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The United States-Iran Conflict: Economic Implications on India

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Summary

The ensuing United States-Iran conflict and the blockade of the Strait of Hormuz have created a huge economic challenge for India. The adverse impact on India's energy security, particularly for petroleum and LPG has had diverse consequences along many sectors. Manufacturing, agriculture, civil aviation and power generation have suffered setbacks leading to lay- offs. The government has taken urgent steps for energy supply diversification, fiscal measures to minimise price increases but the pressure on the rupee and forex reserves continue.

Introduction

The escalation of tensions between the United States (US) and Iran, culminating in a naval blockade affecting maritime traffic through the Strait of Hormuz, represents one of the most consequential geopolitical disruptions in recent times. As a critical chokepoint in the global energy system, the Strait facilitates the transit of nearly one-fifth of the world's petroleum supply. Any restriction, whether actual or anticipated, creates immediate instability in global energy markets, triggering price volatility and supply uncertainty.

For India, the implications of such a disruption are particularly significant. As one of the world's fastest-growing major economies and the third-largest consumer of crude oil, India's dependence on imported energy exposes it to external shocks emanating from geopolitical crises. This paper provides a comprehensive analysis of the economic effects of the Strait Hormuz blockade on India, with particular emphasis on energy security. It further examines the broader macroeconomic consequences, including inflationary pressures, external sector imbalances, currency volatility, sectoral disruptions and long-term structural adjustments.

Strategic Importance of the Strait of Hormuz

The Strait of Hormuz occupies a central position in global energy geopolitics. Connecting the Persian Gulf to international markets, it serves as the principal export route for major oil-producing countries such as Saudi Arabia, Iraq, Kuwait and the United Arab Emirates. Nearly 20 per cent of global petroleum crude consumption passes through this narrow waterway.

The strategic vulnerability of the Strait lies in its geographical constraints. At its narrowest point, it is only about 21 miles wide, making it highly susceptible to military and logistical disruptions. Even a limited blockade introduces systemic risk into global supply chains. The result is not merely physical disruption but also heightened market anxiety, which amplifies price fluctuations.

Energy Security and Oil Price Shock

India's vulnerability to the Strait of Hormuz crisis is rooted in its structural dependence on imported energy. Nearly 85 per cent of India's crude oil requirements are met through imports, with a significant proportion originating in the Gulf region. In February 2026, India imported nearly 91 per cent of its crude oil requirement with about half coming from West Asia.[1]

As a consequence, the most immediate and visible impact of the Hormuz Strait blockade is the surge in global crude oil prices. It has been a fact that disruptions in major transit chokepoints typically result in sharp price increases due to constrained supply and heightened uncertainty. Recent estimates indicate that crude prices have risen from an average of about US$75-80 per barrel (S$101-108) to above US$95-100 (S$128-135), per barrel, representing an increase of nearly 25-30 per cent in a short span. India imports roughly 4.5-5 million barrels per day, which would add up to about 1.7-1.8 billion barrels annually.

A widely used policy estimate suggests that every US$10 (S$13.5) per barrel increase in crude oil prices raises India's annual import bill by approximately US$13-15 billion (S$17.6-20.3 billion); thus, the recent US$20-25 (S$27-33.75) price surge may have already expanded the import bill by US$26-40 billion (S$35.1-54 billion), significantly worsening the current account balance.[2] This alone can widen the current account deficit by about 0.8-1.2 per cent of gross domestic product. It also explains the pressure on the rupee and drawdown on foreign exchange reserves. The macroeconomic consequences of such increase in the import bill are immediate: a widening current account deficit, increased pressure on the rupee and increased fiscal pressure.

India's trade balance is highly sensitive to oil price fluctuations. According to the World Bank, rising commodity prices worsen trade balances in energy-importing countries. Higher import costs, combined with reduced export competitiveness due to rising input costs, contribute to a widening trade deficit and current account imbalance.

The pressure on the external account often leads to depreciation of the Indian rupee. The International Monetary Fund notes that emerging market currencies are particularly vulnerable during periods of global uncertainty.

In addition, India's foreign exchange reserves have experienced a moderate decline, estimated at US$15-20 billion (S$20.3-27 billion) over a short period, reflecting higher import payments and interventions by the Reserve Bank of India to stabilise the currency. While reserves remain adequate, this decline signals increasing external vulnerability under sustained energy price shocks.

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1 K Balachandran, "Crucial Dependence: West Asia's Share in Indian Oil Imports Rose to 54% Just Before the Iran War", *The Hindu*, 21 April 2026, https://www.thehindu.com/business/Economy/crucial-dependence-west-asias-share-in-indian-oil-imports-rose-to-54-just-before-the-iran-war/article70833623.ece.

2 "Every $10 Rise in Crude Could Add $13–14 Billion to India's Import Bill: Report", *The Economic Times*, 10 April 2026, https://manufacturing.economictimes.indiatimes.com/news/energy/every-10-rise-in-crude-could-add-13-14-bn-to-indias-import-bill-report/130169017.

In response, the Indian government has undertaken fiscal adjustments, including reductions in excise duties and rationalisation of indirect taxes on petroleum products, thereby lowering the effective tax burden on refineries and consumers in an attempt to cushion inflationary pressures. While such measures provide short-term relief, the flip side is that they also reduce government revenue, thereby complicating fiscal management.

Natural Gas and Liquefied Petroleum Gas Vulnerabilities

India's dependence on liquefied natural gas (LNG) and liquefied petroleum gas (LPG) imports further amplifies its exposure. The country imports over 50 to 60 per cent of its LPG consumption, much of which transits through the Strait of Hormuz.[3] Disruptions have resulted in intermittent supply constraints and delays in household LPG availability, particularly in regions heavily dependent on imports.

The implications extend beyond households. Natural gas is a critical input in fertiliser production and rising gas prices increase agricultural input costs, potentially affecting food inflation and rural incomes.

Recent evidence from export clusters such as Coimbatore and Tiruppur indicates that declining global orders, compounded by energy shortages and rising logistics costs, have led to temporary shutdowns of micro, small and medium enterprises (MSMEs), reduced industrial capacity utilisation and significant job losses, highlighting the transmission of geopolitical shocks into domestic manufacturing.

Due to shortage of LPG supply, about 30 per cent of the MSME units in Coimbatore had to shut down temporarily rendering around 400,000 jobs at risk.[4] Added to this shortage, Industrial LPG prices increased from ₹1,800 to ₹4,500 (US$20-42 [S$27-58.7]) per cylinder in some cases. This, is critical since LPG is used in textile processing, dyeing, foundries, fabrication and without its production literally stops. Similarly, in Firozabad, near Agra, a town often referred to as a 'City of Glass', where tall chimneys arise out of glass workshops manufacturing bottles, bangles, mirrors and glassware for industrial requirement, have clusters of idle labour standing at various corners since production has been cut by 30 per cent due to LPG shortage. The story is the same over pharmaceutical production units in Baddi in Himachal Pradesh or leather tanneries in Kanpur and Chennai.

Shipping, Insurance and Supply Chain Disruptions

The Strait of Hormuz blockade has significant implications for global shipping and logistics. Increased geopolitical risk leads to higher insurance premiums and freight costs. Such disruptions reduce supply chain efficiency and increase global trade costs.

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3 Ibid.

4 "30% MSMEs Shut in Coimbatore Due to LPG Shortage; Codissia Seeks Centre's Intervention", *The Times of India*, 25 March 2026, https://timesofindia.indiatimes.com/city/coimbatore/30-msmes-shut-in-coimbatore-due-to-lpg-shortage-codissia-seeks-centres-intervention/articleshow/129806416.cms.

For India, these disruptions extend beyond energy imports to fertilisers, petrochemicals and industrial raw materials. Export sectors also face logistical challenges, reducing competitiveness in international markets.

Remittances and Diaspora-Linked Risks

India's economic ties with the Gulf are reinforced by a large expatriate workforce. India is the largest recipient of remittances globally, with a significant share originating from the Gulf countries. Economic instability in the region may reduce employment opportunities for Indian workers, leading to a decline in remittance inflows. In extreme scenarios, reverse migration may occur, placing additional pressure on India's labour market and domestic economy.

Thus, the economic effects of the Strait of Hormuz blockade are widely distributed across sectors of the economy: Agriculture faces rising input costs due to higher fertiliser and fuel prices. Manufacturing experiences increased production costs, reducing profitability. Transport and aviation sectors are directly affected by rising fuel costs. Power generation, particularly gas-based plants, is affected by LNG price volatility.

Policy Responses and Strategic Adaptation

In response to the economic disruptions triggered by the Strait of Hormuz blockade, India has adopted a multi-layered strategy combining short-term stabilisation measures with longer-term structural adjustments. These responses reflect both the immediacy of the energy shock and the broader imperative of reducing systemic vulnerability.

Diversification of Energy Sources

One of the most significant policy responses has been the diversification of crude oil import sources. Historically dependent on the Gulf region, India has increasingly sourced crude from alternative suppliers such as Russia and the US as well as African producers.[5] This shift reduces over-reliance on any single geopolitical region and enhances supply security.

In recent years, discounted crude imports from Russia have played a stabilising role in India's energy basket. Similarly, increased engagement with the US has diversified supply chains, albeit often at higher transportation costs. African producers, including Nigeria and Angola, have also emerged as supplementary suppliers.

However, diversification is not without constraints. Logistical challenges, differences in crude quality and refining compatibility limit the extent to which imports can be rapidly reoriented. Nevertheless, diversification remains a critical hedge against geopolitical risk.

[5] Press Information Bureau, Government of India, "Inter-Ministerial Briefing Held on Recent Developments in West Asia: 70% of India's Crude Imports Now Routed Outside Strait of Hormuz; Energy Supplies Remain Secure", Ministry of Petroleum and Natural Gas, 11 March 2026, https://www.pib.gov.in/PressReleasePage.aspx?PRID=2238525.

Strategic Petroleum Reserves

India has developed strategic petroleum reserves (SPR) as a buffer against short-term supply disruptions. These reserves, maintained at key locations, are designed to provide emergency supplies in the event of supply shocks or price spikes.

While India's SPR capacity currently covers only a limited number of days of consumption, it plays an important role in stabilising markets during crises. The government has also explored expanding storage capacity and engaging in public-private partnerships to enhance reserve levels. However, SPRs are inherently a temporary solution. They can mitigate immediate disruptions but cannot offset prolonged supply constraints or sustained high prices. Their effectiveness depends on timely release and efficient management.

Diplomatic Engagement

India's response has also involved careful diplomatic balancing. Maintaining constructive relations with both Western powers and key Gulf states is essential for ensuring uninterrupted energy flows.

India has traditionally pursued a policy of strategic autonomy, enabling it to engage simultaneously with the US, Iran and the Gulf Cooperation Council countries. This approach allows India to secure favourable energy supply arrangements; ensure safe passage of shipping through contested regions; and protect the interests of its large expatriate population in the Gulf.

Diplomatic engagement also extends to multilateral forums and maritime cooperation initiatives aimed at maintaining freedom of navigation in critical sea lanes.

Energy Transition Initiatives

The current crisis has reinforced the urgency of accelerating India's transition to renewable energy. Initiatives such as those led by the International Solar Alliance aim to expand solar energy capacity and reduce dependence on fossil fuels.

India has made significant progress in expanding renewable energy capacity, particularly in solar and wind power. The promotion of electric mobility, green hydrogen and energy efficiency further complements this transition. However, the transition remains gradual. Fossil fuels continue to dominate India's energy mix and renewable infrastructure requires substantial investment and technological advancement. Nonetheless, the current crisis serves as a catalyst for accelerating this shift.

Long-Term Structural Implications

The Strait of Hormuz crisis underscores the structural vulnerabilities of energy-importing economies in an increasingly volatile geopolitical environment. For India, the implications extend beyond immediate economic disruptions to long-term strategic reorientation.

Acceleration of Energy Diversification and Self-Reliance

The crisis is likely to intensify efforts toward diversifying energy sources and reducing dependence on imported hydrocarbons. This includes not only expanding renewable energy capacity but also exploring domestic energy resources and alternative fuels.

Strengthening Supply Chain Resilience

The disruption of maritime trade routes highlights the need for more resilient supply chains. India may increasingly invest in alternative shipping routes, domestic manufacturing capabilities and strategic stockpiling of critical inputs.

Such measures would reduce vulnerability to external shocks and enhance economic stability.

Expansion of Strategic Reserves and Infrastructure

The limitations of existing strategic petroleum reserves may prompt expansion in both capacity and scope. This could include reserves for natural gas and critical minerals, reflecting a broader conception of energy security.

Maritime Security and Geopolitical Engagement

The crisis also highlights the importance of securing critical sea lanes. India may increase investment in naval capabilities and maritime surveillance to protect its trade routes. Enhanced cooperation with regional and global partners in ensuring freedom of navigation is likely to become a strategic priority.

Reorientation of Economic Policy

Finally, the crisis may influence broader economic policy by reinforcing the need for macroeconomic resilience. This includes maintaining adequate foreign exchange reserves, managing fiscal risks and strengthening institutional capacity to respond to external shocks.

The Strait of Hormuz crisis, while disruptive in the short term, may ultimately serve as a catalyst for structural transformation in India's energy and economic policy, accelerating the transition toward a more diversified, resilient and strategically autonomous economic framework.

Conclusion

The US-Iran conflict and the Strait of Hormuz blockade present a multifaceted economic challenge for India. Energy security lies at the core of this challenge, acting as the primary transmission channel for broader macroeconomic disruptions.

The crisis has intensified inflationary pressures, widened external imbalances and disrupted multiple sectors. It has also exposed vulnerabilities related to energy dependence and external linkages.

While India has adopted mitigation strategies, the structural nature of its energy dependence remains a concern. The crisis, thus, underscores the need for a comprehensive approach to energy security, including diversification, strategic planning and accelerated transition to renewable energy.

Ultimately, the Strait of Hormuz blockade serves as a reminder of the deep interconnection between geopolitics and economic stability. Strengthening resilience against such shocks will be critical for India's long-term economic trajectory.

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