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Middle East 2020:

Shaped by or Shaper of Global Trends?



Mathew J. Burrows

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by Mathew J. Burrows

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EXECUTIVE SUMMARY

With new crises sprouting almost on a daily basis in the Middle East, there is increasing interest in knowing the possible medium- and long-term consequences of the cascading developments in the region. This report attempts to think about the *alternative futures* possible in the Middle East over the next five to ten years. This is a shorter-term forecast than usual,¹ but in the Middle East more deep-seated and structural factors are in flux than in most other regions. A longer-term forecast would allow for more optimism, but would be less useful for decision-makers who not only need a bird's eye view of where developments are headed but also a notion of the pressure points to effect positive change now.

It is difficult to discern any truly positive scenarios in the short term. For example, fixing youth unemployment and building human capital—which the region desperately needs in this increasingly competitive world—is a goal that can only be accomplished over the longer term. Instead, it is more likely that finding political solutions to the increasing conflicts will be a prerequisite to economic and social development. This is opposite from the usual pattern in other regions where economic advances have led to positive political change.

A possible “turning-the-corner” scenario exists that starts with a successful nuclear deal with Iran that could lower Sunni-Shia tensions and open the way to greater regional cooperation. This is not a far-fetched possibility, but nevertheless it is far from assured.

However, a much bleaker scenario—a so-called “sectarianism-on-steroids” outcome—appears to be unfolding during the writing of this report. The recent escalation in sectarian tensions, particularly in Iraq, increases the chances for an all-out conflict between Sunni and Shia powers, which could shatter the Middle East for a generation, similar to what happened in Europe after the First World War. One of the worst things about civil conflict is that it often sparks more violence; according to scholars, such conflicts sometimes take as long as six to nine years to wind down.

Even if the worst case does not happen, a growing “new authoritarianism” could arise in states like Egypt that are not directly involved in the sectarian conflict. Though many expected the Arab Spring to lead to democracy, support for new freedoms has diminished among the middle class who appear, for the moment, to favor stability. Even there, social and religious tensions are bubbling beneath the surface, fraying social cohesion. In this “new authoritarianism” scenario, necessary structural economic reforms will be difficult to undertake.

However troubling and detrimental the current turmoil, identifying the longer range, structural reforms—building better educational systems to teach twenty-first century skills, enhancing the environment for greater entrepreneurship and diversifying economies in the Gulf and other countries from an overdependence on energy exports—is needed more than ever. Although not sufficient in themselves so long as the sectarian conflicts continue to spread, these long-needed reforms are necessary if the region is to overcome its decades-long loss in competitiveness and finally put behind itself the deadly cycle of conflict and violence.

¹ See two previous Strategic Foresight reports, entitled *Envisioning 2030: US Strategy for the Coming Technology Revolution* (December 2013) and *Envisioning 2030: US Strategy for a Post-Western World* (December 2014).

TABLE OF CONTENTS

I. The Middle East in the Eye of the Storm	1
II. Drivers of Change	2
III. Alternative Scenarios	9

I. THE MIDDLE EAST IN THE EYE OF THE STORM

The Middle East will remain the region undergoing the greatest amount of change over the next five to ten years. Middle East futures run a wide gamut from fragile growth and development to chronic instability and potential regional conflicts. The Arab state system is under assault like never before with disintegration of some states, such as Syria and Iraq, as a distinct possibility. The economic outlook is gloomy despite rising public expectations of greater prosperity. High unemployment is coming at the worst time for regional development. Demographically, the youth bulge will remain a driving force over the next five to ten years. Such a large youthful population should be an asset, but is more likely to be a destabilizing force given the high levels of unemployment throughout practically the whole region, including the more prosperous Gulf countries. The global trend in higher food prices also poses a threat to political and social stability in several Middle East countries. For the whole region, education levels—although improving—lag those of other regions, making it more difficult for the Middle East to compete globally.

The pattern of uneven development in the Middle East is likely to continue, with the oil-producing Gulf states offering the most opportunity for their youthful populations as well as talent from other countries, and the gap between these states and the rest of the region getting worse. The financially secure oil producers will be called upon for regional leadership, while also needing to address growing demands at home. New global sources of energy, including the likely export of US unconventional sources of oil and gas, also pose a systemic threat unless the Gulf region becomes increasingly diversified.

The next five to ten years could see Iran break out of its isolation, opening up new opportunities for regional cooperation but also setting the scene for an intensified regional competition for influence. Successful negotiations limiting Iran's nuclear development to peaceful purposes under strict international supervision could start a whole new narrative, triggering a wider set of regional scenarios. Iran has many attributes—an educated population, a low birth rate, and substantial information technology (IT) capacities—that could make it competitive in the regional and global arena. A stronger Iran is likely to be seen by its neighbors in both positive and negative lights. An Iran that begins to put greater priority on economic modernization will give others some degree of leverage over it because of

Iran's desperate need for outside technological help in modernizing its energy and other industries. The recent success of sanctions shows that Iran can be brought to the negotiating table. The "carrot" as well as the "stick" are both likely to be needed in any attempt to steer Iran away from its traditional support for radical and terrorist groups. Rising powers are always disruptive and an economically stronger Iran that begins to normalize its ties with the West will likely upset "apple carts" in the region, even if Iran's behavior is more normal and less belligerent.

A breakdown in the P5+1 talks,¹ which are seeking to limit Iran's nuclear program to peaceful energy purposes, would reinforce the hardliners in the Iranian regime and a possible decision to continue pursuing nuclear weapons. A US and/or Israeli decision to take military action to forestall further development is highly conceivable. If Iran manages to become a nuclear power, an arms race in the region would trigger other powers like Saudi Arabia, Egypt, and Turkey to acquire or develop nuclear arsenals. Washington would come under increased pressure to defend its partners against Iranian aggression.

The Middle East is not just being shaped by global trends, but will most likely determine whether the rest of the world has a good or bad future. Any potential Middle East scenario has huge implications for the rest of the world. This is most obvious for the negative scenarios: a major regional conflict may not be containable and would most likely undermine prospects for the global economy too. The emergence and consolidation of terrorist safe havens—for example in a war-torn Syria and more recently Iraq—would also threaten other countries. On the other hand, situated strategically at the crossroads among Europe, Asia, and Africa, a Middle East that gets on a growth path could provide another cylinder to the global economic engine, adding hundreds of millions of middle-class consumers to the global marketplace. A more prosperous and peaceful world is not possible without a stable and secure Middle East.

1 The P5+1 refers to the five permanent members of the UN Security Council (United States, Russia, China, United Kingdom, and France) plus Germany.

II. DRIVERS OF CHANGE

The Middle East will be shaped by many of the same global trends influencing developments in other regions. Many global trends are double-edged, harbingers of progress but also destabilizing in their immediate impact. Understanding their effects and the roles they will play in the possible futures they can produce in the Middle East is the purpose of this paper.

The State under threat. Even before the Arab Spring and the civil war in Syria, the Arab state system had been weakening. It is good to remember it has been under assault before and survived, although recent challenges appear greater. The Arab state system was created in the wake of the Sykes-Picot Agreement carving up the Ottoman Empire between the United Kingdom (UK) and France, later implemented by the 1923 Treaty of Lausanne. In the 1950s through June 1967, pan-Arabism emerged under the leadership of a charismatic army officer, Gamal Abdel Nasser, president of Egypt. The emphasis on Arab identity threatened the dominant state structure and many of the ruling monarchies at that time. Yet the Nasserist ideology that emerged did not lead to the decline of the state structure, rather it embodied a strong state trying to bring other states into its own orbit, using the mantra of pan-Arab unity against Israel.

In fact, the Arab states proved resilient. The Nasser era marked much Arab state rivalry, most notably, pitting the conservative Saudi Arabia under King Faisal against Nasser. Like today's proxy war between Saudi Arabia and Iran in Syria, the 1960s featured a proxy war between Saudi Arabia and Egypt in Yemen, with the royalist, pro-Saudi faction emerging victorious after a long war of attrition. Although Nasserism contributed to the downfall of the Hashemites in Iraq, the Idriss Kingdom in Libya, and serious tensions in Lebanon, Jordan, and elsewhere, the Arab state system did not collapse. Indeed Syria—subordinated to Egypt in 1958 by the creation of the United Arab Republic—regained independence through secession in 1961.

Another assault on the Arab state system came in 1979 with the Islamic revolution in Iran. Political Islam sought to fill the vacuum left by the decline of pan-Arab nationalism, which was dealt its death blow by Israel with Nasser's defeat in the June 1967 War. Ayatollah Khomeini sought to export the revolution throughout the Arab world under the banner of Islam. But again, revolutionary Iran had limited success in overturning Arab states. The one success abroad for the mullahs was

the establishment of an Iranian foothold in Lebanon under Hezbollah in the early 1980s. Like today, Saudi Arabia led the resistance against the Iranian Islamic revolution by forging a network of Sunni Arab states that wanted to preserve, rather than overturn the regional status quo.

THE MIDDLE EAST IS NOT JUST BEING SHAPED BY GLOBAL TRENDS, BUT WILL MOST LIKELY DETERMINE WHETHER THE REST OF THE WORLD HAS A GOOD OR BAD FUTURE.

Will it be any different today? There are a number of reasons to think that the past is not a guide to the future and the weakening is more long lasting. First, the state is much weaker in terms of ensuring physical security in a number of key countries. Syria and Iraq can no longer project power within their borders, let alone outside their borders. Egypt's domestic challenges prevent it from providing strategic depth for its Gulf allies. Governments' moral authority has also weakened significantly as economic prospects have dwindled for all but a very small elite at the top. In the 1950s and 1960s, governments were largely able to provide economic security to a middle class that in return showed deference to the rulers. According to the Arab Human Development Reports, this social contract has been coming under increasing pressure since the 1970s. No longer can Arab governments "co-opt the educated youth

into what used to be a relatively well paid civil service.”² For most countries in the region, the state no longer has sufficient means, and the number of graduates angling for well-paid employment has exploded. In undertaking market liberalization in the early 2000s, the situation actually worsened with a tiny segment—many of whom were political cronies as well—benefiting from the reform. In 2008, the top ten companies on the Egyptian stock exchange were controlled by less than twenty families and some 40 percent of private sector credit went to just thirty companies.³

Iran at the center of the changing power dynamics. While some would not consider Iran as a Middle Eastern country, there is no argument that Iran is projecting considerable power and influence in the region. Iran’s growing importance derives from its relative gains in regional power as Iraq and other Arab states have grown weaker. The US war in Iraq in 2003 had the strategic effect of removing an important balance against Iranian regional hegemony, namely Saddam’s Iraq. How Iran steers a path in the next decade will affect the broader regional trajectory.

One road that Iran could take would be to focus on modernization and domestic reform. Current policies as well as the isolation caused by sanctions have hollowed out the Iranian economy and created a sea of dissatisfaction among large segments of Iranian society. An agreement with the West that enables Iran to grow its economy could create a new and positive dynamic. Alternatively, if Iran does not come to an agreement with the West, it is likely to become a wrecker of any optimistic scenario for the region. In either case, Iran is a key driver of the region’s future.

A possible change in the geopolitics of the Middle East occurred with the election of President Hassan Rouhani. The rise of the moderate wing in the wake of Rouhani’s election holds out the possibility of a successful outcome to the P5+1 negotiations. A good deal would be one that increases the break out time for any Iranian decision to develop nuclear weapons from the current few months to a few years. The United States probably won’t accept a deal that shortens the break out time to less than a year. Israel and Saudi Arabia may live with a deal that sharply limits Iran’s ability to develop nuclear weapons, but they will be dissatisfied with an agreement that permits continued uranium enrichment or fuel reprocessing.

2 United Nations Development Program, *Strategy of Response to Transformative Change Championed by Youth in the Arab Region*, p. 12, [http://arabstates.undp.org/content/dam/rbas/doc/arab_transformations1/UNDP%20Strategy%20of%20Response%20to%20Transformative%20Changes%20in%20the%20Arab%20Region-Final%20\(2\).pdf](http://arabstates.undp.org/content/dam/rbas/doc/arab_transformations1/UNDP%20Strategy%20of%20Response%20to%20Transformative%20Changes%20in%20the%20Arab%20Region-Final%20(2).pdf).

3 Tarek Osman, *Egypt on the Brink: From Nasser to Mubarak* (New Haven: Yale University Press, 2011).

The Iranian leadership, including Supreme Leader Ayatollah Ali Khomeini, may agree to limit Iran’s nuclear program in order to avoid domestic turbulence and possibly a return to 2009 street demonstrations or worse if the international sanctions are not lifted. The message from the 2013 election was that most Iranians are prepared to sacrifice the nuclear program, or at least the current pace of nuclear development, in favor of economic growth and employment.

WITH A RELATIVELY WELL-EDUCATED POPULATION WITH ONE OF THE HIGHEST LEVELS OF IT CONNECTIVITY IN THE MIDDLE EAST, IRAN COULD TAKE OFF THE SAME WAY OTHER COUNTRIES HAVE.

An agreement that demonstrates an immediate payoff by lifting sanctions could further bolster the moderates, positioning them to introduce domestic reforms, including economic liberalization. Iran desperately needs technical help to modernize its oil and gas production facilities. Increased Iranian gas exports could help diversify supplies for both European and Asian customers. Iranians outside Iran are poised to help with investment capital if the economy is opened up. In this scenario, a positive feedback loop is established that begins to steer Iran along a path toward economic development. Fifty years ago, South Korea, Israel, China, and Finland were relatively non-industrialized, scientifically unsophisticated, raw material exporters. Agricultural products, for example, constituted approximately 70 percent of Israel’s exports during the 1960s. Today, knowledge-intensive products

constitute more than 50 percent of Israel's exports. With a relatively well-educated population and one of the highest levels of IT connectivity in the Middle East, Iran could take off the same way other countries have. However, this is all predicated on Iran not breaking out of its agreement and trying to restart nuclear activities that could lead to nuclear weapons development.

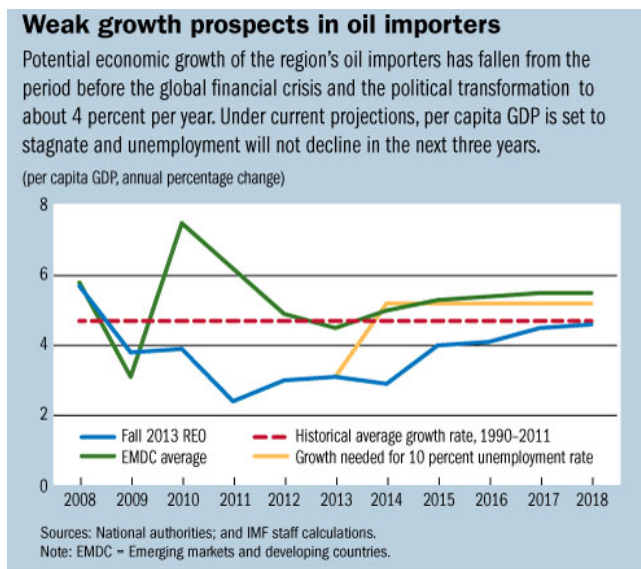
But an alternative—much less positive—scenario is equally conceivable. It is not clear to what extent the Supreme Leader and others like Qasem Soleimani—the commander of the Quds force, the external division of the Islamic Revolutionary Guards Corps (IRGC)—are willing to compromise on the nuclear issue. If negotiations trail on, it could strengthen the hand of hardliners who are not keen on an agreement in the first place. One factor against compromise is Iran's perception of the Obama administration's policy. In both the Syrian chemical weapon crisis and the ongoing Ukrainian crisis, the Administration was seen as avoiding tough action. As long as the Supreme Leader and his key hardline associates do not face an either/or choice, it may be hard to win enough hardliner support for reaching an agreement.

The longer the negotiations continue along an uncertain trajectory, the less likely is an agreement. If the West refuses to extend another interim agreement, the Iranian hardliners could use it as a pretext to end the negotiations, particularly if they see the US Congress as ready to strengthen US sanctions.

A failure is unlikely to mean that Iran and the West go back to the status quo ante. Hardliners will be strengthened. The chances of a military attack by either United States or Israel increase markedly in this scenario, particularly if Iran is seen as renewing its military program. With the moderates discredited, Tehran is likely to step up its "wrecker" behavior, arming Hezbollah and Hamas, redoubling support for Syrian President Bashar al-Assad, and backing Shia opposition groups in Gulf countries.

Also possible if negotiations break down: Iran succeeds in building nuclear weapons, other countries seek to proliferate in response, US credibility is weakened, Iran is emboldened, and several Middle East nuclear scares follow in the coming years as Iran, Israel, and the United States adjust to each other's red lines and the new nuclear balance of power. Such an extended scenario with a much higher threshold of tensions could also be crippling to the regional economy as investors shy away from any risk-taking. The global economy is also likely to be affected if such tensions increase the global price of oil.

Figure 1. Economic Outlook for MENA's Oil Importers



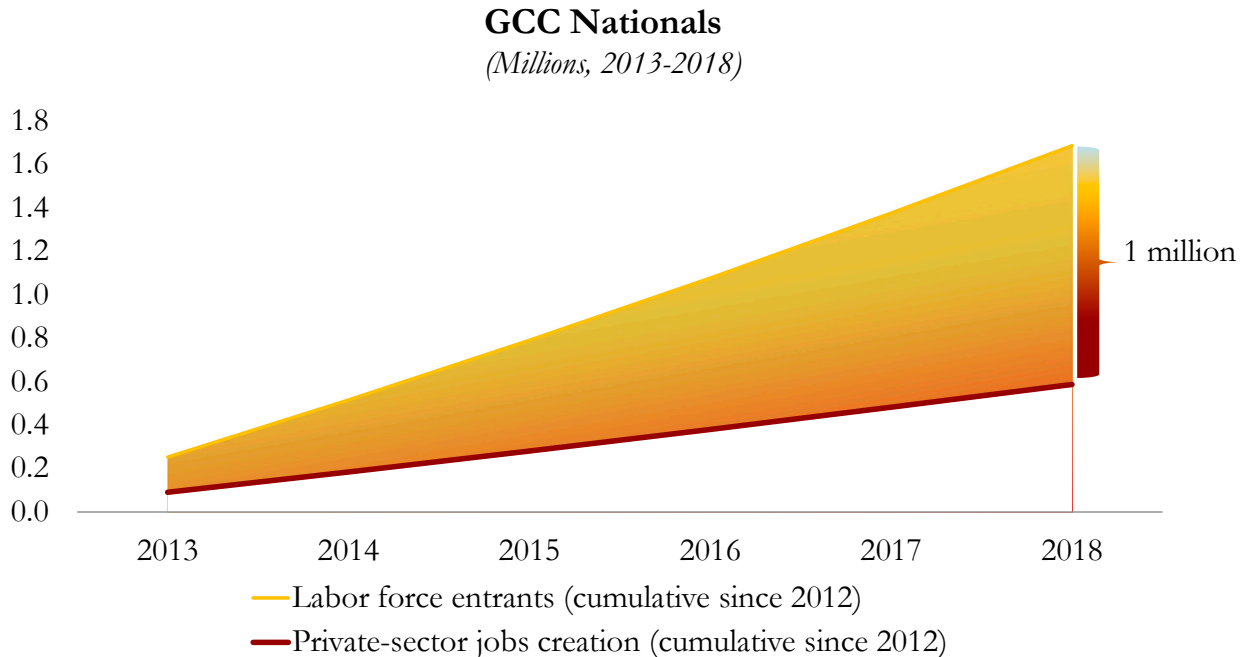
Source: International Monetary Fund, *Regional Economic Outlook: Middle East and Central Asia*, World Economic and Financial Surveys (Washington, DC: IMF, November 12, 2013), <https://www.imf.org/external/pubs/ft/survey/so/2013/CAR111213A.htm>.

The economy, stupid! If anything, the economic outlook for the region as a whole has worsened since the beginning of Arab Spring in December of 2010. While many economies may begin to improve in 2014, a rapid turnaround is highly unlikely over the next five to six years. The International Monetary Fund (IMF) expects the average economic growth in Arab countries to be lower than 4 percent in 2014. The World Bank projects weak growth through at least 2016 (its forecast period). They see growth picking up from 2.8 percent in 2014 to 3.6 percent in 2016, still significantly below 4.6 percent growth in 2010 before the Arab Spring.

Gulf Cooperation Council (GCC) countries are in a stronger position than the rest of the Middle East. According to the IMF, growth will be slower over the next few years than it has been in the recent past. Real GDP in the GCC economies was down to 3.7 percent in 2013 off from 5.2 percent in 2012 and 7.7 percent in 2011. The economies of the six Gulf Arab monarchies are now expected to expand by 4.4 percent in 2014. The IMF believes the "path of oil prices remains the main uncertainty for region." Rising US unconventional oil production is likely to reduce future demand for OPEC oil, necessitating greater efforts by the better-off Gulf countries to diversify their economies. As with the broader region, generating jobs in the private sector is a key challenge. The IMF believes some effort is already being made, but more is needed to make nationals competitive in the private labor market.⁴

4 Ibid.

Figure 2. Bleak Employment Prospects in the Gulf Region



Source: International Monetary Fund, "Middle East and North Africa Regional Economic Outlook," November 12, 2013, <https://www.imf.org/external/pubs/ft/reo/2013/mcd/eng/pdf/mreo1113p.pdf>.

According to the International Labor Organization (ILO), youth unemployment in the Middle East is more than twice the global average and the highest in the world, reaching 27.2 percent in the Middle East and more than 29 percent in North Africa in 2013. Young women are the worst hit—42.6 percent of the female labor force in the Middle East is out of work, 37 percent in North Africa. The youth labor force is expected to decline over the coming years, but this will provide only short-term relief. Long-term demographic projections indicate a return to stronger growth of the youth population by 2020, making it essential that the region develop a labor market that can utilize the new entrants and benefit from the demographic dividend.

In many Middle East and North Africa (MENA) countries, higher educational attainment surprisingly correlates with rising joblessness. According to the ILO, unemployment rates for those with tertiary education are over 43 percent in Saudi Arabia, 24 percent in the Palestinian Territories, 22 percent in the United Arab Emirates (UAE) and Morocco, 14 percent in Tunisia, and over 11 percent in Algeria. Education systems in other countries, such as Egypt and Jordan, struggle to deliver graduates with the necessary skills for finding productive jobs. Given these trends, many young people in the region are both overqualified and underqualified for available positions compared to countries in other regions at similar levels of development.

Skills mismatches in most MENA countries are worsened because the educational systems are characterized

by significant inequalities. Even more so than in the other regions, students coming from a disadvantaged background have less chance of completing their primary education. They also have a lower probability of gaining access to better quality education. Therefore, they will be less able to access university education. This inequality is aggravated by the rapid decline in public investment in education in some countries. Despite large investments in education by some of the Gulf countries, the unequal distribution and, on average, inadequate quality of education, including overcrowding in public universities, insufficient training for teachers and outdated curricula, reduce the returns that many people receive from their education and prevent the region from benefiting from the investment they have made in education.

Technology—A Bright Spot. Youth is an advantage when it comes to IT. No country in the Middle East has a median age older than thirty-one (the United States is thirty-eight, for reference) and 85 percent of Arab Internet users are younger than forty.⁵ According to Google, Saudi Arabia ranks number one globally in YouTube views per capita and the Middle East as a whole ranks second behind the United States in total views. According to a survey conducted by the American venture capital firm Kleiner Perkins Caufield & Byers, Saudis are more likely than any other nationality to

5 Zach Finkelstein, "Why the Middle East Is the Next Big Destination for Online Video," *VentureBeat*, December 20, 2013, <http://venturebeat.com/2013/12/20/why-the-middle-east-is-the-next-big-destination-for-online-video/>.

share “most things” or personal information online. In fact, nine out of ten Internet users in the Middle East peruse social networking sites daily. Middle Easterners also spend their incomes online. Forty-three percent of Internet users in the GCC countries buy products or services online each month. According to Visa, the Middle East is the fastest growing e-commerce region in the world at \$15 billion, growing 45 percent annually,⁶ although it is starting from a very low base.

Internet penetration in most Arabian Gulf countries is on par or higher than in the United States. According to a report by Frost & Sullivan, an American consulting firm, the UAE is expected to be the first country in the world to have 100 percent household broadband Internet penetration. Furthermore, consumers in the Gulf are more likely than almost any other geography to own a smartphone. Two of the top five countries by smartphone penetration are in the Gulf. This has led to a situation where 34 percent of the Saudi Arabian population and 52 percent of the UAE population use smartphones to watch TV. With few options for socializing and poor quality TV content, Arabs are turning to the Internet in droves for entertainment.⁷

All told, there are around ninety million Internet users in the Middle East, which is 40.2 percent of the total population. This means that the Middle East has a relatively low overall penetration rate although it is still higher than the global average at 34.3 percent. The most Internet users in the Middle East can be found in Iran, at forty-two million, followed by Saudi Arabia with thirteen million. The United Arab Emirates is ranked as the third-biggest online market in the Middle East. Although uneven and lagging especially in the poorer countries, Middle Eastern Internet growth is higher than in other worldwide regions.⁸

While the degree of adoption of new technologies is relatively high in parts of the region, measuring the precise economic, social, and political impact is difficult. Governments are at once eager for new technologies and often wary of their possible uses as mobilizing instruments. This ambivalence about the uses of new communications technologies, along with a shallow technological base in the region, is likely to delay and limit the transformational effects of technology relative to other regions.

Vulnerability to Climate Change. The MENA region is particularly vulnerable to climate change despite contributing relatively little—less than 6

THE MENA REGION IS PARTICULARLY VULNERABLE TO CLIMATE CHANGE DESPITE CONTRIBUTING RELATIVELY LITTLE—LESS THAN 6 PERCENT—TO GLOBAL EMISSIONS.

percent—to global emissions. It is one of the world’s most water-scarce and dry regions, with a high dependency on climate-sensitive agriculture and a large share of its population and economic activity in flood-prone urban coastal zones. According to the latest Intergovernmental Panel on Climate Change (IPCC) assessment and the World Bank, the MENA region will become even hotter and drier over the next few decades. Higher temperatures and reduced precipitation will increase the occurrence of droughts, an effect that is already materializing in the Maghreb. Syria saw a number of serious droughts in the past decade, contributing to the rural impoverishment that helped provoke the 2011 uprising. It is further estimated that an additional eighty to one hundred million people will be exposed by 2025 to water stress, which is likely to result in increased pressure on groundwater resources. Many aquifers are seeing extractions beyond their recharge potential. In addition, agriculture yields, especially in rain-fed areas, are expected to fluctuate more widely, ultimately falling to a significantly lower long-term average. Heat waves, an increased “heat island effect,” water scarcity, decreasing water quality, worsening air quality, and ground ozone formation will damage public health, and more generally lead to worsening living conditions.

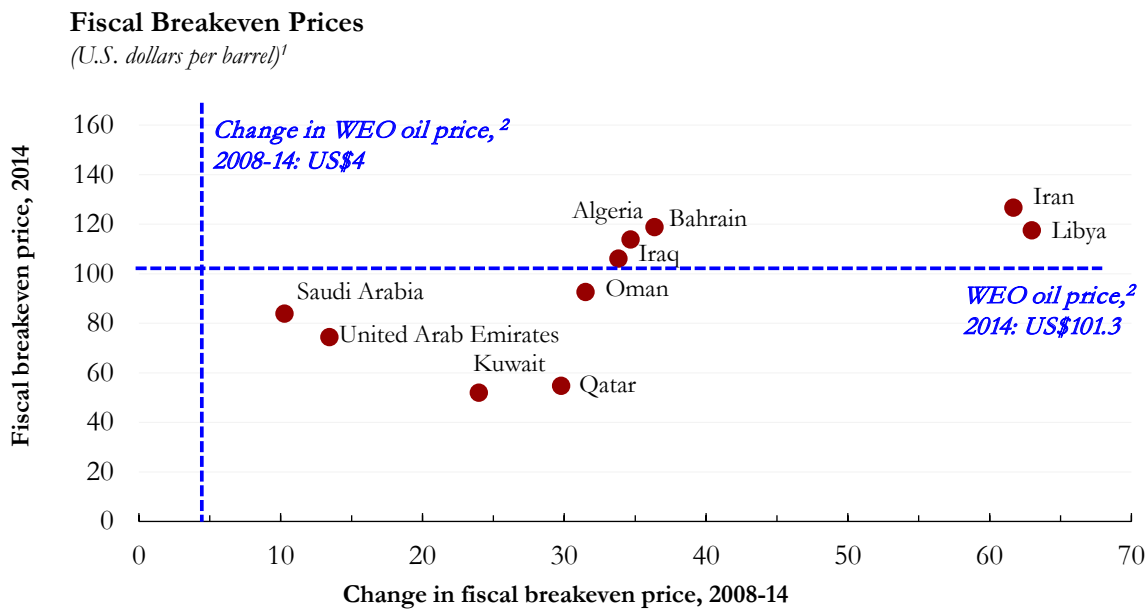
Global models predict sea levels rising from about 0.1 to 0.3 meters by the year 2050, and from about 0.1 to 0.9 meters by 2100. Low-lying coastal areas in Tunisia,

6 Ibid.

7 Ibid.

8 European Travel Commission Digital Portal, “Internet Usage, Middle East,” <http://etc-digital.org/digital-trends/connectivity/internet-usage/regional-overview/middle-east/>.

Figure 3. Government Budgets Squeezed as Oil Prices Decline



Sources: National authorities; and IMF staff calculations.

¹Yemen fiscal breakeven, 2013: US\$215 per barrel.

² Simple average of UK Brent, Dubai, and West Texas Intermediate Spot Prices.

Source: International Monetary Fund, "Middle East and North Africa Regional Economic Outlook," November 12, 2013, <https://www.imf.org/external/pubs/ft/reo/2013/mcd/eng/pdf/mreo1113p.pdf>.

Qatar, Libya, UAE, Kuwait, and especially Egypt are at particular risk. Ability to adapt to climate change phenomena is likely to depend largely on national incomes, with Gulf states better able to mitigate impacts.

Any progress tackling challenges of high unemployment and integration with the global economy could be jeopardized by climate change over the next few decades. Income and employment may be lost as a result of more frequent droughts in rural areas, and floods and sea surges in urban and coastal areas. Changes in temperature and precipitation patterns may result in damage to strategic economic sectors such as tourism or others with growth potential such as high-value-added agriculture.

Higher Food Prices Here to Stay. A number of Middle East countries are vulnerable to food price rises. Long-range forecasts suggest the trend over the past couple decades of decreasing world food prices has reversed itself, and the cost of buying food will take an increasing chunk out of consumers' household budgets, especially those of poor families. The hike in staple food prices is particularly worrisome. Wheat, which is a staple in many regions, is likely to exhibit particularly high price volatility because of significant production occurring in water stressed and climate vulnerable regions in the world. Import-dependent poor countries like Egypt could then feel the impact of food inflation.

There has been some scholarly debate about how much food price spikes contributed to the Arab Spring political uprisings. Whatever one's estimate, there is growing evidence that the upward trend in prices is reaching a point where one could see more widespread instability even absent price spikes.⁹ The well-regarded Chatham House study, *Resource Futures*, used data on food import dependency, share of income spent on food, and prevalence of undernourishment to identify countries particularly exposed to high food prices. Egypt, Algeria, Yemen, Syria, Iraq, and Jordan were among the countries in the Middle East on Chatham House's list.¹⁰ Wealthier Middle East states may be able to craft arrangements with African and Southeast Asian states to partially address food scarcity by buying or leasing large scale farmland, but the long-term prospects for greater and more efficient food production is not proven. The Chatham House study found that in "only 21 percent" of the so-called "land grabs" surveyed outside the region was farming actually started. The study warned, for example, that "growing volumes of production are effectively taken

⁹ Marco Lagi, Karla Z. Bertrand, and Yaneer Bary-Yam, "The Food Crises and Political Instability in North Africa and the Middle East," New England Complex Systems Institute, August 10, 2011.

¹⁰ Bernice Lee, Felix Preston, Jaakko Kooroshy, Rob Bailey, and Glad Lahn, *Resource Futures* (London: Chatham House, December 2012), p. 62.



Growing numbers of refugees will be a long-term liability for the region. Photo credit: Wikipedia (Creative Commons).

outside world markets and insulated from normal patterns of supply and demand.”¹¹

Energy—A Dual-Edged and Wasting Asset.

Energy is another critical resource. For poor countries lacking in their own resources, the relatively high energy prices and their volatility pose a threat to their economic recovery, according to the World Bank. For oil-importing countries like Egypt, Jordan, Morocco, and Tunisia, high oil prices have been an important factor in their growing current account deficits and debt. Electricity black-outs—especially during summer months—pose a threat to the economic recovery in countries like Egypt, Tunisia, and Jordan. For oil-rich economies, it has skewed development, led to premature deindustrialization, and reinforced the subordinate position of the Arab region in the global hierarchy of production. The process has been marked by unbalanced development within and between Arab countries that has hindered manufacturing and agricultural sectors and led to anemic growth of outlying areas.¹² Moreover, even with historically high oil prices, many countries like Algeria, Bahrain, Iraq, and Libya have found it difficult to balance between their spending and revenues. Instability has prevented Libya and Iraq from pumping their oil and getting it to market. Other oil-rich countries, such as Saudi Arabia, now need much higher oil prices to fund the recent expansion in

social welfare programs. Over time, high prices could come down as production increases from US shale oil and other expected conventional and unconventional sources. Additionally, without hikes in the domestic oil price that are needed to reduce rising domestic consumption, Saudi Arabia is on course to become a net oil importer by 2037.

Arab governments are under increasing IMF pressure to cut back subsidies on fuel and food that exacerbate budgetary pressures. Morocco has ended subsidies of gasoline and fuel oil, but continues to subsidize wheat, sugar, and cooking gas used by poorer Moroccans. In mid-2013 Egypt began implementing the first phase of a plan to cut back energy subsidies that use up around one fifth of the country’s budget. More recently, civil society activists from five Arab countries have urged the IMF to ease demands on Arab government to reduce food and fuel subsidies until stronger social-protection schemes and other basic reforms are implemented. The Arab NGO Network for Development (ANND) and the Egyptian Center for Economic and Social Rights (ECESR) argue that social safety nets in Egypt, Jordan, Morocco, Tunisia, and Yemen aren’t adequate and cutbacks in subsidies will hurt the poor and even the middle class.¹³

The Growing Threat of Conflict. Nothing can be more harmful to economic development than conflict. Conflict can set back economic development in a country

11 Ibid., p. 106.

12 United Nations Development Program, *Arab Development Challenges Report 2011: Towards the Developmental State in the Arab Region*, 2011, http://www.undp.org/content/dam/undp/library/corporate/HDR/UNDP-ADCR_En-2012.pdf.

13 Jim Lobe, “Arab NGOs Warn IMF against Sharp Cuts to Subsidies,” Inter Press Service, February 28, 2014, <http://www.ipsnews.net/2014/02/arab-ngos-warn-imf-sharp-cuts-subsidies/>.

by decades even after it concludes. Before 2005, levels worldwide of both interstate and intrastate conflict were on the downswing everywhere and were at historically low rates. The picture is now very different in the Middle East. The recent violence in Gaza is another in a string of conflicts, most notably with the civil war raging in Syria and sectarian strife in Iraq. In Egypt, the military-engineered coup against former President Mohamed Morsi killed more than two thousand people over the course of several months and at the same time Sinai-based terrorist groups have mounted a large number of attacks against the military authorities, resulting in several hundred deaths. In Libya, armed militias continue to clash and the central government lacks a monopoly over the use of force and violence. Syria is no doubt the most serious. There, the largely peaceful demonstrations that began in March 2011 were violently repressed by regime forces, which triggered an armed opposition including radical Sunni Islamist groups. There has been a growing involvement of external actors to the point that the civil war has become largely a Sunni-Shia sectarian conflict within a wider regional cold war pitting Saudi Arabia and other Sunni powers against Iran and its supporters like Lebanese Hezbollah and some Iraqi Shia militant groups.

IF SYRIA FOLLOWS THE PATTERN SIMILAR TO OTHER CIVIL WARS, IT WON'T END SOON, MEANING THAT SECTARIANISM WILL ONLY INCREASE.

The toll on Syria has been devastating, and the future does not look promising. Even if sectarianism did not cause the Syrian conflict, once the sectarian genie is out of the bottle, it is very difficult—if not impossible—to

put back in.¹⁴ If Syria follows the pattern similar to other civil wars, it won't end soon, meaning that sectarianism will only increase. According to scholars, "civil wars like this one last over nine years, on average."¹⁵ Even with support from outside states, violent campaigns in such circumstances from 1900 to 2006 had less than a 30 percent chance of succeeding. During that time, fatalities, casualties, and displacements resulting from the violence are likely to increase, leading to humanitarian catastrophe even worse than what has already transpired.

Scholars studying conflict place the risk of former conflicts reverting to conflict to be about 40 percent in the first decade after conflict termination. Even after the conflict stops, economic development tends to slow. So long as conflict continues, whatever support that exists for democratic governance is undermined. According to the April 2014 Department of State/USAID factsheet on US assistance to Syria, the number of people displaced by the civil war inside Syria is 6.5 million in addition to 2.6 million refugees outside in neighboring countries.¹⁶ In 2010, Syria was dealing with a surging population of over twenty-three million, but this has dramatically reversed. Last year, the population growth rate was 0.8 percent, and it has dropped much further since then. Syria's population is estimated to be just seventeen million by 2015, not counting further deaths and the potential for much higher emigration. Eighty-five percent of the refugees are not staying in camps but with foreign host communities, putting an "incredible strain and impact," on the region, according to the Office of the United Nations High Commissioner for Refugees (UNHCR).¹⁷ The impact of the civil war on Syria will be felt for a full generation to come and repairing the damage done—social, psychological, economic, and political—will take years.

Two other major areas of conflict could also emerge, in both cases as a result of failure of negotiations. A decision by Iran to forsake negotiations and pursue nuclear weapons could spark a major conflict. As has been seen in Gaza, so long as the Israelis and Palestinians fail to make progress toward a peace agreement, there is potential for outbreaks of major violence.

14 Benedetta Berti and Jonathan Paris, "Beyond Sectarianism: Geopolitics, Fragmentation, and the Syrian Civil War," *Strategic Assessment*, vol. 16, no. 4, January 2014, p. 30, <http://d26e8pvoto2x3r.cloudfront.net/uploadImages/systemFiles/Beyond%20Sectarianism.pdf>.

15 Erica Chenoweth and Maria J. Stephan, "Why Civil Resistance Still Works," *Foreign Affairs*, July/August 2014.

16 Numbers from "Working in Crises and Conflict: Syria," USAID website, April 14, 2014, <http://www.usaid.gov/crisis/syria>.

17 UN News Center, "Syrians Internally Displaced by War Expected to Nearly Double to 6.5 Million by Year's End—UN," February 5, 2014, <https://www.un.org/apps/news/story.asp?NewsID=47084&Cr=syria&Cr1=>.

III. ALTERNATIVE SCENARIOS

The Middle East is the region with the widest array of different futures because of the dual-edged nature of many of the drivers and the potential for devastating scenarios if conflict spreads. Three broad possible futures are outlined below. Of the three, the first one—“sectarianism on steroids”—is among the more likely and potentially the most dangerous scenario. Rising sectarianism is currently fueling internal separatist conflicts in Syria, Iraq, and Lebanon, and could end up sparking a major conflict between Sunni and Shia powers. This could spell the end of the Sykes-Picot division of the Middle East into multi-ethnic and/or mixed sectarian states. In the new Middle East in this scenario, states would tend to be a collection of autonomous regions with conflict among them almost constant. The Kurds—big losers in the post-Ottoman era of new states—could be, at last, the big winners.

A “new authoritarianism” in certain states, in part as a response to growing disorder elsewhere, is likely. Some of that is already happening in Egypt where the middle classes have drawn back from support for new democratic freedoms and appear, for the moment at least, to favor stability. An Israeli withdrawal from the West Bank gives a boost to the PA, moving it closer to becoming an actual state. With Iran’s help, Iraqi Shia would reassert power over Sunnis and Kurds.

The most positive scenario, “turning the corner,” is unfortunately the outlier in the short-to-medium term, even though this scenario’s emphasis on economic development is closer to the global norm. Investor confidence in the region is ignited with the far-reaching deal between Iran and P5+1. The efforts to diversify economically in the GCC begin to pay off. Efforts to increase energy efficiency and slow domestic consumption are put in place in GCC countries, which help in strengthening their fiscal position. The uptick in growth in GCC spills over in the broader region. Political and economic decisions are equally important and begin to create a positive feedback loop instead of political developments undermining economic prospects.

A. Sectarianism on Steroids

This scenario sees the continuation of current trends toward fragmentation and decreasing state authority, especially in Iraq, Syria, and Lebanon. With Turkey, Egypt, and Europe increasingly absorbed by domestic issues and the United States less engaged in the region, sectarian conflict between Sunnis and Shias and/or

between Kurds and Arabs could worsen, eventually sparking a major conflict in the region.

A difficult global economic outlook helps to accelerate the growing fragmentation and conflict. Oil demand begins to dip as a result of a plateauing of consumption in the emerging economies, particularly China, and increased shale production in the United States and Canada. The price of a barrel of oil dips below the “break-even” levels of many Middle East oil producers. Youth unemployment stays high, and the IMF lowers its economic forecast for both oil-consuming and oil-producing countries. A looming food crisis adds to the gloom and growing restiveness of most publics.

Syria defaults into a “soft partition” in which enclaves are not totally self-sustainable but are independent of control from Damascus. Conflict feeds on conflict. Assad is unable to finish off the Syrian rebels, who regain some lost territory in a surge. Islamist militias fight each other and with the moderate rebels and Kurds for control over villages and towns mainly in the north and east of Syria. Moderate Sunni rebels maintain control over southern Syria.

Iraq is similarly broken up along ethnic and religious lines. Islamic State of Iraq and al-Sham (ISIS) brutality increasingly alienates Sunnis under its control in the caliphate which spans the Iraq-Syria border. However, worries about retribution from the Shia forces if they reasserted control keeps the ISIS leadership in power. After lengthy negotiations, Turkey acquiesces to Kurdish independence. Economically Kurdistan remains highly dependent on Turkey for getting its oil to market and imports. Shia-held Baghdad does not recognize Kurdish independence; with the exception of Israel, most of the international community has not officially accepted its secession and still hopes that Iraqi unity can somehow be restored. Shia areas are increasingly dependent on Iran’s help for protecting them from incursion from caliphate forces.

The caliphate has called on their Sunni Arab brethren elsewhere in the Levant—not only in Syria but also in eastern Jordan—but reports of the ISIS brutality have repulsed many Sunni Arabs. Most are no longer attracted to a Sunni caliphate carved out of parts of all three countries.

Lebanon has been a weak state for decades, but the increased sectarian fighting in the region reignites a civil war. As Hezbollah remains stuck in the Syrian

quagmire buttressing Assad's forces with manpower and brainpower; Sunni jihadists in Syria and Lebanon wreak revenge on Shia civilians in Hezbollah and pro-Assad neighborhoods in Beirut, Tripoli, and elsewhere in Lebanon. Hezbollah strikes back at Sunni civilians and mosques and the sectarian civil war escalates to replicate, albeit on a smaller scale, the civil war next door in Syria. The burden of hosting the now-permanent Syrian refugee population puts immense pressure on infrastructure, public services, and state finances as well as social stability.

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Overwhelmed with Syrian refugees, the Hashemite Kingdom of Jordan is also fending off a rebellion of the Jordanian East Bankers (non-Palestinian Jordanians) who are angered at the prospect of the King granting Jordanian citizenship for Palestinians living there for nearly fifty years since the 1967 war. As a Palestinian state in the West Bank nears reality, east Jordanians fear that Jordan will become a second Palestinian state.

The growing economic crisis in the GCC encourages the Shia communities to ramp up opposition to the Sunni monarchs. The eastern provinces of Saudi Arabia, where the Shia are in the majority, stage a rebellion that shuts down oil installations for several months. Kuwait is also weakened by ineffective government and a growing

Shia/Bedouin population that upsets the tranquility of this trading state. Bahrain becomes the arena of an escalating conflict between the Shia majority and the Sunni monarchy, which oscillates between appeasement and repression. Saudi Arabia and the UAE reinforce their garrisons in Bahrain as the Quds force strengthens its Bahraini cells, which engage in periodic terrorism. Oman's Sultan Qaboos passes without an heir, leaving a power struggle that highlights Oman's own sectarian tensions. Qatar's royal family splits over whether to continue supporting certain Islamist movements, especially the Muslim Brotherhood, or to realign with Saudi Arabia.

The growing sectarianism makes it impossible for Iran and P5+1 to reach agreement. The US administration comes under Congressional pressure to end the talks as the Saudis and others accuse Iran of supporting the growing Shia rebellion in Gulf countries. The regional cold war between Saudi Arabia and Iran spreads into active conflict in several spots. One of them is Yemen, where the pro-Iranian Houthis, who are a branch of Shia, fight against the Sunni government of Sanaa supported by Saudi Arabia. Other hotspots include Bahrain, the eastern provinces of Saudi Arabia, Oman, Iraq, Syria, Lebanon, Jordan, and possibly Egypt.

As the global economy is increasingly put at risk—particularly in the wake of disruption of Saudi oil supplies—outside actors like the United States, Europe, and even China (which is highly dependent on oil supplies) try to intervene to arrest the conflicts. But the conflicts are so widely spread and involve so many different actors that achieving a peace settlement proves difficult, if not impossible.

Sectarianism on steroids aggravates preexisting tensions in the region. Conflicts are no longer compartmentalized and manageable by a withdrawn Washington. Regional economies—if not the global one—suffer major damage. Winners are hard to find in this scenario, except for the Kurds, who may be beneficiaries of the rise of ethno-nationalist entities and the decline of the Levant state system one hundred years after the Sykes-Picot Agreement gave birth to the modern Arab national state. Except for the Kurds, everyone would lose as sectarian tensions grow in a major conflict with the battleground extending across the whole central Levant region.

B. A New Authoritarianism: State Power Stages a Partial Comeback

In this scenario, economic conditions are challenging but not desperate. All Middle East economies begin to pick up with GCC economies having the best prospects for renewed growth. Youth unemployment remains high everywhere in the region, but begins to subside. GCC countries make the most progress in starting to get more nationals into private sector jobs.



The outcome of P5+1 nuclear negotiations with Iran is critical to the whole region. Photo credit: Wikipedia (Creative Commons).

Sectarian tensions increase but the ISIS victory is short lived. Sunni tribal leaders turn to the new, less sectarian Shia leaders for help against ISIS. The United States and others step up support for striking ISIS. Iran secretly cooperates with the West in the fight against ISIS. The United States puts pressure on the Saudis to begin to mend ties with Iran in view of Iranian efforts against the caliphate. A major Sunni/Shia conflict is avoided. Rather, a new authoritarianism emerges around the fringes of major Sunni/Shia tensions that is fueled in part by the fears of growing disorder. The flip side of growing sectarianism is the increasing importance of the non-Arab countries in the region, Turkey, Iran, Israel, and increasingly Kurdistan, which remain strong enough to clamp down on sources of disorder, particularly domestic ones. Turkey continues to battle Syria's Assad with Ankara extending a humanitarian corridor into rebel-held territory in northwest Syria along the Mediterranean coast and then eastward toward Aleppo. The key question for Turkey is its relations with the other two non-Arab regional powers.

Israel and Turkey—despite differences—manage to cooperate tacitly on ways to keep Assad (and Iran) from winning the civil war in Syria. Economic relations between Turkey and Iran would be energized if there was a successful nuclear deal between Iran and the P5+1.

Israel and the Palestinian Authority fail to reach a comprehensive peace and security agreement and the once-promising Kerry Framework Agreement is unable to be resuscitated. Trying to make the most of a bad situation, Israel decides to pursue Plan B. Under this initiative, Israel unilaterally withdraws from nearly all parts of the West Bank, apart from a company of Israel Defense Forces (IDF) technical personnel monitoring the Jordan Valley. The withdrawal is tacitly coordinated with the PA's assumption of control over the vacated areas, as Palestine becomes a de facto state—albeit one that does not exercise control over its borders.

The middle classes—including the unemployed youth—in the Gulf prefer stability to campaigning for greater freedom. They see the chaos elsewhere and are afraid of being similarly infected. As they seek to snuff out any Shia dissidence, the Gulf monarchies shy away from attempting any liberal experiments at home. These largely status quo regimes do not want to take any chances with democracy.

President Abdel Fattah al-Sisi of Egypt, now in his sixth year, tightens his grip. Saudi and Emirati cash continue to fund Sisi's massive arms purchases from Russia. He delays trying to reform the economy for fear of the political consequences. The army's role in the economy is strengthened.

One generic political problem facing the authoritarian regimes, even in the stable countries, is that a clamp down can only last so long before extremist blowbacks undermine these rulers. Egypt enjoys some stability into 2018, but by 2020, some warning signs reappear. Sisi's repression of the Muslim Brotherhood forces the latter underground. The Muslim Brotherhood has splintered into a violent, extremist version that regularly targets regime officials and their business cronies.

The repression of political Islam that extends from Morocco and Algeria to the Gulf begins to fracture as nonviolent Muslim Brotherhood wings regroup under new younger leadership to contest local and then national elections in Morocco, Jordan, and elsewhere. They appeal to the local population because of their entrepreneurial skills in contrast to the antibusiness, lethargic, and bureaucratic governments led by aging monarchs and ex-generals.

The other Achilles heel of authoritarian republican governments, aside from their ossification, is the absence of legitimate mechanisms of succession. Erdogan and Sisi may remain popular among their core constituencies but they are not able to guarantee continuity in any successor government, even if

succession goes smoothly. This is a problem not only for these countries but also for neighboring countries in the region like Israel and Saudi Arabia. These countries are fine in the medium term with close security ties and/or financial cooperation with Sisi's Egypt, but they dread the possibility of another succession crisis in Egypt similar to the Tahrir Square volcano that could result in a more vengeful Muslim Brotherhood coming to power.

C. Turning the Corner

Iran and the P5+1 clinch a more far reaching deal than anticipated. Iran promises to draw back from interference in the sectarian conflicts in Syria and Iraq in return for full lifting of sanctions and the Europeans' commitment to large-scale technological assistance, particularly for Iran's efforts to modernize its energy refinery and pumping facilities. The regional cold war between Iran and Saudi Arabia begins to thaw as Iran under an increasingly powerful Rouhani government shifts priorities away from revolutionary export of Islam and political hegemony in the region toward economic development. As the moderates around Rouhani gain the upper hand over the hardliners and refocus Iran toward modernization and away from confrontation, Ayatollah Khamenei dies. The new supreme leader is selected from an Assembly of Experts swayed by moderates.

Saudi Arabia and Israel are initially unhappy with the agreement, suspecting that Iran will continue to progress toward a bomb after sanctions are lifted and Iran is able to sell oil freely. Given Iran's knowledge and experience in the nuclear program, the skeptics believe that Iran will eventually break out and go for a bomb, counting on the reluctance of the international community to reinstate sanctions and stop buying Iranian oil. Over time and with prodding from the US government, these and other skeptics will see that Iran is committed to economic development. Israel opens a back channel to Rouhani, seeking reassurances against a breakout. The success of those exchanges is enough to persuade Israel to back away from planning for a military attack. For the first time, Israel sees in Rouhani a "man it can do business with." Soon, Israel is seeking to restart economic relations, which formerly flourished when the Shah was in power.

The new political détente lays the groundwork for a new phase of economic development throughout the region. Foreign direct investment begins to pour back into the region. Global growth remains moderately good, but not robust. Crude oil prices stabilize just above the "break-even" levels of GCC oil producers, spurring greater structural reforms. In an effort to shore up their fiscal balance sheets, GCC governments step up efforts to reduce energy subsidies and accelerate economic diversification. The prospect of an increasingly economically strong Iran in the absence of many

Western sanctions puts added pressure on Gulf and other Arab Middle East states to quickly undertake structural reforms in the face of the growing Iranian competition. Saudi Arabia adopts sweeping reforms including an ambitious Saudi-ization program to train its huge domestic population (not including the expatriates) with skills that can add value to the economy. The Saudi private sector begins to gain traction.

Whereas conflict has fed on itself, the far reaching Western deal with Iran prompts a ceasefire agreement in Syria. The Rouhani government is able to extricate itself from its Syrian quagmire, including pulling back Hezbollah and the Shia Iraqi brigades from Syria. Without substantial aid from Tehran and Hezbollah, the Assad regime finds it difficult to maintain the upper hand. Following the ceasefire, the United States, European Union (EU), and Russia sponsor peace negotiations. Any accord that is reached is not likely to put Syria back together as a strong, unified state. Syria resembles more a weak and divided Lebanon even though the fighting has died down.

The final element is an Egypt that moves away from clampdown toward a more moderate consensus, allowing the Muslim Brotherhood and other Islamic groups to participate in elections. The improved political environment in Egypt, accompanied by a decrease in terrorist incidents, will bring back tourism and foreign direct investment (FDI). As in Pakistan since the election of 2008, the Egyptian military retains a privileged role in security and some foreign policy, but increasingly stays outside politics. Egypt holds a contested election in 2020 in which a non-Muslim Brotherhood coalition prevails. Although these secular voices were not sufficiently organized to win elections following the Arab Spring, they have now gained enough traction to compete with the Islamists for votes.

For this optimistic scenario to occur, everything has to fall in place, beginning with agreement on the nuclear issue, a thaw in the regional cold war, an Israeli-Palestinian settlement leading to a Palestinian state, and a rapprochement between Egypt's military and Islamists. Israel and Turkey restore their warm relations as Israel builds a pipeline from its offshore oil deposits to southern Turkey. "Turning the corner" is not the most likely scenario, but it is not impossible either.

Conclusion

Scenarios one and two overlap in that both share continuing sectarian conflict and fragmentation within the core Levant region, especially Syria. In the second scenario, however, the return of authoritarianism in the periphery, including Egypt and the Gulf monarchies, may make the instability in the core areas more manageable and contained.

Also, the first scenario describes a Middle East in which Sunni-Shia sectarianism has eclipsed Islam vs. the West and the Arab-Israeli conflict as the most salient conflict in the Middle East. This is a fair description of the region today. Looking to 2020, since a major driver of rising sectarianism is the regional cold war between Saudi Arabia and Iran, the future direction of Iran will have a decisive impact on the trajectory that sectarianism takes.

Economic problems are structural and not cyclical, meaning a turnaround in the next four to five years is unlikely. At most, one is likely to see the beginnings of economic recovery toward the end of the forecasting period—so long as the needed reforms start being implemented. Without a better economic outlook, political leadership is likely to be the most important determinant of whether the Middle East future is positive or negative.

Finally, outside actors, such as the United States, Europe, and Asia, are also likely to play critical roles. Clinching a major agreement with Iran could be an important confidence-building catalyst for reorienting the Middle East on a more positive path. Should the first “sectarianism on steroids” scenario unfold, no outside actor, including the United States, could easily quell a major conflict that develops and spawns an endless number of mini-conflicts across a wide swathe of the region. Ironically, Iran is the one country where the United States and the West have more tools to bring about a positive scenario in which the region turns the corner.

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