FOREIGN POLICY RESEARCH INSTITUTE

RUSSIA-SAUDI ARABIA OIL COOPERATION:

THE RISE OF OPEC+?

RUSSIA POLITICAL ECONOMY PROJECT

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COVER: Oil Pumps. Source: Adobe Stock

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About the author

Nicholas Trickett is an Associate Scholar in the Eurasia Program at the Foreign Policy Research Institute and Editor-in-Chief of FPRI's BMB Russia. He is also acting Editor-in-Chief for Global Risk Insights, and has written for *The Diplomat*, *Aspenia*, the *Washington Post*, and *Oilprice*, among other outlets. Trickett received a BA in Comparative Literature and Philosophy from Haverford College, an MA in Russia and Eurasian Studies from the European University in St. Petersburg, and is currently an MSc student in International Political Economy at the London School of Economics and Political Science. His research has focused on Russian energy security, foreign policy, and the intersection of its political economy at home with its international economic interests, namely energy and trade infrastructure.

Executive Summary

Nicholas Trickett

The Russian Federation and the Kingdom of Saudi Arabia, the world's leading oil exporters, were rocked by the collapse of oil prices in 2014. They both initially responded by trying to retain their positions on key export markets. But by December 2016, they had reached an agreement to coordinate production cuts with the Organization of the Petroleum Exporting Countries (OPEC) in hopes of restoring balance to the market. This year has seen both countries state their intentions to form a longer-term partnership and to continue coordination into the future, sparking concern that the two have formed a political entente of sorts. However, a close consideration of the context in which the two states agreed to cooperate suggests it is markets, not politics, that drive cooperation.

Rising shale production in the United States, political risks to oil markets created by sanctions on oil production in Russia, Iran, and possibly Venezuela and differing political interests in the Middle East suggest that energy cooperation is not, at its root, political. Even if Russia continues to coordinate production with OPEC in the longer term, this so-called OPEC+ will likely face the same market challenges that OPEC has faced since the 1980s, with shifts in price, demand, and non-OPEC+ production affecting the market. Oil prices are likely to remain volatile, creating a boom-and-bust cycle for oil markets and Russia-Saudi ties.

The Domestic Roots of the Russia-Saudi Agreement on Production

The Russian Federation's outreach to the Kingdom of Saudi Arabia has earned considerable interest, particularly as Russia steadily increased its diplomatic, military, and economic engagement with the Middle East. As noted by Dmitri Trenin, the "drivers of the Kremlin's policies in the Middle East are geopolitical."[1] It is often assumed that an emergent oil entente between two of the world's top three hydrocarbon producers is also geopolitical, particularly given U.S. interests.

But the doomsday political scenario[2]—an Organization of the Petroleum Exporting Countries+ (OPEC+) including Russia that controls the oil market—mistakes economic circumstance for grand strategy. Russia and Saudi Arabia may make political overtures when convenient, but their cooperation is dependent on broader market conditions neither can control. While cooperation may serve political ends for both states, political cooperation regarding oil production is most likely to follow the boom-and-bust cycle of the oil market as the countries' firms continue to compete.

In 2014, oil prices tumbled from around $110 per barrel in January to under $60[3] by the end of December. Markets destabilized along with budgets and production outlooks. Supply and demand dynamics triggered the rapid drop[4] in prices. The U.S. added 3.5 million barrels per day[5] of production thanks to tight oil, more commonly called shale,[6] between 2008 and 2014. Rising U.S. production outpaced rising demand, which further slowed down in 2014-2015, falling hundreds of thousands of barrels per day[7] short of initial projections from the International Energy Agency (IEA). This coincided with increases in production

1 Trenin, Dmitri. *Russia in the Middle East: Moscow's Objectives, Priorities, and Policy Drivers*. Carnegie Endowment for International Peace, 2016.

2 Bordoff, Jason. "This Isn't Your Father's OPEC Anymore." *Foreign Policy*. June 26, 2018. Accessed July 15, 2018. https://foreignpolicy.com/2018/06/26/this-isnt-your-fathers-opec-anymore/.

3 Breul, Hannah. "Crude Oil Prices down Sharply in Fourth Quarter of 2014." Energy Information Administration. January 6, 2015. Accessed August 20, 2018. https://www.eia.gov/todayinenergy/detail.php?id=19451.

4 OPEC Newsroom. "Saudi Energy Minister Says OPEC Invites Russia to Join as Observer." *Reuters*. June 23, 2018. Accessed July 28, 2018. https://www.reuters.com/article/us-oil-opec-saudi-russia/saudi-energy-minister-says-opec-invites-russia-to-join-as-observer-idUSKBN1JJ0KX.

5 "Tight Oil Test: U.S. Production Growth Remains Resilient Amid Lower Crude Oil Prices." *IHS Markit*. November 20, 2014. Accessed September 28, 2018. http://news.ihsmarkit.com/press-release/energy-power/tight-oil-test-us-production-growth-remains-resilient-amid-lower-crude-oi.

6 Oil produced from petroleum-bearing formations with low permeability such as the Eagle Ford, the Bakken, and other formations that must be hydraulically fractured to produce oil at commercial rates. Shale oil is a subset of tight oil.

7 Zhdannikov, Dmitry, and David Sheppard. "IEA Sees 2015 Oil Demand Growth Much Lower, Supply Hitting Prices." *Reuters*. October 14, 2014. Accessed August 20, 2018. https://www.reuters.com/article/us-iea-oil/iea-sees-2015-oil-demand-growth-much-lower-supply-hitting-prices-idUSKCN0I30TD20141014.

outside the U.S. and Saudi Arabia as well.[8]

Long-term trends were also at issue. Demand was not just short for 2014. It was trending lower[9] than expected for the foreseeable future, pushing down price predictions. Russian and Saudi budgets and policies had to adjust.

Saudi Arabia was projected to balance its budget for the first time since 2005 in 2014, with an estimated 90%[10] of revenues coming from oil assuming Brent crude traded at $71 for the year. Russia assumed that Brent crude would trade at $100 per barrel[11] for its 2014 budget and the initial 2015 budget. Oil and gas revenues account for roughly 30% of Russia's consolidated budget, and the figure ticks slightly higher because taxes on corporate profits in the sector are not labeled oil and gas revenues.[12] Russia's dollar earnings are vital to help finance firms' foreign debt, so the comparative percentage for spending doesn't quite capture the importance of revenues.

In Saudi Arabia's case, the price collapse forced the adoption of a less optimistic $60 per barrel baseline.[13] Though its budget was much more heavily exposed to price fluctuations than Russia's, Saudi Arabia had nearly $780 billion

8 Manescu, Cristiana, and Galo Nuno. "Quantitative Effects of the Shale Oil Revolution." *ECB Working Paper Series* (September 2015). Accessed August 25, 2018.

9 Stocker, Marc. "What Triggered the Oil Price Plunge of 2014-2016 and Why It Failed to Deliver an Economic Impetus in Eight Charts." *World Bank*. January 01, 2018. Accessed July 28, 2018. http://blogs.worldbank.org/developmenttalk/what-triggered-oil-price-plunge-2014-2016-and-why-it-failed-deliver-economic-impetus-eight-charts.

10 *Saudi Arabia's 2014 Budget*. Jadwa Investment, 2013. 1-12.

11 CEIC. "Federal Budget Execution in 2014 and Targets for 2015-2017." Global Economic Data, Indicators, Charts & Forecasts. October 08, 2014. Accessed June 28, 2018. https://www.ceicdata.com/en/blog/federal-budget-execution-2014-and-targets-2015-2017.

12 Sabitova, Nadia, and Chulpan Shavaleyeva. "Oil and Gas Revenues of the Russian Federation: Trends and Prospects." *Procedia Economics and Finance* (2015): 423-28.

13 Torchia, Andrew. "Saudi 2015 Budget Based on Oil Price around $60 - Analysts." *Reuters*. December 28, 2014. Accessed July 4, 2018. https://www.reuters.com/article/saudi-budget-idUSL6N0UB01U20141228.

in foreign reserves[14] as of April 2015. Oil and mineral fuels account for nearly 80% of the Kingdom's exports, meaning its economy was more effectively dollarized than Russia's. The Saudi Arabian Monetary Agency (SAMA) could easily distribute these dollars into the banking system,[15] though maintaining the riyal's dollar peg was costly.

Saudi Arabia had reduced its domestic debt to 1.4% of gross domestic product (GDP), accumulated a large number of assets abroad, and retained a large borrowing capacity.[16] Capital flight was an issue,[17] and the Kingdom could not feasibly abandon the riyal's peg to the dollar because of how dependent it was on imports for its oil sector.[18] These imports are largely priced in dollars, and any devaluation would have likely prompted further capital flight and a loss of investor confidence.

Though the budget deficit climbed to $67.2 billion by early 2015, the Kingdom was willing to offer financial bonuses to the population to buy support and stimulate consumption.[19] Currency reserves could not last forever, however. Riyadh had spent over a third of its reserves by November 2017[20]—clearly an unsustainable pace—and had financed much of its growing budget deficit by using its foreign assets.[21] Clearly, the riyal's dollar peg couldn't be maintained forever at high rates of spending currency reserves.[22]

Russia was also straining. Lower oil prices put pressure on the ruble since oil accounted for about 50% of the value[23] of Russia's exports and lowered natural gas prices, reducing the supply of dollars for Russia's economy. Capital outflows more than doubled in 2014 to $151.5 billion[24] from sanctions post-Crimea and Donbas, causing a depreciation of the value of the ruble.

The Central Bank had spent $70 billion in foreign currency reserves by the beginning

14 Farrell, Sean. "Saudi Arabia Can Last Eight Years on Low Oil Prices, Says Former Adviser." *Guardian*. January 19, 2015. Accessed August 18, 2018. https://www.theguardian.com/world/2015/jan/19/saudi-arabia-last-eight-years-low-oil-price-adviser.

15 Kaminska, Izabella. "Busting Currency Pegs, Saudi Arabia EditionBusting Currency Pegs, Saudi Arabia Edition." *Financial Times Alphaville*. February 6, 2018. Accessed August 19, 2018. https://ftalphaville.ft.com/2015/02/06/2115381/busting-currency-pegs-saudi-arabia-edition/.

16 Fattouh, Bassam. *Oil Market Dynamics: Saudi Arabia Oil Policies and US Shale Supply Response.* The Oxford Institute for Energy Studies, University of Oxford. March 18, 2014. Accessed August 4, 2018. https://www.oxfordenergy.org/wpcms/wp-content/uploads/2015/03/Oil-Market-Dynamics-Saudi-Arabia-Oil-Policies-and-US-Shale-Supply-Response-.pdf.

17 Megaw, Nicholas. "Financial Times Saudi Capital Flight 'overshadowing' Reform Efforts – BAML." *Financial Times*. January 11, 2017. Accessed July 2, 2018. https://www.ft.com/content/5f46a16b-4404-336c-8c02-a6dda4b96e20.

18 Ellyatt, Holly. "Will Saudi Arabia Now Abandon Its Dollar Peg?" *CNBC*. December 29, 2015. Accessed October 3, 2018. https://www.cnbc.com/2015/12/29/will-saudi-arabia-now-abandon-its-dollar-peg.html.

19 Hubbard, Ben. "Saudi King Unleashes a Torrent of Money as Bonuses Flow to the Masses." *New York Times*. February 19, 2015. Accessed October 10, 2018. https://www.nytimes.com/2015/02/20/world/middleeast/saudi-king-unleashes-a-torrent-as-bonuses-flow-to-the-masses.html.

20 Hubbard, Ben, and David D. Kirkpatrick. "The Upstart Saudi Prince Who's Throwing Caution to the Winds." *New York Times*. November 14, 2017. Accessed June 5, 2018. https://www.nytimes.com/2017/11/14/world/middleeast/saudi-arabia-mohammed-bin-salman.html.

21 *Saudi Arabia's 2015 Fiscal Budget*. Jadwa Investment, 2014, 1-13

22 Evans-Pritchard, Ambrose. "Saudi Riyal in Danger as Oil War Escalates." *Telegraph*. December 28, 2015. Accessed September 22, 2018. https://www.telegraph.co.uk/finance/economics/12071761/Saudi-riyal-in-danger-as-oil-war-escalates.html.

23 Aleksashenko, Sergey. "The Ruble Currency Storm Is Over, but Is the Russian Economy Ready for the next One?" *Brookings*. July 29, 2016. Accessed August 1, 2018. https://www.brookings.edu/blog/up-front/2015/05/18/the-ruble-currency-storm-is-over-but-is-the-russian-economy-ready-for-the-next-one/.

24 Afp. "Russia Capital Flight More than Doubled in 2014 to $151 Bn." *Business Insider*. January 19, 2015. Accessed August 2, 2018. https://www.businessinsider.com/afp-russia-capital-flight-more-than-doubled-in-2014-to-151-bn-2015-1.

of November, $29 billion in October alone.[25] The $87 billion National Welfare Fund, one of two created by Alexei Kudrin using oil and gas revenues, was tapped[26] to invest into infrastructure due to the effects of capital flight and sanctions risks on investment. Financial sanctions in particular also bit as they significantly hindered the ability of state firms and banks to borrow from the West, leading to a financial crisis by December 2014.[27] Firms now under financial sanctions also owed as much as $130 billion in foreign loan payments.[28] Only the Central Bank could provide the currency needed to cover debts, and it needed to tap into the $400 billion in reserves available at the end of 2014.[29]

The structure of Russia's currency reserves proved a problem.[30] The Central Bank included currency reserves held in the National Welfare Fund and its sister Reserve Fund, both of which were tapped for spending needs; some was held in gold, and much of the foreign exchange reserves were needed to cover short-term debts. Defending the currency was becoming too costly.

Through a combination of informal capital controls,[31] the Central Bank's decision to let the ruble float, and its choice to raise interest rates 6.5 points to 17.5%,[32] Russia was ultimately able to ride out the worst of the financial effects of the oil price collapse and sanctions. The economy went into recession, wages fell, inflation ran high, and spending had to be cut to bring the deficit down.[33]

Memories of the 1998 default and concerns that foreign powers might use debt as a policy instrument—a prescient concern given more recent talk in Washington about sanctioning sovereign debt—meant Russia refused to issue debt to finance budget deficits despite maintaining a low debt-to-GDP ratio.

Spending was slashed. State expenditures stood at 18.4 trillion rubles in 2014 and declined to 16.7 trillion rubles in 2015.[34] The 2016 figure declined slightly further to 16.4 trillion rubles, and further cuts were needed to avoid adding much to the national debt. By the end of 2015, higher prices were needed to restock currency reserves used for various domestic policy ends.

25 "Ruble Tumbles as Russia Limits Currency Controls." *CNBC*. November 05, 2014. Accessed September 1, 2018. https://www.cnbc.com/2014/11/05/ruble-tumbles-as-russia-limits-currency-controls.html.

26 Kelly, Lidia. "Russia Dips into Pension Fund in About-turn for Putin." *Reuters*. June 20, 2014. Accessed August 4, 2018. https://uk.reuters.com/article/uk-russia-economy-spending-analysis/russia-dips-into-pension-fund-in-about-turn-for-putin-idUKKBN0EV1A720140620.

27 *The Economic and Financial Crisis in Russia: Background, Symptoms and Prospects for the Future*. Report. OSW Center for Eastern Studies. Warsaw: Ośrodek Studiów Wschodnich Im. Marka Karpia, 2015.

28 Kramer, Andrew E. "Russia's Steep Rate Increase Fails to Stem Ruble's Decline." *New York Times*. December 16, 2014. Accessed September 22, 2018. https://www.nytimes.com/2014/12/17/business/russia-ruble-interest-rates.html.

29 «Международные резервы Российской Федерации. [International reserves of the Russian Federation]." Central Bank of Russian Federation. Accessed October 16, 2018. http://www.cbr.ru/hd_base/mrrf/mrrf_7d/.

30 Pfeifer, Ezekiel. "Russia's Currency Reserves: More than Enough or Alarmingly Low?" *Institute of Modern Russia*, July 27, 2015. Accessed October 03, 2018. https://imrussia.org/en/economy/2362-russias-currency-reserves-more-than-enough-or-alarmingly-low.

31 Kelly, Lidia. "Informal Capital Controls Arrest Russian Ruble's Slide." *Reuters*. December 23, 2014. Accessed June 6, 2018. https://www.reuters.com/article/us-russia-crisis-rouble/informal-capital-controls-arrest-russian-rubles-slide-idUSKBN0K10KD20141223.

32 Elliott, Larry. "Russian Central Bank Raises Interest Rate to 17% to Prevent Rouble's Collapse." *Guardian*. December 15, 2014. Accessed July 1, 2018. https://www.theguardian.com/world/2014/dec/15/russia-interest-rate-rise-17pc-rouble-collapse-oil-price.

33 Koptyubenko, Dmitri, Elena Malsheva, Yana Milyukova, and Aleksandr Bikbov. "В бюджете 2016-2018 обнаружилась дыра в 1,5 трлн рублей [In the 2016-2018 budget, a hole of 1.5 trillion ruble was found]." *RBK*. April 13, 2015. Accessed July 3, 2018. https://www.rbc.ru/economics/13/04/2015/552bb9089a7947529ab0f801.

34 Tkachev, Ivan, Anna Zeiman, Igor Moiseev, and Vladislav Shishkov. "Исследование РБК: потерянное десятилетие российского бюджета [RBC Study: The Lost Decade of the Russian budget]." *RBK*. December 9, 2016. Accessed September 28, 2018. https://www.rbc.ru/economics/09/12/2016/584824c89a79474012386691.

Post-Price Collapse Oil Strategy

This initial period was marked by market competition between Russia and Saudi Arabia. Prices fell off a cliff in late November 2014 when Saudi Arabia blocked a potential OPEC production cut.[35] Riyadh then raised production to lower prices, hoping to freeze investments into more expensive oil reserves. Russia's Arctic investments and shale projects were affected. The principle aim of the strategy was to seize as great a share of the market[36] as possible.

Saudi Arabia's concerns about revenues—aided by higher prices—still came first, but it wagered it should inflict short-term pain since it could not stop other producers from trying to increase production.[37] Breakeven prices—the point at which production from an oilfield breaks even financially after adding up all costs—vary country-by-country and field-by-field. National tax regimes and spending obligations related to how oil revenues are collected also affect breakevens. Comparisons are imperfect due to exchange rates, but Saudi Arabia has lower costs than Russia or U.S. shale producers.

Lower prices would then interrupt investment elsewhere. Deloitte estimated that the industry as a whole needed $2.7 trillion of investments outside of the Middle East between 2016-2020 to ensure long-term sustainability.[38] The investment cycle for an oilfield lasts decades. Extreme price volatility therefore stifles investments, particularly since as much as 80% of all spending goes into maintaining output at existing fields. Saudi Arabia's aim was to disrupt just enough investment to return firms' priorities to lower-cost fields, where Saudi Aramco maintains a competitive advantage.

Production increases starting in 2014 were led by the U.S. and Saudi Arabia, with Russian production rising more modestly. Russia's oil sector surprised Brussels and Washington. Sanctions on financial access to Western banks, the import of offshore and shale-relevant technologies and services, and lower prices all should have hindered production. But other factors allowed Russian firms to compensate in the short term.

Russia's companies invest domestically in rubles, but sell oil in dollars, which offsets some effects of lower prices and the ruble's devaluation. Improvements in horizontal drilling enabled increased output and lowered production costs. Overall, growth was achieved from existing fields, and the presence of "low hanging fruit" in the form of oilfields that remained developable despite a

35 Lawler, Alex. "Saudis Block OPEC Output Cut, Sending Oil Price Plunging." *Reuters*. November 28, 2014. Accessed June 2, 2018. https://www.reuters.com/article/us-opec-meeting/saudis-block-opec-output-cut-sending-oil-price-plunging-idUSKCN0JA0O320141128.

36 Kaminska, Izabella. "Why Saudi Arabia's Best Bet May Be to Increase Output." *Financial Times Alphaville*. October 27, 2014. Accessed September 28, 2018. https://ftalphaville.ft.com/2014/10/27/2020412/why-saudi-arabias-best-bet-may-be-to-increase-output/.

37 Fattouh, *Oil Market Dynamics: Saudi Arabia Oil Policies and U.S. Shale Supply Response.*

38 Deloitte. *Short of Capital? Risk of Underinvestment in Oil and Gas Is Amplified by Competing Cash Priorities.* Deloitte Center for Energy Solutions. Deloitte Development LLC., 2016.

lack of external financing or technology.[39]

Though Russia's oil sector proved resilient to sanctions, it wasn't the primary reason why Saudi Arabia's response backfired. Going into 2016, the average marginal cost of production for the oil industry dropped, making extraction sustainable around a price of $60 per barrel for most producers.[40] Production costs for U.S. tight oil dropped as well. By 3Q 2015, the U.S. Federal reserve estimated that tight oil producers could sustainably produce in the $50-75 range to break even on investments.[41]

As U.S. tight oil producers' costs dropped, the likelihood that Saudi Arabia could reduce investment into tight oil by raising production diminished. Russian firms had also managed to increase production because their relative costs in rubles had declined. Worse yet, lower price projections and lower demand did not affect expectations about higher U.S. tight oil production.[42] The prices necessary to drive out competitors from the market were below what Russia and Saudi Arabia's budgets could sustain.

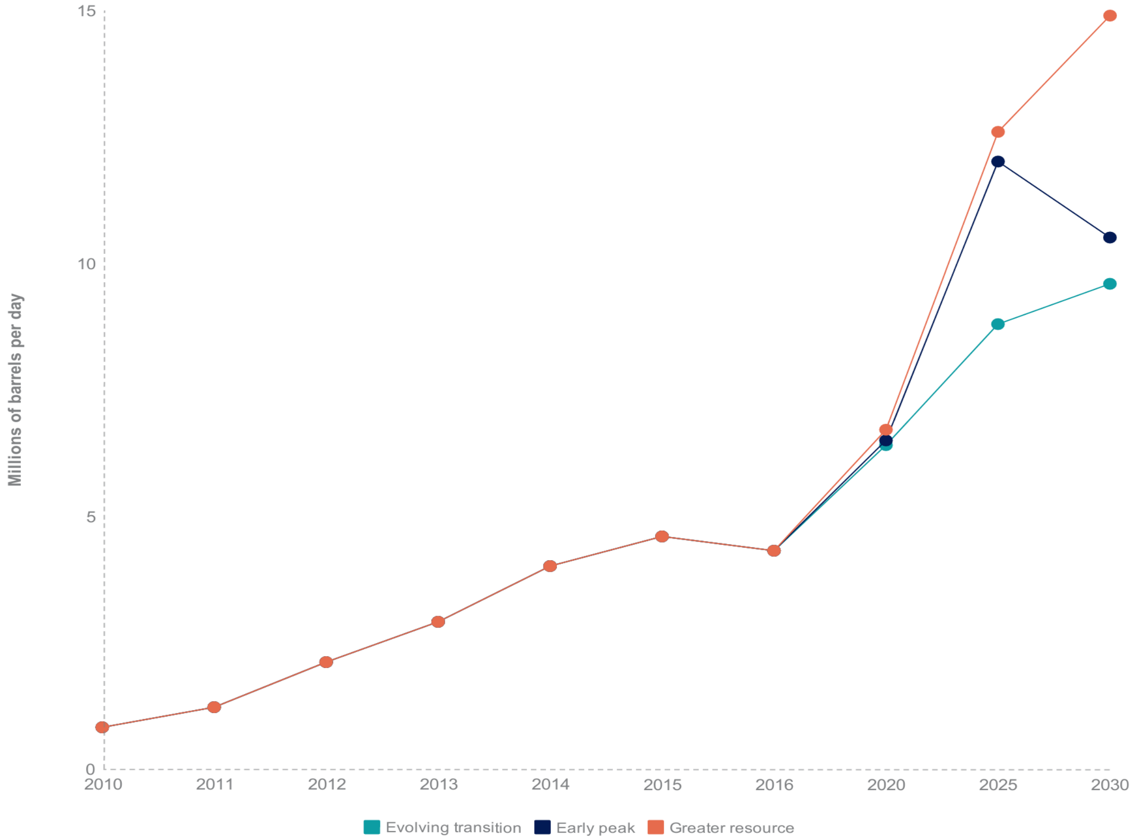
39 Henderson, James, and Ekaterina Grushevenko. *Russian Oil Production Outlook to 2020.* The Oxford Institute for Energy Studies, University of Oxford. February 2017. Accessed June 4, 2018. https://www.oxfordenergy.org/wpcms/wp-content/uploads/2017/02/Russian-Oil-Production-Outlook-to-2020-OIES-Energy-Insight.pdf.

40 Davis, Carolyn. "Marginal Costs to Produce Fall Sharply But Higher Oil Price Still Imperative, Bernstein Says." *Natural Gas Intelligence Shale Daily*. May 20, 2016. Accessed June 28, 2018. http://www.naturalgasintel.com/articles/106496-marginal-costs-to-produce-fall-sharply-but-higher-oil-price-still-imperative-bernstein-says.

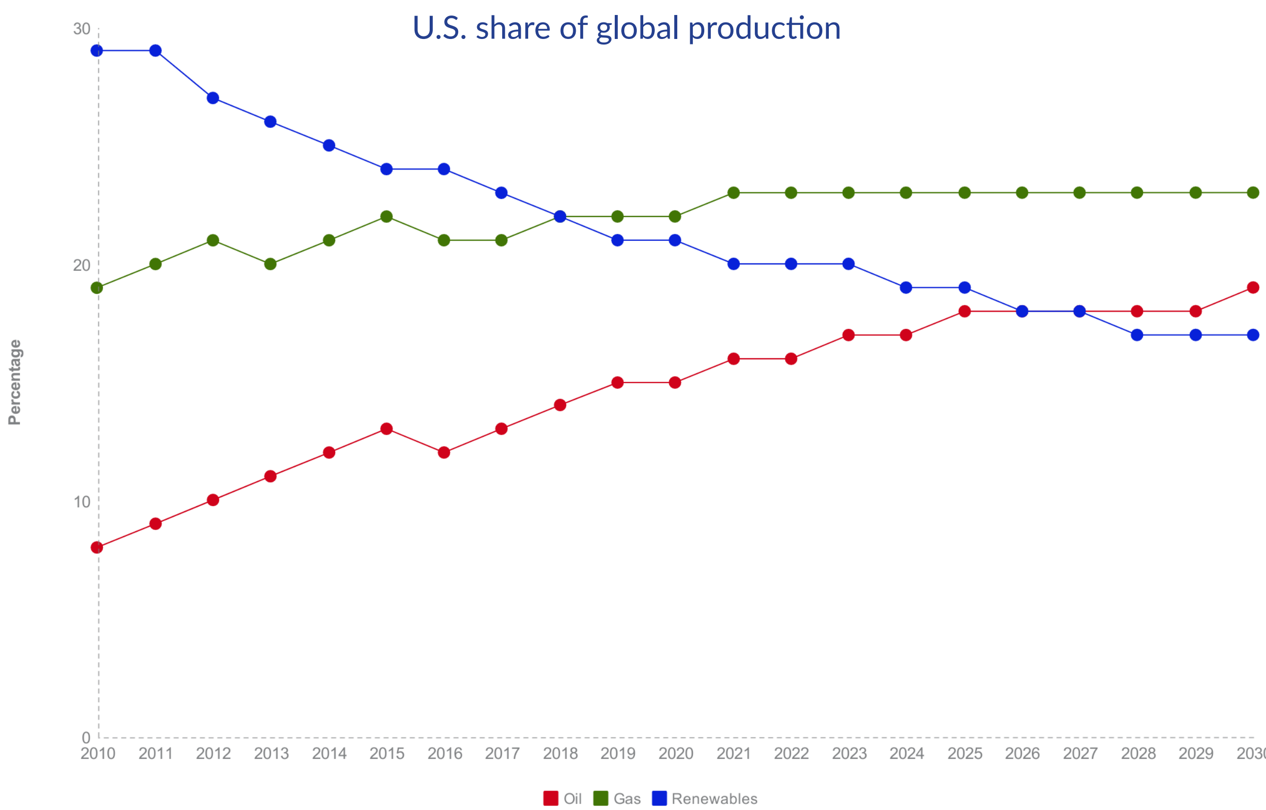
41 Decker, Ryan, Aaron Flaaen, and Maria Tito. "Unraveling the Oil Conundrum: Productivity Improvements and Cost Declines in the U.S. Shale Oil Industry." Federal Reserve. March 22, 2016. Accessed July 5, 2018. https://www.federalreserve.gov/econresdata/notes/feds-notes/2016/unraveling-the-oil-conundrum-productivity-improvements-and-cost-declines-in-the-us-shale-oil-industry-20160322.html.

42 Murali, Danya, and Faouzi Aloulou. "Future U.S. Tight Oil and Shale Gas Production Depends on Resources, Technology, Markets." Energy Information Administration. August 22, 2016. Accessed July 30, 2018. https://www.eia.gov/todayinenergy/detail.php?id=27612.

U.S. tight oil



Source: IEA and OPEC Reports June 2017-June 2018



Source: IEA and OPEC Reports June 2017-June 2018

The OPEC+ Deal Comes Together

By February 2016, it had become clear that letting the market "sort itself out" was not working and threatened the stability of investment planning. Moscow agreed it would freeze production at January 2016 levels in conjunction with Saudi Arabia if others signed onto a production cut.[43]

Russia needed to insulate its budget, and companies needed to preserve production at older fields. Slowly, a consensus formed that tax exemptions or rate cuts for older, Soviet-era fields would become policy, though it was not agreed to in 2016.[44] More importantly, the 2017-2019 budget was designed to avoid extreme deficits assuming oil prices at $40 per barrel.[45] Prices recovered from their nadir below $30 per barrel in January to over $50 by the time the OPEC agreement came together in December 2016.

On September 4, 2016, President Vladimir Putin met with Saudi Crown Prince Mohammad Bin Salman (MbS) on the sidelines of the G-20 summit in Hangzhou, China. According to TASS, MbS told Putin, "We would like to avoid the realization of any negative scenario in the Middle East,"[46] adding that Russian-Saudi ties had a "privileged" character. Production cuts hove into view. The general parameters of the agreement took form by September's end.[47]

November 28 was chosen as a date to hold a conference in Vienna to ratify a production cut between OPEC and non-OPEC producers. But the Saudis reportedly delayed any deal as diplomatic overtures between Russia and Iran took off to determine the shape of the cuts.[48]After tough last moment negotiations, an agreement was signed on December 10 to collectively cut 1.8 million barrels per day of production, 1.2 million from OPEC producers.

43 Sheppard, David, Anjli Raval, and Jack Frachy. "Saudi Arabia and Russia Ministers Agree Oil Production Freeze." *Financial Times*. February 16, 2016. Accessed June 5, 2018. https://www.ft.com/content/da44fb1c-d485-11e5-8887-98e7feb46f27.

44 Fadeeva, Alina, and Margarita Papchenkova. "«Роснефть» опять просит у правительства льготы ["Rosneft" asks for benefits from the government again]." *Vedomosti*. December 14, 2016. Accessed June 4, 2018. https://www.vedomosti.ru/business/articles/2016/12/14/669473-rosneft-opyat-prosit.

45 "Бюджет на 2017-2019 годы окончательно принят Госдумой [The budget for 2017-2019 was fully accepted by the State Duma]." *Rosbalt*. December 9, 2016. Accessed July 13, 2018. http://www.rosbalt.ru/russia/2016/12/09/1574414.html.

46 «Саудовская Аравия совместно с РФ хочет избежать негативного сценария на Ближнем Востоке [Saudi Arabia together with the Russian Federation wants to avoid the negative scenario in the Middle East].» TASS. September 4, 2016. Accessed October 20, 2018. https://tass.ru/mezhdunarodnaya-panorama/3592408.

47 Soldatkin, Vladimir, Rania El Gamal, and Alex Lawler. "OPEC, Non-OPEC Agree First Global Oil Pact since 2001." *Reuters*. December 10, 2016. Accessed June 28, 2018. https://www.reuters.com/article/us-opec-meeting/opec-non-opec-agree-first-global-oil-pact-since-2001-idUSKBN13Z0J8.

48 « Саудовская Аравия отказалась от переговоров с Россией по нефти [Saudi Arabia refused to negotiate with Russia on oil].» *Svoboda*. November 26, 2016. Accessed October 4, 2018. https://www.svoboda.org/a/28140708.html.

OPEC Conference, November 2016. Source: opec.org

Reuters reported that Putin played a decisive role in finalizing the deal.[49] The next day, Russia passed its 2017-2019 budget. Despite its salience, Putin left it to Energy Minister Alexander Novak to handle press statements. Saudi Arabia let others feed quotes to the press about the significance of the cuts.[50] But both had clearly exerted significant political effort to come to an agreement and save their respective budgets.

49 El Gamal, Rania, Parisa Hafezi, and DMitry Zhdannikov. "Exclusive: How Putin, Khamenei and Saudi Prince Got OPEC Deal Done." *Reuters*. December 02, 2016. Accessed September 25, 2018. https://www.reuters.com/article/us-opec-meeting-idUSKBN13Q4WG.

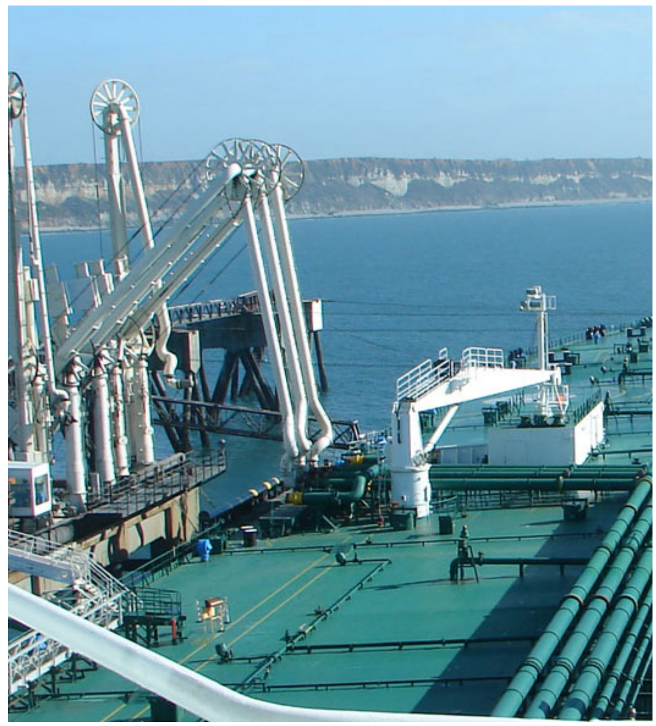
50 Raval, Anjli, and David Sheppart. "Non-Opec Producers Agree to Cut Oil Output." *Financial Times*. December 10, 2016. Accessed August 25, 2018. https://www.ft.com/content/4cd8dce2-beec-11e6-9bca-2b93a6856354.

The OPEC+ Agreement Evolves

By and large, the cuts worked to reduce oil inventories around the world, driving demand above supply by the second half of 2017. Prices accordingly recovered to a $70-80 band by the June OPEC meeting.

Both reported figures and projections before the June 2018 OPEC summit in Vienna showed that crude oil supplies would remain in deficit through 2018.[51] Market rebalancing still left room for differing views on the outlook for oil demand growth. The IEA has been more bearish than OPEC.[52] Tighter emission standards for marine fuels are expected to increase oil demand by as much as 400,000 barrels per day (bpd) per OPEC estimates.[53]

But oil giant BP is warning that the U.S.-China trade war could create an oil demand shock, and other major international oil firms and investment banks have expressed concerns as well.[54] Political factors outside of OPEC and Russia's control are feeding uncertainty over oil prices.

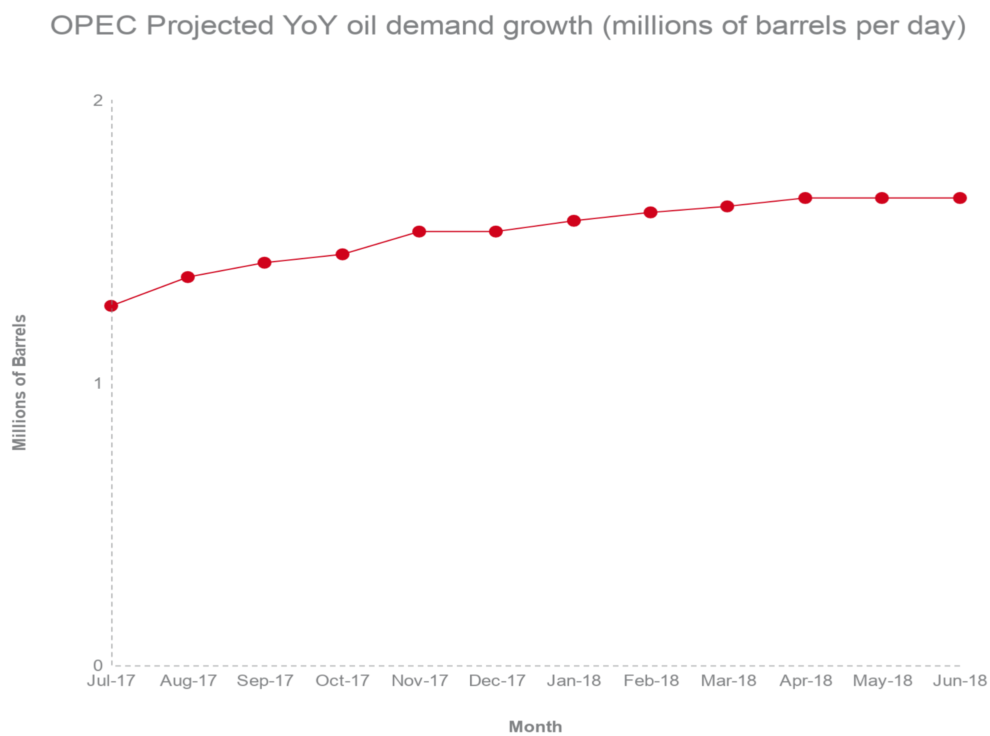


51 "OPEC Meeting, What Lies Ahead?" *Televisory*. November 21, 2017. Accessed September 4, 2018. https://benchmark.televisory.com/blogs/-/blogs/opec-meeting-what-lies-ahead-.

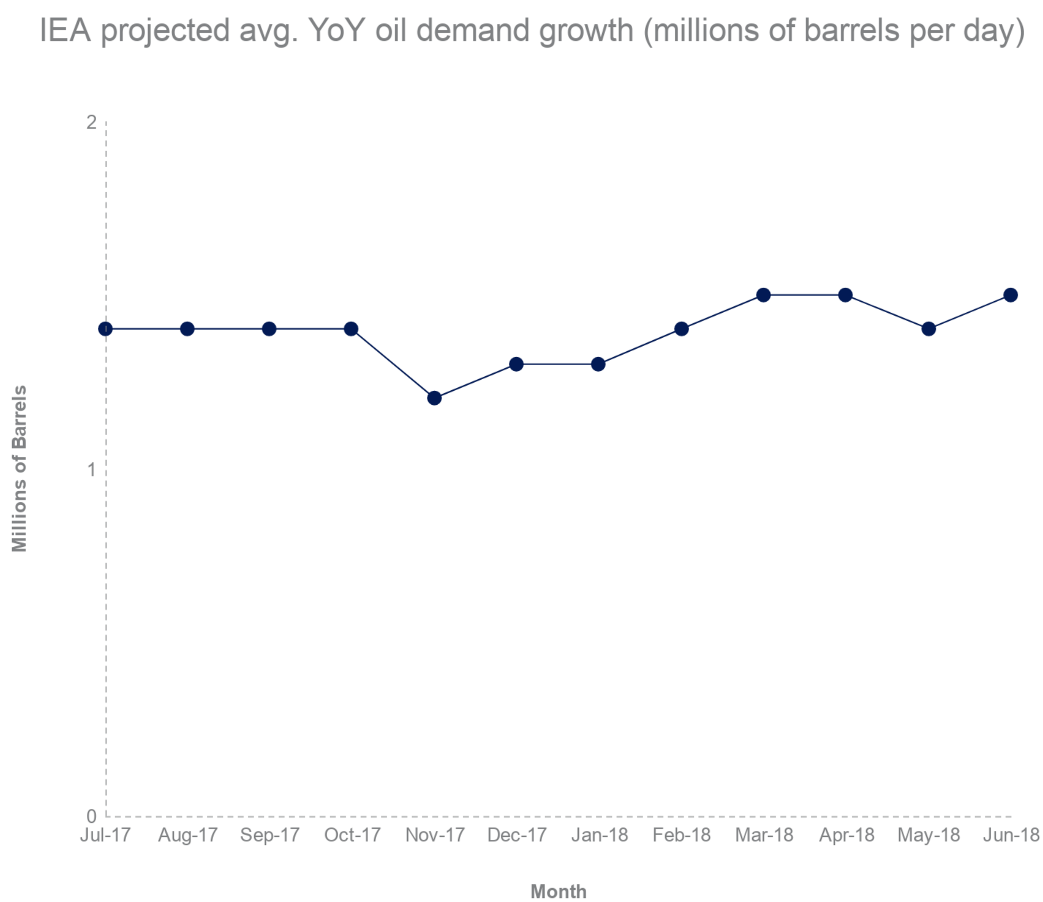
52 Smith, Grant. "IEA Cuts 2018 Oil Demand Forecast as $70 Crude Takes a Toll." *Bloomberg*. May 16, 2018. Accessed July 8, 2018. https://www.bloomberg.com/news/articles/2018-05-16/iea-cuts-2018-oil-demand-forecast-as-70-crude-takes-its-toll.

53 Ban, Jan, Haris Aliefendic, Julius Walker, Tofol Al-Nasr, Eleni Kadati, Hans-Peter Messmer, Joerg Spitzy, and et al. *World Oil Outlook 2040*. Organization of the Petroleum Exporting Companies. Vienna: Organization of the Petroleum Exporting Countries, 2018. https://woo.opec.org/index.html.

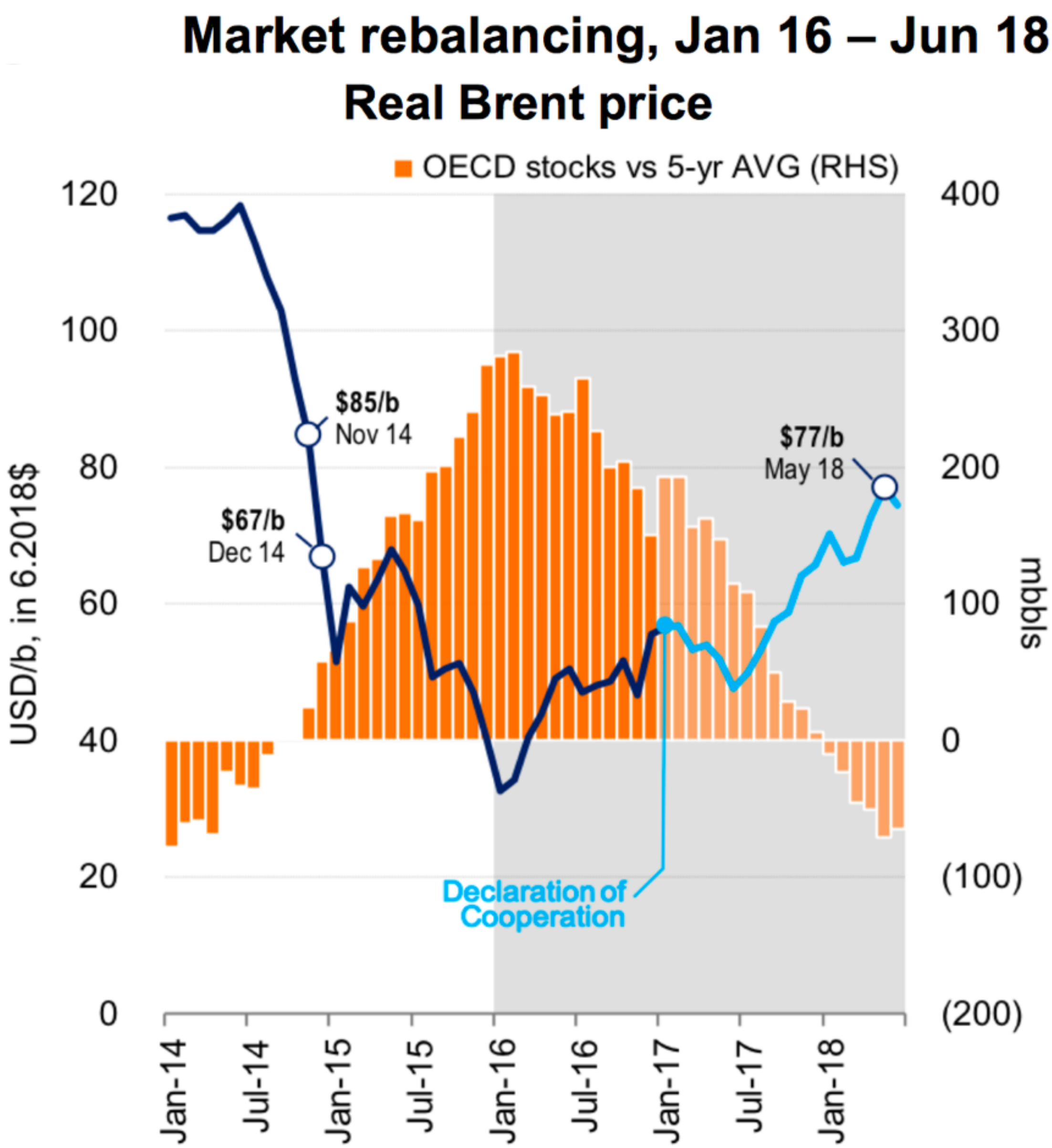
54 Tan, Florence. "U.S.-China Trade War Poses Oil Demand Shock in 2019 - BP." *Reuters*. September 24, 2018. Accessed August 01, 2018. https://uk.reuters.com/article/uk-asia-oil-appec-bp/u-s-china-trade-war-poses-oil-demand-shock-in-2019-bp-idUKKCN1M50B3; and Paraskova, Tsvetana. "Total: Oil Could Rise To $100 And That's Bad News." *OilPrice.com*. September 27, 2018. Accessed October 02, 2018. https://oilprice.com/Energy/Oil-Prices/Total-Oil-Could-Rise-100-And-Thats-Bad-News.html.



Source: IEA and OPEC Monthly Oil Market Reports June 2017- June 2018



Source: IEA and OPEC Monthly Oil Market Reports June 2017-June 2018



Source: IEA, OIES.

Political Influences on the Market

To some extent, the OPEC+ agreement got lucky after December 2016. Even marginal shifts in production can have an outsized impact on prices because demand for oil is inelastic in the short term. People will need to use it no matter the price. Political developments in other oil-producing states took a large number of barrels off the market, easing the difficulty of coordinating cuts.

In June 2015, Venezuela's production stood at roughly 2.4 million bpd. It fell to about 1.5 million bpd by June 2018 and have continued falling.[55] Beijing recently loaned $250 million to Caracas, with plans to loan $5 billion[56] total to prevent further production collapses.

There is little reason to believe the country's oil sector can recover as the country's economic crisis has encouraged mass emigration and scared off international firms.[57] The U.S. is reportedly considering sanctioning imports of Venezuelan crude as well as exports of certain refined fuels, another blow in waiting.[58] The Nicolás Maduro regime's mismanagement of the economy has collectively taken off hundreds of thousands of barrels of oil off the market per day.

Libya's production declined as a result of escalating fighting around vital ports. Production declined over 500,000 bpd after February 2018 due to port closures.[59] However, it has since recovered to over 1 million bpd, its highest point since July 2013.[60] Fluctuations in Libya's production speaks to the risks posed by the country's ongoing civil war.

On May 8, 2018, the United States withdrew from the Joint Comprehensive Plan of Action (JCPOA), which had lifted sanctions on Iran's oil and gas sector.[61] Washington went so far

55 Rathbone, John Paul. "Venezuela's Oil Decline Reaches New Depths." *Financial Times*. May 01, 2018. Accessed July 02, 2018. https://www.ft.com/content/f9cbaec8-4c96-11e8-8a8e-22951a2d8493.

56 Slav, Irina. "China Throws Venezuela's Oil Industry A $5B Lifeline." *OilPrice.com*. July 04, 2018. Accessed July 01, 2018. https://oilprice.com/Energy/Crude-Oil/China-Throws-Venezuelas-Oil-Industry-A-5B-Lifeline.html.

57 Long, Gideon. "Hollowed-out Venezuela Counts the Cost of Crisis." *Financial Times*. September 04, 2018. Accessed August 30, 2018. https://www.ft.com/content/55bd21a8-b02e-11e8-8d14-6f049d06439c.

58 Scheid, Brian, and Eklavya Gupte. "US May Be Prepping Venezuela Oil Sector Sanctions: Analysts." *S&P Global Platts*. September 24, 2018. Accessed August 19, 2018. https://www.spglobal.com/platts/en/market-insights/latest-news/oil/092418-us-may-be-prepping-venezuela-oil-sector-sanctions-analysts.

59 El Wardany, Salma. "Libya Oil Chief Warns Output to Drop Every Day as Ports Halted." *Bloomberg*. July 9, 2018. Accessed July 9, 2018. https://www.bloomberg.com/news/articles/2018-07-09/libya-oil-chief-warns-output-to-drop-every-day-as-ports-halted.

60 "Libyan Crude Output Highest since Jul 2013 at 'more than 1 Mil B/d,' Says NOC Chairman." *S&P Global Platts*. September 23, 2018. Accessed August 23, 2018. https://www.spglobal.com/platts/en/market-insights/latest-news/oil/092318-libyan-crude-output-highest-since-jul-2013-at-more-than-1-mil-bd-says-noc-chairman.

61 Landler, Mark. "Trump Abandons Iran Nuclear Deal He Long Scorned." *New York Times*. May 08, 2018. Accessed August 23, 2018. https://www.nytimes.com/2018/05/08/world/middleeast/trump-iran-nuclear-deal.html.

as to threaten to sanction states that had not cut Iranian oil imports to zero by November 4 in late June.[62] In the last month, Iran has resorted to using "ghost" tankers to hide export shipments, commodities giant Vitol has said it would cease trading Iranian oil once sanctions hit, and importing companies face a great deal of uncertainty as to their exposure.[63]

South Korea has not imported any Iranian oil in three months, and Japan has halted Iranian imports as well.[64] But China and India, the world's biggest growth markets for oil demand, have showed no interest in stopping imports.[65] The cloud of risk around Iran's energy sector and pressure on Iranian exports threatens to take a further 500,000 to 1 million bpd off the market, possibly more in worst-case scenarios.[66] Ultimately, the aggressiveness of U.S. policy on Iran in Syria is likely to be the best leading indicator. The U.S. is formally turning Syria into a proxy conflict given recent statements from National Security Advisor John Bolton suggesting a permanent U.S. presence there until Iran withdraws its presence.[67]

62 Talley, Ian. "U.S. Toughens Stance on Future Iran Oil Exports." *Wall Street Journal*. June 26, 2018. Accessed July 22, 2018. https://www.wsj.com/articles/u-s-signals-zero-tolerance-on-future-iran-oil-exports-1530028859.

63 Vakhshouri, Sara. "Can Iran Weather the Oil-sanctions Storm?" European Council on Foreign Relations. September 20, 1970. Accessed July 01, 2018. https://www.ecfr.eu/article/commentary_can_iran_weather_the_oil_sanctions_storm; Raval, Anjli, and Najmeh Bozorgmehr. "Iran Sends out Ghost Tankers as US Oil Sanctions Loom." *Financial Times*. September 22, 2018. Accessed July 12, 2018. https://www.ft.com/content/d2c7105e-bcf0-11e8-8274-55b72926558f; and Jaganathan, Jessica. "Vitol to Halt Business with Iran after U.S. Sanctions Start- Executive." *Reuters*. September 26, 2018. Accessed August 3, 2018. https://uk.reuters.com/article/uk-asia-oil-appec-vitol/vitol-to-halt-business-with-iran-after-u-s-sanctions-start-executive-idUKKCN1M507U.

64 "South Korea Has Bought No Iranian Crude Oil for about Three Months: SHANA" *Reuters*. September 23, 2018. Accessed August 01, 2018. https://www.reuters.com/article/us-iran-oil-skorea/south-korea-has-bought-no-iranian-crude-oil-for-about-three-months-shana-idUSKCN1M30FE; and "Japan Halts Iran Oil Imports under US Pressure." *Nikkei Asian Review*. August 30, 2018. Accessed July 24, 2018. https://asia.nikkei.com/Politics/International-Relations/Japan-halts-Iran-oil-imports-under-US-pressure.

65 "India Follows China's Lead to Keep Iranian Oil Flowing, Defy US Sanctions Pressure." *News18*. September 03, 2018. Accessed July 01, 2018. https://www.news18.com/news/business/india-follows-chinas-lead-to-keep-iranian-oil-flowing-defy-us-sanctions-pressure-1866377.html; and Adams-Heard, Rachel, and Nick Wadhams. "China Rejects U.S. Request to Cut Iran Oil Imports." *Bloomberg*. August 3, 2018. Accessed June 01, 2018. https://www.bloomberg.com/news/articles/2018-08-03/china-is-said-to-reject-u-s-request-to-cut-iran-oil-imports.

66 Cunningham, Nick. "How Bad Is Iran's Oil Situation?" *OilPrice.com*. July 08, 2018. Accessed September 11, 2018. https://oilprice.com/Geopolitics/International/How-Bad-Is-Irans-Oil-Situation.html.

67 Gould, Joe, and Tara Copp. "Bolton: US Troops Staying in Syria until Iran Leaves." *Defense News*. September 24, 2018. Accessed June 14, 2018. https://www.defensenews.com/global/the-americas/2018/09/24/bolton-us-troops-staying-in-syria-until-iran-leaves/.

Post-OPEC+ Agreement

Against the backdrop of these political pressures on production, an OPEC+ agreement—led by Riyadh and Moscow—was reached on June 22, 2018 to increase production by 1 million bpd.[68] At the September 2018 OPEC+ meeting in Algiers, no further increase was agreed to so as to let markets adjust on their own.[69] But reports surfaced in early October that Russia and Saudi Arabia had secretly agreed to increase production.[70] Mutual increases have thus far been offset by further declines elsewhere, including Venezuela, Angola, and Mexico.[71]

An uncertain market environment for oil prices has left many wondering whether Russian-Saudi political statements of intent to cooperate are significant. OPEC General Secretary Mohammed Barkindo has called for the OPEC+ to remain in effect,[72] staking the cartel's legitimacy on continued cooperation. Russia and Saudi Arabia ultimately dictate the effectiveness of coordinating production. But both states are ultimately driven by economic circumstance. When prices are low enough to affect both states' economic and political ability to incur large revenue losses, cooperation comes easy. When they prices rise, it's a different story.

68 Raval, Anjli, and David Sheppard. "Saudi Arabia Strikes Deal to Raise Opec Production." *Financial Times*. June 22, 2018. Accessed August 11, 2018. https://www.ft.com/content/c2d4232a-7606-11e8-b326-75a27d27ea5f.

69 DiChristopher, Tom, and Natasha Turak. "Brent Crude Closes at Highest Level since Nov 2014 after OPEC Refuses to Boost Output." *CNBC*. September 25, 2018. Accessed July 12, 2018. https://www.cnbc.com/2018/09/24/brent-crude-breaks-80-its-highest-since-2014-as-oil-market-tightens.html.

70 Astakhova, Olesya, and Rania El Gamal. "Exclusive: Saudi Arabia, Russia Agreed in September to Lift Oil Output, Told U.S." *Reuters*. October 04, 2018. Accessed October 10, 2018. https://www.reuters.com/article/us-russia-saudi-oil-exclusive/exclusive-saudi-arabia-russia-agreed-in-september-to-lift-oil-output-idUSKCN1MD0Y8.

71 Paraskova, Tsvetana. "Leaked Document: OPEC Struggling To Lift Oil Production." *OilPrice.com*. October 19, 2018. Accessed September 22, 2018. https://oilprice.com/Energy/Crude-Oil/Leaked-Document-OPEC-Struggling-To-Lift-Oil-Production.html.

72 Dipaola, Anthony. "OPEC Sees Need to Keep Oil Supply Deal as Demand Faces Headwinds." *Bloomberg*. September 17, 2018. Accessed September 30, 2018. https://www.bloomberg.com/news/articles/2018-09-17/opec-sees-need-to-keep-oil-supply-deal-as-demand-faces-headwinds.

Comparing Russia and Saudi Arabia's Oil Sectors

It is necessary to understand the different structures and interests of Russia and Saudi Arabia's respective oil sectors to make sense of the depth of political cooperation alongside the economic and political pressures outlined earlier.

Saudi Arabia's oil sector is dominated by one state-owned monopoly—Saudi Aramco—traditionally run via the Ministry of Petroleum and Mineral Resources. In 2015, the ministry was reportedly "separated" from Saudi Aramco, with MbS becoming head of the Supreme Council of the Saudi Aramco Oil Company (SCSA).[73] Then-CEO Khalid al-Falih—the primary intermediary for OPEC summits and oil politicking with Russia—was moved from his post to the SCSA as chairman of Saudi Aramco. He was also named Energy Minister in 2016.[74] Thus, the decision-making structure for the sector is highly centralized and vertical in nature, with MbS playing an outsized role. Aramco's corporate interests are, by extension, very closely aligned to those of the Saudi state.

The Russian oil sector is split between multiple firms, some private and some state-owned, that then deal with the Ministry of Energy, the Ministry of Natural Resources, and the

Saudi Aramco headquarters (Source: Wikimedia Commons)

Ministry of Finance. Russia's three leading oil firms are Rosneft, Lukoil, and Gazprom Neft. Each have differing strategies and interests and frequently clash domestically over policy as well as the ownership, acquisition, and construction of assets. Rosneft is majority-owned by the state via its parent company Rosneftegaz as is Gazprom Neft through state-owned parent company Gazprom. Lukoil is privately-owned. These different firms, their CEOs' respective networks, and the three ministries mentioned all play roles in shaping and effecting policy before it reaches the Kremlin, which then may act as a final arbiter. Political agreements to cut production must account for differing corporate interests and not just disagreements over the best policy course.

Saudi Arabia has an easier time coordinating its political objectives with the corporate strategy and behavior of Saudi Aramco. By extension, it is also more exposed to

73 Seznec, Jean-François. *The Impact of the Restructuring of the Oil Sector in Saudi Arabia*. The Arab Gulf States Institute in Washington. Washington, DC: Arab Gulf States Institute, 2015.

74 "Saudi Arabia Names Saudi Aramco Chief as New Energy Minister." *Fortune*. May 7, 2016. Accessed October 20, 2018. http://fortune.com/2016/05/07/saudi-arabia-new-oil-minister/.

changes in political whim, largely due to MbS. Russia's ability to observe production cuts and coordinate within its own oil sector is affected by having to mediate a broader array of interests, production limitations imposed by sanctions, and a diffusion of power and interests between actors.

Whereas Saudi Aramco was quickly put to work upping production to flood the market in 2014, Russia committed more political capital domestically to manage cooperation. Production cuts were unpopular with the sector due to Saudi production policy. For example, though Rosneft briefly agreed to cut 25,000 barrels per day of production in November 2014, CEO Igor Sechin expressed considerable doubt about the logic of cuts several weeks before the OPEC+ agreement was reached.[75] Though Lukoil CEO Vagit Alekperov had spoken in support of stabilizing markets, he was predicting the market to return to the $65-90 per barrel range within a few years due to underinvestment in production by January 2015.[76] Cuts were not strictly necessary, though many in the oil sector wanted a more stable market climate with prices high enough to sustain more investment.

As late as September 2018, at the Eastern Economic Forum in Vladivostok, Vladimir Putin himself was touting record oil production figures from 2014 without any reference to cuts or market stabilization.[77] Putin also threw his weight behind raising taxes on oil companies to help with the budget.[78] There were clearly considerable debates ongoing behind closed doors, despite signals early in 2018 that Russia was interested in cooperating with Saudi Arabia. But higher tax rates would only work if prices rose, likely pushing firms to agree. There was, therefore, political impetus from the Kremlin to enforce cooperation within Russia's oil sector.

The same cannot be said for more recent talk of increasing production. The reality is that mutual oil production increases mean very little for political cooperation. After depressing production to raise prices, firms lost a share of the market to other producers, frequently the U.S. Therefore, any agreement to raise production—already dubious since Russia's political control over any individual firm is largely predicated on a scenario where prices have fallen too far—does not signal much politically. It is in the interest of everyone involved, and encourages oil firms to avoid political cooperation so as to secure new gains on markets.

75 Antonova, Elizabeta, Lyudmila Podobedova, Aleksandra Galaktionova, and Asya Sotnikova. "«Роснефть» приняла решение снизить добычу нефти ['Rosneft' decided to reduce oil production]." *RBC*. November 25, 2014. Accessed September 24, 2018. https://www.rbc.ru/business/25/11/2014/5474b0f0cbb20fff42d8586e; and "Сечин: предложение о сокращении добычи нефти выглядит "странным" на фоне действий ОПЕК [Sechin: the proposal to reduce oil production looks 'strange' against the backdrop of OPEC actions]." *TASS*. November 25, 2015. Accessed October 18, 2018. https://tass.ru/ekonomika/2472118.

76 «Как меняется стоимость нефти марки Brent, $/баррель.» *Smart-Lab*. September 15, 2015. Accessed October 19, 2018. https://smart-lab.ru/blog/278404.php.

77 «Встреча с работниками нефтяной и газовой промышленности [Meeting with workers of the oil and gas industry].» Kremlin. September 04, 2015. Accessed October 2, 2018. http://kremlin.ru/events/president/news/50235.

78 "Путин повышает налоги для нефтегазовых компаний [Putin raises taxes for oil and gas companies]." *Vesti Finance*. September 22, 2015. Accessed October 8, 2018. https://www.vestifinance.ru/articles/62603/print.

The View from Washington

Though the roots of cooperation on oil production were largely economic, they cannot be entirely separated from Russia and Saudi Arabia's foreign policy interests in the Middle East. But a brief overview shows that far from forming the basis of deep, structural cooperation between states, oil cooperation appears to be cordoned off from other issues.

Syria is a prime example of the separation of other foreign policy issues from oil. Saudi Arabia has openly backed rebels fighting President Bashar al-Assad and called for Assad's removal via military force if he refused to step down in October 2015.[79] Precisely at that moment, Russia was committing itself militarily to a conflict in which it had long-term security interests in opposition to Saudi Arabia.[80] The two states have never reconciled their disparate stances on Syria. Though tempting to link the timing of the fall of Aleppo[81] in December 2016 with the OPEC+ agreement, there is little evidence that Saudi Arabia was delaying the implementation of a cut due to conditions in Syria. Saudi Arabia only approached Russia over cooperation very early in the year when prices plunged below $30 per barrel.

Some saw hints of Russian-Saudi cooperation in Yemen when, in October 2017, King Salman bin Abdulaziz Al Saud visited Moscow.[82] But Russia vetoed a UN Security Council resolution condemning Iran for violating the Yemeni arms embargo and sending weapons to Houthi rebels in February 2018.[83] The resolution was specifically aimed at implicating the Houthi's in a missile strike aimed at Riyadh. Moscow has not sacrificed its relationship with Iran, surely a sore point for Saudi Arabia politically.

Further to that point, Russia has publicly continued to maintain talks with Iran over coordination in the face of U.S. sanctions.[84] There is little doubt that Riyadh is supportive of Moscow's overtures. The U.S. has expressed concern that Russia would undermine the sanctions regime, likely echoing Saudi Arabia's

79 "Assad Must Step down or Face 'military Option': Saudi Foreign Minister." *Middle East Eye*. September 30, 2015. Accessed October 17, 2018. https://www.middleeasteye.net/news/saudi-foreign-minister-assad-must-go-or-face-military-option-164311177.

80 Al-Saadi, Salam. "Russia's Long-Term Aims in Syria." Carnegie Endowment for International Peace. October 6, 2015. Accessed October 15, 2018. http://carnegieendowment.org/sada/61521.

81 Gilsinan, Kathy. "Aleppo Is Falling." *Atlantic*. December 13, 2016. Accessed October 16, 2018. https://www.theatlantic.com/international/archive/2016/12/aleppo-is-falling/510473/.

82 Semenov, Kirill. "Saudis Could Seek Russian Bailout in Yemen." *U.S. News & World Report*. October 10, 2017. Accessed October 20, 2018. https://www.usnews.com/news/world/articles/2017-10-10/saudis-could-seek-russian-bailout-in-yemen.

83 "Russia Vetoes Resolution Blaming Iran for Arming Yemen's Houthis." *Al Jazeera*. February 27, 2018. Accessed September 24, 2018. https://www.aljazeera.com/news/2018/02/russia-vetoes-resolution-blaming-iran-arming-yemen-houthis-180227065159229.html.

84 «Россия и Иран обсудили сотрудничество перед введением санкций против Тегерана (Russia and Iran discussed cooperation before imposing sanctions against Tehran).» TASS. October 15, 2018. Accessed October 22, 2018. https://tass.ru/ekonomika/5677008.

opolicy line.[85] Russia has also maintained its ties to Qatar, even selling 18.93% of Rosneft's shares to the Qatar Investment Authority after a deal with a Chinese firm fell apart.[86] With Saudi Arabia's prolonged standoff with Qatar in view, it is evident that Russia has not aligned its regional foreign policy in a manner that suggests broader political alignment.

The uncomfortable reality for D.C. policymakers is that little can, or should, be done about Russian-Saudi oil cooperation. The growth of U.S. shale production has introduced a new degree of volatility to oil markets. For now, capacity constraints for export infrastructure limit how much the U.S. can export,[87] but more pipelines are being built. Shale producers' success lowering production costs has significantly limited the ability of traditional low-cost producers like Saudi Arabia to drive them out of the market, and Washington retains considerable sway over markets by deploying sanctions.

This combination of shale production, sanctions power, and price swings creates an increasingly volatile cycle whereby Russia and Saudi Arabia will vacillate between coordination and competition in concert with oil market instability.[88] OPEC+ production cuts also would likely not have been nearly as successful without the combination of production declines in Iran, Venezuela, and initially Libya at the same time. Even if it were real, cooperation would likely have limited effects given how much of the market neither country can control.

Russian firms face a large degree of uncertainty as production comes under pressure going into the early 2020s due to sanctions and a volatile investment climate. Energy Minister Alexander Novak recently warned that Russia may just be three years from reaching peak production.[89] Saudi Arabia, however, does not share these challenges.

There are also growing reasons to see a broad economic slowdown on the horizon, triggered by an escalating U.S.-China trade war and other macroeconomic factors across emerging markets, the U.S., and Europe. In short, the demand outlook is as uncertain as the supply outlook. There is relatively little to fear in Washington regarding any long-term "oil alliance" between Russia and Saudi Arabia.

U.S. policy cannot be nearly as coordinated or fast-acting as Russia or Saudi Arabia because small to mid-size private firms dominate shale production. They cannot adjust quickly. For that reason, it is likely better to assess the costs of Russian-Saudi partnership for Russia in particular. Assuming a three-to-six-year time horizon for oil production to peak in Russia, a volatile investment climate is considerably riskier for Russian firms given production costs, lack of access to shale technology, and lack of technology for offshore Arctic reserves. Price swings will limit the availability of domestic financing or investment from states not observing U.S. and EU sanctions.

Instead of politicizing its production, the

85 Manson, Katrina, and David Sheppard. "US Fears Russia Will Help Iran Evade Oil Sanctions." *Financial Times*. October 21, 2018. Accessed October 10, 2018. https://www.ft.com/content/441d66e4-d480-11e8-a854-33d6f82e62f8.

86 "Qatar Investment Authority Completes Acquisition of 18.93% Shares of Russia's Rosneft." *The Peninsula Qatar*. September 8, 2018. Accessed October 25, 2018. https://www.thepeninsulaqatar.com/article/08/09/2018/Qatar-Investment-Authority-completes-acquisition-of-18.93-shares-of-Russia's-Rosneft.

87 Meliksetian, Vanand. "Solving The Permian Pipeline Problem." *OilPrice.com*. August 28, 2018. Accessed September 1, 2018. https://oilprice.com/Energy/Crude-Oil/Solving-The-Permian-Pipeline-Problem.html.

88 McNally, Robert. "Shale Oil Will Contribute to Future Crude Price Instability." *Financial Times*. February 20, 2018. Accessed August 7, 2018. https://www.ft.com/content/1b911cc8-1583-11e8-9e9c-25c814761640.

89 Slutsky, Maxim. "Russia Is Only 3 Years Away From Peak Oil, Energy Minister Warns." *Moscow Times*. September 19, 2018. Accessed October 1, 2018. https://themoscowtimes.com/news/russia-only-3-years-away-peak-oil-energy-minister-warns-62926.

U.S. would be better served reassessing its regional priorities. After all, attempts to call for production increases in Saudi Arabia[90] are likely to achieve little. Import security and price stability are no longer logical policy foci.

Washington has a considerable advantage over Moscow in the near to medium term in that Russian firms will have to lobby the Kremlin to maintain an active regional policy so they can secure reserves before oilfields begin to deplete in Russia proper. If they fail to do so, Russia's dominant role as an exporter will suffer. Russia, therefore, has more to lose in the Middle East than the U.S. But the fundamentals driving Russian-Saudi cooperation will remain largely competitive, with market extremes forcing the two to cooperate when appropriate despite attempts to insulate budgets from the effects of price drops.

90 Reed, Stanley, and Mihir Zaveri. "Trump Pressures Saudi Arabia to Increase Oil Production." *New York Times*. June 30, 2018. Accessed July 9, 2018. https://www.nytimes.com/2018/06/30/us/trump-oil-saudi-arabia.html.

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