



ISSUE BRIEF

BY JEAN-FRANCOIS SEZNEC

Crude Oil for Natural Gas

Prospects for Iran-Saudi Reconciliation

OCTOBER 2015

The relations between Iran and Saudi Arabia are often presented as an intractable struggle between powers that find legitimacy in their respective Islamic traditions: Shia in Iran and Sunni in Saudi Arabia.¹ The Saudis feel threatened by what they consider an encroaching “Shia crescent” of Iranian influence, extending from al-Sham (Syria-Lebanon) to Iraq, Iran, and Yemen.² The House of Saud, in particular, views this “crescent” as an attempt to bring an end to its stewardship of Islam’s holiest sites and replace it with Shia supervision. Similarly, Iran fears the threat of encircling Sunni influence, stretching across the states of the Gulf Cooperation Council (GCC), through to Egypt, Jordan, Pakistan, and parts of Syria. Certainly, the death of many hundreds of Hajjis from Iran and other countries in Mecca on September 24, 2015, as well as the dispatch of Iranian soldiers to the Syrian front a few days later are creating great tensions between the two Gulf giants. Further complicating this divide are not only differences in size, cultural history, and educational levels, but also the states’ seemingly contradictory economic interests.

In light of such tension, Saudi-Iranian reconciliation seems impossible. However, in reality, the relations between these two powers may be less antagonistic

¹ The author would like to thank Mr. Samer Mosis, a graduate student at Johns Hopkins’s School of Advanced International Studies, for his help in fact checking and editing as well as for his suggestions on improving this paper.

² The term “Shia Crescent” was coined in 2004 by King Abdullah II of Jordan, largely as a response to Iran’s growing influence in Iraqi elections and society. See Robin Wright and Peter Baker, “Iraq, Jordan See Threat to Election from Iran: Leaders Warn against Forming Religious State,” *Washington Post*, December 8, 2004.

Global Energy Center

At a time of unprecedented volatility and opportunity, the Atlantic Council Global Energy Center works to promote global access to affordable, reliable, and sustainable energy.

Alongside government, industry, and civil society partners, the Center devises creative responses to energy-related geopolitical conflicts, advances sustainable energy solutions, and identifies trends to help develop energy strategies and policies that ensure long-term prosperity and security.

than they appear. Saudi Arabia’s use of a sectarian narrative to describe the 2011 uprising in Bahrain and Iran’s self-appointed role as the champion of Shia rights underline how sectarian rhetoric has primarily been utilized by both states as a tool to garner popular support for political ends, not one aimed at destroying the opposing state.³ Indeed, Arabs and Persians have influenced each other since the birth of Islam. Moreover, since the defining battle of Karbala in 680 AD, Sunnis and Shia more often than not have managed to peacefully cohabit. Presently, this propensity for cohabitation is aided by economic factors. Primarily among these is the geographic dispersion of natural resources in the Gulf, with the disparity in supply and demand highlighting the potential to transform economic tensions into mutually beneficial arrangements. In this sense, where Iran is envious, if not resentful, of Saudi Arabia’s role as

³ Fatima Ayub, “The Gulf and Sectarianism,” European Council on Foreign Relations, November 2013, http://www.ecfr.eu/page/-/ECFR91_GULF_ANALYSIS_AW.pdf.

Jean-François Sezne is a Nonresident Senior Fellow in the Global Energy Center and an adjunct professor at the McDonough School of Business at Georgetown University.

the region's leader in crude markets, Iran's substantial natural gas reserves hold the key to alleviating Saudi's surplus in natural gas demand. Accordingly, just as the Gulf powers have set aside sectarian strife in the past periods of détente, overlapping economic and political interests today make reconciliation possible, despite extremist activity in both countries.

Brief History of Past Relations

Since the end of World War II, the Persian Gulf (also referred to as the Arabian Gulf or sometimes, in efforts to avoid political controversy, simply the Gulf) has been a theater of competition between Iraq, Iran, and Saudi Arabia for the region's political and ideological leadership. The First Gulf War effectively put an end to Iraq's respective bid for power, but the competition between Iran and Saudi Arabia continued. By favoring one Gulf aspirant over the other, the United States has repeatedly acted as a third party to this contentious relationship, its foreign policy at times encouraging cooperation and at others goading competition.

Starting with President Richard Nixon, the United States enacted what some have dubbed a "twin pillars policy" in the Gulf, looking to Iran and Saudi Arabia to maintain its strategic interests in the region.⁴ This triangular relationship linked Saudi Arabia and Iran, not only through a mutual patron, but also through common solidarity in the face of communism and Arab nationalism. Yet, deriving from the Nixon administration's view that Iran was the Gulf's predominant economic and military power, security relations with Iran overwhelmingly overshadowed those with Saudi Arabia.⁵ This was best embodied by the Nixon administration's blank check to the Shah of Iran, which effectively allowed Iran to purchase any weapon, short of nuclear, it deemed necessary for its defense; an offer that was not extended to any other US ally, let alone Saudi Arabia.⁶ Nonetheless, while the primacy of the Iranian-US relations surely instilled jealousy, in Saudi powerbrokers, the special place Iran and Saudi Arabia held in American foreign policy led to tacit, albeit short-lived, Iran-Saudi cooperation.

American calculations, the twin pillars doctrine, and a decades-long security structure were all swept away in 1979 by Iran's radical revolution, leaving in its place animosity between Iran and the Gulf monarchies. Iran and Saudi Arabia competed to paint themselves as the

4 Andrew Rathmell, Theodore Karasik, and David Gompert, "A New Persian Gulf Security System," RAND Corporation, 2005, http://www.prgs.edu/content/dam/rand/pubs/issue_papers/2005/IP248.pdf.

5 Stephen McGlinchey, "Richard Nixon's Road to Tehran: The Making of the U.S.-Iran Arms Agreement of May 1972," *Diplomatic History* vol. 37, iss. 4, 2013, pp. 846-848.

6 John P. Miglietta, *American Alliance Policy in the Middle East, 1945-1992: Iran, Israel, and Saudi Arabia* (2002), p. 58.

IRAN AND SAUDI ARABIA COMPETED TO PAINT THEMSELVES AS THE PROTECTORS OF ISLAM AND MUSLIMS WORLDWIDE, WITH BOTH STATES EMPLOYING SECTARIAN RELIGIOUS RHETORIC TO BUILD POPULAR SUPPORT.

protectors of Islam and Muslims worldwide, with both states employing sectarian religious rhetoric to build popular support. With Sunnis comprising 90 percent of the Islamic umma, Saudi Arabia's geographic control of the holy cities of Mecca and Medina and its Sunni heritage gave it the advantage in this battle.⁷ Nonetheless, its leadership was still threatened by Iran's self-characterization as the one true Islamic government.⁸ Iran extended its campaign for the hearts and minds of Muslims by increasingly positioning itself as an advocate for marginalized Muslims, winning over Sunni and Shiite Muslims alike with its bold calls for Islamic unity in the face of Western hegemony.⁹ This threat was only aggravated by Iran's implication in a Bahraini coup plot, sectarian tensions in Kuwait, and the Iran-Iraq War, in which Saudi Arabia backed Iraq. Saudi-Iranian relations reached their lowest point in 1987. That year, over four hundred people were killed when Iranian pilgrims making the *haji*, the Islamic pilgrimage to Mecca, clashed with Saudi police.¹⁰ In retaliation, some ayatollahs amplified their campaign for Iran's Islamic leadership, turning their aim to the Saudi source of legitimacy—its guardianship of Mecca and Medina. Following the violence in

7 Pew Research Center, Forum on Religion & Public Life, *Mapping the Global Muslim Population* (October 2009), <http://www.pewforum.org/2009/10/07/mapping-the-global-muslim-population/>.

8 R. K. Ramazani, *Revolutionary Iran: Challenge and Response in the Middle East* (Baltimore: John Hopkins University Press, 1986), pp. 19-30.

9 Aylin Unver Noi, "A Clash of Islamic Models," Hudson Institute, July 10, 2013, <http://www.hudson.org/research/9770-a-clash-of-islamic-models>.

10 John Kifner, "400 Die as Iranian Marchers Battle Saudi Police in Mecca; Embassies Smashed in Teheran," *New York Times*, August 2, 1987, <http://www.nytimes.com/1987/08/02/world/400-die-iranian-marchers-battle-saudi-police-mecca-embassies-smashed-teheran.html?pagewanted=1>.

Mecca, Ayatollah Khomeini declared that the “vile and ungodly Wahhabi [Saudi rulers] are like daggers which have always pierced the heart of the Muslims from the back,” and that Mecca was in the hands of “a band of heretics.”¹¹ These claims were echoed by high-ranking Iranian politicians, including Speaker of the Parliament Ali Akbar Rafsanjani, and were followed by an Iranian campaign calling for the “liberation” of Mecca from Saudi control.¹² Diplomatic relations were severed in the wake of these events.

The end of the Iran-Iraq War and the death of Khomeini freed Iranian foreign policy from its obligatory confrontational tone. Akbar Hashemi Rafsanjani, who had assumed the Iranian presidency in 1989, proclaimed that “Iran needs to stop making enemies,” to which the Saudi Foreign Minister Prince Saud al-Faisal suggested that the two countries could see “a future of positive relations.”¹³ Diplomatic relations were restored in 1991 and Rafsanjani would go on to meet with Saudi Arabia’s then-Crown Prince Abdullah in March 1997 in Pakistan. The meeting paved the way for Iran’s hosting of the triennial summit of the Jeddah-headquartered Organization of the Islamic Conference (now called the Organization of Islamic Cooperation) in December 1997, where, in a historic thawing of relations Abdullah met with President Mohammad Khatami, Rafsanjani’s successor. In a testament to the potential for reconciliation and cooperation, Abdullah praised the Iranians for their “immortal achievements . . . and their invaluable contributions throughout our glorious Islamic history.”¹⁴ The following years would bring about slow but substantive warming, including the resumption of Iranian participation in the *hajj*, the exchange of military attachés, an agreement of noninterference in each other’s internal affairs, and culminating in the ground-breaking visit of Iranian President Khatami to Jeddah in 1999.¹⁵ Indeed, for a brief period, it seemed that détente had been realized.

Unfortunately, that détente proved fleeting. The 2005 surprise election of hardline populist Mahmoud Ahmadinejad as Iran’s President brought rapprochement to a standstill. Ahmadinejad rekindled Iran’s hawkish foreign policy supporting militant movements in Iraq and Lebanon, announcing the resumption of uranium enrichment

and challenging Saudi Arabia’s role as advocate of the common Arab by emphasizing Iran’s commitment to the Palestinian cause and opposition to Western imperialism.¹⁶ Ahmadinejad’s brinkmanship demolished the Saudi-Iranian détente and amplified fears in Saudi leadership that Iranian influence was spreading across its periphery. Iran at the same time felt increasingly threatened by an American military presence in the Gulf. This military buildup was based on Washington’s cooperation with GCC monarchies, primarily Saudi Arabia. Iranian leaders viewed Saudi Arabia not only as the leader of an international effort to deny Shiite governments rights and influence across the region, but also as the chief transgressor that allowed for the United States’ domination of the Gulf.

Main Areas of Contention Today

Over the last four years, the Saudi monarchy has been increasingly concerned about the influence of Iran in the region. Saudi Arabia has seen Iran’s influence extend to its north in Syria by way of Alawi support and Hezbollah ground forces; in Iraq, by way of Shia militias and political influence in Baghdad; further west, by way of Hezbollah becoming a major player in Lebanese politics; and to the kingdom’s south by way of Iranian activity in Yemen, allegedly supporting the Houthi rebellion.

Competition for Oil Markets

In modern times, energy markets have been used as a tool in the ideological war as much as forces on the ground. Both countries desperately need to maximize their natural resources in order to ascend to the regional leadership role they aspire to. In this realm, Saudi Arabia has a major advantage. It has nearly twice the oil reserves and three times the production capacity of Iran and, more importantly to the global oil markets, it is the only reliable supplier in OPEC.¹⁷

Saudi Arabia initiated the 1973 Arab oil embargo to protest states that supported Israel during the Yom Kippur War. Although the embargo may have affected global prices, it failed to accomplish its stated political goal of ending Western support for Israel.¹⁸ Following this failure, Saudi Arabia has tried very hard to disconnect oil supplies from politics. In the 1970s, unlike Iraq, Libya, and Iran, it did not nationalize foreign companies out-

11 Khomeini’s message to Karrubi, Radio Tehran, August 3, 1987, quoted in BBC Summary, August 4, 1987.

12 Martin Kramer, *Arab Awakening and Islamic Revival* (New Brunswick: Transaction, 1996), pp. 161-87.

13 Afshin Molavi, “Iran and the Gulf States,” in Robin Wright, ed., *The Iran Primer: Power, Politics, and U.S. Policy* (Washington, DC: United States Institute of Peace, 2010), p. 160.

14 Crown Prince Abdullah bin Abdulaziz, Address to the 11th Summit of the Organization of the Islamic Conference, Tehran, Iran, December 9-11, 1997, <http://www.saudiembassy.net/archive/1997/speeches/page0.aspx>.

15 Anthony H. Cordesman, *Saudi Arabia Enters the Twenty-First Century* (Westport, CT: Praeger Publishers, 2003), p. 49.

16 Frederic Wehrey, et al., “Saudi-Iranian Relations since the Fall of Saddam,” RAND Corporation, 2009, http://www.rand.org/content/dam/rand/pubs/monographs/2009/RAND_MG840.pdf.

17 EIA, “International Energy Statistics”; *Worldwide Look at Reserves and Production*, *Oil & Gas Journal* January 1, 2015; EIA, “Iran: International Energy Data and Analysis,” June 19, 2015; EIA, “Country Analysis Brief: Saudi Arabia,” September 10, 2014, p. 3; Anjili Raval, “Saudi Strategy to Retain Oil Dominance,” *Financial Times*, August 6, 2015.

18 Meghan L. O’Sullivan and Jeane Kirkpatrick, “40 Years after Embargo, OPEC Is Over a Barrel,” *Bloomberg View*, October 17, 2013.

IRAN'S MAIN ADVANTAGE OVER SAUDI ARABIA DOES NOT LIE IN CRUDE OIL BUT IN NATURAL GAS.

right but slowly bought the assets of the international oil companies (IOCs) operating domestically. This allowed the Saudi state to take control of its crude operations and sales, all while maintaining excellent relationships with IOCs, a move that has helped the kingdom become a leader in oil technology today.

Oppositely, Iran never managed to develop its oil resources beyond 4 million barrels per day (b/d), (compared to Saudi Arabia's current 10.4 million b/d) and, in the past ten years, has lost substantial production capacity.¹⁹ The loss of capacity, which started with the fall of the shah, culminated in the international embargo on Iranian crude in 2012 and resulted in exports declining to between 1 and 1.4 million b/d from July 2012 to December 2014.²⁰ Moreover, while the cost of Iranian production is low by global standards, it is somewhat higher than that of Saudi Arabia. This is aggravated by the fact that Iranian oil fields are reputed to be in a state of disrepair, requiring extensive investment and technology that Iran can only attain from outside sources.²¹ Yet, if Iran is to attain either, it will find itself in a costly state of dependence on foreign entities, limiting its ability to compete with the Saudis. Comparatively, the cost of Saudi oil extraction today varies somewhere in the remarkably low range of \$1.5 per barrel to \$6.0 per barrel, with a conservative average of \$4.0 per barrel, while Iran's cost is estimated at \$2.0 per barrel to \$7.0 per barrel with an average of \$5.0 per barrel.²² Furthermore, Saudi Arabia is no longer dependent on technology from the IOCs, either because it has developed its own or has easily acquired it from the world's best engineering firms.

19 EIA, "Iran: International Energy Data and Analysis," June 19, 2015; MEES, "August OPEC Production: Output Falls for First Time in Six Months," vol. 58, iss. 36, September 2015.

20 Lloyd's List Intelligence, "Iran Poised to Claw Back Market Share despite Sanctions," March 10, 2015, <http://info.lloydslistintelligence.com/iran-poised-to-claw-back-market-share-despite-sanctions>.

21 Christopher Adams, Najmeh Bozorgmehr, and Ed Crooks, "Iran: The Oil and Gas Multibillion-Dollar 'Candy Store,'" *Financial Times*, July 16, 2015, <http://www.ft.com/intl/cms/s/2/92402244-2975-11e5-8613-e7aedbb7bdb7.html#slide0>.

22 Author's interview with international oil company executives familiar with Arab/Persian Gulf operations for the Saudi side of the estimates and with Dr. Sara Vakshouri for the Iranian figures.

Iran's main advantage over Saudi Arabia does not lie in crude oil but in natural gas (NG). BP now lists Iran as the global leader in NG reserves, giving it the potential to be second largest exporter of NG after Russia.²³ Yet even here Iran has suffered from its political isolation. The decline in Western capital and technology contributed to the lack of maintenance of Iran's gas fields. As a result, today Iran is a net importer of NG. Should Iran refurbish its gas fields, it could become a major power in the NG world, finding it relatively easy to develop pipelines to supply Pakistan, increase its sales to Turkey, and even start selling piped NG to Oman and the United Arab Emirates (UAE). With better-managed gas fields, Iran could also develop its burgeoning chemicals industry, which has been greatly hampered by the lack of supply of methane and ethane. Accordingly, to effectively compete with Saudi Arabia in the energy markets, Iran would be wise to shift its focus away from crude oil production and toward redeveloping its NG fields. It is this potential NG production that could provide Gulf Arab states a viable starting point for renewed cooperation.

Underlining this possibility is Saudi Arabia's natural gas problem. Since 1974, Saudi Arabia's economic growth has been spectacular, growing from a nearly medieval economy in the mid-twentieth century to one of the world's most advanced economies today. This growth has fueled tremendous improvements in health and education, which in turn has resulted in a massive population growth—from around six million people in the early 1970s to nearly thirty million today.²⁴ This combination of economic and population growth has increased the demand for energy exponentially, with domestic demand for both water and electricity growing at about 7.5 percent annually.²⁵

Driven by both industry and household needs, Saudi water and electricity demands are largely met through large-scale flash desalinization projects that cogenerate electricity, most which run on NG. Yet, since about 70 percent of the gas produced in the kingdom (8.4 trillion British Thermal Units (BTU) per day) is associated with oil production, which stood around 10.3 million b/d in 2015, Saudi Arabia has to maintain at least 7 million b/d of crude production in order to provide the associated

23 1201.4 trillion cubic feet (34 trillion cubic meters) of NG reserves. See *BP Statistical Review of the World Energy* (June 2014), p. 20, <http://www.bp.com/content/dam/bp/pdf/Energy-economics/statistical-review-2015/bp-statistical-review-of-world-energy-2015-full-report.pdf>.

24 World Bank Database, "Indicator: Total Population," <http://data.worldbank.org/indicator/SP.POP.TOTL>.

25 Christopher Segar, "Saudi Energy Mix: Renewables Augment Gas," International Energy Agency, November 3, 2014, <http://www.iea.org/iea-energy/issue7/saudi-energy-mix-renewables-augment-gas.html>; Abdel Aziz Aluwaisheg, "Runaway Consumption Alarming for Saudi Arabia," *Arab News*, August 4, 2013, <http://www.arabnews.com/news/460158>.



The 2005 election of hardline President Mahmoud Ahmadinejad heightened Saudi-Iran tensions after a temporary thaw. *Photo credit: Agência Brasil/Wikimedia Commons.*

gas necessary to avoid stifling economic activity.²⁶ To counter this limitation, Saudi Aramco has been seeking to develop non-associated gas fields, finding some success in the Karan dry gas field, which produces 1.8 billion cubic feet per day, and looking to find more in the Arabiyah and Hasbah fields, which could come to production toward the end of 2015. Nonetheless, these fields are difficult and expensive to tap because they are offshore and produce sour gas, which in light of the heavily subsidized domestic NG prices (\$0.75 per million BTUs as set by the Council of Minister), would create large, albeit undisclosed, losses to Saudi Aramco.²⁷ Since NG is plentiful in some parts of the Gulf, it makes little sense for the kingdom to spend a great deal of money to develop expensive alternatives.

Religious Issues: Sunni vs. Shia

For centuries there has been competition between various schools and sects within Islam. However, the competition between these schools often tends to be hijacked for political purposes by power seeking groups and individuals.²⁸ And, when the need for control declines, these vari-

26 US Energy Information Administration, "Country Analysis Brief: Saudi Arabia," September 10, 2014, p. 3, http://www.eia.gov/beta/international/analysis_includes/countries_long/Saudi_Arabia/saudi_arabia.pdf; Saudi Aramco, "Saudi Aramco 2014 Facts and Figures," 2015, <http://www.saudiaramco.com/content/dam/Publications/facts-and-figures/2014-saudi-aramco-facts-figures.pdf>.

27 The cost of extracting NG from the associated gas is not known, but is certainly very low and perhaps not too much higher than the set price of \$0.75/million BTUs.

28 Seyyed Vali Reza Nasr, *Islamic Leviathan: Islam and the Making of State Power* (New York: Oxford University Press, 2001).

ous religious leaders often find it convenient to promote love and understanding of their "brothers." This is why the situation on the ground in the Gulf is more complicated than a simple Sunni-Shia sectarian dichotomy. With Shia making up anywhere from 10 percent to 15 percent of the kingdom's population, most of whom live on the east coast of the kingdom, Saudi leadership fears that Iran is using the kingdom's Shia population to cut into their control of the country.²⁹ Despite long-held political efforts to eradicate and oppress Shiism, the Shia have grown increasingly involved in the running of the country. There are many Shia at Saudi Aramco and other large Saudi companies, and many are involved in politics through the Consultative Assembly of Saudi Arabia, the Majlis as-Shoura. Nevertheless, there is often a feeling of frustration among the Saudi Shia who feel discriminated against and targeted by the more conservative Wahabi elements.³⁰

Though there is a strong religious component to the tensions with Iran, it should not be exaggerated or viewed as the single motivating factor. Even if many in the Saudi leadership view the numerous street demonstrations in the eastern province over the past three years as proof of Iranian meddling, their fear is less that Shiism is seeking to dominate the region and more that Iran is attempting to extend its influence. In other words, it is not so much religion that impacts Sunni-Shia relations, but more of an Arab vs. non-Arab state issue, with Arab Sunnis assuming that the non-Arabs (read Persians) will utilize sectarian issues to their advantage. Furthermore, while Saudi Arabia remains founded upon religious grounds, Wahabi dominance of personal and national identification has eroded.³¹ This transformation has been fueled not only by modernization, but also by the growth of a new form Saudi nationalist sentiment, one that is tightly linked to both the Saudi monarchy and the growth of Saudi Arabia as a powerful, and respected, nation-state.³² It is this form of nationalism that, by superseding polarizing Wahabi doctrine, has allowed the kingdom's population to unite around the idea of being "Saudi," regardless of sect or tribe.³³ Indeed, even though they are

29 "Protests Break Out after a Shia Cleric Is Sentenced to Death," *Economist*, October 16, 2014, <http://www.economist.com/news/middle-east-and-africa/21625868-protests-break-out-after-shia-cleric-sentenced-death-sword-unsheathed>.

30 Paul Raymond, "Yemen Backlash: Gulf Shia Portrayed as 'Enemy Within,'" *Al-Araby al-Jadeed*, April 16, 2015, <http://www.alaraby.co.uk/english/features/2015/4/16/gulf-shia-treated-as-enemy-within-as-yemen-burns>.

31 Caryle Murphy, "Saudi Arabia's Shifting Islamic Landscape," Pulitzer Center on Crisis Reporting, April 1, 2014, <http://pulitzercenter.org/project/middle-east-saudi-arabia-islam-religion-salafi>.

32 Nawaf Obaid, "There Will Be No Uprising in Saudi Arabia," *Foreign Policy*, March 10, 2011, <http://foreignpolicy.com/2011/03/10/there-will-be-no-uprising-in-saudi-arabia/>.

33 Theodore Karasik, "Nationalism Is Taking on a New Meaning in Saudi," *National*, June 7, 2015, <http://www.thenational.ae/opinion/com>

not Hanbali Sunni, many Shafii and Sufi groups in the western provinces, as well as the numerous Zaidi Shia in the south of the country, identify as “Saudi” and are not viscerally opposed to the present leadership. By the same token, Iran is not purely “Persian” or even Shia. There are many Arabs in Iran, both Sunnis and Shia, as well as many non-Arab Sunnis, like the Kurds.³⁴ Hence, while sectarian conflict surely plays a role in the Gulf’s conflicts, it is more a byproduct of hostility between states than its cause.

Interests in Common

The areas of contention between Iran and Saudi Arabia could potentially lead to extensive long-term confrontation.³⁵ Yet, if Iranian and Saudi leaders are able to view sectarianism as undermining their nations’ economic or political interests, they may see beyond shortsighted sectarian rhetoric and pave the way for a more cooperative relationship between the two countries.

Oil and NG Interests

In the summer of 2015, after months of deliberations, the P5+1—the United States, the United Kingdom, France, China, Russia, and Germany, plus the European Union—successfully put forward the Joint Comprehensive Plan of Action (JCPOA) on Iran’s nuclear program. With the JCPOA’s implementation, Iran will not only see international sanctions that have crippled its economy lifted, but will also find a number of new beneficial economic opportunities arise. In a post-JCPOA environment, numerous incentives exist for Iran and Saudi Arabia to cooperate, rather than compete, in energy and economic matters. The most obvious of these incentives lies in the demand and supply of NG in the Gulf. Saudi Arabia needs more access to lower cost NG than it presently can produce from non-associated sources for its own domestic consumption. From Saudi Arabia’s point of view, if it were to find plentiful, low-cost NG within the Gulf, it would not be forced to maintain a high minimum of oil production to produce enough NG to keep its economy going. It would also free up crude oil which is presently used to generate electricity, crude oil that could then be diverted to the world markets, thus giving Saudi Arabia more leeway to influence prices. At this time, Saudi Arabia can only

ment/nationalism-is-taking-on-a-new-meaning-in-saudi.

34 Ali Mamouri, “Iranian Government Builds Bridges to Sunni Minority,” *Al-Monitor*, <http://www.al-monitor.com/pulse/originals/2013/12/iranian-government-builds-bridges-to-sunni-minority-hedsum-app-b.html>

35 John Bell, “The Greater Reality for Iran and Saudi Arabia,” *Al Jazeera*, March 30, 2015, <http://www.aljazeera.com/indepth/opinion/2015/03/greater-reality-iran-saudi-arabia-150330051616953.html>; Kim Ghatas, “The Saudi Cold War with Iran Heats Up,” *Foreign Policy*, July 25, 2015, <http://foreignpolicy.com/2015/07/15/the-saudi-cold-war-with-iran-heats-up/>; Yoel Guzansky, “Saudi Arabia and the Nuclear Agreement with Iran,” *INSS*, July 22, 2015, <http://www.inss.org.il/index.aspx?id=4538&articleid=10116>.

WHILE SECTARIAN
CONFLICT SURELY
PLAYS A ROLE IN THE
GULF’S CONFLICTS, IT
IS MORE A BYPRODUCT
OF HOSTILITY BETWEEN
STATES THAN ITS CAUSE.

influence the markets by increasing production to force prices down, a maneuver that has ultimately been aimed at forcing producers like Russia to cut production and disincentivize Iranian production. If Saudi Arabia did not have to produce at least 7 million b/d for its associated gas, it could cut production to shore up prices, while maintaining the option of flooding the markets. In this scenario, NG could flow at a relatively low cost from the Iranian fields to the UAE and Oman, which, in turn, could limit their imports from Qatar. Qatar could then divert the difference to Saudi Arabia. Of course, if it were to become politically feasible, Saudi Arabia and Iran would find the greatest benefit in directly transferring gas by pipeline on the short distance between the offshore South Pars gas field in Iran and Saudi Arabia. As part of this NG negotiation, the Saudis could also allow for a negotiated slow return of Iran to oil markets by cutting small amounts of production, providing room for a slight increase in Iranian production—a coordinated transition that would satisfy Iran while making little impact on Saudi Arabian revenue. In fact, deriving from the inelasticity of oil, this transition could result in increased revenue for the kingdom.

The Iranians need substantial technology and capital to develop or improve their oil and NG fields. While in total it is estimated that Iran requires somewhere between \$200-250 billion over the next six years in order to fulfill the necessary investments in its oil and gas industry, it will not see more than \$50 billion in usable, liquid assets flow back into the country once sanctions are lifted.³⁶ This requirement for a large input of capital provides Saudi Arabian public and private entities the opportunity for either direct or indirect involvement in financing the rebirth of the wells, especially of the South Pars NG field, which requires over \$40 billion alone, as well as the building of pipelines necessary to get NG flowing to the Gulf.³⁷

36 Sara Vakhshouri, “Iran’s Oil Production Boost Scenarios in a Post-Sanctions Era,” *MEES*, July 3, 2015; United States Institute of Peace, *The Iran Primer*, “US Treasury Official on Nuclear Deal,” <http://iranprimer.usip.org/blog/2015/aug/06/us-treasury-official-nuclear-deal>.

37 Vakhshouri, “Iran’s Oil Production Boost Scenarios in a Post-Sanctions Era,” *op. cit.*



South Pars, an offshore gas field located in the Persian Gulf, is set to play a central role in Iran's energy future. *Photo credit: Alireza824/Wikimedia Commons.*

Saudi Arabia and Iran also could work together to coordinate chemical and fertilizer development. Saudi Arabia today is one of the most successful chemical producers in the world. If Iran's chemical industry, which suffers from lack of NG, wants to grow, it will need to either compete or coordinate with the very efficient Saudi producers. The chemical companies of both countries could mutually benefit from developing advanced chemical production that takes advantage of each of their respective resources and capacities. For example, after sanctions are lifted, Iran's natural abundance of ethane will allow it to develop ethylene downstream production, while the kingdom could push the growth of industries based on naphtha from its refineries, hence freeing up market share for both countries.

There are also a number of possible mutually beneficial ventures, including a move by Saudi Arabia's government-owned Ma'aden, the lowest cost aluminum producer in the world, to establish downstream joint ventures (JVs) in Iran that would capitalize on Iran's high-quality work force and large market. Even more, Ma'aden, as the largest advanced fertilizer company in the Gulf, could produce cheaper, higher-quality fertil-

izers by adopting Saudi phosphates and Iranian ammonia as feedstock. On the private side, entities such as Al Ujain, Sahara, Sipchem, and Tasnee are already involved in the treatment of NG. Saudi's prominent cement companies and others in energy-dependent industries are other potential buyers of Iran's NG, methanol, and ammonia. However, none of these economic scenarios are feasible unless a political settlement between the major antagonists in the Gulf occurs.

Political Interests in Common

When it comes to their own survival, the Iranian ayatollahs and the monarchial Saudi leaders can be pragmatic. Presently, all the states inside and outside the region agree that the self-proclaimed Islamic State of Iraq and al-Sham (ISIS) must be eradicated. Iran and Saudi Arabia are individually waging war against an ideology that demands the annihilation of all Shia and of the present Sunni leadership alike. In an overly ambitious plan, Saudi Arabia is trying to simultaneously destroy the Iranian- and Russian-supported Assad-Alawi clan in Syria, as well as ISIS. Iran is also embroiled in a futile attempt to destroy ISIS on numerous fronts. Yet neither state can afford to spend tens of billions of dollars on

endless wars. Consequently, only through a compromise forged between Iran and Saudi Arabia, and including other Sunni powers such as Turkey and Egypt, can either state see the demise of ISIS. To do so, Saudi Arabia may have to accept that the Alawis remain in the Syrian political process in some capacity, while Iran would have to acquiesce to limiting its efforts to establish a “Shia crescent.”³⁸

Conclusion

In spite of the latest rhetoric triggered by the Mecca tragedy and the renewed tensions over Syria, reconciliation between Iran and Saudi Arabia is possible. Dialogue can easily develop into mutually beneficial cooperation. Across history, sectarian issues are often not causes of bloody wars, but rather are merely the consequences of political struggles, where local leadership utilizes violent sectarianism to rally people around them. In Saudi Arabia, it has meant allowing the Wahhabi extremists to whip up anti-Shia feelings. In Iran, it manifests as the leadership’s premise that they are the true defenders of the Shia religious orthodoxy. The terrible cost of these manipulations can be seen in Yemen, Iraq, and Syria. While this paints a grim picture of reality, it also provides some hope. If sectarian sentiment is not the true source of conflict, then sectarian violence can be tamped down more easily than is generally assumed.

In the late 1990s, the leaders of Saudi Arabia and Iran saw that that they could gain support through economic, business, and political cooperation rather than sectarian issues. Today, leaders on both sides are poised to come to the same conclusion. In the wake of Minister Javed Zarif and President Hassan Rouhani’s accomplishments during the JCPOA deliberations, Iranian moderates have increasingly gained popularity, with Rafsanjani, the loudest advocate for better Saudi-Iranian relations, already acquiring popular support for his latest electoral campaign.³⁹ The success of Iran’s moderate politicians, who are the key to looking beyond sectarian rhetoric, will be largely based on the promise and fulfillment of economic development. If these Iranian politicians rise to power—and the new, young Saudi leadership agrees—cooperation could come in the form of Iran’s minimal re-entry into the oil markets and the focus on natural gas cooperation. Iran could benefit from Saudi investments and purchase of NG, as well as investments

³⁸ It should be reminded that Saudi Arabia used to be very close to the Assad clan. The relationship deteriorated after the assassination of Rafik Hariri attributed by the Saudis to President Bashar al-Assad. Alliances in the Middle East can be very fickle and often change rapidly. Hence, a change of heart by the Saudis against the Assad cannot be dismissed summarily.

³⁹ Rohollah Faghihi, “Hard-liners Rage against Rafsanjani as Elections Near,” *Al-Monitor*, <http://www.al-monitor.com/pulse/originals/2015/08/iran-rafsanjani-elections.html>.

IF LEADERS ON BOTH SIDES REPLACE SECTARIAN RHETORIC BY ECONOMIC COOPERATION, THEY COULD USHER A PERIOD OF LONG TERM DÉTENTE AND PROSPERITY IN THE GULF.

in downstream industrial ventures using chemicals and aluminum produced in Saudi Arabia. Saudi Arabia could have access to plentiful NG at a lower cost than their non-associated NG and have increased markets for their chemicals, fertilizers and metals. With these economic interests in mind, and in a time of plummeting energy prices, there would be additional incentive to work together to curb ISIS. Iran and Saudi Arabia can even work together to bring about governments of national unity in Iraq, Syria, and Yemen. Ultimately, if leaders on both sides make an effort to set aside sectarian tools and instead garner support through economic development, they could very well usher a period of renewed détente in the Gulf.

Atlantic Council Board of Directors

CHAIRMAN

*Jon M. Huntsman, Jr.

CHAIRMAN, INTERNATIONAL ADVISORY BOARD

Brent Scowcroft

PRESIDENT AND CEO

*Frederick Kempe

EXECUTIVE VICE CHAIRS

*Adrienne Arsht

*Stephen J. Hadley

VICE CHAIRS

*Robert J. Abernethy

*Richard Edelman

*C. Boyden Gray

*George Lund

*Virginia A. Mulberger

*W. DeVier Pierson

*John Studzinski

TREASURER

*Brian C. McK. Henderson

SECRETARY

*Walter B. Slocombe

DIRECTORS

Stephane Abrial

Odeh Aburdene

Peter Ackerman

Timothy D. Adams

John Allen

Michael Andersson

Michael Ansari

Richard L. Armitage

David D. Aufhauser

Elizabeth F. Bagley

Peter Bass

*Rafic Bizri

*Thomas L. Blair

Francis Bouchard

Myron Brilliant

Esther Brimmer

*R. Nicholas Burns

William J. Burns

*Richard R. Burt

Michael Calvey

James E. Cartwright

John E. Chapoton

Ahmed Charai

Sandra Charles

Melanie Chen

George Chopivsky

Wesley K. Clark

David W. Craig

*Ralph D. Crosby, Jr.

Nelson Cunningham

Ivo H. Daalder

*Paula J. Dobriansky

Christopher J. Dodd

Conrado Dornier

Thomas J. Edelman

Thomas J. Egan, Jr.

*Stuart E. Eizenstat

Thomas R. Eldridge

Julie Finley

Lawrence P. Fisher, II

Alan H. Fleischmann

*Ronald M. Freeman

Laurie Fulton

Courtney Geduldig

*Robert S. Gelbard

Thomas Glocer

*Sherri W. Goodman

Mikael Hagström

Ian Hague

John D. Harris, II

Frank Haun

Michael V. Hayden

Annette Heuser

*Karl Hopkins

Robert Hormats

Miroslav Hornak

*Mary L. Howell

Robert E. Hunter

Wolfgang Ischinger

Reuben Jeffery, III

*James L. Jones, Jr.

George A. Joulwan

Lawrence S. Kanarek

Stephen R. Kappes

Maria Pica Karp

Francis J. Kelly, Jr.

Zalmay M. Khalilzad

Robert M. Kimmitt

Henry A. Kissinger

Franklin D. Kramer

Philip Lader

*Richard L. Lawson

*Jan M. Lodal

Jane Holl Lute

William J. Lynn

Izzat Majeed

Wendy W. Makins

Mian M. Mansha

William E. Mayer

Allan McArtor

Eric D.K. Melby

Franklin C. Miller

James N. Miller

*Judith A. Miller

*Alexander V. Mirtchev

Obie L. Moore

Karl Moor

Georgette Mosbacher

Steve C. Nicandros

Thomas R. Nides

Franco Nuschese

Joseph S. Nye

Sean O'Keefe

Hilda Ochoa-Brillembourg

Ahmet Oren

*Ana Palacio

Carlos Pascual

Thomas R. Pickering

Daniel B. Poneman

Daniel M. Price

Arnold L. Punaro

*Kirk A. Radke

Robert Rangel

Teresa M. Ressel

Charles O. Rossotti

Stanley O. Roth

Robert Rowland

Harry Sachinis

John P. Schmitz

Brent Scowcroft

Alan J. Spence

James Stavridis

Richard J.A. Steele

*Paula Stern

Robert J. Stevens

John S. Tanner

*Ellen O. Tauscher

Karen Tramontano

Clyde C. Tuggle

Paul Twomey

Melanne Verveer

Enzo Viscusi

Charles F. Wald

Jay Walker

Michael F. Walsh

Mark R. Warner

David A. Wilson

Maciej Witucki

Neal S. Wolin

Mary C. Yates

Dov S. Zakheim

HONORARY DIRECTORS

David C. Acheson

Madeleine K. Albright

James A. Baker, III

Harold Brown

Frank C. Carlucci, III

Robert M. Gates

Michael G. Mullen

Leon E. Panetta

William J. Perry

Colin L. Powell

Condoleezza Rice

Edward L. Rowny

George P. Shultz

John W. Warner

William H. Webster

**Executive Committee
Members*

*List as of September 25,
2015*

The Atlantic Council is a nonpartisan organization that promotes constructive US leadership and engagement in international affairs based on the central role of the Atlantic community in meeting today's global challenges.

© 2015 The Atlantic Council of the United States. All rights reserved. No part of this publication may be reproduced or transmitted in any form or by any means without permission in writing from the Atlantic Council, except in the case of brief quotations in news articles, critical articles, or reviews. Please contact us for more information.

1030 15th Street, NW,
12th Floor,
Washington, DC 20005
(202) 778-4952

AtlanticCouncil.org