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Rapid Oil Price Decline and Enhanced China-Saudi Arabian Cooperation

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Since early December, we have seen various attention-attracting developments in the international oil market. As described in A Japanese Perspective on the International Energy Landscape (613), the European Union agreed on a Russian oil price cap at $60 per barrel on December 2, paving the way for Western countries, including the Group of Seven industrial democracies and Australia as well as the EU, to introduce the Russian oil price cap system on December 5. While the international oil market's reactions to the price cap attracted attention later, crude oil prices continued to decline substantially in the second week of December. The key futures price for the West Texas Intermediate crude plunged from $81.22/bbl on December 1 to $76.93/bbl on December 5 and fell further to $71.46/bbl on December 8, extending its losing streak to six straight market days. In the first eight days of December, it lost some $10/bbl. The key futures price for Brent crude also dropped by some $10/bbl from $86.88/bbl on December 1 to $76.15/bbl on December 8.

Both WTI and Brent prices on December 8 represented their respective lowest levels this year, meaning that these prices fell back to their year-before levels. Crude oil prices began to rise on growing tensions in Ukraine early this year, topped $100/bbl on Russia's invasion into Ukraine and soared above $130/bbl temporarily in early March. They later remained above $100/bbl before turning down in summer. They slipped below $80/bbl in September. Their latest drops mean that their rises amid growing tensions in Ukraine were lost.

It may be needless to note that the biggest factor behind the crude oil price decline is growing concern about global economic deceleration and a subsequent slowdown in oil demand. Energy and food price spikes amid the Ukraine crisis led to rapid global inflation, prompting U.S. and European monetary authorities to tighten monetary policy by raising interest rates substantially. Concern about economic deceleration grew on the monetary tightening, leading the International Monetary Fund to revise economic growth projections downward. A slowdown in oil and other energy demand under the strict zero-corona policy in China, the largest oil importer in the world, also pushed down crude oil prices. Rallies against the zero-corona policy in November have led Chinese authorities to ease the policy. However, how the easing would contribute to an economic recovery is still uncertain.

Crude oil price declines encouraged the OPEC-plus group of oil-producing countries to reverse its policy of increasing oil production continued since 2020 and reduce production by 0.1 million barrels per day in October and by 2 million bpd from November. The OPEC-plus group thus signaled its willingness to defend crude oil prices, contributing to supporting crude oil prices. However, the recent price trend indicates that the global oil demand deceleration's downward pressure on crude oil prices has been greater.

In such situation, the world saw an attention-attracting development that could have great influence on the international oil market, the international energy landscape and energy geopolitics. Chinese President Xi Jinping visited Saudi Arabia and clinched a comprehensive strategic partnership agreement with Saudi leaders.

On December 8, Xi visited the Saudi capital of Riyadh and held talks with Saudi Arabian King Salman bin Abdulaziz Al Saud and Crown Prince Mohammed bin Salman. The Chinese and Saudi leaders agreed to enhance strategic cooperation and collaboration in a wide range of areas, including crude oil trade expansion, investment promotion and cooperation between China's Belt and Road Initiative and the Saudi Vision 2030. They not only called for the enhancement of economic cooperation but also agreed on the importance of respect for national sovereignty and the significance of non-intervention in domestic affairs.

It is natural and obvious that China as the world's largest oil importer and Saudi Arabia as the world's biggest net oil exporter need each other and are destined to deepen their mutual dependence. At a time when Russian oil supply grows insecure and uncertain amid the Ukraine crisis, Saudi Arabia's presence in the international oil market is increasing more and more. Deepening relations with Saudi Arabia is significant for energy security in China that gives priority to stable oil imports. As the gravity center of the international oil market shifts to Asia, particularly China, it is important for Saudi Arabia to increase its presence in and its share of the Chinese market to enhance oil demand security. If developed countries' oil phaseout makes progress, the Chinese market where oil demand is expected to continue expanding until 2030 will become even more important for Saudi Arabia. It will be significant for the two countries to deepen their mutual dependence.

However, China-Saudi Arabia relations are not limited to the energy area. The latest bilateral agreement indicates that they are conscious of enhancing the bilateral strategic economic partnership from a comprehensive viewpoint, including cooperation between the Belt and Road Initiative and the Vision 2030. Their enhancement of cooperation in a wide range of areas is related to their respective ulterior motives. By positioning China as its important partner for the long-term challenge of tackling economic sophistication and diversification, Saudi Arabia may demonstrate its significance to the world, attract attention from developed countries such as Japan, the United States and European countries and diversify international cooperation, while securing support from and cooperation with China. By approaching Saudi Arabia as a linchpin to the Middle East and the most important player in the international oil market, China may secure its economic interests. Geopolitically, China may attempt to increase its presence in and influence on the Middle East by enhancing its relations with Saudi Arabia as its strategic partner. This may drive a wedge between the United States and Saudi Arabia that have had a special relationship regarding geopolitical and oil market stability.

How will the United States view the enhancement of the strategic partnership between China and Saudi Arabia? I am concerned about this question. The U.S. Biden administration's relations with Saudi Arabia have been strained. In only two months after President Joe Biden's visit to Saudi Arabia in July, Saudi Arabia decided to reverse its oil production increase and cut production. In November, the Saudi-led OPEC-plus group decided on a substantial production cut of 2 million bpd, straining Saudi-U.S. relations further. The United States may grow nervous about Saudi Arabia's further approach to China that the United States sees as its biggest competitor. If Saudi Arabia leads the OPEC-plus group to enhance its production cut to cope with the oil price weakness in such situation, U.S.-Saudi relations may be aggravated.

The special relationship between the United States and Saudi Arabia, which has been one of the key factors supporting international energy market stability, is seemingly shaken. As there are a mountain of challenges regarding the maintenance and enhancement of global energy governance, we cannot ignore the fate of the special relationship.

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