# Energy and Economic Implications of the Iran-Israel Conflict

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Brief Analysis

## Three experts explore the war's impact on global energy markets, Iran-Gulf relations, President

**Trump's oil price calculations, and more.**

*On June 26, The Washington Institute held a virtual Policy Forum with Homayoun Falakshahi, Jennifer Gnana, and Gregory Brew. Falakshahi leads Kpler's crude oil analysis team, focusing on global market dynamics and geopolitical drivers. Gnana is a Middle East correspondent focusing on energy, oil policy, and political economy, with articles featured in S&P Global Commodity Insights, Al-Monitor, and other outlets. Brew is a senior analyst with Eurasia Group and author of the book* The Struggle for Iran: Oil, Autocracy, and the Cold War, 1951-1954*. The following is a rapporteur's summary of their remarks.*

## Homayoun Falakshahi

Nerves were high in the energy markets when fighting erupted between Iran and Israel, as 35 percent of seaborne oil trade and 20 percent of liquefied natural gas (LNG) pass through the Strait of Hormuz. Yet both combatants limited their attacks on the energy sector to facilities supplying domestic markets—a purposeful tactic to avoid heavily affecting international markets. Even so, countries in the region tried to export as much of their hydrocarbon supply as possible during the first few days of the war. The situation has since returned to normal, but it is up to Israel to determine whether hostilities resume.

The Iranian regime has threatened to close the Strait of Hormuz several times in past decades but never actually did so, for a number of reasons. First, Iran depends heavily on the strait for its own energy exports. Second, other countries in the region have officially supported Iran during various crises, and closing the strait could push them into Israel's camp. Third, Iran formally shares control over the strait with Oman, a neutral country that has been hosting the recent negotiations with the United States. If Tehran unilaterally closed Hormuz, it would violate Oman's territorial waters. Fourth, closing the strait would antagonize China, Iran's only oil buyer.

President Trump recently stated that it is now okay for Beijing to purchase oil from Iran. This apparent green light could boost oil volumes to China by an estimated 400,000 barrels per day, representing an increase of $10 billion in annual revenues for Iran. Currently, all of Iran's oil and 80 percent of its liquefied petroleum gas (LPG) and fuel oil cargoes go to China. Yet the return of the Trump administration's maximum pressure policy has spurred a decrease in imports over the past few months.

Although the Iran-Israel ceasefire is having a bearish impact on oil prices, the short-term rise during the conflict was sufficient for U.S. producers (mainly shale firms) to secure a minimum price level for their operations. This implies that even if prices drop sharply in the second half of the year, U.S. production has already been secured.

Regarding the recent GPS jamming and manipulation of automatic identification signals reported among vessels in the Strait of Hormuz, the culprit is still uncertain. Iran may have done this to make passage through the strait less safe and increase freight costs—both of which would have a bullish effect on oil prices. Alternatively, ship operators themselves might have taken such action, masking their real locations for fear of being attacked.

Going forward, the ceasefire will likely hold because all sides have publicly declared themselves winners, and none of them have an interest in continuing the war right now. Behind the curtain, however, the fight is not over.

The ceasefire might also be grounds for a wider U.S.-Iran deal or even the reestablishment of formal relations between the two countries. President Trump stated that there is no need for a nuclear deal, arguing that all of Iran's facilities have been obliterated. Yet restoring U.S.-Iran relations would be the best advertisement for his Nobel Peace Prize candidacy.

## Jennifer Gnana

The Gulf states have managed their relations with Iran to ensure that energy sites are not targeted during crises like the latest war. Similarly, the Iran-backed Houthis in Yemen have refrained from any direct attack on Gulf energy infrastructure or crude supplies since March 2023, when Riyadh normalized relations with Iran. Neither Tehran nor the Houthis want to jeopardize this relationship. Moreover, Iranian leaders view Saudi Arabia and the United Arab Emirates as countries with considerable clout to influence the ceasefire in Tehran's favor. Even the Iranian retaliatory attack on the U.S. base in Qatar was carefully choreographed and accompanied by messaging to placate Doha and other Gulf capitals.

Regarding the broader picture in the Gulf, various sectors could be affected if regional tensions cause oil prices to drop below $60 per barrel. A prolonged price dip would force Gulf governments to reassess their massive domestic projects, which depend on the unimpeded flow of oil for funding. The latest conflict will also require them to reassure their large expatriate populations, who comprise the manpower needed to implement those projects. Notably, the projects announced during President Trump's May visit to the region require a stable energy situation to execute, as artificial intelligence and data centers require a lot of power. Current conditions will also heighten the scrutiny on Saudi Arabia's nuclear ambitions.

OPEC has a delicate balance to maintain as well. On one hand, it has sought to avoid drawing President Trump's ire over high oil prices. On the other hand, the organization must make sure that its member countries are content with production quotas and that oil markets are well supplied. Currently, OPEC is increasing production and putting more supply on the market. Yet many Gulf countries have kept oil production tight over the past few years and are unlikely to make drastic changes. For now, they will likely work with Trump to keep prices fairly stable and maintain production levels.

Another trend to monitor is how Iran responds in the longer term, particularly given the prospects for continued proxy militia warfare after the latest conventional military showdown. Even if the ceasefire holds, low-level hostilities in the Red Sea and Strait of Hormuz will likely persist, potentially affecting energy markets.

## Gregory Brew

It is important to situate U.S. policy toward Iran in the context of President Trump's relationship with oil markets. He is quite sensitive to oil prices, viewing them as an important barometer of public sentiment and the U.S. economy. In his view, lower oil prices benefit his domestic political position and mitigate the impact of his other macroeconomic policies.

Trump entered the Iran-Israel war to seize an opportunity. Israeli forces had already imposed tremendous damage on the regime, and the president became increasingly open to the idea of using U.S. military force. After launching calibrated strikes, however, Washington quickly pivoted away from escalation, in part to help pull oil prices back down.

As for Trump's recent statements that Iran is now free to sell oil to China, they do not appear to signal any significant change in sanctions policy. Rather, he appeared to be acknowledging that Tehran will return to its regular export levels with Beijing.

Despite the ceasefire, the risks to energy security will persist—just at different levels. The risk to the Strait of Hormuz will remain low given the disparity in forces between Iran versus the United States and its allies. Tehran also needs to remain on amicable terms with the rest of the Gulf states. Thus, while the regime may take some steps to harass tanker traffic, it would only do so in a limited fashion and as a last resort.

Meanwhile, the Houthis have paused their attacks for now but will presumably attempt to rebuild their offensive capabilities following the last round of U.S. strikes in Yemen. They have accomplished their objectives and also proven their mettle against punishing retaliation. And much like Iran, they have been careful to choose targets that avoid escalation with the Gulf states. Going forward, they will likely seek some sort of rapprochement with Saudi Arabia.

For its part, Israel currently believes it has achieved its objectives, but this contentedness may not last. If Israel feels threatened, it may expand its targeting to include Iran's energy export facilities. Such a scenario would increase the risk of physical disruption to energy markets.

The ceasefire will probably hold for the short term—say, three to six months. Yet the two sides are unlikely to halt their hostilities completely. Israel will continue trying to disrupt Iran's nuclear program and, perhaps, undermine the regime. Even so, the war has proven that the risk to Hormuz remains exaggerated—though energy markets should not become too complacent about the risks to Iran's energy supply if the conflict escalates again.

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