

Answer to Question

The Oil Crisis and Its Repercussions

(Translated)

Question:

The news reported the sudden drop in the price of oil, especially Texas oil, until it reached about \$30 below zero. Even Brent crude, famous for its regular trading, fell about 9% to \$25 a barrel, and the reasons are varied, whether it was because the oil tanks became completely filled or almost overflowing, or due to the effect of the Coronavirus that led to a decline in the economy and the decrease in demand for oil... etc. What are the causes of this oil crisis? Is it continuous? And how does it affect the American and global economy?

Answer:

To realize the reality of the oil crisis in general and the American oil (West Texas) in particular and its impact on the American and global economy, it is necessary to know three economic and political circumstances and their particular impact on Texas oil, then the spread of its impact to Brent oil and then to the American and global economy:

First: Effect of the Coronavirus on oil consumption:

Since the beginning of this year, when the Coronavirus started spreading from China and then to Europe and then to America, and what accompanied this of the imposition of quarantine measures and the suspension of many sectors of the economy in each country, as well as the state of paralysis that affected the movement of airlines due to the travel ban between many of the main countries, especially Europe and America, in fear of the transmission of infection, in addition to the massive confusion in international trade resulting from the sharp lack of demand of non-food and medical goods, then it affected the movement of transport, knowing that land and air transport consume 68% of the oil supply (Independent Arabic, 24/4/2020). And all this led to a global setback for oil demand due to Coronavirus, and this setback was deepening more and more with the increase of the epidemic outbreak from one country to another. The epidemic is accompanied by the paralysis of the economic sectors in every country to which the epidemic is transmitted, but the relationship of this with oil was uneven, so when the epidemic moved to the main western European countries it caused a sharp decline in global demand for oil, because these countries are a big consumer of oil. When the virus reached America and hit it hard, and it consumes 20% of the world's oil, the oil price crisis declined sharply. In digital terms, the demand for oil has collapsed by nearly 30% in a world that consumes nearly 100 million barrels per day, and we take only two statements from the total statements that confirm this collapse in demand:

1- The first statement: [The International Energy Agency predicted today, Wednesday 15/4/2020, that the global demand for oil will decrease by 29 million barrels per day on an annual basis in April, to record levels not seen in 25 years... (Al-Wafd Newspaper website on 15/4/2020)].

2- The second statement: [Russian Energy Minister Alexander Novak announced that the global demand for oil decreased by 20-30 million barrels per day, saying: "We have reached the bottom of the global demand for oil now." (Al-Arabiya Net, 22/4/2020)].

Thus, the demand for oil collapsed at a rate that was not conceivable except in circumstances of world wars! And all of this happened in the period (3-4 months), that is, during the Coronavirus crisis, until Texas oil reached the deep bottom, i.e. about -37, on 20/4/2020, which was called "Black Monday".

Second: The second circumstance is the political circumstance:

Since oil is a strategic commodity, the countries use it to strike other countries, and we are talking here about the American policy that pushed Saudi Arabia towards the oil price war with Russia just one month ago, and to clarify that:

1- America was forcing Russia to reduce its oil production to maintain high oil prices so that the American shale oil companies can compete in the markets, because extracting the American shale oil is very costly, and with this policy Saudi Arabia succeeded, in 3 years, to get Russia to join OPEC in reducing production within the new group known as OPEC Plus by 2.1 million barrels per day. This Saudi agreement with Russia expired at the end of March 2020. It was an agreement before the spread of Coronavirus, and its end coincided with the spread of Coronavirus.

2- With the spread of the Coronavirus in China and the beginning of its transmission to spread in Italy, oil prices started to collapse and reached \$45 per barrel (Brent), and this price level and the continued decline are a danger to American oil producers, and threatens to take them out of the market, and therefore the price must be raised. Then America pushed Saudi Arabia to put pressure on Russia to further reduce production to face the continuing decline in global oil demand due to the virus, so the OPEC Plus meeting took place on 6/3/2020 when Russia refused any additional production cut, for fear of compensating America for the reduction in shale oil!

3- With the failure of the aforementioned OPEC Plus meeting, oil prices collapsed immediately by 10% due to the spread of news of the differences of the OPEC Plus group.

4- A few days after the meeting failed, Saudi Arabia sparked a price war against Russia to force it to take the new cut in five steps:

a- The first step: it abandoned the first agreement (reducing 2.1 million barrels) despite Russia's announcement of its commitment to this previous agreement,

b- The second step: is a huge increase in its oil production, starting from April 1st (the date of the end of the first reduction agreement with Russia) of 12-13 million barrels per day despite the problems of global oil demand due to Coronavirus,

c- A reduction to its Asian clients by \$6 a barrel, the first in history with this level of discount,

d -By this, it wanted the reduction and more of it, for customers dealing with Russian oil to take Russia's share of the market,

e- Hiring giant oil tankers to use them as floating tanks at sea, in order to drown the market with surplus oil.

5- With these steps by Saudi Arabia that were announced in the few days after 6/3/2020 (the failed OPEC Plus meeting), oil prices collapsed by a third (oil prices lost up to a third of their value on Monday in their biggest daily loss since the Gulf War in 1991, after Saudi Arabia indicated that it would increase production to increase market share, while the outbreak of the Coronavirus actually caused a surplus in supply in the market! Then the Brent Crude futures fell 22 percent at \$ 37.05 a barrel, after having previously dropped 31 percent to \$31.02 a barrel, which is the lowest level since 12/2/2016... (Reuters 9/3/2020). Note that Brent Crude is extracted from the oil fields in the North Sea.

And Brent Crude is a mixture of Brent Crude oils - Forties, Oseberg and Ekofisk, and it is used as a standard for pricing two thirds of the world's oil production, especially in European and African markets, and is sometimes exported to the United States and some African countries, if the price is appropriate, after considering shipping costs. Brent crude futures are traded on the Intercontinental Exchange (ICE) in London, meaning that Saudi Arabia, through these steps, pushed oil prices down, and after 1/4/2020, when Saudi steps were taken to be implemented, after the OPEC Plus agreement with Russia ended on the end of March, the oil surplus has become noticeable in the market, which pushed oil prices (compared to Brent) down to less than \$30 during the month of April 4 and before 20/4/2020.

6- This Saudi policy was an American policy to put pressure on Russia, but it was a policy that was drawn up in Washington about two months ago, that is, before the new dimensions of the demand for oil collapse, due to the continued outbreak of Coronavirus with severity, especially within America. With the result of these two factors (Saudi Arabia's policy, pushed by the United States, and the sharp increase in the collapse of demand for oil) the tremendous demolition that the Trump administration made to strike Russia started to strike right and a left and did not exclude its shale oil companies! In other words, what America had planned, to cut oil prices, was not expected to reach this low, and this was caused by the two factors working together: American (Saudi) policy against Russia, and the continuous collapse in world oil demand, that which was not so visible when setting that American policy. The pressure on shale oil companies increased in America. On 2/4/2020, "Witting Petroleum" announced bankruptcy, and a hundred shale oil companies stood on the brink of bankruptcy, because oil prices on the market were lower than production cost prices: (the marginal cost per barrel of shale is about \$35 a barrel... (Arab Markets website, 11/3/2020) According to The Independent Arabic 24/4/2020, West Texas oil futures ranged on Thursday 23/4/2020 between \$15 for June delivery and approximately \$27 for September delivery, and all futures contracts until the end of 2020 were under the price of \$30 and this puts pressure on shale oil.

7- Because of these dangerous conditions that the American oil industry is going through, due to the outbreak of the Coronavirus epidemic, the American administration made many announcements of its intention to intervene between Russia and Saudi Arabia to return to production cuts, and the US President called the Russian President, whose greed was aroused, for the return of communication with America and in coordination with it (not with Saudi Arabia) on oil prices. Trump also contacted Saudi Arabia; Trump said: "We had an excellent conversation with President Putin. We had an excellent conversation with the crown prince." (Euronews, 1/4/2020)

In sum, it can be said that the Trump administration has sponsored a Russian-Saudi agreement to reduce oil production, the largest in history, by about 10 million barrels of oil per day: (OPEC members and their allies reached a standard agreement to reduce global oil production by 10 percent after reduced demand... What has been confirmed so far is that OPEC and its allies will cut production by 9.7 million barrels per day) (BBC, 12/4/2020). This agreement begins implementation on 1/5/2020 and lasts for a period of two months, after which the signatory countries consider the reality of the global demand again to decide the next step. It is a short-term agreement, for two months, awaiting a rise in global oil demand at the end of June. However, it is noticed that the oil price crisis has reached such a depth that the markets did not respond to this very large agreement, so prices did not rise only marginally, but Brent prices fell back below 30 dollars. This is explained by the global demand has decreased by 30 million barrels per day and reduction in production by 10 million barrels per day does not help!

Third: The third circumstance is the US oil reserve.

There are two types of oil stocks in America, the first is the state's strategic reserve, and the second is the companies' stocks. This circumstance, along with the other two circumstances, contributed to the deepening of the oil crisis: part of it relates to the state of the strategic stockpile, while the other part is specific to West Texas Oil, and to clarify that:

1- The strategic oil reserve (of the country) in general is usually underground tanks to store the oil extracted for use in times of crisis, and many countries have built these tanks after the recommendations of the International Energy Organization due to the oil crisis in the war of 1973. Each of the countries of the main consumer countries has its own oil tanks, which can accommodate enough of its need for 30-90 days in case it is cut.

2- In 1975, the US Congress enacted legislation that obliges the federal government to create sites to store sufficient quantities of crude oil to secure the demand for it in the event that supplies are exposed to any type of acute risk. American storage sites are located on the coasts of the

states of Texas and Louisiana, the state is responsible for their tight guarding, and the maximum amount of this strategic stock in America reached 727 million barrels in 2009. In addition to federal reserves, American companies working in the energy field store their own quantities that are equal in total to the Federal Reserve, such surface tanks of companies are numerous in Texas, being the largest state in which oil is produced in America for a long time, which is called "West Texas Crude", as well as in neighboring Oklahoma state, from which Texas oil is transported to the depth of the American mainland.

3- With the previous collapse of oil prices on 6/3/2020 and the ensuing price war between Saudi Arabia and Russia, many countries, especially America and China, started to fill their strategic oil reserves, and Trump had rejoiced at the low prices at the time. America worked to buy cheap oil from Saudi Arabia or others, and before the "Black Monday" came, Texas tanks were somewhat full, if not totally. Thus, the problem of oil stocks has reached the degree of aggravation and saturation, so that directing more extracted oil (in the event of not selling) to storage has become a complex issue, and sometimes not available, meaning, the closing of the storage channel as a solution to oil producers, especially in Texas.

4- Thus, the American strategic oil reserves have been filled with a large percentage, and oil tankers operate at sea as storage facilities, thus exacerbating the problem of storage, as it extended to storage facilities of the West Texas oil at its delivery point at Cushing, Oklahoma State, north of Texas, (and the quantities of crude stored in the United States, especially in Cushing, where the delivery point for West Texas Intermediate U.S. crude is in Oklahoma, with refineries reducing their activities in the face of weak demand (Al-Jazeera Net, 20/4/2020), and the maximum storage capacity of Cushing's point is 76 million barrels. Oil contract holders can receive the same oil usually in Cushing during the time for those contracts, and they can store it in them at normal rates until they are transferred within the American mainland to the inner states, but what happened:

[In Cushing, Oklahoma state, especially where Texas Intermediate crude is stored, inventory volume has increased by five million barrels and is close to the maximum. US stocks of fuel and refined products have also increased, while weekly consumption has declined more than 25 percent over a year due to the isolation measures. (Rai Al-Youm, 25/4/2020)]. Thus it can be said that the unprecedented decline in the global demand for oil, estimated at 30% (i.e. about 30 million barrels of oil per day) is the first and main reason for what we are watching of successive falls in oil prices, and since American - Saudi policy of pressurizing Russia is valid for application only in normal times, not in times of demand crises, it has resulted in a stark exacerbation of the problem of oil prices!

Fourth: All of this affected West Texas oil. Storage facilities in Oklahoma were saturated, and there was no longer room for storage except at very high prices, and those contracts had to be disposed of at any cost. Thus, it led to the West Texas oil crisis or the "Black Monday" on 20/4/2020, when oil was sold at negative \$37 a barrel, and dealers at the stock exchange in America incurred huge losses. What brought matters to this point and aggravated it is what we mentioned above; that is, the fullness of Cushing's tanks, when stocks approach the maximum, which is a very rare procedure, storage prices jumped, and because the prospects for oil consumption, because of the continued closure of the economy, were still vague and suspicious, the storage prices in Cushing's facilities have jumped strongly and have become another factor that pressured the holders of May oil contracts. And so they tried to get rid of them at any cost, so the prices of those contracts went down to 10 dollars, then after that to five, then continued to go to zero in a dramatic scene, and then it went down below zero, the last of these contracts were sold at a negative value of negative \$37.6, amid great astonishment for its bearers, who suffered heavy losses, as well as the stock exchange dealers' astonishment. This is how the "Black Monday" crisis occurred on 20/4/2020 for West Texas oil, and these were its circumstances that were combined together and led to this acute crisis. Then the West Texas oil crisis took place, and Trump's delight was not of aid, by the OPEC Plus agreement between Saudi Arabia and Russia,

when he said on 12/4/2020, "This will create hundreds of thousands of energy jobs in the United States. I would like to thank and congratulate the Russian President Putin and the Saudi King Salman bin Abdel Aziz" (CNN Arabic, 21/4/2020). Trump's joy was far from reality, because the fall of prices in such a terrible way has created great fears in the world and not in America alone. Then the economic crisis intensified, not to mention the energy sector, so its bubbles have become ready to explode!

Note that West Texas Intermediate oil is extracted from oil fields in the United States, and is mainly extracted from Texas, Louisiana, and North Dakota, then transported via pipeline to Cushing, in Oklahoma, for delivery, and West Texas Intermediate crude futures are traded through the New York Mercantile Exchange (NYMEX), owned by the Chicago Mercantile Exchange (CME).

Fifth: On the other hand, since the beginning of the Coronavirus crisis, America has adopted plans for support, rescue, or stimulus, and these plans are phased out, the first is a small plan worth \$8.3 billion of emergency spending to support health programs and enabling it to cope with the outbreak of the Coronavirus epidemic in America. After Coronavirus pandemic hit the economy outside the health sector, [the United States reduced interest rates to almost zero, and launched a \$ 700 billion stimulus program, in an effort to protect the economy from the impact of the Coronavirus. (BBC, 16/3/2020)], and it drowned markets in dollar liquidity to meet the shortage of liquidity. Then it adopted a stimulus plan of \$2.2 trillion on 27/3/2020, the largest plan in American history, and most of it is earmarked for the purchase of corporate debt that stands on the verge of bankruptcy to prevent its collapse, and in the meantime. [The Federal Reserve announced earlier that it would buy at least \$500 billion in treasury bonds and no less than \$200 billion in mortgage-backed securities. The US Federal Reserve System also announced the creation of a new program that would provide up to 300 billion dollars in new financing, in an attempt to support the flow of credit to employers, consumers and companies. (Traders (App), 24/3/2020)]. The amount of health expenses on Coronavirus patients is expected to be disastrous in America, and may push insurance companies to collapse, which are huge companies. America also suffers from a severe unemployment crisis, about 30 million Americans lost their jobs due to the Coronavirus crisis, and because the companies that were hiring them are in a miserable financial situation, their return to their jobs will not be quick this year. This large number is reflected in the public budget by the large number of government aid applicants that have registered to it, more than 22 million unemployed Americans, and the crisis is still going on. If the country continues to adopt large bailout packages, the American currency may witness a terrible collapse that will harm America and all the countries and people that deal in the dollar.

Sixth: This crisis affected not only America, though it was hit severely, but it also affected other countries in the world:

1- As for Europe, its condition is not better than that of its American counterpart; the repercussions of the Coronavirus epidemic have threatened its political structure alongside economic repercussions. The crises we are witnessing in this epidemic in Italy, France, Spain, Germany and Britain have a clear indication. French President Macron warned in a press conference by phone on 26/3/2020 that, "the coronavirus outbreak risked undoing the bloc's central pillars..." He added, "What's at stake is the survival of the European project...The risk we are facing is the death of Schengen (Russia Today 26/4/2020; Reuters 27/3/2020). German Chancellor Merkel said: ("In my view, the European Union is facing the biggest test since its foundation... The important thing is that the bloc strongly emerges from the economic crisis caused by the virus"... (Reuters 7/4/2020). Spain's Prime Minister Pedro Sanchez said on 5/4/2020: "The current circumstances are exceptional and calls for firm positions. Either we rise to this challenge or we will fail as a union..." (German Frankfurter Allgemeine 5/4/2020). The leaders of the European Union in their video meeting on 23/4/2020 agreed on an immediate rescue package of around 500 billion euros, but they left the disputed details for more funding until the

summer. They discussed setting up an aid fund, and issuing joint Coronavirus bonds. But Germany, the Netherlands, Austria and Finland announced their rejection of these bonds and did not agree to the idea of the fund. While France, Italy and Spain support the project and they are the most affected countries. And Germany's refusal is due to the fact that it aspires to give loans in its name so that these countries will be in debt to it to control the other European countries!

2- As for China, the World Bank has warned that "the repercussions of the global economy could cause the growth of the Chinese economy to decline to 2.3% this year compared to 6.1% in the year 2019" (Alhurra.com/usa 10/4/2020). The page quoted a Chinese central bank official saying: "He recommends that Beijing does not set a target for growth this year, given the massive uncertainties it faces." The official Economic Daily Newspaper quoted Ma Jun, a member of the People's Bank of China Monetary Policy Committee, as saying that, "It will be difficult to reach 6% growth," adding that "setting a goal can limit formal measures to deal with the implications of the virus."

3- As for Russia, it depends on 60% of oil and gas exports. Oil is considered the lifeblood of the Russian economy, so it suffers from the losses it incurs, and the Russian currency, the ruble, is in the worst position, as it plummeted until the dollar is worth about 79 rubles after the oil price war. In reports from the Reuters news agency about the situation in Russia, quoting a Russian bank saying that: "the GDP may shrink by 15% if oil prices fall below ten dollars a barrel."

Seventh: Capitalism's failure is exposed more clearly, its inability and confusion in dealing with the Coronavirus crisis have emerged, and selfishness has emerged among its countries, which have been subjected to severe blows that brought them down to the ground, so what remains is only the established rich and correct Islamic ideology. There is an opportunity for the Islamic Ummah to rise again. However, the regimes in the Muslim countries and those supporting them stand in the way of the Ummah's movement, as these rulers insist on their enmity and on linking with the major colonial countries. The Ummah needs sincere truthful leadership that leads them according to the true Islam, and it undoubtedly realizes that Hizb ut Tahrir is the pioneer who does not lie to its people, so it should join it and work with sincerity ﴿وَلَيَنْصُرَنَّ اللَّهُ مَنْ يَنْصُرُهُ إِنَّ اللَّهَ لَقَوِيٌّ عَزِيزٌ﴾ **"And Allah will surely support those who support Him. Indeed, Allah is Powerful and Exalted in Might"** [Al-Hajj: 40].

Dear brothers and sisters, the events indicate that the international position after Coronavirus is not the same as before it. The countries that used to think that they are gods on the earth, and draw rules and laws contrary to what Allah (swt) has revealed to His Messenger (saw), and make falsehood the truth and the truth falsehood. Their failure is proven in front of a small little creation that can hardly be seen, which brought them down to the ground, while they are floundering on how to deal with it, and face it, and they are still stumbling in the darkness of their injustice until they are hit by the words of Allah Al-Qawi Al-Aziz: ﴿وَقُلْ جَاءَ الْحَقُّ وَزَهَقَ الْبَاطِلُ إِنَّ الْبَاطِلَ كَانَ زَهُوقًا﴾ **"And say, "Truth has come, and falsehood has departed. Indeed is falsehood, [by nature], ever bound to depart."** [Al-Isra': 81].

The Khilafah (Caliphate) will dawn again, illuminating the world and spread good throughout the world, ﴿وَيَقُولُونَ مَتَى هُوَ قُلْ عَسَى أَنْ يَكُونَ قَرِيبًا﴾ **"...Then they will nod their heads toward you and say, "When is that?" Say, "Perhaps it will be soon"** [Al-Isra': 51].

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