

## **U.S. Withdrawal from Iran Nuclear Deal and Growing Mideast Geopolitical Risks**

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From May 11 to 14, I had an opportunity to take part in an international conference and meetings with experts in London and Amsterdam to discuss mainly oil, gas and LNG problems. While my discussions with these experts covered a wide range of topics, the most impressive topic for me was Middle Eastern geopolitical risks growing in the wake of the United States' withdrawal from the Iran nuclear deal.

On May 8, U.S. President Donald Trump vowed to withdraw the United States from the Iran nuclear deal that his predecessor Barack Obama achieved through years of international negotiations, giving a great shock to the world. Trump had strongly criticized the deal for including a sunset clause to lift restrictions on Iran's nuclear development after a certain period of time, for failing to restrict Iran's ballistic missile development and providing for insufficient international inspection of Iran's nuclear facilities. As Trump had threatened to withdraw his country from the deal unless these problems are resolved, European parties to the deal tried to coordinate between Iran and the United States. No compromise has been made, however, leading Trump to announce the withdrawal. Most relevant countries, excluding some such as Israel, expressed their regret over and disappointment at the U.S. withdrawal. Iran has offered to remain a party to the deal, while criticizing the U.S. attitude.

In the international oil market, the United States' potential withdrawal from the Iran nuclear deal influenced crude oil prices even before the May 8 announcement. On May 7, the key West Texas Intermediate futures price rose above \$70 per barrel for the first time in 42 months. While the U.S. withdrawal was discounted into oil prices, the WTI futures price remained above \$70/bbl even after the announcement. The benchmark Brent crude futures price also increased to \$78.43/bbl, close to \$80/bbl, on May 15. If the Brent price rises back above \$80/bbl, it will be the first time since November 2014.

There are two factors behind crude oil prices' upsurge on the United States' withdrawal from the Iran nuclear deal amid progress in rebalancing (normalization of oil inventory levels). First, market participants have been concerned about a possible decline in Iran's oil exports that could come on the resumption of U.S. economic sanctions following the withdrawal from the nuclear deal. Iran's recent crude oil exports have totaled about 2.5 million barrels per day. Crude oil prices have risen on concern that an Iranian oil export cut would greatly affect the supply-demand balance in the international oil market.

The international oil market has seen a sharp U.S. shale oil output expansion and remarkable production cuts in Venezuela and Mexico on the supply side, while oil demand has

sustained robust growth. The supply-demand balance is expected to tighten if Iran oil export declines significantly. In my latest discussions with experts in Europe, however, it was pointed out that how Iran's oil exports would decline was uncertain. It is difficult to predict how major European countries remaining parties to the deal, as well as China and other countries, would reduce crude oil liftings from Iran. The impact of the U.S. decision on Iranian crude oil exports may emerge in the next six months. Depending on the impact, crude oil prices could move wildly.

In the discussions in Europe, it was also pointed out that as European countries ask and negotiate with the United States to maintain Iranian crude oil imports and other business transactions with Iran, their tensions could grow with the United States retaining a hardline attitude. Any split between the United States and its European allies over the Iran problem would be a significant problem for global governance. Another problem is who would cover a potential reduction in Iranian oil exports. In this respect, how OPEC and other oil producing countries conducting a coordinated production cut would respond to the Iran problem would be very important for predicting the future of the international oil market. The next OPEC general meeting would attract global attention.

Second, the U.S. withdrawal from the Iran nuclear deal has increased geopolitical risks in the Middle East and raised the possibility of the region being destabilized, as noted by many experts in the discussions. Concerns about the destabilization of the Middle East have attracted attention as a factor that could destabilize the international oil market and cause crude oil price hikes. In Iran, the environment for President Hassan Rouhani who led the nuclear deal is growing severer. President Rouhani has persuaded hardline rivals by winning domestic support for the deal to get the lifting of economic sanctions in exchange for restrictions on nuclear development. The U.S. withdrawal from the deal could lead to the rise of hardline rivals to affect his support base. Although Iran has offered to remain a party to the nuclear deal, various domestic and overseas developments and provocations could shake up Tehran.

The key point is what actions the United States and Israel toughening a hardline attitude against Iran would take while watching the Iranian situation. In early May, Israel caused wide repercussions by claiming that Iran had continued nuclear development even under the nuclear deal. Israel has supported the U.S. withdrawal from the nuclear deal and is toughening its anti-Iran attitude along with the United States. As the nuclear deal designed to prevent nuclear proliferation and ease tensions in the Middle East has reached a turning point, geopolitical risks including the possibility of clashes through growing tensions and provocations have increased suddenly, said multiple experts impressively. It was also noted that a key point to influence the future Middle Eastern situation would be how Saudi Arabia and other Persian Gulf countries deepening disputes with Iran would be involved in Iran's confrontation with the United States and Israel. In addition, on May 14 when the United States relocated its embassy to Jerusalem that Washington has recognized as the capital of Israel, large protests came to the relocation, leading more than 60 people to die in clashes between protesters and Israeli police. In this respect as well, we have no choice but to pay attention to growing geopolitical risks in the Middle East.

Before the 2003 Iraq War, major think tanks in the world analyzed various scenarios for the future of the Iraqi situation. Scenarios subject to analysis at that time included military clashes and war. I remember that these scenarios' consequences and effects on the energy market were also analyzed interestingly. As a matter of course, scenario analysis has its own limitations and cannot necessarily predict a complicated future in any accurate manner. However, such analysis can help

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strategic preparations for various future developments. My discussions with experts in Europe led me to think that the uncertain, chaotic Middle Eastern situation could lead to a need to make new Middle East scenario analysis. In Japan for which the Middle East is the most important supplier of oil accounting for most of its energy supply, we in Japan may have to analyze future scenarios of the Middle East.

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