Evolution and Inspiration of Saudi Arabian Energy Strategy

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Abstract. Saudi Arabia has rich oil resource and accounts for one sixth of the world’s oil reserve, around which its energy strategy has been evolved to oil. This paper firstly reviewed and examined the evolution of Saudi Arabian energy policy by taking into account of the critical role of Organization of Petroleum Exporting Countries (OPEC) in this process. Then how Saudi Arabia had acquired a dominant position in OPEC and how this affect the future of OPEC were discussed. Finally, some recommendations with respect to the energy strategy of other countries were given.

1. Introduction

Saudi Arabia has rich oil resource and accounts for one sixth of the world’s oil reserve. Since the discovery of the Dammam Oilfield in 1938, the world’s largest onshore oilfield, the destiny of Saudi Arabia has been closely connected to oil, around which its energy strategy has been evolved. Previously, it focused on seizing the control of domestic oil resource and international oil market through the OPEC, and currently, it adopts a moderate oil policy intended to maintain its share of international oil market.

At present, Saudi Arabia is the OPEC’s largest oil producer, accounting for one third of the OPEC’s oil production, and with rich oil resource, conciliatory regional policy and pro-Western diplomacy and other well-established advantages, it has occupied a core position in the OPEC power structure. Recently, within the OPEC something has changed, with Qatar withdrawing and member countries such as Iran and Qatar announcing to gradually turn to focus on natural gas, and moreover, the United States has become the world’s largest oil producer. As a result, the OPEC surely will have a declining influence on the world’s oil market. In the future, the OPEC, as never before, will be under huge challenges from the United States, the world’s largest oil producer, and the attitude of the Saudi Arabia will be critical.

In this article, first of all, we will review and examine the evolution of the Saudi Arabian energy policy by taking into account of the critical role of the OPEC in this process. Then we will proceed to look at how Saudi Arabia has acquired a dominant position in the OPEC and how this will affect the future of the OPEC. Finally, we will give some recommendations with respect to the energy strategy of other countries.

2. Evolution of the Saudi Arabian Energy Strategy

In Saudi Arabia, the development of energy strategy was started in the 1960s, when King Faisal realized that oil revenue might provide the funds necessary for economic modernization and national
security, and the focus of the energy strategy was to take back the control of oil resource. In 1960, when the Middle East had become a major oil producer in the world, Saudi Arabia and other 4 oil producers set up OPEC, under which oil producers in the Middle East began to promulgate the uniform oil policy, with an aim to seek for a legitimate status in international oil market and to break up the monopoly of international oil market by the so-called “Seven Sisters”, i.e. seven European and US oil companies. Thereafter, to a considerable extent, it was through the OPEC that Saudi Arabia realized its energy strategy.

In the 1960s, through the OPEC, Saudi Arabia and other oil producers restricted oil production and opposed international oil companies to control and force down oil prices. To a considerable extent, this has contributed to the signing of the Tehran Agreement in 1971, under which oil producers took back the oil pricing power. Subsequently, the OPEC retook the control of national natural resources from international oil companies. When the Middle East War broke up in 1973, in order to strike Israel and its supporters, the Arabian OPEC members announced the take-back of posted prices and directly raised posted prices from 2.89 US dollars to 5.119 US dollars per barrel, and further up to 11.65 US dollars in 1974, resulting in the first oil crisis. In 1975, for the purpose of effectively curbing the then overwhelming power of the OPEC to manipulate international oil market, the International Energy Agency (IEA) was founded by the OECD countries, including the United States, to coordinate national energy policies on behalf of leading oil-consuming countries and to be in better position to cope with the issue of OPEC oil supply.

In the dualistic game between oil producers, as represented by the OPEC, and oil consumers, as represented by the IEA, the OPEC has been weakening in terms of market influence, and later on, it sought to maximize its interest and stabilize global oil market by using oil price mechanisms and production quotas to influence international oil market. In 1978, a revolution erupted in Iran to overthrow the government of Pahlavi, and the second oil crisis occurred in the Middle East as a result of panic oil buying and soaring oil price. Due to oil crisis and high price, non-OPEC countries became motivated to step up oil exploration and development, and their share in the world’s oil production was raised from 50.4% in 1979 to 69.8% in 1985. International oil market was over-supplied and became a buyer’s market rather than a seller’s market. In 1982, the OPEC had no way but to cut oil production and price. To cope with the precipitating price, one of the means for the OPEC is to cut production and maintain stable price, however, such reduction, if prolonged, may reduce its share and undermines its influence on international oil market. When international oil market is balanced in terms of demand and supply, the OPEC also has to discuss the strategic issue whether to cut production and maintain the price or to increase production and the market share.
For the moment, Saudi Arabia focuses on a moderate oil policy intended to maintain a steadily growing share in international oil export market, sustain domestic economic growth and maintain the stable reign of the King. In 2016, it announced the Saudi Vision 2030 (“Vision 2030”), proposing to maintain a strong oil production capacity, vigorously grow natural gas and other energies, including, among others, solar and nuclear energy, etc. Overall, under the Vision 2030, the core of energy strategy is still to maintain a stable oil export. Saudi Arabia is a typical “oil economy”, and for long, its oil revenue has accounted for 40%-50% of its GDP. However, there is a sharp rise in its domestic oil consumption, the share of which in total oil production was raised from 17% in 2000 to 33% in 2017, thus occupying a great amount that otherwise would have been exported. The inclusion of a variety of energies, such as nuclear and renewable, as proposed by the current energy strategy, is primarily intended to ensure the availability of adequate oil for export by using alternative energies and reducing domestic oil consumption.

3. Establishment and Effect of the Saudi Arab’s Dominant Position in the OPEC
In the 1980s, Saudi Arabia voluntarily acted as the OPEC’s floating producer to decide its oil production in accordance with international oil demand, and such cooperative oil policy helped it win the trust and support within and outside the OPEC. Saudi Arabia has faithfully implemented the OPEC quota and is one of few countries that has complied with and even exceeded the reduction target (level of implementation at 157%). This indicates that it not only has complied with its reduction commitment, but also has made extra reduction for the countries not fulfilling their reduction target. At the same time, backed by strong financial resources, Saudi Arabia has been engaged in massive foreign economic aid and satisfied its political and religious appeals by using the Riyal-based diplomacy to provide various aids to the Third-World developing countries. Such a series of conciliatory policies have helped Saudi Arabia become a good example and obtain a dominant position in the OPEC.

Its pro-American stance also contributes to its dominance in the OPEC. In the 1980s, for the purpose of the interdependence as proposed by the United States, Saudi Arabia agreed to settle oil transactions with US dollars to exchange for the take-back of the control of foreign oil companies, including, among others, Aramco, and a long-standing alliance began to be formed between the two countries. From the perspective of the United States, Saudi Arabia is the core of its “Middle East Oil Strategy” and the strong safeguard for its oil export, and it may use the Saudi Arabian dominance in the OPEC to exert an indirect impact on international oil prices. For instance, in 1985, the Reagan Administration compelled Saudi Arabia to raise oil production and implement the “Reverse Oil Shock”, with a purpose to have a significant increase in production, lower the price and encumber the Soviet economy. From the perspective of Saudi Arabia, its comprehensive national strength is characterized by economic affluence and military weakness, it needs the United States to help realize national security, prevail in the Arabian regions and deal with other international concerns. For example, the inclusion of Saudi Arabia into the G20 has much to do with the United States’ eventual consent to the 20-member proposal instead of the 14-member one. As a firm alliance, the United States and Saudi Arabia are always together to combat external threats in the warring and turbulent Middle East, and even the September 11 Event failed to change in any fundamental manner the foundation of their cooperation in respect of oil and security issues.

Looking ahead, Saudi Arabia will have a considerable effect on the development of the OPEC. Generally, the OPEC will see its weakening influence on international oil market and greater changes in its member countries. OPEC has published a study of the benefits after it is dissolved, and some member countries are often said to be going to withdraw, and these indicate that the OPEC now is swinging and subject to various possibilities in the future. Along with the weakening role in profit making and the decreasing market share, member countries will turn to seek for more favorable paths of development, and it will be increasingly difficult for the OPEC to act in concert. There are two reasons: in the first place, the OPEC has the biggest challenge since its foundation, that is, the United States has become the world’s largest oil producer. Therefore, the OPEC will fail to some extent in
respect of its efforts to restrict production and maintain the price”. If the OPEC chooses to cut production, the United States will increase international market supply and keep the price low, and the OPEC will be unable to maintain its market share. If the OPEC chooses to raise production, international oil price will be lowered. For a long time to come, such a powerful competitor will make the OPEC trapped in this “unsolvable” plight, and the uniform decision making does not have much meaning. In the second place, Saudi Arabia has a firm alliance with United States, and they now become more interdependent in military, financial, political and other areas. When the United States is determined to force down oil prices, though Saudi Arabia may seek to work with Russia and other countries, however, in the long run, it still will be cooperative, and this is against the wish of other OPEC members to raise oil prices. Many countries may not want to be exploited by the Saudi-US alliance, and they may withdraw and seek for other chances. Qatar, which has withdrawn from the OPEC, is such an example.

4. Inspiration for the Energy Development Strategy of Other Countries

Currently, international energy governance tends to be multi-centered, and various energy production centers and consumption centers have changing economic and strategic appeals to accommodate the changing international situation. In light of such complicated and pluralistic international energy deployment, various countries have to actively participate in and promote international energy cooperation, find opportunities for more stable, counteractive and profitable cooperation in various international organizations, and ensure the security of the supply of energy export.

Especially, in working with Saudi Arabia, it is necessary to understand its long-standing reliance on the United States, and Saudi Arabia needs time to know and recognize other countries’ industry, technology and capability. As a result, cooperation with Saudi Arabia requires greater mutual exchange and trust and some sort of flexibility.

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