

The NATIONAL INTEREST FOUNDATION

Saudi Arabia and Russia Wage a Price War over Oil Costs

Saudi Arabia has initiated a price war on oil exports, after Russia rejected a proposal from its OPEC partners to cut supply. The oil conglomerate OPEC was attempting to slash its supply of crude oil by 1.5 million barrels per day, to prop up prices amid uncertainty from the coronavirus. Russia rejected this proposition, sensing that it could profit off of the world economy's downward trend. In retaliation, Saudi Arabia cut its oil exporting price by roughly 10% in order to undercut Russian prices. The effect of the price war is already beginning to have a significant impact on the world's oil market, with prices in the United States alone reaching a four-year low.

The conflict between Russia and Saudi Arabia comes after the relationship between OPEC and Russia imploded. OPEC is comprised of 14 nations, primarily in the Middle East, Africa, and South America. Since 2017, the conglomerate has been carefully regulating the supply of oil to keep prices stable. Russia is not a member of OPEC, but has worked in tandem with the organization to moderate the world's oil supply. This partnership fell apart after talks in Vienna earlier this week, with Russia refusing to accept another supply cut. Immediately in the aftermath of this decision, oil prices in the United States crashed by 34% as traders expected a boom in supply.

Russia's decision not to cut their supply of oil indicates a willingness to accept a small recession in the short term with a view to claiming a larger supply of the world's oil market in the long term. Russia's economy is more diverse than Saudi Arabia's, and is therefore better able to absorb a loss in oil revenue in the short term, as the impact of the coronavirus is felt in the world's markets. Conversely, Saudi Arabia's economy is much more inelastic, and oil prices need to be roughly \$80 per barrel for Saudi Arabia to finance its government spending. Currently, prices in the United States are hovering around \$27 per barrel, which has led to uncertainty in Saudi Arabia. Saudi leadership is hoping that by cutting its prices, it will retake some of the market share from Russia.

The impact of the price war was felt immediately on the stock market. Crude oil prices plummeted by 20%, and the Dow Jones Industrial Average crashed over 2,000 points. Additionally, trading was temporarily suspended as losses mounted. Oil stocks Chevron and Exxon Mobil dropped by 10% and 9% respectively, as the market adjusted to the flood of supply provided by Russia and Saudi Arabia. The shock on oil would have had an impact on the market regardless, but the continued spread of the coronavirus has compounded the damage.