Asia Times Online

Hidden energy crisis in the Middle East

By Victor Kotsev
3/12/2011

TEL AVIV - While most of the world is preoccupied with the impact of instability in the Middle East on oil prices and the world economy, a different kind of energy crisis is unfolding practically unnoticed. An ongoing reshuffle in natural gas supplies has left at least two countries - Israel and Jordan - without much of the gas they need.

In general, the politics of Middle Eastern gas will probably be just as dramatically affected by the upheaval as those of oil, but will follow a separate trajectory. Their effect will, at least initially, be more local in nature, and will vary for each country. However, the energy status quo in the region is slated to change dramatically.

On February 5, at the height of the uprising against then-president Hosni Mubarak, a massive explosion rocked a gas terminal near the Egyptian town of El-Arish. The head of the Egyptian natural gas company, Magdy Toufik, blamed it on "a small amount of gas leaking',' but it soon emerged that the most likely cause was an act of terror - in some accounts, two separate terrorist attacks. According to reports in the Associated Press, "The terminal's guards testified that [four masked gunmen] stormed the terminal in two cars, briefly restrained the guards and then set off the explosives by remote control."

The terminal lay on the Arab gas pipeline carrying Egyptian gas to Jordan, Syria, Lebanon and even Turkey. The section that branches off of that pipeline into Israel was not affected, but Egypt shut off gas supplies to the Jewish state as well. Egyptian authorities claimed that the system needed "to cool off',' and that they would resume supplies within a week or so.

Over a month and US$150 million of losses later (for Israel and Jordan combined), the gas is still not flowing. Egyptian authorities are quickly changing their tune: having missed at least two self-imposed deadlines to resume the supplies, until a few days ago they continued to insist that the pipeline would be activated very shortly.

Now, however, they have started to ask for an increase in the price at which they are selling the gas. "Egypt has officially informed Jordan that the gas supplies will resume only if Amman signs an agreement on new rates," an unnamed official told Agence France-Presse on Tuesday.

There is some sound logic in this request, while less so in the manner it was made. For the past five years, Egypt has been selling gas to its northern neighbors at highly subsidized rates despite facing a shortage of gas at home. This led to an absurd situation last year when the Egyptian government was forced to consider buying back its own gas from Israel at a 600% premium to match the market rate. [1]

The Egyptian military regime, facing a dire financial situation, seems intent on righting this injustice.

In the case of Israel, it has some trumps to play, not least of which is the antipathy of the Egyptian street toward the Jewish state. In late 2008, a Cairo court ordered the government to stop the exports, because they were never approved by the Egyptian parliament. Mubarak ignored the order, which did not have a timeline attached to it, but it seems that the current government will use it as an excuse to renegotiate the treaty.

Meanwhile, recent reports indicate that Mubarak and his family are facing indictments for corruption, including possibly for taking bribes in order to ensure the gas deal. [2]

Jordan is even more important than Israel, because it buys more gas and at an even lower price. Whereas Israel currently pays $4.5 per MBTU (million British thermal units - a unit of measurement used for natural gas), Jordan pays $3. Egypt's gas accounts for 40% of Israel's gas imports and 20% of the Jewish state's electricity, while Jordan relies on it for 80% of its electricity production. (Syria's and Lebanon's imports are meager by comparison - Syria, for example, relies on Egypt for only about 7% of its gas).

Thus, the Egyptian leadership is applying a familiar tactic: beating up on Israel to convey a message to the Arab world. Indeed, this is more or less exactly how a message to Amman is being framed. In the words of a Western diplomat in the Jordanian capital speaking to Agence France-Presse, "It is difficult for Egypt to export gas to Jordan, and not Israel, without raising an international outcry."

The crisis has generated a lot of speculation, at least inside Israel. Neither Israel nor Jordan seems in a position to resist the Egyptian overtures. Both have the capacity to use alternative fossil fuels such as diesel and mazut to generate electricity, but this costs roughly 10 times as much as gas does, and has a disastrous effect on the environment.

Currently, the Jewish state is losing about $1.5 million a day from the cutoff, while Jordan's losses stand at $2.2 million a day.
According to the Israeli business newspaper The Calcalist, there are three possible scenarios: either the gas remains cut off permanently (unlikely), or deliveries resume in smaller quantities (moderately likely), or deliveries resume in full but with a price hike (most likely). The Calcalist estimates that an increase in payments of about 33% would settle the dispute; over the course of the 20-year contract, this would bring Egypt an extra between two and three billion dollars from Israel alone.

Most Israeli analysts see in this a temporary solution at best. "While the current disruption appears to be temporary," Zafrir Rinat writes in the Israeli daily Ha'aretz, "those in charge of Israel's energy economy must prepare now for the possibility of more prolonged interruptions, whether due to problems operating the pipeline or a reversal in Egypt's commitment to supplying natural gas to Israel."

What is remarkable is that Israel itself has recently started to eye prospects at becoming a gas exporter. In December 2010, off its Mediterranean coast, the Noble Energy Consortium confirmed the most significant deep-water gas discovery in the past decade: Leviathan. The previous year, a smaller but still major discovery was made at the Tamar field nearby. More statistics can be found here, but the punch line is: "Israel now faces the unprecedented prospect of at least partial energy independence."

It will take several years before gas from the new fields starts flowing, and this is exactly how much time Israel needs to buy. The process faces further complications, as the Benjamin Netanyahu administration already initiated a procedure to raise its tariffs on the profits of the gas companies, but we can assume that with instability in Egypt, officials will do their best to stick to their self-proposed deadline of 2013.

Once the new gas is pumping, it will impact substantially on the energy and geostrategic calculations in the region. In a related development, Cyprus and Israel agreed to delineate their maritime border (in itself a diplomatic advance for the Jewish state), which in turn drew negative attention from other countries, including Turkey and Lebanon. Lebanon has already attempted to claim ownership of the Leviathan, and this may become the next issue of contention between Israel and Hezbollah. [3]

On the other hand, Egypt will probably be relieved, and its relationship with Israel will likely improve. The same applies to Jordan, which may start depending on the Jewish state for some of its energy (in all likelihood, the Israelis would welcome that, if only to have more leverage in the Arab world).

The exploration of off-shore gas fields could also provide some creative solutions to the Israeli-Palestinian talks, specifically related to the sustainability of Gaza's economy.

According to a report in the Israeli business daily Globes, last Sunday, "Prime Minister Benjamin Netanyahu ... proposed to Palestinian Authority President Mahmoud Abbas (Abu-Mazen) to jointly develop the Gaza Marine and Noa offshore natural gas fields. The

Noa field, which has 7-8 billion cubic meters of gas could replace Egyptian gas, if its supply is not resumed, while the 30-billion cubic meter Gaza Marine field could meet the electricity needs of Gaza's 1.5 million residents."

This specific proposal is, at best, tongue-in-cheek. The political climate right now would hardly allow for such a joint project to develop. The Gaza rulers from Hamas have a bitter feud with the Palestinian Authority in the West Bank; both Netanyahu and Abbas are weak internally, challenged by right-wing factions in their own governments. With all the instability in the region, one can never be sure if one's partners of today will still be around tomorrow.

However, under different conditions - for example, a significant advance in the peace talks - the idea could be quite viable. Israel is already drawing most of the gas that it consumes from a smaller find nearby, called Mary-B, which is expected to be exhausted in a year or two.

Other aspects of this thinking - the idea of energy independence for Gaza - can also aide unilateral action by Israel. In my article "A major reshuffle in the Levant" (http://www.atimes.com/atimes/Middle_East/MC05Ak07.html, Asia Times Online, March 4, 2011), I argued that Israel will most likely attempt to disengage fully from Gaza in the near future. Netanyahu's statement can be interpreted in this context as well.

Besides Egypt, the natural gas supply in the Mediterranean region is disrupted by the events in Libya, and somewhat threatened by tensions in Algeria (whose pipe to Spain is expected to be launched soon). But these crises will have very different repercussions, since the local dynamics in each country are different. As opposed to oil, natural gas is very difficult and expensive to ship, and thus it is a more important factor on a regional than on a global scale.

Most of Libya's gas exports go via the Greenstream underwater pipeline to Italy; the Greenstream has been shut off since February 22, meaning that Italy is hit the hardest. According to a Reuters report, however, the closure could actually work to Italy's favor. "The lack of Libyan gas means [Italian oil and gas company] Eni can take delivery of fuel it would have to pay for anyway under take-or-pay (ToP) contracts with Russian export monopoly Gazprom," Reuters writes. [4]

If this analysis is correct, it is conceivable that Gaddafi very carefully picked which resource to shut off first, taking into account the sensitivities of his friend Italian Prime Minister Silvio Berlusconi. By contrast, and despite reductions and the bombing on Wednesday of the major oil terminal of Libya, Gaddafi's oil exports to Europe have not stopped, as a recent Financial Times report indicates. [5]

A common pattern that emerges is that the political upheaval catalyzes powerful existing trends in the regional natural gas market. We can expect instability in the short run followed by a major restructuring of the basic energy relationships in the Mediterranean and the Middle East.

Notes

1.Israel to sell back gas to Egypt at $12b profit – report, Globes, August 24, 2010.
2. Report: Mubarak's sons received millions of dollars for backing Israeli gas sales, Ha'aretz, March 7, 2011.
3. Israel's Leviathan at Sea Newsweek, January 17, 2011.
4. Libya gas cut not all bad news for Eni-SocGen, Reuters, February 28 , 2011.
5. Oil millions still flow for Gaddafi, Financial Times, March 4, 2011.