

How does the Gulf manage the next phase of its love affair with oil?



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Oil has given Saudi Arabia global clout and presence far out of proportion to its population of 30 million. (Reuters)

By a simple fact of geology, the future of the countries of the Arabian Gulf is inextricably linked with the energy business, and in particular with the oil industry. This is the central tenet of the newly published book “Energy Kingdoms” by Jim Krane, former Gulf-based journalist-turned-academic at the Baker Institute for Energy Studies at Rice University in Houston, Texas.

Oil has been responsible for the explosive increase in the Gulf states’ living standards, and for the booming economic development they have experienced since the 1970s, when they managed to persuade the world to pay a reasonable price for the “black gold” that the West had been getting on the cheap until then. Two examples in particular illustrate the importance of oil as an economic determinant. Dubai, ironically because it did not have much oil to begin with,

used oil revenue as seed capital to develop its potential as a hub for transport, trade and tourism. The emirate also offered a haven for oil executives working in less comfortable environments in the region.

Saudi Arabia, on the other hand, is the full-on oil economy, blessed with quantities beyond the dreams of oil explorers in the 1930s. Oil has been the Kingdom's most precious natural resource ever since, and has enabled a standard of living unimaginable to Saudis just a few decades ago. It has also given the Kingdom global clout and presence far out of proportion to its population of 30 million.

Now, Krane argues persuasively, the symbiotic relationship between oil and the “energy kingdoms” of his title is reaching a critical phase. For a number of reasons — mainly shifting demography, domestic economics, global energy forces and environmental change — policymakers in the region might have to rethink, or at least recalibrate, their love affair with oil. The future of the Middle East, and arguably the world, depends on them getting it right.

The “camels to Cadillacs” phenomenon — by which modernization and development were rushed into the Gulf's traditional societies in a few decades — depended above all on the social contract between the rulers of those states and their subjects. Loyalty was assured by guaranteeing economic wellbeing and physical security for the people.

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Above all, that wellbeing demanded energy to provide power, water and comfort in a demanding climate that had previously made all those things extremely difficult. Krane cites the example of Mohamed Alabbar — humbly born one of many children to a dhow captain in the UAE, now the billionaire entrepreneur behind the Emaar empire — as an allegory for that transformation. In many ways, the region has been a victim of its own success in this respect. Cheap,

subsidized energy unleashed a dramatic increase in population, living standards and economic activity that have outstripped the resources of the states to maintain them.

The issue is exacerbated by the fact that subsidies, once granted, often come to be regarded as a right, and are hard to remove without causing widespread public discontent. However, the traditional assumption that cancelling subsidies is automatically a trigger for social unrest is challenged in the book.

Subsidies reduce the price of energy for consumers, but also affect appreciation of its value. Gulf states are energy guzzlers on an extraordinary scale, even in comparison with parts of the world, such as Arizona, that have similar climate demands. There is no escaping the conclusion that the citizens of the region are wasting their most precious asset. Furthermore, big energy consumption at home means that there is less to export to earn the petrodollars that fund the whole cycle. Policymakers in Saudi Arabia and elsewhere are aware of this, hence the big push by Saudi Aramco and others to increase the proportion of domestic power generated by gas, of which the Kingdom is similarly blessed, and the move into petrochemical production.

Saudi attempts at subsidy reduction get praise from Krane, who proves their efficacy statistically. The summer time “crude burn” — when oil is consumed to fire the Kingdom’s gigantic demand for air conditioning and cold water — has fallen over the past three years since subsidy reform began.

Krane ends with a futuristic chapter that looks at regional energy policy against the background of global climate change, which will challenge the hitherto-undisputed position of oil as the world’s energy source of choice. “Energy Kingdoms” should be an essential read for anybody concerned about the future of the Gulf.

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