'Energy Independence' Alone Won’t Boost U.S. Power

By Meghan L O'Sullivan

“We are finally poised to control our own energy future,” said President Barack Obama in his State of the Union message, noting the drastic increase in American energy production from unconventional oil and gas resources.

Controlling our energy future means more than just producing a greater amount of our own energy. It also means harnessing this energy renaissance to meet our global geopolitical needs. We’ve begun to reap the many economic benefits this boom brings -- such as easing the trade deficit and lowering carbon emissions. But we have only started to appreciate how this energy renaissance affects our larger strategic environment. And, not surprisingly, many readers of the tea leaves have confused reality with desire, by hoping more energy at home will mean keeping out of the volatile politics and economics of the Middle East.

First, the facts. A tremendous increase in the production of shale gas means the U.S. no longer anticipates decades of growing natural gas imports, but has the capacity to meets its own needs for decades and possibly even to export. Increases in oil production in the U.S. and Canada have been equally surprisingly; many analysts, in the words of a Citigroup Inc. report this week, anticipate “North American energy independence” by 2020.

FOREIGN PERCEPTION

The first way in which this new energy reality influences American power is through perception. Just as the financial crisis hurt the U.S. abroad by projecting weakness,
our rising energy fortunes strongly counter the now-common global narrative that the U.S. is in decline. Europe, China, Japan and other large economies face futures of ever-growing dependence on imported energy. Even though the U.S. is highly unlikely to become completely self-sufficient, it will spend less acquiring energy from abroad. For China, on the other hand, importing energy will become a greater obsession. Although it is hard to quantify just how this will influence foreign affairs, it will certainly change the tenor of diplomacy.

The boom in shale gas and tight oil is also good news for U.S. allies. Even in the unlikely event the hydraulic-fracturing phenomenon remains limited to North America, it creates more breathing space for our European partners. Some exports of liquefied natural gas from Qatar and elsewhere originally destined for the U.S. have been diverted to Europe. This cheaper gas, sold on the spot market, has given Europe the leverage to challenge the long-term, high-priced contracts under which most of its gas arrives.

Moreover, if the U.S. begins to export natural gas in meaningful quantities and European nations invest in more LNG terminals, their vulnerability to Russian political pressure could ease. They might be able to depend on the U.S. as an energy supplier in times of duress, as during the Suez crisis of 1956. Japan has also made its desire to import American gas very clear. Doing so would help it curb reliance on nuclear energy without having to turn to greater volumes of gas imports from volatile markets.

Just as the U.S. oil and gas bonanza strengthens our allies, it creates difficulties for our adversaries and our more prickly partners. Although Russia has vast quantities of unconventional energy itself, several developments in the global gas markets have fundamentally challenged OAO Gazprom’s longstanding business model. The shale gale, the burgeoning LNG market, Europe’s efforts to integrate its energy grid, and the emergence of smaller, independent Russian companies producing gas and looking to ship it by tanker all have called into question the durability of Gazprom’s reliance on long-term contracts, oil-indexed prices and use of pipelines.
PRICE RISK

Although it is too early to sound the death knell for Gazprom, it is plausible that the company could lose its monopoly on Russia’s gas exports, and even find itself subject to radical and dismembering reforms as President Vladimir Putin looks to boost Russia’s share of global markets.

The challenge posed by the shale revolution to other nondemocratic regimes falls more squarely in the domain of price risk. Increased American production, combined with the possible continued weakness in the global economy and increased conservation in the developed world, could cause the price of oil to fall considerably. Some analysts, such as Citigroup’s Ed Morse, see prices as low as $50 a barrel. Although this seems unlikely over a long period, particularly given the comparatively high “break even” prices of unconventional sources such as oil sands, even a short-term dive could be devastating for many producer countries. The Russian School of Economics came out with a study last month concluding that Russia’s Oil Wealth Fund would be fully depleted if the price of oil fell to $60 a barrel for one year.

Unanticipated boosts in U.S. oil production, in combination with increasing supplies from other sources such as Iraq, could also contribute to the woes of the Organization of the Petroleum Exporting Countries. As with Russia, most OPEC members need prices to stay above $85 a barrel to make their budgets -- many now swollen with post-Arab Spring spending and wage inducements -- meet. For Iran and Venezuela, the per-barrel number is $129 and $124 respectively. OPEC members just might find the discipline to rein in production enough to keep global prices high, but the result would be levels of spare capacity in the system that haven’t been seen for more than a decade. As the metric most closely correlated with price, huge excess capacity will itself cause markets to relax and push down prices.

Finally, the U.S. energy renaissance gives Washington foreign-policy makers a bit more room to maneuver. When the U.S. began to lead the charge for greater sanctions on Iran in the mid-2000s, the price of oil was at all-time highs, making few countries
eager to impose strictures. But, as noted by Daniel Yergin, author of “The Quest: Energy, Security and the Remaking of the Modern World,” increases in American oil production have almost offset the declines in Iranian exports, allowing the Obama administration to proceed with a sanctions-led approach toward Iran’s nuclear program.

NO INDEPENDENCE

Still, despite all this good news, the U.S. energy boom won’t deliver the one geopolitical benefit Americans long for most: a release from the Middle East. True, by 2020 the U.S. will be importing substantially less oil than it does today, and probably none of it will originate in the Middle East. The U.S. will, however, remain invested in stability in that part of the world even if it doesn’t consume a single drop of Middle Eastern oil. Interests other than energy, such as terrorism, nuclear proliferation, the security of Israel and the well-being of more than more than 300 million Arabs, will continue to be high on the U.S. agenda.

The U.S. will continue to have enduring energy interests in the Middle East, given that its allies and China -- the single largest engine of global economic growth -- will become increasingly dependent on the Middle East in the years ahead. Even more important, because all oil is priced on a global market, a disruption in the Middle East will quickly filter back to the U.S. economy. Americans in 2020 may transmit less of their income abroad in the case of a surge in oil prices, but a major increase in global prices caused by instability in the Middle East would be almost as destabilizing to the U.S. as it was when Uncle Sam secured much of its oil from Saudi Arabia.

Saying that U.S. interests in the Middle East will endure does not mean nothing will change. Surprisingly, the U.S. may find that it has less leverage with Middle Eastern governments, not more; being the largest consumer of a country’s export product does provide influence. At the same time, China, despite efforts to diversify energy sources, will be even more invested in this region of the world. Although China has neither the desire nor the capability to challenge the U.S. political and military role in
the Middle East, it will probably need to become more savvy in dealing with the region and its complexities. China’s eagerness to engage the region and U.S. reluctance to maintain its current footprint there could create new opportunities for U.S.-Chinese cooperation, which itself may have positive spillovers in the South China Sea and elsewhere.

**NO STRATEGY**

We are only beginning to understand the many ways in which brightened U.S. energy fortunes will shape the geopolitical landscape. Thus far, most geopolitical ramifications are positive, and have been unfolding as unanticipated good fortune rather than as the product of deliberate strategy. But America needs to rethink its grand strategy; strength in the energy domain can be a major driver of U.S. influence in a world in which American power is more diffuse. The Obama administration needs to better define just what sort of world it wants to emerge in the years ahead. Then, it should think hard about how the new American energy prowess can help deliver that vision. The opportunities are too good to be left to serendipity.

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