SUMMARY OF DISCUSSION POINTS

The Future of Oil in the Middle East: Building Diversified Economies in an Age of Energy Transition

Tuesday 28 July 2020

One key message that emerged from the eighth online summit of The London Energy Club was "the strongest and most promising renewable energy for the Middle East is its youth".

When considering the Middle East, we need to be clear that across the region there are diametrically opposed views about the future of oil, while each country is an entity, with individual issues and concerns. The Middle East is a region of two contrasting systems. One system features a dynamic private sector, digitally savvy youth and open economies. The other has a bloated public sector and closed, controlled economies. So, in any discussion about the Middle East we will need to take these two key factors into account. One size certainly does not fit all.

There is a strong declining trend in global oil demand; after accounting for income and population growth.

This reflects a range of factors such as long-term improvement in energy efficiency and substitution away from oil; trends that had so far been "veiled by the effects of economic and population expansion."

But this trend is poised to become more visible in the coming years, resulting in a path of gradually slowing – and eventually declining – global demand for oil. The latter would peak by around 2040 in our benchmark projection, or much sooner in scenarios of stronger regulatory push for environmental protection and faster improvements in energy efficiency.

Growth of global demand for natural gas is also expected to slow although it is expected to remain positive in the coming decades.

Even when oil demand does peak at some point in the future, it is not going to drop off a cliff because substitute-ability for oil in so many sectors is still elusive – in shipping, aviation, trucking and petrochemicals there are still huge driving forces (for oil demand).

Oil-dependent Middle Eastern economies face a monumental task: as the global energy mix continues to transition, they must manage this change while diversifying away from hydrocarbon reliance. Job creation programmes must be scaled up rapidly, but also sustainably. Governance challenges must be addressed while the social contract is maintained or enhanced.

This is a multi-faceted challenge in the post-COVID environment in which low demand, volatile prices, climate change commitments, worldwide recession and geopolitical tensions severely impact these economies. This diverse group of countries ranges from Algeria in the west to Iran in the east and also includes the six Gulf Cooperation Council countries as well as Iraq, Libya and Yemen. But, ultimately, the mountain they have to climb is the same.

There were around 200 participants and six expert speakers, moderated by the London Energy Club chairman, Mehmet Öğütçü.

The summit’s regional partner was the Iraq Energy Institute, chaired by Yesar Al Maleki.

Other organisations which took an active part in the discussion included, inter alia: the King Abdullah Petroleum Studies & Research Center, United Nations Development Programme, Oxford Institute of Energy Studies, Bosphorus Energy Club, China Academy of Social Sciences, Windsor Energy Group, Middle East Institute, and Policy Center for the New South, Morocco.

What follows are some of the main points from the speakers:

Adam Siemenski, *President of the King Abdullah Petroleum Studies & Research Center (KAPSARC)*

- The subject of peak oil, and whether have reached this point, is still around. It is a subject of fierce debate and has been for a long time; demand verses supply. To date peak oil has not happened.
- Will COVID-19 lead to peak oil, with significant reduction in demand with cars and aviation, advancing climate policies and the challenges of pollution?
- There are three possible scenarios:
    - Full recovery. Strong rebound in economies and GDP up to 2030.
    - Go it alone. Retreat from globalisation, and shrinking economies.
    - Green growth. Impact of the European Green Deal and Green New Deal in the USA, reducing oil consumption.
- My view is that there will be a slow rate of economic growth.
- In terms of the use of oil, technological developments may well prolong the use of oil. If CO_2 can be reused, recycled or stored, fossil fuel becomes more attractive and will last longer.
- In parallel, the economies of the world will continue to need oil and gas. Aeroplanes, ships and trucks will require oil as will the industrial sectors, for the foreseeable future. In addition, there are currently 1.3bn cars on the road. The figure is expected to be 1.8bn by 2030. They cannot all be converted to electric in this timeframe.
- Plausible that priorities will shift in the aftermath of COVID-19. To: jobs, the environment and oil products, with a focus on managing carbon; reduce, re-use, recycle.
- Oil companies are embracing renewables and are investing considerable amounts in new technologies. They have an optimistic, can-do approach, and will assist in the change.
- Peak oil may come, but not soon.

Yesar Al-Maleki, *Director, Iraq Research Institute*

- GDP will contract in oil-producing nations of the Middle East, North Africa, Afghanistan and Pakistan (MENAP) region by 7.3% in 2020.
- The main culprits are: the COVID-19 pandemic and associated declining oil prices, OPEC+ agreement cutbacks and the existing economic under-diversified structures within the region.
- The effects are not limited to economic contraction but include emergency governmental spending in the form of fiscal stimulus packages, short-term emergency measures, erosion of fiscal buffers, accumulation of debt and an evident flight of capital.
- Oil production is down to 63% of normal.
- In order to mitigate COVID-19, governments are making short-term decisions, which do not necessarily match long-term aspirations.
- It is expected that losses in revenue will amount to $152bn in 2020; $11bn in net oil revenues were lost in January to March.
- In humanitarian terms, 14.3 million people have been pushed into poverty, 55 million others are vulnerable and at least 1.7 million jobs are expected to be lost in the Arab region this year.
- Governments support has been mainly in healthcare and in bank support. $40bn in liquidity by various governments have been released. This has been mainly achieved by adjusting current expenditure downwards.
- Debt can be a short-term solution, but need to fix the macroeconomic problems:
    - Development of fiscal frameworks.
    - Transparency.
    - Enhanced liquidity management.
    - Financial sector resilience.
- But the expectation is that, without a vaccine, there will be significant barriers to operating efficiently for a considerable period.

- Need to increase and support the private sector:
  - Regulatory and institutional frameworks.
  - Public sector supporting private sector.
  - Trade integration.
  - Support SMEs.
- Will there be regional energy integration?
- There are many opportunities to utilise free market economics to create integrated electricity markets, oil and gas pipeline networks, and cross-border renewable energy projects.
- For instance, Iraq and the GCC are in the final stages of technically connecting their networks. Iraq is currently suffering a peak supply to demand gap of more than 6000 MW.
- Every year, Iraq and Saudi Arabia burn crude oil in summer to provide electricity for their populations. Gas utilisation, especially flared gas from associated oil production, can be captured and developed by both countries. Iraq is the world's second largest gas flaring country. Even Kuwait suffers from natural gas shortages in summer.

Michal Meiden, *Director China Energy Programme, Oxford Institute for Energy Studies*

- China's involvement in the Middle East is not just oil. It involves oil, investments and geopolitics.

Oil

- China is the largest importer of oil in the global market. 10m bpd in 2019; 12m bpd in 2020. China is benefitting from the price shock; large volumes of oil are being stored.
- China is expected to be the largest source of oil demand growth for at least the next 10 years. Chiefly for transport and chemicals. While striving for self-sufficiency.
- The percentage of China's demand which is purchased from the Middle East is 50%, which has been capped at this figure for the last decade. By contrast, Japan imports 80% of its oil from the Middle East.

Investments

- No need for Chinese money in upstream. But 56% of Chinese investments in the Middle East 2015-2019 were in the energy sector.
- Big investment in renewables; finance and construction: belt and road, clean coal and solar.
- Alongside this, there is investment in infrastructure, particularly in ports. And investment in technology: Huawei.

Geopolitics

- China's strategic view of Middle East politics is "neutrality". The aim is to diversify and grow commercial relationships. No wish to police.
- Relationship with Iran is the possible exception. But details not clear.
- Overall, China's aim is to achieve self-sufficiency and a local supply chain.
- There is a good bi-partisan relationship with the US in the Middle East in terms of both politics and the commercial are good. But the development of a new "cold war" is likely to affect this.
- Third-party countries will be forced to pick sides, including Middle East countries.

Gerald Feinstein, *Senior Vice President, Middle East Institute*

- There have been two shocks in the Middle East – the global pandemic and the collapse in oil and gas prices. These will accelerate geopolitical trends.
- The GCC is looking more at diversifying economies away from dependence on oil and gas, and is accelerating the process.
- The decline in oil prices (now c$40/barrel) had produced budget deficits which has highlighted the effect of remittances in the region.1m expats will leave Saudi in 2020. Affecting: Egypt, N Africa, S Asia and the Philippines.

Relationships

- There is a stabilisation of the relationship between the GCC and Iran, which already started last year. With lack of strong US support, there has been greater focus. Saudi is keen to get out of Yemen. If Saudi leaves Yemen, a major irritant will be removed.
- There is also the competition between Turkey on the one hand and Egypt, Saudi and UAE on the other, with a major issue in Libya.
- USA and China are not really competing on their objectives in the Middle East. The only potential area of concern is Iran.
- The current spat with China is being driven by the US Presidential campaign. Expect to see a reduction in the hostility after 3rd November, whoever wins.
- China is equally dependent with them on its relationship with Saudi Arabia and UAE. Not a one way relationship.
- Cooperation will be the driving force for regional stability.
- Economic diversity in all its forms will be a priority.

Adel Abullatif, *Deputy Director, UNDP Regional Bureau for Arab States*

- The diversification agenda is very important. There is anxiety about the longevity of, and demand for, oil.
- The subject has been on the agenda for a long time, but will it be addressed properly? Has not been hitherto.
- There was an Arab summit on the subject in 2009, covering developmental issues, including the provision of an electrical grid across the region. Little progress.
- The 2011 Arab Spring demonstrated discontent from within. Lists of demands and expectations from their leaders. The heart of the issues were: less control by government, a larger private

sector, transparency and reduction in corruption, and more space for people within the social contract.

- The pandemic will accelerate this process. But there is a lack of skilled labour and citizens are shielded within the public sector.
- There is hope with the new generation of young leaders coming through the system. And many have been educated overseas; Saudi has educated more than 100,000 outside the Kingdom.
- The young demographic means that there is a larger pool of labour, but also a greater demand for jobs. There needs to be access to finance for SMEs, to support them.
- There will be a changing relationship between the state and the citizen. Will this lead to a looser, more diversified society? Challenging.
- But little is likely to happen during a global pandemic. Challenges are more difficult to meet. Pessimistic about diversification. Priority is deeds not words.

Karim El Aynaoui, *President, Policy Center for The New South*

MENA Region

- Different issues in North Africa to the Gulf.
- Most African countries, such as Morocco, have zero oil. The dynamics are very different and pressures are different, as is their relationship with the rest of the world.

Uncertainty

- COVID-19 and oil. Particularly difficult issues in the region.
- Unexplored territories, and not without consequences. There is a price to be paid.

Trends of History

- Does not give much helpful guidance in the present situation.

Oil

- Oil is over, in the long term. Only a matter of time. Hydrogen, solar and others will replace.
- Demand from society: less harmful energy, less carbon, less pollution.

Better than Oil

- Change the mental attitude; change the legacy; create the space.
- Human capital will provide the necessary energy.
- There is the space and opportunity for the younger generation.
- Generational change will drive progress.

Dialogue

- Essential; will multiply initiatives and outcomes.
- Create opportunities for all is the key.

Lord Howell of Guildford, *Former Minister of State (Foreign and Commonwealth Office) and Chairman, Windsor Energy Group, UK*

- Sinophobia is very dangerous. We must not fight the last cold war with China. Hope that the spat will end after the US election.
- The future of Middle East energy will be based on the cheapest and most convenient energy source. Electric cars have yet to win the argument. Charging, batteries. Don't write off oil yet.

The next meeting of the London Energy Club will be held by webinar on 10 September 2020 at 13:00 BST (London time), focusing on *the What do the EU Green Deal and Green Stimulus mean for governments and business?*

Register at: https://bit.ly/2D3qkXH

Membership: Please contact A.watson@londonenergyclub.org for enquiries regarding membership.