

The Petrodollar Weapon

Saudi Arabia's Oil Strategy and the Global Power Dynamic: Lessons from 1985 and Implications for 2025

Axis Institute

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Executive Summary: *This analysis examines Saudi Arabia's evolving oil production strategy within the context of contemporary great power competition in global oil markets, drawing instructive parallels with the Kingdom's consequential market intervention during the mid-1980s that contributed to the Soviet Union's economic collapse. In 2025, as OPEC+ accelerates production increases amid falling global prices, Russia confronts a fiscal crisis of historic proportions, with oil revenues declining 27% year-over-year in 2025 and budget deficits reaching record levels. The United States has imposed unprecedented sanctions on Rosneft and Lukoil, Russia's two largest oil producers. This convergence of coordinated Western pressure and Saudi market strategy represents a contemporary echo of Cold War-era economic warfare, with potentially decisive implications for the conflict in Ukraine and the broader architecture of international order.*

I. Introduction: The Return of Petropolitics

Four decades ago, in September 1985, Saudi Arabia made a fateful decision that would reshape global geopolitics. After years of restraining production to support oil prices, cutting output from ten million to just two million barrels per day, the Kingdom reversed course dramatically, flooding global markets with petroleum. Within four months, oil prices collapsed from \$32 to \$10 per barrel, delivering what many analysts describe as a decisive blow to the Soviet economy. The USSR, already burdened by the costs of its Afghan occupation and systemic economic inefficiencies, lost more than \$20 billion in 1986 alone—approximately 7.5% of its annual income.

Today, the dynamics of the global oil market bear striking resemblance to that transformative period. Saudi Arabia has once again initiated a significant production increase, OPEC+ is unwinding years of coordinated output restraints, and Russia faces an escalating fiscal crisis that threatens its capacity to sustain military operations in Ukraine. This analysis examines the historical precedent, assesses current market conditions and their geopolitical implications, and evaluates whether history may be repeating itself with consequences equally momentous to those witnessed in the late Cold War.

II. Historical Context: The 1985 Oil Price Collapse and Soviet Decline

The Strategic Environment of the Early 1980s

The Soviet Union entered the 1980s as a petroleum superpower, ranking among the world's largest oil producers with vast reserves in the Caucasus and Western Siberia. The oil price shocks of 1973 and 1979, driven by the Arab oil embargo and Iranian Revolution respectively, had generated enormous windfalls for Moscow, with revenues funding both domestic expenditures and support for client states across the developing world. By 1985, oil exports constituted the Soviet Union's primary source of hard currency earnings, making the command economy acutely vulnerable to price fluctuations.

Saudi Arabia's position during this period was complex. Throughout the early 1980s, the Kingdom had served as OPEC's 'swing producer,' absorbing production cuts to maintain price stability while other cartel members, particularly Iran and Iraq, then engaged in their devastating eight-year war, cheated on agreed quotas to maximize revenues. By 1985, Saudi production had fallen from approximately ten million barrels per day at the decade's start to barely two million, representing an enormous sacrifice in foregone revenues and market share to maintain global price stability.

The Casey Connection: Intelligence Cooperation and Economic Warfare

The extent of U.S.-Saudi coordination in engineering the 1985 price collapse remains a subject of historical debate. According to Peter Schweizer's account in 'Victory: The Reagan Administration's Secret Strategy That Hastened the Collapse of the Soviet Union,' CIA Director William Casey met with his Saudi counterpart in 1981 and shared intelligence assessments of Soviet oil production vulnerabilities. Schweizer argues that Casey explicitly linked oil prices to the broader U.S.-Saudi security relationship, signaling Washington's interest in leveraging petroleum markets against Moscow.

Richard Allen, President Reagan's National Security Adviser, subsequently stated that Casey negotiated directly with King Fahd regarding Saudi production policy. The results were dramatic: in the four months following September 1985, Saudi extraction surged from two million to ten million barrels per day. While some analysts attribute this decision primarily to Saudi frustration with OPEC quota violations rather than

explicit American pressure, the timing and magnitude of the production increase, occurring despite depressed prices, strongly suggest strategic rather than purely commercial motivations.

Economic Impact on the Soviet Union

The consequences for the Soviet economy proved catastrophic. External debt exploded from \$15 billion in 1984 to over \$30 billion by 1986, eventually reaching \$50 billion by decade's end. Mikhail Gorbachev's reform programs, perestroika and glasnost, were conceived partly in response to the fiscal crisis precipitated by collapsing energy revenues. Lacking the hard currency necessary to import consumer goods and maintain subsidies to Eastern European satellites, Moscow could no longer sustain the economic foundations of its empire. By 1991, the Soviet Union had dissolved under political and economic pressures.

"The oil crisis significantly helped the US win the Cold War against the USSR: the economic recession led Mikhail Gorbachev to make hugely unpopular political decisions. An attempt to reform the governmental system was largely hopeless due to the lack of funds."

— Russia Beyond, historical analysis of the 1985 oil crisis

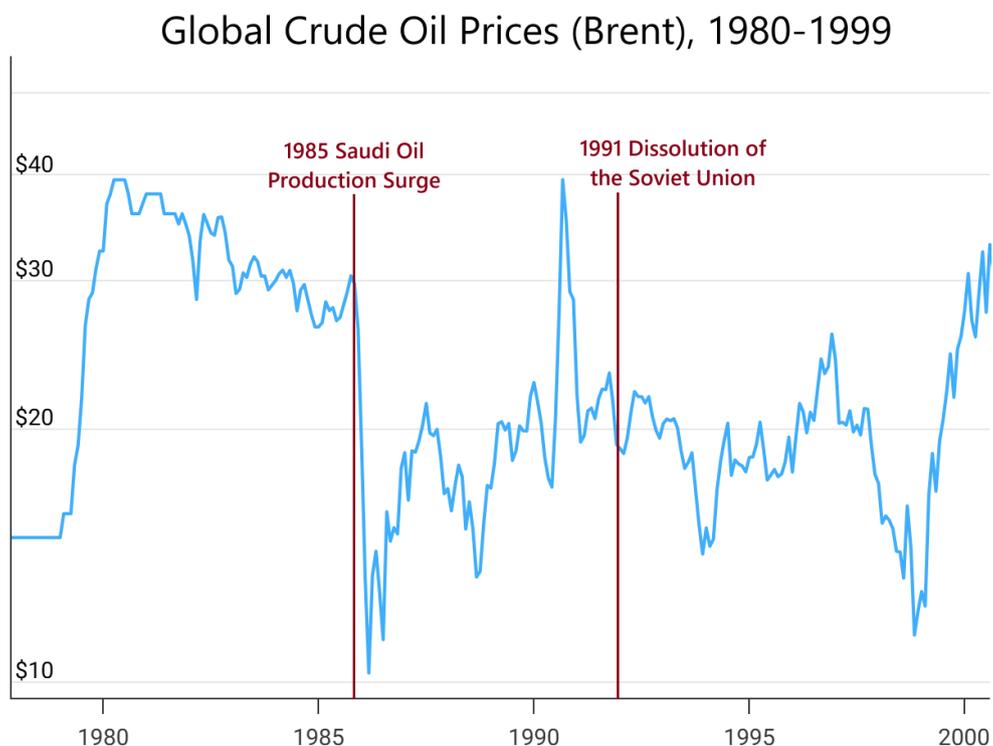


FIGURE 1: Global Crude Oil Prices (Brent) 1980-1999. Price of oil collapsed to \$10/barrel in early 1986, propelling key events in Soviet economic decline. Source: Macrotrends Oil Historical Prices]

III. The Contemporary Parallel: OPEC+ Strategy in 2025

The Production Increase Decision

Beginning in April 2025, eight OPEC+ members, Saudi Arabia, Russia, Iraq, UAE, Kuwait, Kazakhstan, Algeria, and Oman, commenced a phased unwinding of the 2.2 million barrel per day voluntary production cuts that had been maintained since late 2023. According to official OPEC communications, the group implemented production adjustments of 411,000 barrels per day in May, June, and July 2025, citing 'healthy market fundamentals and a positive market outlook.' The combined increases for the second quarter of 2025 totaled 960,000 barrels per day, representing approximately 44% of the previous cuts.

Saudi Arabia has borne the largest share of these increases. The Kingdom's OPEC+ allocation rose from its constrained baseline to approximately 9.37 million barrels per day by June 2025, with further increases through the summer months. Under the December 2024 roadmap, Saudi production could reach nearly 10 million barrels per day by December 2025, a level not seen since before the 2020 pandemic-era cuts. According to U.S. Energy Information Administration data, Saudi production in 2024 averaged 9.0 million barrels per day, down 13% from 2022 levels before the extended voluntary cuts were implemented.

Strategic Motivations

The production increases occur against a backdrop of declining global oil prices, suggesting motivations beyond simple revenue maximization. Brent crude, the international benchmark, has fallen from above \$80 per barrel in early 2025 to approximately \$62-63 per barrel by late November 2025, representing a decline of roughly 18% from 2025 highs. Multiple investment banks have revised their price forecasts downward: Goldman Sachs projects Brent averaging \$60 per barrel through year-end 2025 and \$56 in 2026; Morgan Stanley forecasts \$62.50 for the second half of 2025; and Barclays has reduced its outlook to \$66 for 2025 and \$60 for 2026.

Several factors appear to drive Saudi strategy. First, the Kingdom seeks to reassert production discipline within OPEC+ following persistent quota violations by members including Iraq and Kazakhstan. The Institute for Energy Research notes that Saudi Arabia is 'pushing OPEC+ to speed up production increases from previous output cuts

to punish Iraq and Kazakhstan for not complying with their production quotas.' Second, Riyadh may be positioning to capture market share from U.S. shale producers, whose break-even costs increasingly exceed current price levels. Third, and most relevant to this analysis, the production surge compounds pressure on Russia's and Iran's petroleum-dependent economies at a moment of acute fiscal vulnerability.

IV. Russia's Fiscal Crisis: Revenue Collapse and Budget Strain

Deteriorating Oil Revenues

Russia's budgetary dependence on petroleum revenues creates acute vulnerability to the current price environment. According to analysis from the Centre for Research on Energy and Clean Air, Russia's monthly fossil fuel export revenues in October 2025 declined to €524 million per day, 'the lowest they have been since the full-scale invasion of Ukraine'. Oil and gas revenues for the first ten months of 2025 totaled approximately 7.5 trillion rubles (\$92.8 billion), representing a decline of 2 trillion rubles (\$24.6 billion) compared to the same period in 2024, a shortfall of approximately 21%.

The revenue decline has accelerated markedly through 2025. According to the Free Russia Foundation's analysis, year-over-year oil revenue declines progressed from 14% in January-May to 17% by June, 18% in July, 20% in August, and 21% by October. The Russian government has been forced to revise its 2025 budget assumptions, reducing projected revenues by 1.79 trillion rubles (\$22.6 billion) to 38.51 trillion rubles (\$485.9 billion). The anticipated deficit has increased from the originally budgeted 1.17 trillion rubles (\$14.8 billion) to 3.79 trillion rubles (\$47.8 billion), equivalent to 1.7% of GDP.

The Urals Price Collapse

Russia's benchmark Urals crude has experienced particularly severe price deterioration. Following the U.S. Treasury's October 22, 2025 designation of Rosneft and Lukoil as Specially Designated Nationals, the most significant sanctions targeting Russia's energy sector to date, Urals prices at Black Sea export terminals collapsed to \$36.61 per barrel, the lowest level since March 2023. The discount relative to Brent widened to approximately \$23.50 per barrel, nearly double the \$11-14 discount

prevailing before the sanctions announcement and approaching the \$30+ differentials observed immediately after the 2022 invasion.

This price structure poses existential challenges for Russian petroleum economics. According to Incorr's energy consultancy, Russia's oil production costs have escalated at least 3% annually, driven primarily by rising finding and development expenses. The Institute of International Finance projected Russia's fiscal break-even oil price at \$77 per barrel for 2025, though some estimates suggest it may exceed \$80 when accounting for the full costs of new field development. With Urals trading below \$55, and potentially as low as \$36 at certain terminals, every new well drilled represents a net loss for Russian producers.

Budget Deficit Crisis

Russia's cumulative budget deficit from January through August 2025 reached 4.2 trillion rubles (\$52.5 billion), representing 74% of the revised full-year target after only eight months. The KSE Institute's analysis characterizes the deficit as 4.5 times larger than during the same period in 2024 and 'exceeding all recent records.' Oil and gas revenues fell 20% year-over-year while expenditures, driven predominantly by military spending, surged 21%.

The National Welfare Fund, Russia's primary fiscal buffer accumulated from prior petroleum windfalls, has been substantially depleted. Liquid assets in the fund declined to approximately 4.0 trillion rubles (\$48 billion) by mid-2025, down from over 6% of GDP at the end of 2021 to roughly 1.9% of GDP currently. The Moscow Times reports that Kremlin economists have warned the fund 'could be depleted by 2026' at current drawdown rates. The Bank of Finland's analysis suggests that if oil prices materialize as predicted by futures markets, the Russian budget deficit could reach approximately 5 trillion rubles (2.3% of GDP) annually in 2025-2026.

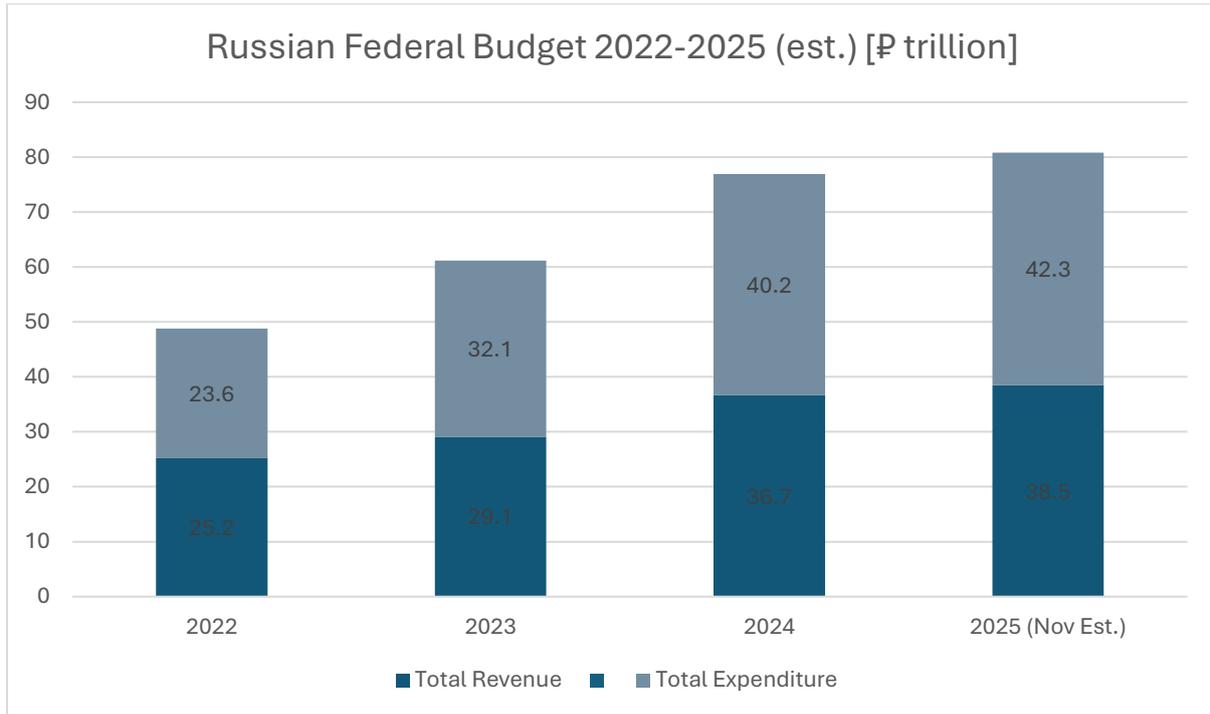


FIGURE 2: Russian Federal Budget (revenues and expenditures) for 2022, 2023, 2024, and 2025 (annualized)

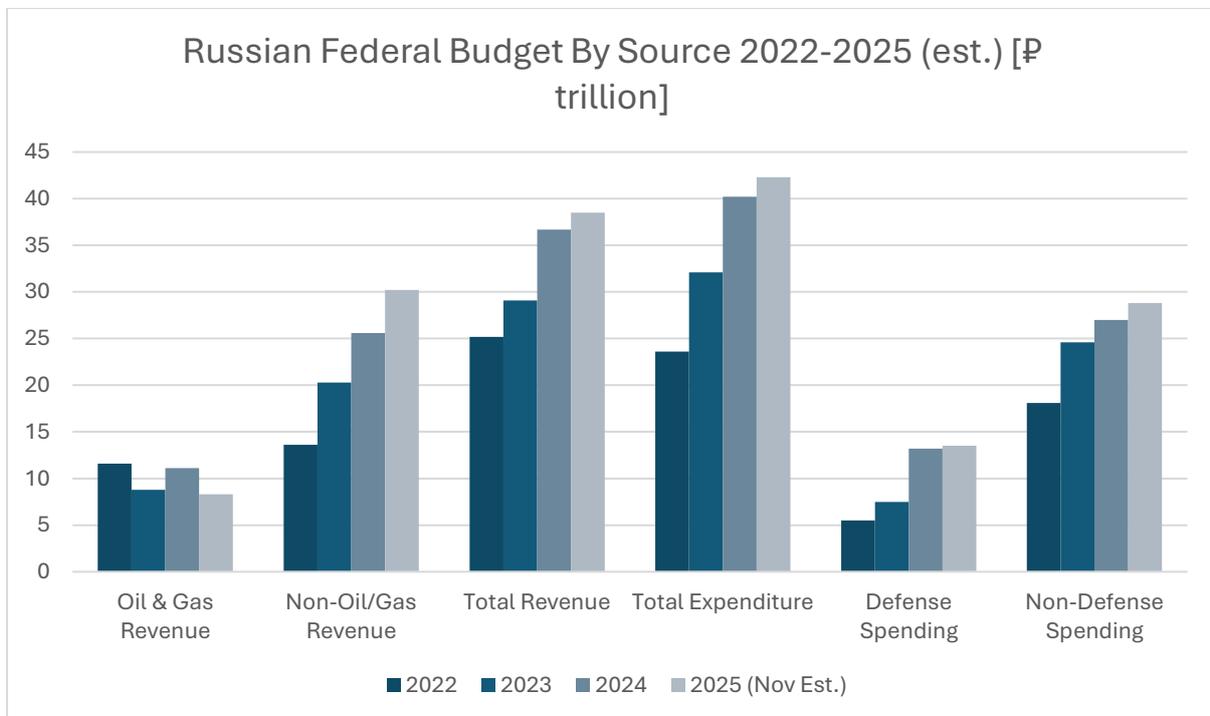


FIGURE 3: Russian Federal Budget (revenues and expenditures) for 2022, 2023, 2024, and 2025 (annualized)

V. The Sanctions Escalation: October 2025 Designations

On October 22, 2025, the U.S. Department of the Treasury's Office of Foreign Assets Control imposed full asset-blocking sanctions on Rosneft and Lukoil, Russia's two largest oil companies, along with 34 of their domestic subsidiaries. Secretary of the Treasury Scott Bessent announced the action stating, 'Now is the time to stop the killing and for an immediate ceasefire. Given President Putin's refusal to end this senseless war, Treasury is sanctioning Russia's two largest oil companies that fund the Kremlin's war machine.' These designations represent the most significant expansion of Russia-related sanctions during the second Trump administration.

The sanctions' scope is substantial. According to Treasury Department analysis, Rosneft and Lukoil together produce approximately 55% of Russia's oil and contribute about 25% of overall Russian government revenue. Combined with earlier designations of Surgutneftegaz and Gazprom Neft, approximately 70% of Russia's crude oil export volumes are now produced by sanctioned entities. The designations require all transactions involving these companies to be wound down by November 21, 2025, with payments to blocked entities deposited in frozen accounts.

Market response was immediate. Major Chinese state refiners Sinopec and PetroChina, along with Indian purchasers including Reliance Industries, Bharat Petroleum, and Hindustan Petroleum, have suspended or significantly reduced purchases from sanctioned Russian suppliers. India's largest Russian oil importer, Reliance Industries, has sharply increased its purchases of cheaper Middle Eastern crude as a direct consequence of the new restrictions. Middle Eastern oil producers, led by Iraq, Saudi Arabia, and the UAE, have captured significant market share in India, with their combined share rising from 50% in December 2024 to 55% by mid-February 2025 according to Vortexa.

VI. Saudi Arabia's Long-Term Positioning: The Jafurah Development

Beyond immediate market dynamics, Saudi Arabia is executing a transformational expansion of its hydrocarbon production capabilities that will strengthen its position as the world's preeminent energy supplier for decades. The Jafurah unconventional gas field, the Kingdom's largest non-associated gas development, contains an

estimated 229 trillion standard cubic feet of raw gas and 75 billion stock tank barrels of condensate. According to Saudi Aramco, phase one operations commenced in the third quarter of 2025, with production expected to ramp from 200 million standard cubic feet per day to 2 billion standard cubic feet per day by 2030.

Total lifecycle investment at Jafurah is projected to exceed \$100 billion. In August 2025, Aramco signed an \$11 billion lease and leaseback arrangement with a consortium led by BlackRock's Global Infrastructure Partners for Jafurah midstream processing facilities, representing significant foreign direct investment into Saudi energy infrastructure. Amin H. Nasser, Aramco's President and CEO, characterized Jafurah as 'a cornerstone of our ambitious gas expansion program,' noting its role in supplying energy required to power new growth sectors, such as AI data centers, in the Kingdom.

The gas development serves multiple strategic objectives. Domestically, it enables Saudi Arabia to displace oil-fired power generation with cleaner-burning natural gas, freeing additional crude volumes for export. At peak production, Aramco's unconventional gas program is expected to replace approximately 500,000 barrels per day of domestic oil consumption, volumes that can then enter international markets. The Jafurah development alone will replace over 300,000 barrels per day at peak output, effectively expanding Saudi export capacity without requiring new crude production investments.

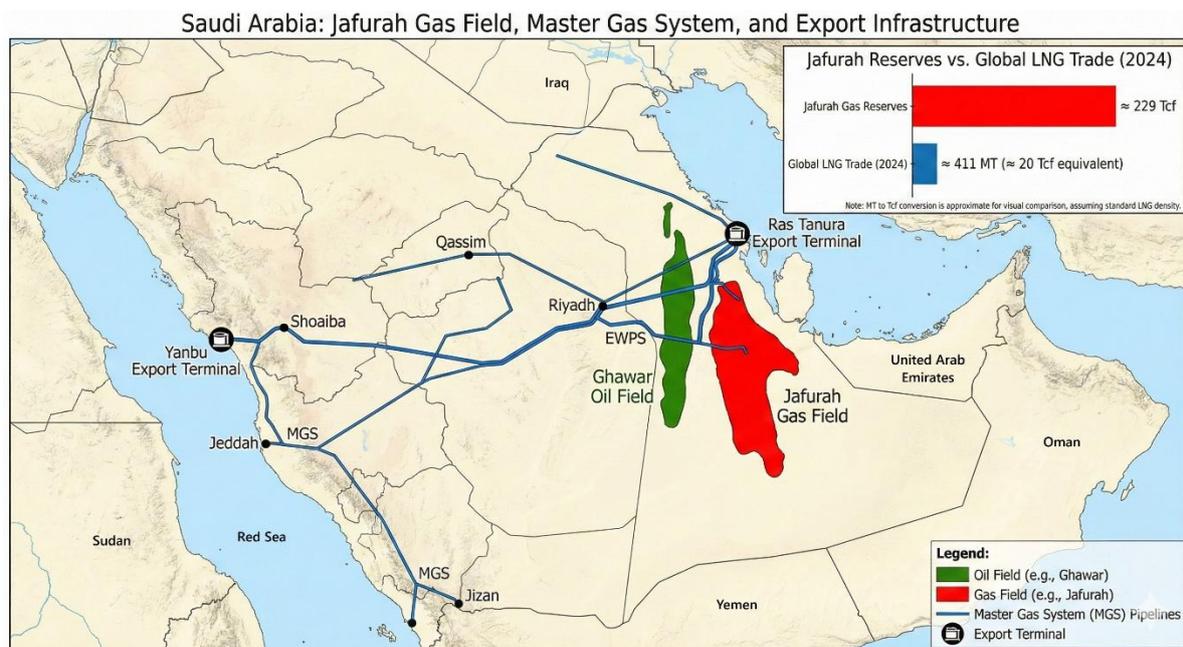


Figure 4: Map of Saudi Arabia's Oil and Gas Infrastructure (simplified)

VII. Competitive Dynamics: Saudi Arabia vs. Russia in Asian Markets

The struggle for market share in Asia's two largest petroleum import markets, China and India, represents a critical battleground in contemporary energy geopolitics. Prior to Russia's 2022 invasion of Ukraine, Saudi Arabia ranked as the leading crude supplier to both nations. Western sanctions and the subsequent requirement for Russian producers to offer steep discounts displaced Saudi volumes where Russia captured the top position in Chinese imports and rose from marginal supplier to India's largest crude source by 2023, accounting for nearly 40% of Indian imports.

The October 2025 sanctions have begun reversing these dynamics. Centre for Research on Energy and Clean Air data indicates that while China remained Russia's largest fossil fuel customer in October 2025, accounting for €5.8 billion (44%) of top-five importer purchases, Chinese seaborne crude imports from Russia fell 21% month-on-month. Rosneft and Lukoil supplies were entirely absent from deliveries made in the final week of October, despite the OFAC sanctions not taking effect till November 21. Indian imports have similarly declined, with state refiners and private giants alike reducing Russian purchases in favor of Middle Eastern alternatives.

Saudi Arabia has actively exploited this opening. According to industry reports, the Kingdom has offered competitive discounts to Asian buyers, directly challenging Russia's primary commercial advantage in these markets. The Institute for Energy Research notes that Saudi Arabia is increasing production by almost one million barrels per day, despite lower expected oil prices, to reassert discipline in OPEC+ and expand the group's market share, thereby solidifying its relationship with the United States. With approximately 2.2 million barrels per day of spare capacity, Saudi Arabia possesses the operational flexibility to absorb displaced Russian volumes while still increasing total supply.

VIII. Historical Parallels and Divergences

Similarities to 1985

The structural parallels between the 1985 Saudi production surge and current market dynamics are substantial. In both periods, Saudi Arabia increased production despite depressed prices, accepting short-term revenue losses to achieve longer-term strategic

objectives. In both cases, the target economy, the Soviet Union then and Russia now, depended heavily on petroleum exports to finance government operations and, critically, military expenditures. Both situations featured coordinated Western pressure, with U.S. intelligence and diplomatic efforts complementing market-based economic warfare.

The fiscal mechanisms of pressure also demonstrate continuity. Just as the Soviet Union's budget deficit exploded following the 1985-1986 price collapse, Russia's current deficit has reached record levels. The depletion of sovereign wealth reserves, then Soviet gold and currency holdings while now Russia's National Welfare Fund, follows a similar trajectory. And the downstream political consequences of fiscal strain, necessitating difficult choices between military spending, domestic subsidies, and economic reform, echo across four decades.

Important Distinctions

Several factors distinguish the contemporary situation from its Cold War antecedent. First, Russia has proven more adaptable than the Soviet command economy in redirecting trade flows and balancing its fiscal budget. Despite Western embargoes, Russia has maintained substantial export volumes by pivoting toward Asian markets, though at significantly discounted prices that compromise revenues. Second, the global energy landscape has transformed fundamentally where renewable generation, electric vehicles, and energy efficiency improvements create structural headwinds for petroleum demand that did not exist in the 1980s. Third, China's emergence as both Russia's largest remaining customer and a potential strategic partner introduces complexities absent from the bipolar Cold War system.

Perhaps most significantly, the scale and sophistication of Western sanctions in 2025 exceeds anything attempted during the Cold War. The designation of Rosneft and Lukoil as SDNs, blocking access to the U.S. financial system and threatening secondary sanctions against non-compliant foreign institutions, represents an economic weapon that did not exist in 1985. The combination of comprehensive financial sanctions with coordinated OPEC+ production increases and targeted attacks on Russian refining infrastructure creates simultaneous pressure across multiple vectors of the petroleum value chain.

IX. Implications and Outlook

For Russian Economic Sustainability

Russia's capacity to sustain current expenditure levels, particularly the record military allocations constituting approximately 40% of federal spending, appears increasingly constrained. The Free Russia Foundation's analysis concludes that the deficit is likely to be higher in the remaining months of 2025 and the years 2026–2028, as the current trends and economic model suggest. With the National Welfare Fund potentially exhausted by 2026 and oil revenues declining 20%+ year-over-year, Moscow faces difficult choices between monetary financing (accelerating already-elevated inflation), additional taxation (further suppressing civilian economic activity), or expenditure reductions.

For the Ukraine Conflict

The convergence of oil market pressure and comprehensive sanctions directly constrains Russia's war-fighting capacity. Secretary Bessent explicitly framed the Rosneft/Lukoil designations as intended to support President Trump's efforts to achieve an immediate ceasefire. In Washington, the economic logic is straightforward: depleting Russia's fiscal resources limits its ability to finance military operations, procure equipment, and sustain the elevated defense spending necessary for prolonged conflict. Whether this pressure proves sufficient to alter Russian strategic calculus, as it eventually did for the Soviet Union, remains the central uncertainty in today's global power dynamics.

For Global Energy Markets

The current market structure, combining OPEC+ production increases, weak global demand growth, and expanding non-OPEC supply from the Americas, suggests sustained pressure on oil prices. The International Energy Agency has forecast supply exceeding demand by approximately three million barrels per day between late 2025 and end-2026. For petroleum-exporting nations lacking Saudi Arabia's financial reserves and low production costs, this environment portends significant fiscal strain. For importing nations, particularly in Asia, the availability of competitively-priced crude from multiple sources reduces vulnerability to supply disruptions and enhances energy security.

X. Conclusion: The Petrodollar Weapon Revisited

The events of 2025 demonstrate that petroleum remains a strategic commodity with geopolitical significance extending far beyond commercial markets. Saudi Arabia's decision to increase production amid falling prices, the comprehensive sanctioning of Russia's largest oil companies, and the resulting fiscal crisis confronting Moscow collectively represent a contemporary application of the economic warfare techniques that proved so consequential in the 1980s. Whether this pressure will produce outcomes as decisive as the Soviet collapse remains contingent on factors including the duration of hostilities in Ukraine, China's willingness to absorb Russian exports at discounted prices, and Russia's ability to manage fiscal strain without triggering broader economic or political instability.

What is clear is that the Kingdom of Saudi Arabia has once again demonstrated its willingness to deploy its unmatched production capacity and financial resilience in service of broader strategic objectives, accepting near-term costs to reshape market dynamics and, potentially, the trajectory of global power dynamics. As the world witnessed four decades ago, the decisions made in Riyadh regarding oil production can reverberate far beyond petroleum markets, influencing the balance of power between nations and the fates of empires. History does not repeat, but it often rhymes, and the echoes of 1985 resonate unmistakably in the oil markets of 2025.

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