Saudi Arabia to Cut Oil Production Sharply in Bid to Lift Prices

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Saudi Arabia said it would unilaterally cut 1 million barrels a day of crude production starting next month, a surprise move signaling the kingdom's worry that a resurgent coronavirus is threatening global economic recovery.

The announcement Tuesday came after Riyadh agreed earlier in the day with other big producers to keep the group's collective output flat, after a now-monthly assessment by the Saudi-led OPEC cartel and a group of big producers led by Russia. In that deal, the two groups, collectively called OPEC-plus, agreed to a complex deal to hold production broadly unchanged from current levels.

Oil prices, which had already risen sharply on news of the OPEC-plus deal, soared on the Saudi announcement. In early afternoon trading Tuesday, West Texas Intermediate futures, the U.S. benchmark, were up 5.2% to $50.11 a barrel, passing through the $50 mark for the first time since last February, though it settled up 4.6% at $49.93. Brent crude rose 4.9% to $53.6070 a barrel.

Saudi Energy Minister Abdulaziz bin Salman said the unilateral move was made "with the purpose of supporting our economy, the economies of our friends and colleagues, the OPEC-plus countries, for the betterment of the industry."

While a boon to oil-dependent countries such as Saudi Arabia, the price rebound also is good news for an energy industry laid low by the demand-sucking pandemic. Oil companies including Exxon Mobil Corp. and Royal Dutch Shell PLC have taken large write-offs, cut jobs and slashed spending plans to adjust for what looked like a long period of low oil prices. Shell and BP PLC cut their dividends for the first time in years.

In recent months, though, prices started bouncing back more strongly than expected. Many economies in Asia, particularly China, seemed to have put the pandemic behind them. Several Western vaccines have been approved for use, raising hopes that governments there could help curb the spread of the virus, too, and get economies humming again.

Companies most likely to benefit from any sustained higher prices are the nimble U.S. shale producers that can more quickly ramp production up and down. If oil prices stay firmly above $50 per barrel, shale companies would spend roughly $62 billion this year on oil-and-gas production, about 11% more than they would have spent if prices were in the mid-$40 range, according to consulting firm Rystad Energy.

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More recently, though, producers big and small have watched warily as virus cases soared in the U.S. and Europe and vaccine efforts, at least in the West, moved slower than many expected. A new variant of the virus, first identified in the U.K., has sent cases soaring there and has since been identified in many other countries, including the U.S.

Saudi Arabia's move comes after it has ceded in recent years some of its oil-market clout to Russia. The two have long had a hot-cold relationship working together to stabilize prices. In recent months, Russia insisted on being able to open its taps, fearful it could lose market share to shale producers. Saudi Arabia pushed to move more cautiously.

Christyan Malek, head of oil-and-gas research at JP Morgan, said the Saudi cut could hurt the kingdom's market share in the short term, but that it also underscored its unrivaled ability to quickly turn on and off the spigot to move prices. "A small cut now is no big deal," he said. "Small pain for massive gain later."

Earlier Tuesday, an informal group of some of the world's biggest oil producers effectively agreed to maintain their collective oil output at current levels through February, warning of heightened risks to the global economy—and to oil demand—from a resurgent coronavirus.

In a statement Tuesday confirming the deal, the consortium, which includes the 13-member Organization of the Petroleum Exporting Countries and a Russia-led group of 10 producers, said "rising infections, the return of stricter lockdown measures and growing uncertainties have resulted in a more fragile economic recovery."

The group has said it is committed to eventually restoring almost 10 million barrels a day—or about 10% of pre-Covid-19 global demand—of production that it cut at the beginning of the pandemic to steady prices. But so far it has restored just 2.5 million of those cuts. In recent months, it has signaled that restoring further production would take much more time than anticipated.

The OPEC-plus deal wasn't straightforward. It publicly accommodated Russia's insistence that it be allowed to open its own taps to protect market share. OPEC-plus said Russia and Kazakhstan, which had both opposed keeping overall group production flat, would be allowed to increase output by a combined 75,000 barrels a day in both February and then another 75,000 barrels a day again in March.

The monthly allowance—accounting for just 0.075% of 2019 global demand—was interpreted by markets as a face-saving concession to Russia. Saudi Arabia, meanwhile, told delegates it would agree to compensate for the small boost by deepening its own cuts, meaning the group as a whole wouldn't lift production, according to delegates. But the kingdom didn't signal to fellow OPEC members or Russia the scale of its compensating cut.

At the height of last year's coronavirus outbreak, OPEC-plus agreed to cut output by a record 9.7 million barrels a day and envisioned restoring it in increments of 2 million barrels a day assuming demand would return. In the summer, the group moved to return the initial 2 million barrels, and last month agreed to add a further 500,000 barrels a day in January.

Russia initially was opposed to keeping current production levels and had pushed for an increase of another 500,000 barrels a day for February, according to delegates familiar with the discussion. Moscow argued that oil demand would return as world-wide vaccination programs start to make a dent in the pandemic, delegates said.

But Saudi Arabia and most other producers wanted the current output restrictions extended, people familiar with their view said, since they were concerned about the return of lockdowns and what they considered the slow rollout of vaccines. Algeria, for instance, pushed for them to be maintained until the end of March, they said.

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