A floor hand helps line up a pipe for drilling in the Bakken shale formation last year near Watford City, N.D. Drilling and hydraulic fracturing are increasing U.S. oil output amid a decline in demand. Getty Images

Oil prices posted their biggest one-day drop in nearly two years Tuesday as a U.S.-led wave of crude has crashed into weak global demand, threatening the stability of some countries and providing an economic lifeline to others.

Tuesday’s slide of 4.5% by U.S. crude oil to $81.84 a barrel on the New York Mercantile Exchange left the price down 20% since the start of June. That was the lowest closing price since June 2012, and some analysts predict the price will fall as much as $10 a barrel lower.

The same factors that sank prices Tuesday are behind oil’s four-month tumble, which is pressuring countries from Russia to Iran to Venezuela. World-wide demand is stagnant, and the International Energy Agency cut its full-year oil-demand growth forecast Tuesday to the lowest level in five years.

Yet oil output remains high. In the U.S., hydraulic fracturing has unleashed a torrent of new crude that is flooding the market. U.S. output is expected to increase again this year, according to Ed
Morse, global head of commodities research at Citigroup Inc. C +3.15% Lower crude prices could slow next year’s growth.

Despite the steep drop in oil prices, the Organization of the Petroleum Exporting Countries, which controls about one-third of global oil supplies, has been unwilling to rein in production. Saudi Arabia is focused on maintaining market share even if it means cutting prices, a controversial stance addressed in a rare public letter Tuesday from Saudi Prince al-Waleed bin Talal to the kingdom’s oil minister. Iran signaled Tuesday that it also would accept lower prices.

As a result, the retail price of gasoline for the average American has dropped nearly 15% since late June to an average $3.17 a gallon as of Tuesday, according to Gasbuddy.com, a gas price-finding app. Many analysts expect prices at the pump to drift below $3 a gallon in many parts of the U.S. if crude prices keep sliding.

**Related Video**

Crude oil futures rose after sliding last week to its lowest point since April 2013. What does the price say about the sector? Robert Thummel of Tortoise Capital Advisors joins MoneyBeat. Photo: Getty.

Every one-cent drop in gas prices means a $1 billion annual decline in energy spending by Americans, estimates Brett Ryan, U.S. economist at Deutsche Bank.

“It’s like a tax cut that consumers can use to eat out more often, buy more goods or help save for a new home,” he said.

The savings isn’t “a huge boost to GDP, but it’s a positive for U.S. corporates and makers of goods and services,” Mr. Ryan added. Tom Kloza, chief oil analyst for Gasbuddy.com, said the typical American family is saving about $50 a month based on the decline since June.

Brent, the global oil benchmark, fell 4.3% to $85.04 a barrel on Tuesday, a nearly four-year low. It was Brent’s largest one-day percentage drop since September 2011.

Other economists warned that the overall impact on the U.S. economy could be negative, since the recent slowdown in global growth is one of the biggest reasons for tumbling fuel prices. The same is largely true in Europe.
“If we don’t have markets to sell our exports to, that will be a drag for the overall economy even if consumers have a little extra to spend after buying their gasoline” said James Hamilton, an economics professor at the University of California, San Diego.

The possible economic and political consequences vary widely around the world. Venezuela, a major oil exporter and OPEC member, could veer into political crisis because of sharply lower crude prices, some analysts say.

Venezuela relies on imports for much of its food, cars and other goods, but the country is increasingly short of hard currency needed to pay for those staples.

In contrast, energy-import dependent Japan, South Korea and Taiwan are likely to get an economic boost even if the oil-price slide ends unexpectedly soon.
Until recently, crude prices stayed high despite the rising supply because wars and civil strife created disruptions in the oil market. Now, though, “there is an abundance of geopolitical risk, but there is an even greater abundance of oil,” said Daniel Yergin, vice chairman of research firm IHS Inc.

The seeds of the supply shock were planted a little more than a decade ago in north Texas when U.S. companies pioneered horizontal drilling techniques combined with hydraulic fracturing technology. The result: wringing oil and gas out of rocks previously thought to be unworkable.

Since 2004, U.S. oil production is up 56%, the equivalent of pumping an extra 3.1 million barrels a day on top of the regular U.S. oil output from traditional oil fields in places like Oklahoma and the Gulf of Mexico. Last week, Exxon Mobil Corp. Chairman and Chief Executive Rex Tillerson said North America has entered a “new era of energy abundance.” U.S. demand for gas and other fuels is down 8% since 2004.

OPEC could face deepening internal rifts if prices remain low, because some members want to pump more to keep their coffers filled. Venezuela needs oil prices well above $120 a barrel to balance its budget, according to a recent Deutsche Bank report. Angola has a budget based on $98 a barrel.

While the U.S. has slashed oil imports, China has steadily increased its dependence on foreign crude. More than 61% of the oil China consumes will be imported next year, according to official estimates.

The drop in global petroleum prices comes as China’s economic growth engine is slowing. Economists widely believe China might miss its economic growth target of 7.5% for the year. Low oil prices could help by bringing down production costs for a wide range of industries and keeping inflation tamed.

“Lower oil prices act as an easing mechanism for the Chinese economy as its economic growth slows,” said Société Générale CIB economist Wei Yao. “It’s a relief to Chinese policy makers.”

India’s politicians and central bankers are also happy about the downturn, which helps shrink India’s huge fuel subsidy bills and eases inflationary pressures. India imports about 75% of its energy. Fuel prices have fallen enough that state-run fuel stands aren’t suffering losses on each liter of diesel sold.

In Venezuela, President Nicolás Maduro’s government is struggling with a collapsing currency and shortages of everything from baby diapers to toilet paper to medicine to car parts.

Venezuela already was running low on hard currency because of rampant spending at home and other problems.

When prices of oil were close to $100 a barrel earlier this year, Venezuelans across the country rose up to protest shortages and what many leaders of the demonstrators called the government’s bungled management of the economy.

“Venezuela’s oil prices have been high for several years now, and the country is still struggling to pay its debt at those prices,” said Russ Dallen, a partner at brokerage firm Caracas Capital Markets.
Asdrubal Oliveros, head of Caracas-based consulting firm Econanalitica, said Venezuela has few options. “Venezuela can generate as much noise as it wants within OPEC, but it’s Saudi Arabia that calls the shots,” he said. Venezuela’s central bank and finance ministry didn’t respond to requests for comment.

On Tuesday, Russian President Vladimir Putin acknowledged that the national budget is “stressed” because of the fall in oil prices. Russia’s central bank is working on a “shock scenario” that envisages a drop in oil prices to $60 per barrel. Russia relies on revenues from oil and gas exports for about half of its federal budget revenues.

Economists say falling oil prices could kill off Russia’s flagging economic growth, forecast at no more than 0.5% this year. Evgeny Nadorshin, chief economist at Russian conglomerate AFK Sistema, said Russia’s economy could begin contracting by the end of this year if oil prices remain near $90 a barrel.

Leading Russian politicians and executives believe the Saudis are pushing down prices to target Russia’s oil-export-dependent economy and Mr. Putin, as an extension of ongoing sanctions.

Speaking on Russian state television last week, former Russian Finance Minister Alexei Kudrin suggested there could be “a kind of agreement of leading countries, importers and exporters, the U.S. and the Middle East, that production will be increased and the price will be kept low.” Such claims are reminiscent of Russian theories about the 1980s price drop that some historians believe played a role in the fall of the Soviet Union.

The impact of falling crude prices in North America will likely be positive because motorists could wind up with additional discretionary income.

But if the number of rigs drilling wells declines, there could be resulting pockets of economic contraction in places such as Midland, Texas, or Fort McMurray, Alberta, the home of the oil sands.

Of course, falling prices would eventually force companies and countries to cut production, many analysts predict. But it isn’t clear who would make the first move. “We’re in uncertain territory” because the global oil market has changed so much in the past few years, said Richard Mallison, an analyst with research firm Energy Aspects.

When oil prices cratered in the late 1990s, a long lull in investments followed. And by the time the financial crisis erupted in 2008, demand for crude outstripped supply—and oil prices hit a record $145.29 a barrel.

This time around, oil prices could rebound if production is cut and the global economy improves. Iain Pyle, an analyst at Bernstein Research, said he expects oil prices “certainly north of $100 next year.” A lot depends on whether producers of U.S. shale or OPEC members curtail production. Shale can be especially expensive to produce. If the rebound in crude-oil prices is slow, it could hurt large, Western oil companies. Bernstein estimates that Royal Dutch Shell PLC and BP PLC need oil to be above $85 a barrel for their current operations to break even. Any sustained drop could mean the companies have to scale back development.

—Benoît Faucon, Ezequiel Minaya, Mark Magnier and James Marson contributed to this article.

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