

# The impact of an “America First” policy on stability in the Middle East: The impact on oil markets?

---

**Professor Paul Stevens**

Distinguished Fellow, Chatham House

Professor Emeritus, University of Dundee

Distinguished Fellow, Institute of Energy Economics, Japan

IEEJ International Energy Symposium 2017

Tokyo 18<sup>th</sup> May 2017

**CHATHAM  
HOUSE**

The Royal Institute of  
International Affairs

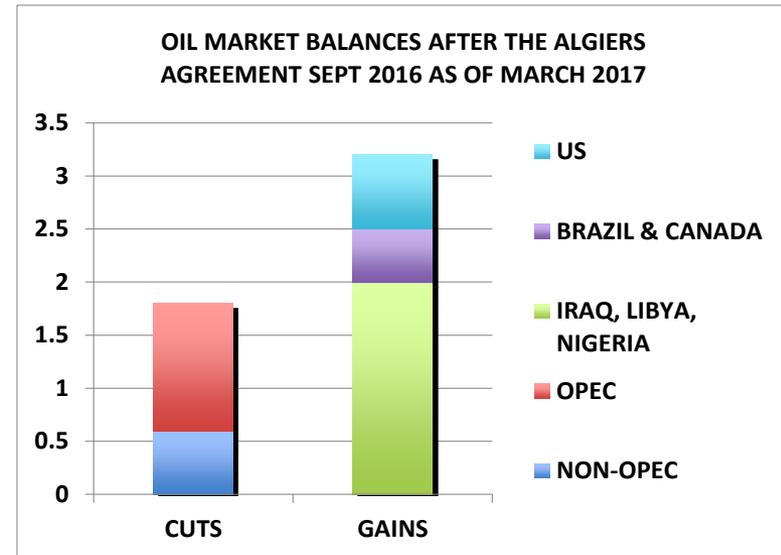
# Presentation outline

---

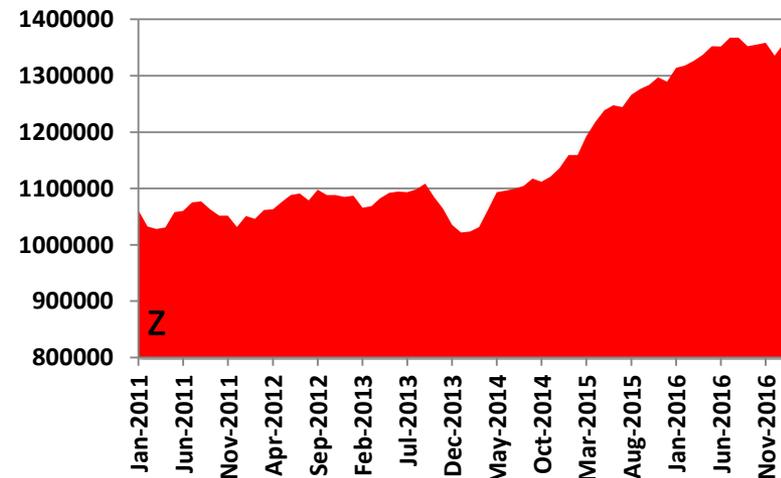
- **Problems of ‘Trumpian Uncertainty’**
  - What does it mean? Even after 100 days...
  - Focus on the oil market and the MENA region’s role in that market in a ‘Trumpian World’
- **Current state of the oil market: lower for longer?**
- **Trumpian impact on MENA?**
  - Oil producers and lower prices: Saudi Arabia
  - Iran and the JCPOA
  - Jerusalem and US embassies

# Current state of the oil market: Lower for longer?

- December 2016 agreement cuts 1.8 mn b/d (o.6 Non-OPEC)
- The cuts were too little
  - Algiers target in Sept = 29.8 mbd by Jan. In March, even accounting for 1.2 cut, OPEC producing 31.8 mbd. Needed another 2 mbd
  - As for compliance???
- Market balancing is some way off
  - Existing huge stock overhang
  - Nigeria, Libya and Iran excluded from cuts
  - Not all Non-OPEC is included and 'America First Policies' will only increase supply
  - On May 25<sup>th</sup> OPEC will have to extend (increase?) the December cuts
  - Prospects for oil prices are not good ....



US Oil Stocks 2011- Feb 2017 (excluding SPR)



# Current state of the oil market: Lower for longer?

---

- **Continuing unbalanced market** = oversupply = downward pressure on prices
  - What is the floor price? In a competitive market = SRMC tight oil <\$25 and falling because of improved efficiency
- **Price ceiling** from the U.S. “fracklog” and new wells (encouraged by ‘America First Policies’) and increased price elasticity of supply ~\$60
  - For example: between Jan and March EIA forecast for 2017 increased by 0.5 mn b/d reflecting higher prices
- **BUT** price forecasts always require a ‘health warning’: “Geopolitics and can be bad for your price forecasts” especially in a world of ‘Trumpian Uncertainty’.

# Presentation outline

---

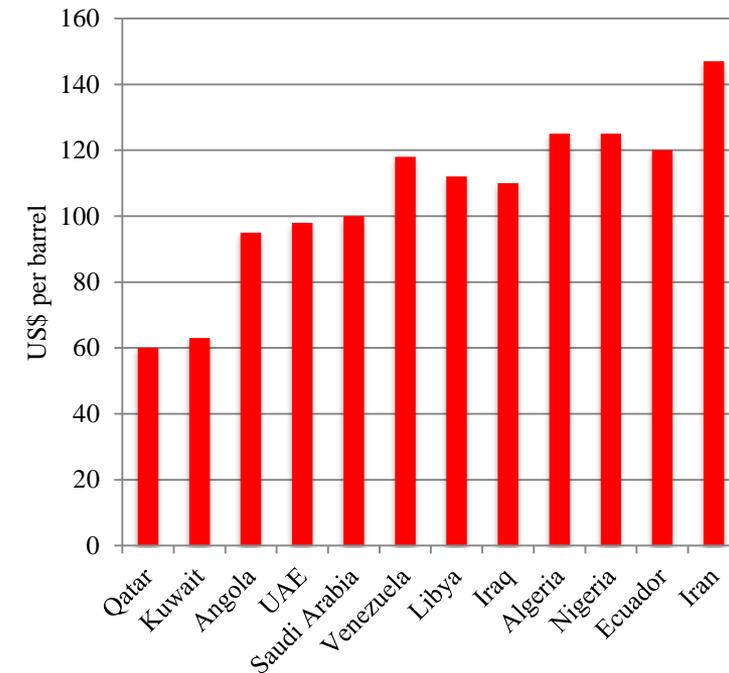
- Problems of ‘Trumpian Uncertainty’
  - What does it mean? Even after 100 days...
  - Focus on the oil market and the MENA region’s role in that market in a ‘Trumpian World’
- Current state of the oil market: lower for longer?
- Trumpian impact on MENA?
  - Oil producers and lower prices: Saudi Arabia
  - Iran and the JCPOA
  - Jerusalem and US embassies

# Trumpian impact in MENA

## Oil producers and lower prices: Saudi Arabia

- Generally: producers, revenue needs and political unrest
  - All adds to the region's instability
  - Trump's attack on Syria illustrates the potential for the return of a geo-political premium? Very short-lived BUT in future if Trump compounds regional instability ...?
- The Saudi oil strategy – make the supply curve go the right way - took much longer than expected
  - 'Break-even price' versus 'shut-in price'
  - Problems with achieving 'market share'
  - Uncertain over relations with the new Trump administration and his promise to “eradicate radical Islam”

OPEC Budgetary Break-Even Price 2014



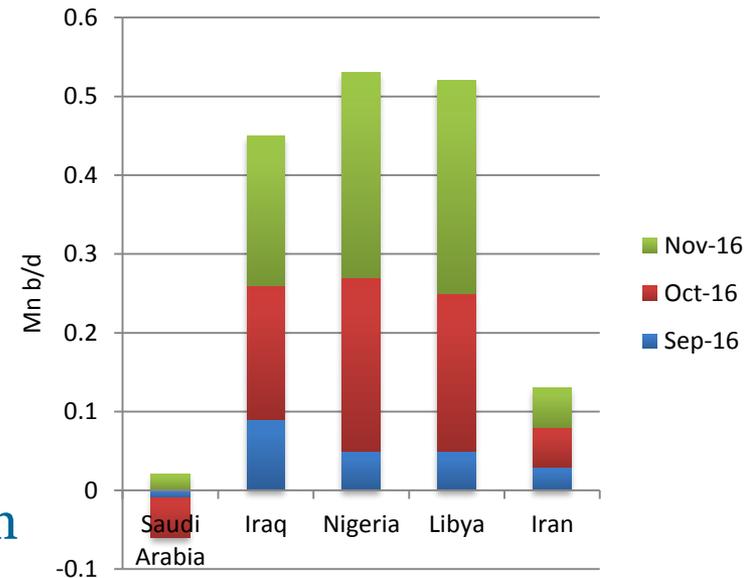
Source: Ali Aissaoui , 2014

# Trumpian impact in MENA

## Saudi Arabia's oil policy

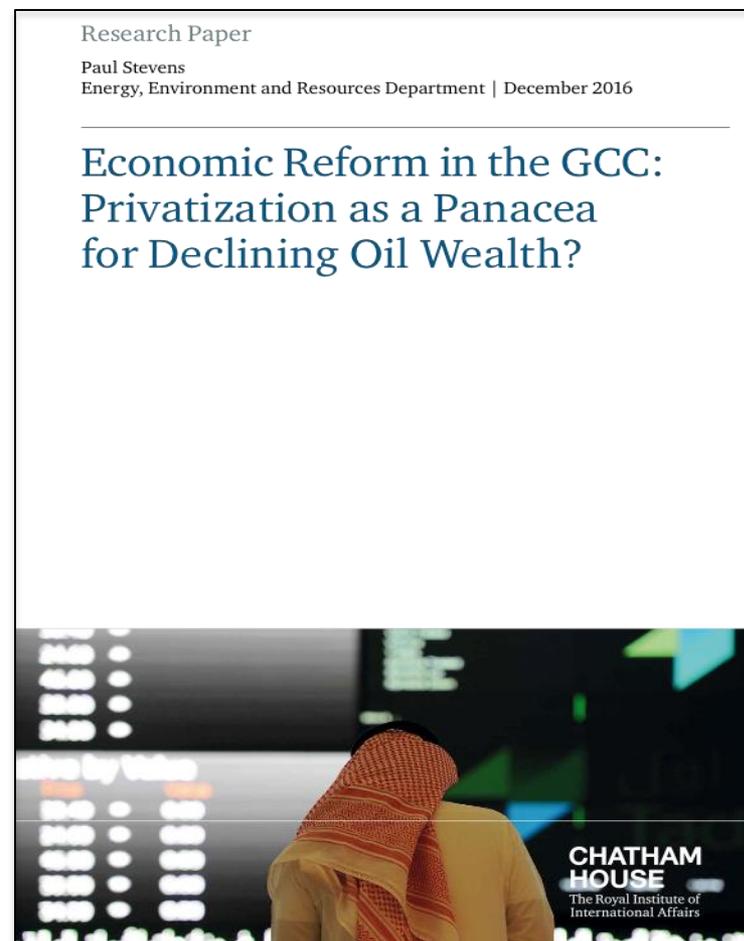
- At the start of 2016, when 'victory' appears close
  - US tight oil slowing; stocks plateauing; price rising:
 Saudi Arabia changes policy:
  - tries to regain control via agreements: April -Doha; September -Algiers; December -Vienna
- Why?
  - Mohammad bin Salman under pressure
    - Pressures from the rest of the family
    - Yemeni military adventure failing
    - Growing opposition to reforms
    - Financially: reserves fall faster than expected (Summer 2014 \$750bn; Dec 2016 \$536bn; currently <\$500bn)
    - Saudi Aramco struggling with production. October could not get above 10.9 mn b/d
- Future Saudi strategy in a world of 'Trumpian Uncertainty'?
  - Restore spare capacity cushion
  - Market share versus a controlled market: May 25?
  - Privatization of Saudi Aramco ...

Production change from 3rd quarter 2016 (IEA data)



# Saudi Arabia's oil policy: privatization?

- There are problems
  - What will be sold off? Above versus below ground assets
  - Poor transparency and poor profitability
    - Tax reform reducing tax rate from 85% to 50% - previously 93% of Saudi Aramco's profit to government
  - What happens to the 'national mission'
  - The underlying ideology also explains why governments will make a mess of the exit



<https://www.chathamhouse.org/publication/economic-reform-gcc-privatization-panacea-declining-oil-wealth>

# Trumpian impact in MENA

## What are the prospects for relations with Iran?

---

- Sanctions off BUT: Snap back clauses threaten and financial sanctions remain as do sanctions against the IRGC
- JCPOA probably safe BUT Congress (and Trump?) likely to create/enforce sanctions: Iranian Presidential elections (May 19) lead to a backlash against the US? Remember Iran is in a position to add to the (already) unstable situation in MENA
- Serious barriers to restoring (increasing) Iranian production
  - Old fields needing the Consortium's EOR programme 1977-8. Production struggling lacking access to parts and technology
  - NIOC technical capabilities seriously damaged by politically driven retirements during Ahmadinejad's regime
  - Iranian Petroleum Contract promising BUT:
    - Not yet fully approved in Tehran. IPC is very controversial
    - Facing intense competition from other producer governments' opening acreage
    - IOC upstream investment pot is contracting.
- Will take a lot longer than many think to increase production – recent numbers distorted by running down stocks
- Meanwhile – could Iran be forced into 'retaliation' compounding MENA instability – remember the geo-political premium on prices?

# Trumpian impact in MENA

## US policies to the Israeli-Palestinian problem?

---

- Moving the US Embassy to Jerusalem, possibly the most dangerous of Trump's election promises?
- If carried out, likely to lead to massive popular protests throughout the region creating further massive regional instability
  - Threatens US supported regimes
  - Generate massive anti-US feelings and anti-US action
  - How would an 'America First' policy respond when the results of anti-US action appear on Fox News?





CHATHAM HOUSE

[www.chathamhouse.org.uk](http://www.chathamhouse.org.uk)

# THANK YOU FOR YOUR ATTENTION

[pstevens@chathamhouse.org](mailto:pstevens@chathamhouse.org)