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Qatar ‘rises above’ its region: Geopolitics and the rejection of the GCC gas market

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**Qatar ‘Rises Above’ Its Region: Geopolitics and the Rejection of the GCC
Gas Market**

**Research Paper, Kuwait Programme on Development, Governance and
Globalisation in the Gulf States**

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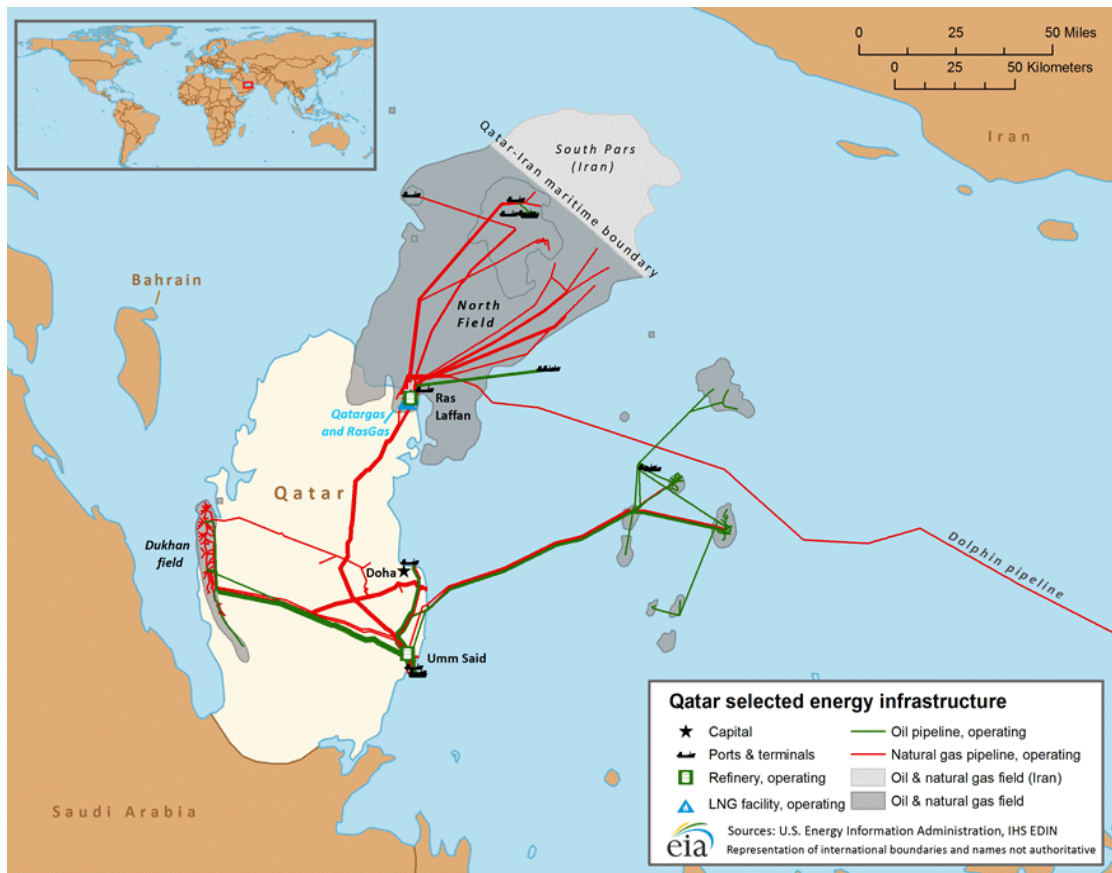
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Qatar's energy infrastructure

Qatar ‘Rises Above’ its Region: Geopolitics and the Rejection of the GCC Gas Market

JIM KRANE AND STEVEN WRIGHT

Abstract

Five member-states within the Gulf Cooperation Council (GCC) have developed shortages of natural gas, while the sixth, Qatar, controls an ideal source of supply. But proximity and friendly relations within the Arabian Peninsula bloc have failed to provide the basis for sufficient cross-border trade. Several factors continue to thwart regional gas distribution, starting with the GCC’s institutionalized undervaluation of natural gas. During the 1990s, amid faltering negotiations for a GCC-wide gas network, Qatar succeeded against the odds in attracting investment partners and building an export sector in liquefied natural gas (LNG). The unprecedented size and low cost base of Qatar’s LNG industry allowed Qatar to reap political and economic gains far beyond those regionally available. The diminutive peninsular monarchy has since used a network of long-term export contracts and protective security alliances to emerge from Saudi domination, while parlaying its comparative advantage in natural resources into a role of outsized global influence. Meanwhile, as the undersupply crisis has deepened within neighbouring monarchies, Qatar’s 2005 moratorium has closed off the possibility for increases in gas production. Forthcoming prospects for regional distribution of Qatari gas only appear plausible under future conditions of spare capacity, and when combined with a regional willingness to pay prices competitive with those in external markets.

Keywords

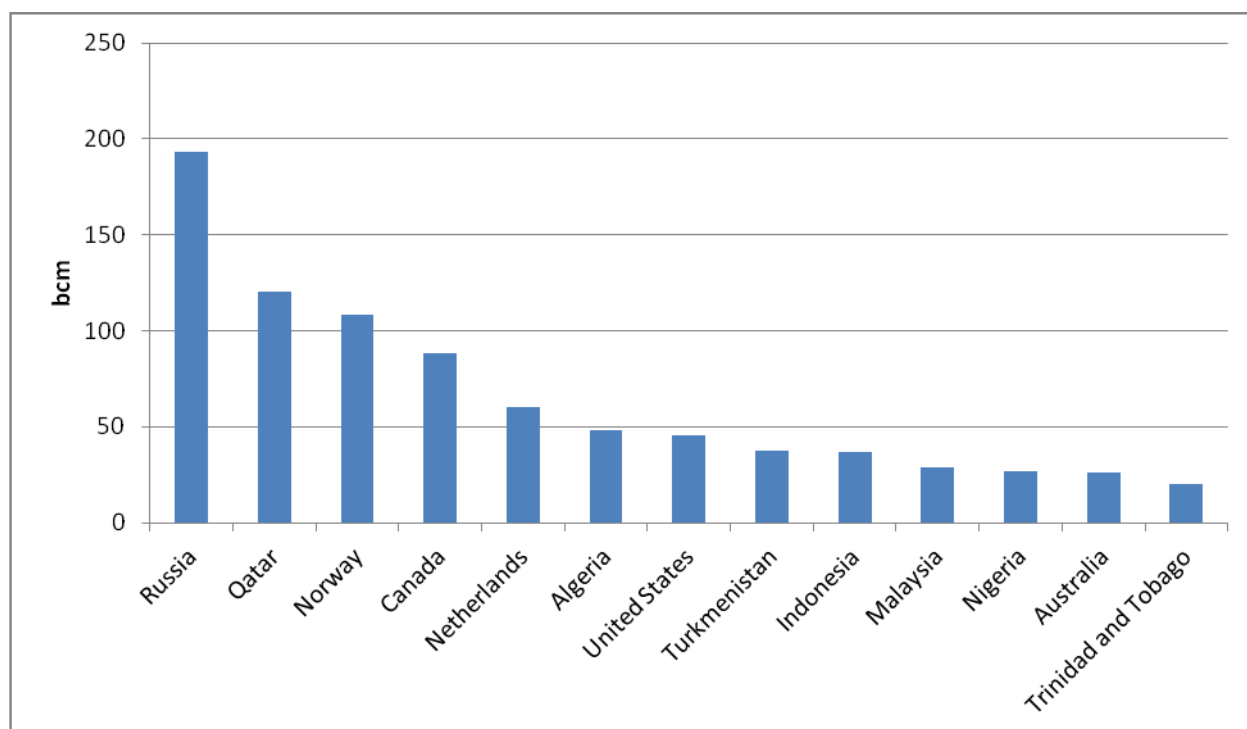
energy geopolitics; GCC; Gulf politics; international relations; LNG; natural gas; Qatar

1. INTRODUCTION

A curious imbalance afflicts energy markets in the Persian Gulf region. Five of the six Gulf monarchies exhibit shortages in domestic supply of natural gas. Two of them – Kuwait and the United Arab Emirates (UAE) – have turned to market-priced imports of liquefied natural gas (LNG), mostly from outside the region. Meanwhile, the sixth Gulf monarchy, Qatar, holds the world’s third-largest conventional reserves and is the second-largest natural gas exporter globally (Figure 1).

Why has Qatar, given its enormous resources and relatively small domestic needs, sought supply relationships on an international level while leaving regional demand unmet? Conversely, why have Qatar’s neighbours spurned past opportunities to import gas from Qatar, while those opportunities were on the table? After all, Qatar, like its neighbours on the

Figure 1. *Rankings of natural gas exporters, 2012*



Source: IEA (2013a).

Arabian Peninsula, is a member of the Gulf Cooperation Council (GCC), a monarchical bloc that links these six Sunni Muslim-led regimes through trade, customs and immigration treaties, even marriage ties.¹ A currency union among them is planned. If the five gas-short monarchies are unable to produce sufficient gas from their own reserves, surely it makes more economic sense for them to import via pipeline from a well-endowed regional ally, rather than enter the competitive global LNG market with prices that include mark-ups for liquefaction and transport?

The answers to these questions flow from two broad categories: pricing and politics. Briefly, gas-short GCC states have historically been unwilling to pay what Qatar considered a reasonable price for its gas. In part because of this recalcitrance, Qatar has 'risen above' the GCC market. It sought instead to export its gas as LNG to far-flung customers where it secured much higher prices on long-term bilateral contracts, and later, by selling surplus cargoes on the spot market. The success Qatar has enjoyed on its way to becoming the world's largest LNG exporter has allowed it to build an extraordinary level of global influence and improve its national security. It has done this by compiling links to powerful importing states

¹ Marriage ties between the ruling family of Qatar, the al-Thani, and that of Dubai, the al-Maktoum, include the marriage of Sheikha Mariam, the elder sister of Dubai's current ruler, who was married to the former Qatari Emir Sheikh Ahmad bin Ali al-Thani, who died in 1977. See Peterson (2007: 24).

that have become stakeholders in the security of continued Qatari supply (Wright 2011). Qatar's gains in revenue, political influence and stability have reduced its inclination to pursue regional sales. In the medium term, at least, Qatari supply appears unlikely to assuage unmet demand in neighbouring monarchies.

We address these points, first, by focusing on the current state of gas trading in the Gulf and the shortage of supply in the region (section 2). In section 3 we discuss the development of Qatar's foreign and security policy within the context of its strategic and geopolitical objectives. This section provides the foreign policy background for Qatar's energy calculations. In the final substantive section (section 4) we tie together our analysis and assumptions by presenting the implications for regional gas markets, within the context of increasing diversity in global gas supply.

2. THE PERSIAN GULF GAS TRADE AND BALANCE

Behind questions of regional gas trading is a shift in perceptions of natural gas in the oil-exporting countries of the Gulf. In the early decades of oil production, gas was considered a near-worthless by-product and provided to domestic markets at low prices that reflected the cost of production. More recently, gas has come to be valued as a key domestic resource that can be deployed to substitute for more valuable oil in the domestic economy, assisting states in maintaining oil exports in the medium and longer term. Gas demand has risen within the power generation and industrial sectors, as well as in enhanced oil recovery applications, where it is reinjected into depleting oil reservoirs. Gulf states have recently exhibited a new willingness to invest in gas-specific exploration and production and to pay much higher prices for gas imports. These states have also begun to invest in expensive marginal increases in domestic gas production.²

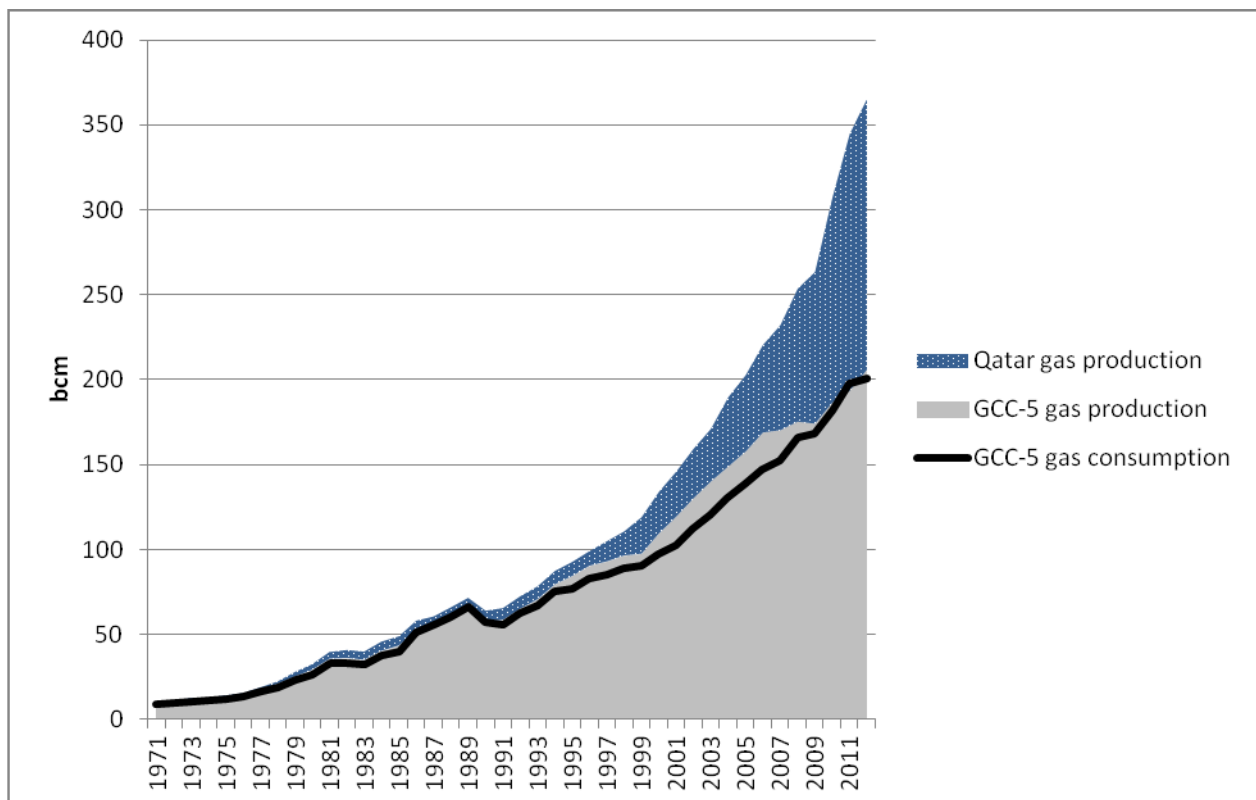
However, it may be premature to describe the embryonic state of cross-border gas trading in the Gulf as a 'gas market'. Inside each country, prices of domestic resources are set by the state at some of the lowest levels in the world. Most bulk natural gas in the Gulf monarchies is sold at fixed prices of (more or less) US\$1 per million British thermal units (MMBtu). Such underpricing drives many of the market distortions covered in this paper. On the one hand, low prices relative to those available in unsubsidized markets contribute to increased *demand* for gas. On the other, low fixed prices undercut *supply* of gas by reducing the profit-making incentive for exploration and production. Given the expense involved

² Unconventional gas developments such as the Shah project in Abu Dhabi, Khazzan Makarem in Oman, and others under consideration in Kuwait and Saudi Arabia entail lifting costs as high as US\$8 per million British thermal units (MMBtu), far above fixed domestic gas prices.

relative to prevailing prices, investors need special commercial terms to attract them to invest in gas production for domestic markets. Otherwise, as Mabro (2006) and Razavi (2009) have shown, low domestic prices incentivize investors to seek higher returns available through market-priced exports, even when those gains are outweighed by the economic benefits of using the gas domestically.

Price distortions are thus a key factor behind shortages in the Gulf. Low prices drive demand as well as the inability to meet demand, through development of large but underutilized reserves in most of the ‘gas-short’ monarchies. As shown in Figure 2, the GCC-5 states (i.e. not including Qatar) consume nearly all the gas they produce. In 2011, the GCC-5 temporarily became a net importing region, producing 193 billion cubic metres (bcm) and consuming slightly more, 198 bcm. For ruling elites in the UAE, Oman and Kuwait, it appears politically preferable to seek marginal increases in supply through imports rather than challenge established interests reliant on subsidized energy.

Figure 2. *Gas production in Qatar shown in comparison to gas production and consumption in the remaining five GCC states, 1971–2011*



Source: IEA (2013a).

2.1. Pipeline exports

The only significant cross-border gas pipeline in the GCC is the Dolphin Pipeline, which began carrying gas from Qatar to the UAE in 2007. In 2008, an extension began delivering Qatari gas to Oman. Dolphin Energy, the joint venture which owns and operates the pipeline, is controlled by Abu Dhabi state investment conglomerate Mubadala, with minority stakes held by Occidental and Total. The Dolphin Pipeline is endowed with a nameplate capacity of 33 bcm per year (3.2 bcf/day), but its current operational capacity is limited to just 20 bcm/year. In 2011, it operated at about two-thirds nameplate capacity, carrying 17 bcm from Qatar to Abu Dhabi and Dubai, and a further 2 bcm to Oman. The pipeline could be filled to capacity if equipped with additional compression, but pricing disputes have undermined Qatari willingness to earmark additional gas for the pipeline.³

Gas from the Dolphin Pipeline was delivered to the UAE at an initial price of US\$1.25/MMBtu. That price rises slightly each year and stood at approximately US\$1.50 in 2012. The pricing formula, negotiated before the sustained rise in oil and gas prices that started in 2002, is now considered a significant windfall for the UAE. While Qatar judged the exports politically important during negotiations in the 1990s, subsequent disagreement over Qatar's attempts to seek higher prices for the remaining capacity – and a recalibration of Qatari geopolitical priorities – have pushed Qatari gas marketers to seek oil-linked prices and markets outside the Gulf.

The pricing conundrum is based on opposing valuation methods. Qatar's neighbours are willing to pay what they consider a reasonable mark-up on production costs below US\$1/MMBtu. But Qatari officials, who value gas by the far higher netbacks from customers in Asia and Europe, view regional requests for 'discounted' gas as unrealistic. It bears noting that LNG marketers representing Qatar's two state gas firms, Qatargas and RasGas, also represent joint venture partners that include major international banks and oil companies.⁴ These are shareholder-owned corporations, which see no value in selling below prevailing market prices. Qatar's gas marketers have steadfastly demanded that regional buyers pay commercially competitive prices equivalent to the netback value of global LNG exports; meaning that once the expenses of transport and liquefaction are deducted, Qatari gas should fetch the same price whether it is exported to Japan or to Abu Dhabi. In short, Qatar's gas contracts hinge on preferences for the highest long-term price, followed by secondary expectations about the political and economic stability of a prospective importing country.

³ The World Bank (2013: xvi, 44) estimates the capital cost of compressors at US\$18 million.

⁴ ExxonMobil, Total, ConocoPhillips and Shell among them

Recent sales provide further information on the value of gas in the Persian Gulf. First among them is the so-called ‘interruptible supply’ of between 1.2 bcm and 3 bcm/year of Qatari gas sold to Abu Dhabi via the spare capacity in the Dolphin Pipeline. That gas is reportedly priced near US\$5/MMBtu. In 2011, Dolphin Energy resold Qatari gas in the UAE for between US\$7 and US\$10/MMBtu.⁵

While the Dolphin Pipeline can be considered a mixed success, the failure of other pipeline proposals has curtailed supply, particularly in Kuwait and the UAE. In the UAE’s case, privately owned Crescent Petroleum built an undersea pipeline from its Sharjah base to an offshore receiving platform on the Iranian side of the Gulf. Crescent’s pipeline was to have delivered up to 5.2 bcm/year of Iranian gas, but it has been sitting empty since 2006.⁶ Iranian political opposition to an agreed export price below US\$1/MMBtu is said to be behind the cancellation (Adibi and Fesharaki 2011). Further pipeline failures are discussed below.

2.2. LNG Exports

With sufficient gas supply unavailable domestically – and pipeline proposals blocked by disputes over price or territorial limits – Dubai and Kuwait have turned to LNG imports at prevailing prices (between US\$11 and US\$16/MMBtu in recent years) many times higher than gas delivered through the Dolphin Pipeline. In 2011, Dubai imported 1.4 bcm and Kuwait 3.2 bcm. (See Tables 1 and 2.) Abu Dhabi announced in 2012 that it would begin importing LNG in 2014. Bahrain is exploring a similar development. In Saudi Arabia an official in the Ministry of Petroleum and Mineral Resources told one of this paper’s authors that gas imports were also under consideration.⁷

2.3. The GCC gas deficit

Despite difficulties in sourcing sufficient supply at favourable prices, the GCC is expected to grow even more reliant on gas, given increasing demand for power and desalinated water and plans for industrial diversification. Drivers include rising population and per capita incomes, employment in gas-intensive industries such as petrochemicals and fertilizer, and domestic

⁵ International oil company (IOC) executive with knowledge of the sales; interviewed on condition of anonymity, Doha, 29 November 2011.

⁶ Badr Jafar, CEO, Crescent Petroleum; interview, Sharjah, 12 March 2012. See also Carlisle (2010).

⁷ Saudi energy official, Ministry of Petroleum and Minerals; interviewed on condition of anonymity, Riyadh, 15 October 2012. The potential for gas imports into the kingdom is controversial since import prices could set a new benchmark value for Saudi domestic gas, which has long been sold at a fixed price of 75 US cents/MMBtu. Industrial competitors argue that low gas prices provide an unfair cost advantage to Saudi petrochemical exports. Gas imports might also bring unwanted scrutiny of Riyadh’s long-term fitness as the world’s energy supplier of last resort, although they could also give more flexibility to the kingdom’s swing producer role by providing an alternative to associated gas. See also Alyousef and Stevens (2011).

Table 1. Regional gas trade by pipeline (bcm), 2011

To	From Azerbaijan	From Turkmenistan	From Qatar	Total imports
Iran	0.39	10.20	-	10.59
Oman	-	-	1.95	1.95
UAE	-	-	17.25	17.25
Totals	0.39	10.20	19.20	29.79

Source: BP (2012).

Table 2. GCC LNG imports and source countries (bcm), 2011

To	From Trinidad and Tobago	From Spain (re- export)	From Qatar	From UAE (Abu Dhabi)	From Egypt	From Nigeria	From Australia	From Malaysia	Total imports
Kuwait	-	0.08	1.52	0.05	0.07	0.80	0.26	0.39	3.18
UAE (Dubai)	0.25	-	0.92	-	-	0.09	0.08	0.08	1.43
Totals	0.25	0.08	2.45	0.05	0.07	0.89	0.34	0.48	4.60

Source: BP (2012).

gas-for-oil substitution aimed at maximizing oil exports. The US Energy Information Administration (EIA) projects that gas consumption in the Middle East's generating sector will grow by nearly 150 per cent by 2035, accompanied by only small amounts of nuclear and renewable generation replacing declining use of liquid fuels (EIA 2011: ch. 5, fig. 83).

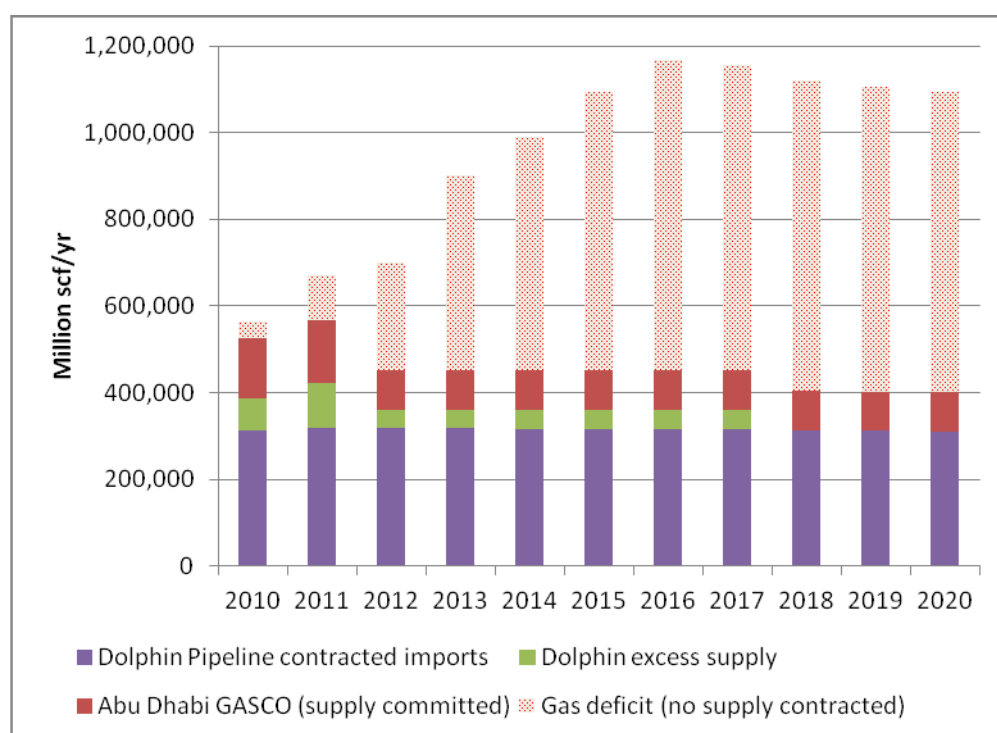
In the gas-short GCC, the marginal cost of procuring additional gas to meet these needs is far higher than the cost of domestic associated gas. For example, Figure 3 projects Abu Dhabi's large potential shortfalls to 2020. The Abu Dhabi leadership opted to import LNG to bridge this deficit and in 2012 launched construction of a regasification terminal.⁸ The price differential is roughly sevenfold. Current supply costs nearly US\$1.50/MMBtu. LNG imports will be priced above US\$10.⁹ Abu Dhabi's gas deficit only begins to shrink after 2017, when the first of four planned nuclear power stations is scheduled to begin operating.

In Oman, a government that had considered coal-fired generation in 2009 has re-embraced natural gas. However, with conventional reserves expected to be near depletion by the mid-2020s, Oman is developing unconventional reserves where lifting costs could run beyond US\$8/MMBtu, as mentioned earlier. Energy sector executives predict that Oman will cease LNG exports when contracts end in 2024, with priority shifted to job creation and power

⁸ Note that Abu Dhabi is an exporter of LNG under long-term contracts that end in 2019.

⁹ Abu Dhabi energy sector official; interviewed on condition of anonymity, Abu Dhabi, 12 March 2012.

Figure 3. *Abu Dhabi's gas deficit, 2010–2020*



Source: Abu Dhabi Water and Electricity Co.

Note. scf = standard cubic foot.

generation.¹⁰ Due to domestic demand, Oman's LNG export terminals are running at about 20 per cent below full capacity of 14 bcm/year (11 million tonnes per annum) (Darbouche 2012).

In Saudi Arabia, a US\$9 billion gas exploration and production campaign aims to slow the growth of crude oil and diesel in the power sector by substituting with gas. Saudi Aramco hopes to increase gas output by 50 per cent above 2011 production of 280 million cubic metres (MMcm) per day, but, like Oman's, most of its non-associated reserves – that is, gas that is extracted without simultaneous production of crude oil – consist of difficult formations of tight or shale gas, as well as corrosive sour gas. The kingdom has also announced plans to invest in nuclear power, but long lead times imply increasing medium-term reliance on fossil fuels. Meanwhile, Saudi Aramco has been unable to convince the government to raise domestic gas prices capped at 75 US cents/MMBtu.

In Kuwait, political infighting has blocked plans to develop non-associated gas production. As a result, Kuwait intends to increase refinery production of heavy fuel oil to replace more valuable diesel and crude in the power sector. Kuwait's gas-fired power plants

¹⁰ Officials in Oman's Ministry of Oil and Gas and an Oman-based IOC executive; interviewed on condition of anonymity, Muscat, October and November 2011.

will probably increase reliance on LNG imports (Wood 2011). Nuclear power, once considered a possibility, was rejected after the 2011 earthquake and tsunami in Japan.

2.3.1. The Gulf as an importing region

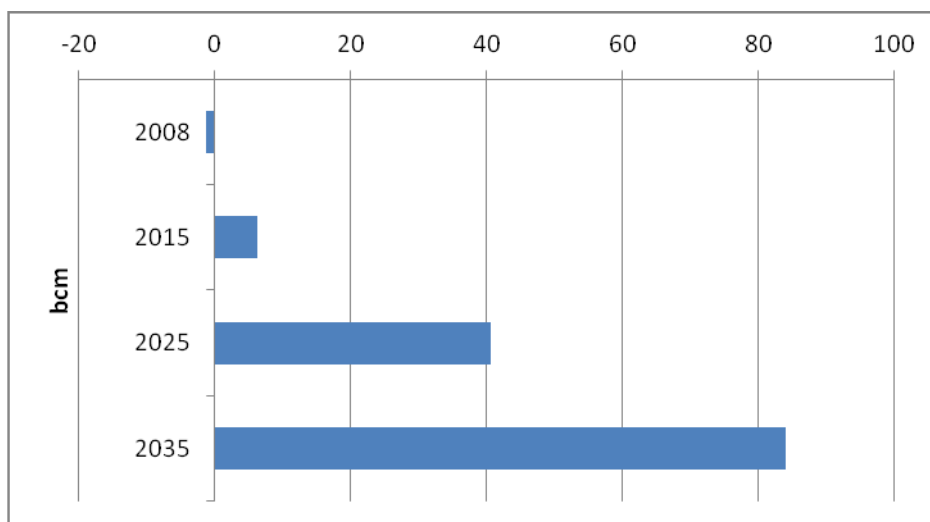
Despite the discomfort of paying global market prices for a commodity recently considered ‘free’, the GCC – Qatar excepted – is becoming a gas-importing region. The EIA projects that the Arabian producer countries (the UAE, Kuwait, Bahrain, Oman and Yemen) will require 40 bcm in yearly imports by 2025 and double that in 2035 (Figure 4). The EIA expects that Saudi Arabia, which consumes all of its gas production domestically, will remain self-sufficient. However, as mentioned above, a top official in the Saudi Ministry of Petroleum and Minerals said that gas imports were a possibility: ‘Everything is on the table. You can’t rule anything out.’¹¹

Barring major discoveries, it appears that the limits of the GCC’s inexpensive gas supply have taken shape. In all but Qatar, marginal increases in gas demand will be met by higher-cost sources, mainly non-associated and unconventional gas, or market-priced imports.

2.4. Monetizing Qatari gas reserves

In contrast with the five gas-short Gulf monarchies, Qatar controls a vast resource representing 15 per cent of the world’s conventional reserves. The Qatari state has leveraged this gas to transform the barren peninsula into the world’s richest country, on a per capita

Figure 4. *Projected imports of UAE, Kuwait, Oman, Bahrain and Yemen, 2008–2035*



Source: EIA.

¹¹ Saudi energy official, Ministry of Petroleum and Minerals, interviewed on condition of anonymity; Riyadh, 15 October 2012.

basis, while securing less tangible benefits such as global influence, political autonomy and enhanced security (discussed further in section 3).

Qatar shares with Iran the world's largest single field of non-associated gas, with nearly 40 trillion cubic meters (Tcm) of gas spread over 9,700 square kilometres, about two-thirds of which lie below Qatar and its territorial waters. The North Field, as it is known in Qatar, was discovered by Shell in 1971, the year of Qatari independence. At the time, it was considered a disappointing find of 'stranded' gas that could not be exported (Dargin 2011; Flower 2011). What was a disadvantage in the 1970s is now perceived as a great advantage. The fact that the field's chief resource is non-associated gas allows Qatar great flexibility, since gas production is not linked to that of oil and therefore is unrestricted by Organization of Petroleum Exporting Countries (OPEC) quota or market demands for oil. Natural gas liquids (NGLs) are produced in tandem with gas, but production of these NGLs is also unrestricted under OPEC rules. The North Field's lack of crude oil has thus become a crucial ingredient in Qatar's ability to develop the field independently of OPEC – and Saudi – oversight, aiding the tiny monarchy in its long quest to reduce Saudi hegemony. Elsewhere in the Gulf, the situation is reversed. Gas availability depends on crude oil extraction. In times when market or quota strictures dictate curtailed oil production, less gas is available for domestic power generation and other use.

Plans to develop the North Field and monetize the gas were launched under the then emir, Sheikh Khalifa bin Hamad al-Thani, in the 1980s. The field began to produce in 1991, with gas used for power generation, industrial projects and reinjection into the depleting onshore Dukhan oilfield. Around this time, Qatar sought an export agreement with its five neighbouring monarchies that would have launched a pipeline network delivering 10 bcm/year of North Field gas to its eastern neighbours the UAE and Oman, and a further 16.5 bcm/year in a western pipeline to Bahrain, Saudi Arabia and Kuwait. For the Qataris, pipelines appeared a more appealing option than the daunting prospects for investment in gas liquefaction and export infrastructure. Pipeline construction costs were estimated at US\$2 billion and were to be divided among the six monarchies. Conversely, Qatar's share of its initial LNG investment was US\$4 billion, double the state's 1991 GDP, and providing less than a quarter of the pipeline's export volume (Hashimoto, Ellass and Eller 2004).

But prospects for a pipeline soon soured. Saudi Arabia dropped out in 1990 and then refused to grant transit rights for a pipeline from Qatar to Kuwait after a series of

confrontations on its disputed border with Qatar.¹² The Hawar Islands border dispute between Qatar and Bahrain (resolved by a binding ICJ ruling in 2001) also stood in the way of the pipeline, as did what now appear as unrealistic price expectations. At the time, Dubai was reportedly willing to pay no more than US\$1/MMBtu for gas intended for industry, utilities and for reinjection to enhance oil recovery from a depleting reservoir (Hashimoto, Ellass and Eller 2004).

In 1995, Qatari Crown Prince Hamad bin Khalifa al-Thani deposed his father, the then ruler Sheikh Khalifa. The palace coup set off a new round of political clashes with Saudi Arabia, which backed the ousted emir.¹³ Under Sheikh Khalifa, Qatar had been closely aligned to Saudi Arabia and its foreign policy was largely subservient to Saudi dictates. The takeover by Sheikh Hamad and, a year later, the emergence of the provocative Al Jazeera news network dragged Qatari–Saudi ties to a new low. During a GCC summit in Muscat in 2001, the then Saudi Crown Prince Abdullah is reported as having accused the Qatari broadcaster, which began twenty-four-hour broadcasts in 1999, of ‘being a disgrace to the GCC countries, of defaming the members of the Saudi royal family, of threatening the stability of the Arab world and of encouraging terrorism’ (Da Lage 2005). In 2005, Saudi Arabia once again blocked plans to build a Qatari gas export pipeline through its territorial waters to Bahrain and Kuwait (Fineren 2012).

Contributing to the lost gas trading opportunities were pricing disputes. Qatari officials have since suggested that negotiators from neighbouring states lacked an understanding of the shortages they would face by the mid-2000s, and were unprepared to make concessions that would have significantly enhanced their medium-term energy security (Fineren 2012).

At first glance, Qatar’s North Field development timeline appears a lengthy one, with twenty-five years between the field’s discovery in 1971 and its first export of LNG in 1996. However, for the five Gulf monarchies now in need of gas, the opportunity to procure it from Qatar must have appeared fleeting. From the signing of the first Dolphin Pipeline agreement in 1998 Qatar sought contractual markets for its gas for just seven years, until it abruptly halted further sales in 2005, declaring a moratorium that remained in effect at the time of writing.

¹² The border dispute was solved when the frontier was agreed between the two states in 2001, but relations were damaged in other ways, including when US troops which vacated bases in Saudi Arabia shifted to new bases in Qatar. See Hashimoto et al. (2004) and Da Lage (2005: 59).

¹³ Khalifa himself took power in a similar palace coup, deposing his cousin, Ahmad al-Thani, in 1972, just a year after Qatari independence. The 1995 coup took place during gas contract negotiations, undercutting Qatar’s position in talks with buyers in Japan. The new emir, Sheikh Hamad, gave immediate backing to expanded exports and to improved ties with the West and Asia (Hashimoto et al. 2004: 29).

The full implications of the gas shortfalls affecting the GCC-5 only began to be understood around the time that the Qatari window of opportunity was closing.¹⁴

Qatar wisely pursued a second track in its gas monetization plans by investing in gas liquefaction and export infrastructure, dating to a 1984 joint venture agreement bringing together Qatar Petroleum with BP, Total, and Japanese trading houses Marubeni and Mitsui.¹⁵ The 1992 replacement of BP with US oil major Mobil, with its existing LNG development credentials, injected much-needed financial and political security into the project. Earlier investors, including BP, were leery of investing in the volatile Persian Gulf region, which, just a few years earlier, had seen more than 500 oil tankers attacked during the Iran–Iraq ‘tanker war’.¹⁶ Investor concerns were assuaged by the presence of a US oil major and the implied deepening of US defence cooperation a year after the US-led reversal of Iraq’s occupation of Kuwait.

Japan’s participation was also crucial to the success of the first LNG venture, named Qatargas. Japanese entities contracted to buy nearly all the plant’s LNG, while also financing the US\$5 billion downstream portion of the project and the construction of the required tanker ships. Qatar rapidly developed its LNG export capacity. It inaugurated its first three export trains in 1996, reached world number 1 status by 2006, and by 2012 attained its capacity goal of 77 million tons per annum (mtpa) or 105 bcm/year.

Qatar’s lucrative LNG ventures validated the tough stance it had pursued in simultaneous export discussions with neighbouring monarchies. Qatari state firms and their joint venture partners were able to negotiate long-term bilateral contracts with Asian and European importers at prices that, with few exceptions, were linked to oil or derivative product indexes. Further, Qatar’s shift in market preference came alongside a significant increase in market pricing for gas. With gas prices contractually linked to oil prices – and oil prices beginning a sustained rise in 2002 – global gas prices soon grew to many multiples of their fixed prices in the GCC. For instance, Qatari LNG shipments to Japan assumed average prices of US\$3.45/MMBtu during negotiations. At launch in 1996, Qatargas LNG was priced around US\$4/MMBtu, and thereafter prices fluctuated with the price of oil, bottoming out at US\$2.75 at the end of 1998, reaching nearly US\$17 in 2008 and surpassing that level after 2010 (Flower 2011).

¹⁴ Engineers at Total are said to have discovered the UAE’s looming gas deficit in 2005 and alerted the UAE government to the coming shortfall, but, at the time, could not find willing listeners. By 2008 the gas deficit in the UAE and elsewhere in the Gulf monarchies became public knowledge.

¹⁵ Mobil replaced BP, which withdrew in 1992. Mobil became part of ExxonMobil in 1999.

¹⁶ Abu Dhabi’s tanker ships delivered LNG to Japan unmolested throughout the tanker war.

Higher gas prices available outside the Gulf region spurred Qatar's LNG push while encouraging it to drop plans for increased regional pipeline exports. At the same time, low fixed gas prices within the region continued to thwart investment in increased production for local use.

2.4.1. The moratorium

Opportunities to procure increased production of Qatari gas came to an abrupt halt in 2005, when Qatar's energy minister Abdullah al-Attiyah declared a temporary halt to further gas extraction and exports beyond those already planned. The rationale for this 'moratorium', as it became known, was described publicly as a period required for modelling the reservoir to assess its potential longevity. However, restrictions that were initially supposed to last for two years have been repeatedly extended and at the time of writing were said to remain in effect until at least 2015.¹⁷ Qatari officials have denied suggestions that the moratorium is linked to specific geological problems and say it originates from a more general concern for the reservoir's health. Other energy executives in Qatar have said the moratorium on new production is based on technical and economic concerns:

- first, to understand the reservoir's reaction to sustained production of 23 billion cubic feet (bcf) per day;
- second, to cool Qatar's overheating economy and double-digit GDP growth;
- third, to ensure that Qatar, in moving quickly from 10 per cent of global LNG market share to 30 per cent, could find reliable markets for all of its production, especially given the growth in spot markets for LNG that have created competing supply options to traditional long-term contracts.

3. ENERGY'S ROLE IN QATARI FOREIGN AND SECURITY POLICY

Qatar's conduct of foreign relations, and its policies dealing with energy exports and national security, provides a textbook example of a small state deftly exploiting its comparative advantage to achieve an international presence far beyond that merited by its size. Qatar's global ambitions are often portrayed as manifestation of the policymaking goals of regime-connected elites, especially its ruling family. But it is important to recognize that Qatar's aims have been enabled by its successful and rapid economic development.

¹⁷ See, for example, the EIA's Qatar page, at www.eia.gov/countries/cab.cfm?fips=QA; or this statement from BP: www.qatar.doingbusinessguide.co.uk/partner-profiles/bp.

Qatar's security policy evolved markedly in the period following Sheikh Hamad's 1995 accession. Energy took the integral role that it maintains under his successor, Sheikh Tamim, who assumed control upon his father's voluntary abdication in June 2013. To understand the linkages between Qatar's energy policy and its foreign and security policies, it is important to appreciate the evolution of Qatari foreign relations.

Qatar is a small state in what has historically been an unstable neighbourhood. Despite its close cultural ties and treaty relations with Saudi Arabia, Qatar tends to view the kingdom simultaneously as an ally and hegemon. This perception is shared to some degree by the other Gulf monarchies, which generally follow Saudi Arabia's lead on foreign relations and oil export policy. The other regional hegemon, Iran, has traditionally posed a much greater threat to the Gulf monarchies. Iran–GCC relations have historically been undermined by mistrust, conflict and territorial claims. New ideological threats emerged after the 1979 revolution, including those manifested in the Sunni–Shiite sectarian divide, in revolutionary ideology that challenged monarchical legitimacy, and in attempts to weaken links between the GCC and the United States.¹⁸ The close presence of Iran is thus a key factor in Qatar's drive to bolster national security.

Qatari rulers have traditionally sought protective alliances with external powers, in line with the overlapping tributary tribal alliance networks which characterize the region's history. As far back as the 1900s, Sheikh Jassim bin Mohammed al-Thani pioneered the playing of major powers against one another as a means of achieving security while avoiding dependence on any one power.¹⁹ Qatar thus entered into protective relationships with the al-Saud, the Ottomans, the British and, in the current era, the United States. The leadership has consistently intended to leverage these ties to achieve the hard security needs of a small state while allowing for political stability, economic growth, and greater autonomy of action in both domestic and foreign policy.

In this context we can better grasp the moves made in the aftermath of the 1995 coup d'état, in which Sheikh Hamad faced immediate needs to shore up domestic support before pursuing his ambitions in economic and foreign policy. The new ruler's first year in power was marked by a serious test when neighbouring monarchies threw their support behind the ousted former emir, Khalifa, culminating in the unsuccessful counter-coup attempt of 1996.

¹⁸ For more on GCC–Iran relations, see Nonneman (2004), Cronin and Masalha (2011) and Anthony (2011).

¹⁹ This approach was notably copied by Sheikh Mubarak bin Sabah Al Sabah (Sheikh Mubarak the Great), who ruled Kuwait from 1896 to 1915.

The uncertainty and turbulence characterizing relations between Qatar and its neighbours underlined the need for a multifaceted foreign policy geared toward overcoming these threats.

3.1. The US role

Improving ties with the United States was the first step. Close US–Qatar relations are a recent development. Washington did not establish an embassy in Doha until 1973. During the 1980s, Washington froze diplomatic and security cooperation after learning of Qatar’s black market purchase of US-made anti-aircraft missiles (Blanchard 2012). Stronger ties developed during the US-led restoration of Kuwaiti sovereignty in 1991, when Washington established a formal military presence in the Gulf, including Qatar.²⁰ At the time, major US military deployments were based in Kuwait and at the Prince Sultan Air Base in Saudi Arabia. When Saudi domestic opposition made maintenance of US troops in the kingdom untenable for the al-Saud, Qatar began making overtures to host an American deployment in hopes of enhancing security. In 1996, Sheikh Hamad invested US\$1 billion on construction of the Al Udeid Airbase in the Abu Nakhlah area southwest of Doha, even though Qatar had no indigenous air force (Blanchard 2012: 12).²¹ Qatar adopted further policies to complement its US tilt, including the opening of an Israeli trade office in Doha in 1996, and the funding of Doha branches of several satellite US university campuses and notable think-tanks, including the RAND Corporation. Security was the grand strategic pillar in Qatari foreign policy, and the United States was integral to its success.

Washington’s decision to redeploy US forces from Saudi Arabia to Qatar brought a major improvement in Qatar’s insecure environment, particularly since the 1995 coup. In 2003, the US Central Command moved its Air Operations Centre from Prince Sultan Airbase in Saudi Arabia to Al Udeid, from where it controlled US air manoeuvres in the wars in Iraq and Afghanistan. A second major base at the adjacent Camp As-Sayliyah also hosts US troops involved in regional conflicts. The domestic stability arising from the US military presence allowed Qatar to consolidate development policies and enact political reforms. These reforms have, in turn, contributed to increases in economic and governance capacity that set the stage for the transformative economic growth Qatar has experienced since 2002.²²

²⁰ Qatar agreed to destroy the US-made Stinger missiles as part of a bargain allowing US forces to operate from Qatari territory. The US Senate repealed the ban on military and diplomatic cooperation on the basis of the US defence secretary’s assertion that it was in the US interest to re-establish US–Qatari security relations, due to Qatari support for US troops in the Middle East. See Blanchard (2012: 11 fn. 32).

²¹ Here it is also possible to draw a parallel with decisions made in 1916 by the Qatari leadership, which entered into a special treaty relationship with the British in order to gain protected military status.

²² Security relations under treaty with the British played a similar stabilizing role from 1916 to 1971.

3.2. *Energy's role in Qatari foreign relations*

As US–Qatar relations have evolved, so has energy's role in national security. While Qatar's desire to enhance US ties was driven by basic security needs, it harboured two further strategic requirements that ran counter to its dependence on America. First, Qatar exhibited a strong wish to improve its regional autonomy with respect to a dominant Saudi Arabia. Second, it sought to diversify its security requirements beyond a simple reliance on America. Sheikh Hamad's government leveraged energy policy to build new strategic relationships that succeeded in fulfilling these needs. In effect, Qatar's exports – especially of natural gas – have enmeshed it in other states' energy security calculations while shifting it away from Saudi influence. As importing states have come to depend on Qatari supply, their dependence has led them to become stakeholders in Qatari domestic political stability and external security. These relationships have bolstered autonomy and provide Qatar with what is best described as a diversified security framework. Thus Qatar's extraordinary energy resources relative to its population have extended this small state's geopolitical reach beyond the norms usually seen in international relations. This was most clearly observed during the height of the Arab Spring as Qatar adopted a proactive foreign policy that contrasted with the quieter stances of its neighbours. Qatar was particularly active in supporting the Libyan revolution and, more controversially, backing the rise to power of Mohammed Morsi's Muslim Brotherhood in Egypt following the overthrow of Hosni Mubarak.

As part of this diversified security framework, the significance of Qatar's bilateral energy relations with major Asian and European powers should not be underestimated. These energy contracts form an important part of consuming countries' economic and energy security calculations, which instil in them a vested interest in maintaining a secure and stable flow of Qatari resources. This is not to argue that a hard-security umbrella has been *replaced* by a diversified framework. Without the US presence, the energy lifeline would be vulnerable. But the Qatari gas exports, fostered independently of OPEC and largely on the basis of long-term contracts, have allowed the Qatari state to grow *less reliant* on US diplomatic support. These contracts have nurtured special and supportive relationships between Qatar and its customers based on combined economic and security interests, and therefore enhance Qatar's geopolitical capacity.²³

The grand strategic aims of Qatar's innovative foreign policy can therefore be interpreted as maximizing independence of action through enhancements in Qatari autonomy

²³ This approach is complemented by Qatar's sovereign wealth investment strategy, through which it reaps further political influence.

within the region, while augmenting national security. These aims have largely been fulfilled. As mentioned, Qatar's break with regional norms of discreet involvement in international affairs was notably on display during the pan-Arab uprisings since 2011 under the former (now 'Father Emir') Hamad bin Khalifa. Yet following the 2013 succession of Sheikh Tamim as emir, a recalibration of Qatar's priorities has taken place. Focus has shifted to internal economic and social development, through a ministerial reorganization and appointment of a more technocratic cabinet. This is not to say that Qatar's foreign policy has changed direction; but the previous proactive and interventionist foreign policy seems to have been eclipsed by greater focus on domestic development.

Qatar's geopolitical achievements have come at the nexus of energy, foreign relations and national security, and stand in contrast to the security frameworks adopted by its GCC neighbours. Saudi Arabia has also leveraged energy exports to enhance its security, by cultivating an influential relationship with Washington through its role as the global energy market's swing producer. Qatar takes a different route. Instead of relying on global market power, it uses a diverse set of bilateral linkages forged through long-term export contracts, which represent an innovative security formulation in the international system.

4. DISCUSSION: IMPLICATIONS FOR REGIONAL SUPPLY

Where does this leave the gas-short countries in the Gulf region? For the five neighbouring monarchies, the implications of LNG's role in Qatar's foreign and security policies mean that Qatar's desire to trade hinges mainly on commercial profit, but also on strategic criteria of political influence and market development. Using this framework, how would Qatar approach the proposition of increased exports to its neighbours?

Qatar could further its strategic goals of building additional political capital among its neighbours and perhaps securing greater autonomy from Saudi Arabia by increasing its gas exports to the UAE, Oman, Kuwait and Bahrain. But, given the likelihood of an opportunity cost in selling additional gas to its GCC neighbours, Qatar is likely to maintain its preference for exports to competitive markets which lack expectations of low prices. Qatar's past behaviour implies that it places more value on the benefits to its security and autonomy that arise from expanding market share and trade relations with Europe and Asia than it does to any such benefits that may arise from increased trade with its immediate neighbours. This perception is demonstrated by Qatar's unwillingness to increase exports through the Dolphin Pipeline. If Qatar placed sufficient value on increasing dependence on itself within the UAE

and Oman, it could simply fill the pipeline's unused capacity.²⁴ Since it has not done so, it would appear that the marginal benefits of increasing exports to its neighbours are outweighed by those of exports outside the region.

4.1. Implications of a shifting gas market

However, would Qatar's calculations change if the opportunity cost were reduced? That is, how would Qatar behave if an increase in global LNG supply brought down the price of LNG in Asia? How would it react if GCC neighbours were willing to pay higher long-term prices?

A proliferation of large gas discoveries and increases in production – along with slowing demand in Europe – suggest the future possibility of an oversupplied global market. Some of the increased supply was due to expanded exploration and discoveries of new sources of gas such as those in the Eastern Mediterranean, East Africa and Australia. The largest increase stemmed from unconventional gas production in the United States, linked to technological advancements in hydraulic fracturing and horizontal drilling. Increased US shale gas production has reduced America's need for imports, displacing supplies in global trade and pushing down prices in North America and Europe. These effects are expected to grow as US production increases and shale gas extraction spreads to other parts of the world. The EIA expects the United States to become a net exporter of LNG by 2016 and an overall net exporter of gas by 2018 (EIA 2014: 13), while the IEA expects US natural gas production to continue rising until at least 2035.²⁵

The global market effects of US shale gas production would have been stronger had it not been for a sudden spike in demand in East Asia, triggered by the shutdown of Japan's nuclear power sector after the 2011 Fukushima disaster. Japan thus provides a destination for displaced cargoes of LNG. Further ahead, continued increases in gas demand in China and India are expected to provide large future markets for Qatari LNG, as continued increases in US gas production incentivize Qatar to develop further its economic linkages with the East.

The market effects of further LNG exporters coming on stream in Africa, the Levant, Russia, North America and especially Australia – which is expected to emerge as the world's second-largest LNG exporter after 2015 – could eventually produce a gas glut.²⁶ Even so,

²⁴ An investment in the increased compression required to increase the Dolphin Pipeline's capacity to nameplate levels of 3.2 bcf/day was reported to be under way at the time of writing. This would allow the possibility of a 1 bcf/day increase in exports by 2015. Whether gas will be made available remains to be seen. See John (2013).

²⁵ US production is expected to reach nearly 840 bcm by 2035, up from 649 bcm in 2011. See IEA (2013b: 108–9).

²⁶ According to forecasts using the Rice World Gas Trade Model described in Medlock (2014).

Qatar is among the LNG providers with the lowest unit costs,²⁷ which allow it to maintain profitable exports during periods of very low prices. A drop in world gas prices or a loss of a major export market could provide an incentive for Qatar to reconsider the value of a nearby export market, especially where bid prices near netbacks from external markets. But, as mentioned, Qatari decisions regarding gas exports – and especially those involving LNG – are governed not only by domestic considerations but also by the commercial requirements of its international oil company (IOC) joint venture partners. Qatar has shown willingness to use gas as a stabilizing resource for friendly governments, as evidenced by its offer to donate five LNG shipments to Egypt in 2013. However, even these were to have been purchased by the Qatari government at prevailing commercial rates.²⁸ If political instability became an issue among its neighbours and it appeared that gas exports could bolster public support for friendly regimes, Qatar might find a compelling case for revisiting discounted exports.

Further ahead, evolving gas market dynamics will influence the potential for renewal of several of Qatar's first twenty-five-year Japanese export contracts, which expire in 2021 (Darbouche 2012). Once again, the availability of a regional market could offset loss in market share elsewhere. Either way, it appears that the emergence of rival geopolitical energy centres will compete for the primacy Doha now enjoys. As the long-term competitive picture evolves, so may the attractiveness of the regional gas market.

5. CONCLUSION

Since 1996, the tiny Gulf state of Qatar has exploited a prodigious supply of a resource once considered nearly worthless to usher in a golden age for itself. Exports of natural gas have brought the peninsular monarchy wealth, security and political influence far beyond the typical capacity of a rentier autocracy. Qatar's rise to global prominence has opened doors around the world, converting powerful trading partners into stakeholders with an interest in the stability of its monarchy, while insulating it from political dominance by larger neighbours which once called its shots. In its dealings with the United States, Qatar skilfully seized an opportunity to reset soured relations, and built a strong military and commercial alliance that has secured its once-shaky national defence. US security guarantees, in turn, provided Qatar the breathing space to build an extraordinarily lucrative and well-timed LNG export sector.

For the five gas-short Gulf monarchies, the onset of Qatar's golden age means they have been edged out of the equation. Gas import opportunities lost amid a series of seemingly

²⁷ Unit costs of Qatari LNG are said to be globally 'unmatched'. See Ibrahim and Harrigan (2012: 7).

²⁸ The Qatari government was said to have agreed to pay Qatargas II and its partners Total and ExxonMobil US\$13/MMBtu for the Egyptian donation. See Reuters (2013).

petty price and border disputes also wound up encouraging Qatar's development of much more politically and commercially attractive markets. This is further reinforced given the divergence of Qatar from some of its GCC neighbours with regard to Egypt and Iran. In effect, Qatar has 'risen above' prickly relations with its erstwhile trading partners in the region and now sees its fortunes increasingly tied to big economies in the East. For the gas-short GCC, it would appear that the window of opportunity for securing sufficient supply of Qatari gas has closed.

In the longer term, it is possible that this closure may be revisited. The entry of new suppliers and disruptive technology into global gas markets bodes well for gas importers in the GCC and globally. Whether Qatar will accept an increased role for itself in the regional gas trade remains to be seen. If regional and international gas prices begin to converge, Qatar will have to balance its geopolitical preferences for creating international stakeholders with the potential benefits of cementing relations with regional partners and embracing a more meaningful GCC collective. Until then, Qatar's horizons remain global.

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