

Strategic Importance and Challenges of Middle East Energy Problems

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I had an opportunity to visit Qatar's Doha on February 19-22 to participate in an international energy conference and exchange views with energy players in the country. As the Arab Spring destabilization, the tense Iranian situation and other geopolitical risks have led energy players in the world to pay attention to the importance of the Middle East, I would like to summarize key points that impressed me through the exchange of views in Doha.

First, I strongly felt the firm existence of a common view that the center of gravity regarding energy problems in the world has been shifting. Even at present, the United States, European countries and other industrial nations belonging to the Organization for Economic Cooperation and Development are clearly important when energy problems are considered. Over a long run, however, non-OECD countries including China, India and other Asian emerging economies will inevitably grow more important in the international energy market, as indicated by their economic and population growth. Long-term energy outlooks of the International Energy Agency and the Organization of Petroleum Exporting Countries as well as our institute have commonly projected that Asian energy demand growth will be the largest factor that moves international energy problems. The exchange of views in the Middle East gave me an opportunity to feel anew that how to respond to the growing importance of Asia is the biggest issue for energy players in the Middle East.

The Middle East's energy demand problems have also surfaced not only as an urgent challenge but also as a medium to long-term challenge. Energy policy makers in the Middle East now cannot ignore the seriousness of local energy demand problems which are accelerated by economic and population growth and policy-controlled low energy prices. While the Middle East is growingly expected to play a key role as the world's energy supply base, how to respond to substantial energy demand growth in this region can affect the region's export capacity and become a problem that cannot be ignored in the context of the world energy situation.

As Asian and Middle Eastern energy demand growth drives the global demand expansion, the relative importance of U.S. and European demand will decline. Particularly, the United States may take advantage of expanding supply of unconventional energy resources to substantially reduce demand for oil and gas imports and depend on neighbors in the Americas for energy imports. From the viewpoint of international energy trade, the strategic interdependence between Asia and the Middle East will deepen further. In this sense as well, the center of gravity may shift.

The second problem is that both the supply and demand sides must make huge investments in response to growing demand amid the shift of the gravity center. According to our institute's analysis, \$31 trillion in cumulative global investment, including \$12 trillion in Asia and \$2 trillion in the Middle East, will be required for the 2009-2035 period in the Reference Scenario where present supply and demand trends will continue. Asia and the Middle East thus account for nearly a half of the global investment. Investment targets in Asia and the Middle East are very different. This is a point of interest. While the electricity sector (including electricity generation, transmission and distribution) will account for three quarters of total investment in Asia, the oil sector will capture the largest share (\$835 billion) of total investment in the Middle East, followed by the gas sector (\$638 billion) and the electricity sector (\$600 billion). Large-scale investment will thus be required in response to demand growth in Asia and the Middle East. The problem is that there is no guarantee that timely and appropriate investment will be made.

Rather, the exchange of views has led me to find that it could be difficult to secure appropriate investment due to a mountain of uncertainties regarding growing geopolitical risks, relations between investment host countries and investors such as international oil companies, the roles of national oil companies in China, India and other countries, the destabilization of international crude oil prices, domestic energy price problems and other matters. Uncertainties over investment can also apply to the case for investment in energy conservation responding to growing demand, as well as in supply of oil, gas and other energy sources. While great energy conservation potentials can be expected, no optimism can be warranted about smooth energy conservation.

Third, I strongly recognized the importance of the abovementioned geopolitical risk problem anew through the exchange of views. Regarding the Iranian situation that has been growing tense, discussions focused on the impact of the oil embargo, and China's and India's responses. I recognized energy players' strong interests in safe passage through the Strait of Hormuz. I felt that while many energy players see Iran's Hormuz blockade as unlikely, they have serious concerns about the tense regional situation including the possibility of Israel's preemptive attacks on Iran. Based on these concerns, they are interested in the impact of some contingency situations. In this sense, we are highly required to collect and analyze relevant information.

I also became conscious that the Arab Spring destabilization and its impact on the energy situation, though having reduced their media exposure behind the dominant Iranian crisis in Japan particularly, still exist as important problems in the Middle East. The Arab Spring destabilization has not fully spilled over to major oil producing countries belonging to the Gulf Cooperation Council. Given their abundant deep-rooted and structural problems, however, we must closely watch the Middle East and North Africa situation in the future. Regarding the Arab Spring destabilization, energy players may pay attention first to oil supply disruptions such as those seen in Libya. But there may be other relevant problems. For example, major oil producing countries may now prefer higher crude oil prices to accommodate increased spending on domestic stabilization measures while sustaining balanced budgets. They may also be forced to maintain domestic energy prices at low levels for the social stabilization, failing to hold down domestic energy demand growth. The Arab Spring destabilization has thus exerted various and massive effects on the energy situation in the region.

As the importance of oil and gas in the electricity generation sector has increased in Japan since the March 2011 Fukushima Daiichi Nuclear Power Plant accident, the stabilization of international oil and gas markets has been very significant for Japan's energy security. Given this point, Japan may have to keep close watch on the Middle East situation, analyze the situation appropriately and implement resources diplomacy and other measures for securing stable energy supply.

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