

## ADVERSE CONSEQUENCES OF IRANIAN-U.S. TENSIONS



Increasing tensions between Iran and the United States are having wide ranging effects including: increasing conventional arms sales to Arab allies of the United States, creating a drag on the U.S. economy through higher oil prices, increasing the demand for Canadian tar sands, consequently causing additional emissions of greenhouse gases into the atmosphere, spurring calls for U.S. missile defense deployments, harming the U.S.-Russia relationship, and slowing down or possibly derailing further U.S.-Russia nuclear arms reductions. The source of animosity between Iran and the United States is not just the Iranian nuclear program, but this is arguably the main point of contention. Other issues include Iran's influence on the Iraqi government, Iran's support of Hamas, and in general Tehran's power projection throughout the Persian Gulf region. While there are no easy solutions, the issues I want to call attention to here are the several adverse consequences that have already arisen because of the impasse between Iran and the United States.

U.S. government officials have encouraged and approved more conventional military sales to Arab allies such as Saudi Arabia and the United Arab Emirates in order to counter the perceived growing military and political threats from Iran. According to a recently published Congressional Research Service report, U.S. arms sales to Saudi Arabia grew from \$4.2 billion in 2003-2006 to \$13.8 billion in 2007-2010 and such sales to the UAE increased from \$1.4 billion in 2003-2006 to \$10.4 billion in 2007-2010.<sup>2</sup> While not all of these sales can be attributed to these states' concerns about Iran, the perceived threat from Iran increased during those time periods as Iran built up its uranium enrichment program and ballistic missile capabilities. The Iranian threat has resulted in a windfall profits for U.S. defense contractors.

While it is highly uncertain as to how much the Iranian threat has pushed up the price of a barrel of oil, it is better known how much an increase in oil prices affects the costs that U.S. consumers pay. Rather than give a full accounting of these costs here, I will simply point out that according to Chris Lafakis, an energy and financial markets economist at Moody's Analytics, that the \$18.50 increase in oil in early 2011 if sustained over the full year would cost U.S. consumers \$20.4 billion just in higher home heating oil and diesel prices and would cost an additional \$46.3 billion in higher gasoline prices. This does not include higher food costs. Oil prices have recently been in the \$90 to \$110 per barrel range. Iranian leaders have warned that draconian sanctions imposed on their country would spike oil to \$250 per barrel.<sup>3</sup> While most Western analysts disagree, there appears to be widespread agreement among energy analysts that a war with Iran could cause oil to double in price. This could have hundreds of billions of dollars worth of economic harm to the U.S. economy if sustained over a long period of time.

High oil prices have made the Canadian tar sands very profitable. It can cost about \$30 per barrel to extract oil from these sands. Thus, the price for a barrel of oil has to be significantly above this threshold for this method to compete with so-called easy oil extraction. But “easy” oil has become scarce and has reached peak production in many parts of the world, especially the United States. And as worldwide demand for oil increases, oil companies are turning more and more to the hard to extract oil deposits. But oil sands extraction is an energy intensive process that releases more greenhouse gases to the environment as compared to “easy” oil extraction. Another environmental concern is that tar sands underlie more than 140,000 square kilometers of Canadian forests.<sup>2</sup>

Returning to the problem of direct threats from Iran, proponents of missile defense have called for a robust defense against Iran’s ballistic missiles although Iran has yet to develop intercontinental range missiles. To begin to counter this threat, in March, the Obama administration deployed the USS Monterey, equipped with missile interceptors to the Mediterranean Sea. This deployment represents the initial part of phase 1 of the proposed four phase system. As Yousaf Butt and Theodore Postol have assessed in an FAS Special Report, the later phases could conceivably be perceived as a threat to Russian ballistic missiles although they caution that the missile defense system remains will likely confront major technical challenges against realistic missile threats.<sup>3</sup> Nonetheless, the deployment of a U.S. missile defense system has already stimulated heated rhetoric from Russian leaders, who may be mostly playing to a domestic audience when they have suggested that they may withdraw from New START, the latest U.S.-Russia nuclear arms reduction treaty. Even if Moscow continues with adhering to New START, further arms reductions are in jeopardy if the United States and Russia cannot work together to resolve the tensions over missile defense and Iran.

As you have undoubtedly noticed, the fall issue of the PIR is appearing just at the official start of winter. I apologize for this delay. The editorial staff at FAS consists of only two people and they have several other duties at FAS. They are committed to increasing the quality and length of the PIR. I hope you will have noticed that the length of each issue is two to three times the length of issues prior to 2011. On behalf of the editorial staff, I am very grateful for your support of FAS.

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<sup>1</sup> Richard F. Grimmett, “U.S. Arms Sales: Agreements with and Deliveries to Major Clients, 2003-2010,” Congressional Research Service Report, December 16, 2011.

<sup>2</sup> Rick Gladstone, “Iran, Facing New Sanctions, Warns of Oil at \$250 a Barrel,” *New York Times*, December 5, 2011.

<sup>3</sup> Giuseppe Marconi, “Are Canadian Tar Sands Profitable?” Oil-Price.net, January 27, 2010.

<sup>4</sup> Yousaf Butt and Theodore Postol, “Upsetting the Reset: The Technical Basis of Russian Concern Over NATO Missile Defense,” FAS Special Report No. 1, September 2011.