

HIGHLIGHTS

- Political Developments
- Oil-Related Developments
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Political Developments

1) Syria

THROUGHOUT THE LAST FORTNIGHT, Syria witnessed battles at various fronts, as rival forces and militia sought to consolidate their territorial gains. First, fighting continued in Aleppo between government forces in the southwest of the city and rebel militia in the east. The latter included elements of the Jabhat Fatah Al Sham [Syrian Victory Front], the new name of the former Al Qaeda-affiliated Jabhat Nusra, which last month, formally de-linked itself from its parent body, mainly to avoid being targeted by US-led coalition forces as a terrorist organization.

Government forces were supported by air strikes which blunted rebel attempts to take the town. The fighting in Aleppo yielded the horrific photograph of the blood-soaked boy, Omran Daqneesh, in an ambulance, and led to renewed calls to end the fighting, calls that have largely gone unheeded.

The other front was the strafing of ISIS and Jabhat Fatah positions by Russian aircrafts. The significant development here was that Russia carried out bombing raids on 16th August from an Iranian airbase, the Hamadan base, 50 km north of Hamadan city, the first occasion that Russia has used an Iranian base to launch military assaults in Syria. This led a US spokesman to suggest that Russia may have violated UN sanctions relating to prohibitions on supply, sale and transfer of combat aircrafts to Iran; this was firmly denied by Russia, which said that the use of Iranian facilities was only temporary. The Iranian Defence Minister criticized Russia for publicizing the use of the Iranian base as a “kind of show-off” and “ungentlemanly” and said the Russians wanted to show “they are a superpower to guarantee their share in the political future of Syria”. On 22nd August, Iran announced that Russia had stopped using the base.

Observers believe that by publicizing the use of the Hamadan base, Russia was conveying to the Americans its frustration at the US’s hesitation to coordinate more deeply with Russia on military and diplomatic actions in Syria- in short, to treat it like an equal power. The event also reaffirms the close military and political ties that have been forged in the Syrian cauldron between Russia and Iran.

The third front in the fighting was the town of Hasaka in northeast Syria. This town became a “flashpoint” over the last fortnight as the province of the same name (of which it is the capital) is strategically located at the point where the Iraqi, Syrian and Turkish borders meet. Hence, its capture is a priority for the Syrian Kurdish force, the

People's Protection Units [PYD], which already controls 90% of the town and has been fighting the pro-government militia, the National Defence Forces [NDF], and the national army, for the remaining portion. Though the town has an Arab majority, its control would provide the region's Kurds with contiguous territory over the three countries and, in the words of a Kurdish analyst, serve as "the hub to secure a broader Kurdish region". The province itself has very fertile soil and has oilfields. At month-end, a cease fire was arranged under US-Russian auspices. Kurdish parties are suggesting that the political arrangements put in place at Hasaka could constitute a model of power-sharing arrangements for a federal Syria when peace is finally restored in that country.

However, at month-end, peace seemed quite remote as Turkish forces, made up of aircrafts, tanks and armoured personnel carriers entered northern Syria on 24th August, opening a fourth front in the Syrian conflict. It took place just four days after an ISIS suicide bomber killed 54 people in the south-eastern Turkish city of Gaziantep. Named "Operation Euphrates Shield", the Turkish force consisted of 30 tanks and about 450 soldiers in the first instance, and was directed at both the ISIS and the PYD, that had taken Manjib last month and was now seeking to take full control of territory all across the border with Turkey. Turkey later said that it might expand its military presence to as many as 15,000 soldiers in coming days.

The Turkish incursion into Syria, which is accompanied by pro-Turkish rebel Turcoman and Arab elements (some of whom have been accused of atrocities earlier), suggests that Turkey might now put in place the "buffer zone" at the Syrian border that it has been agitating for, for over a year. The intervention has been condemned both by the Assad government and an alliance of 23 Kurdish parties, while western media have reported that the Turkish forces have focused more on Kurdish militia than on the ISIS. The Turkey-based Kurdish movement, PKK, has claimed responsibility for a suicide bombing at Cirze, at the Syrian border, in which 11 police men were killed.

On the political front, Turkey announced an easing of ties with the Assad regime. Prime Minister Binali Yildirim affirmed that Ankara would accept Bashar Assad "for now" and that the latter had now recognized the danger posed to Syria and the region by the expansion of Kurdish forces all across the border. Yildirim added that his country would work with Assad in coming months to ensure that Syria was not divided on ethnic lines.

Separate from this frenetic military activity, there have been some more low-key but important Syria-related diplomatic initiatives from China and India. First, a senior Chinese military officer, Rear Admiral Guan Youfei, was in Damascus mid-August and had meetings with the Syrian Defence Minister and senior Russian military officers in Syria. Before his departure, the Admiral, who is the head of the Office of International Military Cooperation of the Central Military Commission, indicated China's interest in expanding military cooperation with the Syrian government, including personnel training and humanitarian assistance. According to Chinese news reports, China has already positioned military advisors in Syria and has provided the country's army with sniper rifles and rocket launchers.

Within a week of the Chinese visit, the Indian Minister of State for External Affairs, Mr. MJ Akbar was in Damascus, where he met President Bashar al Assad. According to news reports, the minister sought Syria's help to locate Indians involved with the ISIS, some of whom were suspected of recruiting Indians and also planning attacks in India on the lines of the carnage carried out by the ISIS in Dhaka recently. During the visit, the two sides agreed to revive the development projects signed with Indian companies before the conflict, including a power plant and a steel plant.

2) Yemen

WITH THE BREAKDOWN IN PEACE TALKS IN KUWAIT in early August, the US and UK have initiated a new peace process, possibly in association with Russia. There was a flurry of diplomatic activity in the Saudi sea-port of Jeddah, where Russian Deputy Foreign Minister Mikhail Bogdanov had talks with the Saudi Foreign Minister, suggesting a Russian mediation effort at Iran's behest. Within a few days, this was followed by the visit to Jeddah of US Secretary of State John Kerry, who participated in a "quartet" meeting in Jeddah that included the GCC foreign ministers, the UN special envoy for Yemen and a senior UK diplomat. In public remarks, Kerry said that

there was need for a comprehensive settlement in Yemen, which would include “in the first phase, a swift formation of a new national unity government, the withdrawal of forces from Sanaa” and the transfer of heavy weapons by the Houthis and those allied to them to “a third party”.

Separately, it was reported at month-end that the Yemeni army, backed by Saudi aircrafts, had “liberated” the southern Abyan province from Al Qaeda and ISIS militants. The Al Qaeda fighters are said to have taken refuge in the surrounding mountains, while the others fled to the Houthi-controlled Baydha province.

Oil-Related Developments

THROUGH THE LAST FORTNIGHT, oil markets reacted positively to indications of a possible production “freeze” being agreed to at the informal meeting of OPEC and some non-OPEC members in Algiers, from 26th-28th September, on the sidelines of the International Energy Forum (IEF) meeting. Markets were specifically buoyed by two statements: one, by the Saudi Energy Minister, Khalid al Falih, saying that, “if there is a need to take any action to help the market to re-balance, they [the Saudis] would do [so] in cooperation with OPEC and major non-OPEC members”. The other was from the Russian Oil Minister, Alexander Novak, following his visit to Riyadh, when he said: “We are ready to achieve the widest possible level of coordination [with OPEC] ... and put in place joint measures to achieve oil market stability, with the condition that these measures will not be for a limited period of time.”

Enthused by what observers have called “investor enthusiasm”, oil prices climbed upwards to \$48.91/barrel [Brent] on 16th August and to \$51.17/barrel on 19th August. WTI prices also rose to \$46.21 and then to \$47.44 during the same period. On 24th August, Iranian Oil Minister Bijan Zanganeh announced that he would be attending the Algiers meeting. On 26th August, the Saudi Energy Minister said he thought an output freeze would be “positive”, though he firmly ruled out a cut in production.

Analysts have noted that, unlike in April this year, when the earlier attempt at freezing output had ended in failure in Doha, this time round there is less tension among leaders and, in the words of a commentator, “the market is beginning to believe change is in the air”. The principal reason for this is that the major producers, Russia, Iraq, Iran and Saudi Arabia, are already producing at or near their maximum levels. Saudi Arabia produced an additional 440,000 b/d between January and July this year, to take its total output to the record level of 10.67 mbd; Iran produced an additional 600,000 b/d, to reach total output of 3.85 mbd, slightly less than the 4 mbd it produced before sanctions.

Against this background, most observers believe that, even if an output freeze is agreed to at Algiers, it will hardly have much impact on prices, given that OPEC producers are producing a record 33.1 mbd, one million b/d more than the average of 2015, and two million more than in 2014. This has, of course, helped to increase OPEC's global market share from 32.6% in 2014 to 35% at present.

However, given that global demand is not increasing, analysts suggest that prices could again slide downwards to around \$40/barrel. This would be encouraged by an increase in shale oil production due to more rigs being deployed in the US; with prices around \$50, in the last eight weeks, an additional 76 rigs have been put into operation, in anticipation of the output freeze agreement in Algiers. This is the largest increase in rig deployment since 101 rigs were added two months before the mid-June 2014 price fall.

Non-Oil Economic Developments

1. AFTER VISITS TO THE US AND FRANCE, to bolster support for Saudi Arabia's Vision-2030 economic transformation plans, the Deputy Crown Prince, Prince Mohammed bin Salman, has from 29th August

embarked on a **tour of his country's two major Asian oil importers, China and Japan**, after which he will attend the G-20 meeting at Hangzhou, China, from 3rd-4th September. Observers have noted that the Kingdom's ties with Asian countries will be crucial since they are the principal buyers of its oil and major participants in its infrastructure projects; they could thus be important investors in Saudi plans to float an IPO of a percentage of its oil flagship, ARAMCO.

2. TO HANDLE THE BUDGETARY DEFICITS CAUSED by low oil prices, GCC sovereign funds and government-related entities **issued bonds** valued at \$45 billion in the first six months of this year, followed by banks whose bonds were worth \$30 billion. Other entities that issued bonds were entities in the power, renewable energy, telecom, and utilities sectors. Saudi Arabia is expected to go in for its first international bond issue in October, hoping to sell at least \$10 billion of bonds in that month. Proceeds are expected to be used to fund the Vision 2030, the country's ambitious economic transformation plan, as also the budgetary deficit which is estimated at \$80 billion this year.

3. RUSSIA HAS SHOWN INTEREST IN DEVELOPING Saudi Arabia's nuclear power sector. This was announced by the visiting Russian Energy Minister, Alexander Novak, who was responding to Saudi plans to set up 16 nuclear power plants in the next 20 years, at a cost of \$80 billion; when completed, they will meet 20% of the country's power needs.

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(The views expressed are personal)