ananta centre

West Asia Digest

MONTHLY .... FEBRUARY 2016 | VOL 01 ISSUE 01

Ananta Centre is pleased to launch a new initiative — a monthly newsletter focusing on major political and economic developments in West Asia that are of crucial importance for India's long term interests.

Our effort will be to keep you informed and updated on the developments in the region and their implications for India. We hope you will find this initiative informative and useful. We shall be grateful for your comments.

Highlights

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Overview

THE PRINCIPAL DEVELOPMENT of interest to India has been the **three-day visit to Delhi and Mumbai of the Crown Prince of Abu Dhabi, Sheikh Mohammed bin Zayed**, who, during the illness of the ruler of Abu Dhabi and the president of the UAE, is the de facto political head of the country. Commencing from 10 February, the visit took place just six months after the path-breaking visit of Prime Minister Narendra Modi to the UAE in August last year, the first visit of an Indian prime minister since that of Mrs Indira Gandhi in 1981.

This visit signals the interest of the UAE leadership to establish a "comprehensive strategic partnership" with India that would be anchored in expanded energy and economic relations and would encompass enhanced political, security and defence ties as well. The UAE has announced a $75 billion fund dedicated to the development of India's infrastructure, including: railways, ports, roads and highways, and airports. The two countries have also pledged to expand ties in the areas of hydrocarbon and renewable energy, and frontier areas such as IT, cyber security, space and nuclear power.

Clearly, the UAE is concerned about the deteriorating regional security situation, with Iran and Saudi Arabia embroiled in strategic competition across the region, two wars raging in Syria and Yemen, Iraq deeply polarized, and the forces of sectarianism and jihad shaping the ongoing conflicts. While the UAE is allied with Saudi Arabia, as a major energy, trade, financial and logistical centre in the region it cannot but be concerned about the adverse implications of these contentions. As the crown prince said on arrival, the UAE would like to see India, with its "poise, balance and wisdom", pursue a "just solution" to the region's problems, a clear invitation to India to engage itself in promoting security in West Asia.

The other interesting development is the unique initiative in modern-day governance launched in the UAE. First, on 8-10 February, it hosted the **World Government Summit**, which was addressed by world political and business leaders, including: President Barack Obama, President Paul Kagame of Rwanda, the World Bank President, and Mrs Mary Robinson, former President of Ireland. The participants discussed three documents pertaining to shape and role of governments in future: Work Technology in Employment, Smart Cities for Public Value and Advanced Science for the Future of Government, the focus being on the global enhancement of public services through technological innovations.

The UAE then went further: it announced a **new council of ministers** with a number of young ministers, including several women ministers. Portfolios distributed among these ministers included: tolerance; happiness; youth affairs; community development and climate change and environment.

Oil Prices

THE COLLAPSE OF OIL PRICES has of course complicated the economic and political scenario in the region which has the world's principal hydrocarbon producers. Prices plunged from over $100/barrel in June 2014 to a low of $ 27/b towards the end of January, before stabilising at around $ 32-35/b this month. However, v**olatility remains the watchword:** prices swing yo-yo-like in response to various news reports. Last month, prices went up by a few dollars on reports that Russia and OPEC might do a deal on production cuts, or that Venezuela might persuade its OPEC partners to agree to an emergency meeting where production cuts would be on the agenda; they came down once again on reports of sluggish growth in China and high oil inventories in the US.

But, **cuts in production are not on the horizon:** any cut by OPEC would be quickly matched by higher production by non-OPEC producers; it would also encourage US shale oil producers, struggling with the low prices and often producing at heavy losses, to bounce back into the market. In fact, oil consultants Wood MacKenzie have reported that oil producers remain resilient in that the low oil prices have reduced oil production only by 100,000 barrels per day since the beginning of 2015. It has noted that 3.4 million barrel per day of oil is being produced at a loss at current prices of about $ 35/barrel, with some producers happy to take a short term loss in anticipation of future increases rather than shut down operations altogether. Still, US producers are operating just a third of the rigs as compared to a year and a half ago and US production is expected to lower by about one million b/d in 2016 as against the peak of last year.

It is true that several producers sense a **"super contango"** in terms of which prices in the near future will be much higher than at present so that it makes sense to store low cost oil rather than shut production. With most storage already in use, they are today opting for "floating storage", ie, keeping oil in crude carriers in anticipation of oil price premiums of $ 10 or more per barrel in a year's time. The problem is that global storage capacity is also being stretched to its limits: Cushing, Oklahoma, the "pipeline crossroads of the world", has stored a record 64.7 million barrels, about 88% of its total capacity, with little sign of an upward movement in prices.

The numbers game continues: producers are encouraged by reports that prices will go up by about $ 15/b to $ 46-48/b by the end of 2016, largely due to a fall in non-OPEC production of about 600,000 barrels per day. OPEC and the International Energy Agency [IEA] however are offering different forecasts: IEA believes that global oil glut will worsen in 2016 since global demand and global stockpiles would have peaked: thus, prices would not go up significantly. OPEC sees non-OPEC production declining more steeply, by 700,000 b/d. However, Morgan Stanley have revised their price forecasts for 2016 from $ 59/b, announced in January, to just $29/b in the last quarter of this year.

Amidst all these uncertainties, **Saudi Arabia** is rejoicing in the fact that it has managed to **maintain its market share of 1.2 million b/d in the US market** when sea-borne supplies from most sources have been drastically reduced. First, its heavier oil is not in direct competition with the lighter US shale oil. More importantly, it has built firm "strategic partnerships" with the major US refiners over several decades, including with stakes in their operating entities, a downstream integration that kept its supplies intact. It hopes to repeat this strategy with China as well: after all, protecting market share in this period of over-supply is at the heart of GCC strategy; as more expensive oil is driven out of the market, stability will return. But, no-one seems to know when and at what price level.

The GCC Economic Scenario

ALL THE ECONOMIES in the GCC countries have been hit by the low oil prices. **Saudi Arabia's fiscal reserves** in 2015, at $ 612 billion, were at a four-year low, and poorly placed as compared to reserves of $ 732 billion in 2014. The reserves are expected to experience a further fall of $ 50 billion in 2016. Again, with a 60% fall in its oil income in

2015, its budget deficit was $ 98 billion, and likely to be about $ 107 billion this year. The Kingdom has raised bonds of $ 30 billion domestically and has also announced increases in prices of fuel, electricity, water and gas.

This year, we will continue to see GCC economies adversely impacted by low oil prices, with a fall in expenditure of 6%, leading to a non-oil growth rate of just 2%. Business outlook is mixed: government spending is expected to boost project activity but introduction of taxes such as VAT would increase the cost of doing business and discourage foreign investment.

The UAE continues to look relatively good: Dubai airport handled 78 million passengers in 2015, making it the busiest airport in the world; expansion plans envisage that its capacity will reach 118 million passengers in 2023. Dubai's core strengths with regard to logistics, trade, manufacture, construction, tourism and financial services ensure that in 2016 it will record a 4% GDP growth rate inspite of the low oil prices. Dubai will continue its focus on developing its knowledge economy, with the **Dubai Smart City** at the centre of this enterprise, supported by large-scale legal reforms such as: the Public-Private Partnership Law and a new UAE Commercial Companies Law, which will facilitate project execution and encourage foreign enterprises to work in the country.

Another important barometer for the economic health of the GCC countries is spending on **information and communications technology** [ICT]. Here again, given the regional political and economic scenario, the outlook is modest: GCC's ICT spending in 2016 is estimated at $ 66 billion, reflecting growth of just 3% over last year, while IT spending is likely to be $ 29 billion, a growth of 4% over 2015. UAE will lead ICT spending in the region with $16.7 billion, with half going to the telecom sector.

Project investment in the GCC over the next four years is estimated at $ 480 billion, including $ 330 billion for infrastructure development. UAE is expected to pursue some of the most expensive projects, such as the expansion of the Al Maktoum Airport at $ 32 billion and the Al Gharbia Chemical Industries City at $ 20 billion.

Iran

SATURDAY, 16 JANUARY, 2016, was celebrated as **"Implementation Day"** by Iran and large sections of the international community, the day on which the International Atomic Energy Agency [IAEA] declared that Iran had fulfilled its key commitments as required by the Joint Comprehensive Plan of Action [JCPOA] it had negotiated with the P5+1 countries a few months earlier. Thus, the US, EU and the UN have terminated or suspended all nuclear-related sanctions that have hurt the economy so harshly. Observers noted that Iran had speeded up the implementation process and completed it a few months earlier than anticipated, possibly so that the government would benefit from a positive outcome in the Majlis (parliamentary) elections slated for 26 February.

It has immediately benefited from the **release of $100 billion in frozen funds**, but these have already been earmarked for domestic projects, boosting the capital of its banks and to meet outstanding foreign bills. It is also reluctant to bring huge funds into the domestic economy all at once for fear of inflation.

Iran is now open for global business to boost its economy and improve the lives of its 77 million-strong population. Its $ 400 billion GDP makes it the second largest economy in the region, after Saudi Arabia. It is presently looking at a modest growth of 3% this year, but its leaders are looking at 8% growth annually up to 2020. Realising this will be a difficult proposition given the low oil prices and poor state of its **hydrocarbon infrastructure**. The latter is expected to attract considerable foreign investment: the Russian company, Tube Metal Company (TMC), a world leader in pipes for the oil and gas sector, is looking at the prospect of Iran needing pipes valued at $ 100 billion for its energy sector. Half-finished projects at Iran's petrochemical complex at Assaluyeh, in the Gulf, will also need foreign partnerships to be completed.

Agriculture is another sector that is receiving priority attention. Already a major agricultural producer of wheat, sugarcane and fruits, Iran hopes to use foreign investment and technology to boost domestic production of produce and processed items so that it becomes self-sufficient and possibly even an exporter.

Iran is being viewed as an **attractive market for ICT investment:** this segment is expected to grow by 30-40% in the next three years so that it would emerge as the second largest regional market after Saudi Arabia. Areas receiving priority attention are: system infrastructure, software storage, cloud-based solutions, IT services and cyber security.

With the easing of sanctions, Iran also plans to become an attractive **tourism destination**, getting about 25 million tourists by 2025, who would generate about $ 30 billion in revenues.

Iraq

THE SCENARIO RELATING to Iraq is much less positive. The collapse of oil prices has aggravated the woes of the country already suffering from an ongoing conflict against the "Islamic State" and the presence of millions of displaced persons and Syrian refugees. Iraq obtains 90% of its federal revenues from oil sales, which also constitutes 99% of its exports: the fall in prices has meant that monthly revenues, which were over $ 7 billion two years ago, are now about $ 2 billion, though it is selling the maximum oil possible, about 3.6 million b/d. This has affected the Kurdish region as well, where the regional government has failed to pay its soldiers fighting the ISIS for several months.

Iraq's budget for 2016 had been based on an oil price of $ 45/b; it is looking at a deficit of $11billion this year. Overall, the country is in the grip of a severe financial crisis. Panacea offered by well-intentioned commentators include doing away with subsidies and reducing employment in government, both daunting challenges in that beleaguered country.

Prime Minister Haidar Al Abadi has just announced that he will replace his council of ministers, drawn from different political blocs, with a team consisting of technocrats. However, given that Iraq's political order has been structured on the basis of accommodation of various communal parties that reflect the fault-lines of that divided polity, there are doubts about his ability to implement this plan.

Outlook for Indian Business

THE REGIONAL SCENARIO consists of two contradictory elements: extraordinary enthusiasm generated by the visit to Delhi and Mumbai of the Crown Prince of Abu Dhabi, Sheikh Mohammed bin Zayed, with the attendant promise of a significant upsurge in political and economic ties, and gloomy prospects due to the low oil prices, sluggish global and regional outlook, and the bitter contentions and conflicts across West Asia, centred at the Saudi-Iran strategic competition. Over the last ten days, local media have projected the extremely optimistic outlook of Indian entrepreneurs in the UAE with regard to energy, trade, IT cooperation and the congenial environment for Indian start-ups, as also the prospects for UAE investment in Indian infrastructure, industry and energy projects.

Of course, there are reasons for concern as well. The economic scenario has been turbulent and oil prices remain volatile, which has posed the following challenges: cuts in government outflows; reduced consumer spending; increased competition; flight of talent, and need for greater productivity to maintain margins.

But, the bases for optimism are substantial: continued government spending on infrastructure, mainly in the UAE in connection with EXPO-2020; reasonable growth prospects given the global scenario, and confidence in the political leadership. The positive outlook projected by Indians in the UAE is therefore well-placed.

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(The views expressed are personal)