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ENERGY BRIEF

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SYRIAN OIL INDUSTRY COULD FACE EU SANCTIONS AS VIOLENCE PERSISTS

Syria's oil industry may find itself confronting sanctions from the European Union this week as the regime of President Bashar al-Assad continues to crack down hard against demonstrators demanding political reforms. More than 2,200 civilians are reported to have been killed by the Syrian army and agents after five months of public unrest.

Now that Libyan rebels have overthrown the 42-year dictatorship of Muammar Qadhafi in Libya, attention is turning to Syria where the Assad family has ruled with a firm grip since 1970. The violence that the current regime has shown against the Syrian people is reminiscent of the ruthless suppression that the president's father, Hafez al-Assad, exercised in Hama to put down a revolt there in 1982.

Earlier this month, US President Barak Obama signed an executive order that froze assets held by the Syrian government in the US and banned the import of Syria crude oil or petroleum products of Syrian origin. The move is largely symbolic in that the US does not import crude from Syria. President Obama's action follows calls by a number of Congressional representatives who urged the president to take some action in response to the violence perpetrated against civilians in Syria. It also follows the introduction in 2004 of sanctions against Damascus imposed by then President George W. Bush. US oil companies operating in Syria at that time exited the country and there has been almost no connection between the US and Syrian oil industries since.

Europe is another matter and the impact of sanctions imposed by it could cause Damascus serious concern and hit it financially hard. The EU is reported to be considering some form of sanctions against Syria's oil sector that may be put into place as soon as August 30. Depending on the strength of EU sanctions, European refineries and trading companies could also feel the brunt. Germany and Italy are the main importers of Syria crude and the UK's Shell and France's Total have large stakes in the Syrian crude operations through the Al-Furat Petroleum Company (AFPC) and Deir al-Zour Petroleum Company respectively.

Syria is producing around 380,000 bpd of crude oil. Last year, Europe received around 160,000 bpd of the country's exports. An EU ban of oil trade with Syria would create a serious cash flow problem for the state, but already Damascus has begun to look for new markets in east Asia, notably China and India. Chinese and Indian oil companies are active in developing some oil fields in Syria, but Syria exports consist primarily of the heavy Soudieh crude which requires the cracking capacity of a sophisticated refinery.

As a relatively small producer, a ban on Syrian crude imports is unlikely to have a significant impact on the global market, but it could shake things up in Europe for a time, especially in light of the absence of Libyan crude, which was a major source of supply for European refineries.

Syria relies on EU countries for about 30% of its petroleum product imports and upon Turkey and Russia for another third. Complicating the situation is the fact that subsidies paid by the government to cover domestic sales are creating a major expense for the government. The first half of 2011 has cost Damascus $2.5 billion for subsidies, the government has itself reported.

A report in the *Financial Times* on August 24 said that a number of major international oil traders and oil companies are quietly backing away from doing business with Syria as the chance of EU sanctions loom. The business daily mentioned that Vitol, Trafigura, BP, Shell and Total are main buyers of Syrian crude and the key product suppliers. It said that companies with outstanding contracts with Damascus to either buy crude or supply products expected that they would not be able to fulfill those agreements if sanctions were imposed.

The UK firm Gulfsands Petroleum announced last week a new discovery in Block 26 and stated that it plans to continue operations in Syria where its main assets are located. The statement did not mention the political unrest in the country or the EU sanctions under consideration.

On August 24 Gulfsands announced that it was in compliance with all US, EU and UK sanctions that now exist against Syria, following a report that the company was associated with President Assad's cousin, Rami Makhlouf, whose has been included in several sanction lists. Mr. Makhlouf is estimated to hold wealth of some $6 billion had holds interest in many of Syria's main companies.

Gulfsands said that it had suspended all payments to interests held by Mr. Makhlouf, who owns Al Mashrek, which in turn holds a 5.75% share in Gulfsands. The UK firm said it had suspended Al Mashrek's voting, dividend and transfer rights, and that the company is not represented on Gulfsand's board and has no influence over its decisions.