The world oil market has transitioned over the past year from a situation characterized by concerns about scarcity based on disruption events to one defined by substantial oversupply. The shift toward substantial oversupply has drawn the market focus back to the question of cartel behavior and the policy preferences of Saudi Arabia and OPEC.

Going forward, the chief determinant of production restraint within OPEC, or the lack thereof, will be the policy preferences of Saudi Arabia and its core Gulf Arab partners—so-called core-OPEC—rather than the membership of the cartel as a whole. Given the lack of OPEC cohesion, Saudi policy preferences are what truly matter. The Saudis have announced that they intend to maintain current production levels to preserve their market share.

Saudi Arabia’s ample financial reserves should get them through a few years of low prices, but running down their reserves could constrain their financial options in the longer term.

In this current market environment in which severe price pressure is beginning to constrain supply growth, geopolitical event risks could play a key role. Prominent among these risks are possible oil supply disruptions or additions by Iran, Iraq, and Libya.

While a number of countries will see negative impacts on their economies or political stability as a result of lower oil prices, two stand out—Venezuela and Russia. Venezuela’s problems will be the more immediate and could include social upheaval.

Global oil market transitioning

The world oil market has transitioned over the past year from a situation characterized by concerns about the potential for scarcity based on disruption events to one defined by substantial oversupply and the need for a major slowdown in the rate of supply growth. Still, several geopolitical risks have the potential to significantly affect the extent to which the market is oversupplied.