

Last-minute deal on oil production cuts

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Using a mixture of arm-twisting, threats and a sleight of hand, US President Donald Trump has secured an agreement from Saudi Arabia and Russia to at least temporarily end their oil price war that erupted last month and cut production.

The deal, which Trump pushed for in the wake of the plunge in oil prices, was on the point of collapse over the weekend because of Mexico's refusal to make cuts to the extent demanded by Saudi Arabia. It was finally stitched together on Sunday.

The fear was that if an agreement had not been reached the oil price would have crashed when trading opened today, after dropping from levels of around \$50 per barrel to as low as \$20.

Under the deal, Russia and Saudi Arabia will together reduce production by about 9.7 million barrels a day, more than double the cuts agreed to during the global financial crisis of 2008. Cuts by other oil-producing countries will bring the overall reduction in supply close to 20 million barrels a day, around 20 percent of the total supply.

However, there are doubts that even these major reductions will halt the price slide. Global demand for oil has fallen by 30 percent because of the economic impact of the coronavirus pandemic, slashing its price by 40 percent since the beginning of March.

According to the *Wall Street Journal*: "Investors remain concerned that the cuts may not be enough to support higher prices in the coming weeks as world-wide lockdowns pummel demand for gasoline, diesel and jet fuel."

It said some analysts had warned they were "too little, too late" with oil consumption expected to fall by as much as 30 million barrels a day throughout this month.

Last week, the talks assumed an on-again off-again character. Agreement appeared to have been reached on Thursday when members of the G20 group, currently

under the chairmanship of Saudi Arabia, issued a statement saying they would "commit to doing whatever it takes, both individually and collectively" to ensure that the oil market made a recovery.

Speaking after the G20 meeting, Fatih Birol, an official of the International Energy Agency, said the "shock waves" of the pandemic created the oil price slump and threatened "global economic stability."

He said the emergency measures would not provide a "quick fix" but, like the effect of confinement in containing the COVID-19 spread, they could help to "lower the peak and flatten the curve."

However, in a further sign of the incapacity of global organisations to deal with the deepening economic crisis, the G20 call had little effect.

Mexico continued to insist it would not cut its production to the extent demanded by the Saudis. It only committed to reduce its output by 100,000 barrels a day, well below the Saudi demand for a 350,000 barrel production cut.

Fearing a crash in the markets if the deal failed to go through, Trump stepped into the breach and said the US would compensate for the Mexican shortfall by a reduction of 300,000 barrels per day in American output.

It is unclear how that will take place. The US is not committed to direct cuts claiming that the fall in its output will take place as a result of the drop in market prices.

When the proposal was first raised in the back-and-forth negotiations last week, Trump said he expected the Mexican government would "reimburse" the US in return for American production cuts. He did not specify what he meant and the White House declined to comment when asked for an explanation.

The main factor in pushing the Saudis to the deal was a threat by Trump, issued earlier this month, to impose tariffs on crude imports.

Republican senators from US shale oil-producing states also weighed in, holding a meeting for nearly two hours with the Saudi energy minister on Saturday during which they threatened the long-standing ties between the US and the Saudi regime.

One of the reasons for the decision by the Saudis to launch the price war, after an earlier agreement with Russia had broken down, was to force higher-cost US shale oil producers out of the market.

“The Saudis spent over a month waging war on American oil producers, all while our troops protected theirs. That’s not how friends treat friends,” said North Dakota Republican senator Kevin Cramer after the meeting with the Saudi minister.

In the event, political considerations played a major role in securing the agreement, fragile as it is.

The Putin regime is dependent on oil revenues for about one-third of its budget. With analysts warning that the price collapse threatened to create “a serious risk to the Russia’s economy,” Putin is anxious to avoid such turmoil as he seeks to change the constitution and extend his term of office.

“A month ago, no one could have predicted such a crisis and falling demand,” the Kremlin spokesman Dmitry Peskov told reporters on Friday.

While the Saudis started the war, the resultant precipitous decline in oil prices has put in jeopardy plans by the country’s de facto ruler, Crown Prince Mohammed bin Salman, to transform the country’s economy. His plans for launching infrastructure projects are dependent on oil sales. For his part, Trump is concerned that further price falls will hit oil-producing states that are crucial for his re-election campaign.

He is also fearful that a wave of bankruptcies and defaults could have flow-on effects for financial markets because of the dependence of many shale-oil producers on risky junk bonds for their financing.

As is par for the course, Trump greeted the news of the deal with wildly exaggerated claims. The big oil deal is done, he tweeted on Sunday. “This will save hundreds of thousands of energy jobs in the US.”

However, it is doubtful whether the deal will even hold together and, even if it does, whether it will prevent a further fall in prices as a result of the greatest contraction in the global economy since the Great Depression.



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