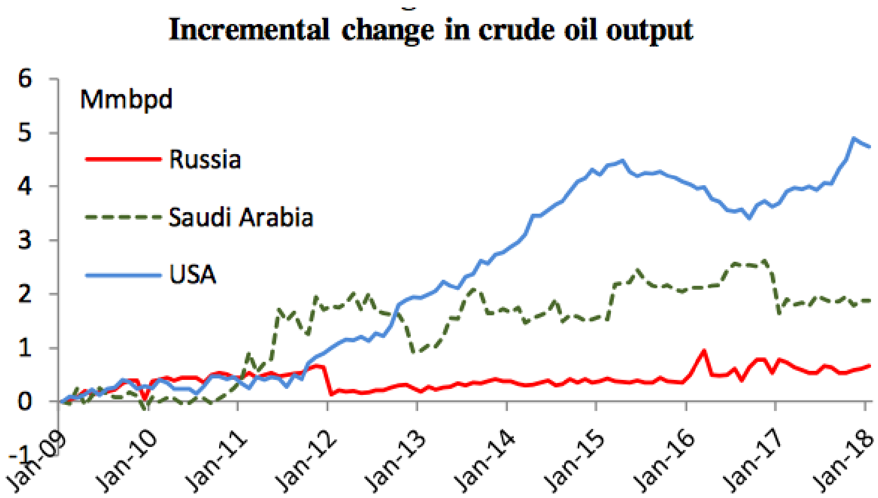
Why is this study important?

This paper, published as an *IICEC Energy and Climate Research Paper*, discusses the dynamics that the “big-three” global oil producers (Saudi Arabia, Russian and the United States) have played in establishing today’s world oil market, and how their actions are going to shape its future. According to the paper, while the world is transitioning towards a low-carbon future, and this transition could lead to dramatic and disruptive price volatility due to strategic warfare (*warchest* as the author puts it) in the global oil market based on the various interests of the states. Hence, at this juncture, the significance of understanding the past-present-future time chain, how new oil market developments in the “big-three” have changed the oil industries, why and how their strategies have shifted and what these changes mean, comes into play. The paper presents a thorough description of *what is happening* in the global oil market by delving into the challenges faced by the big-three, in order provide the reader with a comprehensive understanding. Overall, as the author puts it “the challenge is how to find compromise for many producing and exporting countries with different revenue needs and different degree of financial resilience.”

Research Summary

Unprecedented developments took place in the global oil markets in the last past five years; new market fundamentals have created a new geography of global petroleum trade.



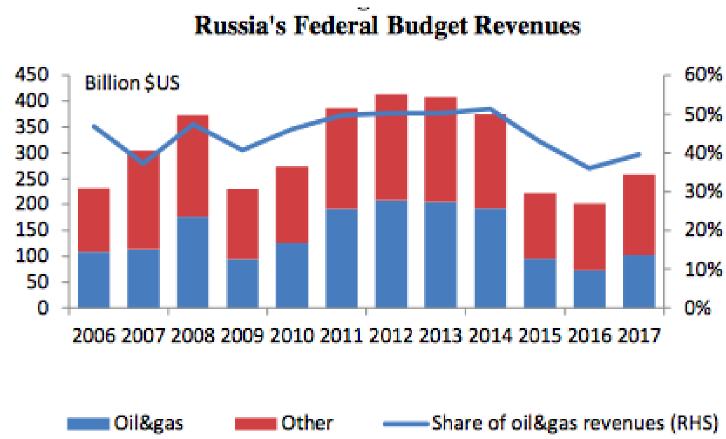
Source: CEPR NRU HSE, JODI data

Long and painful market rebalancing took place between 2014-2018, due to strategic warfare in the global oil market. For example, OPEC (Saudi Arabia being the key force behind OPEC) hoped for a blitzkrieg in November 2014, when it decided not to restrict its output, which caused oil prices to drop from $100 in 2014 to below $30 in January 2016. However, U.S. unconventional oil’s resilience to low oil prices has resulted in financial stress on all OPEC producers and has not made the U.S. frackers immediately change course. OPEC, according to its logic, was waiting to would regain the ability to influence the market and would be better able to affect prices with much smaller production cuts, had US frackers left the market because of low prices.

The oil boom in the United States continues due to the shale oil revolution; the United States has become a refined product net exporter. Since 2009, US crude output has increased by 92%, and from 2009 to 2017 U.S. crude oil imports declined 24%, from 9 to 6.8 mmbpd. However, the U.S. will not replace Saudi Arabia as a swing producer, based on Yermakov's reasoning. Instead of becoming a swing producer, the role of the United States is "finding the balance between the rush to produce and achieving profitability for its tight oil developments. Now that most of U.S. tight oil producers have secured their position on the global supply curve, it is time to return to profitability in operations. This is likely to require oil price to be in the $60 to $80 per barrel corridor."

Pointing out the shift in Saudi Arabia's policy in November 2014 raising questions about her future role in the oil markets. Saudi attempts to raise prices with production cuts might be thwarted by an elastic U.S. supply response thereby limiting the price increase Saudi Arabia might otherwise achieve. But Yermakov points out that Saudi Arabia is reinventing her role as market balancer; the role that she was doing for many years as OPEC's swing supplier.

The collapse of oil prices from mid-2014 through 2016 caused difficulties for Russia. Russia's economy is to a certain extent diversified and has the ability have a prolonged resilience to economic stress by diversifying the Russian economy away from dependence on hydrocarbons, macroeconomic stabilization, and import substitution policies. Nonetheless, the implementation of these strategies were not as easy as it used to be in 2009 since the oil price has been under $60 per barrel on average for three years, shrinking revenues and constraining Russia's energy sector.



Source: CEPR NRU HSE, data from Russia's Ministry of Finance

The Central Bank of Russia decision to use the floating exchange regime rate and making use of the policy of weak ruble in the 2014-2016 crisis proved to be beneficial for the economy and the ruble did not strengthen when the oil price increased to $70 per barrel as Russia started to save the revenues over $40 into the rainy day fund to finance budget deficit as needed. Russia also proved that she is resilient to produce crude oil at times of low oil prices and was the number one producer in the world in 2017. Yermakov concludes that "even if Russia may never be as strong as it looks, it is also never as weak as it looks".