Our View: China as Oil Market Manager Keeping Prices Stable

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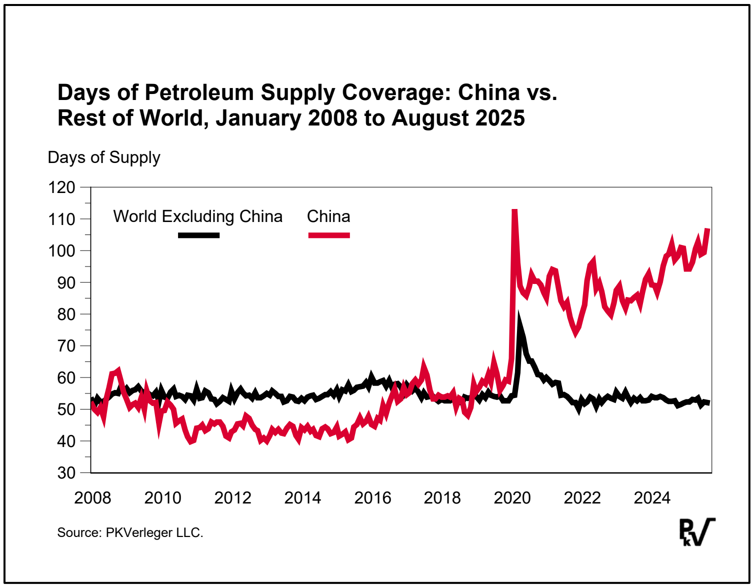
Economists have written paper after paper on how to stabilize commodity markets. Thousands of books and analyses on the subject came out after John Maynard Keynes popularized the idea a century ago. Interest waned after 2000, though, as new, risk-offsetting financial market instruments became available. Today, few economists and absolutely no one in the energy industry thinks about commodity market stabilization schemes, including the authors of the IEA's widely circulated monthly report.

Chinese economists and officials are the exception. China is now managing the oil market, following Keynes' prescriptions, to keep prices between \$60 and \$70 per barrel.

It is doing this by aggressively adding to stocks as the oil-exporting nations boost production. The rise in inventory coverage (days of supply) shown in the figure here illustrates China's success. Compare the increase in Chinese coverage with the static movement for the rest of the world. China may continue this process for another eighteen months, possibly even storing oil in foreign locations.



China is also building stocks of materials other than oil, as noted by a Chinese official in this statement quoted by S&P Global on September 8: "The government has recently asked us to build up the stocks. Resource security is the priority for China, stockpiling not only petroleum, but also minerals, grain, medical supplies."

We see several explanations for the Chinese actions.

> China may be preparing for a future conflict with the United States. Nations worried about going to war often accumulate critical materials just in case.
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> China may want to keep prices in the \$60s to benefit its export industry. The country is the world's most prolific exporter of manufactured goods. Higher oil prices are a boon to its manufacturers as the value of Chinese shipments fluctuates positively with oil prices.

> China may also want to preserve competition in the world oil market. Many see the production increases announced by OPEC+ as an effort to shut down high-cost producers, especially US firms. China may want to prevent this to keep the market from becoming more concentrated.
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> China may also want to keep oil prices high to boost sales of electric vehicles. The country is now flooding Africa and South America with low-cost EVs. Its officials may think they can speed up electrification by keeping oil prices at current levels.

Whatever its reasons, China, not OPEC or OPEC+, is now the manager of the world oil market.