

The Economic Dimension of a Pivot Away from the Middle East

Mark Finley

In many aspects, the direct linkages between the economies of the Middle East and the United States are small—at least in relation to the size of the US economy. But the centrality of oil to the US (and the global) economy, combined with the outsized influence the Middle East region has on the global oil market, makes the region a critical factor in the United States' economic well-being. While an eventual transition away from oil and other fossil fuels is likely to change this dynamic, this transition is expected to be slow, meaning the Middle East will loom large for US economic security interests for decades to come.

The countries of the Arabian/Persian Gulf have, to different degrees, long been central to the production and export of hydrocarbon products to the United States and the rest of the world. For this reason, the following data and analysis will focus, where possible, on these nations, although other producers in North Africa—Libya and Algeria, for example—also play an important role in the supply of oil and natural gas to the international economy.

The Big Picture: Direct Economic Connections Are Limited

The countries bordering the Arabian/Persian Gulf (hereafter, the Gulf states: Bahrain, Iran, Iraq, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates) comprise a relatively small share of the global population and economy, 2 percent and 4 percent, respectively.¹ Additionally, these countries account for relatively small shares of key indicators of US economic and financial relationships: just 2 to 3 percent of US trade in goods and services (in dollar value). Indeed, none of these countries is a top-20 trading partner for the United States among importers or exporters.² One strategically important exception to this overall picture of a small role for the Gulf states in US trade is arms sales, where the Middle East accounted for roughly 40 percent of American global exports from 2018 to 2022.³

Similarly, the United States is not a large trading partner from the perspective of the Gulf states; the US is the largest exporter to only Qatar, ranking behind China for all other countries under discussion here.⁴ For energy trade, nearly 80 percent of the region's oil and liquefied natural gas (LNG) exports are sold in Asia, compared with 3 percent of oil exports (and no LNG) being sold to the United States.⁵ Moreover, the Gulf states are not large contributors to other dimensions of US international economic relations; they account for small shares of US foreign direct investment

-
- 1 "Global Population Data for 2021," World Bank, undated, <https://data.worldbank.org/indicator/SP.POP.TOTL.>; "GDP Based on PPP, Share of World," International Monetary Fund, undated, <https://www.imf.org/external/datamapper/PPPSH@WEO/OEMDC/ADVEC/WEOWORLD>.
 - 2 For trade rankings, see: "U.S. International Trade in Goods and Services, December and Annual 2022," U.S. Census Bureau and U.S. Bureau of Economic Analysis, February 7, 2023, https://www.census.gov/foreign-trade/Press-Release/ft900/ft900_2212.pdf. For shares of trade in goods in 2022, see: "U.S. Trade in Goods by Country," U.S. Census Bureau, undated, <https://www.census.gov/foreign-trade/balance/>. For shares in trade in services in 2021, see: "Table 2.2. U.S. Trade in Services, by Type of Service and by Country or Affiliation," U.S. Bureau of Economic Analysis, July 7, 2022, <https://tinyurl.com/3f3du26m>.
 - 3 Pieter D. Wezeman et al., "Trends in International Arms Transfers, 2022," Stockholm International Peace Research Institute, March 2023, https://www.sipri.org/sites/default/files/2023-03/2303_at_fact_sheet_2022_v2.pdf.
 - 4 "Saudi Arabia Trade," World Integrated Trade Solution Database, undated, <https://wits.worldbank.org/countrysnapshot/en/SAU>. Unfortunately, country-specific data on export destinations *from* the Gulf states is not widely available (for many Gulf states, "unspecified" is by far the largest export destination), so we report here only leading countries exporting *to* the Gulf states.
 - 5 "Statistical Review of World Energy," BP, 2022, www.bp.com/statisticalreview.

(both inbound and outbound, at 6 percent and 1 percent, respectively), and hold just 4 percent of the total number of US Treasuries held abroad.⁶

The (Indirect) Importance of Oil

Like other direct indicators of US international economic relations, US oil imports from the Gulf states are relatively small.⁷ The impact of the US “shale revolution” on both American oil import dependence and global oil markets has been well-documented. With the US now a small net oil exporter, a widespread impression in the US has developed, which sees the country as no longer vulnerable to Middle East regional developments. But the oil price spike of 2022 exposed the myth and reminded US policymakers and consumers that the oil policies of the Gulf states remain critical elements of the United States’ economic well-being—at least for now. In the US (and elsewhere), soaring fuel prices have boosted inflation, damaged consumer and business confidence, and lowered the approval ratings of political leaders.⁸

In 2022, the US Department of Energy reported that the US imported about one million barrels per day (mbd) from the Gulf states—12 percent of total (gross) oil imports, sufficient to meet 5 percent of domestic demand. This is well below the peak of 2.8 mbd imported in 2001, which represented nearly a quarter of US imports and 15 percent of domestic demand.⁹ These reductions are similar to those among most other US oil trading partners, and have been driven by the growth of domestic production (the shale revolution), which has made the United States the world’s largest producer of oil (and natural gas), and has turned it from the world’s biggest oil importer into a small net exporter. It is important to note that while the United States is a *net* oil exporter, it remains intricately connected with global markets for both crude oil and refined products due to

6 “Direct Investment by Country and Industry, 2021,” U.S. Bureau of Economic Analysis, July 21, 2022, <https://www.bea.gov/sites/default/files/2022-07/dici0722.pdf>.

7 Note that this discussion includes both crude oil and refined products such as gasoline and diesel when referring to “oil.”

8 Mark Finley and Anna Mikulska, “Energy Transition, Energy Security, and Affordable Fuel: How the Energy Crisis Can Help Policymakers ‘Thread the Needle,’” Baker Institute for Public Policy, August 5, 2022, <https://www.bakerinstitute.org/research/energy-transition-energy-security-and-affordable-fuel-how-the-energy-crisis-can-help-policymakers-th>.

9 “Petroleum and Other Liquids: U.S. Imports by Country of Origin,” U.S. Energy Information Administration, undated, https://www.eia.gov/dnav/pet/pet_move_impcus_a2_nus_ep00_im0_mbbldpd_a.htm.

the complexities of managing a continent-wide marketplace and because of quality and regional mismatches between domestic oil production and refining capacity. In 2022, the US Energy Department reported that the United States *exported* 9.6 mbd of crude oil and refined products, while *importing* 8.3 mbd.¹⁰

But while the United States has achieved overall self-sufficiency and reduced its direct dependence on imports from the Gulf states, its economy remains vulnerable to oil price shocks because oil remains the US economy's largest energy source. And vulnerability in turn means that the Gulf states remain vital to US economic interests because of their central role in driving global oil markets. Within the US, oil last year accounted for 36 percent of total domestic energy consumption. This was followed by natural gas (33 percent of total energy use), renewable energy (13 percent), coal (10 percent), and nuclear energy (8 percent).¹¹ Moreover, oil is the world's largest energy source, in 2021 accounting for over 30 percent of global energy use (followed by coal and natural gas, at 27 percent and 24 percent, respectively).¹² And in the global context, the Gulf states remain central players. They account for nearly half the world's proven oil reserves, roughly 30 percent of global production, and one-third of global oil trade. Indeed, the US Energy Department estimates that roughly 20 mbd flow through the strategic Strait of Hormuz daily.¹³

The importance of the Gulf countries to the global oil market is further accentuated by their participation in OPEC and the larger "OPEC+" group, through which they seek to cooperatively manage oil supply and prices. The OPEC+ group was organized in 2016 in response to the dramatic growth in US shale production, which was taking global market share at the time, and which had caused OPEC countries to engage in a damaging price war with US producers a year prior. Bringing Russia and other cooperating countries into the group greatly increased the share

10 "Monthly Energy Review, Table 3.1 Petroleum Overview," U.S. Energy Information Administration, undated, <https://www.eia.gov/totalenergy/data/browser/index.php?tbl=T03.01#/?f=A&start=1949&end=2022&charted=6-12-15>.

11 "Monthly Energy Review, Table 1.3 Primary Energy Consumption by Source," U.S. Energy Information Administration, undated, <https://www.eia.gov/totalenergy/data/browser/index.php?tbl=T01.03#/?f=A&start=1949&end=2022&charted=1-2-3-5-12>.

12 "Statistical Review of World Energy."

13 "The Strait of Hormuz Is the World's Most Important Oil Transit Chokepoint," U.S. Energy Information Administration, June 20, 2019, <https://www.eia.gov/todayinenergy/detail.php?id=39932>.

of global oil production under active management, and has been a key element in the improvement of political ties between Russia and the Gulf states.¹⁴ Finally, and critically, these countries account for virtually all of the world's spare production capacity—unused production facilities that can be quickly tapped to increase production in an emergency, currently estimated at about 3.5 mbd.¹⁵ The region's spare capacity in particular commands significant influence in global oil markets in times of crisis.

The global nature of the oil market is what connects US vulnerability to the Gulf countries, even though direct US oil purchases from the region are small. Both crude oil and refined products are widely traded internationally, and the fact that shippers can divert cargoes to seek the highest profits means that changes in prices of both crude and refined products in the US are closely correlated with global price changes. In essence, the lesson for US policymakers and consumers is that when the price of oil increases anywhere in the world, it increases everywhere, and that developments in the Gulf states therefore matter for US “prices at the pump.”

Recognition of this connection was evident in US President Joe Biden's July 2022 visit to Saudi Arabia, part of a (failed) attempt to convince the kingdom's leaders to increase production. With prices at the pump soaring in the run-up to that year's US midterm elections, Biden, who had earlier promised to make Saudi Arabia a pariah due to its human rights violations, was forced to seek assistance from a country that held the lion's share of global spare production capacity.¹⁶ His request was rejected, and indeed Saudi Arabia followed up by working with Russia in October 2022 to announce large production cuts by the OPEC+ group.¹⁷

14 Kristian Coates Ulrichsen et al., “The OPEC+ Phenomenon of Saudi-Russian Cooperation and Implications for US-Saudi Relations,” Baker Institute for Public Policy, October 18, 2022, <https://www.bakerinstitute.org/research/opec-phenomenon-saudi-russian-cooperation-and-implications-us-saudi-relations>.

15 “Short-Term Energy Outlook Data Browser, Table 3c.: OPEC Crude Oil (Excluding Condensates) Production,” U.S. Energy Information Administration, May 9, 2023, <https://www.eia.gov/outlooks/steo/data/browser/#/?v=7>.

16 Steve Holland et al., “Biden Fails to Secure Major Security, Oil Commitments at Arab Summit,” *Reuters*, July 16, 2022, <https://www.reuters.com/world/middle-east/biden-hopes-more-oil-israeli-integration-arab-summit-saudi-2022-07-16/>.

17 Hanna Ziady, “OPEC Announces the Biggest Cut to Oil Production since the Start of the Pandemic,” *CNN Business*, updated October 5, 2022, <https://www.cnn.com/2022/10/05/energy/opec-production-cuts/index.html>.

Looking Ahead: Dependence or Independence?

Will US vulnerability to oil shocks—and with it the economic importance of the Gulf states to US strategic interests—ease in the future? Such an outcome is widely anticipated in both the United States and the region, as electric vehicles are expected to displace the internal combustion engine and more aggressive climate policies loom on the horizon. This has contributed to the discussion of a potential US pivot away from the region. But the pace of the “energy transition” is highly uncertain and is likely to play out over several decades. Uncertainty is a crucial dimension of this discussion; as the great American folk-philosopher and baseball player Yogi Berra is reported to have said, “It’s tough to make predictions, especially about the future.”

The US Energy Department’s reference case projects that oil will remain the country’s leading energy source in 2050 (at 34 percent of energy use), with consumption of about 20 mbd—close to current levels.¹⁸ In contrast, in 2021 the International Energy Agency’s (IEA) sustainable development scenario projected that US oil demand could fall by 70 percent by 2050, at which point it would account for only about 15 percent of total energy use.¹⁹ To a certain degree, these outlooks differ because they serve different objectives: the US Energy Department seeks to show the most likely outcome based on current policies, while the IEA’s outlook is a “what if” scenario showing the need for additional policies to achieve a sustainable outcome. Importantly, the IEA emphasizes that massive actions would be needed beyond existing policies or even current governmental commitments to achieve its scenario. But the massive range of potential oil demand outcomes across these analytic efforts highlights the tremendous uncertainty of future developments in public policy (especially regarding climate change), as well as the pace of technological innovation. And in turn, these uncertainties drive a similarly large range of potential future pathways for future US (and global) oil demand.

While acknowledging that the US and global long-term oil demand outlook is massively uncertain, one can confidently project that, on

18 “Annual Energy Outlook 2023, Table 11: Petroleum and Other Liquids Supply and Disposition (Reference Case),” U.S. Energy Information Administration, 2023, <https://www.eia.gov/outlooks/aeo/data/browser/#/?id=11-AEO2023&cases=ref2023&sourcekey=0>.

19 “World Energy Outlook 2021,” International Energy Agency, October 2021, <https://www.iea.org/reports/world-energy-outlook-2021>. Note that the IEA’s subsequent “World Energy Outlook 2022” included a net-zero scenario but did not include detailed country-specific oil consumption for 2050 in its public data release.

current trends, it appears likely that the US economy's dependence on oil will persist for decades to come, and that US strategic planning must act more aggressively to reduce that dependence, or to plan for how to address continued vulnerability.

The Gulf region's importance to global oil supplies and trade may grow in the medium term, with Saudi Arabia, the UAE, and Iraq all planning to increase oil production capacity within the next five years. And the easing of western sanctions against Iran—or increased sanctions-busting—could see additional supplies return to the market. Over the longer term, much will depend on the (highly uncertain) pathways for global oil demand and non-OPEC supply—but the region's large, low-cost base of oil reserves suggest that it will continue to play a leading role, even if the global market shrinks significantly. Indeed, the market share for OPEC countries (with Gulf states playing the leading role) is predicted to rise from now until 2050 in all of the IEA's scenarios.

From the perspective of regional oil producers, this same uncertainty regarding future oil demand trends looms large—though it is important to note that many oil producers believe that future oil demand prospects are relatively robust, and will be driven by emerging economies, even as the industrialized world's vehicle fleet electrifies rapidly. For example, OPEC's *World Oil Outlook 2022* predicted that global oil demand will reach nearly 110 mbd by 2045, up from about 100 mbd currently.²⁰ The possibility that aggressive climate mitigation policies will cause a sharp reduction in global oil demand is nonetheless driving the urgency of regional efforts to diversify economic activity and government revenues away from oil production and export. For example, Saudi Arabia's *Vision 2030* and its related *National Transformation Program* seek to diversify the Saudi economy and reduce its dependence on oil revenues, and to achieve a broader transformation of the Saudi government and society.²¹ Additionally, the possibility that US oil dependence may decline is adding to concerns about the future of US oil security guarantees and driving (or at least contributing to) the region's efforts to steer a more neutral path on the global stage.

20 "World Oil Outlook 2022," Organization of the Petroleum Exporting Countries, 2022, https://www.opec.org/opec_web/en/publications/340.htm.

21 "Vision 2030," Kingdom of Saudi Arabia, undated, <https://www.vision2030.gov.sa/>; "National Transformation Program," Kingdom of Saudi Arabia, undated, <https://www.vision2030.gov.sa/v2030/vrps/ntp/>.

The question of dependence also looms large for the Gulf states themselves, especially regarding their dependence on oil exports for both economic growth and government revenues. Much depends on the success of national economic diversification plans. Success in these efforts could allow the Gulf states to pursue long-term oil strategies aimed at maintaining low prices and growing market share as a means to monetize their large hydrocarbon resources without depending on high prices to sustain government revenues.²² But note that the near-term revenue requirements of these diversification programs have ironically raised the importance of near-term oil revenues and increased the likelihood of efforts to boost short-term revenues by cutting production.²³ Moreover, the focus on sustaining high oil prices to boost revenues would be longer-lived if a failure to diversify leaves these states highly dependent on oil exports over the longer term.

What Would a Pivot Mean for Economic Interests?

With the shale revolution having made the United States a significant exporter of both oil and natural gas, there is a newly important additional dimension to the US-Middle East economic relationship, namely one of competing suppliers. A US “pivot” away from the region would risk raising the profile of the United States as a competing producer. As with oil demand, the outlook for oil supply is massively uncertain, but the US Energy Department’s long-term outlook projects a small increase in domestic US oil production and exports between now and 2050, and a doubling of US LNG exports (with the United States already having surpassed Qatar as the world’s largest LNG exporter).²⁴ For oil, Gulf producers led by Saudi Arabia engaged in a price war in 2014 and 2015 that sought to discipline US shale producers and

22 Spencer Dale and Bassam Fattouh, “Peak Oil Demand and Long-Run Oil Prices,” Oxford Institute for Energy Studies, January 2018, <https://a9w7k6q9.stackpathcdn.com/wpcms/wp-content/uploads/2018/01/Peak-Oil-Demand-and-Long-Run-Oil-Prices-Insight-25.pdf>.

23 Summer Said and Stephen Kalin, “Saudi Arabia’s Oil Production Cuts Reflect Cost of Reshaping Economy,” *Wall Street Journal*, April 3, 2023, https://www.wsj.com/articles/saudi-arabias-oil-production-cuts-reflect-cost-of-reshaping-economy-7fb6e09c?mod=Searchresults_pos1&page=1.

24 “The United States Became the World’s Largest LNG Exporter in the First Half of 2022,” U.S. Energy Information Administration, July 25, 2022, <https://www.eia.gov/todayinenergy/detail.php?id=53159>.

investors.²⁵ While price wars are clearly damaging to the Gulf states' revenues as well, a US pivot away from the region could lead to more confrontational oil policies.

In addition to its potential impact on oil price volatility, a US pivot could also impact the reliability of Gulf state oil exports. Would the withdrawal of the US military/security umbrella embolden opponents of regional regimes? The potential interruption of oil flows through the Strait of Hormuz, as well as the actual disruption of Saudi production following the September 2019 attack on Eastern Province oil facilities (and subsequent attacks on facilities in the UAE), highlight the potential risks. Alternatively, would a US pivot (either real or prospective) drive the Gulf states to be more active in managing their regional conflicts in a way that would reduce risks to oil supplies?

Current trends suggest that the US is likely to remain vulnerable to oil price volatility, and that the Middle East is likely to remain a key driver of global (and therefore US) oil prices. And in turn, these trends suggest that the Gulf countries will remain important to US and global economic well-being. Accordingly, without a greater policy focus on accelerating the move away from oil within the US economy, a pivot away from the Middle East will remain challenging, at least economically.

25 A brief—and intense—price war in the early days of the global COVID-19 pandemic in 2020, meanwhile, was driven by Russia's reluctance to join OPEC in aggressive production cuts, and saw US oil prices dip briefly below zero. While US production fell sharply due to the price war, shale producers were not the immediate target.