GCC Hydrocarbon Economies and COVID

Old Trends, New Realities

Edited by
Nikolay Kozhanov · Karen Young · Jalal Qanas

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ISBN 978-981-19-5461-0 ISBN 978-981-19-5462-7 (eBook)
https://doi.org/10.1007/978-981-19-5462-7

This Palgrave Macmillan imprint is published by the registered company Springer Nature Singapore Pte Ltd.
The registered company address is: 152 Beach Road, #21-01/04 Gateway East, Singapore 189721, Singapore

Acknowledgments

The editors would like to thank all the authors involved in this book as well as the Gulf Studies Center at Qatar University that supported this project and made it possible.

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CHAPTER 1

Introduction

Nikolay Kozhanov

The negative impact of the coronavirus pandemic on the hydrocarbon producers of the Gulf Cooperation Council (GCC) is raising serious questions about the need to change the focus of Gulf energy security from the necessity to protect the interests of Gulf oil consumers to the need to ensure the interests of oil producers themselves. By the beginning of the COVID pandemic, the GCC countries had already been tested by contracting economic growth, falling incomes from oil exports, low oil and gas prices, unpredictable hydrocarbon market fluctuations, sluggish growth in oil demand, as well as rising competition with other oil and gas producers. For the GCC hydrocarbon producers to adequately respond to emerging challenges, it is important to clearly define and understand the origins of these issues, the majority of which are deeply connected to the oil and gas market transformation which started long before the coronavirus pandemic, but was speed up under its influence.

The book considers the impact of COVID-19 on the GCC member states through the prism of challenges faced by their hydrocarbon sector. Yet, the publication's discourse is not solely focused on the problems

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N. Kozhanov et al. (eds.), *GCC Hydrocarbon Economies and COVID*,
https://doi.org/10.1007/978-981-19-5462-7_1

experienced by the oil and gas industries of the GCC member states after the beginning of the COVID pandemic. Instead, the contributors analyze how these challenges and subsequent response to them affected other aspects of the GCC socio-economic and political development. Consequently, the collective monograph discusses the direct impact of the COVID on the energy sector of the GCC, socio-economic consequences of the oil market crisis for the region and its potential fallouts for the international relations of the Persian Gulf.[1]

The COVID-19 hit the economy of the Gulf monarchies and their oil and gas sector in several ways simultaneously. First of all, the global oil glut forced the GCC countries to wage a severe price war for hydrocarbon markets' share. Moreover, in Spring 2020, oil producers had to fight not so much for expanding their market presence but rather for securing what they have while being pressured by falling demand. This turned the market competition into a bloody knife fight where everything goes. Moreover, during spring–summer 2020, the sharp drop in oil prices has significantly erased the boundaries of suppliers' regional specialization, opening up access for some players to new markets, further increasing competition. Thus, in the Asian market the GCC countries had to compete not only with Iraq, Russia, and among themselves, but also with the oil producers of Latin America and West Africa also joined the fight.

With the beginning of recovery in oil consumption in Europe and Asia and the substantial increase in oil and gas prices by 2022, the situation has somewhat improved and the competition between producers got less aggressive, but the situation is still far from being normal. The current crisis has proved that the future of the GCC countries and their oil and gas sector will not be cloudless. One of the main problems will be the growing tensions in the global energy markets. There will be competition between the Gulf countries themselves. The economic development model of the leading GCC states is approximately the same. This means that they will not be able to avoid competition with each other, given approximately the same directions for their exports, visions of sources to fund economic development, as well as the overlapping

[1] The use of the term "Persian Gulf" in this book does not endorse any nationalistic agenda. The editor and authors use it following the most common practice to name the body of water that in some studies is also called "the Arabian Gulf." Moreover, in the book the preference is given to the shorter version of the geographical name—"the Gulf"—in order to avoid sensitive and unnecessary political discussions.

ambitions regarding the markets of new energy resources. However, the possibility of cooperation cannot be completely excluded. The general attitude of the leading players to increase the volume of oil and gas production makes the GCC countries talk about the possibility of implementing joint projects. Recently, the management of the Abu Dhabi National Petroleum Construction Company (NPCC) was debating the company's ongoing infrastructure projects in the KSA and the possibilities for NPCC to participate in the implementation of Kuwaiti plans to bring oil production to the level of 3.2 million barrels per day by 2025.

However, the far bigger challenge for the GCC countries will be represented by growing tensions between them and hydrocarbon—first of all, oil—consumers. On the other hand, the current crisis proved the thesis that reducing the role of OPEC and traditional producers in regulating the oil market was controversial. Yet, on the other hand, it also demonstrated that oil consumers will be gaining more influence on the market as well. With the progress of energy transition and the expected return of frequent market oversupply, it is demand, not supply, that will play an increasingly important role in determining the dynamics of oil and gas prices. An excess of oil on the market is already expected in 2022 while, according to some estimates, by 2030, there may be up to 10 million excess barrels per day on the market. Moreover, an attempt by producers to exert pressure on price changes by regulating production volumes will cause an increasingly sharp reaction from consumers. Meanwhile, the expected oversupply and high level of uncertainty in the market will give producers certain levers of influence.

The priority of this book is to offer a comprehensive view of the COVID impact on the dynamics of the socio-economic changes in the GCC. This study tries to demonstrate that the GCC countries should not blame only COVID-19 for their misfortunes. It only amplified the negative impact of those processes that were launched a long time ago. The book argues that, under these conditions, it is impossible to expect that the end of the pandemic crisis will lead to a gradual return to the pre-COVID-19 situation. The world has entered an era of frequent market fluctuations, limited predictability and intense competition. Subsequently, the old rules will not work effectively, and any solution to the problems currently experienced by the GCC countries should be focused not so much on fighting the consequences of COVID-19 itself, but on curbing the negative consequences of deep processes, whose damaging impact on the Arab monarchies was only worsened by the pandemic.

The collective monograph shows that the issues experienced by the oil and gas sector of the GCC economies had direct impact on all aspects of the socio-economic and political life of the Gulf states. Subsequently, the set of measures in response to the market changes is supposed to be comprehensive covering not only the oil and gas industry. The key elements of potential response by the GCC member states to faced challenges will also be discussed in the book including:

- prospects for economic diversification;
- role of sovereign wealth funds in the mitigation of the negative impact of oil market crisis to the Gulf economies;
- readjustments in the structure of the international relations of the Gulf countries;
- preservation of the OPEC+ role as market regulator;
- development of renewables and green energy sources;
- promotion of the natural gas role as a transition type of fuel (from hydrocarbon to non-carbon fuels).

The second chapter of the book argues that until very recently, and to the average Gulf citizens, their nation's economy seems to be structured around exchanging oil and gas rents and revenues for expenditures on cars and smart phones. The trouble now is that, as a result of the steep decline in petroleum demand mainly due to the continuous aftermath of Covid-19, and of the resulting glut in supply and the fluctuations in oil prices, those fossil fuel products buy ever fewer imports and build fewer infrastructures. Although oil prices were restored to levels that are pretty acceptable by the industry, they remain insufficient for the public budgets of many Gulf petroleum producers, which need an oil price of at least US$85 per barrel (nominal 2021) to be able to cover their growing expenditures. Consequently, since at least 2014, the public budgets in most Gulf countries have been in red. Nevertheless, the recent unsustainable increase in oil prices to higher levels will sooner or later badly impact the medium- to long-term demand for hydrocarbons. This element will add to another real problem in the Gulf: oil and gas resources in the region started to lose their strategic importance, and their exports to the consuming markets are to further decrease. In fact, as a result of amazing technological advances in recent years, oil and gas are now found almost everywhere, petroleum production is growing almost everywhere, while the consumption of petroleum products and natural gas is declining almost everywhere. Here Covid-19 has been exerting further negative impacts on petroleum demand, especially in the transportation sector.

Chapter 3 by Steven Wright continues this discussion by stating that the COVID-19 pandemic has acted as an accelerant to systemic fiscal challenges the GCC states were projected to face. These longer-term fiscal challenges were a result of fundamental shifts in the global energy market toward lackluster demand, an oversupply of oil and gas, and depressed prices. Moreover, the shift toward carbon -neutrality, and investment in renewables by key regions such as the European Union and China, have added to the long-term outlook on fossil fuel demand. This article examines such trends with respect to Qatar and the LNG sector. It offers reflections on what this has meant for pricing, market convergence, and LNG prospects being increasingly a transitional fuel toward cleaner renewable sources.

In Chapter 4 a collective of authors led by Dr. al-Sarihi discusses the prospects for renewable energy in the GCC during the post-COVID era. According to them, in spite of the abundance of renewable energy resources, especially solar and wind, the current share of renewable energy in the Gulf Cooperation Council (GCC) countries—Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates—does not exceed 1% of the region's total primary energy supply or total installed power capacity. The GCC region holds almost 30% of the world's total proven oil reserves and around 20% of its total proven natural gas reserves. Such abundance of hydrocarbon resources however should not prevent the GCC states from seeking to develop alternative cleaner energy sources due to the following reasons. The region faces the challenges of energy security with demand increasing on average 5% per year; rising greenhouse gas emissions; almost 99% reliance on oil and gas resources to meeting domestic energy needs; and adverse impacts of climate change on the oil and non-oil-based sectors. Renewable energy also presents an opportunity for the GCC countries to diversify their economies away from oil and creating jobs for their growing population. Aware of the aforementioned factors, between 2014 and 2020, the total renewable electricity installed capacity in the GCC states increased by almost 1140%. This paper addresses two questions: what the reasons behind such underutilization of renewable energy resources in the GCC states are, and why there has been a significant increase in the deployment of renewables over the last five years. The paper also assesses the impact of COVID-19 pandemic—which hit the GCC states by a double shock: oil prices collapse and health crisis—on the GCC progress to adopting renewable energy.

Chapter 5 by Dr. Karen Young moves the reader's attention to the issues of the GCC economic recovery from the consequences of Covid-19. Like many countries across emerging markets, the plan for economic recovery from the Covid-19 pandemic across the GCC relies on government outlays in social support and public health, a renewed effort to attract foreign direct investment, access to international debt capital markets and some serious fiscal consolidation. In many ways though, the economic policy response to Covid-19 is just an acceleration of some very specific trends already underway across the GCC. The policy shifts we saw in 2020 are really a continuation of the shifts that began in 2015 with the decline in oil prices. What is new is more differentiation between Gulf Cooperation Council (GCC) state approaches that now lead to a competitive economic policy landscape. This is a broader effect of an energy inflection point in the global economy: plentiful oil supply, less oil demand, more competitive options of renewable energy, and a more discerning investor and consumer of carbon-intensive products.

According to the author, the Covid-19 pandemic is just speeding things along, and we see now a wider aperture across the GCC on: (1) Tax policy (2) Labor market regulation (3) Immigration policy. The pandemic has also made the economic diversification policies that were innovative all the more difficult to execute in the past year. Projects in tourism, airlines, entertainment, along with investment in private schooling and destination or mega-cities could not accelerate as planned. Resilience in these economies has also been weak in unsurprising ways, particularly across job creation and employment. Labor markets are still so contentious across the GCC because of the persistent demographic divide between foreigners and citizens. Citizenship rights and a shared understanding of the social contract continue to define the economic possibilities of Gulf political economies.

Luciano Zaccara and Nesibe Hicret Battaloglu compare the structural socio-political responses offered by the GCC states to the challenges posed by COVID-19 with that of Arab Spring. They argue that like it happened after the Arab Uprisings in 2011, a development originated outside the GCC region directly affected all its members and required a quick response from the authorities. While the responses from the GCC governments to the uprisings was a combination of institutional, redistributive, and repressive measures to guarantee the stability of the political elites and regimes; the Covid-19 Pandemic is demanding even more strategic responses that could guarantee the continuity of the economic models and the social contracts that are at the core of the state formation in the GCC. Having rentier and oil-dependent economies, the Covid-19 pandemic drastically reduced the GCC states income due to the worldwide and mainly Chinese economic slowdown. On the other hand, the worldwide mobility restrictions conditioned economic models heavily relying on foreign manpower. But also, like in the rest of the world, put at stake the government's performances in dealing with the difficulties that the pandemic posed for every GCC state.

Chapter 6 looks into the impact of COVID-19 on the situation with the migrant workers in the GCC. The author attempts to address certain critical questions regarding the topic of the migrant workers in the Gulf region amid the spread of the Covid-19 pandemic, with a focus on the state of Qatar. She argues that the understanding of migration process in the Gulf region requires a systematic and proper contextualization of migration to the Gulf region. Consequently, Menon proposes a new seven-stage concept of Gulf migration including the period of the Covid-19 pandemic that brought the entire world to a standstill.

The issue of climate change and the Gulf policies to handle it are discussed by Greg Shepland in Chapter 8. He rightfully points out that the economies of the GCC countries, having been negatively impacted by Covid-19, now face the longer-term challenge of climate change. Over the coming decades, climate change will affect these countries in several ways. First, countries that consume hydrocarbons may, as part of the transition to renewable energy, buy less oil and gas, reducing the revenues available to GCC governments. Second, climate change will bring higher temperatures and a rise in sea level. Higher temperatures will necessitate the use of more energy for air-conditioning and will also put GCC residents at risk if there are failures in electricity supply, as summer temperatures will be "unliveable" without air-conditioning. Sea-level rise will require large sums to be spent on protecting or moving/rebuilding infrastructure in coastal areas. Third, there will be severe environmental damage, because of factors such as the rise in sea temperatures and more frequent and more severe dust storms. The GCC countries will need to find ways of responding to these challenges.

In Chapter 9 Nikolay Kozhanov argues that the events of 2019–2020 clearly demonstrated the need to review our understanding of the Gulf energy security. Since the late 1960es (if not earlier) its concept has been spanning around the need to ensure the sustainability of oil consumers' access to the regional hydrocarbons. The vision of oil as a unique, finite, and unevenly distributed resource (the demand for which often exceeded the supply) was only making the world further confident that ensuring the energy security of the GCC is solely limited to the stability and physical security of crude imports from the region. However, the picture is much more complex. The security of consumers' interests does not mean that the interests of crude producers are automatically respected. On the contrary, producers' access to consumer markets and their ability to trade hydrocarbon resources at desired prices and in necessary volume should be ensured separately. Moreover, the protection of these interests has key importance for the existence of countries like GCC member states that are heavily dependent on incomes received from oil and gas exports.

For decades and until recently, the global oil market was relatively dominated by oil producers (the degree and nature of this dominance has been uneven for the last 70 years, however), thus, making the task to protect their interests easier. Nevertheless, since the early-2010s the market balance has been gradually changing in favor of buyers. In 2020, the sharp and unprecedented drop in oil demand caused by the coronavirus pandemic led to an equally unprecedented oversupply that changed the oil market in favor of buyers, significantly weakening the position of sellers. This change reduced the importance of hydrocarbons as a "unique" resource, giving its consumers the right to choose among suppliers offering the cheapest price. Suddenly, the GCC countries have received the urgent call to ensure their own sustainable access to markets in order to guarantee the adequate development of their own economies, including the oil, gas, and petrochemical sectors. In other words, there has been a shift in the focus on ensuring the energy security of the GCC countries from protecting the interests of oil consumers to protecting the interests of oil producers.

This, in turn, had the direct impact on the perception of the issue of physical security of hydrocarbon exports from the GCC countries. The growing oil (over)supply and the understanding by oil consumers that the significance of Gulf as a source of oil supplies is decreasing changed the situation a lot. By 2018, consumers had stopped panicking when hearing about production shocks caused by political risks in the Persian Gulf, Middle East, and even beyond. It is notable that, in 2018–2019, neither the instability of oil production in Libya, nor the practical disappearance of Iran and Venezuela from the market had long-lasting effect on prices (at best, they were only preventing them from further sharp decline). Even the supposedly Iranian-inspired attack on Saudi Arabia's oil production and refining infrastructure in September 2019 had only a short-term impact on the market although the volume of oil single-time taken from the market was historically unprecedented since 1973. Under these circumstances, it is not surprising that in the context of a much larger excess of oil supply in 2020 caused by COVID-19, the world has almost ceased to respond to the Iranian–American tensions in the Gulf, in particular, without noticing either the resumption of the USA and Iran confronting each other in the spring of 2020, or new attempts by the Houthis to shell the territory of the KSA and UAE in 2021–2022.

The discussion of the issue of energy security is continued in Chapter 10 that studies the dynamics of Iran–Saudi relations. According to the authors, the relationship between the GCC and their neighboring country Iran is far too complex to be defined by a Sunni–Shiite rivalry or by an Arab–Persian rivalry only. This relationship is also framed by the question of the energy security of one of the richest oil and energy regions in the world. With invested interest in the region by a number of global players, the clash of ethnicities and minority groups, a number of political and cultural dilemmas, and border disputes, Iran and the Gulf lay at the front line of conflict and tension. This chapter looks closely at the rivalry between Iran, and the biggest and most influential Gulf state, the Kingdom of Saudi Arabia. Although their conflict has been aggregated by a number of past and current issues, yet, in the last couple of years, the tension has escalated further by an event, and a main player, and those would be the Oil Crisis, and the former American president, Donald Trump. The use of oil as a political tool is widespread, and America's foreign policy toward the two Middle Eastern countries, Iran and Saudi Arabia is no different. The oil crisis is a stage of ongoing conflict for the two countries, and this paper will investigate what this crisis means to the area, and the impact of the USA on the rivalry and the establishment of energy security.

Chapter 11 of the book attempts to analyze future prospects for OPEC+. First, it briefly revisits the origins of contemporary OPEC and non-OPEC cooperation since the signing of the Declaration of Cooperation in 2016 and the alliance's approach to market balancing in 2020 until the present day. The circumstances of each period have been critical in shaping the current state of OPEC and non-OPEC cooperation and will have a considerable impact on the group's trajectory in the long term. The alliance has endured crises before, but the life of the DOC has so far been short enough that many of the dynamics governing the views of key members early on remain highly relevant in the present day. Then, the chapter examines the dynamics shaping OPEC+and its market balancing strategy through 2021 until the eve of Russia's invasion of Ukraine. During this time, the group's acute lack of spare capacity grew in its significance as a key oil market variable, calling attention to the fact that its ability to manage markets would likely become increasingly constrained in both the near and long term. Even without the considerable volatility presented by Russia's uncertain future with the group, this factor will likely contribute to many issues surrounding group cohesion in the coming years. As wealthier producers invest in additional spare capacity while their less prosperous counterparts struggle to reverse capacity losses due to natural declines or aging, poorly maintained infrastructure, the national interests of the group's members will diverge to an ever greater degree.

Chapter 11 gives special focus to the oil market impact of the Ukraine war, which represents a critical juncture for OPEC and non-OPEC cooperation. The invasion triggered one of the largest energy market price shocks in decades, leading prominent oil market commentator Javier Blas to draw comparisons to the market disruptions of 1973, 1979, and 2003. Notably, these historic supply disruptions largely took place as a result of geopolitical dynamics concentrated in the Middle East; Russia's status as a major global power in addition to being one of the top three oil-producing countries in the world underscores the truly unprecedented nature of the still-unfolding situation. Finally, the chapter turns its attention to future prospects for OPEC and non-OPEC cooperation within the framework of the DOC. In order to mitigate the effects of a rapidly evolving situation in both Russia's war on Ukraine and its implications for the global economy, the chapter will consider potential impacts of the crisis, as well as some of the ways in which OPEC+may choose to address its spare capacity issues as the primary determinants of the group's future. Indeed, it is currently difficult to suggest that any other factors would be as impactful or relevant to the future of OPEC and non-OPEC cooperation, which for a time was viewed by many as a potentially permanent feature of oil markets, potentially long after peak oil demand has been reached.

Chapter 12 by Jalal Qanas analyzes the Sino-GCC relation and their mutual growing interdependency. It also examines the new Chinses Belt and Road Initiative (BRI) and the role of the GCC countries in it. The chapter argues that Sino-GCC economic relations started growing in the 2000s when GCC countries started looking toward East due to declining oil demand in the West. In 2004, the free trade agreement was signed, and in 2010, China–GCC business form was founded to strengthen the bilateral ties. In 2014, the Chinese president met GCC delegation to promote belt and road initiative. Both parties agreed to cooperate with each other for successful implementation of the BRI project to achieve mutual economic gains. Since then, China has successfully developed strategic economic partnerships with all six GCC countries to increase its foothold in this region. The maritime location of GCC strengthens the Chinese military presence in Africa. GCC's strategic location also facilitates the Chinese expansion in Indian Ocean. Cooperation of GCC is also vital for implementing the China–Pakistan corridor project. BRI has also cemented the Sino-GCC strategic relations, as GCC countries are currently considering BRI as an opportunity to implement their economic visions that are based on economic diversification. The project has enabled China to play wider economic role in GCC, and strong presence in this region serves multiple geopolitical objectives of BRI. However, some key factors that are limiting the China's engagement in GCC include domestic conflicts, regional rivalry, GCC's sensitivity to U.S.' concerns, China's hesitation to securitize its footprint in GCC by applying military power, its core focus on expanding economic and technological cooperation, neutral stance on geopolitical conflicts, and China's reluctance to directly challenge the U.S. dominance in GCC region.

CHAPTER 2

Challenges Facing the Gulf Petroleum Industry: Covid-19, New Technologies, Energy Transition

Naji Abi-Aad and Nikolay Kozhanov

2.1 Introduction

The outbreak of the Covid-19 epidemic and the resulting economic downturn have undermined the already weakened position of the global oil and gas industry. Since the transportation sector depends on 60 percent of energy from oil consumption, movement constraints were quickly interpreted into reduced oil demand. Consequently, various crude oil indices reached their lowest level by mid-2020, when the daily global oil consumption declined to less than 75 million barrels, compared to some 100 million barrels earlier that year, before recovering afterward.

The demand for natural gas has also fallen sharply due to widespread quarantine in various parts of the world, especially China, India, and

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N. Kozhanov et al. (eds.), *GCC Hydrocarbon Economies and COVID*,
https://doi.org/10.1007/978-981-19-5462-7_2