

BUSINESS

War with Iran delivers another shock to the global economy

BY PAUL WISEMAN

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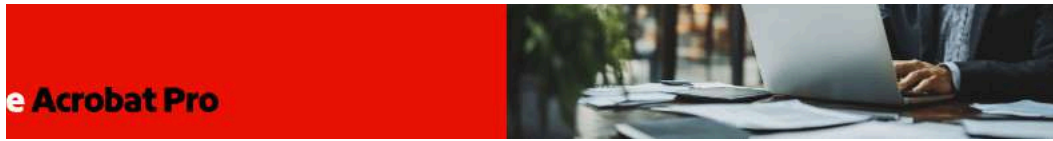
WASHINGTON (AP) — The [war with Iran](#) is doing collateral damage to the world economy.

The conflict is driving up energy and fertilizer prices; threatening food shortages in poor countries; destabilizing fragile states such as Pakistan; and complicating options for the inflation fighters at central banks like the Federal Reserve.

Causing much of the pain: the [Strait of Hormuz](#) — through which a fifth of the world's oil passes — was effectively shut down after the U.S. and Israel launched missile strikes Feb. 28 that killed [Iranian leader Ayatollah Ali Khamenei](#).

“For a long time, the nightmare scenario that deterred the U.S. from even thinking about an attack on Iran and which got them to urge restraint on Israel was that the Iranians would close the Strait of Hormuz,” said Maurice Obstfeld, a senior fellow at the Peterson Institute for International Economics and former chief economist at the International Monetary Fund. “Now we’re in the nightmare scenario.”

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According to AAA, the average price of U.S. gasoline has shot up to \$3.48 a gallon from just under \$3 a week ago. Prices could be felt even more significantly in Asia and Europe, which are more dependent on Middle Eastern oil and gas than the United States.

In India, restaurants are already warning of possible shutdowns as the government prioritizes gas supplies for households. Thailand has suspended overseas travel for civil servants and urged them to take stairs instead of elevators. The Philippines has introduced a temporary four-day work week for some government agencies, while Vietnam is encouraging people to work from home.

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20 million barrels of oil a day go missing

Every 10% increase in oil prices — provided they persist for most of the year — will push up global inflation by 0.4 percentage points and reduce worldwide economic output by as much as 0.2%, said Kristalina Georgieva, managing director of the International Monetary Fund.

“The Strait of Hormuz has to be reopened,” said economist Simon Johnson of the Massachusetts Institute of Technology and recipient of the 2024 Nobel memorial prize in economics. “It’s 20 million barrels of oil a day going through there. There’s no excess capacity anywhere in the world that can fill that gap.”

The world economy has shown it can take a punch, absorbing blows from the Russian invasion of Ukraine four years ago and from President Donald Trump’s massive and [unpredictable tariffs](#) in 2025.

Many economists express hope that global commerce can stagger through the latest crisis.

“The world economy has shown itself capable of shaking off significant shocks like broad U.S. tariffs, so there is room for optimism that it will prove resilient to the fallout of the war on Iran,” said Eswar Prasad, professor of trade policy at Cornell University.

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Timing is everything

Especially if oil prices can fall back to the \$70-to-\$80-a-barrel range, wrote economist Neil Shearing of Capital Economics, “the world economy may absorb the shock with less disruption than many fear.”

But a lot of ifs remain.

“The question is how long is it going to go on?” said Johnson, also former IMF chief economist. “It’s hard to see Iran backing down now that it’s announced this new leader” — [Mojtaba Khamanej](#). The son of the slain ayatollah is believed to be even more of a hardliner than his father.

Also muddying the outlook for an end to the crisis is uncertainty about what the United States is trying to achieve. “This is all about President Trump,” Johnson said. “It’s not clear when he’s going to declare victory.”

Economic winners and losers

For now, the war is likely to create economic winners and losers.

Energy importers — most of Europe, South Korea, Taiwan, Japan, [India](#) and China — will get clobbered by higher prices, Shearing wrote in a commentary for London’s Chatham House think tank.

Pakistan finds itself in an especially bleak position. The South Asian country imports 40% of its energy and relies especially heavily on liquified natural gas from Qatar, supplies of which have been cut off by the conflict. Higher energy prices will squeeze Pakistani families and damage their economy.

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Far from cutting interest rates to provide some relief, though, the country's central bank will probably have to raise them instead, say economists Gareth Leather and Mark Williams of Capital Economics. That is partly because inflation remains uncomfortably high in Pakistan — and higher energy prices threaten to make it worse.

But oil-producing countries outside the warzone — Norway, [Russia](#), Canada — will benefit from high oil prices without the risk of missile and drone attacks.

Energy isn't the only issue. Up to 30% of world fertilizer exports — including urea, ammonia, phosphates, and sulfur — pass through the Strait of Hormuz, according to Joseph Glauber of the International Food Policy Research Institute.

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Disruption in the Strait has already cut off fertilizer shipments, raising costs for farmers — and is likely pushing food prices higher.

“Any countries with significant agriculture sectors, including the United States, would be vulnerable,” Obstfeld said. “The effects are going to be most devastating in low-income countries where agricultural productivity may already be challenged. Add this extra cost component and you get the prospect of significant food shortages.”

Where things stand in the US

The United States, now a net exporter of energy, should gain slightly overall from higher oil and gas prices. But ordinary families will feel the pain at a time when [Americans are already furious](#) about high costs ahead of November's midterm elections.

U.S. households pay \$2,500 a year, or nearly \$50 a week, to fill up their cars, said Mark Mathews, chief economist at the National Retail Federation. A 20% increase in gasoline prices means an extra \$10 a week out their budgets, forcing them to cut back elsewhere. “If I have to pay more for an essential, then I would reduce a discretionary item,” Mathews said.

If oil prices remain around \$100 a barrel, analysts at Evercore ISI calculated, the resulting higher gasoline prices will wipe out for most Americans the benefits of higher tax refunds this year arising from Trump's

2025 tax cuts. Only the top 30% would still see a gain.

A quandary for central banks

The Iran crisis also puts the world's central banks in a bind. Higher energy prices feed inflation. But they also hurt the economy. So should central bankers raise rates to curb inflation — or cut them to give the economy a lift?

The Fed is already divided between policymakers who think a weak American job market needs help from lower rates and those still worried that inflation remains stuck above the central bank's 2% target.

"Their minds will easily go to the 1970s," Johnson said, when conflict in the Middle East and an Arab oil embargo sent oil prices rocketing. Central bankers are haunted by the memory that their predecessors "didn't get it right in the 1970s. They thought it was a temporary shock. They thought they could accommodate with lower interest rates, and they ended up regretting that because inflation became much higher."

Johnson predicted that higher energy prices ignited by the war with Iran are "going to massively intensify the debate inside the Fed" and make U.S. rate cuts less likely.

Anne D'Innocenzio in New York, Christopher Rugaber in Washington, Aniruddha Ghosal in Hanoi, Vietnam, and Anton Delgado in Bangkok contributed to this report.

