



# How the war on Iran exposes global economic interconnectedness (Episode 29)

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March 24, 2026

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The war against Iran by the United States and Israel has spread turmoil through oil and natural gas markets, spiking prices and threatening the world economy. How will the war impact the global economy, climate, and the determination of many countries to pursue energy from renewable sources? Adnan Mazarei (PIIE) joins host Monica de Bolle to explore the ramifications of another war in Iran; what it means for oil, natural gas, and other critical input markets; and how it might affect environmental efforts and the green transition.

This podcast is produced by the Peterson Institute for International Economics.

**MONICA DE BOLLE:** The war against Iran launched by the United States and Israel has disrupted oil and natural gas markets globally as commerce through the Strait of Hormuz came to a virtual halt.

What does the war mean for oil globally? Will this force a green transition, or will the effects of the war further disrupt supply chains and hamper environmental efforts?

You're listening to an episode of Policy for the Planet, a podcast exploring the global response to the climate crisis. I'm your host Monica de Bolle, a senior fellow at the Peterson Institute for International Economics.

To help us dive in deeper, I'm joined by:

**ADNAN MAZAREI:** Adnan Mazarei, non-resident senior fellow at the Peterson Institute in Washington, D.C.



**MONICA DE BOLLE:** Adnan's work at the Institute focuses on the major economies of the Middle East and Central Asia and the long-term financial and macroeconomic challenges they face.

This episode was recorded on March 12.

So Adnan, welcome to the show. I thought we'd dive right in, given that the topic is hot. Please give us an overview of how the war in the Middle East is affecting oil and LNG (liquefied natural gas) markets and where you see trends heading in the near term.

**ADNAN MAZAREI:** The war with Iran has brought about the largest disruption ever in oil markets. As you know, about 20% of the world's oil output and 20% of LNG go through the Strait of Hormuz. With the start of the war, traffic through the Strait of Hormuz has come to a virtual halt, not a complete halt, but a virtual halt.

There are alternatives to the strain of Hormuz. For example, there is a pipeline in Saudi Arabia, there is a pipeline in the UAE, but amounts that they can carry are limited. As a result, oil and gas prices have shot up considerably, especially natural gas prices. The International Energy Agency, which is a group of the consumers of petroleum have agreed to release 400 million barrels from their strategic reserves. This is roughly twice the amount that was released during the Ukraine War, the early stages of the Ukraine War. However, in the past, this has only contributed about two million barrels a day of additional supplies.

If push comes to shove, this can go up to four, but it will not take care of the entire disruption in supply.

I think this war is not about to end soon. It's most very likely it will go on for a few weeks. In my opinion, the most important factor that will determine when the war ends is the fear of inflation, especially in the US, and its possible impact on the November elections.

**MONICA DE BOLLE:** So I want to come back to that point later, but let me ask you something before we jump into a few other things. And that is, even if the war were to end relatively soon, wouldn't it still be the case that oil markets are not simply going to normalize from one day to the next, right? It's going to take a while, especially when you consider that perhaps some countries may have shut down refineries,

Perhaps other things are going on, but in any event, when you have a disruptive shock such as this one, you can't just flip a switch on and off and turn the production of oil on



and off that way. So if I'm correct in this view, and please correct me if I'm wrong, wouldn't it be the case that even if the war to be a ceasefire, we would still be seeing the kinds of pressures in oil markets that we're seeing right now?

**ADNAN MAZAREI:** You're absolutely correct. I've heard oil experts saying it will take about four weeks or so for the markets to normalize, even if the hostilities ended today. So we are going to be stuck with the outcome of this war for a while. As you mentioned, for example, Qatar has cut off the production of LNG.

These are not facilities that could be turned around on the dime. It will take a while and the markets will have to live with the consequences for a while.

**MONICA DE BOLLE:** So let's go back to the, not yet to the inflation story, but to something else, which is we've been talking about oil, we've been talking about natural gas, but of course, one thing that the war does reveal is how interconnected the global economy still is, despite the fact that we've been using a lot of tariffs, been using a lot of protectionist measures and so on. And we see that from fertilizers to critical minerals, there are lot of indirect effects that are coming down the pipeline. So could you please talk a little bit about that and the broader disruption in supply chains that we see?

**ADNAN MAZAREI:** Sure, as you rightly said, oil and gas get used in the production of everything. Food, fuel, petrochemicals, and on and on and on. For example, petrochemicals get used in the production of solar panels. Higher energy prices are going to hit particularly by...they are particularly going to artificial intelligence, their data centers, which are highly energy intensive.

That might lead, for example, to a cutback in US growth on the margin. In general, countries that have supply chains that are most convoluted and dependent on oil and gas will obviously be the hardest. Countries that have lower stocks of fuels and other things will be hit. For example, the microchip industry in East Asia is likely to get hit. Critical minerals are going to be hit. Plans for expansion of processing of critical minerals are going to be hit. For example, Saudi Arabia has been planning to become a critical minerals processing platform using raw materials from Africa for consumption in various parts of the world. Those are now going to be affected. There will also be financial impact. There's volatility in asset prices. Fear of inflation will of course lead to higher interest rates. Today I saw some information showing that mortgage prices, mortgage rates in the US are already picking.

**MONICA DE BOLLE:** All encompassing, in other words.



**ADNAN MAZAREI:** Everything is going to be affected.

**MONICA DE BOLLE:** I want to pick up on the things you've said about solar panels and critical minerals. But before I do that, let me just phrase things this way. We've seen some people arguing that if oil prices remain high, and I think we've pretty much established that at least for the time being, that is the reality we're living in, that this will likely provide a boost to investments in renewable energies. Well, we've just talked about how, you know, the oil and gas and everything else that's related to oil and gas ends up feeding supply chains everywhere, including supply chains related to renewable energies and other climate adaptation policies.

So my question to you is, first of all, do you agree with the view that renewables become more attractive in some sense or investments in renewables become more attractive? And more specifically, what regions and countries, you've already said some of this, but what regions and countries do you think are likely to see greater investments in renewables in this general context?

**ADNAN MAZAREI:** Overall impact on energy investment is not clear to me. In the longer term, if wiser minds prevail, and that's a big if, we should see exactly what you said, higher investment in renewables, greater shift from fossil fuels. Some countries, for example, in Europe and East Asia are likely to do that.

But it is very unlikely that such investment will happen in the US under the current administration. In fact, you are going probably to see greater encouragement to investment in fossil fuels. In the short run, it might actually get worse. For example, even countries that realize there needs to be more investment in green energy, may end up investing more in fossil fuels just to get over the hump in the next few years. Secondly, natural gas prices go up, they are resorting more to the use of coal in energy production, electricity production.

It is not going to be smooth sailing. I said, much depends if wiser heads prevail and the world is not a positive area when it comes to people having wise heads.

**MONICA DE BOLLE:** In relation to the US, you were saying that it could even be the case, given that the US isn't oil exporter, it could even be the case that the fossil fuel industry, which by the way is what the current government really does want to entice and benefit, that that ends up being much more prominent than anything on renewables. And of course, we've just had the...



A year ago, we had the walking back of subsidies and tax breaks and other fiscal incentives for renewable energies that were contained in the Inflation Reduction Act. So I think that in itself kind of underlines the point that you've just made with respect to the US. Would you agree?

**ADNAN MAZAREI:** Absolutely, absolutely. You're not going to see more. Green energy, you're not going to see wind electricity towers coming up in the US in the next few years. We may see actually more investment in new refineries, more offshore production of oil.

**MONICA DE BOLLE:** So let's now do a 360 degree and go back to, it literally is that, go back to the beginning when we were talking about inflation and you said a few interesting things about that. So let's talk about it, particularly in the context of the US. We know the US has become a major oil and natural gas exporter in recent years, and yet we see gasoline prices rising quite a bit. So my first question to you is one, can you explain why that is? Because it's confusing for some people. And what other price increases related to the war is the U.S. consumer likely to face?

**ADNAN MAZAREI:** Monica, as you rightly said, the US has become an oil exporter. It has also become a net natural gas exporter. But prices for petroleum and gas products are set internationally. Just because the US is in a favorable position in terms of net trade doesn't prevent prices going up. Secondly,

Even if the U.S. is well endowed in natural gas and oil, there are limits to the capacity of refineries.

There are also issues about the quality of oil that is needed in some refineries or not. For example, Venezuela produces heavy oil, which is suitable for use in the US, but it has to be imported. Higher energy prices are likely to pass on to shipping costs, petrochemicals we discussed, plastics, fertilizer, electric vehicles and so forth. They're likely to pass on to the cause of use of artificial intelligence.

Of course, over the past decades, energy intensity of output in the US has come down. The US Federal Reserve has shown considerable independence has strong credibility and that has prevented prices from going up now looking ahead there are questions whether the Fed will be able to maintain that level of independence things are going to be difficult and the new incoming chair of the Federal Reserve may not have as easy of a time in cutting rates.



**MONICA DE BOLLE:** On top of it all, because as we both know, supply shocks coming from oil, yes, we are not facing the same kind possibly of supply shock that we've seen in the past. Nonetheless, it is a supply shock. And that always puts policymakers on the back foot in terms of what to do, right? Because you have two forces that affect the economy. have stagnating forces which affect growth. And at the same time, you have inflationary forces that are driving in the opposite direction. It's a kind of a traditional dilemma, as it were, isn't it?

**ADNAN MAZAREI:** Absolutely, you're on the mark.

**MONICA DE BOLLE:** So, Adnan, you've recently written a very interesting paper with Greg Auclair on the America First Investment Pledges. Does the war affect your conclusions?

**ADNAN MAZAREI:** I think the conclusions of the paper still stand. Countries entered those arrangements with the U.S. for several reasons. One, economic benefit. Two, fear of U.S. tariffs and protectionism. And those countries need to remain under the U.S. security umbrella. Okay. Now.

The US Supreme Court has ruled against the use of tariffs under the International Emergency Economic Powers Act, but the US government has other frameworks at its disposal. So I don't think that ruling is going to affect anything. The US will still be able to put pressure on from the perspective of protectionism on those countries.

Secondly, those countries which are mostly in the Gulf cooperation council countries in the Persian Gulf and in East Asia, Korea, Japan, and Taiwan, they will need to remain under the US security umbrella. And arguably, they need to remain under that umbrella more than before the Iran-Iraq war. So they're not going to pull back on that. What could change is the ability of those countries to fulfill their pledges.

The East Asian countries have been hurt considerably by these energy price increases and that will increase as we go along. The Gulf Cooperation Council countries are suffering drops in oil revenues. Although oil prices are going up, that doesn't mean necessarily they can export. Second, their defense spending will need to change considerably.

Third, the risk premium they face in international financial markets is likely going to increase and their countries like Saudi Arabia, which is a net capital importer, may have to pay more. Foreign direct investment will be much more careful about coming into the



GCC countries. Also, the growth model of those countries may be affected. As a result, even if they may want to continue those pledges, they may have to step back, recalibrate, and even delay some of those commitments.

**MONICA DE BOLLE:** Well, Adnan, thank you very much for that very sobering outlook as to what we face. I'm with you. Sane and sober minds don't always prevail. So I think we'll have to see what happens from here on out. But thank you very much for coming on Policy for the Planet. It was a pleasure to have you.

**ADNAN MAZAREI:** Thank you for having me on your program.

**MONICA DE BOLLE:** You've just finished an episode of Policy for the Planet — thanks for joining us! Don't forget to rate, review and subscribe.

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Until next time, here's to creating meaningful impact through interesting conversations.