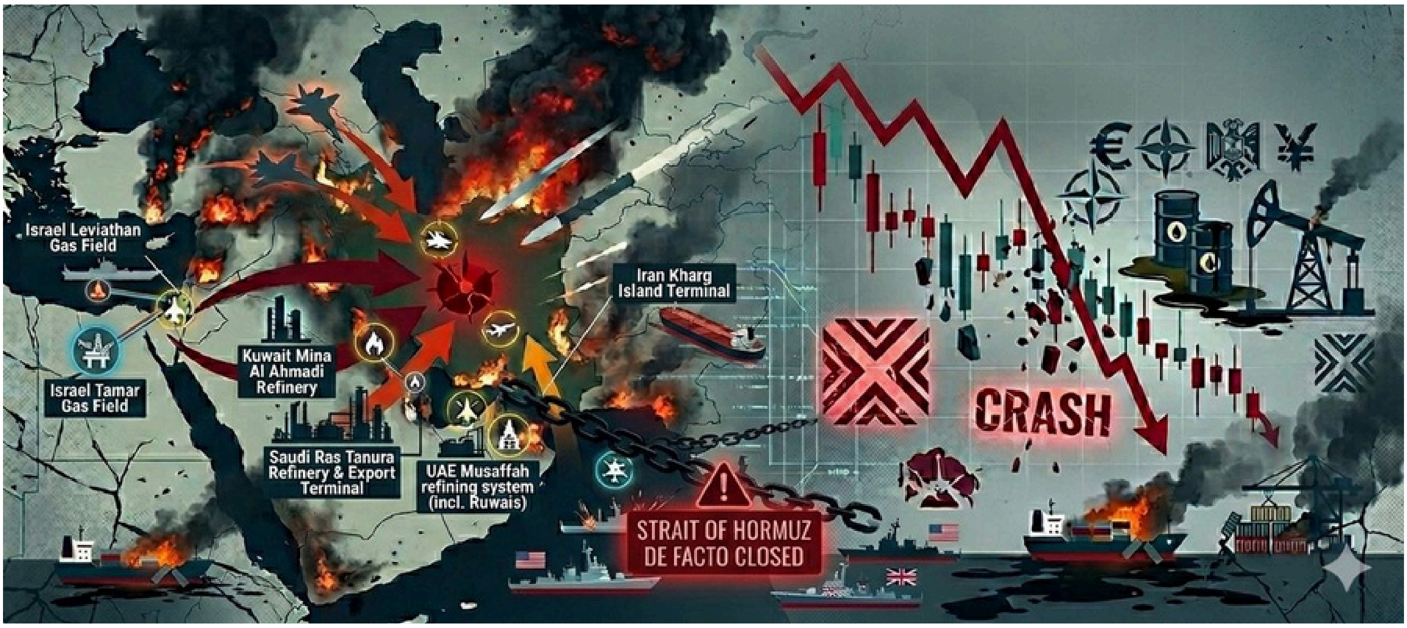
9 March 2026

From Geopolitical Shock to Macroeconomic Stress - 2

Energy Shock and Financial Repricing



Executive Overview

The escalation of tensions between the United States and Iran illustrates how geopolitical developments can quickly evolve into macroeconomic shocks when they intersect with critical energy infrastructure. Because a substantial share of global oil and liquefied natural gas flows transit through the Strait of Hormuz, heightened geopolitical risk in the Gulf region can trigger repricing in energy markets and inflation expectations. Even without a full disruption to shipments, uncertainty surrounding supply security can embed a geopolitical risk premium into crude oil prices, amplifying volatility across global markets and reinforcing inflation pressures in energy-importing economies.

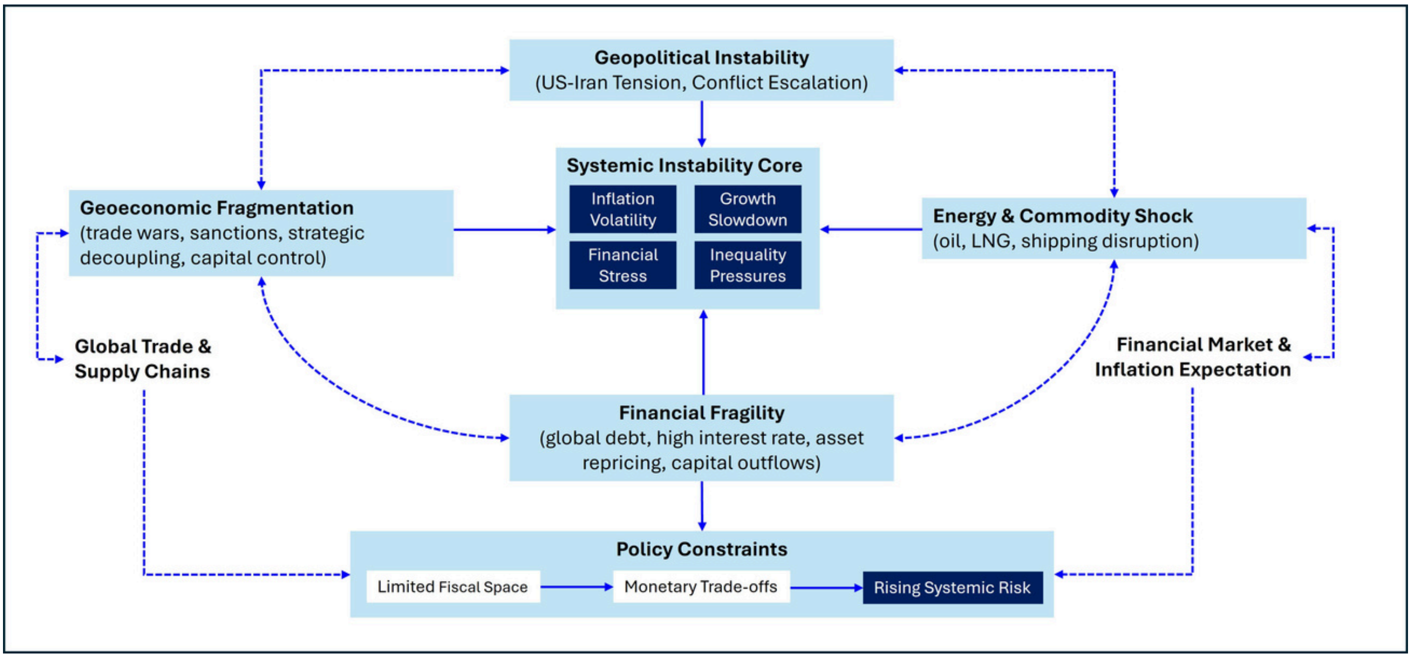
For Malaysia, the economic transmission of this shock is likely to occur primarily through global energy price movements rather than direct trade exposure to the Middle East. While Malaysia's trade and tourism linkages with the region remain relatively limited, higher oil prices can influence domestic inflation dynamics, logistics costs and fiscal balances through increased subsidy expenditure. Under our baseline scenario of Brent crude averaging around USD90 per barrel and the ringgit remaining below RM4.00 per US dollar, Malaysia's economy is expected to remain resilient with GDP growth projected at 4.6% in 2026. However, if elevated energy prices persist for several months, cost pass-through effects across supply chains and rising fiscal subsidy pressures could reduce growth by around 0.3–0.4 percentage points and complicate the policy trade-off between inflation management and growth support.

1. Energy Shock in a Polycrisis Environment

The escalation of tensions between the United States and Iran represents more than a conventional geopolitical confrontation. It unfolds within a broader global environment characterised by overlapping economic, financial and political vulnerabilities. In recent years, the global economy has increasingly exhibited features of a polycrisis, where multiple shocks interact and reinforce one another rather than occurring in isolation. Energy security concerns, geoeconomic fragmentation, financial fragility and political instability now form an interconnected system in which disturbances in one domain rapidly propagate across others.

The conceptual framework illustrated in the polycrisis model highlights how these dynamics converge around a core of systemic instability. Rising geopolitical tensions can trigger supply disruptions in energy markets and global trade routes, amplifying inflation volatility, weakening growth and increasing financial stress. These pressures interact with an already fragile global financial structure characterised by historically elevated debt levels and tighter monetary conditions. As a result, geopolitical shocks today tend to transmit more rapidly and persistently through the global economy than in previous decades.

Figure 1: Global Polycrisis Framework: From Geopolitical Shock to Systemic Stress



source: IPPFA

Energy markets sit at the centre of this transmission mechanism. Unlike sector-specific shocks such as trade disputes or regulatory actions, energy disruptions propagate across nearly all sectors of economic activity. The geographic concentration of energy infrastructure and shipping routes further magnifies systemic risk. A significant share of global oil and liquefied natural gas flows transit through narrow maritime chokepoints, particularly the Strait of Hormuz, making stability in this region critical to global price formation and supply reliability. In this context, the US–Iran escalation represents a particularly potent source of macroeconomic risk because it intersects directly with the infrastructure underpinning global energy markets. When tensions emerge near major energy hubs or maritime chokepoints, markets respond not only to the disruption itself but also to the expected duration of supply uncertainty. This leads investors to embed a structural risk premium into energy prices, transmitting through inflation expectations, financial market volatility and global growth.

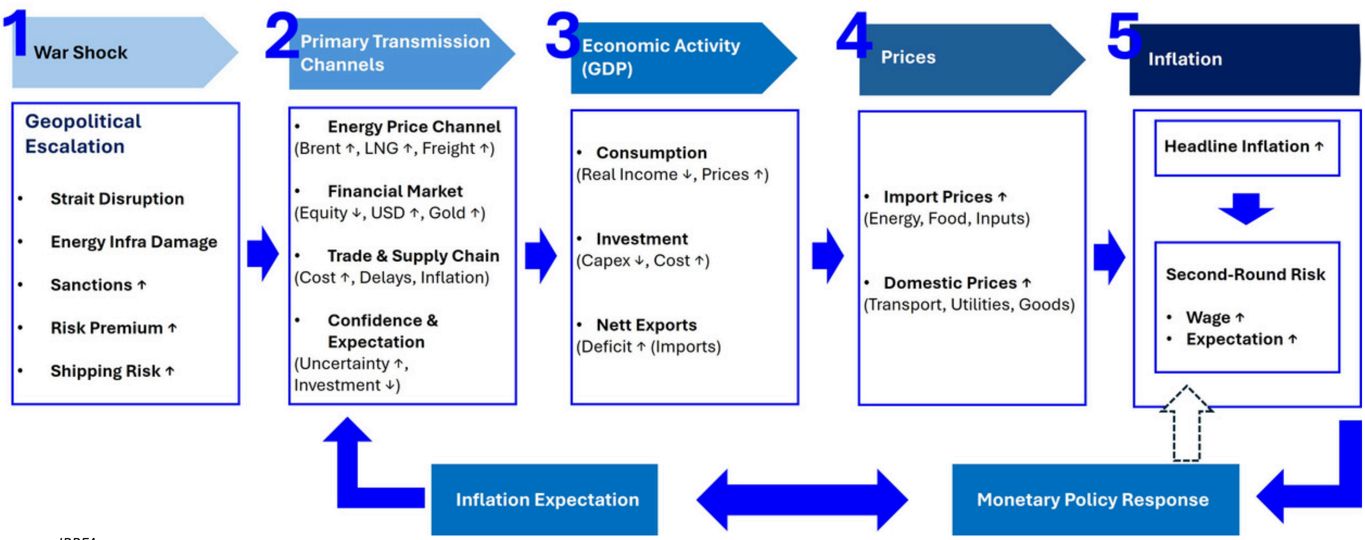
The broader implication is that geopolitical shocks are increasingly functioning as macroeconomic shocks. The current escalation illustrates how a regional conflict can rapidly evolve into a global economic event through interconnected energy, financial and trade channels. In such an environment, the key question facing policymakers and markets is not simply whether disruptions occur, but how long uncertainty persists and how deeply it becomes embedded in expectations. As the following sections will demonstrate, the transmission from geopolitical escalation to macroeconomic stress operates through several reinforcing channels, beginning with energy markets and extending into financial conditions, global trade flows and domestic policy constraints.

2. Economic Transmission of Energy-Driven Geopolitical Shocks

Geopolitical conflicts that intersect with major energy infrastructure transmit through the global economy via several reinforcing channels. Unlike conventional geopolitical events that remain largely contained within diplomatic or military domains, energy-related disruptions rapidly propagate through commodity markets, financial systems and global supply chains. As a result, the macroeconomic consequences extend far beyond the immediate region of conflict.

The transmission mechanism typically begins with an initial geopolitical shock that raises uncertainty around energy supply and transportation routes. In the case of the current US–Iran escalation, risks are concentrated around key energy infrastructure and maritime chokepoints in the Middle East, particularly those linked to global oil and liquefied natural gas trade. Even in the absence of a full physical disruption, the perception of supply vulnerability can trigger a rapid repricing of energy assets as markets incorporate the possibility of prolonged instability.

Figure 2: Economic Transmission Model of War Shock



source: IPPFA

The first transmission channel operates through energy prices. Heightened geopolitical risk typically pushes crude oil and liquefied natural gas (LNG) prices higher as markets incorporate potential supply disruptions and maritime security risks. Even without an immediate physical disruption, vulnerabilities around key energy infrastructure or transport routes can trigger a rapid repricing of energy assets as markets assess the reliability of future supply. Because energy is a critical input across most sectors of the global economy, higher energy prices quickly feed into transportation, industrial production and agricultural supply chains, generating immediate cost-push inflation. Sustained increases in energy prices can therefore impose measurable macroeconomic costs, weakening growth while raising inflationary pressures, as illustrated in Table 1.

Table 1: Global Macroeconomic Impact of Sustained Oil Price Shocks

Oil Price Scenario (Brent Avg)	Global Growth Impact (ppt)	Global Inflation Impact (ppt)	Transmission Mechanism
+USD 10/bbl sustained	–0.15 to –0.20	+0.2 to +0.3	Consumption and production cost shock
USD 95–105/bbl	–0.3 to –0.6	+0.4 to +0.7	Rising input costs and policy constraints
>USD 120/bbl	–0.8 or more	+0.8 to +1.2	Stagflation risk and demand compression

source: International Energy Agency, U.S. Energy Information Administration, OPEC, IMF, Bloomberg Intelligence; author estimates.

A second transmission channel operates through financial markets. Geopolitical escalation typically triggers risk-off behaviour among investors, leading to higher equity market volatility, stronger demand for safe-haven assets such as gold and the US dollar, and repricing across bond markets. These adjustments tighten global financial conditions, raising borrowing costs and increasing uncertainty around investment decisions.

Table 2: Cross-Asset Market Reaction to Middle East Geopolitical Shocks

Date	Event	t-1 Brent (USD)	t-1 Gold (USD)	t-1 VIX	t-1 DXY	t-1 USD/MYR (RM)	Oil % (t)	Oil % (t+1)	Gold % (t)	Gold % (t+1)	VIX % (t)	VIX % (t+1)	DXY % (t)	DXY % (t+1)	USD/MYR % (t)	USD/MYR % (t+1)	Shock Type
28-Feb-26	US–Iran Tension	72.87	5278.93	19.86	97.61	3.8925	6.70%	8.90%	0.80%	1.60%	8.00%	18.70%	0.80%	1.50%	0.90%	1.40%	Type C
13-Jun-25	12-Day War	66.42	3385.92	18.02	97.92	4.222	3.40%	3.70%	1.40%	0.00%	15.50%	6.00%	0.30%	0.10%	0.60%	0.50%	Type B
26-Oct-24	Israel Strike	72.39	2747.56	20.33	104.26	4.3427	-4.40%	-4.60%	-0.200%	1.00%	-2.60%	-4.90%	0.10%	0.10%	0.50%	0.80%	Type A
7-Oct-23	Hamas Attack	72.72	1833.01	17.45	106.04	4.7142	1.80%	2.90%	1.50%	1.50%	1.40%	-2.40%	0.00%	-0.20%	0.40%	0.30%	Type A
24-Feb-22	Russia Invasion	75.44	1909.01	31.02	96.19	4.1842	-1.80%	-3.80%	-0.30%	-1.00%	-2.30%	-11.10%	1.00%	0.40%	0.50%	0.40%	Type C
30-Aug-21	Afghanistan Exit	58.88	1817.57	16.39	92.69	4.191	-0.80%	-1.30%	-0.40%	-0.20%	-1.20%	0.50%	-0.10%	-0.10%	-0.80%	-0.90%	Type A
3-Jan-20	Soleimani Strike	49.22	1529.13	12.47	96.85	4.0887	-0.70%	-0.40%	1.50%	2.40%	12.40%	11.10%	0.00%	-0.20%	0.30%	0.40%	Type A

Shock Type
Type A: <2%, Symbolic / contained / political
Type B: 2-5% Oil Reaction, Regional escalation
Type C: >5% Oil Reaction, Systemic supply or duration risk

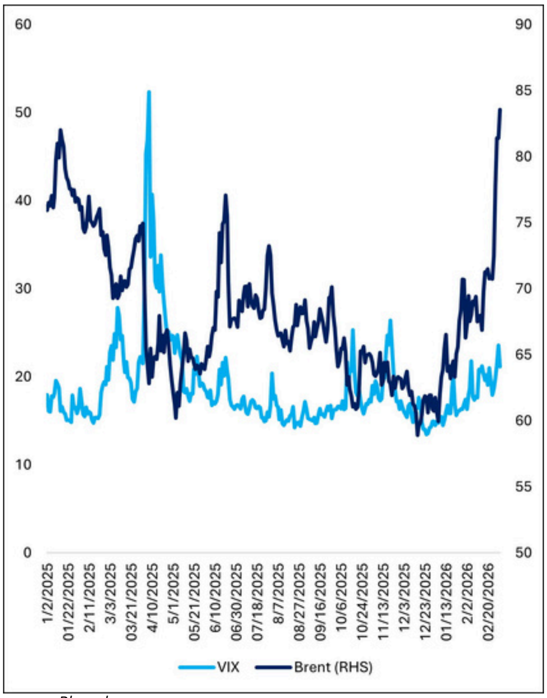
source: IPPFA, Bloomberg, news compilation

Historical evidence suggests that financial markets tend to exhibit consistent behavioural patterns during periods of geopolitical escalation. As shown in Table 2, episodes associated with heightened geopolitical tension in the Middle East are typically accompanied by rising market volatility, reflected in higher VIX levels, alongside stronger demand for safe-haven assets such as gold and the US dollar. At the same time, crude oil prices often react sharply during the initial phase of geopolitical escalation, particularly when tensions involve major energy-producing regions or critical shipping routes. This early reaction reflects the market's tendency to price immediate supply risks and uncertainty surrounding the duration of potential disruptions. In many cases, these market reactions moderate once investors reassess the likelihood of sustained supply disruption or broader regional escalation. When tensions remain contained, oil prices and market volatility typically stabilise as supply conditions prove resilient and shipping routes remain operational. The magnitude and persistence of these cross-asset movements therefore provide a useful framework for interpreting geopolitical events. Relatively limited market reactions tend to characterise contained political shocks (Type A), such as targeted military actions or diplomatic confrontations. Regional escalation events (Type B) typically involve sustained military exchanges or broader conflict dynamics that raise concerns over regional stability. By contrast, systemic supply risk events (Type C) occur when tensions threaten critical energy infrastructure or major shipping routes, creating the potential for significant disruption to global energy markets and wider macroeconomic consequences.

The third transmission channel runs through global trade and supply chains. Disruptions to shipping routes, higher insurance costs and delays in maritime logistics can raise the cost of international trade and reduce the efficiency of supply networks. In energy-intensive sectors such as manufacturing, chemicals and transportation, these disruptions can translate into higher production costs and weaker output.

These channels ultimately converge at the macroeconomic level through their effects on consumption, investment and trade balances. Higher energy prices erode household purchasing power and reduce real incomes, while rising uncertainty discourages corporate investment and capital expenditure. For energy-importing economies, deteriorating trade balances and currency pressures may further amplify inflationary pressures.

Chart 1: Brent Oil Price vs Market Volatility



source: Bloomberg

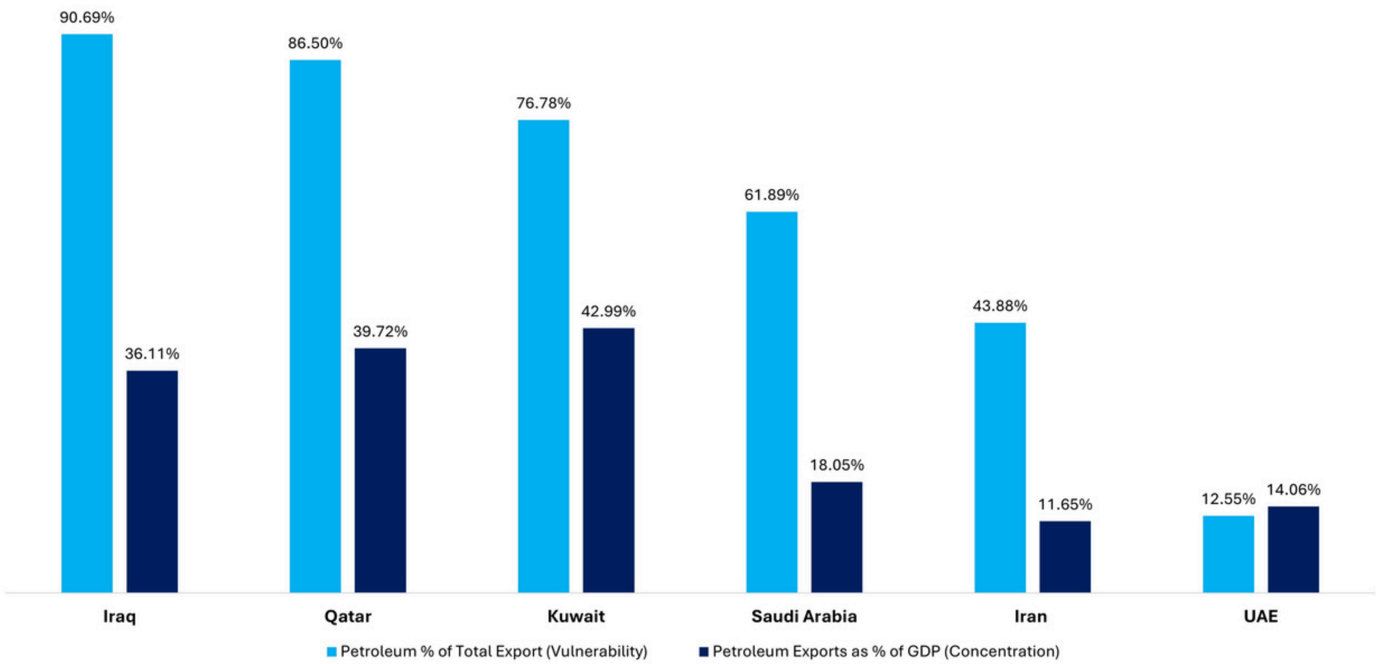
At the same time, inflation expectations become increasingly sensitive to energy market developments. If energy price shocks persist, firms may pass higher costs onto consumers, raising the risk of second-round inflation effects through wages and price-setting behaviour. This dynamic complicates the policy response for central banks, which must balance the need to contain inflation with the risk of further weakening economic activity. Taken together, the transmission from geopolitical escalation to macroeconomic stress operates through an interconnected system of energy prices, financial markets and global trade flows. As these channels interact, the initial geopolitical shock becomes embedded in expectations, asset prices and policy constraints, amplifying its macroeconomic impact.

3. Strategic Energy Infrastructure Under Escalation Risk

The economic significance of the current US–Iran escalation is closely linked to the geographic concentration of critical energy infrastructure across the Middle East. The region hosts some of the world’s largest oil production fields, refining complexes and liquefied natural gas export facilities, making it a central pillar of the global energy system. Major producers including Saudi Arabia, Iran, the United Arab Emirates, Kuwait and Qatar collectively account for a substantial share of global oil and LNG supply. Much of this production capacity is clustered around the Persian Gulf, creating a highly interconnected energy network in which disruptions in one location can quickly propagate through international energy markets. Because global supply chains depend heavily on stable energy flows from the Gulf region, geopolitical tensions occurring within this area tend to generate reactions far beyond the immediate conflict zone.

A defining feature of this system is its dependence on a limited number of maritime transport corridors. Energy exports from Gulf producers rely heavily on tanker routes that pass through narrow strategic waterways before reaching global markets. The most important of these corridors is the Strait of Hormuz, a narrow maritime passage connecting the Persian Gulf with the Arabian Sea. A substantial internationally traded crude oil and liquefied natural gas transits through this corridor each day, making it one of the most critical energy chokepoints in the world. Any disruption affecting shipping activity in this corridor therefore carries the potential to influence global energy supply conditions and price dynamics.

Figure 3: Oil Export Dependence of Major Gulf Producers



source: OPEC Annual Statistical Buletin (table 1.1), Qatar Planning & Statistics Authority (PSA) Economic Reports

Several Gulf economies exhibit a high degree of dependence on petroleum exports as a source of national income and export revenue. As illustrated in Figure 3, countries such as Iraq, Qatar and Kuwait derive a dominant share of their export earnings from oil and gas, with petroleum revenues also accounting for a significant portion of economic activity. In many of these economies, hydrocarbons also play a central role in fiscal revenues, government spending and external balances. Oil exports finance a large share of public expenditure, including infrastructure investment, social spending and sovereign wealth accumulation. This structural reliance on hydrocarbon revenues means that fluctuations in global energy demand and prices can have significant macroeconomic implications for these economies.

Beyond domestic fiscal dynamics, the concentration of petroleum production within the Gulf region also reflects its strategic position within the global energy system. Collectively, major Gulf producers account for a substantial share of global crude oil exports and maintain some of the largest proven reserves in the world. Several of these producers also operate large-scale refining complexes and LNG export facilities that supply energy to major consuming regions across Asia and Europe. As a result, production capacity in the Gulf functions as a critical stabilising component of the global oil market, particularly during periods of supply disruption elsewhere. In our view, this concentration reinforces the systemic importance of energy infrastructure located within the region, as disruptions affecting production facilities or export terminals could quickly influence global supply conditions.

The implications extend beyond the producing economies themselves. Because global energy markets rely heavily on stable supply from Gulf exporters, geopolitical tensions affecting the region can rapidly influence expectations regarding the availability and reliability of future energy shipments. When geopolitical risks increase, energy traders and financial markets begin to price in the possibility of production disruptions, transport bottlenecks or restrictions on shipping activity. As a result, geopolitical escalation that threatens energy infrastructure, production facilities or maritime shipping routes can quickly alter expectations regarding global energy supply.

The Strait of Hormuz represents one of the world's most critical energy transit corridors, with major oil production facilities, export terminals and military installations concentrated within a narrow geographic area. As illustrated in Figure 4, the strait lies at the intersection of major oil production hubs, export terminals and naval installations across the Gulf region. Several large-scale energy production hubs, export terminals and refining complexes operate in close proximity to this corridor, while military bases belonging to regional powers and external actors are positioned along the surrounding coastlines. The geographic concentration of both energy infrastructure and military assets around the Strait of Hormuz further amplifies these risks. Oil production hubs, export terminals and refining complexes are located within relatively short distances of key shipping lanes, meaning that disruptions affecting either production infrastructure or maritime transport routes could have immediate implications for global energy markets. In addition, the presence of military installations across multiple coastal states increases the probability that geopolitical tensions could intersect directly with the physical foundations of global energy supply.

Figure 4: US–Iran Escalation and Strategic Energy Infrastructure in the Strait of Hormuz

source: visual generate by Gen-AI

Markets therefore respond not only to the possibility of physical disruptions but also to uncertainty surrounding the continuity and reliability of future deliveries. Even when actual supply flows remain intact, heightened geopolitical risk can encourage precautionary behaviour among traders, refiners and shipping companies. These responses may include increased inventory accumulation, adjustments to tanker routing or higher insurance premiums for vessels operating in the region. In periods of heightened geopolitical tension, even the perceived risk of disruption can therefore lead traders to incorporate a structural geopolitical risk premium into global energy prices.

Even in the absence of a full closure of the strait, geopolitical tensions can influence energy markets through several indirect mechanisms. Shipping companies may delay tanker movements, reroute vessels or reduce traffic through the corridor in response to heightened security risks. War-risk insurance premiums for vessels operating in the region can also rise sharply during periods of conflict, increasing transportation costs for energy shipments. These logistical disruptions effectively tighten global supply conditions by slowing the movement of oil and LNG exports and increasing uncertainty surrounding delivery schedules.

Table 3: Strategic Energy Infrastructure Under Escalation Risk

Country / Scenario	Facility	Type	Approx. Capacity	Estimated Capacity at Risk (per day)	Major Client Countries	Strategic Notes
Saudi Arabia	Ras Tanura Refinery & Export Terminal	Refinery + Export Terminal	Refining ~550,000 bpd; Export ~6–7 mbpd	Up to ~6 mbpd export flows exposed	China, Japan, South Korea, India, US	Largest Saudi crude export hub affecting Asian supply.
Qatar	Ras Laffan Industrial City	LNG production	~77 mtpa LNG	~10–15 mtpa LNG disruption risk	Japan, South Korea, China, India, EU	Supplies roughly 20% of global LNG trade.
Kuwait	Mina Al Ahmadi Refinery	Refinery	~346,000 bpd	Refined product disruption risk (~0.35 mbpd)	China, South Korea, Japan, India	Major export refinery serving Asian markets.
UAE	Mussafah / Ruwais Refining System	Refining & storage	~922,000 bpd	Refined product disruption risk (~0.9 mbpd)	Japan, South Korea, India, China	Key Gulf refining hub supporting regional supply.
UAE	Fujairah Oil Industry Zone	Storage & export hub	~70–75 million barrels storage	Shipping and storage disruption risk	Asia, global shipping	Strategic oil storage hub outside Strait of Hormuz.
Iran	Kharg Island Export Terminal	Crude export terminal	~5–7 mbpd loading capacity	~1.5–2 mbpd export flows exposed	China (dominant buyer)	Iran's primary crude export outlet.
Israel	Leviathan Gas Field	Offshore gas field	~12 bcm/year (~1.1 bcf/day)	~1.1 bcf/day gas supply risk	Egypt, Jordan	Major Eastern Mediterranean gas supply node.
Israel	Tamar Gas Field	Offshore gas field	~10 bcm/year (~0.9 bcf/day)	~0.9 bcf/day gas supply risk	Israel, Egypt	Critical for Israel's domestic electricity supply.
Oman	Port of Duqm Energy Hub	Refinery & export hub	~230,000 bpd refinery	Refined product disruption risk (~0.23 mbpd)	Asia, global shipping	Alternative export hub bypassing Hormuz chokepoint.
Iraq (Kurdistan)	Khor Mor Gas Field	Onshore gas field	~700–750 mmscfd (~0.7 bcf/day)	~0.7 bcf/day gas exposure	Domestic Iraq	Largest gas field supporting Kurdistan power supply.
TOTAL ESTIMATED EXPOSURE	Oil Export Flows: ~7.5 – 8 mbpd potentially exposed LNG Supply: ~10 – 15 mtpa disruption risk Regional Gas Supply: ~2.5 bcf/day potential disruption					Reflects systemic energy supply risk under escalation.

source: IPPFA, corporate website, news compilation

Table 3 highlights the structural concentration of critical energy infrastructure across the Gulf region and the systemic risks arising from this geographic clustering. Many of the facilities listed function as primary export gateways for global energy markets. Saudi Arabia's Ras Tanura terminal represents the kingdom's largest crude export hub, while Qatar's Ras Laffan Industrial City is the world's largest LNG export complex and accounts for a significant share of global LNG supply. Iran's Kharg Island terminal similarly serves as the primary outlet for the country's crude exports. The presence of these large-scale facilities within close proximity to the Strait of Hormuz underscores the strategic importance of the region as a central node in the global energy system.

A key feature revealed by the table is the degree to which global energy flows are concentrated in a relatively small number of export facilities and transport corridors. Several of the sites listed handle multi-million-barrel-per-day export volumes or large-scale LNG shipments, implying that even partial operational disruptions could generate disproportionate market reactions. Unlike more diversified supply networks where disruptions can be absorbed through alternative routes or facilities, the Gulf energy system relies heavily on a limited number of large export hubs located near a single maritime chokepoint. In our view, this structural concentration significantly increases the sensitivity of global energy markets to geopolitical developments in the region, as supply expectations can shift rapidly when tensions escalate.

The estimated exposure figures presented in the table further illustrate the potential scale of disruption under a severe escalation scenario. In aggregate, the infrastructure listed suggests that approximately 7.5 to 8 million barrels per day of oil export flows and around 10 to 15 million tonnes of LNG supply could face disruption risks. Given that many of these exports are directed toward major Asian importers such as China, Japan, South Korea and India, disruptions affecting these facilities could quickly tighten regional energy supply conditions and contribute to upward pressure on global energy prices.

Table 4: Summary of Daily Impact (Estimate)

Category	Daily Volume/Cost	Economic Impact
Hormuz Energy Transit	~20 mbpd crude oil (~USD1.6–1.7bn/day at USD80 to 82 Brent)	One of the world's most critical global energy supply arteries
Oil Price Risk Premium	Potential USD5 to 10/bbl increase	~USD0.5 to 1.0bn/day additional global crude expenditure
Shipping & Insurance Costs	War-risk premiums may rise 50 to 100% (Marsh estimate)	Higher freight costs and slower tanker movements
LNG Trade Exposure	~20% of global LNG shipments transit the corridor	Tightening LNG supply risk for Asia and Europe

source: IPPFA, Energy Information Administration (EIA), International Energy Agency (IEA), Bloomberg, industry insurance estimates; author calculations.

Building on the infrastructure exposure highlighted in Table 3, the summary estimates in Table 4 illustrate the broader economic significance of the Strait of Hormuz within the global energy system. At prevailing Brent prices of around USD80 to USD82 per barrel, we estimate that roughly 20 million barrels per day of crude oil transit through the corridor, representing one of the largest energy supply arteries in the world. At this price range, the value of oil shipments moving through the strait amounts to approximately USD1.6 to USD1.7 billion in daily trade flows, highlighting the scale of economic activity dependent on uninterrupted maritime transit through this corridor.

Even relatively moderate increases in oil prices resulting from geopolitical risk, such as a USD5 to USD10 per barrel risk premium, could translate into an additional USD0.5 to USD1.0 billion in daily global energy expenditure. At the same time, higher war-risk insurance premiums and shipping disruptions could significantly increase freight costs and delay tanker movements across the region. The corridor also plays a critical role in global LNG markets, with roughly 20 percent of global LNG shipments passing through the strait, implying that disruptions to maritime traffic could quickly tighten supply conditions in both Asian and European energy markets. Taken together, the concentration of strategic energy infrastructure, shipping routes and export facilities around the Strait of Hormuz means that geopolitical escalation in the region carries significant systemic implications for global energy markets. In our view, developments affecting shipping activity and infrastructure security in the strait will be a key determinant of whether the current US–Iran tensions remain a temporary geopolitical disturbance or evolve into a broader disruption to global energy supply.

4. Global Macroeconomic Exposure to Middle East Energy Supply Disruptions

The potential disruption of energy flows through the Strait of Hormuz carries significant implications for the global economy due to the scale of oil and gas exports that transit the corridor. A substantial share of internationally traded crude oil originates from Gulf producers whose exports rely heavily on this maritime route. As a result, the stability of shipping activity through the strait plays a critical role in maintaining global energy supply balances. When geopolitical tensions increase the perceived risk of disruption in this corridor, energy markets typically respond through higher prices, increased volatility and precautionary inventory adjustments. In such an environment, even the expectation of supply uncertainty can influence global energy prices and financial market sentiment.

In our examination of global energy trade patterns, we find that exposure to potential supply disruptions is particularly pronounced in Asia. Several of the world's largest energy-importing economies — including Japan, South Korea, India and China — depend heavily on crude oil shipments originating from Gulf producers. Because a large share of these imports transits through the Strait of Hormuz, disruptions to shipping routes could quickly tighten regional energy supply conditions. Higher energy costs would transmit rapidly through transportation, industrial production and food supply chains, reinforcing cost-push inflation pressures across the region. This structural dependence means that geopolitical escalation in the Gulf region has the potential to generate immediate macroeconomic spillovers across major Asian economies.

Table 5: Macroeconomic Exposure to Middle East Energy Supply Disruption (Scenario Simulation)

Economy	Oil Import Dependence on Middle East	GDP Growth Baseline (%)	GDP After Shock (%)	Inflation Baseline (%)	Inflation After Shock (%)	Current Account Baseline (% GDP)	Current Account After Shock (% GDP)
Japan	~90%	0.6	0.3	2.1	2.7	3.6	2.9
South Korea	~70%	1.8	1.5	1.8	2.3	3.9	3.3
India	~60%	6.2	5.9	4.0	4.5	-1.4	-1.9
China	~45–50%	4.2	4.0	0.7	1.0	2.8	2.4
European Union	LNG exposure	1.6	1.4	4.6	5.0	1.9	1.5

source: IPPFA, IEA oil trade statistics; Reuters energy market analysis; author estimates.

To assess the potential macroeconomic implications of an energy supply disruption, we combine baseline macroeconomic forecasts for 2026 with a stylised oil price shock scenario associated with heightened geopolitical risk in the Gulf region. In our estimate, a sustained increase in oil prices resulting from supply uncertainty would generate a modest but noticeable deterioration in growth outcomes across major energy-importing economies while simultaneously raising inflationary pressures. Economies with the highest dependence on Middle Eastern crude imports experience the most visible adjustment in macroeconomic indicators. Japan and South Korea, for instance, exhibit a measurable slowdown in growth alongside higher inflation, reflecting their strong reliance on imported energy and the sensitivity of industrial production to fuel costs.

India and China also experience inflationary pressures under the simulated scenario, although the growth impact appears somewhat more contained. In our view, this reflects the relatively larger role of domestic demand and the greater diversification of energy supply sources in these economies. Nevertheless, higher oil prices would still feed into transportation costs, electricity generation and manufacturing supply chains, gradually affecting broader price dynamics. For large emerging economies such as India and China, sustained increases in energy prices could also complicate macroeconomic policy management by forcing policymakers to balance inflation control against the need to maintain growth momentum.

Europe faces a somewhat different but still meaningful exposure through the global liquefied natural gas market. In recent years LNG has become an increasingly important component of Europe's energy supply following the sharp reduction in pipeline gas imports from Russia. A significant share of LNG exports from Qatar and other Gulf producers must transit through the Strait of Hormuz before reaching global markets. As a result, disruptions affecting maritime shipping routes in the Gulf region could tighten global LNG supply conditions and contribute to higher gas prices across Europe, particularly during periods of elevated seasonal demand.

Taken together, the potential macroeconomic impact of an energy supply disruption can be understood through several reinforcing transmission channels. First, higher crude oil and LNG prices directly raise production and transportation costs, generating cost-push inflation across energy-importing economies. Second, higher energy prices weaken household purchasing power and increase operating costs for energy-intensive industries, thereby weighing on economic growth. Third, heightened geopolitical uncertainty can trigger financial market volatility, tightening global financial conditions and discouraging investment. In combination, these channels illustrate how geopolitical shocks originating in energy markets can quickly propagate through the broader global economy.

Beyond regional energy exposure, disruptions to Gulf energy supply would carry broader macroeconomic implications through global commodity markets. Higher oil prices would feed directly into transportation costs, industrial production and agricultural supply chains, reinforcing inflationary pressures across both advanced and emerging economies. At a time when many economies continue to navigate elevated debt levels and restrictive monetary conditions, sustained increases in energy prices could complicate the policy trade-offs faced by central banks. Higher inflation expectations could delay monetary easing cycles, while weaker growth prospects may simultaneously constrain fiscal policy responses.

In our view, the key risk associated with the current US–Iran escalation lies not only in the possibility of a direct supply disruption but also in the persistence of geopolitical uncertainty surrounding the Strait of Hormuz. Even without a complete interruption of shipping activity, heightened tensions can encourage markets to incorporate a structural geopolitical risk premium into energy prices. Such dynamics can generate spillovers across financial markets, inflation expectations and global growth prospects, reinforcing the broader macroeconomic consequences of geopolitical shocks within an already fragile global economic environment.

5. Malaysia: Macroeconomic Implications of the Energy Shock

The escalation of geopolitical tensions in the Middle East has renewed concerns regarding the stability of global energy markets, particularly given the strategic importance of the Strait of Hormuz in global crude oil and LNG trade. For Malaysia, the macroeconomic implications of such developments arise primarily through movements in global energy prices rather than through direct trade exposure to the region. While Malaysia remains a modest exporter of crude oil and natural gas, the domestic economy is still sensitive to fluctuations in global energy prices because petroleum products play a central role in transportation, logistics and production costs across multiple sectors.

In the early phase of an energy price shock, the transmission to the Malaysian economy typically occurs through transportation and logistics costs. Higher global oil prices increase fuel expenses for freight, aviation and land transportation, which subsequently raise the cost of distributing goods across domestic supply chains. These pressures tend to emerge relatively quickly in logistics-intensive sectors such as food distribution, retail supply networks and manufacturing inputs. Consequently, the first signs of inflationary pressure during geopolitical energy shocks often appear in transportation services and food prices before gradually spreading across the broader consumer price basket.

The duration of geopolitical tensions is a key determinant of whether the economic impact remains limited or becomes more widespread. If the conflict remains short-lived, the shock may largely be confined to temporary volatility in commodity markets and financial conditions. However, if tensions persist for an extended period, the transmission mechanism can evolve through multiple stages within the domestic economy. As illustrated in table 6, the initial phase of the shock is characterised by higher global energy prices and market uncertainty. Over time, these pressures propagate through transportation costs, supply chain disruptions and imported input prices, eventually influencing broader macroeconomic conditions.

Table 6: Malaysia Impact Transmission Framework

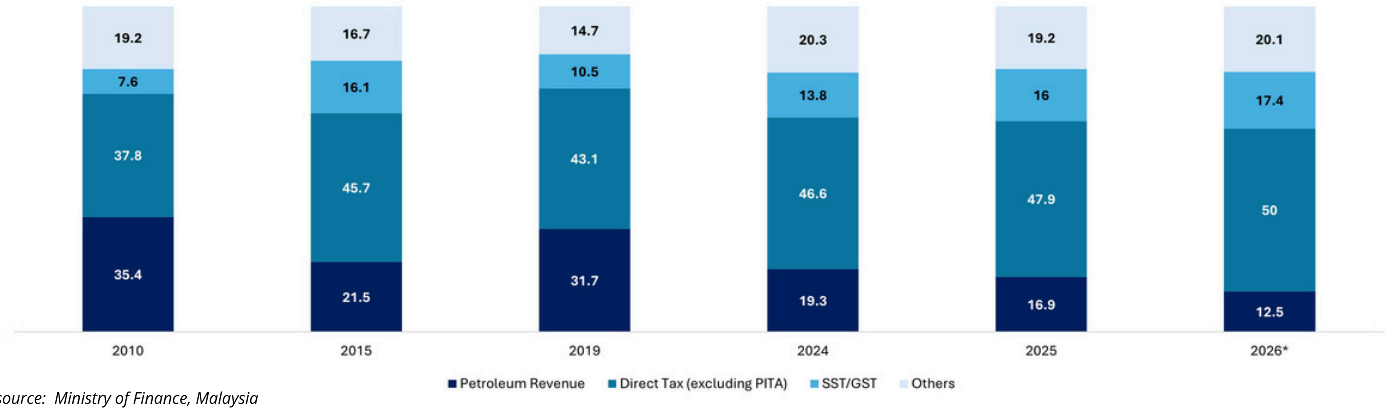
Impact Round	Conflict Duration Assumption	Primary Channel	Transmission Mechanism	Activation Window	Malaysia Outcome
1st Round	1–14 days (headline shock)	Energy & Market Sentiment	Brent spike; LNG risk premium; global risk-off	0–3 months	Direct CPI impact softened as RON95/diesel prices remain fixed; inflation expectations rise; defensive sector rotation; ringgit volatility contained but sensitive
2nd Round	2–4 weeks (persistent risk premium)	Cost Pass-Through	Higher freight, insurance, industrial diesel & logistics costs	3–6 months	CPI gradually rises via food, transport & imported inputs; corporate margin compression; subsidy does not fully shield supply chain
3rd Round	4–8 weeks (elevated oil sustained)	Fiscal Subsidy Stress	Subsidy bill rises sharply if pump price fixed at RM1.99	6–9 months	Fiscal space narrows; deficit sensitivity increases; crowding-out risk; inflation delayed but fiscal vulnerability rises
4th Round	1–3 months (FX repricing phase)	FX & Imported Inflation	Ringgit adjusts to duration risk; import costs rise	9–12 months	Imported inflation amplified; tighter financial conditions; higher subsidy burden if ringgit weakens; BNM policy flexibility constrained
5th Round	>3 months (structural shock)	Growth & Financial Conditions	Aggregate demand softens; tighter credit; weaker real income	12–18 months	Slower consumption; softer GDP growth; delayed easing cycle; risk of policy trade-off between inflation and growth

source: IPPFA

The framework highlights how external energy shocks can gradually propagate across different sectors of the Malaysian economy. In the first stage, global oil prices respond to geopolitical risk premiums as markets price in potential supply disruptions. If elevated prices persist, higher transportation and logistics costs begin to affect production and distribution costs across multiple industries. Over time, these pressures can feed into consumer prices, fiscal balances and financial conditions. In our view, the duration of geopolitical tensions therefore represents the critical variable determining whether the shock remains largely contained within commodity markets or evolves into broader macroeconomic stress. Beyond the inflation channel, movements in global oil prices also influence Malaysia's fiscal position through petroleum-related government revenue. Historically, petroleum income represented a major source of federal government revenue, particularly during periods of elevated oil prices. However, Malaysia's fiscal structure has evolved significantly over the past decade as the government diversified its revenue base toward non-petroleum sources.

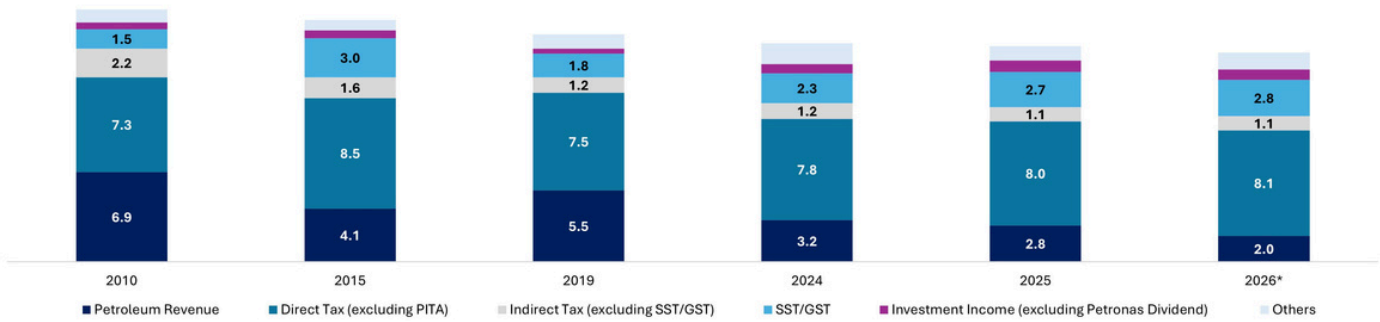
As illustrated in Figure 5, petroleum-related revenue once accounted for a dominant share of total government income during the early 2010s when global oil prices were significantly higher. Over time, however, the contribution of petroleum revenue has moderated as non-petroleum taxes expanded. Direct taxes, consumption-based taxes and other non-petroleum revenue streams now represent a larger share of federal income, reflecting structural diversification within Malaysia's fiscal framework.

Figure 5: Petroleum-Related and Non-Petroleum Revenue (% of total revenue)



source: Ministry of Finance, Malaysia
note: 2026 Budget estimates

Figure 6: Federal Government Revenue (% of GDP)



source: Ministry of Finance, Malaysia
note: 2026 budget estimates

This shift in revenue composition carries important macroeconomic implications for the stability of Malaysia's fiscal framework. In earlier periods, when petroleum income accounted for a larger share of government revenue, fiscal outcomes were closely tied to developments in global energy markets. Sharp movements in crude oil prices could translate directly into significant fluctuations in government income, creating greater volatility in fiscal balances and increasing the sensitivity of public finances to external commodity cycles. As global oil prices rose, petroleum-related revenue could expand rapidly, while periods of lower oil prices often resulted in sizeable declines in fiscal income. Over time, however, the increasing role of non-petroleum taxes has gradually reduced this dependence. The expansion of direct taxation, together with the contribution from consumption-based taxes such as the Sales and Services Tax (SST), has broadened the government's revenue base and strengthened fiscal resilience. As a result, government finances today are less directly exposed to energy price fluctuations than in earlier decades. This structural diversification implies that movements in oil prices no longer translate into large swings in fiscal revenue to the same extent as before.

Consequently, the macroeconomic transmission of oil price shocks to Malaysia's economy has also evolved. Rather than primarily affecting fiscal income, energy price shocks now tend to influence the economy through other channels, particularly through inflation dynamics and government expenditure. Higher oil prices increase transportation and logistics costs across domestic supply chains, which can feed into consumer prices through higher food and goods distribution costs. At the same time, the government's fuel stabilisation mechanisms may require higher subsidy expenditure when global oil prices rise, partially offsetting the additional revenue generated from petroleum-related income. A similar structural shift is evident when revenue is examined relative to the size of the economy. As shown in Figure 6, petroleum-related revenue as a share of GDP has gradually declined over time, even though overall government revenue remains broadly stable relative to economic output. In earlier periods of elevated oil prices, petroleum income represented a substantial component of fiscal resources relative to GDP, reflecting both high global energy prices and the importance of the hydrocarbon sector in Malaysia's economy. However, the chart indicates that the macroeconomic importance of petroleum revenue has diminished as Malaysia's economic structure diversified and non-energy sectors expanded. This evolution suggests that while energy prices remain an important macroeconomic variable, Malaysia's fiscal position today is better insulated from commodity price volatility than in previous decades.

Further detail on Malaysia's fiscal structure is provided in Table 7, which presents the composition of federal government revenue for the 2024–2026 period. The table shows that Petroleum Income Tax (PITA) remains a distinct component within the direct tax category, while other petroleum-related income streams appear within non-tax revenue. Although petroleum-related income continues to contribute meaningfully to government finances, its relative importance has declined compared with earlier years as other revenue sources expanded.

Table 7: Federal Government Revenue Composition (2024–2026)

Component	RM Million			Change (%)			Share (%)		
	2024	2025	2026*	2024	2025	2026*	2024	2025	2026*
Tax revenue	240,192	253,400	270,383	4.8	5.5	6.7	74	75.8	78.8
Direct tax	171,693	177,145	187,357	0.2	3.2	5.8	52.9	53	54.6
of which:									
CITA	92,776	97,033	103,353	1.1	4.6	6.5	28.6	29	30.1
Individuals	41,099	44,859	49,069	8.8	9.1	9.4	12.7	13.4	14.3
PITA	**20,528**	**16,906**	**15,698**	**-21.3**	**-17.6**	**-7.1**	**6.3**	**5.1**	**4.6**
Indirect tax	68,499	76,255	83,026	18.4	11.3	8.9	21.1	22.8	24.2
of which:									
SST	44,758	53,424	59,627	26.2	19.4	11.6	13.8	16	17.4
Excise duties	13,383	12,508	12,791	1.8	-6.5	2.3	4.1	3.7	3.7
Import duty	3,072	3,077	3,081	1.2	0.2	0.1	1	0.9	0.9
Export duty	2,092	1,920	1,913	2.6	-8.3	-0.3	0.6	0.6	0.6
Non-tax revenue	84,426	80,715	72,741	-1.6	-4.4	-9.9	26	24.2	21.2
Licences and permits	17,041	15,879	15,726	1.8	-6.8	-1	5.2	4.8	4.6
Investment income	45,782	50,374	36,676	-18	10	-27.2	14.1	15.1	10.7
Total revenue	324,618	334,115	343,124	3.1	2.9	2.7	100	100	100

source: Ministry of Finance, Malaysia
note: 2026 Budget estimates

The diversification of fiscal revenue sources plays an important stabilising role during periods of energy price volatility. Direct taxation and indirect taxes such as the Sales and Services Tax (SST) now form the backbone of government revenue, reducing fiscal sensitivity to fluctuations in global oil prices. Nevertheless, higher oil prices can still increase government expenditure through domestic fuel stabilisation mechanisms designed to shield households and businesses from global price volatility. As a result, the net fiscal impact of rising oil prices depends on the balance between additional petroleum-related revenue and higher subsidy expenditure.

To evaluate the potential macroeconomic implications of sustained increases in oil prices, we conduct a scenario analysis linking Brent crude price assumptions, exchange rate conditions and domestic fuel subsidy dynamics. The framework draws on historical relationships between energy prices, transportation costs and consumer price inflation, as well as Malaysia's fiscal exposure to fuel stabilisation measures.

Table 8: Malaysia Oil Shock Transmission Matrix

(Assuming RON95 maintained at RM1.99)

Brent (USD)	USD/MYR	Additional Subsidy (RM bn)	CPI Impact (ppt)	GDP Growth Adjustment (ppt)	Fiscal Sensitivity	Policy Implication
80	3.90	5–6	+0.1–0.2	–0.1	Manageable	Neutral policy stance
80	4.05	6–7	+0.2–0.3	–0.2	Mild pressure	Monitor FX pass-through
90	3.90	8–10	+0.4–0.6	–0.3	Subsidy rising	Inflation manageable
90	4.05	10–12	+0.6–0.8	–0.4	Fiscal sensitivity increases	Policy trade-off emerges
100	3.90	13–15	+0.8–1.0	–0.5	Fiscal space tightens	Limited easing space
100	4.05	16–18	+1.0–1.3	–0.6 to –0.8	Material fiscal stress	Tight macro constraints

source: IPPFA

The scenario matrix illustrates that the macroeconomic impact remains relatively manageable when Brent crude prices remain around USD80 per barrel. Under such conditions, inflationary pressures are contained and fiscal subsidy costs remain broadly consistent with existing policy assumptions. However, the economic impact becomes more pronounced as oil prices move toward the USD90–100 range. In this environment, higher transportation costs and imported input prices begin to propagate through domestic supply chains, increasing production costs and generating broader cost-push inflation pressures. At the same time, maintaining domestic fuel price stabilisation mechanisms significantly increases fiscal expenditure as global energy prices rise. Under the current policy framework, RON95 prices are capped at RM1.99, which effectively shields consumers from global price volatility but transfers part of the cost burden to government finances. As oil prices approach USD90 per barrel, the fiscal cost associated with maintaining this price ceiling increases materially, particularly if elevated prices persist for several months.

Another potential transmission channel relates to international tourism flows. However, aviation data indicates that connectivity between the Middle East and Malaysia represents only a modest share of total international arrivals. Flights from the Middle East account for approximately 43,000 weekly seats out of more than 645,000 international seats arriving in Malaysia. This suggests that while geopolitical tensions may affect travel sentiment in the region, Malaysia's tourism sector remains primarily supported by intra-Asian travel demand.

Table 9: Total International Flights and Seat Capacity 2024/2023 (Flight to Malaysia)

Destination Region	Malaysia				Growth	
	2024		2023			
	Frequency/Week	Seats/Week	Frequency/Week	Seats/Week	% Frequency/Week	% Seats/Week
South East Asia	1,760	316,473	1,697	303,871	3.7	4.1
North East Asia	774	168,004	537	120,665	44.1	39.2
South Asia	347	65,327	312	58,693	11.2	11.3
Central Asia	11	2,736	4	941	175	190.8
Middle East	**136**	**43,216**	**141**	**46,095**	**-3.5**	**-6.2**
Europe	34	10,400	33	10,145	3	2.5
Africa	11	3,166	6	1,760	83.3	79.9
North America						
Southwest Pacific	136	36,172	149	39,899	-8.7	-9.3
Grand Total	**3,209**	**645,494**	**2,879**	**582,069**	**11.5**	**10.9**

source: Tourism Malaysia

While tourism represents one potential transmission channel, Malaysia's broader external exposure to the Middle East also warrants examination. In particular, bilateral trade linkages provide another indicator of the extent to which geopolitical developments in the region may directly influence Malaysia's external sector.

Beyond tourism flows, Malaysia's direct trade exposure to the Middle East also remains relatively limited compared with its broader global trade relationships. While several Gulf economies are important energy producers and play a significant role in global commodity markets, Malaysia's merchandise trade with the region represents only a relatively small portion of its total external trade. As shown in Table 10, Malaysia's exports to selected Middle Eastern economies remain modest when compared with the country's overall export base, which exceeds RM1.5 trillion annually. Trade flows are primarily concentrated in a small number of markets, particularly the United Arab Emirates and Saudi Arabia, which serve as regional commercial and logistics hubs for the broader Gulf region.

Table 10: Malaysia's Trade Exposure to Selected Middle Eastern Economies (RM million and % share of total trade)

Country	2024				2025			
	Exports (RM million)	Export Share (%)	Imports (RM million)	Import Share (%)	Exports (RM million)	Export Share (%)	Imports (RM million)	Import Share (%)
Iran	2,443	0.16%	159	0.01%	2,174	0.14%	279	0.02%
Iraq	1,447	0.10%	1,029	0.08%	1,019	0.06%	2,361	0.16%
Oman	1,600	0.11%	3,004	0.22%	1,265	0.08%	7,276	0.50%
Qatar	1,095	0.07%	5,166	0.38%	1,009	0.06%	2,357	0.16%
Saudi Arabia	7,457	0.49%	37,280	2.72%	5,405	0.34%	26,511	1.82%
United Arab Emirates	14,563	0.96%	27,662	2.02%	16,533	1.03%	25,830	1.78%
Total (Selected Middle East)	**28,605**	**1.90%**	**74,300**	**5.42%**	**27,405**	**1.71%**	**64,614**	**4.44%**
Total Malaysia External Trade	**1,509,291**	**100.00%**	**1,370,237**	**100.00%**	**1,606,650**	**100.00%**	**1,454,847**	**100.00%**

source: Department of Statistics Malaysia

The data suggest that Malaysia's economic linkages with the Middle East through merchandise trade remain relatively contained. As shown in Table 10, exports to the selected Middle Eastern economies accounted for approximately 1.7% of Malaysia's total exports in 2025, while imports represented around 4.4% of total imports. Although trade with markets such as the United Arab Emirates and Saudi Arabia forms the largest component of Malaysia's economic engagement with the region, their combined value remains relatively small compared with Malaysia's overall external trade, which exceeds RM1.6 trillion annually. This relatively limited trade exposure implies that the current geopolitical tensions in the Middle East are unlikely to generate significant direct disruptions to Malaysia's trade flows. Unlike economies that rely heavily on energy imports from the region, Malaysia's external trade structure is diversified across multiple markets, particularly within Asia and regional manufacturing supply chains. As a result, while bilateral trade with Gulf economies remains economically meaningful for specific sectors, the broader Malaysian economy is unlikely to experience a substantial contraction in external trade as a direct consequence of the conflict.

Consequently, the principal transmission channel through which geopolitical tensions in the Middle East may affect Malaysia's economy is more likely to operate through global energy price movements rather than direct trade exposure. Rising oil prices can influence domestic inflation dynamics, transportation costs and fiscal balances through higher logistics expenses and subsidy expenditure, even if Malaysia's direct trade relationships with the region remain relatively limited. Taking these dynamics into account, we maintain our Malaysia GDP growth forecast at 4.6% for 2026, assuming Brent crude prices average around USD90 per barrel while the exchange rate remains broadly below RM4.00 per US dollar. Our current projection represents a modest upward revision from the 4.5% growth forecast published in February, prior to the escalation in US–Iran tensions. The revision reflects stronger-than-expected domestic demand conditions, resilient private consumption and continued investment activity across several key sectors during the early part of the year.

Consistent with this baseline scenario, we expect Bank Negara Malaysia to maintain the Overnight Policy Rate at 2.75% throughout 2026 in order to support domestic economic momentum while ensuring inflation remains contained. Current price pressures remain largely supply-driven rather than demand-driven, suggesting that monetary policy can remain broadly accommodative while policymakers monitor developments in global energy markets. Nevertheless, the persistence of geopolitical tensions remains an important downside risk to the outlook. If the escalation extends beyond three months, the macroeconomic transmission could move beyond the initial energy price shock toward broader cost pass-through effects involving logistics costs, imported inputs and fiscal subsidy pressures. Under such a scenario, Malaysia's GDP growth could decline by approximately 0.3 to 0.4 percentage points, reflecting weaker household purchasing power, tighter financial conditions and rising fiscal constraints.

In our assessment, the principal macroeconomic risk associated with the current geopolitical episode lies less in the initial increase in oil prices and more in the duration of elevated energy prices. Short-term spikes in crude prices typically generate only temporary inflation volatility. However, if elevated prices persist for several months, the transmission effects can become more entrenched through logistics costs, imported input prices and fiscal subsidy pressures. Under such circumstances, the policy trade-off between inflation containment and growth support may become more pronounced, particularly if subsidy expenditure increases while household purchasing power weakens.

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