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War and the Oil Price Cycle

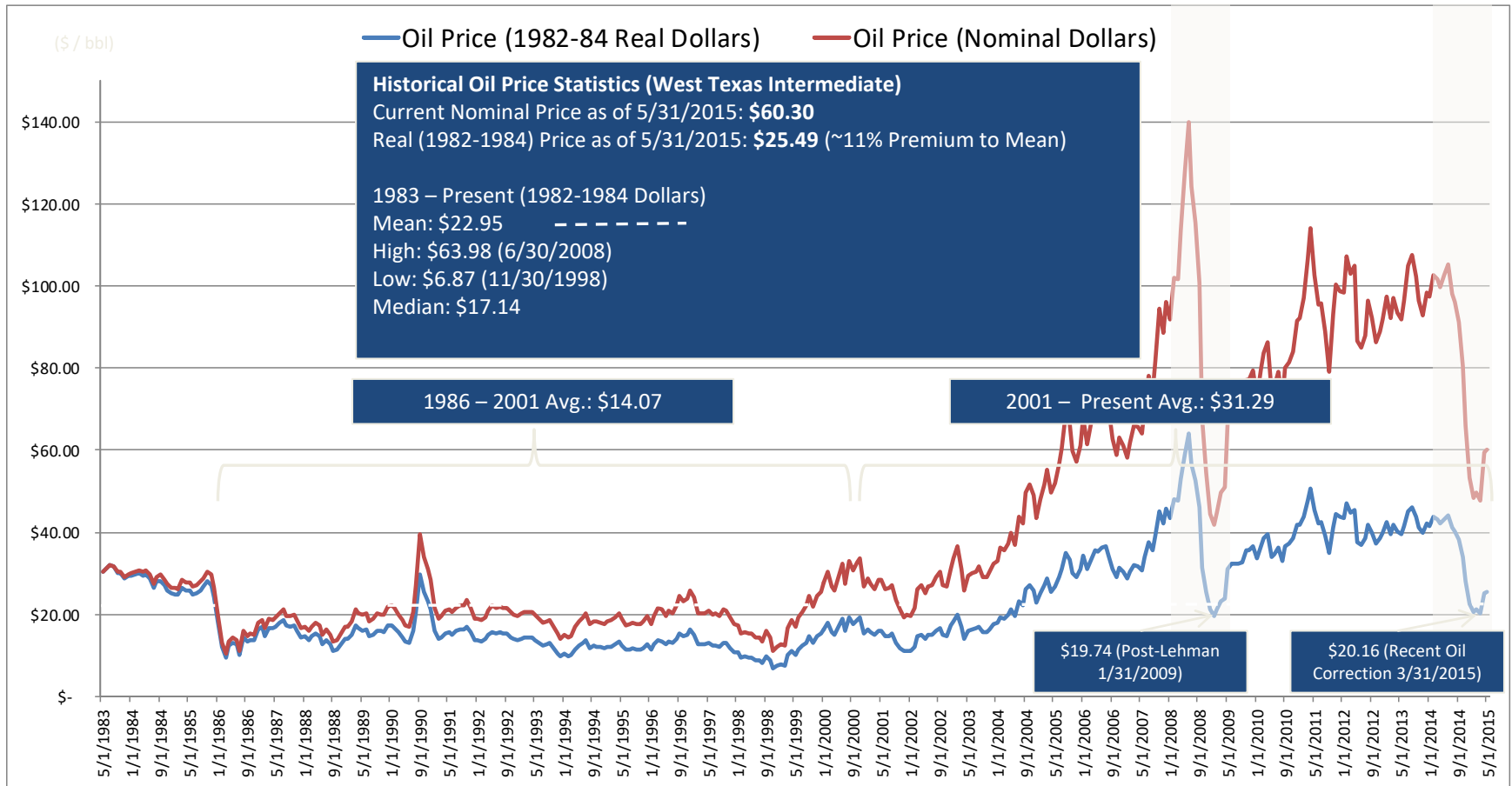
Oil Law of Averages Rule: Future will be like the past

- **Conflict or regime implosion will create a major supply disruption. Saudi-Iranian proxy war is escalating.**
- **Oil prices are cyclical and down cycles don't last**
- **Economic recovery is re-stimulating commodities super cycle**

In historical terms, 2000s looked anomalous

Monthly Nominal and Real Oil Prices from May 1983 - 2015

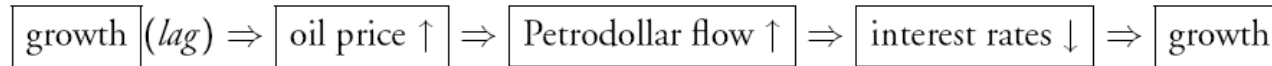
- China super cycle not likely to return to the same extent
- Depletion/Peak oil theory discredited



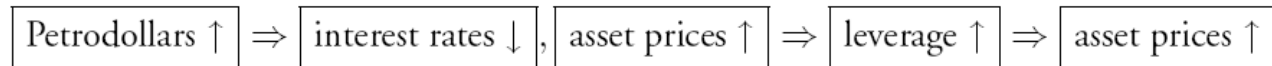
Source: Bloomberg, West Texas Intermediate (WTI) Cushing Crude Oil Spot Price: USCRWTIC Index, CPURNSA Index as of May 31, 2015

Cyclical Petrodollar Recycling and Financial Crises

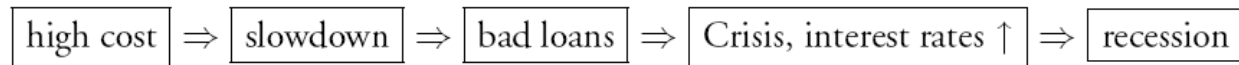
- Feedback mechanism during booms



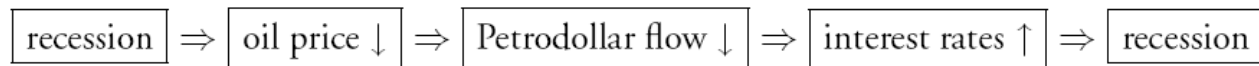
- Hubris (*80's: countries don't go bankrupt; 00's: house prices don't fall!*)



- Eventually (*Minsky moment; Ponzi finance*)

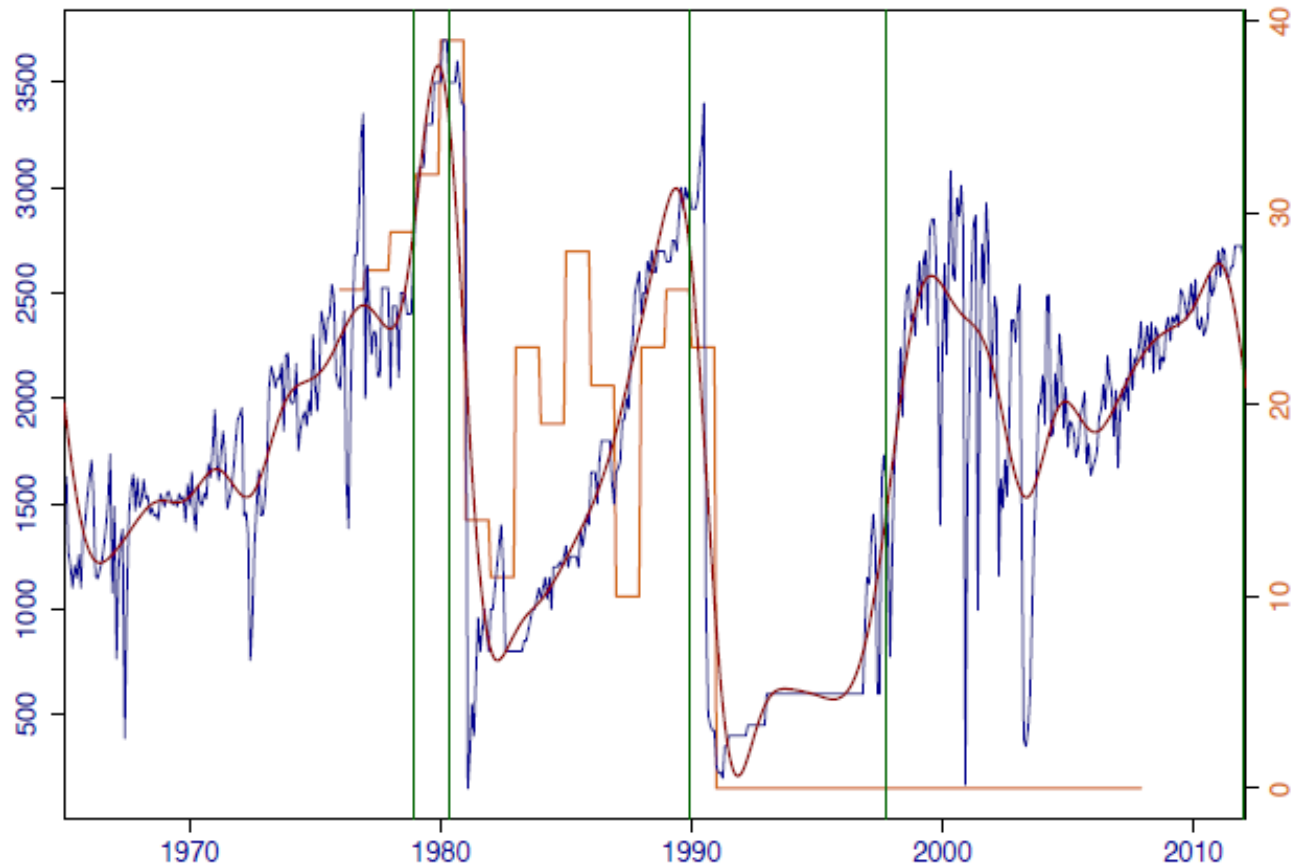


- Feedback mechanism during busts



- Low cost of production + monetary and fiscal policies (*lag*) \Rightarrow economic growth + geopolitical strife (*lag*) \Rightarrow $\boxed{\text{oil price } \uparrow}$. . .

The Effect of Wars on Iraq



Regime Change Did Not Disrupt Venezuela's Production

