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Recent Developments in US Energy Policy
New independence for the US and increasing bloc formation in the Gulf region

by Stefan Lukas

While the United States has exploited new technology to become the world's largest oil producer, the new US energy policy is proving to be a game changer for countries in the Middle East. US allies, particularly in the Gulf region, have to adjust to the United States' reoriented Middle East strategy, which is possible to some extent with the oil market. The situation is different, however, with regard to gas. Especially Qatar, as the world's second largest exporter of gas, is becoming a new economic rival, which is also impacting the region's political landscape. These developments are leading to the formation of blocs in the Middle East, which will also have consequences for the region's European partners.

The new energy independence of the United States

In the 1970s, when a number of Arab states in the *Organisation of Petroleum Exporting Countries* (OPEC) responded to the renewed conflict with Israel by joining forces to exert pressure on Western nations, the Achilles' heel of the West and especially of the United States was suddenly exposed. While in Germany and other Western states the oil embargo imposed by the Arab nations resulted in driving bans on specific days, the United States was negotiating with its Arab allies and Israel to resolve the conflict as soon as possible and avoid further oil shortages.

Nobody at the time could have imagined that 40 years later the United States, of all countries, would be the largest producer of black gold and, in particular, of gas. The crucial turning point came with a technique that was being used by small oil companies in Texas to remain reasonably cost-effective. The method known today as fracking was, and continues to be, highly problematic both ecologically and, to a certain extent, economically. From 2011, however, fracking enabled the United States to become more and more independent of OPEC's oil policy and to establish itself as an exporter of oil and especially gas.

The American turnaround on the energy market finally occurred when, in 2016, Congress revoked the *Energy Policy and Conservation Act*, which since 1975 had banned gas and oil exports from the United States. The policy shift was made possible with the help of US enterprises such as ConocoPhillips and Exxon Mobil. The United States has now surpassed Saudi Arabia as the largest gas producer and this year will probably surpass Russia as the leading oil and gas producer.

The distribution structure in the United States presented the greatest challenge in this connection which, on account of political decisions, had been geared towards imports since the 1970s. This applied not only to the pipeline network but also to the terminals where imported gas and oil are fed into the US network. Over the past eight years, this network, including its distribution stations, has been modified to transport newly extracted gas from heartland states such as Dakota and Wyoming to coastal transshipment points. The fact that the US administration will continue to focus on exports and that this is not merely a temporary fracking boom can be seen from the aspirations of the Obama and Trump administrations to build a total of 13 new LNG terminals on the East, West and Gulf Coasts. *Liquefied Natural Gas* (LNG) is natural gas that has been cooled to a temperature of -164°C and condensed into a liquid. This allows the gas to be transported over long distances by LNG tankers. In recent years, LNG production has become the most important guarantor of the US administration's new energy policy, and recently even naval exercises have been specialising in protecting and escorting LNG tankers across the oceans.

While the United States has now achieved a new energy independence from external actors thanks to fracking and LNG production and may therefore pursue its foreign policy with greater self-assurance, the US administration and US companies face two problems. First: Where are the markets for this newly gained potential? And second: What is the best way to deal with former producers, especially the Gulf States? From the US perspective, the first problem will be solved by exporting to long-standing allies in Europe, Asia and other regions, parts of which are poorly connected to competing distribution networks, if at all. The Obama administration, for example, supported the construction of new LNG terminals in Europe to sell more US gas on the European market, which is strongly dominated by Russian, Norwegian and Arab gas. Since 2011, new LNG terminals have also been built in Lithuania, Poland and Finland. In addition, LNG terminals that are reported to have been designed specifically for US gas imports are under construction in Croatia and will probably also be built in Brunsbuettel, Germany, in the near future. The latter has only recently been pledged to the US administration by the European Commission in return for the United States' decision not charge additional customs duties.

This highlights one of the main difficulties of the US strategy. Gas imported from the United States has so far been too expensive for the European market and can barely compete in price with gas from northern and eastern Europe. Therefore, demand for US gas is not particularly high in Europe. The new LNG terminals in Poland and Lithuania, for example, are only being used to just over half of their full capacity since Russian gas supplied through existing pipelines is much cheaper. German energy companies also believe that the construction of an LNG terminal is unnecessary for Germany as the existing LNG capacities rented in Rotterdam are not even in full use. Much the same applies to other future customers of US gas such as Japan and Korea, which have already concluded contracts with Russia on gas supplies and the construction of new pipelines. The political dimension of US gas is usually a key aspect for the customers since it cannot be in their interest to become too dependent on a small number of actors that dominate the market. Even the Chinese government recently entered into negotiations with the US government on future supplies of American gas in order to lessen its dependence on gas from Siberia.

The second problem to be solved by the US administration and, in particular, by US foreign policy as a result of this new independence is much more complex, especially with regard to US allies in the Gulf. The United States is facing a dilemma. The Gulf region, with Qatar, Saudi Arabia and the United Arab Emirates (UAE), includes several of the world's largest gas and oil producers with which the United States is now competing. At the same time, the United States is the major security guarantor for these countries, which at the same time purchase the largest number of US weapons worldwide. The United States is now using different approaches to solve this growing dilemma.

From political mediator to economic rival

The new role of the United States as an oil and gas exporter will probably have the greatest impact in terms of foreign policy on countries in the Persian Gulf, which the current US President has bluntly made public. While civil wars are being fought in Syria and Iraq, and Iran and its proxies have again been sanctioned in spite of the nuclear deal, the partnership between the United States and its allies in the Gulf region has also changed. Their relationship was previously based on the principle that the United States would buy oil and gas from its Gulf allies, in return for which the Gulf States received a security guarantee, whereas now this principle is being challenged by American autarky. The Gulf States had been in a position to deal with Washington at other levels since they were able to influence the oil and gas markets and thus exert pressure on the United States. This became particularly obvious in the years between 2011 and 2014 when Saudi Arabia, in particular, increased its oil production in an attempt to exert pressure on the emerging fracking industry in the United States. As this was only partly successful due to massive state subsidies granted by the US government and, moreover, as the decline in oil prices caused a major Saudi budget deficit, the Gulf States sought to establish a new policy of economic and political cooperation with the US administration under Donald Trump. From now on, oil prices were to be stabilised in coordination with Washington at a level that would allow US companies to be sufficiently profitable and the states of the Gulf Cooperation Council (GCC)[1] to at least balance their budgets.

An example of this new approach to oil pricing was not least the Saudi government's decision in June 2018 to meet Trump's request that Saudi Arabia agree not to increase its production capacities and thus avoid an oil price decline. Moreover, the US withdrawal from the nuclear deal with Iran not only placed new pressure on the Iranian oil and gas industry, but also caused oil prices to increase, which is in the interest of both the United States and the GCC member states. Although this approach was possible for the oil market and was in the interest of nearly all GCC member states, a compromise solution for the gas market is much more difficult to achieve. Qatar, in particular, which is after Australia the world's second largest gas exporter and currently controls about 30 percent of the global gas market, has been one of the major rivals of the United States since 2016, along with Iran and Russia.

The Qatar crisis and increasing bloc formation in the Gulf

Over the past decades, the United States has sought to play a mediating role in the region and, in particular, between its allies in the Gulf, whereas since early 2017 its role has become somewhat ambivalent and might even fuel conflicts. The crisis that emerged in June 2017 between Qatar on one side and Bahrain, Saudi Arabia, the United Arab Emirates and Egypt on the other, is clear evidence of this development. Tensions between the emirates and kingdoms in the Gulf region are nothing new. Back in 2014 and 2015, for example, the Saudi ambassador was recalled from Qatar in protest over Qatar's reporting of the Arab Spring as well as over the bilateral relations between Doha and Iran. But the sustained blockade by former allies in the Gulf has now taken on a hitherto unknown dimension that is making it increasingly difficult for all parties involved to develop a face-saving and therefore practicable exit strategy.

The Obama administration had largely managed to moderate major conflicts among the GCC states. Under the Trump administration things are completely different. This escalation has been caused mainly by seemingly unconditional US support for the Saudi royal family since the dismissal of US Secretary of State Rex Tillerson, the erosion of multilateral cooperation, and not least by stronger US competition with Qatar on the gas market. But what conditions affect this new economic competition given the existing security partnership?

Qatar finances more than 60 percent of its budget with gas exports and has already come under pressure during the blockade imposed by its neighbours. It is true that the emirate, or rather its state fund, the Qatar Investment Authority, still has reserves of about 340 billion US dollars, but particularly imports of food and other consumer goods have become considerably more expensive. Therefore, Qatar is all the more dependent on its gas exports. Over the past ten years, Qatar has also dramatically expanded its gas network and capacities with the help of companies such as BP, Total and Shell. Shell alone has invested more than 13 billion US dollars in innovative technologies in the country over the past decade and is unwilling to scale down this investment despite the blockade. Qatar's relations with Iran also set the emirate apart. The emirate is closely tied to its neighbour in the north by the world's largest gas field (North Dome / South Pars) and cannot afford to antagonise Iran and risk losses in gas production. Qatar is therefore keen to maintain good relations with Iran as well as with Oman, both of which control the Strait of Hormuz. Oman also serves as a major mediator in the blockade and is currently in the process of becoming an important trading partner for Qatar.

On account of this constellation, it was only a matter of time before a confrontation, even a political and economic one, occurred between Qatar and the United States, which has been the emirate's original

[1] The GCC is an organisation that was established in 1980 by the states of the Arabian Peninsula to settle security and to a certain extent economic conflicts among GCC member states and, at the same time, coordinate the military potentials of the individual states.

protecting power since the withdrawal of the UK in 1971. Due to the fact that Qatar, like the United States, relies on LNG technology and has built four LNG terminals, both gas exporters are competing for the same customers. Of particular interest are the East Asian countries such as Japan, Korea, China and Taiwan, which so far have been importing most of their gas from Qatar. According to the new US strategy, it is mainly Korea and Japan that will receive gas from the United States, which will also sharpen the competition with Qatar. The blockade was originally imposed by Saudi Arabia and its allies for other reasons, but energy policy constraints probably also played a part. The blockade is forcing Qatar to offer gas at significantly lower prices in order to amortise the costs of its high imports in the food and transport sectors. The question is, how long will the emirate be able to withstand the pressure? Since the dismissal of Rex Tillerson there have been no US mediation efforts, and with Mike Pompeo the post of US Secretary of State has been taken by a hardliner when it comes to relations with Iran, with which Qatar still has close ties.

The lack of mediation by the United States, and the harsh blockade imposed by Saudi Arabia and its allies, has resulted in a growing divide in the Middle East which is not only affecting economic policy, but will increasingly impact security policy. On one side of this divide there is the United States and its allies Israel, Saudi Arabia, the United Arab Emirates, Egypt and other smaller states that are particularly averse to the idea of Iran regaining strength in the Middle East and are thus united in their fear. On the other side, closer ties can be seen gradually forming between Iran, Qatar and Turkey, which are being forged by Tehran and consolidated by joint military exercises and large-scale multilateral investments. For example, Qatar has invested 20 billion US dollars in Turkey alone, and Istanbul built a new military base in the emirate when the Qatar crisis erupted and now has 2,000 troops stationed in the Gulf. Smaller countries like Oman and Kuwait have since acted as mediators between the two blocs and may benefit from this position but at the same time must avoid being drawn too deeply into the political conflicts.

In spite of renewed tensions between the Gulf States, the United States continues to be the most important security guarantor for its allies in the region. This is evident not only from the presence of currently around 38,000 US troops in the Gulf, but also from an increasing number of arms deals in the region. The best example is again Qatar, which presents the strongest economic competition to the US arms industry in the region and at the same time is one of the largest customers for US weapons technology. Shortly after the crisis started, Qatar placed an order for several F-15 fighter jets at a total value of more than 12 billion US dollars. The emirate's strategic role is still of major significance for the United States, given that the Al-Udeid Air Base hosts an important forward headquarters of the *United States Central Command* (CENTCOM) – despite constant criticism from Abu Dhabi and Riyadh.

While the United States under President Trump, and/or his son-in-law and Middle East adviser Jared Kushner, is confidently pursuing its new Middle East policy, it is particularly the European partners that are faced with a growing number of problems arising from bloc formation in the region. It is mainly at the economic and political level that foreign policy negotiators from Germany and neighbouring states are finding it increasingly difficult making progress without alienating the other side. Saudi Arabia's crown prince Mohammed Bin Salman has already threatened to disallow any future German investments in his country if the German government continues to intensify its relations with Iran. At the political level, mediation efforts in the region are becoming more complicated since compromises and settlements in the crisis regions of Syria, Yemen, Iraq and Libya will be harder to achieve in future. This blockade will persist as long as rivals from the Middle East fail to reach a compromise with the United States as a new actor on the gas market. Given that the Iranian government is not expected to back down in the foreseeable future and that Qatar has also demonstrated considerable staying power in weathering the blockade, tensions are unlikely to ease in the months ahead.

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