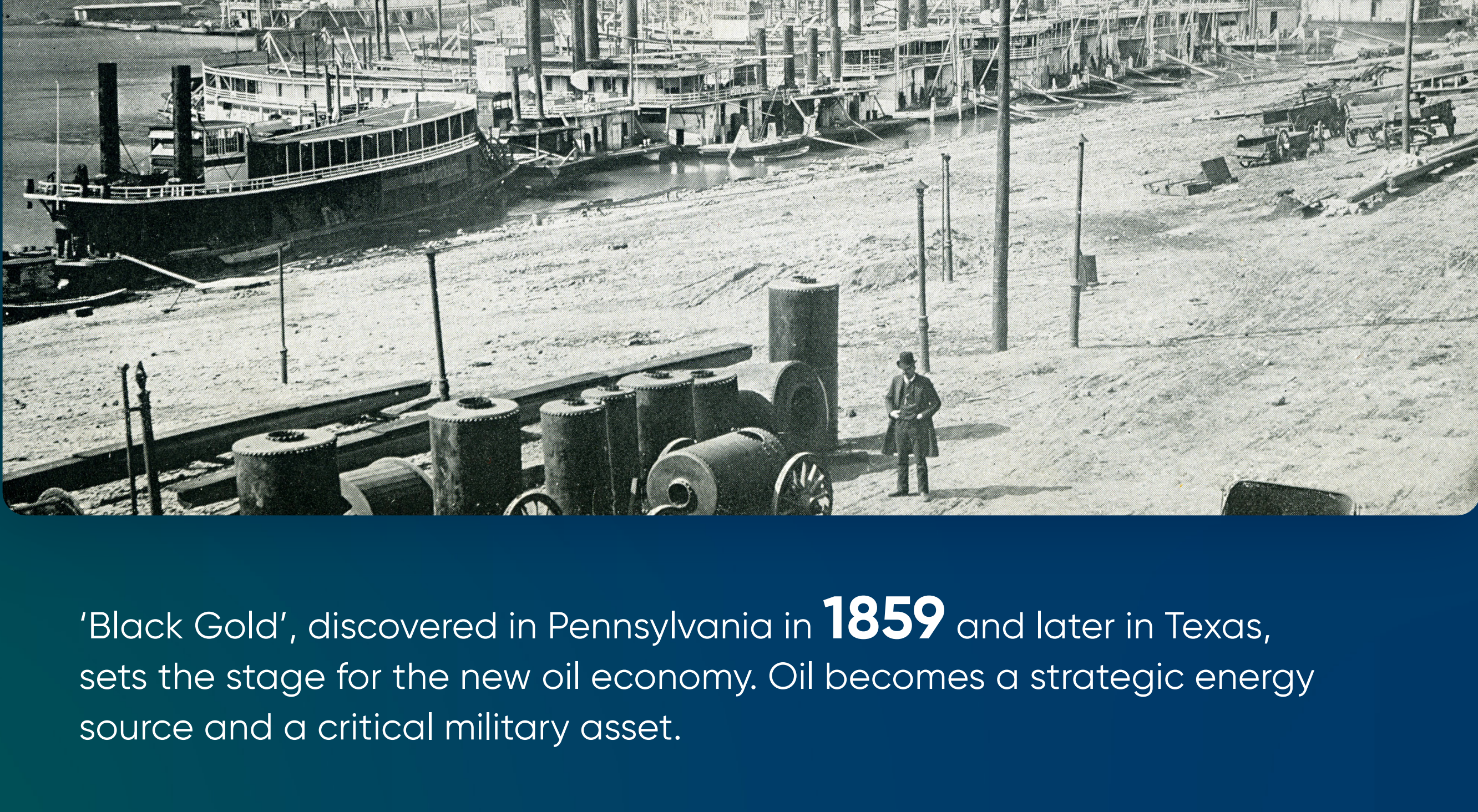


Economic Lessons from Oil Shocks: 1850–today

Oil prices profoundly affect global markets, inflation, and political strategies. Oil has shaped global economies and the outcome of wars since the mid-1800s.



1859 Black Gold



'Black Gold', discovered in Pennsylvania in **1859** and later in Texas, sets the stage for the new oil economy. Oil becomes a strategic energy source and a critical military asset.

Once diesel fuel replaces steam, oil become crucial to the outcome of World War II. **The hunt is now on:** vast oil reserves are discovered in Venezuela, Canada, Saudi Arabia, and Persia.

1973–1974 Oil Embargo



October 1973, OPEC imposes an oil embargo on the US, following Nixon's **\$2.2 billion aid** request to Congress for Israel amid the Yom Kippur War.

American oil prices soar, exacerbated by limited domestic production and the 1970s devaluation of the dollar; in 3 months, oil prices nearly **quadruple**.

1978–1979 Oil Shock



The Iranian Revolution, **1978–79**, ends with Sheikh Khomeini taking control.

Iranian oil output declines by close to **5 million** barrels per day (7% of world production). Hoarding and a booming global economy drive oil prices high.

1981–1982 Volcker's Reaction



Paul Volcker raises the federal rate from **11%** to a peak of **19%** by 1981.

This, along with other measures, reduces inflation from nearly **15%** to **4%** by the close of 1982. The US enters the worst recession since the Great Depression.

Net net? A 20-year economic slowdown in industrialized nations.

1990–1991 | 2003–2011 Gulf Wars and Big Oil



1990–1991
Iraq attacks Kuwait in 1990. Oil prices more than **double**

2003–2011
1 day after the US and allies launch a massive attack on Iraq, oil prices in New York plunge an unprecedented **\$10.56** a barrel to **\$21.44**.

Oil did not make a U.S. war against Iraq inevitable ... but it set the stage.

Before the 2003 invasion, Iraq's oil industry was fully nationalized, closed to Western oil companies.

Today, it is privatized, dominated by foreign firms.

2001 9/11



Bin Laden decides the United States is a paper tiger, the rest is history. The price of Brent Crude rises by **5%** but drops **25%** in 2 weeks.

While the results of the attack are massive and lingering, the effects of terrorist attacks on oil prices are typically short-lived..

2024 and beyond

Israel, Hamas, and The Axis of Resistance

China purchases over **95%** of Iran's exported oil; the US sanctions on Iran could drive oil prices to \$200, if Israel takes out oil Installations in Iran. A wider regional war could push prices even higher, putting the U.S. and Western Europe in a recession worse than 2008.

It can go either way

Increases in oil prices can raise transportation, production, and heating costs, thereby lowering corporate earnings, and curtailing discretionary spending. Inflationary pressure can lead to upward pressure on interest rates.

On the other hand? Investors may associate increasing oil prices with a booming economy.

While we are less oil-dependent today, supply disruptions – from geopolitical risks, wars, and economic shocks – still send shockwaves through the economy.

Oil Prices / Geopolitical risk

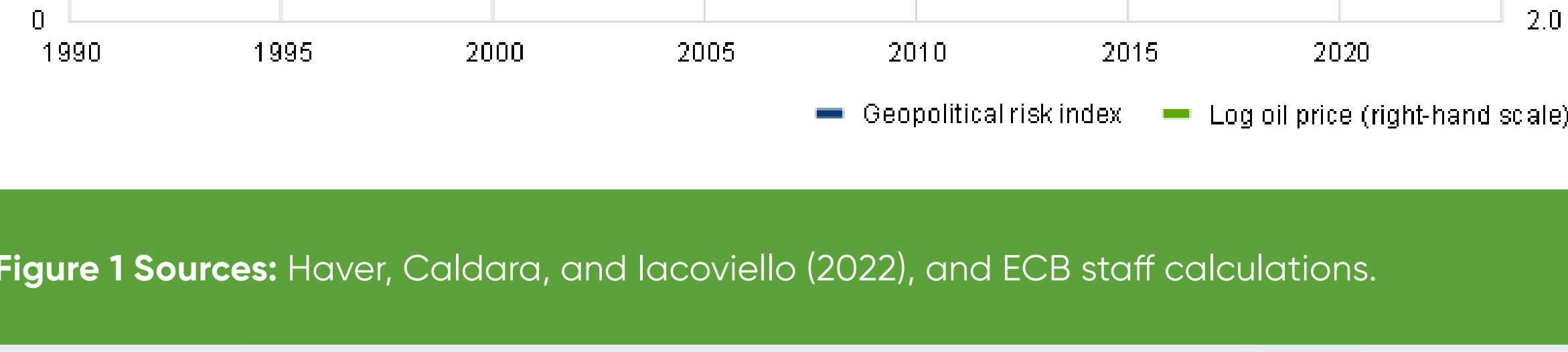


Figure 1 Sources: Haver, Caldara, and Iacoviella (2022), and ECB staff calculations.