

Iran Oil Shock or Inflation? Why War-Driven Energy Prices Pose a Different Economic Problem

March 12, 2026 - Americans are once again watching gasoline prices climb as conflict involving Iran disrupts global oil markets. The increase shows up quickly at the pump and soon appears in airline tickets, shipping costs, and grocery prices. To many households, the surge feels like inflation returning. But many economists argue that the current situation is not the same kind of inflation central banks normally try to control. Instead, it is what economists call a supply shock, a sudden disruption in the availability of a key resource that raises prices even when overall demand in the economy has not changed. And increasing interest rates won't do a thing to change it. In fact, doing that could very well make the situation much worse.

When war or geopolitical instability restricts oil supply, the global price of crude rises. Energy companies pay more for oil, refiners pass those costs to gasoline stations, and transportation companies face higher fuel bills. Because energy is embedded in nearly every part of the economy, the effects spread through shipping, manufacturing, food distribution, and travel.

The result is higher prices, but the cause is fundamentally different from inflation driven by excessive consumer demand or rapid growth in the money supply. This distinction matters for economic policy.

Central banks such as the Federal Reserve typically respond to inflation by raising interest rates. Higher borrowing costs slow spending and investment, which can reduce demand and eventually ease upward pressure on prices.

However, higher interest rates do not create more oil. They do not reopen shipping routes or increase the number of barrels produced in global markets. When the source of higher prices is a geopolitical disruption rather than overheating demand, monetary tightening may have little effect on the underlying problem.

Economists often point to the oil shocks of the 1970s as an example. During that decade, sudden cuts in global oil supply pushed energy prices sharply higher. Policymakers responded with aggressive interest rate increases intended to contain inflation. While the rate hikes eventually slowed price growth, they also triggered deep recessions and unemployment.

That period introduced the term stagflation, a painful mix of high prices and weak economic growth.

Responding too aggressively to energy driven price increases risks repeating that pattern. If borrowing costs rise while energy prices are already squeezing household budgets and business costs, the result can be a double hit to the economy.

Consumers may face higher gasoline and food bills while also paying more for mortgages, credit cards, and car loans. Businesses dealing with rising transportation and manufacturing expenses may also see their financing costs increase, discouraging hiring and investment.

In that environment, economic growth can slow rapidly even as headline inflation numbers remain elevated because of energy prices.

That is why many policymakers and economists focus closely on "core inflation," a measure that excludes food and energy prices. Core inflation attempts to capture broader price trends driven by demand in the economy rather than short term volatility in commodity markets.

If core inflation continues to decline while energy prices rise due to war, the case for maintaining or even lowering interest rates becomes stronger in the eyes of some economists. The argument is that monetary policy should respond to underlying inflation trends, not temporary shocks that originate outside the domestic economy.

Lower interest rates could help offset some of the economic strain caused by higher energy costs. Cheaper borrowing can support business investment, encourage hiring, and reduce interest expenses for households already dealing with rising fuel prices.

In addition, lower rates can support sectors such as housing, manufacturing, and construction that are especially sensitive to borrowing costs. By helping businesses maintain production and employment, easier financial conditions could cushion the broader economy while the energy shock works its way through global markets.

None of this means energy driven price increases are harmless. For households living paycheck to paycheck, a jump in

gasoline prices can strain already tight budgets. Transportation costs can ripple through the price of groceries and everyday goods.

But from a policy perspective, the distinction between inflation caused by strong demand and price increases caused by disrupted supply remains critical.

If the current rise in energy prices is primarily the result of war driven supply constraints rather than overheating economic activity, higher interest rates will not solve the problem. In fact, tightening financial conditions during an energy shock could risk slowing the economy unnecessarily.

As policymakers evaluate the path ahead, the key question may not be whether gasoline prices are rising. It may be whether the broader economy is still experiencing sustained inflationary pressure once volatile energy markets are taken out of the equation.

If other measures of inflation continue to ease, the debate over interest rates may increasingly turn on a simple question. Are policymakers fighting inflation, or are they responding to a temporary shock that monetary policy cannot fix?

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