

## Opinions

# From Russia to Iran, the consequences of the global oil bust



By **Fareed Zakaria** Opinion writer August 20

While we have been watching the Islamic State and discussing Iran, something much bigger is happening in the world. We are witnessing a historic fall in the price of oil, down more than [50 percent](#) in less than a year. When a similar drop happened in the 1980s, the Soviet Union collapsed. What will it mean now?

Nick Butler, former head of strategy for BP, told me, “We are in for a longer and more sustained period of low oil prices than in the late 1980s.” Why? He points to a perfect storm. Supply is up substantially because a decade of high oil prices encouraged producers throughout the world to invest vast amounts of money in finding new sources. Those investments are made and will keep supply flowing for years. Leonardo Maugeri, former head of strategy for the Italian energy giant Eni, says, “There is no way to stop this phenomenon.” He predicts that prices could actually drop to \$35 per barrel next year, down from more than \$105 last summer.

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A primary reason for the accelerated price decline is that Saudi Arabia, the world’s “swing supplier” — the one that can most easily increase or decrease production — has decided to keep pumping. The Saudis “know it hurts them but they hope it will hurt everyone else more,” says Maugeri, now at Harvard. One of Saudi Arabia’s main aims is to put U.S. producers of shale and tight oil out of business. So far, it has not worked. Though battered by plunging prices, U.S. firms have used technology and smart business practices to stay afloat. The imminent return of Iran’s oil — which markets are assuming will happen, but slowly — is another factor driving down prices. So is the increasing energy efficiency of cars and trucks.

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Major oil-producing countries everywhere are facing a fiscal reckoning like nothing they have seen in decades, perhaps ever. Let’s take a brief tour of the new world.

Venezuela: Hugo Chávez’s popularity, his “21st-century socialism” and his mismanagement of the country’s economy were made possible by one factor: a prolonged oil boom. His successor has inherited a bankrupt country that will not be able to service its [debts](#). Oil makes up [96 percent of Venezuela’s exports](#). [Its economy](#) is estimated to shrink by 7 percent this year, having already contracted by 4 percent last year. (One of the reasons that Cuba has been looking to reach accommodations with the United States is that it knows that its sugar daddy in Caracas is out of cash.)

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Russia: As with Chávez, Vladimir Putin's popularity coincided perfectly with a steep rise in oil prices, which meant higher Russian GDP, government revenue and, thus, subsidies to the people. All that is reversing course. Russia's economy is projected to shrink by [3.4 percent](#) this year. Oil and gas revenue make up [half](#) the government's income. Crucially, revenue for Gazprom, the national gas giant, is estimated to fall by [almost 30 percent](#) this year. "Remember, Gazprom is the machine that provides finances for Putin's clique that runs the country," said Butler, now at King's College London.

Iraq: Oil makes up about [90 percent](#) of the Baghdad government's revenue, and despite the fact that it is pumping out as much as possible, it faces a massive drop in available funds. This is the backdrop behind the fragility of the government and also the rising levels of sectarian strife — which have paved the way for the Islamic State. With limited resources, the Shiite government in Baghdad is hard-pressed to make patronage payments to the Sunnis. Next up, a major confrontation between the Kurds and the central government over the sharing of oil revenue.

Iran: Despite the initial windfall that Tehran will get from the relaxation of international sanctions, it is, like most petro-states, dysfunctional. In fact, the International Monetary Fund estimates that it needs prices to be [almost \\$100](#) a barrel to balance its budget. In the medium term, it will face pressures just like the others.

Many American experts and commentators have hoped for low oil prices as a way to deprive unsavory regimes around the globe of easy money. Now it's happening, but at a speed that might produce enormous turmoil and uncertainty in an already anxious world.

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