‘Some believe the situation is déjà vu.’

A Tale of Two Oil Crises

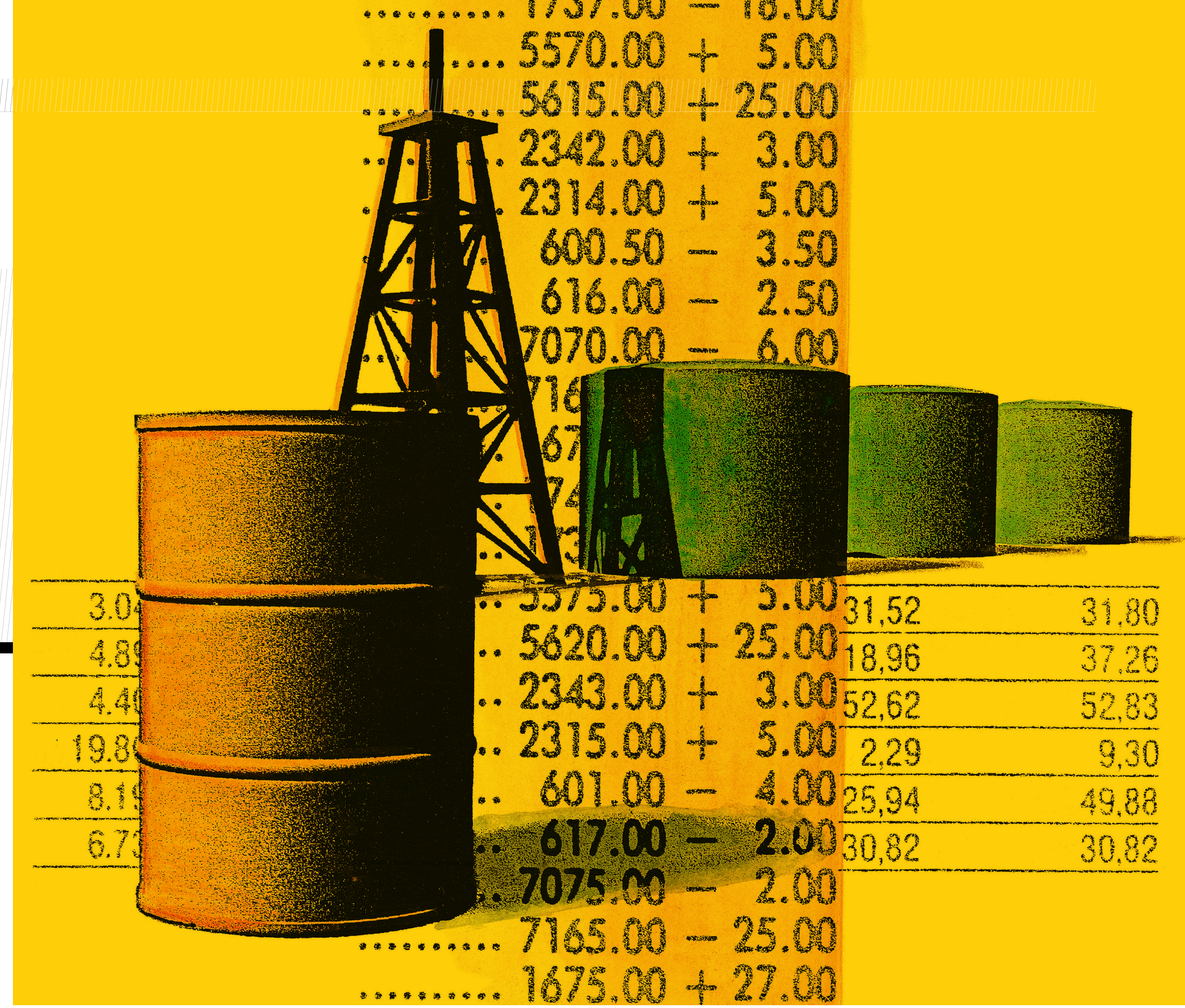
In recent decades, most people have expected energy to be both reasonably priced and plentiful. Not so in 1973, when the Arab member states of OPEC (the Organization of Petroleum Exporting Countries) imposed an embargo on oil sales to the US and other developed countries. Soon after, Americans faced gasoline shortages and rising inflation that would continue through 1980. Thankfully, shortages and high prices didn’t return for decades—not until earlier this year, when the US and Israel went to war against Iran.

By disrupting oil supplies in the Middle East, the war has sent prices higher, just as we saw in the 1970s. Some observers believe the current situation is like déjà vu. But while these two crises are similar, there are distinct differences between them, says Jay Hatfield, CEO of Infrastructure Capital Advisors. “There’s been a whole bunch of incorrect conclusions,” he says.

First difference: The closure of the Strait of Hormuz this year has prevented 20 percent of global oil production from being shipped. Compare that with the Middle East’s 37 percent share of global oil production in 1973.

Because the recent disruption represents a smaller portion of oil output, prices haven’t jumped as much. Between July 1973 and early 1980, prices surged from $3.56 a barrel to $39.50, according to Federal Reserve data. A comparable increase today would put the current price of a barrel at more than $700, Hatfield says. Instead, the cost of light sweet crude oil has approximately doubled, from $67 per barrel earlier this year to a high of $113 in the spring.

Second difference: In 1973, the US was a net importer of oil, which made the country more vulnerable to the Arab blockade. Since then, the nation has emphasized the importance of energy security, says Rob Thummel, a senior portfolio manager at Tortoise Capital. Over the past decade or so, new ways of oil drilling have been developed. Having new technology and massive oil deposits means the US has the capability to pump more, he says. Ultimately, that output surge has led to the US becoming a net exporter of oil plus related products, and it is now energy self-sufficient. “Shale oil has a competitive advantage,” Thummel says. “It has uncovered a significant amount of oil and natural gas that really reduces the risk of us running out of fuel.”



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And the US government is taking a different approach to the problem than it did in the 1970s. Back then, the country lacked an understanding of inflation. When the government instituted price controls to try to stymie inflation, it exacerbated it instead, driving it up to 14 percent by 1980. But price controls usually lead to shortages. That’s because when the price cap is lower than the market price, producers tend to ratchet down or completely halt their output, experts say. So far this year, we haven’t seen gasoline shortages because the US has relied on the market to set competitive prices. “Supply-and-demand response in the market is critical,” Hatfield says. Still, inflation in the US isn’t at a comfortable level.

There is some good news, however. In the spring, the United Arab Emirates, one of the Middle East’s leading oil producers, decided to leave OPEC, thereby freeing it to pump more oil. (It was the second member nation to quit the group, having been preceded by Qatar in 2019.) “Once the war is over and supplies are back to prewar levels, we’re going to see much lower prices of oil as a result of this decision,” says Bernard Haykel, professor of Near Eastern Studies at Princeton University.

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Portrait by ROB DOBI