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Energy Prices Hit the Gas



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n the surface, it sounds like the early 1970s, with shortages at gas pumps and homeowners suffering through soaring heat prices. But this isn't the energy crisis of 1973, when a group of oil-rich Arab countries embargoed oil exports to the US and other countries. It's actually what is happening in large pockets across the globe, only it has

a new name: energy insecurity.

Make no mistake: even since before Russia's invasion of Ukraine, the world has been in the midst of an extended period when energy sources are not available at affordable prices. The problem is particularly acute in Europe, but many experts are expecting some shock waves throughout the global economy. “We are certainly in an energy crisis,” says

James Penny, chief investment officer at TAM Asset Management. Indeed, the cost of European natural gas, used for home heating and electricity, jumped more than eightfold between February and November last year. A barrel of Brent crude oil has seen a bigger rise in two years than the world saw in 1973 to 1974, when oil prices tripled. Amid rising prices, media reports prompted panic fuel buying, creating a shortage last year, Penny says.

The knock-on effect of energy prices rising is immediate on the economy and on government policy makers, Penny says: “It affects central banks [and] consumer pocketbooks.” Household budgets get squeezed simply by covering essential fuel costs, leaving less for discretionary purchases. All of which isn't great news for corporate profits, which will likely get hit by lower sales to consumers and higher business costs.

To be sure, the oil business is always volatile. Prices, as many people recall, were depressed during the start of the pandemic. But as the economy started booming, supply for the growing energy demand in a wide range of sectors couldn't keep up. Few predict any easing this year, citing mounting concerns over inflation.

But it's not all economics. Geopolitics is, of course, a big player in all this, as the early stages of tanks rolling into Ukraine showed. Russia has been a major supplier of natural gas in Europe, and natural gas is behind much electricity generation there, which is critical to businesses. Weakness in Europe, meanwhile, would also be disastrous for other countries. Since the end of WWII, Europe's rich countries—the UK, Germany, and France—have helped boost the developing world.

High energy prices have historically halted economic expansions. “Virtually every recession we've had was precipitated by an energy crisis,” says Jack Ablin, chief investment officer at Crescent Capital. In this case, the shift away from traditional energy sources may be also playing a significant role. “The plan to transition to green energy means there's going to be a lot of pain,” says Steve Hanke,

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a professor of applied economics at Johns Hopkins University. A poster child for the problem is Germany, Europe's largest economy. It decided to decommission all its remaining nuclear power plants by year-end.

At the same time, the power infrastructure for renewable energy isn't there to fill the gap. “If you have wind and solar, you have to have someplace to store the energy,” Hanke says. Unfortunately, extant battery technology remains too far short of the massive requirements to make enough difference. Because of the lack of storage, manufacturers stand to get hit hard. In simple terms, lack of sun or wind will mean supply shortages and rising costs. “The price peaks are already tremendous,” Hanke says. ▮

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