution is unlike the revolution of forty years ago, and it seems unlikely to transform the Gulf directly. In some ways, the effects of the unconventional energy revolution for the GCC are similar to the ways the GCC states experienced the Arab uprisings of 2011: turbulence abroad, some domestic unrest, heightened uncertainty, and perceptions of threat—but no radical changes at home. That is to say, a revolution is under way, but it's going on somewhere else.

The six countries still produce nearly a quarter of the world's oil.<sup>1</sup> Global oil demand remains relatively robust, and U.S. production has probably had a greater role insulating prices from spikes due to supply interruptions than in collapsing global prices.

**While the economic impact is limited, especially in the short term, the U.S. boom has a profound strategic impact on the GCC.**

How can such a fundamental revolution in the world's largest energy consumer have so little impact among some of the world's largest producers? Several factors, discussed below, contribute to the limited direct economic impact of the U.S. unconventional energy boom on the GCC. The most important (and simplest) reason is that, taken as a whole, the world's hunger for energy has grown and will continue to grow. But while the economic impact is limited, especially in the short term, the U.S. boom has a profound strategic impact on the GCC. The unconventional revolution in North America is feeding an existing narrative of a coming U.S. abandonment of the Gulf and a need to find alternatives to U.S. security partnerships. For the Gulf states, no ready alternatives are apparent, and the

uncertainty comes at a time of increasing apprehension about their domestic security environment. In part as a consequence, the Gulf states are increasingly proactive in the economics and politics of the surrounding states, which has its own impact on U.S. diplomatic and security policy in the Middle East.

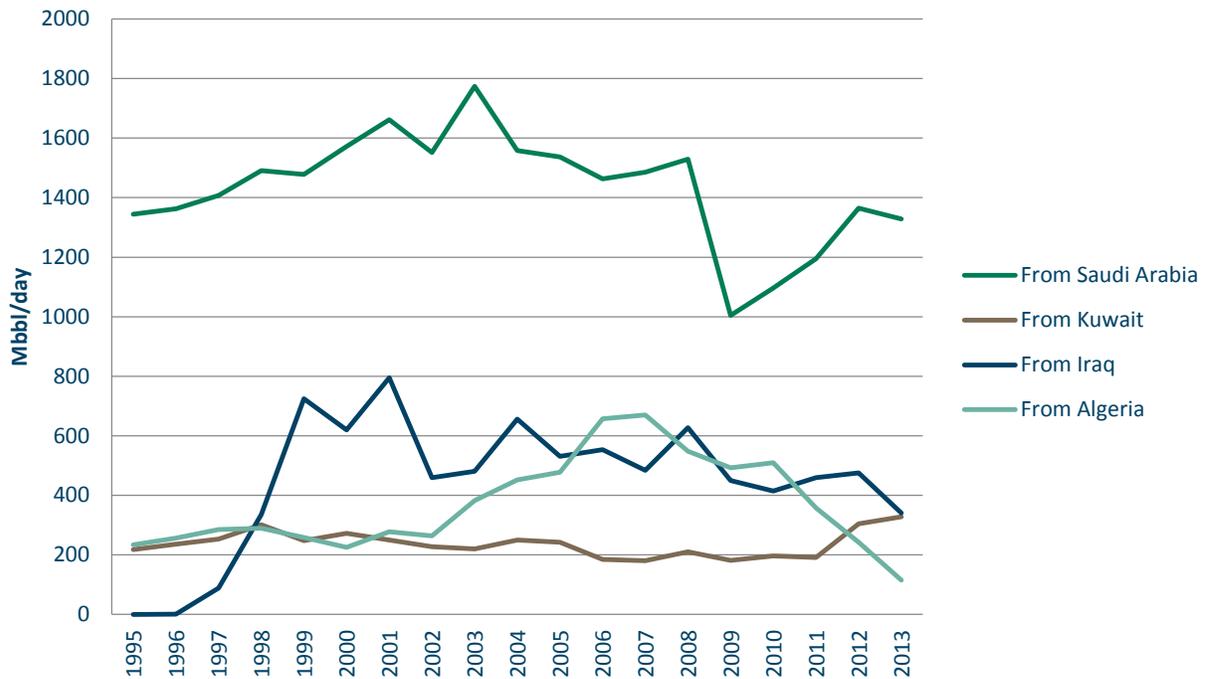
## THE U.S. UNCONVENTIONAL BOOM

Today, the United States is in the midst of a new energy revolution. Expansion of U.S. production of unconventional oil and gas since 2011 has overturned many long-held assumptions about the future of global energy markets. The United States has added nearly 3 million barrels of oil per day (bbl/d) of production since 2008—growth greater than the total production of the United Arab Emirates (UAE), the world's eighth-largest oil producer. The United States recently surpassed Russia as the world's largest oil and natural gas liquids producer, and the U.S. Energy Information Administration (EIA) projects the United States will produce an average of 9.5 million bbl/d of crude oil by 2015.<sup>2</sup> That would be a production total not much less than what Saudi Arabia currently produces. Consumption in the United States, meanwhile, is projected to remain relatively flat.

Unconventional gas production is also booming. As recently as 2006, projections showed the United States becoming increasingly dependent on natural gas imports. Much has changed in the interceding years; the 2014 EIA projections indicate that the United States will become a net natural gas exporter in 2018. (For more on the dynamics and impact of the U.S. shale boom and its global implications, see the CSIS Energy and National Security Program's recent report, *New Energy, New Geopolitics*).<sup>3</sup>

The success of unconventional production in the United States has naturally raised questions of whether similar production booms will follow elsewhere. Among GCC countries, Saudi Arabia and the UAE have begun to produce unconventional gas resources to help meet rising domestic demand. Saudi Arabia's first production came online in 2013, and it is exploring the potential to produce unconventional natural gas in multiple areas,<sup>4</sup> amidst efforts to double its total gas production.<sup>5</sup> The UAE has begun developing resources in the western region of Abu Dhabi.<sup>6</sup> Qatar has had a moratorium on gas exploration in

## U.S. Imports of Crude Oil and Petroleum Products



Source: U.S. Energy Information Administration

its North Field since 2006, now extended through 2015. Rapid developments in unconventional production in the Gulf do not seem imminent.

For other oil producers in the Middle East, questions about unconventional oil or gas production seem premature. Libya, Iran, and Iraq are struggling with conventional production—Libya because of disruptions ensuing from its revolution and ongoing civil strife, Iran because of sanctions, and Iraq potentially due to its new political turmoil. The greatest near-term challenge for these countries is not U.S. unconventional production—it is solving the political problems that have impeded their ability to produce and export oil, regardless of what happens with energy production in the United States. As oil prices have fallen, these countries' challenges have only grown, because companies have less incentive to operate in high-risk environments when demand is slack and profit margins have shrunk.

### LIMITED DIRECT IMPACTS

For the Middle East, until the recent price slump, oil prices remained high compared to historical levels. They likely

would have been even higher without U.S. unconvensionals. Indeed, at a meeting in July 2014, the Organization of the Petroleum Exporting Countries (OPEC) decided not to revise production targets, citing ongoing difficulty meeting high demand for oil and a high level of unplanned OPEC production disruptions.<sup>7</sup> Saudi Arabia even anticipated needing to raise its production to meet demand for OPEC oil. Even as prices have fallen, veteran analysts point to slower demand growth in Asia and robust inventories, rather than rising U.S. production, as the unexpected factors driving prices down.<sup>8</sup>

Despite the fact that total U.S. oil imports declined by 2.12 million bbl/d between March 2010 and July 2014, U.S. imports from the Gulf actually rose slightly in that same period, by 240,000 bbl/d. In July 2014, the United States imported 1.2 million bbl/d of oil from Saudi Arabia (13 percent of imports that month) and 375,000 bbl/d from Kuwait (4 percent)—similar to the volumes imported from those countries for much of the 1990s and 2000s.<sup>9</sup> The impact has been felt elsewhere. For example, U.S. imports from Libya and Iraq have declined by nearly 50 percent since 2007 and 2008, respectively,<sup>10</sup> and U.S. imports from Algeria have dropped by 80 percent since 2010.<sup>11</sup> U.S.

imports from other members of OPEC in Latin America and Africa have fallen as well.

The real growth markets for GCC producers have long been in Asia. Emerging economies—led by China—account for nearly all global net energy demand growth.<sup>12</sup> China, Japan, and South Korea were three of the top five net oil importers in 2013, and GCC countries supplied 34 percent, 74 percent, and 71 percent of their crude oil imports that year, respectively.<sup>13</sup> On the gas side, Qatar supplies a third of South Korea’s and China’s LNG (liquefied natural gas) imports, and 18 percent of Japan’s LNG imports; the UAE and Oman are also important LNG suppliers for Japan and South Korea.<sup>14</sup> Asian countries are nervous about their own energy security; for example, the recent gas deal signed by Russia and China demonstrates China’s eagerness to lock in supplies. GCC countries will continue to enjoy high demand from Asian consumers, with whom they have cultivated strong relationships. Even though weakening demand from Asia has contributed to the recent price declines,<sup>15</sup> and Asian demand growth may not be as robust as Middle Eastern suppliers would like in the future, its growth remains stronger than OECD demand growth.

**Qatari officials have indicated that they see the U.S. unconventional gas boom as an investment opportunity for them.**

The future of gas markets is even more difficult to predict at present than the future of oil markets, and that uncertainty affects Qatar more than any other Gulf state. But even here the impacts of North American energy production have been minimal. Qatar is among the world’s top producers of natural gas, and it remains the world’s largest LNG exporter. Qatar exports most of the gas it produces via LNG terminals, and 93 percent of that is shipped to Asia and Europe.<sup>16</sup> Most of Qatar’s exports are secured through sales and purchase agreements through at least 2020, and Qatar has demonstrated its ability to secure market share

amidst strong competition.<sup>17</sup> While the overall impact of the U.S. revolution on Qatar’s market position is hard to predict, Qatari officials have indicated that they see the U.S. unconventional gas boom as an investment opportunity for them. Qatar, the UAE, and Saudi Arabia have all expressed interest in investing in U.S. and Canadian unconventional energy projects,<sup>18</sup> and Qatar is already a partner with Exxon in one such venture<sup>19</sup>—the goal being to leverage their significant financial resources to share in the benefits of expanding production abroad. Finally, Qatar also remains a major oil exporter. Even as Qatar has become a major natural gas producer and exporter, it still earns about as much money from oil as from gas.<sup>20</sup>

## AN ERA OF UNCERTAINTY

Despite the foregoing, it would be simplistic to claim that new North American production will barely affect the Gulf.<sup>21</sup> The uncertainty that U.S. unconventional developments beget has multiple impacts that fall into two buckets: (1) uncertainty about the United States’ global role and intentions, which affects foreign policy decisionmaking in the Gulf; and (2) uncertainty about markets, which drives domestic resource allocation.

### *1. The United States as an Uncertain Superpower*

The U.S. energy revolution arrived just as the Arab uprisings and enduring sectarian violence in Syria and Iraq heightened the threats GCC leaders perceived. At least superficially, observers saw growing U.S. energy production as a sign of rising “energy independence.” The effect was to make Gulf states skeptical of U.S. intentions toward them precisely at the moment they were feeling most vulnerable.

Of course, high energy prices created a different kind of independence for the Gulf states. Saudi Arabia and the UAE have sought to respond to what they see as emerging, region-wide efforts by political Islamists (especially the Muslim Brotherhood) to assume power; domestic threats to their own political systems; and provocative Iranian behavior. In response, they intervened militarily in Bahrain to help quell an uprising, and Saudi Arabia alone pledged more than \$8 billion in 2011 to support Bahrain, Oman, and Yemen (though disbursement of the aid has stalled).<sup>22</sup> Both countries have also provided financial aid for military and humanitarian purposes in connection with the civil war in Syria, where GCC leaders oppose President Bashar

**The U.S. energy revolution arrived just as the Arab uprisings heightened the threats GCC leaders perceived.**

al-Assad's continued rule. Along with Kuwait, they have assisted Egypt with pledges of more than \$12 billion in cash, loans, and fuel assistance<sup>23</sup> as well as political support and advice. The UAE, as well, contributed to the international military intervention in Libya and has helped to shepherd efforts to boost Egypt's economic reform and growth under President Sisi.<sup>24</sup> Qatar, on the other hand, supported Muslim Brotherhood-led governments and other Islamist groups in Tunisia, Libya, Egypt, and Syria. Qatar's ambitious gamble on the future role of Islamist politics in the wake of the Arab uprisings reflected its leadership's determination that security for Qatar rests on maintaining a broad array of partnerships and its stature as an important player in the international community.<sup>25</sup> High oil prices did not cause these actions, but they have bolstered GCC governments' ability to pursue their objectives.<sup>26</sup> Lower oil prices could constrain their ability (or at least their willingness) to be so financially generous to their neighbors.

The GCC's new activism is a reaction to regional upheavals, but it also reflects the impact of a narrative that emerged over the past few years of a coming U.S. abandonment of the Gulf. Leaders of many of the status quo-supporting states in the Middle East think that the United States has entirely misunderstood and mishandled the region since the Arab uprisings began, when the United States, in their view, abandoned a close ally in Egypt with little hesitation. With the region in turmoil, they find current U.S. advice not merely unhelpful, but actually dangerous.<sup>27</sup> Several concurrent U.S. actions and trends drive GCC leaders' concerns over the reliability of U.S. security guarantees to them.

First is the U.S. willingness—and some GCC leaders would argue, eagerness—to negotiate with Iran on its nuclear program.<sup>28</sup> Apart from specific concerns over the negotiations themselves, which GCC leaders criticize as

insufficiently considerate of their concerns about Iranian support for Shi'a proxies around the region that threaten their security,<sup>29</sup> the long-term fear is that normalized U.S.-Iranian relations would weaken the U.S. commitment to GCC security. That is of particular concern given that GCC leaders are well aware of their reliance on the United States. Acknowledging this dynamic, Saudi Prince Bandar bin Sultan reportedly stated in fall of 2013 that Saudi Arabia might seek to “shift” away from the United States in part due to Washington growing closer to Tehran; the source who reported the prince's sentiments stated that “Saudi doesn't want to find itself any longer in a situation where it is dependent.”<sup>30</sup>

U.S. inaction across the Middle East and the announced “Pivot to Asia” reinforced the sense that Gulf leaders might be in a one-sided partnership. President Obama's decision not to conduct airstrikes on Syria in September

**Opinion leaders in the region also lambasted the Obama administration's lack of enthusiasm for the overthrow of President Mohammed Morsi in Egypt.**

2013, shortly after Assad apparently deployed chemical weapons against civilians, proved particularly frustrating.<sup>31</sup> Opinion leaders in the region also lambasted the Obama administration's lack of enthusiasm for the overthrow of President Mohammed Morsi in Egypt.<sup>32</sup> While the United States still maintains a large military presence in the Gulf, the much-discussed intention to shift the balance of forces toward the Asia-Pacific (where important long-term interests lay) also contributed to a sense, which took on “a life of its own,” that the United States had disengaged from the region.<sup>33</sup>

Adding to this are a confluence of governance and public opinion challenges in the United States, which indicated to foreign leaders that even when the United States wants

to extend its commitments to them, it might not always be able to fulfill them. Some observers have suggested that overtures to Iran represent an attempt to distract the American people from failed wars in Iraq and Afghanistan and “a sharp decline in their country’s economic growth, increased unemployment, and rising debt levels.”<sup>34</sup> The effect of sequestration on the Department of Defense and the seeming inability of the U.S. Congress to take any actions of consequence have been noticed abroad. Government shut-downs, the fight over the Affordable Care Act, the struggle to create a functional healthcare.gov web site, and deepening polarization have led foreign observers to wonder what the United States is able to do.<sup>35</sup> In addition, the U.S. public remains largely averse to new military entanglements. While public opinion has broadly supported the current airstrikes in Iraq and Syria, interest in any broader offensives has remained limited, and GCC leaders can see how that constrains potential U.S. action on their behalf. Seen from the Gulf, these factors combine to signal a U.S. retreat from the region, which they see as part of a broader shift in the U.S. approach to global leadership.<sup>36</sup>

**Rhetoric about energy independence—  
which both U.S. political parties employ—  
suggests the United States can free  
itself from hopeless problems and  
troublesome allies.**

The problem for GCC leaders is that no one else can or will provide the security guarantees to them that the United States does. China has yet to build the capability or demonstrate the willingness to fill the kind of role the United States currently does, despite its reliance on the Gulf for energy. Europe’s military strength is waning. Any guarantees Russia could offer would be treated warily—and in any case, Russia’s steadfast support for Assad has set it at odds with GCC leaders.

The U.S. energy revolution did not create these dynamics,

but it feeds into them. Rhetoric about energy independence—which both U.S. political parties employ<sup>37</sup>—suggests the United States can free itself from hopeless problems and troublesome allies and encourages perceptions that the United States is a fair-weather friend. That provides little incentive for leaders to rethink regional policies and goals which are separate from and often indifferent to those of the United States.

The recent formation of a coalition to conduct airstrikes against the Islamic State militant group in Iraq and Syria, which all six GCC states support to varying degrees, might seem at first to alleviate some of these concerns. But GCC leaders likely interpret the U.S. decision to target the Islamic State as a blip in current trends in U.S. policy rather than a reversal of it. First, even amidst the height of popular support in the United States for action in Iraq and Syria, the Obama administration has continued to advocate and insist upon limited air support and weapons provision to groups fighting the Islamic State rather than a more significant direct U.S. involvement—“no boots on the ground” has remained the mantra. U.S. support for opposition fighters in Syria is reportedly limited to strengthening their capacity to defend territory from which the Islamic State retreats, rather than empowering them to attack the Islamic State,<sup>38</sup> as Gulf leaders would surely prefer. Moreover, the strength of the coalition as a partnership is unclear. The Pentagon has stopped publicly commenting on the contributions of Gulf Arab coalition members to the military effort,<sup>39</sup> either out of respect for concerns that those governments might face domestic blow-back, or because their contributions have diminished. And Gulf frustration at U.S. policymakers’ attitudes toward the Gulf has not gone away: there were loud protests from Gulf diplomats after Vice President Joe Biden stated in early October that “our biggest problem is our allies”—including Saudi Arabia and the UAE.<sup>40</sup>

Most importantly, the joint effort against the Islamic State has not changed the fact that fundamental policy aims and interests remain at odds. U.S. aims appear limited to dealing with the threat the Islamic State poses to civilian populations and the territorial integrity of Syria and Iraq, while mitigating the risk of attacks on U.S. soil. Gulf members of the coalition maintain more ambitious goals of toppling Bashar al-Assad and, ideally, pushing back against Iranian influence with the new government in Iraq in the context of their broader regional cold war with Iran.

## Economic Resources of GCC States

Country	GDP in 2014 (\$US billions)	General government gross debt in 2014 (% of GDP)	Gross national savings in 2014 (% of GDP)	Estimated sovereign wealth fund holdings (\$US billions)	Foreign currency and gold reserves in July 2014 (\$US billions)
Bahrain	34.05	47.07	25.87	10.5	5.68
Kuwait	179.33	5.9	54.76	410	31.25
Oman	80.54	8.13	38.31	19	17.41
Qatar	212.01	25.47	56.02	170	43.04
Saudi Arabia	777.87	2.58	45.83	762.5	58.03
UAE	416.44	11.43	33.46	1,078.5*	73.50**

Sources: IMF World Economic Outlook database (2014 staff estimates); SWF Institute estimates; GCC central bank statistical bulletins

\*Combined estimated value of ADIA, ADIC, Emirates Investment Authority, IPIC, Investment Corporation of Dubai, and Mubadala

\*\*UAE data from June 2014

The fact that negotiations over Iran's nuclear program continue, no matter how events evolve as the participants near the November 24 deadline for reaching an agreement, still rankles Gulf Arab leaders who would prefer a more comprehensive approach to reining in Iranian actions around the region.

These trends have only reinforced GCC leaders' perceptions that they can and should be more proactive in defense of their own interests around the region. Saudi Arabia and the UAE have continued to play an active role overseeing Egypt's path forward under President Sisi, and the UAE is reported to have provided aircraft used to bomb forces opposing General Khalifa Hiftar in Libya earlier this fall.<sup>41</sup> Egypt, the UAE, Saudi Arabia, and Kuwait are also reportedly discussing a regional alliance to combat Islamic militants in Libya, Yemen, and around the region.<sup>42</sup> A more active Gulf role around the region does not necessarily conflict with U.S. interests, but it does drive events in ways that affect U.S. options in the region.

### 2. Market Uncertainty and High Domestic Stakes

While some of the GCC concern is at the political and strategic level, a whole other set of concerns relate to the practical and commercial consequences of unconventional energy, especially as the future seems increasingly unpredictable. Some in the GCC have warned that their

leaders need to take the competitive threat from U.S. unconventional production more seriously.<sup>43</sup> Some analysts also argue that a global turn away from oil to other sources of energy, growing energy efficiency, and the possibility of dampened demand from Asia all undermine the long-term demand for OPEC oil and the long-term outlooks of most Middle Eastern economies.<sup>44</sup> Recent price declines complicate this picture even further: on the one hand, cheaper oil could help stave off fuel switching to other sources of energy, bolstering producers' market power in the long term. On the other hand, lower oil prices mean fewer revenues for GCC governments.

The GCC countries can accommodate a short-term oil price drop. Years of high oil prices have helped governments save, invest, and reduce government debt. Saudi Arabia, Kuwait, Qatar, and the UAE all have robust sovereign wealth funds that they have used to invest in diverse holdings around the world. Their government debt as a percentage of GDP is low, and their central bank reserves, savings, and investments are large (see chart above). Bahrain and Oman are more vulnerable, but they may rely to some extent on the generosity of their GCC neighbors.

A more sustained decline in oil revenues, however, would strain Gulf economies. GCC governments face rising public spending commitments, particularly for social welfare and

water and energy subsidies—and these commitments have grown in response to concerns about unrest since the Arab uprisings began.<sup>45</sup> GCC governments still get most of their revenue and export earnings from oil and gas, and most activity in GCC economies is ultimately derived from oil and gas revenue.<sup>46</sup> If oil revenues stay low, governments will eventually be forced to face more sensitive budgetary decisions about spending on public salaries, housing, education, and health care. Low oil prices could also put downward pressure on oil-linked natural gas prices, which would reduce Qatar’s revenues.

During past periods of suppressed revenues due to low oil prices, countries in the region often prioritized spending on the most politically sensitive categories (those that affected the most people most immediately) over investments that would drive future non-oil economic activity and growth. When Saudi Arabia faced sustained low prices and large budget deficits in the 1980s and 1990s, for example, it made some peripheral spending cuts, but primarily it relied on a twofold strategy for covering its revenue needs: it took on large amounts of debt, and it exercised what diplomacy it could to try to influence world prices and its own market share.<sup>47</sup>

Planning for future growth may also suffer. In the UAE, scares associated with oil price slumps contributed to an accelerated urge to diversify the economy, particularly in Dubai.<sup>48</sup> But the federal government shelved strategic development plans in the 1980s due to lack of resources to implement them—which ultimately led to uncoordinated development.<sup>49</sup> This occurred even as overall budgets, spending on social programs, and budget deficits alike grew.<sup>50</sup> In Qatar, reduced revenues led to stalled and then declining government spending as well as budget deficits from the mid-1980s into the 1990s.<sup>51</sup> The very small size

**In the face of falling revenues, governments will likely spend existing resources and take on debt before making spending cuts they fear would provoke opposition.**

**Changing global energy market dynamics will affect whether other regions deem stability in the Middle East vital to their own interests, and what they are willing to do to ensure that stability.**

of Qatar’s population meant that social spending was not disrupted, but economic pressures prompted leaders to accelerate their effort to develop a “civic myth” justifying the Al Thanis’ rule, and economic mismanagement may have contributed to support among ruling family members for the 1995 coup.<sup>52</sup>

These countries made it through the years of low prices—warnings about their stability are not new—but decisions they made in response to low prices hurt their overall macroeconomic health and outlook. For years, the experience has fueled their sense that diversification is urgent, and the current shifts in global energy markets are a reminder that rapid and unexpected changes can occur in the market in which these countries make their living. These shifts may intensify governments’ desire to diversify their investments and sources of income, potentially bringing new urgency to efforts to reform their economies.<sup>53</sup> Alternately, the political vulnerabilities GCC states face could lead instead to a renewed focus on the short term, as they feel pressure to maintain or even expand spending on public welfare. In the face of falling revenues, governments will likely spend existing resources and take on significant debt before making spending cuts they fear would provoke opposition, in the hope that more lucrative times would return soon enough. If they follow this path, their ability to commit to the diversification efforts they know to be necessary will erode. They will also have fewer resources available for making the investments in energy and industry infrastructure that are needed to sustain those sectors in the future.<sup>54</sup>

Greater international uncertainty also makes reforming the consumption and subsidization of energy in the

GCC increasingly urgent. The EIA projects Middle East consumption of natural gas will continue to rise, nearly doubling from 13.1 trillion cubic feet in 2010 to 25.2 trillion cubic feet in 2040,<sup>55</sup> with much of this increase in the Gulf. Rising consumption of energy domestically remains a major threat to GCC states' ability to maintain or extend their export capacity.<sup>56</sup>

The possibility of a period of sustained lower prices in the context of the current unrest in the Middle East thus presents fewer immediate challenges to the GCC than it would to its neighbors, but lower energy prices and domestic energy challenges could squeeze revenues and force more difficult policy choices. Sustained low prices would complicate GCC countries' outlooks, but they are unlikely to add significantly to trouble in a region that already has plenty.

## THE NEW GAME

The growing energy production that has dramatically affected the United States has had little direct effect on the GCC so far, but it still matters for the GCC.

Uncertainty over future prices and revenues could change how GCC governments make economic decisions today, affecting their long-term economic prosperity. The same uncertainty could either limit or propel their ability or willingness to act politically across the rest of the Middle East and North Africa. How secure or threatened Gulf producers feel in the new global energy environment may shape their ability and desire to play a role in international politics beyond the region, too.

Changing global energy market dynamics will also affect whether other regions deem stability in the Middle East vital to their own interests, and what they are willing to do to ensure that stability. Consumers in both Asia and Europe are growing more dependent on energy imports, not less. Their own energy security and economic growth depend in part on whether more proactive Gulf foreign policies make for a more stable or more turbulent Middle East, and this dependence will affect their policies toward the region and how they want the United States to act there. For example, a recent analysis advises European policymakers to seek closer cooperation with the United States and the GCC on maritime security.<sup>57</sup>

Policymakers, investors, and analysts should observe these developments without expecting sudden, dramatic shifts

in the Gulf; they should instead look for subtle shifts in worldview and cost-benefit analysis in response to the unconventional revolution. Those shifts will determine how GCC countries act to ward off perceived threats and how they balance their domestic and foreign policy priorities. Those decisions will in turn affect how the United States interacts with them and the challenges and opportunities the United States faces in the Middle East. What is taking place may not be a revolution for the GCC, but it is a new game. ■

## ACKNOWLEDGEMENTS

*Sarah Ladislaw, Frank Verraastro, Guy Caruso, and Michelle Melton of the CSIS Energy and National Security Program and Jon B. Alterman provided invaluable advice and feedback on drafts of this paper. Any errors are my own.*

## NOTES

1. This share is calculated based on total oil supply figures for 2013. U.S. Energy Information Administration (EIA) International Energy Statistics, <http://www.eia.gov/cfapps/ipdbproject/IEDIndex3.cfm?tid=5&pid=53&aid=1> (accessed June 12, 2014). World oil supply was 90.33 million bbl/d in 2013. Total oil supply for the GCC countries in 2013 was as follows: Saudi Arabia—11.59 million barrels per day (bbl/d); UAE—3.23 million bbl/d; Kuwait—2.81 million bbl/d; Qatar—2.07 million bbl/d; Oman—945,000 bbl/d; Bahrain—55,200 bbl/d.

2. EIA, “Short-Term Energy and Winter Fuels Outlook (STEO),” October 2014, [http://www.eia.gov/forecasts/steo/pdf/steo\\_full.pdf](http://www.eia.gov/forecasts/steo/pdf/steo_full.pdf).

3. Sarah O. Ladislaw, Maren Leed, and Molly A. Walton, *New Energy, New Geopolitics: Balancing Stability and Leverage*, CSIS, April 2014, [http://csis.org/files/publication/140409\\_Ladislaw\\_NewEnergyNewGeopolitics\\_WEB.pdf](http://csis.org/files/publication/140409_Ladislaw_NewEnergyNewGeopolitics_WEB.pdf).

4. See Abdelgheni Hendi, “Saudi Aramco Allocates Shale Gas for Industrial Projects,” Society of Petroleum Engineers, May 27, 2014, <http://www.spe.org/news/article/saudi-aramco-allocates-shale-gas-for-industrial-projects>; Alex Edwards, “Saudi Aramco Announces Shale Gas Investment,” *Asharq al-Awsat*, October 22, 2013, <http://www.aawsat.net/2013/10/article55319936>; and “Saudi Shale Gas Drilling Bears Fruit: Aramco Head,” AFP, October 14, 2013, <http://www.globalpost.com/dispatch/news/afp/131014/saudi-shale-gas-drilling-bears-fruit->

aramco-head. Saudi Arabia has also identified potential exploitable shale gas reserves in the Empty Quarter, at South Ghawar in the Eastern Province, and in the north at al-Jalamid. See “Saudi Arabia to Test Shale Gas Viability in the Empty Quarter,” 2B1st Consulting, June 13, 2014, <http://www.2b1stconsulting.com/saudi-arabia-to-test-shale-gas-viability-in-empty-quarter/>.

5. “Saudi Aramco CEO: Oil Industry ‘Needs Timely Investments,’” *Arab News*, August 26, 2014, <http://www.arabnews.com/economy/news/620836>.

6. Kirsten Westphal, Marco Overhaus, and Guido Steinberg, *The US Shale Revolution and the Arab Gulf States*, SWP Research Paper, November 2014, [http://www.swp-berlin.org/fileadmin/contents/products/research\\_papers/2014\\_RP11\\_wep\\_ovs\\_sbg.pdf](http://www.swp-berlin.org/fileadmin/contents/products/research_papers/2014_RP11_wep_ovs_sbg.pdf), 26. SWP’s excellent report advances a similar argument to this analysis paper and was released as this paper was being finalized.

7. Wael Mahdi, Grant Smith, and Nayla Razzouk, “OPEC Keeps Output Level Below Second-Half Demand Forecast,” Bloomberg, June 11, 2014, <http://www.bloomberg.com/news/2014-06-11/opec-leaves-output-target-unchanged-at-30-million-barrels-a-day.html>.

8. Frank A. Verrastro, Lawrence Goldstein, and Guy Caruso, “Oil Markets: Trouble Ahead, Trouble Behind,” CSIS, October 10, 2014, <http://csis.org/publication/oil-markets-trouble-ahead-trouble-behind>.

9. EIA, “U.S. Imports of Crude Oil and Oil Products Monthly by Country of Origin,” [http://www.eia.gov/dnav/pet/pet\\_move\\_impcus\\_a2\\_nus\\_ep00\\_im0\\_mbb1\\_m.htm](http://www.eia.gov/dnav/pet/pet_move_impcus_a2_nus_ep00_im0_mbb1_m.htm) (accessed October 20, 2014). The amount of oil the United States imports from Qatar and the UAE is much smaller and varies from year to year.

10. Imports from Libya have also fluctuated significantly month to month since 2011 depending on the country’s security situation and oil export capacity, which since mid-2013 has been very limited.

11. EIA, “U.S. Imports of Crude Oil and Oil Products Annually by Country of Origin.”

12. International Energy Agency, *World Energy Outlook 2013* (Paris: OECD/IEA, 2013), 55.

13. EIA, “Short Term Energy Outlook,” January 2014, <http://www.eia.gov/forecasts/steo/archives/jan14.pdf>; Percentages compiled from EIA country analyses: “China: Analysis,” February 4, 2014, <http://www.eia.gov/countries/cab.cfm?fips=ch>; “Japan: Analysis,” October 29, 2013, <http://www.eia.gov/countries/cab.cfm?fips=ja>; “South Korea: Analysis,” April 1, 2014, <http://www.eia.gov/countries/cab.cfm?fips=KS>.

14. EIA country analyses of China, Japan, and South

Korea.

15. Benoit Faucon and Summer Said, “OPEC Members’ Discord Adds to Slide in Oil Prices,” *Wall Street Journal*, October 5, 2014, <http://online.wsj.com/articles/opec-members-discord-adds-to-slide-in-oil-prices-1412361852>.

16. EIA, “Qatar: Analysis,” January 30, 2014, <http://www.eia.gov/countries/cab.cfm?fips=qa>.

17. Westphal et al., *The US Shale Revolution*, 19-21.

18. “Mideast Energy Giants Invest in North American Shale,” *Zawya*, February 4, 2014, [https://www.zawya.com/story/Mideast\\_energy\\_giants\\_invest\\_in\\_North\\_American\\_shale-ZAWYA20140204102652/](https://www.zawya.com/story/Mideast_energy_giants_invest_in_North_American_shale-ZAWYA20140204102652/).

19. “Exxon and Qatar Plan to Ship US Natural Gas to Britain,” Reuters, March 10, 2013, <http://www.reuters.com/article/2013/05/10/lng-goldenpass-idUSL2N0DR33E20130510>.

20. UNCTAD international trade statistics through 2012, available at <http://unctad.org/en/pages/Statistics.aspx>. The exception was in 2011, when the value of natural gas exports slightly exceeded the value of petroleum and petroleum products exports.

21. See for example Lananh Nguyen and Grant Smith, “OPEC Sees Shale as No Threat: Welcomes Output from Iran, Libya,” Bloomberg, January 27, 2014, <http://www.bloomberg.com/news/2014-01-27/opec-sees-shale-as-no-threat-welcomes-output-from-iran-libya.html>; Sarah Kent, “IEA: Shale Gas No Longterm Threat to OPEC,” *Wall Street Journal*, November 12, 2013, <http://online.wsj.com/article/BT-CO-20131112-702859.html>.

22. International Monetary Fund, “Saudi Arabia: 2012 Article IV Consultation,” IMF Country Report No. 12/271, September 2012, p. 4, <http://www.imf.org/external/pubs/ft/scr/2012/cr12271.pdf>.

23. Not all of this assistance has been delivered. See Asa Fitch, “Gulf Nations’ Sway Rises in Egypt,” *Wall Street Journal*, July 1, 2014, <http://online.wsj.com/articles/gulf-nations-sway-rises-in-egypt-1404235734>.

24. Simeon Kerr and Heba Saleh, “UAE Focuses on Economic Reform in Egypt in Battle Against Islamism,” *Financial Times*, June 19, 2014, <http://www.ft.com/intl/cms/s/0/fa674ef0-f187-11e3-9161-00144feabdc0.html>.

25. Mehran Kamrava, “Mediation and Qatari Foreign Policy,” *Middle East Journal* 65, no. 4 (Autumn 2011), <http://www18.georgetown.edu/data/people/mk556/publication-61175.pdf>.

26. Laura El-Katiri, Bassem Fattouh, and Richard Mallinson, “The Arab Uprisings and Political Instability: Implications for Oil & Gas Markets,” Oxford Institute for

Energy Studies, March 2014, <http://www.oxfordenergy.org/wpcms/wp-content/uploads/2014/03/MEP-8.pdf>.

27. Jon B. Alterman, “A Deeper Difference,” *Middle East Notes and Comment*, January 2014, [http://csis.org/files/publication/1114\\_MENC.pdf](http://csis.org/files/publication/1114_MENC.pdf).

28. See for example Eyad Abu Shakra, “America’s Regional Blunders,” *Asharq al-Awsat*, October 3, 2013, <http://www.aawsat.net/2013/10/article55318201>.

29. Jay Soloman and Lawrence Norman, “Iran Talks Strain Mideast Alliances,” *Wall Street Journal*, November 8, 2013, <http://online.wsj.com/articles/SB10001424052702304448204579185572146100640>.

30. Amena Bakr and Warren Stroble, “Saudi Arabia warns of shift away from U.S. over Syria, Iraq,” Reuters, October 22, 2013, <http://www.reuters.com/article/2013/10/22/us-saudi-usa-idUSBRE99L0K120131022>.

31. Ibid.

32. See for example Tariq Alhomayed, “A Crisis Made in Washington,” *Asharq Al-Awsat*, July 22, 2014, <http://www.aawsat.net/2014/07/article55334540>.

33. Abdulkhaleq Abdulla, “The American withdrawal from the Middle East that wasn’t,” *Gulf News*, May 26, 2014, <http://gulfnews.com/opinions/columnists/the-american-withdrawal-from-middle-east-that-wasn-t-1.1338914>.

34. Antoine Safer, “Debate: The Gulf states will find it hard to join the Iranian nuclear talks,” *Asharq Al-Awsat*, July 21, 2014, <http://www.aawsat.net/2014/07/article55334503>.

35. See for example Hisham Melham, “Obama’s Tormentors,” *Al-Arabiya*, November 1, 2014, <http://english.alarabiya.net/en/views/news/world/2014/11/01/Obama-s-tormentors-.html>.

36. Abdullah Al-Shayji, “Overhauling the GCC-US partnership,” *Gulf News*, May 4, 2014, <http://gulfnews.com/opinions/columnists/overhauling-the-gcc-us-partnership-1.1328019>.

37. See for example “Senators Urge Majority Leader to Allow Floorvote on Keystone XL Pipeline,” U.S. Senate Committee on Energy and Natural Resources, June 24, 2014, <http://www.energy.senate.gov/public/index.cfm/2014/6/senators-urge-majority-leader-to-allow-floor-vote-on-keystone-xl>; “President Barack Obama’s State of the Union Address,” White House, January 28, 2014, <http://www.whitehouse.gov/the-press-office/2014/01/28/president-barack-obamas-state-union-address>.

38. Rajiv Chandrasekaran, “Syrians to be trained to defend territory, not take ground from jihadists, officials say,” *Washington Post*, October 22, 2014, [http://www.washingtonpost.com/world/national-security/syrians-to-be-trained-to-defend-territory-not-take-ground-from-jihadists-officials-say/2014/10/22/8ca13cf2-5a17-11e4-bd61-346aee66ba29\\_story.html](http://www.washingtonpost.com/world/national-security/syrians-to-be-trained-to-defend-territory-not-take-ground-from-jihadists-officials-say/2014/10/22/8ca13cf2-5a17-11e4-bd61-346aee66ba29_story.html).

39. Justine Drennan, “Who Has Contributed What in the Coalition Against the Islamic State?” *Foreign Policy*, October 22, 2014, [http://complex.foreignpolicy.com/posts/2014/10/14/whos\\_contributed\\_the\\_most\\_in\\_the\\_coalition\\_against\\_the\\_islamic\\_state](http://complex.foreignpolicy.com/posts/2014/10/14/whos_contributed_the_most_in_the_coalition_against_the_islamic_state).

40. Hanna Kozłowska, “Joe Biden’s Latest Gaffe: the Truth or an Ultimate Embarrassment?,” *New York Times*, October 9, 2014, [http://op-talk.blogs.nytimes.com/2014/10/09/joe-bidens-latest-gaffe-the-truth-or-an-ultimate-embarrassment/?\\_php=true&\\_type=blogs&\\_r=0](http://op-talk.blogs.nytimes.com/2014/10/09/joe-bidens-latest-gaffe-the-truth-or-an-ultimate-embarrassment/?_php=true&_type=blogs&_r=0).

41. David D. Kirkpatrick and Eric Schmitt, “Arab Nations Strike in Libya, Surprising U.S.,” *New York Times*, August 25, 2014, <http://www.nytimes.com/2014/08/26/world/africa/egypt-and-united-arab-emirates-said-to-have-secretly-carried-out-libya-airstrikes.html>.

42. Hamza Hendawi, “Egypt, Gulf Arab allies eye anti-militant alliance,” AP, November 3, 2014, <http://bigstory.ap.org/article/7da735d6ad77416d9867bb1897867345/egypt-gulf-arab-allies-eye-anti-militant-alliance>.

43. Saudi Prince Alwaleed bin Talal has stated that new shale oil discoveries in North America “are threats to any oil-producing country in the world,” contradicting statements made by leaders in Saudi Arabia’s oil ministry. Jacquie McNish, “Saudi Billionaire Sees a World Awash in Oil,” *Globe and Mail*, November 15, 2013, <http://www.theglobeandmail.com/report-on-business/international-business/african-and-mideast-business/saudi-billionaire-sees-a-world-awash-in-oil/article15472661/>.

44. Robert Springborg, “The Energy Revolution’s Impacts on the Arab World,” Middle East Institute, June 10, 2014, <http://www.mei.edu/content/article/energy-revolution%E2%80%99s-impacts-arab-world>.

45. Bernard Haykel, “Saudi Arabia and Qatar in a Time of Revolution,” CSIS, February 2013, <http://csis.org/publication/gulf-analysis-paper-saudi-arabia-and-qatar-time-revolution>.

46. According to data from IMF Article IV Consultations ([www.imf.org](http://www.imf.org)), dependence on hydrocarbons (oil and gas) for government revenue is approximately 56 percent in Kuwait and the UAE, 62 percent in Qatar, 87 percent in Bahrain and Oman, and 92 percent in Saudi Arabia. Standard & Poor’s recently released a report indicating that it sees GCC countries’ continued high reliance on hydrocarbons as their key vulnerability, with Oman and Bahrain particularly at risk. See Trevor Cullinan, “Hooked on Hydrocarbons: How Susceptible are Gulf Sovereigns to Concentration Risk?,” Standard & Poor’s Ratings Service,

June 30, 2014. For a more in-depth discussion of the nature of GCC economies' broader dependence on hydrocarbons, see Steffen Hertog, "The Private Sector and Reform in the Gulf Cooperation Council," Kuwait Programme on Development, Governance, and Globalisation in the Gulf States no. 30, July 2013, [http://eprints.lse.ac.uk/54398/1/Hertog\\_2013.pdf](http://eprints.lse.ac.uk/54398/1/Hertog_2013.pdf).

47. F. Gregory Gause III, "Saudi Arabia Over a Barrel," *Foreign Affairs* 79, no. 3 (2000): 80–94.

48. Christopher Davidson, *Dubai: The Vulnerability of Success* (New York: Columbia University Press, 2008), 107.

49. Ali Tawfik Al Sadik, "Evolution and Performance of the UAE Economy, 1972–1998," in *United Arab Emirates: A New Perspective*, ed. Ibrahim Al Abed and Peter Hellyer (London: Trident Press, 2001), 217.

50. *Ibid.*, 219.

51. "Persian Gulf States: Qatar," U.S. Country Studies, U.S. Library of Congress, <http://countrystudies.us/persian-gulf-states/77.htm>.

52. Mehran Kamrava, *Qatar: Small State, Big Politics* (Ithaca: Cornell University Press, 2013), 116, 123.

53. Andrew Torchia, "As oil price slides, Gulf's private business may benefit," Reuters, October 26, 2014, <http://www.reuters.com/article/2014/10/26/us-mideast-investment-gulf-idUSKBN0IF0CM20141026>.

54. Springborg, "The Energy Revolution's Impacts." Springborg notes that "while GCC budgets are generally in balance and sovereign debt relatively low, surplus revenues to meet escalating costs for upstream development activities are not readily available."

55. EIA, "International Energy Outlook 2013: Natural Gas," July 25, 2013, [http://www.eia.gov/forecasts/ieo/nat\\_gas.cfm](http://www.eia.gov/forecasts/ieo/nat_gas.cfm). New projections will be available in late July 2014.

56. For a more in-depth discussion of this challenge see Westphal et al., *The US Shale Revolution*, 24–25.

57. *Ibid.*, 32.

This analysis paper is produced by the Center for Strategic and International Studies (CSIS), a private, tax-exempt institution focusing on international public policy issues. Its research is nonpartisan and nonproprietary. CSIS does not take specific policy positions; accordingly, all views, positions, and conclusions expressed in this publication should be understood to be solely those of the author(s).

© 2014 by the Center for Strategic and International Studies.

## CSIS MIDDLE EAST PROGRAM

### Jon B. Alterman

Senior Vice President, Zbigniew Brzezinski Chair in Global Security and Geostrategy, and Director

### Haim Malka

Deputy Director and Senior Fellow

### Carolyn Barnett

Research Fellow

### Rebecka Shirazi

Program Coordinator and Research Associate

### Waleed Al Bassam

### Meaghan DeWaters

Interns

Please visit our website at [www.csis.org/mideast](http://www.csis.org/mideast) to learn more about the program's work.