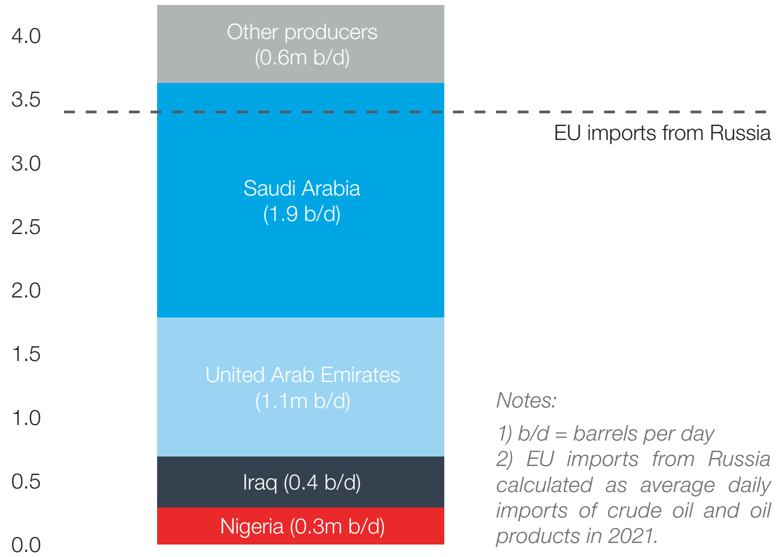
Accuracy

EMBARGOES AND ENERGY PRICES

July 2022

With the global economy in turmoil, energy prices are exploding. A general rising trend in the prices of oil and gas since mid-last year has been compounded in recent weeks by the war in Ukraine and the economic reprisals taken by the West against Russia. These reprisals now include a partial embargo on Russian hydrocarbons. But what does that mean in the short term? And how does the current situation compare with the oil crisis of the 1970s? Let us delve into the matter in this Economic Brief.

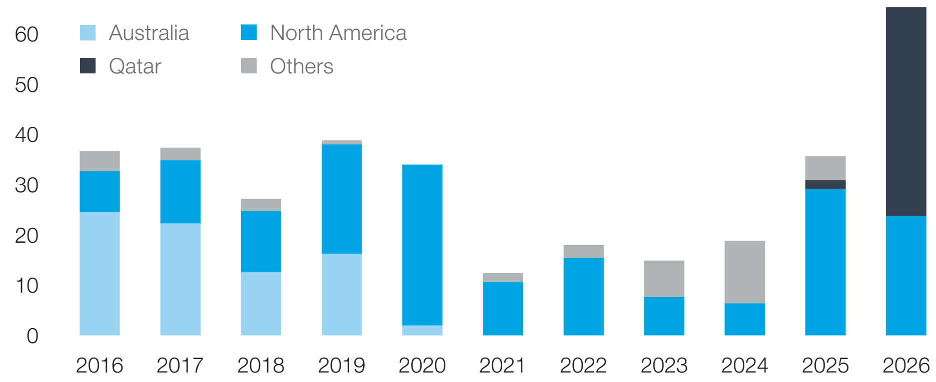
Current excess oil production capacity (excluding Russia & Iran)



Sources: Accuracy & OECD

Europe will face some difficulty when implementing its embargo on Russian oil and gas. The European Union on average imports 3.4 million barrels of oil each day from Russia. Assuming the same level of oil consumption and a full embargo on Russian oil, Europe would take up 80% of all current excess production capacity, leaving very little room for manoeuvre for oil production globally. This issue is intensified by the fact that Russia may struggle to find alternative outlets for its production, with insurers currently unwilling to insure Russian maritime deliveries due to Western sanctions.

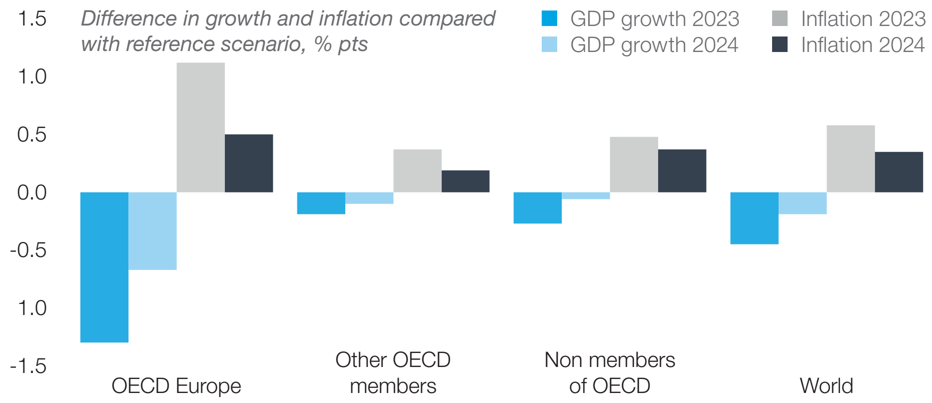
Small increases in liquefied natural gas production capacity in the short term (billions m³)



Sources: Accuracy & OECD

Difficulties also arise for Europe when trying to find alternative sources of natural gas. This graph shows where new liquefied natural gas capacity has been and will be created from 2016 to 2026. Quantities remain limited in the immediate future, raising the question of where the EU will be able to find new suppliers before Qatar ramps up production in 2026.

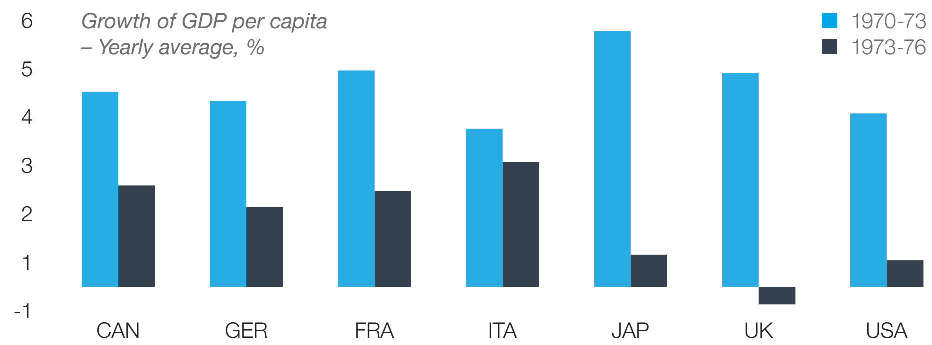
An embargo on Russian gas would have a lasting effect on growth and inflation in Europe



Sources: Accuracy & OECD

The OECD forecasts a twofold impact of an embargo on Russian gas in Europe: a fall in GDP growth and a rise in inflation. The graph opposite demonstrates this dual effect by comparison to the OECD's reference scenario. It shows that the impact felt in Europe as a result of such an embargo is much more significant than that felt elsewhere, with growth cut by 1.3 points in 2023 and inflation exacerbated by 1.1 points in the same year.

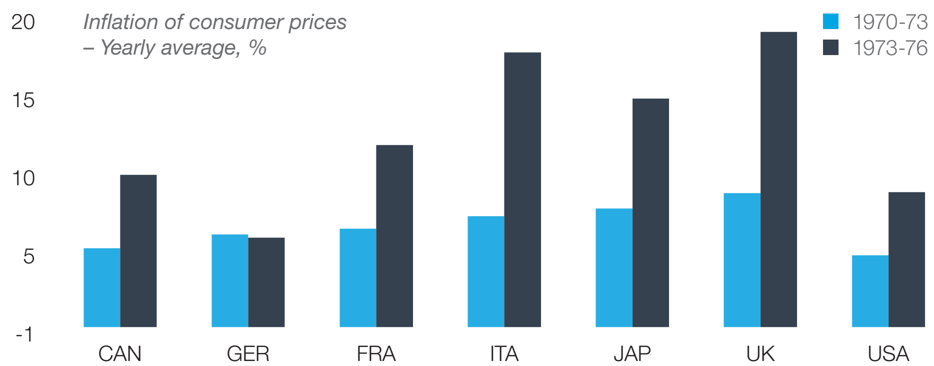
Slowdown in growth in the last oil crisis...



Sources: Accuracy & OECD

But how does this crisis compare with the oil crisis of the 1970s, when the Middle East blocked supply of oil to the West? Growth of GDP per capita drastically fell as a result of the crisis some 50 years ago, roughly halving in Canada, Germany and France and declining much more substantially in Japan, the UK and the US, as shown opposite.

...and a significant rise in inflation



Sources: Accuracy & OECD

The crisis also led to a substantial rise in inflation, almost doubling in many Western countries. So parallels can certainly be drawn between the past crisis and the situation today. However, we can take heart from the fact that oil prices remain below their peak in the 70s and early 80s and inflation, though high, remains lower than the levels seen in the past.

An embargo on Russian hydrocarbons serves as another way for Europe and the West to inflict economic damage on Russia and to reduce the considerable funds the country has at its disposal to continue the war in Ukraine. However, such an embargo will come at a heavy price for Europe: further decreases in growth and further increases in inflation. At a time when populations are already struggling, this may well be a bitter pill to swallow.