



Counting the economic cost of the Iran-Israel conflict

Israel and Iran have traded strikes over the past week and while there are a large number of ways the conflict could go from here, the risk of further escalation is mounting. Not only would this cause enormous damage to Iran's economy, but spillovers to neighbouring countries could also intensify.

To recap, Israel conducted strikes last Friday targeting Iran's nuclear facilities, military bases, and high ranking personnel. In retaliation, Iran returned a barrage of missiles and the two nations have traded daily strikes since.

So far at least the conflict has not escalated beyond Iran and Israel, but comments from President Trump have raised fears of US involvement. He has demanded Iran's "unconditional surrender", posted veiled threats at Iran's Supreme Leader, and reiterated demands for nuclear negotiations in which Iran foregoes its uranium enrichment.

We have written a number of reports looking at the implications of the conflict on regional economies, global energy markets, the global economy and financial markets, as well assessing potential scenarios of where the conflict could escalate. All of this can be viewed on our [Key Issues](#) page.

For Iran, aside from the humanitarian cost of war, the longer and more intense the conflict becomes, the greater the economic cost too. Of the major wars across EMs in the past three decades, GDP has, on average, contracted by 33% peak-to-trough. Of those in the Middle East that rises to almost 50% – notably Kuwait (56.5%) and Iraq (64.0%) during the Gulf war in 1991. Iran's economy accounts for 0.85% of global GDP and, if we were to assume a similar fall in output, this would directly knock around 0.4%-pts off of global GDP growth – equal to our estimate of the damage of Trump's tariff policies.

A slump in Iran's economy would spill over onto those with close trade ties. The UAE is the most vulnerable with its exports to Iran equal to 1.2% of GDP, followed by Oman (0.5%), and Turkey (0.3%).

A key question, of course, is whether the conflict embroils neighbouring countries. We've highlighted that the thawing of relations between the Gulf states and Iran has significantly reduced this risk. But Ayatollah Khamenei has spoke of repercussions if the US were to get directly involved and this may involve strikes against US military assets in the region, such as major bases in Qatar, Bahrain, Kuwait, the UAE, and Iraq. In this high tension environment, there is a greater chance of a misstep that inadvertently pulls these countries into the conflict.

So long as oil infrastructure in the Gulf remains intact, past experience suggests that growth in the region could actually *strengthen* despite the conflict. For one thing, Gulf oil producers could move to raise oil output to offset supply disruptions in Iran – a similar move occurred in 1991 as Kuwait's production collapsed. The conflict, of course, comes against the backdrop of the recent push by OPEC+ to recapture market share.

Meanwhile, the conflict has pushed oil prices higher – Brent crude is currently trading at \$77pb, a 20% rise since the start of the month. The combination of rising oil output volumes and higher prices will have boosted oil export receipts and government revenues. As a rough exercise, if Saudi Arabia opted to offset the loss of Iran's ~1.5mn bpd of oil exports that would boost the Kingdom's oil export receipts by 2.5% of GDP at current oil prices (on an annualised basis). And if prices rose to \$100pb it would be equal to nearly 4% of GDP (assuming that its ability to export oil hasn't been affected).

For now at least, that would enable fiscal policy to remain loose. That would go some way to supporting non-oil sectors which may otherwise suffer if the conflict weighs on business and consumer confidence.

The week ahead

We expect Morocco's central bank to cut interest rates by 25bp next week. (See [Data Preview](#).)

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Data Preview

Tuesday 24th June – Morocco Interest Rate Announcement

Forecasts	Time (BST)	Previous	Consensus	Capital Economics
Key Policy Rate (%)	-	2.25%	-	2.00%

BAM has one left in the chamber

We think that Morocco's central bank, Bank Al-Maghrib (BAM), will deliver a final 25bp interest rate cut next week, though there's a risk that the backdrop of the Israel-Iran conflict and higher oil prices could keep rates unchanged.

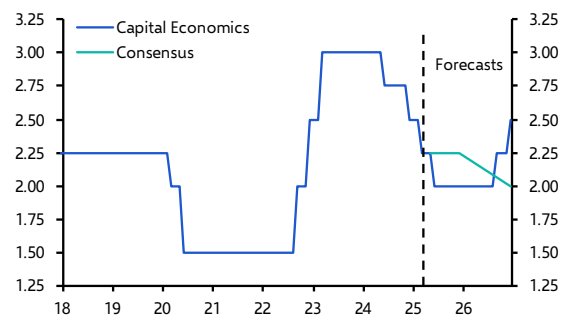
At its previous quarterly board meeting, BAM policymakers cut the key policy rate by 25bp, to 2.25%. The accompanying statement pointed to the slowdown in inflation and successful anchoring of expectations in line with price stability goals. At the same time, policymakers showed a desire to support activity and employment.

Since March's meeting, the headline inflation rate has slowed further to 0.7% y/y in April and we expect it to hover around 0.5-1.0% y/y over the remainder of this year. Meanwhile, while bank lending grew by 5.4% y/y in April, the fastest pace in a year, growth in output from the manufacturing sector slowed and the unemployment rate came in at 13.3% in Q1, just shy of its all-time high. Against

this backdrop, we expect BAM to cut interest rates by 25bp, to 2.00% next week.

However, the combination of uncertainty of Trump's trade war and the escalating Iran-Israel conflict may prompt officials to stand pat and wait for a more stable global economic backdrop. Even so, if the rate cut is pushed back to Q3 we expect that to be the last in the cycle and for interest rates to be left on hold well into 2026. (See Chart 1.)

Chart 1: Bank Al-Maghrib Key Policy Rate (%)



Sources: Bank Al-Maghrib, CEIC, [Capital Economics](#)



Economic Diary and Forecasts

Upcoming Events and Data Releases

Date	Country	Release/Indicator/Event	Time (BST)	Time (GST)	Previous*	Median*	CE Forecasts*
Fri 20 th	Mor	Consumer Prices (May.)	-	-	-0.3%(+0.7%)	-	(+0.9%)
	Kuw	Consumer Prices (May.)	-	-	+0.2%(+2.3%)	-	(+2.1%)
Sat 21 st	-	No Significant Data or Event Scheduled	-	-	-	-	-
Sun 22 nd	-	No Significant Data or Event Scheduled	-	-	-	-	-
Mon 23 rd	Leb	Consumer Prices (May.)	-	-	(+13.0%)	-	(+12.8%)
Tue 24 th	Mor	Interest Rate Announcement	-	-	2.25%	-	2.00%
	Oma	Consumer Prices (May.)	-	-	+0.5%(+0.9%)	-	(+1.1%)
	Jor	Industrial Production (Apr.)	-	-	(+1.7%)	-	-
Wed 25 th	Sau	Balance of Payments (Apr., SAR)	07.00	10.00	+19.8bn	-	-
	Sau	Non-oil Trade (Apr.)	07.00	10.00	(+6.7%)	-	-
Thu 26 th	Bah	Consumer Prices (May.)	-	-	(-0.5%)	-	(-0.3%)
Also expected during this period							
15 th -22 nd	Egy	GDP (Q1)	-	-	(+4.3%)	-	(+6.0%)
15 th -30 th	Bah	GDP (Q1, q/q(y/y))	-	-	(+3.4%)	-	(+3.8%)
	Jor	GDP (Q1, q/q(y/y))	-	-	(+2.7%)	-	(+2.4%)
	Qat	GDP (Q1, q/q(y/y))	-	-	+0.4%(+6.1%)	-	(+2.9%)
16 th -21 st	Egy	Trade Balance (Apr.)	-	-	-\$2.5bn	-	-
26 th -3 rd	Qat	Consumer Prices (May.)	-	-	+0.8% (+0.5%)	-	-0.1% (+0.1%)
Selected future data releases and events							
29 th Jun	Sau	International Reserves (May.)	-	-	+\$416bn	-	-
	Sau	Private Sector Credit (May.)	-	-	(+15.2%)	-	-
30 th Jun	Mor	GDP (Q1, q/q(y/y))	-	-	(+3.7%)	-	-
2 nd Jul	Egy	Foreign Exchange Reserves (Jun.)	-	-	\$48.5bn	-	-
3 rd Jul	UAE	Whole Economy PMI (Jun.)	05.15	08.15	53.3	-	-
	UAE	Dubai Economy Tracker (Jun.)	05.15	08.15	52.9	-	-
	Sau	Whole Economy PMI (Jun.)	05.15	08.15	55.8	-	-
	Kuw	Whole Economy PMI (Jun.)	05.15	08.15	53.9	-	-
	Leb	Whole Economy PMI (Jun.)	09.00	12.00	48.9	-	-
	Qat	Whole Economy PMI (Jun.)	10.00	13.00	50.8	-	-
6 th Jul	Egy	Whole Economy PMI (Jun.)	05.15	08.15	49.5	-	-
7 th Jul	Tun	Consumer Prices (Jun.)	-	-	(+5.4%)	-	-
	Jor	Private Sector Credit (May.)	-	-	(+5.9%)	-	-
10 th Jul	Sau	Industrial Production (May.)	07.00	10.00	(+3.1%)	-	-
	Egy	Consumer Prices (Jun.)	-	-	+1.9%(+16.8%)	-	-
	Egy	Core Consumer Prices (Jun.)	-	-	(+13.1%)	-	-
	Egy	Interest Rate Announcement	-	-	24.00%	-	-
	Egy	Industrial Production (May.)	-	-	(+3.1%)	-	-
11 th Jul	Jor	Consumer Prices (Jun.)	-	-	+0.2%(+2.0%)	-	-
15 th Jun	Sau	Consumer Prices (Jun.)	07.00	10.00	(+2.2%)	-	-

*m/m(y/y) unless otherwise stated. Sources: Bloomberg, LSEG Data & Analytics, [Capital Economics](#)



Main Economic & Market Forecasts

Table 1: Central Bank Policy Rates

	Policy Rate	Latest (19 th Jun.)	Last Change	Next Change	Forecasts	
					End 2025	End 2026
Saudi Arabia	Reverse Repo Rate	4.50	Down 25bp (Dec. '24)	Down 25bp (H2 '26)	4.50	4.00
Egypt	O/N Deposit Rate	24.00	Down 100bp (May '25)	Down 100bp (Jul. '25)	18.00	11.00
UAE	Repo Rate	4.40	Down 25bp (Dec. '24)	Down 25bp (H2 '26)	4.40	3.90
Algeria	Discount Rate	3.00	Down 25bp (Apr. '20)	Down 25bp (H2 '26)	3.00	3.00
Qatar	Deposit Rate	4.60	Down 30bp (Dec. '24)	Down 25bp (H2 '26)	4.60	4.10
Kuwait	Discount Rate	4.00	Down 25bp (Dec. '24)	Down 25bp (H2 '26)	4.00	3.50
Morocco	Key Rate	2.25	Down 25bp (Mar. '25)	Down 25bp (Jun. '25)	2.00	2.00
Oman	O/N Repo rate	5.00	Down 25bp (Dec. '24)	Down 25bp (H2 '26)	5.00	4.50
Tunisia	BCT Key Rate	7.50	Down 50bp (Mar. '25)	Up 250bp (H2 '25)	12.00	12.00
Jordan	Policy Rate	7.75	Down 25bp (Nov. '24)	Down 25bp (H2 '26)	7.75	7.25
Bahrain	1-Wk deposit facil.	5.25	Down 25bp (Dec. '24)	Down 25bp (H2 '26)	5.25	4.75

Sources: LSEG Data & Analytics, [Capital Economics](#)

Table 2: Currencies and Commodity Price Indices

	Currency	Latest (19 th Jun.)	Forecasts		Commodity Price	Latest (19 th Jun.)	Forecasts	
			End 2025	End 2026			End 2025	End 2026
Saudi Arabia	SAR/USD	3.7517	3.7500	3.7500	Brent crude (LCOc1)	77.14	60.00	50.00
Egypt	EGP/USD	50.53	53.00	58.00	Asian LNG (JKMc1)	13.88	13.50	8.50
UAE	AED/USD	3.6720	3.6725	3.6725				
Algeria	DZD/USD	130.07	140.00	155.00				
Qatar	QAR/USD	3.6412	3.6400	3.6400				
Kuwait	KWD/USD	0.3063	0.3070	0.3070				
Morocco	MAD/EUR	10.51	10.25	10.00				
Oman	OMR/USD	0.3850	0.3845	0.3845				
Tunisia	TND/EUR	3.38	4.75	5.25				
Jordan	JOD/USD	0.71	0.71	0.71				
Lebanon	LBP/USD	89,900	100,000	100,000				
Bahrain	BHD/USD	0.3770	0.3769	0.3769				

Sources: LSEG Data & Analytics, [Capital Economics](#)

Table 3: GDP and Consumer Prices

	Share of World ¹	GDP ²					Consumer Prices ²				
		2023	2024	2025	2026	2027	2023	2024	2025	2026	2027
Saudi Arabia	1.09	0.5	2.0	4.3	4.5	2.8	2.3	1.7	2.3	0.8	1.8
Egypt	1.15	2.9	3.1	5.0	5.3	6.3	34.0	28.0	15.5	8.8	7.5
UAE	0.44	3.6	4.0	5.8	6.5	4.0	1.8	1.8	0.8	1.0	0.8
Algeria	0.43	4.1	3.8	2.5	2.0	1.0	9.3	4.0	4.0	4.5	4.5
Morocco	0.20	3.4	3.2	4.3	5.0	5.3	6.1	0.9	1.3	2.0	2.5
Qatar	0.18	1.5	2.5	3.0	5.5	15.0	3.1	1.2	0.0	1.3	0.8
Kuwait	0.13	-1.7	-2.6	2.0	4.8	1.3	3.6	2.9	2.5	2.0	1.3
Oman	0.11	1.2	1.7	2.0	3.5	2.5	1.0	0.5	0.8	0.8	0.8
Tunisia	0.09	0.0	1.4	1.5	1.0	2.0	9.3	7.0	7.0	9.5	9.0
Jordan	0.06	2.6	2.5	2.3	1.5	1.5	2.1	1.6	2.5	1.0	0.5
Bahrain	0.05	3.9	2.6	1.5	1.8	2.0	0.1	0.9	0.0	2.0	2.0
Lebanon	0.04	-1.0	-8.0	-0.5	5.0	5.3	221.3	45.2	13.2	8.8	8.5
MENA	3.97	2.1	2.5	4.1	4.6	4.4	14.3	10.0	6.1	3.9	3.8

Sources: CEIC, LSEG, [Capital Economics](#). 1) %, 2024, in PPP terms. 2) % y/y annual average.



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