VOLUME 3, ISSUE 5 MAY 2015

Energy International Risk Assessment

An Independent Monthly Review

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Letter From The Editor

This month our Energy International Risk Assessment (EIRA) newsletter celebrates its second anniversary and looks into the future with even stronger conviction towards the targets of truth and independence it has set to achieve.

We thank our international readership for their dedication and trust. We also thank, yet again, our good friends, the members of our international network of highly specialised experts that make the production of EIRA possible.

We kindly remind you that besides the EIRA newsletter, which is disseminated electronically every month, you are welcome to visit our website EIRANEWS.COM for more information on energy developments.

Yours Sincerely,

George Hatziioannou
Editor

Greece: Tsipras Plays Russian Card To Pressure EU

High expectations ahead of the talks held by Greek PM Alexis Tsipras in Moscow were frustrated by the modest outcome. The visit had not produced concrete and tangible gains, although Financial Times and some other European media outlets did not rule out that a deal was struck behind the scenes.

In any case, the visit was marked by intense speculations on whether Greece while seeking closer ties with Moscow was breaking Europe's energy unity. More fodder for rumours emerged after Gazprom's CEO Alexei Miller's met with PM Tsipras and Energy Minister Lafazanis in Athens in late April. Yet, once again the end-result appeared as vague as the outcome of the previous talks in Moscow. In particular, nothing meaningful was announced on the delicate issue of the onshore leg of the Turkish Stream across Greece and further on.

As a soothing prize for both sides came the statement by Energy Minister Lafazanis that an agreement, including the sensitive issue of lowering prices for Gazprom's gas, would be signed in the foreseeable future. In a clear hint that Greece expects a *quid pro quo* deal, and smoothing the road to a compromise, Mr Lafazanis reiterated that the "Greek Stream Pipeline is a priority for Greece".

At least on the surface, Athens seems to accept the business rationale behind the construction of the Greek Stream, as an extension of Turkish Stream. Once in place, it would eradicate current transit risks linked to the aging Ukrainian pipeline system (although Turkey as a substitute transit country may prove to be not a godsend). What is more certain, is that Greece by joining the "band wagon" would see direct foreign investments, emergence of new jobs, and eventually a guaranteed flow of revenues in the form of transit fees.

Would Greece watch Russia re-invigorate its appetite for acquisitions abroad too? It could be the case, but probably at a later stage. The Greek media outlet *Capital* pointed out that, according to its sources, "for the time being, Gazprom's strategy is not focusing on purchasing further assets in Europe."

The intricate issue has been the level of discounts for imported gas. Greece is seeking to reduce it energy bills to alleviate the overall burden on its economy. Sources in the industry are skeptical of any breakthrough since the last price revision of Gazprom's gas supplies took place in 2014 (standard long-term contract stipulates such corrections only once in three years).

For the Greeks it looks disappointing although some consolation can be found in the assurances by Mr Miller that Gazprom realizes the true value of cooperation with European countries eager to join the mega-project and would be forthcoming in negotiating the terms and conditions of their involvement on the ground.

In theory, an international consortium of Russian and European companies could build the pipeline's extension in Greece, capitalizing on the proven model applied by the South Stream's conglomerate of trans-European energy majors.

Once again, the chances of Greek Stream coming on stream are not a given since the veto power of the European Commission should not be underestimated. However, Gazprom's chief specifically noted that the project, read — the Greek segment, would be implemented in full conformity with the EU regulations.

So far, the reaction from Brussels was kept along the lines of "wait and see" attitude. The European Commission's spokesperson Anna Kaisa Itkonen stated that it is too early to pass any judgment. "Before we can draw conclusions on how the Third Energy Package or any other EU legislation should be implemented, we have to see the route and the role of all participating countries will play in the project", she said. However, Ms Itkonen admitted that their services are "analyzing the impact of such plans regarding regulatory and financial feasibility." This can be interpreted as promising answer "maybe" but not as a categorical "no".

That said, the diplomatic shuttle activities between Athens and Moscow brought about a barrage of warning shots from politicians in support of the war of sanctions on Russia. They clearly blamed Greek PM of breaking the ranks quoting the dissident views of Alexis Tsipras on the sanctions and, in the wider context, on the intent to reform the EU anti-crisis strategy to make it work, finally.

Political overtones were heard loud and clear in many comments over Mr Tsipras' attempt to diversify his foreign policy leanings and find lucrative deals to enliven the debt-laden Greek economy. In the European Parliament, Liberal MEP Guy Verhofstadt commented on Twitter: "The Greek Prime Minister should stop trying to play Putin against the EU. Putin cannot save Greece, the EU can."

The last argument is not very convincing for the Greeks. In the last five years, following the EU recipes of fighting the entrenched debt crisis have brought nothing but havoc to the economy and additional sufferings for the people.

Yet, the absence of any *concordat* signed and sealed between Greece and Russia as a result of Tsipras' visit to Moscow does not support assumptions that Greece is eager and will eventually become Russia's "Trojan horse" within the European Union. Moscow, to put it on the record, vehemently denies such allegations.

What is more likely, the young and charismatic maverick of the thoroughly frustrated Greece is playing the Russian card to put pressure on the EU. In order to squeeze out the vitally important concessions Alexis Tsipras, negotiating from a position of weakness, would be foolish not to tease and irritate the big bosses of the "Troika" by showing he has got an alternative to turn to, despite the fact that his visit to Moscow has not yielded any result. At least, any visible result.

American LNG For Europe: Panacea Or Delusion

Back in March 2014, gas market analyst Thierry Bros, author of 'After the US shale gas revolution', professed that American liquefied natural gas (LNG) will not be reaching Europe until 2015 or 2016. One year down the road, it looks like a self-fulfilling prophecy with plenty of symptoms that the US is on the right track and is zeroing in on its ambitious strategy to become world's largest gas exporter.

Natural gas production in the US remains an indisputable success story. In 2014, the volumes went up 12.7% over the average indicators of growth in the interval of 2010-2013. In December 2014, the shale gas share in the overall production reached 52.5%, which is 4.9 points above the statistics for December 2013.

The upward trend is by all means guaranteed with consensus forecast (based on estimations by CEDIGAZ, EIA, IEA, EVA, HIS, ICF, BP, etc.) predicting the US gas production will reach 920 bcma by 2025, and 1029 bcma by 2035.

For the time being, the United States Department of Energy has issued licenses for the construction of 9 LNG terminals with a capacity of 119 bcm. Given the long queue of other aspiring LNG exporters, the total US export potential could reach 376 bcma by 2018.

However, industry exports assume that the actual export of American LNG will not exceed 68 bcma by 2025, and would go up to 107 bcma only by 2035 (and that is twenty years from now).

Actually, the volumes of US LNG pale in comparison, for instance, with China's gas consumption which is expected to reach 400 bcm in 2020, and with its import dependence exceeding 40%, meaning the most dynamic global economy will be in need of annual supplies of 160 bcm of imported gas. It opens a window of opportunity for US LNG producers who will almost certainly view China as a lucrative market with an impressive growth potential.

Despite the somewhat vague prospects of American LNG becoming a game-changer on the European energy market, one thing seems to be certain: the arrival of US LNG would give importers in Europe some more bargaining

power with existing suppliers, since it might exert pressure on the prices. This would be indeed helpful. But only if significant volumes of US LNG make it to Europe and, even more importantly, if the price is right. The latter cannot be ascertained.

First of all, there is a natural prerequisite: European and Asian prices for LNG must converge or the spread must narrow. Current trend supports this aspiration although it could still be reversed. Asia and Pacific, according to all forecasts, will be responsible for 50% of gas consumption growth in the next decades. The region would be ready to absorb additional volumes of imported gas, which will drive prices up conserving the present status of the region as a premium energy market.

Take the case of GDF Suez, which acquired export rights at Sempra Energy's Cameron LNG plant in Louisiana in 2013. The French energy major struck deals to sell all of its 4 million tonnes per year of capacity to buyers in Japan, Taiwan, China and Chile. The key detail of this news is that GDF Suez had earmarked "all of its 4 million tonnes per year" for customers in Asia and Latin America while Europe is conspicuously missing from the list.

It has been estimated by industry experts that in the short term, until the end of 2015, the Asian markets will offer a premium of around 1.78 USD/Mbtu, thus attracting most of the uncontracted LNG.

The classical example of an awkward miscalculation is the case of the LNG-terminal to be finalized in Poland which had already signed a contract with Qatar. Last year, it came as a revelation that Qatari LNG will be at least 30% more expensive than Russian pipeline gas.

As for the end price of US LNG for Europe, it will naturally incorporate the whole chain of costs, stretching from production at well head to delivery to liquefaction plant, freight and insurance, regasification and shipment to the end buyer (e.g. wholesale buyer/ distribution company/consumer). The current calculations, circulating within the energy experts' community, claim that should the price of US LNG exceed the European hub price by 3.0 USD/Mbtu, the whole concept of the delivering American gas across the Atlantic for profit goes bust.

Then again, it has not been the best kept secret that American shale gas companies are not making acceptable rates of return. The prices on the domestic market, determined at Henry Hub, are below replacement costs. Companies survive because they are extracting gas as a by-product of petroleum liquids in the same wells, and until recently they subsidized their operations by selling crude which was far more expensive. The recent oil price crunch has put pressure on marginal shale gas producers and could well spell doom for some of them.

To sum up, Europe could profit immensely from US LNG imports, although it could hardly be a panacea, but only under at least two conditions. First, there should be physically enough volumes to be shipped across the Atlantic. And, second, European buyers must be ready to pay the same high prices as Asian and Pacific customers. By saying "Pacific", it is Latin America which is kept in mind where the emerging new economies show a growing appetite for energy.

If the two conditions are not met, LNG "Made in the USA" would be hi-jacked by the highest bidders who happen to live and operate in Asia. Poor Europe would be left on the sidelines of this money-spinning trade, and, probably, left in the cold.

Would Craiova Group Become A Godsend For The Balkans?

A new regional union is being created in Eastern Europe, in the Balkans, to be more precise. Bulgaria, Romania and Serbia declared their desire to form a new unofficial group able to push their regional interests through different international bodies, primarily the EU. They were inspired by the success of the Visegrad Group formed by Poland, Czech Republic, Slovakia and Hungary.

Prime Ministers of the three Balkan States met in Craiova (Romania) and proposed to call their informal union Craiova Group.

Victor Ponta of Romania said that he would like "to lay the foundations of cooperation between Bulgaria, Romania and Serbia in Craiova and to welcome 'the Craiova Group'. We are not joining hands against anyone; we are uniting to promote the shared interests of our countries." The Craiova Group could be just like the Visegrad Group: three countries deliberating, sharing positions, having joint projects and supporting each other".

He added that the Group would be open to other States of that region.

The agenda was focused mainly on economic issues although they paid attention to some political issues. Bulgaria and Romania being EU member states voiced their full support to Serbian entry into the EU in the making. The two countries also expressed their wish to join efforts in gaining access to the Schengen free visa zone. So far they were denied this privilege.

On the practical side, the three leaders concentrated on infrastructure projects, linked both to transport and energy. They were anticipating the construction of regional motorways and high speed railways, and of new gas pipelines.

Boiko Borisov of Bulgaria pointed out the need to join efforts to finance major infrastructure projects, expressing hope that other neighbors would be interested in the participation in such projects.

Most emphasis was put on new gas infrastructure in the Balkans. There are some major elements which are aggravating the local market situation.

First, the gas market is not huge due to the fact that Balkan countries are poor and cannot afford paying for gas, even if offered at a relatively low price. To create an attractive market for gas, the Balkan nations would be wise to find other sources of revenues with a steady cash-flow.

Second, the cancellation in December 2014 of South Stream pipeline project, supported by Russian Gazprom and some European and national energy companies but opposed by the European Commission and the US, has resulted in a vacuum in gas delivery routes' security. Up to now, the bulk of natural gas was coming to the Balkans from Russia through Ukraine, but that traditional route seems to be not secure any longer due to still rising regional tension with an unpredictable outcome.

Third, the European Commission is looking for alternative sources for gas and interconnectors capable of bringing natural gas to the Balkans by alternative routes. The problem is that pipeline gas from Northern Europe will be too expensive to be consumed here and other than Russian sources are physically insufficient to cover the demand. Additional Azeri gas will serve only to feed the TAP pipeline and locally produced gas is nothing but "small beer". The only realistic alternative to Russian gas could be gas from Iran once it has been relieved from the sanctions' grip. But that gas would come on-stream in sufficient volumes after several decades of consistent investments into Iranian gas production and transportation system. Besides, the price should be right for South-East Europe and the EU in general. On top of these uncertainties, it is no secret that Iran is a tough negotiator and less secure than Russia. Currently, for instance, Turkey is importing gas from Russia, Azerbaijan and Iran, and the Iranian gas is the most expensive.

Fourth, Gazprom now is pursuing a different market strategy and wants to bring its gas for the Balkans at the Turkish-Greek border, pumping it through the proposed Turkish Stream pipeline. From that entry point this gas has to be delivered to the consumers, in Italy, Central Europe and the Balkans, thus replacing the existing Ukrainian route of delivery. The Russian monopoly is not allowed by the EU Third energy package (TEP) to produce and sell gas while being the owner of the pipelines. Subsequently, transportation network on the EU territory, primarily, the pipelines should be built by European market players. As result, now the industry, with some political support within

certain EU member states, is looking for ways to be connected to the Turkish Stream.

Greece is pretty active in this respect and is discussing with Russia how to build a pipeline with a capacity of roughly 47 bcm of gas. That amount will transit through Greece but where would it go from there?

Considering only the projects which already have been put on the table, even theoretically, we may find at least 4 options:

- A second line of TAP pipeline, bound to Southern Italy. Than line would not be exempted from Third Party Access rules and will be obliged to transport other than gas from Azerbaijan, which is now the primary resource base for TAP, gas from other producers. Actually, the easily available in sufficient volumes gas to feed that second line could be only of Gazprom's origin but this "marriage" of Azeri and Russian gas will be conditional on a political decision at the highest level to be taken in Brussels;

- A viable and already being discussed possibility of a pipeline going through FYROM, Serbia, Hungary and up to Austria, approximately following the route of the on-shore part of the defunct South Stream;

- An EU sponsored project of a Vertical gas corridor linking Romania, Bulgaria and Greece or, in a reverse mode, the existing Transbalkan pipeline delivering now Russian gas from the Ukrainian border to Romania, Bulgaria, Turkey and Greece;

- These networks could be connected to a Slovak pipeline project, called Eastring with its end point in Slovakia. From this country gas coming up from the European South-East can be dispatched to any destination due to a well developed gas transportation system in that part of Europe.

It's not guaranteed that any of these projects would be implemented; some concepts could merge, or fail.

The Craiova Group was in agreement that the Vertical gas corridor was a good idea. They gave it full support but avoided debates on how to fill the pipe with alternative gas other than Russian. Without defining a secure source of gas, the planned pipeline will remain empty or might copy paste the fate of the collapsed Nabucco/ Nabucco West projects.

From that perspective, within the Craiova Group configuration the most interesting is the position of Bulgaria which suffered the most from South Stream cancellation, having lost overnight the ascertained foreign investments, new jobs and transit fees.

So far, Bulgaria is note for being a vociferous critic of the Turkish Stream project and its supporters; it endorses the TEP rules and proposes to create a hub in Varna with gas of unidentified origin to be traded there. At the same time, the government in Sofia is skeptical about Gazprom's promise to abandon the Ukrainian transit route but is careful not to alienate Russia any further. Bulgaria is still issuing permissions for the cancelled South Stream, calls for the lifting of the EU sanctions against Russia and keeps a low profile on the antitrust case of the Commission against Gazprom. It's rather obvious: Sofia doesn't have any alternative to South Stream and is the big loser in that game.

FYROM: To Turkish Stream Or Not To?

Political life in Skopje may appear somehow bizarre for an external observer these months. Illegal phone calls interceptions, accusations of violation of press freedom, rumors of plots and coups' preparation.

At the very end of April 2015, a new and potentially risky factor was added to the local political landscape. Armed gunmen coming from Kosovo attacked a border line police post. The 40 militiamen were identified as servicemen of the Kosovo Liberation Army (KLA, or Ushtria Çlirimtare e Kosovës - UÇK), an ethnic-Albanian paramilitary organization which fought for the separation of Kosovo from Serbia in

1998-1999. The gunmen seized 4 police guards and later released then, yet promising to establish on that soil an "Albanian state".

The revival of Albanian nationalism is politically very dangerous for the fragile FYROM State, where 25-30% of the 2 million populations are ethnic Albanian. In 2001, the country was in convulsions due to an Albanian uprising, the insurgents were demanding more rights and freedoms. The conflict was settled by the Ohrid accord giving local Albanians more political and civil rights and a wider representation on all levels of government.

Albanians are Muslim while the majority of the population is Slavic and Orthodox Christians. Albanians have the reputation of relying on the US support.

The Governmental coalition was formed be a Slavic party (VMRO-DPMNE, which was nationalistic and pro-NATO) and of the Democratic Party of Albanians (DPA); the last has quit in March 2015 creating political turmoil and instability. DPA was demanding additional rights for the Albanians in the country and for an official recognition of Kosovo.

The Prime Minister, Nicola Gruevski, doesn't have support of MPs from other minority parties and may rely only on a relative majority in the Parliament.

Meanwhile, the opposition continues attacks on the Government, claiming that the border incident was a provocation intended to detour the attention from the ongoing political debate. The opposition is accusing the Government of oppressive control over the media and the judicial system of corruption, while the authorities allege that the opposition is preparing a coup d'etat.

The EU Foreign Ministers called on the political opponents in Skopje to behave in a responsible way and to restart a political dialogue in order to find a durable solution for the crisis.

In that context, a supposed former US agent, Wayne Madsen, appeared on a local TV channel and revealed that the US administration was masterminding a "color revolution", in other words, a regime change, counting on Albanian nationalists as the main strike force. One local expert concluded that the undeclared goal was to create instability in FYROM and the wider region in order to derail two major infrastructure projects: a China-sponsored railway from Athens to Budapest and a gas pipeline starting from Gazprom's Turkish Stream and passing from Greece and FYROM and bound to Serbia, Hungary and Austria.

Europe Vie With Pakistan For Iranian Gas

The slightly nervous anticipation of Western sanctions against Iran being lifted (probably after the final deal on its nuclear program is signed and sealed on 30 June) has led to an exemplary race to be first past the pole. The prize sough is the huge, still mostly theoretical, natural gas export potential of Iran.

How really big could be the volumes of Iranian gas to be earmarked for foreign markets, remains a billion dollar or rather a billion euro or renminbi question. What is more certain is that the heir to the Persian Empire sits on vast and, more importantly, proven reserves of around 34 trillion cubic meters.

Large figures impress but ply if taken out of the context. Iran must be put on the record as an advanced pro-gas and thoroughly gasified nation. The share of natural gas in the energy mix is 65%, and the urban areas can boast of 95% gasification level. Iran has one of the largest car fleet running mostly on CNG (3.5 million) with 2200 filling stations across the country. Since 2000, national gas consumption was rising by 12% per year, and the total volume went up 2.5 times.

All in all, it translates into an ample and deep domestic market. Statistics for the last year, in accordance with the Iranian calendar year which ended on 20th March, show that Iran consumed a total of 173.8 billion cubic meters (bcm) of natural gas. Despite delivering gas to Turkey (10 bcma), Iran remains a netto-importer.

To join the ranks of stable and reliable purveyors of natural gas to the global market, Iran will have to address the pressing issues of lack of relevant infrastructure and export services, as well as the need to upgrade the existing and partially crumbling production and transportation facilities.

It would take immense inwards investments to gear up domestic production. There are two factors aggravating this uphill battle: firstly, Western sanctions have deprived Iranian oil and gas industry of loans and credits; secondly, while 35.05% of gas deposits are located onshore, the bulwark, and that is 64.95%, is offshore which requires a lot of finances, both initial and as current assets, and also sophisticated equipment for exploration and subsequent production.

The tomorrow's extra gas volumes are needed already today to cover the burgeoning appetite of the Iranian industry and households. Whatever is left after domestic clients are comfortable with the supply side, would be allocated to the export portfolio. Apart for money, this task would demand time.

Basically, these objective hurdles will inevitable postpone the emergence of Iran as a strong player on the gas market. Nevertheless, the undeclared competition for luring Tehran into contractual obligations has begun with Europe and, in particular, Pakistan finding themselves pitted against each other.

In April, China National Petroleum Corporation, CNPC, has committed itself to build 700km pipeline to connect Iran and Pakistan, reanimating the long-stalled project of linking the two neighboring countries with a turbulent history of uneasy relations into an energy alliance.

Pakistan has been in the grips of a chronic energy deficit for too long, and the situation worsened from year to year becoming almost the ultimate curse. The concept of bringing in Iranian gas was negotiated and agreed upon by both sides but then effectively frozen due to pressure on Pakistan coming from the United States and Saudi Arabia. Yet, the prospect of the abandonment of sanctions which would make doing business with Iran legal, spurred plenty of behind the doors diplomatic activities. It has been reported that Islamabad persuaded China to get fully involved and help to kick off the construction of the Pakistani section.

It comes in the wake of Tehran's completion of its 900-kilometer part of the pipeline from an Iranian gas fields. Now that CNPC, with full backing of the political leadership of China has embarked on the venture, there is likelihood that the project would be brought to fruition. The Chinese loan will cover 85% of the financing, the rest falls on the Pakistani government. The estimated price tag would $1.5 billion to $1.8 billion for the pipeline, or $2 billion provided the parties agree on the construction of an optional Liquefied Natural Gas terminal at Gwadar.

All parties to the agreement are expected to be the winners. In two years time, Pakistan, definitely tired of the monotonous fuel shortages for its power-generation plants, could rely of the supply of Iranian gas enough to produce 4,500 megawatts of electricity which is compatible with the current electricity shortfall. China will benefit from laying bricks into its new project of an "economic corridor" which would link the Pakistani port of Gwadar (administered by Chinese managers) to southwestern China with road and rail connections.

Now, what about Iran? It will secure a customer for its export gas. The demand for gas of the 180-million nation cannot be underestimated, so it is long-term linkage and source of revenues (despite doubts of whether Pakistan will always be in position to be a payable client). Anyway, so far it is not a game-changing contract: the deal signed in 2014 stipulated the delivery of only 8 bcma of Iranian gas.

The political dividend reaped by Tehran cannot be discounted. The deal distances Pakistan from the USA which insisted that Islamabad instead of Iranian gas should buy Qatari LNG. The price is the stumbling block: Qatar was used, until recently, to selling its LNG at Far East premium markets at a price of 19-20 USD/Mbtu while Pakistan cannot afford to pay more

than 13-15 USD/Mbtu.

In February 2014, Saudi Arabia provided financial aid to Pakistan to the tune of USD 1.5bln. The Finance Minister in Islamabad called it a "gift". Local experts interpreted this gesture of good will on the part of the House of Saud as an attempt to further block the implementation of the Iran-Pakistan gas pipeline project.

Once again, politics interfered into the business domain. The same is applicable to the policy of the European Commission to diversify gas suppliers to reduce what it calls "dependence" on Gazprom's pipeline gas. Brussels wants to enable Iran to become an alternative gas supplier via Turkey.

One of the options is to pump Iranian gas into the "Southern Corridor" network, namely into TANAP running across the Turkish territory and then into TAP pipelines going through Greece and Albania and then heading towards Southern Italy. Rovnag Abdullayev, Azeri state energy company SOCAR's president, specifically emphasized that "If Iran has gas in the future, it won't have other option but to use TANAP pipeline to supply its gas to other markets."

This is possible, at least in theory, but in practice Iran will weigh carefully all the options before making firm commitments. Some European energy experts have concluded recently that "before considering Europe as a lucrative option, Iran is likely to first look at the Iraqi, Pakistani, Indian or even Chinese markets where demand is growing and prices are higher."

It sets Europe and Asia on a collision course in their understandable interest in getting a share in the untapping the hydrocarbon reserves of Iran first. The race has begun, and now Tehran can play a choosy and capricious bride yet undecided.

Saudi King Salman And His Silent Revolution At The Top

Exacerbated chaos in the Middle East has pushed Saudi Arabia, the local Sunnite superpower, to adapt to the creeping evolution, which is threatening the stability of the Kingdom's dynasty.

The move corresponded to the access to Saudi throne (23 January, 2015) of a new monarch, King Salman, 79.

From the Saudi perception, they are facing number of internal and external challenges. The challenges are as follows:

- Iran's "expansionism", Tehran is using fellow Shiite population in order to establish friendly regimes in some countries with ethnic Arabs as a dominant group;
- A shift in the US attitude toward Iran against on-going talks to find a solution over the Iranian nuclear program which may result in the reintegration of Iran into the international community;
- Rise of radical Islamist movements (al-Qaeda, Muslim Brotherhood, Islamic State) which could be instrumental in the removal of the House of Saud from power and could even bring about the fragmentation of the Kingdom;
- Rivalry between different branches of the Royal dynasty made up of some 7,000 members against the background of the heating up social unrest.

Only 2 months after becoming the Custodian of the Two Holy Mosques King Salman disclosed the new policy course he intends to pursue. The King launched a military campaign against Houthi insurgency in neighboring Yemen, limited far the time being to airstrikes. His Government has put together a Sunnite coalition against the insurgents perceived in Riyadh as Iranian proxy, luring into the coalition, at least formally, non-Arab countries, like Pakistan and even Turkey. To some extent, the standoff with Iran was presented, although not in this wording, as a Sunnite-Shiite battle royal for the supremacy in the region.

It's not clear to what extent Iran renders its

support to the Houthis and what the degree of Iranian influence on the rebels is.

The Houthis are called after the name of their founder, Hussein Badreddine al-Houthi, killed by the army in 2004. It is a tribe from the mountains in North-West of Yemen; they are Zaidi, a dissident branch of Shiism. In September 2014, they have seized the capital city, Sanaa, ousted the President, Abed Rabbo Mansour Hadi, who found refuge in Aden, the strategic port in the south of the country but later, attacked by Houthis, fled the country and is now residing in Riyadh.

Saudi Arabia declared that the goal of its military campaign was to reinstall Mr. Hadi as President and affirmed that Houthis were Iranian proxies threatening the regional stability (see Yemen. A Dangerous Proxy War, EIRA, Volume 3, Issue 4 April 2015).

The Saudis failed miserably, so far. On the battlefield they were not able to stop Houthis who would not retreat although the Saudi claimed to have destroyed heavy weaponry of the insurgents, including ballistic missiles, and inflicted heavy losses. But they failed to rally and send out ground forces from Egypt and especially from Pakistan, perceived as crucial to the success of the operations in Yemen. Saudis are now at a crossroad.

If they do not achieve their military goals in Yemen and do not defeat the Houthis (they seem to be unable to do it alone), they will be perceived as weak despite Saudi military spending which are 8 time bigger than, for example, those of Iran.

If Saudi Arabia goes on with the bombardments, there will be growing international criticism for heavy consequences from the humanitarian point of view. By the way, President Hadi is losing support even among the anti-Houthis fighters, even in Aden, as result of the destructions from Saudi air strikes bringing a humanitarian crisis.

Independent analysts are skeptical about the success of the Saudi bombing exercises.

The air campaign in Yemen, which was decided and designed apparently by Saudi Arabia alone, has put its US ally in a delicate position. Washington is negotiating with Iran a deal on curtailing its nuclear program; it also needs Iranian support in the fight against the Islamic State in Iraq and Syria. Americans wanted to maintain a balance in the region while simultaneously securing the loyalty of Saudi Arabia and other Gulf petro monarchies and normalizing relations with their adversary, Iran. The US provided logistics and some other support to Saudi Arabia in its incursion into Yemen, but insisted the Saudis should limit its operations because the Americans believed the Saudis had overreacted over a perceived Iranian threat in Yemen. Anyway, the main US interest in Yemen was to fight the local and powerful branch of al-Qaeda, known as Al-Qaeda in the Arabian Peninsula (AQAP). That American war was sidelined in the ongoing internal conflict in Yemen and especially against the Saudi intervention.

It should not be neglected an internal, for Saudi Arabia, aspect of the operations in Yemen. The bombings ignited a patriotic, nationalistic spirit. The majority supported that Government action with only the Shiite part of the population (10%) and some rare intellectuals mutely voicing their dissent. The campaign was also supported by a rather unusual Western-style communications campaign by the military, which was organized with the assistance of a Dubai-based PR firm. Some insiders in Riyadh pretend that one of the goals of the whole operation was to promote the new Minister of Defense, Mohammed bin Selman, and to make him an anti-Shiite national hero. It was a success.

In that context Saudi Arabia preferred to stop the military operation after 3 weeks arguing that the military goals were achieved. The Saudis announced passing to the next stage: without ceasing the bombing routine to reduce its scope and to start working on a political settlement of the crisis.

All involved parties claimed victory. In fact, Saudis didn't even come close to achieving their main goal that is to bring the President Hade back to power. On top of it, they do not seem to

have an exit strategy for the conflict. They avoided a total nightmare which would break out should they have started a ground operation, but they had produced a power vacuum in their neighboring country with tribal, religious, clan-based and other local factors destabilizing and even *somalizing* the weak country. Instability at their southern borders is a serious threat for Saudi Arabia, and it is plausible that Iran could have wished for such an end result sparring with its Sunnite arch-rival.

On the other front, Riyadh acted to consolidate the broken ideological and political unity of the Gulf States and of the Sunnite Arab world. The instrument of that rallying was the emphatic denunciation of the Iranian threat, with Iran vilified having allegedly had the upper hand in the regional rivalry. For Saudi Arabia it amounts to a remarkable reconciliation with some opponents, Qatar in the first place, despite dogmatic differences between the branches of the Sunni Islamism. That standoff has brought not only tensions between those countries but also clash of interests in third countries, including Egypt and embattled Libya and Syria.

There are signs that a kind of common ground was found, at least in Syria. Some Islamist groups fighting President Basher al-Assad regime and also clashing with each other (they are sponsored by opposed to each other Gulf monarchies) have apparently entered into some kind of cooperation agreements, encompassing Turkey as well. As a result, they immediately registered success on the ground, including decisive victories in the strategic Adlib region.

Some sources report on a possibility to fix the deep controversy between Saudi and Qatari around the Muslim Brotherhood movement, especially in Egypt. Riyadh sees that particular branch of political Islamism as a threat to the Royal dynasty and the established order in the country. Doha (and Ankara!) regards the "brothers" as instrumental in reorganizing the MENA region in a more efficient way. However, this is not ensured: Brotherhood proved not to be able to rule once installed in power. The Muslim Brothers lost in the military standoff (Libya), were the perfect losers in Egypt and lost the elections in Tunisia.

It's possible that that development has brought comfort to Saudi Arabia. There are rumors of a possible settlement through Turkish mediation. The ousted Egyptian president, Mohammed Morse of the Brotherhood, could be released from jail in exchange for the consent of Cairo to send army units to fight Islamists in Libya.

The message is the following. That new policy line should be not only limited to Yemen but be expanded to cover the whole region and to engage all the challengers, be it Iran, IS or any other. In case of success, similar operations could follow, and some indications that this forecast could be correct we find in Syria. An influential Saudi columnist with supposed connections with the Royal family, Jamal Kasogi, has called that approach 'Selman's Doctrine', by the name of the King.

The risk of new Saudi military operations made nervous Iraq. Riyadh keeps its commitment to participate in the bombings of IS' positions in this country which is good news for Baghdad. At the same time, Saudi Arabia is suspicious about the role of Iran in the fight against IS, which may facilitate further rapprochement between Iran and Iraq.

The new and more dynamic approach to foreign policy issues compared to the traditional Saudi politics required also new men at the top. At the very end of April, King Salman made some important and not only symbolic changes in the ruling team. New people were brought forward to fill in the positions of number 2 and 3 of the Kingdom thus installing a new order in the line of succession. King Salman pushed aside the crown prince, his youngest half brother, Prince Muqrin bin Abdulaziz, 69. Officially, it was on his request due to bad health. But rumor has it that crown prince was not quite acceptable as a possible future King because of his origin: his mother was supposed to be a slave of Yemeni origin. Anyway, King Salman set a precedent: the choice of his predecessor, the late King Abdallah, was not respected.

Instead he propelled to the position of crown prince, who is the first in line of succession, his own nephew, the Interior Minister, Prince Mohammed bin Nayef, 55, known also as MBN. He's the author of the anti-al-Qaeda strategy,

which is not surprising since the terrorists unsuccessfully attempted to kill him back in 2009. Apparently, MBN will be the next King.

The deputy crown prince is the favorite sun of King Salman, Prince Mohammed bin Salman, or MBS. His exact age is not known for sure, he's believed to be in his 30s. Now he's occupying the position of Defense Minister and is said to be the head of the military campaign in Yemen and, in a broader way, the brains behind the projection of Saudi military might across the region to oppose and neutralize the Iranian challenge. If events evolve in next decades following that scenario, MBS would succeed to MBN who doesn't have direct male descendants.

MBN and MBS are known to have excellent relations with the US.

Both of them, as King Salman, are coming from the most powerful branch of the Royal family, the Sudairi clan. They are the posterity of Hassa bint Ahmed al-Sudairi, the favorite wife of the founder of the Kingdom, the King Abdel Aziz; she gave birth to 7 of his 35 sons. They Sudairi clan was ruling the country for decades, under the King Fahd, but under the King Abdallah they have lost their sublime status. Now they are back to the top, the three most powerful rulers of the Kingdom come from this clan.

The change of guard is a strong message to the country; the time has come to break the entrenched system of succession. The King's title for the first time will not be passed from one brother to another but will go to another generation of the House of Saud. Until now, only sons of the founder of the Kingdom (established in 1932) were occupying the throne since the death of their father in 1952. This custom led to an evident problem for the monarchy: ageing, poor health, and gerontocracy.

Some strategic posts at the very top could be now held by persons not part of the Royal family. The new Foreign Minister is now Adel al-Jubeir, the former Ambassador to the US. His fast elevation is illustrated by the fact that it was he who announced, during a rare press conference, the start of the bombing campaign in Yemen. A month later Adel al-Jubeir was boosted to the position of the head of the Kingdom's foreign policy.

Finally, it's interesting to note that the evolution in Saudi Arabia didn't affect the world oil market and didn't bring any change in prices' curves. Even the revolutionary reforms within the establishment of the number one oil producer are not able today to impact the fundamentals of the global oil market.

Another event may be of more interest to the energy markets: the change at the top of Aramco, the Saudi State oil producing company. The Oil Minister, Ali al Naimi, 79, was replaced and the vacated seat was offered to his deputy at Aramco, Khalid al Falih, 59, who was also named Health Minister. He's widely regarded as the next Oil Minister after gaining some governmental experience at a secondary post.

Another pretender to that powerful ministerial job could be Prince Abdul Aziz bin Salman, the 4th son of the King. From the beginning of the year, he's the official number 2 in the Oil Ministry, although the standing Saudi tradition stipulates that members of the Royal family are not placed to administer the main business of the country. But King Salman is full of surprises: isn't he shaking the established order?

Anyway, these personal changes at the top of the Saudi oil industry will not affect the content of the oil policy which is firmly based on the premise that, at least for the moment, it is expedient for Saudi Arabia to maintain its production quota and share of the market, even confronted by lower prices.

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