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Saudi neomercantilism in the oil price war

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Abstract

Purpose – The so-called “oil price war” of 2014-2016 took place between several main global oil producers; OPEC (led by Saudi Arabia), Russia and the newcomer; American tight oil or fracking oil. These oil producers were competing against each other over market shares in the global oil market, by maintaining their high oil production rates, even if this led to a decline in oil prices and a reduction in revenues from oil sales. As energy politics need more coverage in International Political Economy (IPE) theory, this paper aims to argue that Saudi Arabia’s policies during the oil price war of 2014-2016 reflected a policy of neomercantilism, which is the IPE equivalent of the school of realism in International Relations (IR).

Design/methodology/approach – This paper tests for neomercantilism by testing three of its main definitional components. The first definitional component is that the state, as the political authority, intervenes in the economic decisions. The second component is the primacy of the state interests over business corporate profits, or the primacy of political and security considerations over short-term economic and corporate profit considerations. The third is the zero-sum or relative gains nature of dealings between states. Afterwards, this paper tests for neomercantilism in the Saudi policy by examining how each of these definitional components is reflected in the Saudi policy during the oil price war.

Findings – As energy politics need more coverage in International Political Economy (IPE) theory, this paper argues that Saudi Arabia’s policies during the oil price war of 2014-2016 reflected a policy of neomercantilism, which is the IPE equivalent of the school of realism in International Relations (IR).

Originality/value – As energy politics need more coverage in International Political Economy (IPE) theory, this paper argues that Saudi Arabia’s policies during the oil price war of 2014-2016 reflected a policy of neomercantilism, which is the IPE equivalent of the school of realism in International Relations (IR).

Keywords Saudi Arabia, Oil price, Neomercantilism, Zero-sum

Paper type Research paper

1. Introduction

A “price war” for market share is a type of trade war where each state decreases its prices to attract more buyers and obtain a larger market share. This has happened in the period between 2014 and 2016 in the global oil market. During this period, three of the world’s major oil producing countries, Saudi Arabia, the USA and Russia competed against each other by keeping high production rates to maintain their market shares in the global oil market.

This paper attempts to find an explanation in International Political Economy (IPE) theory to this event, with a focus on neomercantilism, which is the nearest equivalent in



International Political Economy (IPE) theory to the International Relations (IR) theory of realism. This paper argues that neomercantilism offers a plausible explanation for the Saudi oil policy during the price war. The Saudi policy of inducing a decline in prices to protect its market share, where the long-term strategic gains of protecting market share overcame short-term profits or revenue gains, displayed a Saudi application of neomercantilism.

H1. The Saudi policy during the oil price war of 2014 reflected an application of neomercantilism.

It is not the scope of this paper to examine the role of OPEC as an organization, given that OPEC is fragmented between “price hawks” who favor high prices (like Iran and Venezuela), and “price doves” who do not mind low prices (like Saudi Arabia, Kuwait and the UAE) (Naughten, 2014). It is also not the scope of this paper to discuss the economic theories or economic equations of this price war, as I only intend to discuss the price war in terms of IPE theory.

One limitation to this paper is that it is not possible to know the intentions of the decision-makers. According to Fattouh, writing about oil decisions in Gulf Cooperation Council countries, like Saudi Arabia for example, is marred by a:

[...] poor understanding of the process of decision-making and traditions of governance in the Arab world [due to] the lack of transparency in GCC oil policy development [...] the lack of reliable sources of information, and the limited availability of data (Fattouh, 2015).

Similarly, according to Stevens, Aramco, the Saudi national oil company, shrouds itself in so much secrecy which makes it “extremely difficult” to judge the Saudi oil strategy (Stevens, 2012, p. 173). Despite this setback, the analysis in this paper will be based on the information available in news outlets and research institutions[1].

An important point to make would be how the Saudi Government sees the geopolitical importance of market share in the global oil market. The government in Riyadh sees that having a large market share ensures long-term economic and political advantages for Saudi Arabia, which would precede a short-term revenue maximization policy.

First, having a large market share would guarantee “demand security” for the vast Saudi oil supplies. Saudi Arabia has the largest, or one of the largest, oil reserves in the world (about 265 billion barrels). These oil reserves will not deplete before one hundred years by some estimates, and the Saudi economy needs to ensure that these revenues will remain sellable in the long-run. So Saudi Arabia needs to secure long-term external markets and customers to export this oil in the future. Revenue maximization is good for the Saudi economy in the short-term. But, in the long term, Saudi Arabia needs to ensure having a foothold in major markets to secure future sales on a large scale. Having a large market share would also deter any competing oil producers out of these markets.

Second, a large market share would ensure political influence in the importing countries. Without it, in Yergin’s words, Saudi Arabia would be reduced to “a more marginal role on the world stage,” which would run “counter to the fundamental percepts of the kingdom’s security policy.” As will be explained, the government in Riyadh can instruct Aramco to sell oil to certain countries even if at less profit, to ensure having good strategic and political relations with these countries (Ambah, 2008; Fattouh *et al.*, 2015; Marcel, 2006, p. 79; Worth and Moawwad, 2008; Yergin, 1992, p. 747).

The first section of this paper gives a brief explanation of the school of neomercantilism as a mainstream theory of IPE, and as the other face of the coin of realism (so to speak). The second section of this paper offers a literature review of how IPE dealt with energy issues, especially production policies and their effect on the neomercantilist competition between

states. The third section gives a historical background of the events which started in 2014 and led to the oil price war. The fourth section dissects neomercantilism into three of its main definitional components (namely the centrality of the state as the main actor, the primacy of political goals over economic goals and the zero-sum nature of dealings between states) and attempts to translate them into empirical indicators in the Saudi policy[2].

The research questions which the paper attempts to answer are:

- RQ1. Did the Saudi state intervene in the economic decision-making and decide that Saudi Arabia should maintain high oil production to start an oil price war?
- RQ2. Did Saudi Arabia sacrifice short-term economic profit for the sake of long-term political (and geopolitical) goals during the price war?
- RQ3. Did Saudi Arabia engage in a zero-sum game for market share where “relative gains” instead of “absolute gains” were the basic rule of the game, and the loss of one oil exporter’s market share is a gain for the other oil exporter?

2. The neomercantilist theory of International Political Economy (in comparison with other theories of International Political Economy)

The theory and practice of mercantilism, in its classic form, goes back to the period from about 1500 to about 1750. During this period, the great European powers were engaged in trade competition against each other, where each state tried to increase its exports and decrease its imports to maintain a surplus in the trade balance and accumulate as much bullion (gold and silver) as possible. Trade balance surplus, and bullion, were considered a source of national pride and power, and were used to finance the building of greater armies and military power for the purpose of colonization and waging war against the other great powers of the time. This classic form of mercantilism saw international relations as a zero-sum game, where the gain of one party necessitated the loss of the other party.

Today, the modern equivalent of this classic version of mercantilism is neomercantilism. There are two main differences between mercantilism in its classic form, and neomercantilism. The first difference concerns the time or the era. Historians tend to attribute classic mercantilism to the era before Adam Smith’s *The Wealth of Nations*, which was published in 1776 and offered a liberalist critique against the theory and practice of mercantilism. However, Smith’s theory of economic liberalism did not put an end to the theory or practice of mercantilism. The practice and theory of mercantilism which continued after the publication of Adam Smith’s *Wealth of Nations* is what IPE theorists call “neomercantilism.” Based on this, liberalism would differ with classic mercantilism in that the real wealth of nations is not in the amount of bullion, but in the nation’s productive capacity. (However, liberalism would agree with neomercantilism in that power flows from productive capacity). Nevertheless, liberalism disagrees with both of classic mercantilism and neomercantilism in that liberalism sees trade as a positive-sum game while classic mercantilism and neomercantilism see trade as a zero-sum game. This is discussed below in further detail (Kirshner, 1999, pp. 70-72).

The second difference between classic mercantilism and neomercantilism is the measure of a state’s economic power. Classic mercantilism measured economic power in terms of “bullion”; the gold and silver which the state accumulated as a result of a balance-of-trade surplus.

Contemporary neomercantilism, on the other hand, is not primarily concerned with a trade or a balance-of-payments surplus. According to Gilpin, neomercantilism “can take

many forms in the contemporary world”, including the desire for a balance-of-payments surplus, the imposition of import and/or export controls, the expansion of world market shares, preponderance in advanced technologies and other forms of economic power (Gilpin, 1975a, pp. 45-46).

According to Cohn, neomercantilism is the “IPE counterpart” of realist theory in IR. (Cohn, 2016, p. 55). The most important factor of this equivalence between neomercantilism and realism is that both approaches believe in power relations between the different actors on the international stage, where the strong overcomes the weak in an international power hierarchy.

Furthermore, both of realism and neomercantilism emphasize the centrality of the state in global political and economic events. Both view the world in terms of a zero-sum game, or relative gains, in which one state’s gain is another state’s loss. Like realists, neomercantilists give priority to politics over economics. Neomercantilists recognize the importance of the market (as do liberalists), but they believe that the market must serve the interests of the state, and that the government must make sure that the market serves the state’s power *vis-à-vis* other states.

Neomercantilists also believe that the state must “play an active role in promoting trade, shaping investment policy, and supporting national firms” (Cohn, 2016, p. 51, 55, 56). This interventionist role of the state is especially true, given the realist expectation that the state would intervene when the interests of its domestic actors diverge from the interests of the state and from the necessities of national interest, while liberalists would expect harmony between the interests of the state and the interests of the domestic actors (Kirshner, 1999, pp. 73-74).

In other words, according to Gilpin (1975a), Hettne (1993), Kirshner (1999) and Ziegler (2010), neomercantilism believes that political considerations have primacy over economic considerations, even if it meant the sacrifice of short-term economic gain. Furthermore, political activity decides the shape of economic activity.

Due to this equivalence between neomercantilism and realism, several scholars treat “realism” (in IR) and “neomercantilism” (in IPE) as one and the same paradigm, and do not offer deep differences between them. These authors simply equate “realism” and “neomercantilism” in their writings, without offering a distinction between both approaches. These include Gilpin who has called this approach “mercantilism”, “statism”, “protectionism”, “state-centric realism”, “economic nationalism” and other names, without offering a clear distinction between all of these different terms (Gilpin, 1975a, passim, Gilpin, 1987, pp. 31-34 and Gilpin, 2001, pp. 15-23). Jones stresses the similarities between mercantilism in IPE and realism in IR, arguing that mercantilism is “in accords” with the realist school of IR, since both believe that economic policy is to be “based upon the certainty of conflict with other [states] and the need to ensure that the state [is] optimally placed to sustain itself in such eventuality.” Jones seems to imply that what he calls “economic realism” is not the same as “neomercantilism”, as he says that both are “corollary” [he did not say “identical”] to each other, but he does not offer a distinction between them, and, throughout his work, he keeps treating them as one (Jones, 1986, p. 8, 10, 11, 14, 81 and passim). Nowell calls the paradigm “the realist-mercantilist theory”, and does not offer a distinction between realism and mercantilism (Nowell, 1994, p. 21 and passim).

Other authors, on the other hand, argue that “realism” does not simply translate to “neomercantilism”. Although they fully acknowledge that both approaches are equivalent to each other in IR and IPE, these authors do point out the differences between realism and neomercantilism. Cohn, for example, argues that realism in IR focuses on the military-security aspects of power, while neomercantilism as an IPE perspective focuses more on the

economic aspects of power. Another difference, according to Cohn, is that, although both of realists and neomercantilists see the state as having primacy over domestic actors, neomercantilists address the role of the domestic arena more than realists do, and this is due to the neomercantilist focus on economic issues. For example, neomercantilists would examine the relation between the state and the business corporations, and strategies to promote exports and decrease imports (Cohn, 2016, p. 5, 12, 51, 55, 56). Similarly, Kirshner argues that mercantilism focuses on many economic and monetary issues which are “not relevant for the study of realism” (Kirshner, 1999, p. 89). Indeed, even though realism and mercantilism “appear to go hand in glove with each other,” (to use the words of Drezner (2010)), most realists (perhaps with Robert Gilpin as “an obvious and important exception”) believe that “international economic exchange has no impact upon the international political system,” and most realists fail to incorporate domestic politics into their analysis (Drezner, 2010). Thus, says Kirshner, it would more accurate not to equate mercantilism or neomercantilism with realism (Kirshner, 1999, p. 89).

Neomercantilism is one of the three main schools in IPE. Another major school of IPE is liberalism. Both schools have common features; both believe that the state is the main actor in IPE, and both believe in the importance and impact of domestic political and economic actors on the foreign policy of the state. Nevertheless, there are differences between both schools. Neomercantilism believes in power politics, while liberalism believes in peaceful cooperative relations. Neomercantilism believes that political considerations of national security are given priority over economic considerations, and that the state sacrifices short-term economic interests for the sake of long-term political and security considerations. Liberalism, on the other hand, believes that economic considerations have precedence over political considerations; politics follow economics, not the other way around. Liberalism believes that the state is giving up some of its sovereignty to the corporations and non-state actors who engage in global economic interaction, and that the state cannot stop this trend. Neomercantilism, on the other hand, believes that the state is controlling the flow of these actors and can stop it if so chooses.

Neomercantilism believes that relations between states, including trade and economic relations, are based on zero-sum, relative gains, while liberalism believes that the interaction between states can be a positive sum game where all actors can emerge as winners from the interaction between states. As stated previously, liberalism as an ideology started with Adam Smith’s *Wealth of Nations*, published in 1776 as a critique to the mercantilist practices of the time (Cohn, 2016, passim and Gilpin, 1975a, passim).

Apart from neomercantilism and liberalism, a third trend in IPE is critical theory. It is based mainly on Marxism and Neo-Marxism, with their wide-ranging variations which make it difficult to sum them all up in one short paragraph. There are common features between Marxism and neomercantilism. Both schools believe in the inevitability of conflict between the actors in IPE. Both schools believe in power relations between the actors in IPE, where the powerful is dominating, or exploiting, the weak. Both schools believe that interaction in the realm of IPE is based on a zero-sum game, where one side’s loss is the other’s gain. However, there are differences between both schools. Neomercantilism believes that the state is the main actor, while Marxism generally believes that non-state actors, especially the multinational corporations, are the main actors in IPE. Neomercantilism believes that the state’s national interest takes precedence over economic factors, while Marxism believes that economic factors, especially the corporate interests of the multinational corporations, have precedence over the national policy of the state. There are variations between the different approaches and sub-theories within Marxism, which cannot all be tackled here. (Cohn, 2016, passim and Gilpin, 1975a, passim).

Based on the aforementioned, one would ask: How can we test a certain event, or a certain policy, for neomercantilism? To test if the ideology of neomercantilism was applied in the Saudi oil policy between 2014 and 2016, I attempt to focus on the three most important tenets, or definitional components, of neomercantilism and examine them closer; the active, interventionist role of the state, the primacy of political goals over economic goals and the zero-sum nature of international relations. This is done with the aim of translating these three definitional components of neomercantilism into empirical indicators.

3. Literature review

In this section, I divide the relevant literature into two categories. The first theme discusses the role of energy in neomercantilist IPE. The second theme tackles the place of price wars for market share in IPE theory and how it relates to Saudi oil production policies.

Several authors have previously used neomercantilism to discuss energy politics. Charles Ziegler, for example, focuses on Russia's energy exports. He argues that Moscow's use of its natural gas exports to expand Russia's influence in Europe and Asia is an application of neomercantilism, since the government in Moscow is employing the Russian energy resources and energy companies (private and state-owned) to achieve its political and strategic foreign policy goals. Ziegler's analysis of neomercantilism focuses on the primacy of the state or the government, and on the use of economic tools to achieve political and strategic goals. Ziegler does mention the competition between Russia and other producers, like the Middle Eastern producers, over the Asian oil market (Ziegler, 2010, *passim*), but he does not sufficiently analyze this competition from the perspective of the 'relative gain' or 'zero-sum' side of neomercantilism.

Leverett has coined the term "resource mercantilism," which he defines as:

[...] the use of economic and foreign policy instruments by national governments to help their state-owned national energy companies (NECs) secure access to overseas hydrocarbon resources on more privileged bases than simple contracts based on market prices.

Taking China and India as case studies, Leverett's contribution is that he offered two levels on which this state-NEC relationship works within "resource mercantilism." The first level is the political level, or the "top-down" approach where the government in Beijing or New Delhi instructs the NECs to base their economic decisions on the country's energy security. This level is the opposite of liberal economic practice, and sees energy resources as not simply an economic commodity, but as a strategic necessity which the international market cannot be trusted to provide. The second level is the economic or corporate level, or the "bottom-up" approach. At this level, the NEC (due to economic liberalization and restructuring, such as partial privatization or listing the company on various stock exchanges) is given autonomy to refuse some projects suggested by the government, if these projects are against the corporate profit interests of the NEC. Neither level offers a full explanation of resource mercantilism, so both have to be taken into consideration. Leverett then offers a critique of the resource mercantilism policy, saying that there is no evidence that the Chinese and Indian NEC investments in energy resources abroad would necessarily provide enough energy supplies for their home countries (Leverett, 2008, *passim*).

Leverett's work, despite being thorough and detailed, has a major flaw; His definition of "resource mercantilism" restricts mercantilism in the energy sector to only the demand side, or only to the question of how to secure energy resources for the consumers or purchasers. This would mean that oil producers, like Saudi Arabia or Russia for example, who need to secure foreign markets to export their oil to, would not fit in Leverett's definition of "resource mercantilism." Leverett leaves an academic gap where one needs to find a

definition for “resource mercantilism” which would incorporate both of the demand side and the supply side (i.e.: how to secure foreign markets for the exporters).

Regarding the literature on oil price wars, the 2014 oil price war was not the first time that Saudi Arabia raised its oil production and caused a decline in oil prices to weaken its competitors. A similar incident has happened back in 1986. Only a few authors paid attention to the Saudi application of oil price wars over history.

In December 1985, Saudi Arabia raised its oil production to intentionally lead to a reduction in global oil prices. Svante Karlsson, Robert Mabro and Daniel Yergin argue that OPEC’s 1986 oil price collapse was indeed a result of an oil price war launched by Saudi Arabia to protect its market share in the global oil market. There were two problems which led Riyadh to launch this price war in late 1985. The first problem was that OPEC, led by Saudi Arabia, wanted to regain the market share which it has lost to non-OPEC producers before 1986, especially Norway and the United Kingdom. The Saudi loss of market share, in Daniel Yergin’s words, was:

[...] reducing Saudi Arabia to a more marginal role on the world stage. The rapid fall away in political influence and significance [...] ran counter to the fundamental percepts of the kingdom’s security policy. (Yergin, 1992, p. 747).

The second problem was that, before 1986, Saudi Arabia was playing the role of swing producer[3], as it was reducing its own output to try to raise the global price of oil. Saudi oil production fell from 10 million barrels per day in 1981 to 2.2 million barrels per day in the summer of 1985, which was less than North Sea production. But cutting production meant lost revenues and loss of market share for Saudi Arabia. The Saudi budget started to suffer from deficit, and foreign reserves dwindled. This was an outrage for Riyadh; The Saudis were reducing their own production to keep the prices up, so that other producers would profit while Saudi Arabia was suffering from losses! Thus, OPEC and Saudi Arabia increased their production to fight for market share, even if this meant a reduction in the global oil price and in revenues from oil exports. Saudi Arabia doubled its output from 2 million barrels per day to 4.5 million barrels per day. Oil price fell from \$31 per barrel in November 1985, to \$10 per barrel in April 1986, and to \$6 in some cases. The problem was not resolved until Washington convinced the Saudis that such a policy was not good for the American and global economy. In July 1986, OPEC agreed to a price range of \$17-\$19 per barrel. Saudi revenues were down by 11 per cent due to the oil price war of 1985-1986, but Saudi Arabia won this price war, as it was able to protect its market share (Karlsson, 1986, p. 284, Mabro, 1998, passim and Yergin, 1992, pp. 747-760).

Only a few authors discussed price wars for market share. Robert Mabro is averse to oil price war policies which pursue larger market shares, arguing that it is “not a sensible policy” because its costs can be very high and its future benefits are “too uncertain.” “No oil-exporting country has the ability, that is the financial resources and the political power, to engage in price wars,” wrote Mabro. Oil price wars can be justified, according to Mabro, only if the collapse of export volumes and market share was “so significant as to require a drastic price war to improve position on the volume front” (as with Saudi Arabia in 1986, as previously explained), or when an exporter wishes to “gain entry into a particular market or increase its penetration.” But outside these specific instances, according to Mabro, the pursuit of market share would not be sensible policy (Mabro, 1998, p. 2, 39). Indeed, this paper proves Mabro’s point that, because price wars cause losses in revenues, and because the states who wage such price wars cannot sustain these losses for long periods of time, the price wars for market share usually do not work. The case of 2014-2016 shows the Saudi failure. In 1986, however, Saudi Arabia was genuinely under-producing and suffering from

losses due to its underproduction, so it had to wage a price war to protect its market share, and it succeeded [Table I](#).

The existing literature does not clearly make a link between price wars for market share on one side, and IPE theory on the other side. This paper fills a gap in the IPE literature which lacks enough work on linking global market share to state power, especially in such a strategic sector as the global oil market.

The following sections explain the historical background of the 2014 oil price war, followed by how the definitional components of neomercantilism were reflected in the Saudi oil policy of 2014.

4. Historical background: the oil price war of 2014-2016

In June 2014, oil prices rose to a high of \$112 per barrel due to instability in the Middle East ([Crude oil prices down sharply, 2015](#)). Within the span of a few months, however, oil prices

Year	Average price per barrel
1984	28.2
1985	27.01
1986	13.53
1987	17.73
1988	14.24
1989	17.31
1990	22.26
1991	18.62
1992	18.44
1993	16.33
1994	15.53
1995	16.86
1996	20.29
1997	18.86
1998	12.28
1999	17.44
2000	27.6
2001	23.12
2002	24.36
2003	28.1
2004	36.05
2005	50.59
2006	61
2007	69.04
2008	94.1
2009	60.86
2010	77.38
2011	107.46
2012	109.45
2013	105.87
2014	96.29
2015	49.49
2016	40.68
2017	52.51

Table I.
Average annual
OPEC crude oil price
from 1984 to 2017 (in
US dollars per barrel)

Source: "Average annual OPEC crude oil price from 1960 to 2018 (in US dollars per barrel)", *Statista*, accessed June 13, 2018, www.statista.com/statistics/262858/change-in-opec-crude-oil-prices-since-1960/

declined to \$47 per barrel in January 2015 ([Udland, 2015](#)). A year later, prices fell even further to \$27 per barrel in January 2016. This sharp decline in oil prices was due to a rise in global oil supplies and a fall in global demand for oil, especially with the Saudi-led decision by OPEC to maintain high oil production ([Riley, 2016](#)), which will be explained below.

The story of the oil price war could be divided into three main parts: the sharp decline in oil prices in 2014 despite the geopolitical threats in the Middle East, followed by the start of the price war (or Saudi Arabia's decision to "leave it to the market") ([Fattouh, 2015](#)), and ending with a series of agreements in 2016 (including the Saudi-Russian agreement of September 2016, the OPEC agreement of November 2016, and the agreement between OPEC and non-OPEC oil producers in December 2016).

The first part is the sharp decline in the global oil price in 2014. Oil prices reached a high of about \$112 per barrel in June 2014 due to the crises in Syria, Libya, Iraq and the rise of the Islamic State. Despite these geopolitical threats in the Middle East, however, prices declined rapidly to about \$60 per barrel in December 2014. There were several reasons for this decline in oil prices despite the geopolitical threats. The first reason was the decline in demand for oil in Asia and Europe due to the global economic slowdown. The second reason was the increased production in Libya, Angola and the USA ([Lorenzetti, 2014](#); [Moore, 2014](#); [Philips, 2014](#)).

The second part is the so-called "oil price war". Fearing that other global oil competitors would take up their market share, different global oil producers kept high production, and resisted calls to reduce their production to help raise the oil prices back to its previous levels. This oil price war saw three major producers competing against each other: Saudi Arabia (and OPEC), Russia and the USA.

The "oil price war" started with OPEC's decision in November 2014 (renewed every six months until June 2016) to maintain OPEC's oil production at 30 mbpd (million barrels per day). This was a high rate of production, and it led to a global decline in oil prices. Saudi oil production reached record levels of over 10 mbpd. OPEC took this decision to keep global oil prices down, force the American fracking (slang for "hydraulic fracturing", a new technique to extract oil from shale rock in the USA) out of business by making its profits less than its costs, and maintain OPEC's market share which was being taken over by non-OPEC production ([Keating, 2014](#); [Reguly, 2015](#)). Publicly, however, OPEC declared that this move was a purely economic decision, with no political intentions against any country. ([Davos, 2015](#)).

(OPEC was not entirely united on this Saudi-led decision to keep production high, however. There were calls from within OPEC to reduce production and raise prices. These calls came from countries like Iraq, Iran, Venezuela, Algeria and others, who needed higher oil prices to balance their budgets. ([Algeria calls for OPEC, 2014a](#); [Algeria calls on OPEC, 2014b](#); OPEC calls for widespread, 2014; [OPEC rejects call, 2014](#)) But Saudi Arabia was able to overcome this disagreement within OPEC and convince all of the OPEC members that it was better to keep production high and prices low for a certain period, to fight American fracking which was threatening OPEC's market share ([Inside Story – Who's really benefiting, 2014](#)).

The Saudi Ministry of Oil defended the Saudi-led OPEC decision to keep production high by saying that Saudi Arabia only wanted to defend its market share. It added that this was actually good for the global economy, because another oil producer with less quality oil would fill the Saudi market share if Riyadh gave it up. Also, the Ministry said that Saudi Arabia was showing its commitment to market principles by not changing its production to reduce prices, adding that the Saudi economy was strong enough to endure the low oil prices and the decline in revenues ([Ferro, 2015](#); [Raval, 2014a, 2014b](#)). Similarly, Saudi Aramco said

that oil was “a market-driven business” so it would be wrong for Riyadh or OPEC to reduce production and “control the market” (McAuley, 2014). This Saudi pro-liberal rhetoric, which was displaying support for free-market mechanism, was actually a diplomatic cover-up for a Saudi neomercantilist agenda. Despite the pro-market discourse, the Saudi state was intervening to prevent a reduction in oil supplies and an adjustment of oil prices, for the purpose of protecting the Saudi long-term national security and market share at the expense of the short-term profits and the oil revenues flowing into the Saudi economy.

Saudi Arabia was not the only country willing to endure low oil revenues to protect its market share. Russia, the world’s second-largest oil exporter after Saudi Arabia, said that it was prepared to keep production at a high level (about 10 mbpd) even if the price of oil fell below \$60 per barrel, (which was \$40 lower than Moscow needed to balance its budget) (Tully, 2014).

Similarly, the American Government did not express concern about the low oil prices. In fact, an increase in the price of oil by \$10 per barrel would reduce real GDP growth in the USA by roughly 0.4 per cent for the next four quarters (Morgan Stanley, 2014). This is why the American economy usually welcomes a decline in oil prices, unlike other oil producing countries whose economies are heavily dependent on oil exports revenues (Colman, 2015).

Several conspiracy theories were raised about this sharp decline in oil prices and OPEC’s refusal to reduce production. For example, Russian President Vladimir Putin hinted at a possible Saudi- American conspiracy against Russia, and at a possible conflict between traditional oil and American tight oil, but admitted that these were only speculations without real proof (Putin says oil market price conspiracy, 2014). The Iranian Supreme Leader and Venezuelan President made similar statements (Iran’s supreme leader says plunge in oil price political, 2015).

The third part of the story is the steps taken by Saudi Arabia and other global oil producers, especially Russia, to end the oil price war in late 2016. Steps to end the oil price war included a series of agreements between Riyadh and Moscow, and agreements between OPEC and non- OPEC producers. Another step was OPEC’s decision in November 2016 to cut production by a total of 1.2 mbpd (million barrels per day) for the first time since 2008, as will be discussed below.

On September 5, 2016, on the sidelines of the G20 summit in Hangzhou, China, Saudi oil minister Khaled Al Falih and Russian energy minister Alexander Novak signed a joint statement which said that both ministers “recognize the current challenges in the supply side of the global oil market [...] which made the market, as a whole, more volatile and therefore unstable.” To solve this problem, both ministers agreed to jointly and continuously review the oil market and recommend joint actions to secure the stability of the oil market (TEXT – Saudi-Russian joint statement, 2016). This was a major step to restore normality to the oil prices and to end the oil price war.

This was followed by two OPEC agreements in late 2016. The first OPEC agreement took place on November 30, following the OPEC meeting in Vienna, when OPEC members agreed to reduce production and set ceilings and caps for production. In this agreement, OPEC agreed to reduce production by 1.2 mbpd, down to 32.5 mbpd, which was the January 2016 level. (The OPEC ceiling was officially 30 mbpd, as explained previously. But the actual OPEC production exceeded this amount due to record output from Saudi Arabia, increased Iraqi production, increased Libyan production, the exemption of newly returned member Indonesia from OPEC commitments, and Iran’s insistence to raise its production back to its pre-sanctions levels). Saudi Arabia, alone, agreed to cut its production by 0.486 mbpd, which meant that it would bear 42 per cent of this oil output reduction. Iraq agreed to cut its production by 0.210 mbpd, while Iran

was the only country which was allowed to raise its production (by an amount of 0.09 mbpd). Libya and Nigeria were exempted from the agreement ([El Gamal et al., 2015](#); [OPEC should consider return, 2015](#); [Razzouk et al., 2016](#)).

The second OPEC agreement was on December 10, 2016, between the (then) 13 OPEC members[4] and 11 non-OPEC countries (Azerbaijan, Bahrain, Brunei, Equatorial Guinea, Kazakhstan, Malaysia, Mexico, Oman, Russia, Sudan and South Sudan). In this agreement, the 11 non-OPEC producers agreed to cut their production by 0.558 mbpd, where Russia alone would cut 0.3 mbpd ([Non-OPEC oil producers to cut output, 2016](#)). The OPEC production cut of 1.2 mbpd and the non-OPEC cut of about 0.6 mbpd brought the total production cut to about 1.8 mbpd[5].

Following these agreements, one has to ask about the result of the price war: Did Saudi Arabia win or lose the oil price war? The answer to this question would depend on the target of the price war to begin with.

If the Saudi target was to “kill fracking” in the USA, then Riyadh has definitely failed. American fracking has shown its ability to survive and even improve by increasing the efficiency and reducing the cost of extraction[6]. For example, a 2016 report by the Energy Information Agency (EIA, a research institution affiliated to the US Department of Energy) concluded that:

[...] average well drilling and completion costs in five onshore areas evaluated in 2015 were between 25 per cent and 30 per cent below their level in 2012, when costs per well were at their highest point over the past decade. ([Trends in US oil and natural gas, 2016](#)).

Furthermore, because of breakthroughs in production technology and efficiency, fracking acquired the ability to stay competitive even with oil prices as low as \$45 per barrel ([Gramer, 2017](#)).

If the target was to maintain the Saudi market share, then Riyadh has, once again, lost the price war, as it is difficult to find an indicator which shows that Saudi Arabia has actually won the oil price war. As the figures in the next section will show, Saudi Arabia has lost market shares to Iraq and Iran in China and other Asian states, has lost market share in the American market due to fracking, and has suffered domestic fiscal problems because of the loss of revenue as a result of this price war[7].

The Chinese demand for oil, for example, has been leading the growth in global demand for oil in recent years. Therefore, the data on China’s imports of crude oil offer an approximate picture of the oil exporting countries who are gaining market share and those who are losing in the global oil market. Even though this would not be a correct scientific method to study the global oil market dynamics, the Chinese oil import numbers can be considered a minimized reflection of the global oil market ([Russel, 2017](#)).

The Saudi share of Chinese oil imports decreased from 19 per cent in 2013 to 16 per cent in 2014 to 15 per cent in 2015. Russia’s exports to China, on the other hand, increased from 9 per cent in 2013 to 13 per cent in 2014 to 20 per cent in 2015 ([Marcon International, 2019](#); [Lim, 2015](#); [Exceed KSA, 2019](#)). In 2016, Russia surpassed Saudi Arabia for the first time ever as China’s leading crude exporter ([Aizhu and Meng, 2017](#)). American oil exports also found their way to China and competed against Saudi Arabia, OPEC and Russia in the Chinese market ([Bershidsky, 2017](#)).

Saudi Arabia also lost market share in the USA. The Saudi share of US oil imports fell from 17 per cent in 2013 to 14 per cent in 2015 ([Raval, 2016](#)). The Saudi loss of market share in the American market was a gain for the American oil producers, as the USA no longer needed to import as much oil as it used to in the past, given the increased supply from domestic American producers.

Saudi Arabia was more fortunate in Europe, as Saudi oil exports increased their market share in Europe at the expense of Russia, which always considered Europe to be its traditional export market for oil and gas (Widdershoven, 2017) Table II.

In addition to this loss of Saudi market share, Saudi reserves fell from \$746bn to \$536bn between 2014 and 2016. The drop in oil revenues, combined with the costs of Operation Decisive Storm in Yemen and the generous Saudi system of subsidies and low taxes, resulted in an unsustainable economic situation. This led to a downgrade in Saudi credit rating in 2016 (Borroz and Meighan, 2017). Fitch downgraded its rating of Saudi Arabia from AA in August 2015 to AA- in April 2016, Standard and Poor's downgraded the Saudi rating from AA- in February 2015 to A+ in October 2015 to A- in February 2016, and Moody's downgraded Saudi Arabia's rating from Aa3 in 2011 to A1 in May 2016 (Moody's downgrades Saudi Arabia's, 2016; Saudi Arabia – Credit Rating, 2018).

The question of this paper is: Does the oil price war of 2014 reflect neomercantilism on the part of the Saudi Government, or not? The next section tests for neomercantilism.

5. Testing for neomercantilism: the definitional components of neomercantilism as applied to the 2014 oil price war

Three main tenets of neomercantilism are tested to see if they were reflected in the Saudi oil price war of 2014. The first tenet is the centrality of the role of the state, or government intervention. The second tenet is that political and geopolitical imperatives have precedence over short-term economic gain. The third is the zero-sum nature of the relations between states. If these characteristics are evident, then it would show that the Saudi policies in 2014-2016 were a reflection of a neomercantilist policy.

Regarding state intervention (the first tenet), Janice Thomson (1995) argues that a part of a state's sovereignty is "having the authority to define the political". This means that the government decides which issues are "political", (which means that the government should intervene directly in this issue), and which issues are non-political (i.e. economic, social,

Country	2013 (%)	2015 (%)
South Africa	52.9	21.9
Taiwan	35.8	32.2
Japan	35	35.6
South Korea	31.3	30
Belgium	19.8	26.7
China	19.4	15.4
France	18.3	18.6
Thailand	18.1	17.4
Brazil	18.1	22.6
India	18	19.7
USA	17.1	14.4
Spain	14.1	10.5
Canada	12.1	13.2
Italy	11.6	8.8
The Netherlands	11.3	7.9

Notes: Even though Saudi Arabia is a low cost producer of oil, it has lost ground to rivals including Russia and Iraq in key markets. The figures below are from facts global energy (FGE)

Source: Anjli Raval, "Saudi Arabia loses oil market share to rivals in key nations", *Financial Times*, March 28, 2016, www.ft.com/content/5e8c1d52-f19f-11e5-aff5-19b4e253664a

Table II.
Saudi market share
by percentage of total
country imports

cultural, religious and similar low-politics issues, in which case the government would delegate authority to non-state actors or institutions) (Thomson, 1995, p. 222).

In certain oil-producing states, if the government is to directly intervene in oil policy, or treat oil as a “political” issue, then this would be through the state-owned national oil companies (NOCs). These national oil companies are considered political tools of the state, and they have played a role in the oil price war of 2014. Neomercantilism, which focuses on the role of the state, would view these state-owned NOCs as economic tools which the state uses to achieve its political targets. Examples include Aramco of Saudi Arabia and Rosneft of Russia (Stevens, 2012, p. 185, 218).

Because oil plays such a crucial role in the Saudi economy, oil pricing and production decisions are determined at the highest levels of government, according to the Saudi Arabia Monetary Agency (SAMA) (Al-Yousef, 2010). The Government in Riyadh (the Saudi oil ministry) is responsible for dealing with OPEC, oil supplies and production volumes, environmental laws, and opening the Saudi oil sector to private investors, while Aramco is responsible for applying these directives (Marcel, 2006, p. 78, 79).

Another factor which would show the primacy of the state, according to the school of neomercantilism, is the way in which the actors, or the players, tried to put the oil price war to end. The key players, or actors, who agreed to end the price war were not the oil companies. Rather, it was agreement between the governments in Riyadh and Moscow which ended the price war, in addition to the agreements involving the OPEC governments and the non-OPEC governments. The involvement of the states, or the governments, through their oil ministers, shows the direct involvement of the state, which is a main feature of neomercantilism (TEXT – Saudi-Russian joint statement, 2016).

On the second tenet, the primacy of political goals over economic goals, Gilpin argues that if tension occurred between political and economic considerations, then politics and the state’s interests would take priority over economic considerations. The “essence” of neomercantilism, Gilpin says, is “the subservience of the economy to the state and its interests – interests that range from matters of domestic welfare to those of international security” (Gilpin, 1975b, p. 25).

The neomercantilist criterion of the “subservience of the economy to the state” applies to the Saudi refusal to increase oil supplies between 2014 and 2016, to protect their market shares. Two points have to be clarified, however. First, it is not clear that the objectives of the Saudi state and those of Aramco diverge from each other (Stevens, 2012, p. 186, 187). This means that the “political” and the “economic” are usually the same, but the fact that the government takes decisions of production (see the previous criterion) shows that the “political” side has more control over the “economic” side.

Second, because of its legacy as a former American private firm^[8], Aramco has a tradition of managing itself by itself without intervention from the Saudi Government, except for oil production levels which are considered a “political decision” taken by the Government in Riyadh (Stevens, 2012, p. 193, 209, 210, 211, 216).

According to Marcel, the government in Riyadh gives directives to Aramco to maintain its strategic market share (in the American, European or Asian markets, for example), even if at lower profit, to maintain good relations with these countries. Here, Aramco plays a crucial role in supporting these political priorities of the Saudi state (Marcel, 2006, p. 78, 79)^[9].

In mid-2015, Saudi Arabia needed an oil price of \$87 per barrel to balance its budget, (while Russia, for example, needed an oil price of \$105 to balance its budget) Oil break-even prices, 2015.

Oil prices at the time were around \$50 per barrel, which was much less than what the Saudi budget needed. But Riyadh was willing to sacrifice the price in return for what it saw as a long-term goal of maintaining its market share.

As the figures on Saudi oil market shares show, however, this policy has actually failed.

The third important tenet of neomercantilism is that dealings between states are based on a zero-sum nature (as opposed to a positive-sum game), or relative gains (as opposed to absolute gains). As the figures on the market shares show, one oil exporter's gain in a foreign market is another oil exporter's loss. We have seen, for example, that Russia's gains in the Chinese market are a loss for the Saudis, the Saudi gains in the European markets are a loss for Russia [...] etc.

Again, the presence of this third important tenet is further proof that the Saudi policy is engaged in a global neomercantilist competition with other major oil exporters.

6. Conclusion

This paper uses neomercantilism, as a theory of IPE, in an attempt to make a theoretically sensible link between the political factors and the economic factors of the global oil market. Despite not being able to know the intentions of Saudi decision makers due to the lack of publicly available information, this paper attempts to fill a gap in IPE. No previous paper has linked energy, or the oil price wars, to the three definitional components of neomercantilism; the primacy of the state's role, the primacy of political and security implications over short-term economic imperatives, and the zero-sum nature of the global political economy.

After dissecting neomercantilism into the three main characteristics stated above, this paper deduced that these three tenets of neomercantilism were indeed reflected in Riyadh's oil price war. Riyadh has sacrificed the short-term economic benefits of high oil prices to protect a long-term national security goal; market share. Maintaining the Saudi market share in the global oil market ensures demand security in the long term and ensures a degree of Saudi political leverage in the importing countries. Another evidence of the primacy of the state is that when a series of deals were reached in 2016, it was the governments, not the oil companies, who sealed these agreements. Regarding the zero-sum nature of the oil market, the figures do show that one oil producer's market gain is another's market loss. The Saudi oil price war of 2016 has failed to gain the market share which Riyadh has lost in Asia or the USA, due to strong competition from Russia, American fracking, and other oil producers, and because the Saudi economy was unable to sustain the costs of the price war.

Although neomercantilism, as a theory, can explain the global oil market, the results of this paper call into question the feasibility of the practice of neomercantilist policies in the global oil market, and the extent to which such policies can protect the economic and national security interests of states. It also calls into question the ability of liberal and Marxist theories (and policies) to explain the economic and geopolitical vagaries of the political economy of the global oil market.

Notes

1. [Stevens \(2012\)](#) uses the same approach.
2. I have borrowed the phrase "translating the definitional components into empirical indicators" from [Thomson \(1995\)](#).

3. A “swing producer” is an oil producer whose task was to increase and reduce its oil supplies to “absorb the fluctuations” in global supply and demand for oil, to help adjust the global oil supplies and thus moderate the global oil price (Al-Yousef 2010, Passim and Kemp, 2017).
4. Equatorial Guinea joined OPEC in May 2017, thus becoming the fourteenth member of the organization.
5. There are indications that the oil price war may not be over yet, despite these agreements between Saudi Arabia and Russia. For simplification, however, I will discard these further developments and stop the historical narration and analysis at the time of the agreements in late 2016.
6. Even as oil prices fell in 2016, US oil production only fell by about 800,000 barrels a day, but then quickly bounced back in 2017 to more than 9 mbpd (Gramer, 2017)
7. Other analysts would argue that Saudi Arabia’s policy managed to add 1 per cent to Saudi market share, but this is a temporary, short-term gain which has come at large costs for Riyadh and can be easily lost again, especially that American shale production has managed to adapt to the low-price market and reduce its costs (Upadhyay, 2016)
8. The origins of Aramco go back to the 1930s when American major oil companies established a company in Saudi Arabia to extract oil.
9. However, Marcel has told the author in an e-mail in July 2018 that this trend of government intervention may have receded a little, with the partial privatization of Aramco and with the advent of the reformist policies of King Salman and Prince Mohamed bin Salman.

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