Impact of the GCC Crisis on Global Energy Markets

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For decades, Gulf Cooperation Council (GCC) countries have been a pillar of the global energy market for their wealth of resources and political stability. However, their current infighting might lead to a strategic shift in how the world looks at the geopolitics of the GCC. The diplomatic row that began on June 5, when Saudi Arabia, the United Arab Emirates (UAE), and Bahrain cut diplomatic relations, transport links, and trade ties with Qatar, has been contained but remains in place. While there is no immediate impact on energy trade, the uncertainty and longevity of the crisis might have long-term reverberations in the global market.

Energy Supply Routes

Accounting for nearly 40 percent of global oil reserves and 24 percent of gas reserves, GCC countries benefited between 2011 and 2014 mostly from the growing demand in emerging markets and the Middle East's political unrest, with oil prices exceeding $100 per barrel. Since then, traditional concerns about oil and gas supply routes have increased. The current GCC crisis will only intensify them.

While the initial shock of the measures against Doha was absorbed, confusion prevailed in the energy and shipping markets. Supertankers typically travel back-to-back around multiple GCC ports to load nearly two million barrels of crude oil per month and save on transportation costs. The UAE's al-Fujairah port, located near the Strait of Hormuz, serves as the major bunkering hub where ships transit on their way to Asia, Europe, and North America. Since the diplomatic row began, these tankers were left with no clear guidance on the restrictions they might face in their traditional routes. The International Energy Agency (IEA) noted that the GCC spat caused "logistical headaches," with a backlog of cargoes and increasing shipping costs.

For instance, two UK-bound Qatari liquefied natural gas (LNG) shipments on June 8 abruptly changed direction in the Gulf of Aden, which led to a spike in UK and US natural gas futures. There was no clarity as to whether the measures taken against Doha in the Suez Canal apply to all vessels coming in and out of Qatari ports or strictly to Qatari-owned vessels. If the canal is ultimately closed for Qatari LNG exports—an event not supported by international law—then carriers heading to Europe will have to add three to four weeks of travel via Africa to their itinerary.

Furthermore, on June 7 the Abu Dhabi Petroleum Authority issued two contradictory circulars that added to the confusion. While the first circular eased restrictions on oil tankers going to and from Qatar, the second circular later in the day denied entry "for all vessels arriving from, or destined to Qatar, regardless of its [sic] flag." In addition to Jebel Ali, the UAE's al-Fujairah port serves as the oil trading hub and a major refueling point for all ships entering or leaving the Gulf area.

Qatar and its willing trade partners came up with ways to circumvent these sanctions.

Maersk, the world's biggest container line, opened an alternative route to transport LNG containers in and out of Qatar via Oman's Salalah Port. On June 20, Qatar Petroleum launched a "temporary" ship-to-ship fuel bunkering facility at Ras Laffan. Qatar's Hamad Port is also looking to sign agreements with shipping companies to improve direct services; India's Mundra Port was one of the first signatories. Ships from China's Shanghai are now re-routed via Iraq, making the voyage to Qatar 27 instead of 20 days long. The other alternative for Qatar, which comes with political risks, is to take the Iranian route.

Even with traders scrambling to adjust their routes, it is worth noting that the ban is not as strict on energy products as it is on other commodities. In fact, nine out of 13 tankers that loaded crude oil in Qatar since June 5 also took cargo from Saudi Arabia and/or the UAE. Despite European concerns that Egypt could close the Suez Canal, international vessels carrying Qatari LNG are still passing through the canal, though at a lower rate than before the crisis. All this uncertainty is exposing the vulnerabilities of the GCC energy market. The oil market remains volatile, Dubai is losing some of its bunkering role to Oman, and shipment companies are now using small tankers to make separate stops in GCC ports, while Qatar might have to increase the price of its gas to accommodate all these adjustments.

The LNG Market as a Stabilizing Factor

Saudi Arabia's Minister of Energy, Industry, and Mineral Resources Khaled Al-Falih was right when he said he expected the crisis not to have an immediate impact on the crude oil market. The deal reached in December 2016 by the Organization of Petroleum Exporting Countries (OPEC) limiting oil production to 1.2 million barrels per day remains intact. Last May, that agreement with non-OPEC members like Russia was extended until March 2018. Qatar produces only 2 percent of the agreed-upon OPEC deal, or 30,000 barrels per day. Short of military intervention in Qatar, the oil market should not be impacted. The greatest danger to the energy market remains a drop in crude oil prices if the current OPEC deal is not respected or not extended beyond March 2018.

In contrast to the oil market, Qatar is a global leader in LNG, ranking third in natural gas reserves after Russia and Iran and providing 30 percent of the world's LNG supplies, mainly to Asia and Europe. A disruption in the production, shipment, or pricing of Qatari LNG could impact European countries, compelling them to rely instead on Russian gas—a move they would prefer to avoid considering political tensions with Moscow. Indeed, there has been a realization by all sides that disrupting the global energy market would trigger alarm bells, most notably in Europe and Asia; hence, disrupting LNG exports has remained a red line throughout the crisis.

Furthermore, the concerned parties in the GCC crisis did not trigger a full-fledged energy war among them. Qatar did not shut the Dolphin gas pipeline that transports LNG from its North Field to the UAE, Oman (which received more than two billion cubic feet per day), and Egypt (which, last year, imported 60 percent of Qatar's LNG via third party traders). In return, the UAE and Egypt did not completely shut off Qatari LNG transiting through Jebel Ali and the Suez Canal. Abu Dhabi owns 51 percent of the Dolphin pipeline while the UAE's gas system relies on gas imports from Qatar, hence potentially making the national electric grid vulnerable to a blackout. However, any move by Qatar to cut the gas supply to the UAE and Egypt not only means an all-out escalation but also could damage the country's reputation as a reliable leader in the global gas market. That is more significant than ever now in light of Qatar's decision in April 2017 to lift the moratorium on development of the North Field, which would ultimately allow Doha to produce an additional two billion cubic feet per day.

The Long-term Impact of the Crisis

Energy security is no longer a given in the Middle East with political instability surrounding key waterways, most notably the Suez Canal, Bab al-Mandab, and the Strait of Hormuz. GCC countries that have long resisted making a concerted effort to pursue energy security because of national sovereignty sensitivities are entering a new era during which securing their trade routes will be an essential part of their mode of operation.

In that sense, Washington's ambivalent position has raised questions in Europe and Asia, considering their countries' vulnerabilities to the ongoing crisis. Two key factors played out in recent weeks: 1) Washington, or at least the White House, briefly backed away from its role as a stabilizing force in the GCC; and 2) the United States understood that it is immune from any direct economic impact from the crisis. Indeed, the United States last imported gas from Qatar in 2013, while—during the last year alone—it received 11 percent of its petroleum needs from Saudi Arabia, ranking a distant second after Canada (38 percent). Although US dependence on Middle East energy sources has decreased significantly in the past decade, any shortage internationally will create uncertainty and impact the global economy; an example is the United Kingdom, which imports a third of its natural gas from Qatar and would face serious energy challenges if that were to change.

Obviously, beyond energy, there are other components of US policy that are important to address in this context, mainly the al-Udeid military base in Qatar, which houses nearly 11,000 US personnel, the strong partnership with the GCC countries, and the regional fallout of the ongoing crisis. Washington would be wise to balance these relationships and calculations, and Secretary of State Rex Tillerson has recently taken the lead in facilitating the mediation efforts—which so far have no clear end in sight. The ambiguity of US policy and the status of these reconciliation efforts are leaving the energy market on edge regarding what to expect, even though the assumption is that diplomacy trumps disputes when the global energy market is at risk.

While business as usual was not disrupted, the brief chaos concerning supply routes will have a long-term effect. European and Asian countries will most likely rethink how much their economies should rely on energy resources from the GCC market. With global oil demand expected to remain high until 2040, most notably for road freight and aviation, renewables and natural gas are becoming the future of energy sources in the coming two decades. The price volatility of crude oil in recent years is compelling economies around the world to become less dependent on oil. Meanwhile, competitive gas suppliers are emerging in Australia, North America, and Iran.

The most crucial strategic impact of the GCC crisis is the damage that has been largely self-inflicted. For the first time, GCC countries showed readiness and willingness to potentially endanger their energy security for political ends. While the daily operations were not significantly disrupted, the cloud the Qatar crisis has left will not go away soon enough.