Rising Tensions between Saudi Arabia and Iran Threaten Regional Oil Supplies

Summary

- Saudi Arabia’s execution of Shia cleric Nimr al-Nimr and an attack by Iranian hardliners on the Saudi Embassy in Tehran have triggered a deepening crisis in already poor relations between Saudi Arabia and Iran, putting the Persian Gulf’s approximately 20 percent of global oil supplies at risk of disruption.

- Initial oil impacts from the increased tension between Iran and Saudi Arabia have been limited or even bearish. Both nations appear likely to continue seeking market share as Iran begins returning approximately 0.4 to 1.0 mbd to the market in 2016 now that sanctions have been lifted. Additional downward pressure could also emerge from attempts by both nations to undercut each other’s selling prices, putting further strain on producers everywhere, including in the United States, and reducing the chances of OPEC members agreeing to cut production.

- The fracas raises the likelihood of instability in Saudi Arabia, particularly in the Eastern Province, a majority-Shia area and the locus of secessionist sentiment. If further radicalized, this activity could manifest itself in attacks on Saudi Arabia’s oil fields and infrastructure, both concentrated in the province. The world’s largest conventional oil field, Ghawar, which produces approximately 6 mbd, and largest oil processing facility, Abqaiq, are located here.

- While both Saudi Arabia and Iran wish to avoid direct warfare, the intensified rivalry and breakdown of relations raise the risk that an unexpected event or provocation could prompt a chain reaction, bringing Tehran into open warfare with Riyadh and its allies. Such a conflict would immediately place more than 11 mbd at risk. If other nations along the Gulf were to enter, the total number of barrels at risk would rise to approximately 19 mbd. Besides forcing the United States to extend its military and diplomatic resources, an open conflict in the Persian Gulf would pose a major risk to U.S. efforts to combat ISIS.

- The effects of the tensions are likely to increase oil price volatility, preventing U.S. businesses and consumers from being able to properly plan, budget, and invest. If escalating tensions severely threaten oil supplies or result in disruption, the impact would be magnified, negatively affecting the U.S. economy and testing American foreign and military policy.
Introduction

On January 2, 2016, Saudi Arabia executed 47 people on terrorism charges. Alongside al-Qaeda linked Sunni extremists were four Shia prisoners, most notably the influential dissident cleric Nimr al-Nimr, who had urged protests against the House of Saud and even advocated secession of Shia-dominated regions, mainly in the oil-rich Eastern Province.

Nimr gained popularity primarily in his home city of Awamiyah and neighboring Qatif as many Shia grew impatient with the pace of reforms aimed at answering their complaints about government neglect or discrimination. Nimr’s arrests in 2009 and 2013 prompted protests in the Shia population centers of the Eastern Province, and his influence continued to grow.¹ As much of his popularity growth was attributable to anger at the mistreatment of Shia prisoners, his death at government hands could increase instability and secessionist activity in the Eastern Province.

In addition to heightening sectarian tensions in the Eastern Province, the execution sparked a backlash from hardliners in Iran, culminating in protesters ransacking Saudi diplomatic buildings in Tehran and Mashhad. Saudi Arabia and its allies reacted swiftly and decisively to isolate Iran diplomatically in the aftermath of the riots, indicating that the longstanding animosity between the Islamic Republic and the House of Saud is reaching new highs. With Iran and Saudi Arabia already support different sides in conflicts in Yemen and Syria, the execution proved an unexpected catalyst of heightened tensions, and a further spark in the newly intensified environment could set off a chain reaction with significant implications for security throughout the Middle East and for global oil markets, with major costs for the U.S. military and the oil-dependent American economy.

Strategy and Motivations

To analyze the potential impacts of escalating tensions, it is important to understand possible directions for the crisis. To do so requires an understanding of the motivations behind the nexus of decisions and policies that have brought Saudi Arabia and Iran to where they are today.

Saudi Arabia’s Decision Making

Saudi authorities justified the execution of Nimr al-Nimr by saying that he was guilty of terrorism, despite international condemnation² of his trial. Regardless of the veracity of the government’s allegations against a cleric who, despite urging Shia secessionism did not openly call for violence, the execution sent a stern message from a Kingdom that sees itself embattled. With Iranian influence perceived in prior protests and riots in the Eastern Province—Saudi sources say there have been hundreds of security force members killed or wounded there³—Riyadh undoubtedly wanted to show that it could assert its regional primacy and what it views as its right to defend its regime. Against the backdrop of civil wars in Yemen, Iraq, and Syria, each of which features a Shia contingent receiving backing from Iran (and in Saudi eyes, particularly in Yemen, being directed by Iran), Saudi Arabia considers Iran a source of largely unchecked aggression in the Middle East.

The current state of the oil market may also be a contributing factor behind Saudi Arabia’s hawkishness. With the nation’s total reserve assets having dropped by more than $100 billion in less than a year due to the low-price environment, the country has cut fuel subsidies and is planning to slash other spending. As such factors are raising the possibility of popular discontent, the killing of Nimr rallied jingoistic fervor among much of the conservative Sunni population that forms the base of support for the government.5

Perhaps most useful for Saudi Arabia, the execution provoked a response in Iran that supported its view that Iran was seeking to undermine its sovereignty. After news broke of Nimr’s killing, a protest at the Saudi Embassy in Tehran by hardline Iranians turned destructive as some of those assembled attacked and ransacked the empty building; similar scenes at the Saudi consulate in the northeastern Iranian city of Mashhad exacerbated the crisis. The failure of Iran to protect the Saudi diplomatic presence from Molotov cocktail–wielding rioters was seen by Riyadh as an endorsement of the violence, and Saudi Arabia quickly broke off diplomatic and trade ties with Iran. Echoing coalition–building efforts during the Saudi entry into the Yemeni civil war last spring, Riyadh encouraged its allies to follow suit. Bahrain, Sudan, Somalia, Djibouti, and the Comoros—all beneficiaries of military or economic aid from Riyadh—cut ties with Iran, while Kuwait and Qatar recalled their ambassadors and the United Arab Emirates downgraded its relations. To further rally regional opposition to Iran, Saudi Arabia called special meetings of the Arab League and the Organization of Islamic Cooperation to condemn Iranian actions (votes to do so were only opposed by Iran and Lebanon) and maintain a united front.

Iranian Reaction: A Strategic Break with the Past?

Iran has seen the execution and the subsequent downgrading of ties by Riyadh and its allies as an orchestrated attack on its interests. “These actions by Saudi Arabia are aimed at covering up their own domestic problems, obscuring their recent failures in the region, and putting pressure on Iran. Saudi foreign policy in the region has been one based on oppression, violation, developing terrorism, and undermining regional security,” said President Hassan Rouhani in a recent address. In the same speech, however, he made it clear how his government is committed to trying to avoid letting what he called the political “stone–throwing” of Riyadh drag Tehran into actions that could derail Iran’s economic recovery following the end of sanctions.8 Having fought against domestic and external foes to conclude

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8 Etarnaad, “President, Emphasizing Serious Response to Attackers of Saudi Embassy, Told the Judiciary: Accelerate the Trials” ریسجمهور با تاکید بر برخورد جدی با عاملان حمله به سفارت عربستان از فقه قضاییه، January 7, 2016.
the nuclear deal, the Rouhani government does not want hardline provocateurs at home to prevent the payoff from being realized. He condemned those Iranians who had made “an attack on the reputation of the Islamic Republic of Iran” by ransacking the embassy, urging that the dozens detained have their trials accelerated due to the seriousness of their actions. Support from Supreme Leader Ali Khamenei (albeit buffeted by public anti-American remarks) for diplomatic resolutions of the detainment of U.S. sailors and the separate prisoner swap that included Washington Post correspondent Jason Rezaian have shown potential signs of efforts to limit the likelihood of direct conflict with the United States. Some, however, could interpret the detainment of the sailors, their forced appearance on Iranian TV, and praise for their captors by Khamenei, as well as recent rocket tests near U.S. ships in the Persian Gulf, as increased assertiveness by Iranian security forces acting with a sense of impunity. Regardless of what recent events truly portend for the future, Saudi perceptions of a potential Iranian rapprochement with the United States alongside aggressive behavior are likely to make Riyadh even warier of Iran’s intentions and ability to act unchecked in the region.

Diplomatic Impact with the United States and Europe
If this trend continues, despite the blowback to Iran from the embassy attack, it will most likely fuel fears in Riyadh following the conclusion of the nuclear deal between Iran and the P5+1 that U.S.-Iran ties are growing at Saudi Arabia’s expense. Rouhani’s recent trip to France and Italy, which helped cultivate greater commercial ties between Iran and Europe, will also undoubtedly concern Saudi Arabia. Friendship between the governments in Washington and Tehran is, in reality, still impossible for the foreseeable future, given issues including the continuation of unilateral U.S. sanctions against Iran and American objections over Iran’s support for groups like Hezbollah and the Assad government in Syria and its antagonism toward Israel. However, the conclusion of the nuclear deal prompted reports of private condemnation of the accord, even as King Salman gave it polite acceptance in public. Considered prudent diplomacy by the Obama administration, the fledgling nuclear deal that has held so far, the liberation of the five Iranian-Americans held in Iranian prison, and the resolution of the sailors’ detainment, are viewed by Riyadh (and some in Washington as well) as American weakness against Iran (or even an embrace of Iran).

Possible Regional Impacts
As Iran and Saudi Arabia had long been at odds over regional political and security issues, the deterioration in their relations would not at first appear to be a great change, but the suspension of trade ties could be a major weapon for Riyadh against Iran. Among Middle Eastern nations, Saudi Arabia has been among the top four sources of imports and exports from Iran in recent years. While it is still far less significant to Iran’s economy than other nations, particularly China, an enforcement of the Saudi trade ban could cause pain to Iran, particularly if the U.A.E. also cuts its deep trade ties to Tehran. Thanks in part to heavy trade through Dubai, the Emirates are a crucial economic partner of Iran. Eleven percent of Iran’s exports in the last Iranian calendar year went through the U.A.E., while over 19 percent of Iran’s imports arrived from there.

Going forward, neither Iran nor Saudi Arabia is seeking direct war with the other. But the raised tensions, shifting regional ties, and economic fallout emanating from the execution and its aftermath

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9 Id.
13 IMF, Direction of Trade Statistics.
raise the level of security risks in the region. Since King Salman ascended the throne a year ago, a more assertive approach to domestic and regional threats has emerged in the Kingdom, with Crown Prince Mohammad bin Nayef and defense minister Mohammad bin Salman each pushing hawkishness through a ruthless approach to counterterrorism and by leading Saudi Arabia into operations in Yemen that have lasted longer than a year, respectively. Likewise, even with the shift towards greater diplomacy with the West, Iran’s foreign policy hawks and the Islamic Revolutionary Guard Corps (IRGC) remain extremely assertive within the region, and the potential for conflict is raised by the recent deepening of the dispute.

With King Salman’s health reportedly deteriorating, the elevation of Mohammad bin Nayef and Mohammad bin Salman to such influential positions and in the presumed line of succession could cause internal strife within the royal family. Not only might this increase the likelihood of instability and internal chaos in the case of a succession battle, raising the chances for a sustained uprising in the Eastern Province, but it could prompt further bold actions in the Middle East by Mohammad bin Salman in an attempt to assert the new order. Either of these developments could cause domestic or regional crises, threatening oil infrastructure.

### Oil Market Implications

The Middle East region produces more oil than any other region in the world, totaling approximately 28 mbd, or 30 percent of the world’s supply in 2014. More than 40 percent of this supply is from Saudi Arabia, which also holds the vast majority of the world’s spare oil production capacity (typically—although not always—used to help offset disruptions to supply). Iran produces approximately 3.3 mbd of petroleum and other liquids at present. International sanctions on Iran were lifted on January 16, 2016 with the full implementation of the Joint Comprehensive Plan of Action, and as a result Iran’s output is expected to rise between 0.4 and 1.0 mbd year-over-year in 2016. The International Energy Agency forecasts 0.3 mbd by the end of the first quarter.

OPEC’s meeting in December 2015 resulted in no change in approach from member countries towards an oversupplied market. Moreover, Saudi Arabia, which increased production in part to offset the effect of Iran sanctions, does not appear willing to now reduce production to accommodate the return of Iranian oil to the global marketplace. In fact, Saudi Arabia continues to maintain relatively high levels of output even since prices began falling in 2014 and has lowered official selling prices to customers in Europe and Asia in recent months.

Against this backdrop, the initial impact of the increased tensions between Iran and Saudi Arabia in the oil market has been minimal. If anything, the aftermath of the execution of Nimr al-Nimr has exerted downward pressure on oil prices, as greater animosity would seem to make the prospects of a deal between Riyadh and Tehran to limit output less likely. The lower prices offered by Saudi Arabia, announced shortly after the diplomatic flare-up, could possibly signal a short-term race to the bottom with Tehran in the hopes of complicating Iran’s efforts to find buyers for its returning crude.

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15 SAFE analysis based on data from: U.S. EIA.
16 Id.
While the possibility of high oil prices emerging from the current tensions is a real one that poses significant risks to the U.S. and world economies, it is important to note that the ongoing reinforcement of low oil prices carries its own risks, particularly among countries whose economies are heavily reliant on oil export revenues. Saudi Arabia is likely best positioned to ride out lower prices due to its massive, although declining, financial reserves ($608 billion as of the end of 2015, down from a record $737 billion in August 2014\(^\text{21}\)), but could also be encouraged into more hawkish action abroad, like the Yemen conflict. Countries far worse prepared economically, like Venezuela and Iran, could become increasingly politically unstable and more erratic in their foreign policy if their governments feel sufficiently threatened by low oil revenue, and the ever-assertive Putin government could engage in further provocation abroad if put under enough pressure.

With tensions higher between the two regional producers, there is an increased likelihood of supply disruption. The Persian Gulf, lying between them, is home to the Strait of Hormuz through which approximately 30 percent of daily global maritime oil trade flows (the volumes ranged from 15.7 mbd to 17.0 mbd between 2009 and 2013).\(^\text{22}\) Thus, despite the current global oversupply, the quantities of oil that must pass through the waters between these two embittered rivals is sufficient to pose a risk to global oil prices. Even today, and especially when the market eventually rebalances, the global nature of the oil market means that insecurity in the Middle East region poses a risk to oil prices everywhere.

With the potential of the Saudi–Iranian dispute to cause both downward and upward movement in oil prices, one prime danger the escalating tensions pose comes in the form of increased oil price volatility. Notably, as oil prices fell from July 2014, volatility returned to levels not seen since 2008–2009 when prices fell from the historic highs of July 2008 (See Figure 2).\(^\text{23}\) Although the causes include factors well beyond the tensions between Iran and Saudi Arabia, oil prices have swung 25 percent lower since the start of the year alone, and therefore volatility remains elevated in 2016 thus far.\(^\text{24}\) Meaningful levels of oil price volatility are likely to remain in at least the short to medium term, negatively affecting the planning and budgeting of consumers and businesses alike.

In addition to the prospect of continued and potentially greater price volatility, a Middle East in the throes of protracted regional conflict, with Saudi Arabia pitted against Iran in a proxy war, would likely result in a larger, more enduring risk premium attached to the prevailing global price of crude oil due to fears of deepening political instability, terrorism, and war. These effects would likely be far greater than other recent examples of elevation in the risk premium, such as in 2012 when

\(^{21}\) Reuters, “Saudi c.bank net foreign assets drop 3.1 pct m/m in December,” January 28, 2016.


\(^{23}\) SAFE analysis based on data from: EIA.

\(^{24}\) Id.
Iran threatened multiple times to close the Strait of Hormuz unless sanctions against it were lifted, causing several short-term oil price spikes.\textsuperscript{25} Prolonged regional tensions with multiple simmering hotspots and the threat of full-fledged war ever present could likely create a premium on par with what could have been expected from Iran gaining nuclear status, estimated at up to a 25 percent addition to the price of oil by the Bipartisan Policy Center (BPC) in a 2012 report.\textsuperscript{26} With relations between countries in the region likely to deteriorate further, prices may remain permanently elevated in the event of similar threats or provocations.


Potential Oil Supply Disruption in Saudi Arabia from Upheaval in the Eastern Province

Nimr al-Nimr’s base of support lay in the Eastern Province, where the majority of the population is Shia, and upheaval there could cripple the Saudi oil industry. The potential for a heightened sense of injustice against the Shia population there in the wake of his execution is high; immediately after his death was announced, Saudi security forces clashed with protesters in the region, particularly in Nimr’s hometown of Awamiyah, where one protester was killed, and the nearby city of Qatif. The province is the heart of Saudi Arabia’s economy, home to more than half the nation’s oil production and the world’s largest conventional oil field, Ghawar, and its largest oil processing complex, Abqaiq.

While the Saudi government is well aware of the security risks it faces in the Eastern Province, the possibility of domestically planned attacks there has likely been elevated by the decision to execute Nimr. Terrorists seeking to harm the central government would need look no further than the region’s many oil fields, processing plants, and export terminals. A partial disruption, caused by taking any of the province’s major onshore fields offline, would have severe effects—in addition to the massive Ghawar field, which can produce nearly 6 mbd, Khurais can produce 1.2 mbd, and the Shaybah, Qatif, Khursaniyah, and Abqaiq fields all produce between 0.4 and 1.0 mbd. Even excluding spare capacity at those fields, if Saudi fields offshore are included, the total production relying on the province reaches over 9 mbd. The province is also home to the bulk of Saudi Arabia’s refining and export processing facilities. The Abqaiq facility, which processes approximately 7 mbd before sending it to nearby refineries or export terminals and reportedly has an even greater capacity, sits near the coast of the Eastern Province, not far from the epicenters of dissent in Qatif and Awamiyah.

A 2006 attack on Abqaiq, attributed to al-Qaeda (which, despite its failure, contributed to a 6 percent oil price increase in a single day), shows precedent that newly emboldened or newly formed militant groups could cause considerable damage given the opportunity. If violence in the Eastern Province were significant enough to cause a complete shutdown of the area’s production and export capacity, approximately 10 mbd in exports and over 9 mbd in production would be lost from the global oil market, likely resulting in a catastrophic price increase, even in a slack market. While it is difficult to quantify future price impacts in today’s market, in 2012, BPC suggested a descent into conflict in the Eastern Province taking even 7.7 mbd temporarily off the market would result in an oil price spike of 55 percent over a year.

Any attack taking meaningful amounts of Saudi oil off the market would be harmful not only due to the loss of supply to the global market, but also because this could deprive the world of its main source of spare capacity. This spare capacity can provide a short-term buffer in the event of unexpected supply disruptions or demand surges that cause oil price volatility. Moreover, Saudi spare capacity is currently estimated to be at its lowest levels since 2008 as it continues to produce in excess of 10 mbd despite lower oil prices. If spare capacity were rendered unavailable the world would be without one of its primary defenses against supply disruptions. The challenge would be exacerbated if markets were tighter.

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27 Financial Times, ”Saudi police kill one in execution backlash,” January 4, 2016.
29 Id.; Note: Although Saudi Aramco lists its capacity as being greater than 7 mbd, many sources refer to the plant’s redundancy and mention its full capacity as 13 mbd, citing Saudi officials. See, e.g., New York Times, “Suicide Bombers Fail to Enter Saudi Oil Plant,” February 25, 2006.
30 SAFE analysis based on data from: U.S. EIA.
31 Robb and Wald, supra.
32 Note: The International Energy Agency defines spare capacity as that which can be brought online within 30 days and maintained for an extended period.
Worst-Case Scenario: Open War
Having long preferred to fight their battle for influence indirectly in theatres like Yemen and Syria, it would be unlikely for either nation to jump directly from the current level of tension to attacking the other’s sovereign territory, particularly as Iran remains scarred by memories of deaths and economic destruction wrought by the Iran-Iraq War of 1980–1988. Yet, with tensions having steadily risen due to factors like the Yemen conflict, Saudi fears about Arab Spring–like uprisings being exploited by Iran, and Saudi worries that the nuclear deal could free Iran to instigate operations against Riyadh and its allies, an escalation into direct conflict cannot be ruled out. While such a war has always been unlikely, if it were to happen, a chain reaction like the one triggered by the execution of Nimr would almost certainly be necessary to spark it.

If Iran moved to direct attacks against Saudi Arabia, the Kingdom’s largest processing and export terminals on the Persian Gulf would be likely targets for Iranian retaliation. A prime target would be Abqaiq. Iranian missile inaccuracy and robust Saudi missile-defense systems mean that Iran would probably be unable to inflict enough damage to do more than remove excess capacity from the Saudi production and export chain. However, a successful strike on a major Saudi facility—which might require Iran to develop either a significantly larger missile stock or improved missile guidance—could severely reduce global oil supply. For example, an attack that crippled Abqaiq could be only partially compensated for with Saudi spare capacity and global stockpiles. The loss of Abqaiq would cause a loss of 4.5 mbd or higher from the world oil market even if Saudi Arabia rerouted as much oil to other processing facilities as possible, according to a 2011 analysis.33

Any attacks on Saudi or other Gulf Cooperation Council (GCC) terminals or facilities could also prompt reprisal by the targeted countries—or by the United States—against Iranian facilities on the Persian Gulf. The most crucial would be Iran’s terminal at Kharg Island, which was attacked during the Iran–Iraq War. Not only is this facility responsible for as much as 98 percent of Iran’s crude oil exports, but it has recently expanded its storage capacity to 27 million barrels and Iranian officials say it is capable of handing up to 7 mbd in exports.34

The success of Saudi Arabia’s efforts to get its allies to join its diplomatic response against Iran in the wake of the embassy riot is indicative of Riyadh’s strategy to isolate Iran in the region. Similarly, it would no doubt seek involvement of its allies in any war with Iran, much as it developed a regional coalition to support its operations in Yemen. This would likely open up installations in Bahrain, Kuwait, and potentially the U.A.E. and Qatar to retaliation from Iran. Coastal facilities that would be at risk of disruption include the Ruwais and Jebel Dhanna refinery and

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34 Iran Daily, “20% Rise in Kharg crude export capacity,” May 9, 2015.
export terminals in the U.A.E., which process at least 2 mbd of Emirati oil,\textsuperscript{35} the Mina al-Ahmadi, Mina Abdullah, Al Shuaiba, and Mina Saud terminals in Kuwait, with a combined capacity of over 2 mbd\textsuperscript{36}, and Qatari terminals which export just over 1 mbd between crude oil and refined products.\textsuperscript{37} It is also possible that, with sectarian tensions a major factor in any potential war to emerge, the Shia-dominated south of Iraq could be the site of attacks by Sunni extremists. In 2013, a truck bomb attributed to al-Qaeda exploded at one of Basra province’s main ports.\textsuperscript{38} With most of the province’s 3.4 mbd in exports leaving from the massive Al Basrah Oil Terminal, an attack on an oil facility there could be catastrophic for an Iraqi government embattled by ISIS, and affect oil prices globally. Overall, accounting for the potential of a conflict to bring approximately 2.5 mbd of Iranian oil off the global market as well, a worst-case scenario of open regional war could put over 19 mbd at risk. Such a disruption would not only cause prices to skyrocket, but oil scarcity would have further geopolitical implications as nations scrambled to maintain access to suddenly limited energy resources.

In addition to oil, a conflict could drastically impact other energy markets. Most notably affected would be natural gas, with Qatar the world leader in liquefied natural gas (LNG) exports. If its facilities, particularly the Ras Laffan complex, were to be targeted, one-third of global LNG trade could come offline.\textsuperscript{39} This would be particularly problematic for U.S. allies in Asia, as Japan and South Korea are Qatar’s two largest LNG customers.\textsuperscript{40}

Impact on U.S. National Security

While the United States remains a strong ally of Saudi Arabia in part due to the crucial role the Kingdom plays as the world’s pivotal oil supplier, its foreign policy options have remained deeply constrained. The U.S. military has given logistical support to Riyadh for its operations in Yemen—all the while aware that the extensive nature of the campaign poses risks of unleashing further regional chaos and emboldening terrorist groups with deeply anti-American sentiments—and pressured the Saudi government to cease the bombing campaign.\textsuperscript{41} The heightened tensions in the region now may serve to make some wary of Riyadh’s strategy, but the importance Saudi Arabia’s oil means little is likely to change in terms of U.S. military support for the country.

The sparking of a more open conflict in the region would necessitate U.S. involvement, regardless of American military priorities elsewhere. The United States has repeatedly sought to assuage Saudi concerns that Iran will expand its regional power in the aftermath of the removal of nuclear sanctions, culminating with a very public expression of support for Riyadh against Iran during King Salman’s visit to Washington last September.\textsuperscript{42} The United States would thus be unlikely to avoid committing significant military assistance to Riyadh in a conflict.

These constraints are increased by connections to Saudi allies in the region, who have also expressed concern about the nuclear deal with Iran and sought assurances from Washington. Bahrain, perhaps the most vivid face of Sunni states cracking down on Shia opposition and deeply suspicious of Iran, is also a

\begin{itemize}
\item \textsuperscript{37} U.S. EIA, “Qatar,” October 20, 2015.
\item \textsuperscript{38} Al-Monitor, “After Bombing, Basra Governor Sees ‘Political’ Price to Pay,” August 19, 2013.
\item \textsuperscript{40} BP plc, “Statistical Review of World Energy,” 2015 Edition.
\item \textsuperscript{41} Washington Times, “U.S. pressures Saudi Arabia to stop bombing Iran-backed rebels in Yemen,” April 30, 2015.
\item \textsuperscript{42} See, e.g., USA Today, “Obama reassures Saudi Arabia over Iran,” September 4, 2015.
\end{itemize}
crucial U.S. ally in the Persian Gulf. The U.S. has maintained a military presence on the island since World War II, and currently has more than 8,000 troops based there, a number that has increased in recent years both to bolster naval patrols and security operations in the Persian Gulf. The U.S. Navy’s Fifth Fleet is also headquartered there, but naval officials have been quick to downplay notions that the escalating crisis will impact U.S. operations in Bahrain.

Kuwait also remains firmly and vocally suspicious of Iran’s regional intentions. Not only did it recall its ambassador from Tehran in the aftermath of the embassy riot, but the following week it sentenced two men to death and gave lengthy prison sentences to 20 more for spying for Iran. Kuwait has long cultivated deep military ties with the United States, currently serving as an eager host for 15,000 American troops.

In addition, thousands of U.S. troops are stationed in other Gulf Cooperation Council (GCC) nations, such as the U.A.E. and Qatar, the latter of which houses the regional headquarters of U.S. Central Command. First and foremost, the high U.S. military presence in the countries along the Persian Gulf is in part a consequence of the importance the nation places on the secure flow of international oil trade. But, as the escalating crisis shows, that presence—while providing a level of deterrence—in turn raises the potential military risks to the United States from increased tensions in the Saudi–Iran rivalry.

Further, an intensified conflict has the side effect of complicating efforts to cultivate a more robust regional response against ISIS, which could have security implications for U.S. interests worldwide. A war involving Iran and the GCC states which host U.S. troops would severely hamper the ability of the U.S. military to counter ISIS, a group which has already inspired a major terrorist act on American soil in the form of the San Bernardino shootings of last December. A conflict would tie up U.S. military resources in the region, distracting them from the fight against ISIS, and hamper the U.S. effort to coordinate attacks against ISIS by regional allies, who would find a war with Iran a far higher priority.

Conclusion

Iran and Saudi Arabia, and the entire Middle East region, are important sources of supply to the global oil market. Rising tensions between the regions two most powerful nations is a major concern for the global economy given the key role oil has in transportation and places the United States in a position where it may need to extend its military and diplomatic resources to intervene. If rising tensions ever become a long-term regional war, oil prices will very likely experience higher volatility and higher risk premiums. And due to America’s continued dependence on oil in its transportation sector, U.S. consumers and companies will pay the price. Until steps are taken to diversify fuel use, America will remain constrained in its foreign policy and its military options and consumers will remain hostage to conflicts and tensions in the Middle East and throughout the world.

Contributors

Mehrun Etebari, Policy Lead, Geopolitics
Jeff Gerlach, Policy Analyst
Paul Ruiz, Policy Associate

For media inquiries, please contact Ellen Carey, ecarey@secureenergy.org and (202) 461-2382.

46 Heritage Foundation, “2015 Index of U.S. Military Strength.”