

August 2026

We Don't Have to Import Inflation

Policy Lessons
from the Strait
of Hormuz and
Ukraine
Supply Crises

By Michael Madowitz

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The Hormuz crisis is about much more than oil, but global oil stocks offer a solution to the next broad commodity crisis.

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Key Takeaways

- Inflation has posed a destabilizing risk to both economies and democratic institutions, as shown in this decade through the closure of the Strait of Hormuz and the supply shocks resulting from the invasion of Ukraine.
- Progressive policymakers must develop more proactive approaches than the limited, reactive tool kit central bankers have at their disposal to prevent inflation shocks.
- The Hormuz crisis has shown us the cascading consequences of disruptions to supply chains that provide primary inputs like oil, fertilizer, and aluminum. The resulting shortages deal a blow to the economy that cannot be addressed by interest rate adjustments.
- Broader investments in strategic capacity, such as buffer stocks and strategic reserves, can help reduce price volatility and maintain global stability.

Introduction

The months-long Strait of Hormuz crisis is an energy markets disaster that will be with us for months to come. The downstream effects of supply disruptions are showing up in markets

well beyond energy, where they could take even longer to normalize.

As the 2020s continue to remind us, modern supply chains are complex, and outsourcing strategic considerations to private markets can create economic fragility. Those sources of fragility can be major contributors to inflation and shortages, underscoring the need for industrial strategies to both stabilize economies and ensure political and economic sovereignty, akin to investments in national security.

The disruptions from the Hormuz crisis are especially acute because the region is a key producer of primary inputs (general inputs to numerous production processes), specialized inputs (those that are crucial and difficult to substitute in production), and energy-intensive materials, all of which create significant downstream effects.

This brief provides an overview of some of the most consequential supply disruptions of the Hormuz crisis along with some of the policy tools that could better insure against individual supply disruptions and inflation shocks. Given the politically destabilizing risk inflation has posed to democratically elected governments this decade, progressive policymakers must develop more proactive approaches than the limited, reactive tool kit central bankers have at their disposal to prevent inflation shocks.

Advanced economies need not import inflation when crises occur due to geopolitical conflict, whether instigated by Russia in 2022 or the US in 2026. Setting aside the dubious foreign policy choices that precipitated the current crisis, insuring against physical commodity shock—driven inflation is a domestic policy strategy that can pay macroeconomic resilience dividends for both the [Middle Powers](#) that Canadian Prime Minister Mark Carney described earlier this year and superpowers like the United States.

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Industrial Policy as an Inflation-Management Tool

We are once again seeing a real-time example of the case for strategic reserves, [buffer stocks](#), and spare production capacity for even abundant commodities. As is the case with fossil energy, simply expanding domestic production cannot insulate Americans from price shocks—reducing price volatility requires investments in inventories and spare capacity, which private markets punish. Central banks have few tools to address energy-driven inflation—[prescribed responses](#) to supply shocks are limited, which puts the burden of response on different economic tools.

The postwar order that birthed the Bretton Woods system to stabilize currencies stopped short of enacting a bolder progressive vision to [stabilize crucial commodity prices](#) with international stockpiles. The 1956 Suez Crisis prodded advanced economies to partially adopt this approach with fossil energy, giving rise to buffer stocks like the [US strategic petroleum reserve](#). Releases from these global [energy reserves](#) coordinated by the International Energy Agency, along with [China's use of its own oil reserves](#), have dramatically blunted the energy shock of the Hormuz crisis.

These buffering strategies [are not costless](#)—building initial inventories requires diverting spending from other priorities, even if the ongoing costs have little impact on public budgets—but they can be part of investments to improve resilience and shelter economies from importing inflation.

This is more than a technocratic concern: The wave of inflation following Russia's invasion of Ukraine wiped out democratically elected governments across advanced economies. Public investment in national defense is expensive and accepted as a cost of maintaining sovereign, stable democracies; similar investments in strategic industrial capacity to maintain economic sovereignty should be considered part of this framework.

Shortages of Ubiquitous Commodities

Primary Inputs

The breadth of effects from the Hormuz crisis stems in part from the region's role in primary commodities that are key inputs to making numerous other materials.

Take sulfur. Sulfur is the most produced industrial chemical and is used across a striking variety of industries. Sulfur mining dates back centuries, but today most sulfur is produced as a byproduct of [refining oil](#). Crude oil with a high sulfur content is described as sour, and many of the world's top [sulfur exporters](#) are countries that produce lots of sour crude oil. Modern combustion engines run on low-sulfur fuels, and the most cost-efficient refining processes not only remove sulfur from fuels but capture and sell what would otherwise be waste as a byproduct.

Sulfur is an important input in diverse supply chains such as batteries (and therefore electric vehicles), pharmaceuticals, metal production, and skin creams. It's used as part of finished products like soap and also consumed in chemical reactions, often as sulfuric acid, to refine products like sugar and copper. But its [largest use](#) is in creating fertilizer, and the loss of Gulf production has taken almost half of [seaborne sulfur](#) off the world market, dealing potential blows to farms that rely on global fertilizer production.

Other key fertilizers are impacted by the closure of the strait as well, principally ammonia and urea. Fertilizer supply chains are relatively regional, and the Gulf region supplies much of the [fertilizer imports](#) to [East Africa](#) and South Asia, particularly India. [Between 15 and 50 percent](#) of global fertilizer product supplies have been impacted worldwide. As the supply crisis has stretched on, shortages of fertilizer have begun to affect [crop planting seasons](#), threatening to reduce yields and thus global food supplies.

Russia's war in Ukraine stretched supply chains for many abundant commodities, so there was even less slack to absorb this shock than usual. While it's difficult to produce our way out of some of the most produced chemicals on earth, strategic reserves and buffer stocks can mitigate these risks.

Expanding the ability to produce and store fertilizer products free from chokepoints would shore up a global resource and ensure a more resilient food supply. The US could be an especially important contributor to stability for global fertilizer supplies—a welcome change from its role in disrupting markets in 2026—because the disconnect between the [US and global natural gas markets](#) gives US producers a cost advantage in a market that has been shaken by large shocks over the last five years.

Making economies resilient to specialized input shocks requires cooperation between governments, which can make strategic investments that markets would punish, and private companies, which have unique knowledge of their supply chain risks.

Specialized Inputs

With each supply chain disruption since COVID-19, it seems the world learns about different obscure industrial materials, and so it is with the Hormuz crisis. Russia's invasion of Ukraine shined a light on [neon and krypton gases](#), which play a role in laser and semiconductor production. This crisis has raised concerns about helium—particularly because the AI boom calls for considerable helium use in manufacturing memory and computer chips. Helium has a number of [applications](#) beyond semiconductor manufacturing, including welding and extreme cooling, with the primary uses varying across regions. Asia uses helium mostly for semiconductor production, while US helium is crucial to cooling the magnets employed in more than [40 million MRI scans](#) Americans receive every year.

The helium supply crunch somewhat mirrors the natural gas crunch: In both cases, the losses that come from moving liquefied gases long distances by ship limit trade outside of regional markets. While the loss of Russian natural gas and Gulf helium has left both markets unbalanced, worldwide helium inventories are significant and have buffered the shock so far.

This supply chain will take longer to recover, however. Much of the specialized transportation equipment needed to maintain and store liquid helium near absolute zero is out of place and may have been damaged while stranded behind a blockade. The vulnerability of semiconductor production to this disruption may not be fully known until the second half of the year.

Plastic resins are also under strain as a result of the crisis. Plastics are derived from petroleum, and these products play a crucial role in the production of materials we don't think of as plastics. Packaging and other low-cost uses are seeing substitution, but [synthetic fabrics](#) and other specialty applications are seeing supply and cost pressures. Asian snackmakers have come up with especially [innovative solutions](#) to the loss of dye compounds, but [condom makers](#) have raised prices and risk demand destruction.

Specialized inputs are, by definition, special—it can be difficult to identify which lack close substitutes or are used widely in the economy before a shock. The strategic value of high-performance chips and rare earth minerals is a forecasted concern. The vulnerability of the US housing market to a [garage door shortage](#) was not.

Making economies resilient to specialized input shocks requires cooperation between governments, which can make strategic investments that markets would punish, and private companies, which have unique knowledge of their supply chain risks. This cooperation should not just happen as part of a frenzied response to major disruptions, as it does now, but become part of a much more mundane ongoing state capacity, identifying critical input vulnerabilities and investing in strategic stockpiles and capacity where possible.

Energy-Intensive Goods

Available resources, particularly energy access, shape economic geography. Economic historians have documented how growing energy production pairs with the development of major industries, like coal with steel in the Allegheny region, or hydroelectric power with aircraft manufacturing in the Pacific Northwest. The Middle East, the largest global energy production region of the last 50 years, has developed globally significant energy-intensive industries that are caught in the Hormuz chokepoint.

Aluminum is the third most common element on Earth, but converting the ore to finished metal is so energy intensive ([20–40 percent](#) of the final cost) that aluminum smelting geography is highly influenced by energy access. Cheap renewables have given countries like [Iceland](#) an edge in this industry, but dedicated gas-fired power plants in the Gulf fuel many of the world's largest aluminum plants. In the short term, the Hormuz closure has taken [nearly 10 percent](#) of aluminum production offline, and [strikes at large smelters](#) may affect longer-term production. Aluminum is a crucial input to many heavy industries, including aerospace and automotive manufacturing, where its light weight helps reduce use of gasoline and jet fuel.

Fertilizer production is also [energy intensive](#), with many steps of the chemical reactions to generate nitrogen relying on natural gas. The loss of production from Russia and Ukraine was largely due to the colocation of fertilizer production with natural gas infrastructure in the region, and the loss of Gulf production is similarly tied to the region's natural gas reserves.

The Gulf energy industry doesn't just pull oil and gas out of the ground. Many of the most concerning effects of the Hormuz crisis have been from the loss of refined products in global markets. The region's globally dominant refining industry wouldn't be in the region if not for the Gulf's fossil fuels.

Still, the most acute global shortages are in markets for specific products like gasoline, diesel, jet fuel, and cooking gas, which come from the Gulf's large refining capacity. The loss of access to this refining infrastructure adds another dimension to the difficulty of responding to the Hormuz energy crisis.

In the short term, increasing aluminum recycling rates, a margin where the US has even more capacity to respond than peers, is sound industrial policy. Aluminum is almost perfectly recyclable, and the US can reduce the global strain on aluminum markets and unlock many other benefits by simply bringing its [recycling rates](#) in line with other developed countries.

In the longer term, developing more independent aluminum production capacity requires [both investment and energy](#), as well as a strategy to compete with the lower-cost, [clean aluminum investments China](#) is making today.

The loss of refined products from the Gulf points to another opportunity in the energy transition: As Western economies reduce fossil fuel use, public investments to maintain a portion of the resulting excess refining capacity can be a cost-effective policy to reduce price volatility and maintain global stability.

Building Strategic Capacity to Better Manage Supply-Side Inflation

Amid a second wave of inflation with frustrating parallels to the post-COVID global inflation surge, it's important to examine the lasting inflation and price-level impacts of broader commodities market disruptions.

Monetary policy is a reactive tool to limit inflation spillovers at the cost of a weaker economy overall, but broader investments in strategic capacity are possible. Public investments in buffer stocks and strategic reserves—whether in primary products like fertilizers, specialty inputs like helium, or energy-intensive goods like aluminum—can temper price and physical commodity shocks.

Public policies readily shift from market to strategic production in wars—most famously in

America’s turn to the [Arsenal of Democracy](#) under President Franklin D. Roosevelt—but protecting economies and democracies from shocks and inflation should be considered a priority in its own right.

These solutions are not free—maintaining strategic reserves and excess capacity, by definition, requires more resources. But insurance is often worth the price, and public policy needs to offer solutions to cost shocks, not just apologies.

In a century where militaries have internalized “[the enemy gets a vote](#)” on the battlefield, democracies around the world need to reconsider what investments are worth making to ensure hostile regimes don’t get a vote on other countries’ inflation and ultimately at the ballot box.

Suggested Citation

Madowitz, Michael. 2026. “We Don’t Have to Import Inflation: Policy Lessons from the Strait of Hormuz and Ukraine Supply Crises” Roosevelt Institute, August 12, 2026.

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AUTHORS

Michael Madowitz

PRINCIPAL ECONOMIST

Michael Madowitz is the principal economist at the Roosevelt Institute, shaping economic strategy across programmatic areas.



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