Policy Backgrounder

The War in the Gulf to the US Midterms

The US' rejection of Iran's recent proposal for a quick reopening of the Strait of Hormuz does not preclude further negotiations but does extend the timeline for an end to the conflict, likely at least past the US midterm elections. This Backgrounder evaluates several near-term scenarios for the conflict and business implications.

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- The likeliest scenario for the immediate future (at least through the November elections) is the status quo – with elevated energy prices and variable rates of ships transiting the Strait of Hormuz based on events. Recent Houthi attacks on Saudi Arabia, however, raise the question of whether the US might join a localized response.
- The broad issues remain the same: control of the Strait of Hormuz, the US naval blockade, the status of frozen Iranian assets, and the Iranian nuclear program. The US will also want assurances for Gulf allies. The ability of ships to transit the Bab al-Mandab and of Saudi Arabia to export through the East-West Pipeline will have critical impacts on the timeline.
- While there is the possibility of an "October surprise" agreement before the elections, the US publicly doubts this and signaled that it will put great pressure on Iran after the November elections, possibly leading to an agreement at that time. Other scenarios, including a resumption of large-scale military attacks, are low in the immediate and near-term.
- Beyond energy industries, the principal business impacts are on petrochemicals, including fertilizer shortages that could lead to lower plantings and higher food prices; shipping and the availability of maritime insurance; and follow-on economic effects, including on interest rates and economic activity, from elevated energy prices and reduced supply as the Northern Hemisphere prepares for winter.

Status Quo – For Now

The US and Iran negotiated a ceasefire in June which expired in August. In the absence of a further ceasefire, the status quo of a continued US blockade and other military operations in the region and occasional attacks and retaliation is the most likely scenario through the US midterm elections. Commercial traffic through the Strait of Hormuz would almost certainly not return to anything close to the pre-war level of about 120 ships per day; levels of traffic would rise and fall depending on events and the availability of maritime insurance. This scenario implies continued higher energy prices; continued pressure on Iran's economy from a lack of oil revenues; and continued pressure on Saudi Arabia, the UAE, Qatar, Iraq, and other Gulf economies.

Iran is losing billions of dollars in oil revenue from the blockade, and its capacity to export oil by other means is limited.[1] During the weekend of September 25-26, traffic through the Strait fell sharply, to five tankers, and Qatar canceled LNG shipments to some Asian customers. (Overall, Qatar's LNG exports have reportedly fallen 96% year-on-year to August 2026.[2]) By definition, the longer duration of the status quo affects both regional economies and the global economy more negatively, adding pressure on business. The US' economic pressure has also extended to other sectors, notably aviation; both Oman and Iraq have closed their airspace to Iranian civil aircraft, increasing Iran's isolation.[3]

In this scenario, Iran could also take other actions, such as encouraging further military responses from the Houthis in Yemen to put pressure on Saudi Arabia (Iranian involvement in the recent Houthi attacks on Saudi Arabia has not been proven) and on the West through cyberattacks or other means. But these could easily provoke a military response, so Iran's calculus here would presumably depend on its assessment of whether renewed military action would hurt the US and whether Iran can withstand further military and economic pressure.

Timing: effect of the midterms

Further, at the UN General Assembly in late September, the President stated that he believes Iran will make a deal after the US November elections "because it doesn't make sense for them not to. . . . I have a big decision to make": a deal with Iran "that will let them rebuild and create a far greater country than ever was before" or to "annihilate the Islamic republic and do it quickly, never giving them a chance to destroy people or continents?"[4]

The language indicates that the US may be including a renewed push on the nuclear issue as part of a deal; it also signals that while there could be an "October surprise," which could give the US a win before the election, the timing is more likely after the US midterms.

Attacks on Saudi Arabia

Perhaps taking advantage of the US' stated reluctance to engage in large-scale attacks before the midterms, and also in response to Saudi and Yemeni attacks seeking to push back Houthi positions, including around the city of Mokha, the Houthis have stepped up attacks on Saudi Arabia, including three strikes on Riyadh's King Khalid International Airport that led to fatalities

and the closing of the airport. The timing could also be related to the World Petroleum Congress to be held this week and the upcoming Future Investment Initiative meeting,[5] to discourage attendance given the risk of potential further attacks. Saudi Arabia states that the meetings will proceed as scheduled, but together with the suspension of air service earlier in the war through the important gateways in the UAE and Qatar, international aviation has been among the industries most affected by the conflict. Prior to the recent attacks, an Asian aviation group reported that overall fares between Asia and the West remain elevated, though the premium for nonstop flights (rather than those stopping in the Gulf) had declined to pre-war levels.[6]

Prospects for a Negotiated Ceasefire Agreement

Iran's recent proposal to "reopen" the Strait of Hormuz in seven days was based on principles in the June agreement. It required as preconditions that the US lift the naval blockade of Iran (which would permit free transit of Iranian oil) and unfreeze a portion of Iranian funds. As a part of this proposal, Iran and Oman would control the Strait – a significant change since January when the Strait was regarded as an international waterway – but would postpone discussion of maritime fees.

The US rejected the proposal but suggested that indirect US-Iran negotiations are continuing through third-party mediators including Qatar. Any negotiations – presumably after the US midterms -- would confront the same issues: who would control the Strait of Hormuz? Would prenotification of transits be ships be required? Would maritime "fees" be imposed on shipping? Would Iranian assets be unfrozen as part of the agreement? Perhaps most important, what is the timing and order of the concessions – neither the US nor Iran will agree to a timetable in which one party has an advantage? Iran has been clear that lifting the US blockade is an absolute precondition for reopening the Strait – but this would effectively end the US' economic pressure campaign on Iran, currently its principal option other than resuming large-scale military strikes.

More broadly, Western, Gulf, and Asian shipping companies strongly dislike the principle of maritime fees, which would presumably be in addition to the purchase of commercial insurance. If Saudi Arabia were to endorse the concept of joint Iranian/Omani control of the Strait (ships entering via Iranian waters and leaving via Omani waters), that would sharply increase the likelihood of this scenario.

Other complications include the Iranian demand for a ceasefire "on all fronts" (including Lebanon) and the issue of Iran's nuclear program. While the US has suggested in recent weeks that a deal could be "many years" away – a sign that reopening the Strait is the more important objective of US policy – the US maintains its position that Iran can never possess a nuclear weapon.

In the event of a negotiated ceasefire, spot energy prices could come down but the price of energy would remain elevated for some time as forward contracts have already been purchased. Saudi Arabia has also canceled some LNG shipments to Europe for the winter and

would need time to resume exports (although the East-West Pipeline is reportedly functioning once again). There would be some impact on Japan and South and Southeast Asia from lower prices in the near-to-medium term. Large stockpiles in China reduce the impact there. A shortage of tankers also reduces immediate downward pressure on energy prices,[7] and the effect is magnified if shipping does not transit the Bab al-Mandab but takes a longer route around Africa.

One factor potentially delaying or lessening the possibility of this scenario is the effect of the killings of former Iranian leadership early in the war. Who in Iran has the power to make a deal, and would a deal be acceptable to a sufficient number of leadership groups in Iran? These questions are more complicated now than before the war.

Resumption of Active US Bombing Unlikely – For Now

The June ceasefire did not prevent all kinetic activity in the region. At times, there was an exchange of incidents between Iran and the US, which included retaliation against the Gulf countries and US-affiliated targets in the region. Absent a ceasefire, resumption of large-scale active US bombing is a potential scenario, albeit less likely in the near-term. The US is reluctant to resume large-scale attacks except in retaliation to direct attacks on US forces or US interests. The war remains unpopular in the US, continued attacks would drive up energy prices leading to further concerns about affordability before the midterms at a time when the US Strategic Petroleum Reserve is at its lowest level in several decades, and the Gulf allies strongly disfavor large-scale military attacks now lest they face retaliation that would hurt their economies further.

In addition, Iran has threatened that in the event of renewed US aggression, it would “definitely change the weapons and geography of the war”;[8] this could include expansion of Iranian attacks to the Indian Ocean, widening the area which the US Navy must defend to enforce the blockade and in practice weakening it somewhat.[9]

In this scenario, there would presumably be further US responses to Iranian attacks, and a presumed more intense military response from the Houthis in Yemen, leading to further pressure on the Bab al-Mandab and shipping in the Red Sea and possibly further military response from Saudi Arabia (perhaps joined in some way by the US). There could also be a risk of resumed attacks in Israel, leading to a resumption of active operations in Lebanon (a scenario which could also influence the Israeli elections in October). Further, Iran could also more directly target US and other Western interests through cyberattacks or other means.

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Endnotes

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