

The consequences of Russia's invasion of Ukraine on global energy and the diversification of the GCC economies

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Economic Diversification in the Gulf States: Reality and Perspective

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Security of supply - traditional approach

- The Russian invasion of Ukraine has revived strong concerns for security of supply
- Traditional definition: The uninterrupted availability of energy at affordable prices
- Key components:
 - Allocation through market mechanisms
 - Interdependence as guarantee of stability

Security of supply – post Russia's invasion of Ukraine

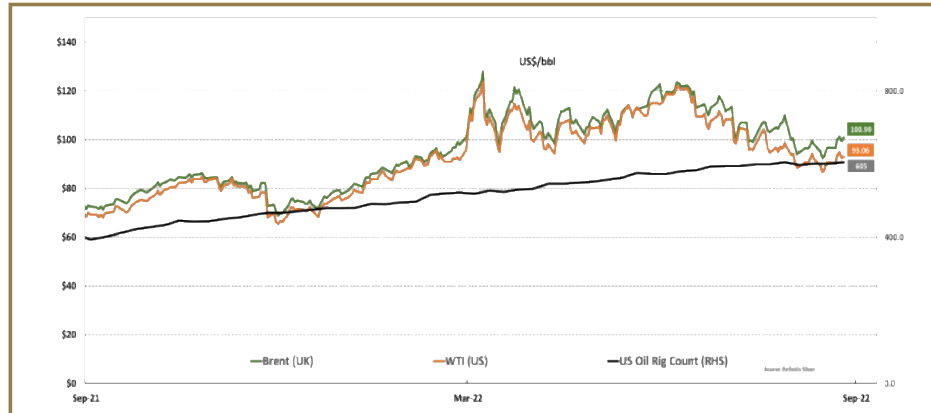
- Need for respect of basic international norms
 - Not entirely new: precedents were South Africa, Iran, Iraq, Libya, Venezuela...
 - Where the red lines are remains uncertain
- High level of dependence on non-complying actors is a limitation of freedom of foreign policy, even if in context of interdependence
- Due to large role played by oil and gas-related revenue, direct link between energy trade and war-making capability
- Hence: politicization of energy trade – depend mostly or exclusively on countries that share respect for basic international norms

Undoing interdependence

- The process of undoing the links of interdependence is not easy and very costly
- Oil and gas prices were increasing even before the invasion, and are now exploding
- Nevertheless there is no going back to the previously existing situation
- The new emphasis on collective security of supply resurrects the original mission of the International Energy Agency
- Substitution of fossil fuels will also be accelerated

Oil and gas prices are very high

The closing price (\$/Barrel) as of Friday 26 Aug 2022 – October Futures



Benchmark Oil Prices

Brent ICE

100.99

Weekly Change \uparrow 4.4%

YTD Change \uparrow 20.6%

WTI NYMEX

93.06

Weekly Change \uparrow 2.5%

YTD Change \uparrow 14.6%

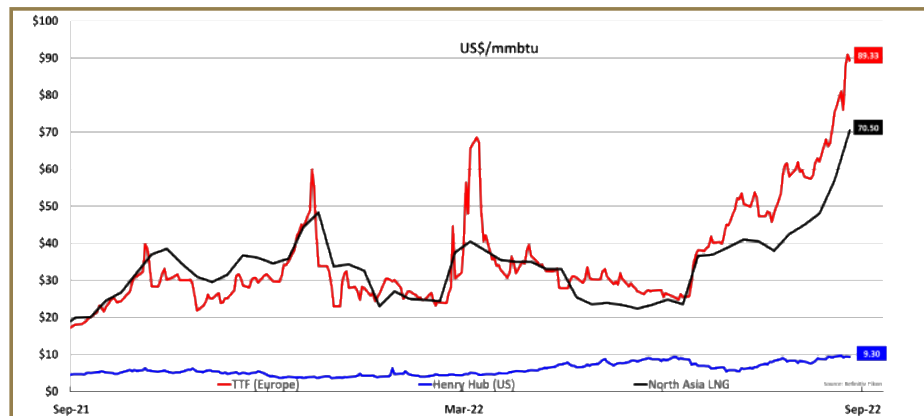
DME Oman

10149

Weekly Change \uparrow 5.6%

YTD Change \uparrow 24.1%

The closing price (\$/mmBtu) as of Friday 26 Aug 2022 – October Futures



Benchmark Gas Prices

NE Asia LNG

70.50

Weekly Change \uparrow 23.7%

YTD Change \uparrow 103.8%

Europe TTF

89.33

Weekly Change \uparrow 18.66%

YTD Change \uparrow 189.6%

US Henry Hub

9.30

Weekly Change \downarrow 0.4%

YTD Change \uparrow 66.9%

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The dilemma of Gulf producers

- The United States and other IEA countries have called on Gulf producers to increase production and bring down prices
- This call has been ignored: Saudi Arabia, the UAE and Kuwait want to stick to OPEC+ and defend high prices
- In the coming months/years upstream oil and gas investment will concentrate in IEA and non-OPEC countries, the international oil market will be segmented
- Notably, Qatar and Oman are not members of OPEC

Decarbonisation drives diversification

- Demand for oil and gas will not decline abruptly in IEA countries, but it will not be increasingly satisfied by the producers with cheapest oil, as had been expected
- Increasing emphasis will be put into decarbonising fossil fuels through greater use of clean energy and CCS, aiming at the reduction of scope 1, 2 and 3 emissions
- Diversification policies should focus on the decarbonisation of fossil fuels and their transformation into decarbonised fuels (hydrogen, ammonia) or non-fuel intermediate industrial products (petrochemicals, aluminium, steel...) while minimising emissions
- This requires very large investment and maximum financial discipline, even in a context of high hydrocarbon prices

Carbon pricing and the CBAM

- The EU will continue relying on carbon pricing as main decarbonisation tool
- It will also implement a Carbon Border Adjustment Mechanism to discourage imports from high-emitting countries
- Nevertheless, the migration of emission-intensive industrial processes to countries where emissions are more easily avoided or contained will continue. There will be opportunities for the Gulf countries.
- However, “decarbonised enclaves” in carbon-intensive economies will not be acceptable: the whole economy must be decarbonised

Decarbonisation and security of supply

- The concern for decarbonisation coupled with security of supply and affordable energy prices points to a world of closer ties with suppliers of hydrocarbons or other energy commodities that are both politically reliable and committed to mitigating climate change
- Countries that display little acceptance of international norms will be frowned upon and offered fewer opportunities
- Economic diversification in a context of international cooperation is only possible if basic international values and norms are respected