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HIGHLIGHTS

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I Political Developments

1. Syria: The month began with news that President Putin and the leaders of Iran and Turkey had on 4 May agreed on the setting up of four “safe zones” in Syria, later referred to as “de-escalation” zones; these are: the city of Idlib, held by militia led by the Al Qaeda-affiliated Jabhat Nusra since mid-2015; north of the city of Homs, where the Turkish-backed Free Syrian Army (FSA) is dominant; the eastern countryside of Damascus, Al Ghouta, controlled by the Saudi-backed Jaish al Islam since 2012, and the city of Daraa in the south shared by the FSA and Islamic groups. There are reports that hundreds of rebel fighters have started moving out of government-held areas to areas controlled by rebel forces.

Besides the ceasefire, the agreement also provides for supply of humanitarian aid and the return of refugees to the safe zones. An observer has noted that, with the safe zone plan in place, the partition of Syria between the US, Russia and Turkey seems aimed at dividing the population according to political allegiance, not according to religion or sect.

These safe zones are to be patrolled by forces from Russia, Iran and Turkey, though there are reports that peace-keeping forces could also come in from “non-controversial” countries, such as members of BRICS countries, Algeria, Egypt and the UAE. Neither government nor US-led coalition aircraft will be permitted to attack these safe zones. The Syrian government has rejected any role for the UN in monitoring the implementation of the safe zones. The Russian spokesman at its permanent mission in New York has said that Russia has tabled a draft resolution at the Security Council and expects it to be approved in a week’s time.

While the peace initiative has brought about an immediate lull in the fighting from 7 May, observers have noted some serious shortcomings in the plan. It does not say whether residents in these zones are free to move to other zones. It is also silent on the fate of the ISIS “capital” Raqqa, where US-led Syrian Democratic Forces (SDF) are making advances, as also with regard to the Kurdish-controlled territory east of the Euphrates or the Turkish-controlled border cities of Jarabulus, Al Bab and Azaz. Finally, it does not offer any clarity about government-formation and power-sharing in the major Syrian towns Damascus, Tartus, Latakia and Afrin, which are presently government-controlled.

In terms of next steps, it is understood that Putin will now push his draft constitution at Geneva-IV,

scheduled to be convened on 15 May, which provides for limiting presidential authority and autonomous provinces.

Separately, US-led SDF forces moving towards Raqqa, have captured most of the ISIS-held town of Tabqa, which is 55 km west of Raqqa, and has a population of about 85,000 people. However, the strategically important Tabqa dam is still under ISIS control.

US military backing for the Syrian Kurd forces, including enhanced weapons supplies, has led to strong criticisms from Turkish leaders. President Erdogan told a press conference: "We want to believe that our allies will prefer to side with us, not with a terrorist organisation." He hoped that recently taken decisions would be changed by the time he visits the United States later this month. Earlier, Prime Minister Binali Yildirim told reporters the U.S. failure to consider Turkey's sensitivities "will surely have consequences and will yield a negative result for the U.S. as well".

2. Yemen: There are reports that, following discussions in Moscow last month between Putin and Sheikh Mohammed bin Zayed, Crown Prince of Abu Dhabi, Russia is pursuing a political solution to the Yemen conflict, outside of UN channels, with former Yemeni president Ali Abdullah Saleh. It is seeking a future consensual Yemeni government, possibly by detaching Saleh from his Houthi allies. (Saleh's support for the Houthis is critical for the al Houthi-Saleh bloc to retain its influence across northern and central Yemen.) This effort seems to be working: news reports from the Saudi Press Agency on 10 May said that Saleh had asked media outlets close to him "to discredit Houthi leader Abdul Malik Al Houthi and expose him", particularly on how he had "sold the country's interests to Tehran cheaply" and expose the fact that the Houthis "are just a band of thieves seeking spoils of war, positions of ministers and funds".

While there is no independent confirmation of these comments, Saleh has been quoted as saying that he is ready for dialogue with Saudi Arabia. He has also rejected the Hadi government and insisted on the need for a new government. It seems that his emissaries have been meeting Saudi officials over the last few weeks in Berlin.

Much to Hadi's dismay, the UAE seems to be building ties to individuals identified with the Southern Movement that continues to press for greater autonomy, if not outright independence, from Yemen's central authority. On 27 April, Hadi had dismissed several senior officials in the south who were close to the UAE, which then led to strong anti-Hadi demonstrations in Aden.

In a new challenge to Hadi, the former governor of Aden, Major General Aidarous Al Zoubeydi, sacked by Hadi last month, has announced the setting up of a new "transitional political council of the south", that includes five provincial governors and former state minister Hani bin Braik, who had also been sacked by Hadi in April. However, members of the secessionist "Southern Movement" have not been included in the council.

A commentator, Stephen Seche, has noted the UAE's on-going strategic investments in southern Yemen. For instance, the UAE is reportedly building an airstrip on Perim Island, which lies in the middle of the strategic Bab el-Mandeb, through which about 4 million barrels of oil pass each day. Other observers have also noted that Abu Dhabi is building roads at all of Yemen's major ports, from Mukalla in the east to Mocha on the Red Sea coast. Seche concludes: "The Emiratis appear increasingly determined to shift their focus from short-term tactical advantage to long-term strategic stabilization ... by moving ahead with plans that appear to support a much longer-term investment in Yemen, one that may include redrawing the map of the country."

3. Saudi prince attacks Iran: Saudi deputy crown prince and defence minister, Prince Mohammed bin Salman, rejected any possibility of dialogue with Iran. He said that the aim of the Iranian regime "is to reach the focal point of Muslims (i.e., the holy city of Mecca) and we will not wait until the fight is inside Saudi Arabia ... we will work so that the battle is on their side, inside Iran, not in Saudi Arabia. He added that Saudi Arabia had the resources to "uproot Al Houthis and Saleh in a matter of days", but did not do so to avoid heavy Saudi casualties and large-scale Yemeni civilian casualties.

In the same hour-long interview, Prince Mohammed also claimed that his radical reforms were

succeeding in protecting the kingdom against low oil prices, and he promised massive investments in coming years to help diversify the economy beyond oil.

He said more than half of the tens of billions of dollars that Riyadh expects to raise by selling shares in national oil giant Saudi Aramco would be reinvested domestically by the kingdom's top sovereign wealth fund, the Public Investment Fund (PIF), to create jobs and earn revenue. In the three years after the share sale, the PIF will spend over 500 billion riyals (\$133 billion), with between 50 and 70 percent going to develop promising non-oil sectors such as mining and logistics within Saudi Arabia, the prince said.

Though the prince projected an optimistic outlook, observers believe that the country still faces major problems. For instance, serious uncertainties overshadow Saudi Arabia's efforts to restructure its economy, specifically the amount the government will raise through the sale of the Aramco shares. (It has predicted the sale will value the company at \$2 trillion, but some private analysts expect a significantly smaller figure.)

Iran responded to the prince's anti-Iran remarks by saying that it is ready for talks with Saudi Arabia to promote regional peace despite what Tehran called "unlawful and inflammatory" remarks made recently by the Saudi deputy crown prince. In a letter to the UN secretary general, Iran said that Tehran has "no desire, nor any interest, in an escalation of tension in our neighbourhood" and that Iran is "ready for dialogue and accommodation to promote regional stability, combat destabilizing extremist violence, and reject sectarian hatred." It concluded by saying: "We hope Saudi Arabia will be persuaded to heed the call of reason."

A day later, Iranian remarks had become more belligerent: Iran will hit back at most of Saudi Arabia, with the exception of Islam's holiest places, if the kingdom does anything "ignorant", Tehran's defence minister Hossein Dehghan was quoted as saying.

4. Trump's visit to West Asia: In a historic gesture, President Trump has announced that Saudi Arabia will be the first foreign country he visits as president, becoming the first US president to make his inaugural foreign tour to an Arab or Muslim country. Administration sources have said that they picked Saudi Arabia as a first stop on the tour in a bid to counter widespread claims that the president is Islamophobic. This impression is not surprising given that Trump had spent the campaign promising a ban on Muslims' entry into the US and then twice had tried to implement a version of the ban through administrative order, though he was thwarted by courts that blocked both efforts.

Trump is also underscoring both the success of Saudi outreach to the new administration, and the determination of the President to recommit to the Saudi-led strategic alliance providing stability in an unstable region. An Arab daily has said that the talks with GCC leaders will focus on "confronting the antagonistic behaviour of Iran in the region, looking at ways to deter Tehran and put an end to its blatant interference in the domestic affairs of other countries".

A pro-Saudi commentator, Ali Shihabi, sees this visit as a solid US commitment to defending the Gulf monarchies from Iran, ISIS and Al Qaeda that are making a determined effort to bring down the monarchies that "constitute the front line in the battle against terrorism". Shihabi goes on to say that Iran, ISIS, and al-Qaeda all want to replace the Gulf monarchies, with rulers under the sway of Iran's Shia theocracy or, in the case of ISIS and al-Qaeda, with a radical Sunni caliphate.

Trump's tour, starting from Riyadh on 21 May, will take him to Israel and the Vatican. A US writer, Kimberley Dozier, says the trip indicates that Trump is re-aligning the White House with Saudi Arabia's and Israel's anti-Iran position. It is also a signal that Trump is returning to the Bush-era reliance on Sunni Arab strongmen to control an unstable West Asia.

In Riyadh, besides the bilateral summit with King Salman bin Abdulaziz, Trump will be meeting with members of the Gulf Cooperation Council, as well as members of the Organization of the Islamic Cooperation, minus Iran and Syria. In a curtain-raiser to the visit, Saudi foreign minister Adel al-Jubeir said that the visit would enhance cooperation between the US and Muslim countries in the fight against terrorism.

In the run-up to the Trump visit, Washington is trying to push through contracts worth tens of billions of dollars in arms sales to Saudi Arabia, some new, others already in the pipeline. Items under discussion include: the Terminal High Altitude Area Defence (THAAD) missile defence system with several batteries, valued at about \$1 billion, and a C2BMC software system for battle command and control and communications, as well as a package of satellite capabilities.

Combat vehicles made by BAE Systems, including the Bradley Fighting Vehicle and M109 artillery vehicle, are also under consideration as part of the Saudi package. The discussions also include previously reported contracts or items under negotiation for years. One such deal, an \$11.5 billion package of four multi-mission surface combatant ships and accompanying services and spares, was approved by the State Department in 2015 but not finalised.

Also under discussion are more than \$1 billion worth of munitions including armour-piercing Penetrator Warheads and Paveway laser-guided bombs. The Obama administration had suspended the planned sale because of concerns over the Saudi-led military campaign in Yemen and civilian casualties.

Saudi Arabia has also announced that its sovereign fund will invest about \$ 40 billion in infrastructure development in the US, with formal announcements being made just before the Trump visit.

II Oil-Related Developments

The oil price scenario remained volatile largely because the OPEC and non-OPEC cuts in production, announced in November last year, have failed to make a major dent in oil inventories, even as US rig counts have continued to increase steadily. Oil prices fell to their lowest in six months on 5 May, when Brent went to \$ 45. Both Brent and WTI rose sharply to over \$ 48 (Brent) and over \$ 45 (WTI), following Saudi Arabia's OPEC governor's statement that: "There's an emerging consensus among participating countries on the need to extend the production agreement reached last year." Oil analyst Fereidun Fesharaki has said that OPEC was certain to extend the cuts when its ministers met on 25 May. He added that OPEC would need to keep limiting production until as late as the end of 2018.

At an oil conference in Kuala Lumpur, Saudi energy minister Khalid al Falih said on 8 May that the oil market is improving from early last year when markets were at a low. Stockpiles at sea have declined and U.S. inventories will continue their downward trend, he added. Global demand, meanwhile, will probably be stable from the "healthy rate" seen last year, driven by China and India, the Saudi minister said, adding that Asia was the most important market. There's about 20 million barrels a day of combined demand growth and natural oil-field output declines that need to be offset, Al-Falih said. "No matter how fast U.S. shale grows, it won't make a dent in that number," he said.

OPEC, in its monthly report released on 11 May, has forecast that non-OPEC oil production in 2017 will be 950,000 b/d instead of the 580,000 b/d it had projected earlier. Most of this production will be US shale oil, estimated to rise by about 600,000 b/d this year. However, contrary to present trends, Goldman Sachs have noted that the oil market is rapidly re-balancing, while IEA has predicted that, with OPEC and non-OPEC cuts in production which will go into the second half of this year, demand could exceed production. Goldman Sachs has projected prices in the fourth quarter at \$ 57 for Brent and \$ 55 for WTI.

III Economic Developments

Saudi economic scenario: In an interview with Bloomberg, Saudi Arabia's vice minister of economy and planning, Mohammed Al Tuwaijri made the following main points:

(I) Sale of international bonds: Al Tuwaijri said that the finance ministry's debt management office may decide to tap the market in the fourth quarter this year. The size of the issuance will depend on market conditions and investor appetite but could potentially be as much as

\$10 billion. Saudi Arabia's first dollar-denominated sukuk in April was expected to raise only \$5 billion; in fact, the sale raised \$9 billion because it had an "oversubscribed book with a lot of strategic investors who wanted more."

Domestically, the government still plans to raise about 70 billion riyals (\$ 18.6 billion) this year.

(ii) Balancing the Budget: He expressed confidence that the budget would be balanced by 2020.

(iii) Four Privatizations to Start With: The government had surveyed the market to identify suitable targets and made a list of 16 entities that are prime for privatization, along with more than 100 public-private partnership opportunities. Four "low hanging fruits" will start the privatization process potentially this year: the Saline Water Conversion Corporation, a power generation company under Saudi Electricity Co., grain silos and sports clubs.

(iv) Spending on Infrastructure: He affirmed that the government was "very committed" to mega projects that would help achieve the objectives of Vision 2030, its blueprint for life after oil, particularly infrastructure projects. He cited Jeddah's new airport and Riyadh's metro system, under construction, as examples.

(The views expressed are personal)
