

Energy Prices and Financial Crises

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[Simple-]Argument Overview

- 1 There is a secular (economic) cycle in oil prices – driven by the business cycle and construction lags
- 2 The cycle's swings can be amplified by (and feedback into) financial crises, as well as geopolitical risks
- 3 Geopolitical events may act as catalysts; their (occasionally) severe effects must be studied within the context of financial conditions
- 4 The current *bubble* in oil prices is in part caused by lax financial regulation and the lack of Bretton-Woods-like discipline
- 5 The battery of solutions and preventive measures is obvious, but the political will for implementation is difficult to sustain

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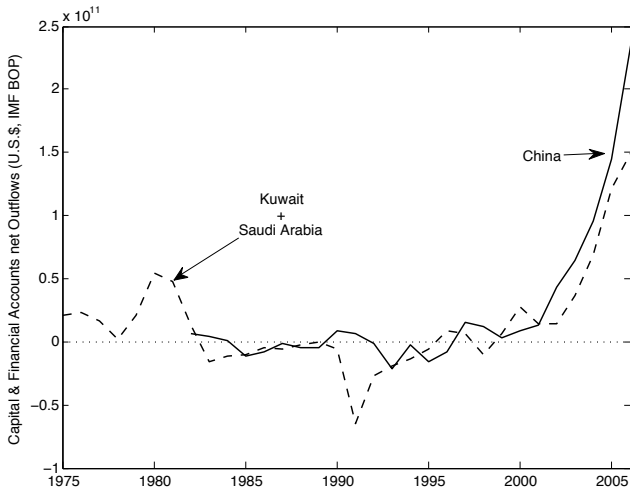
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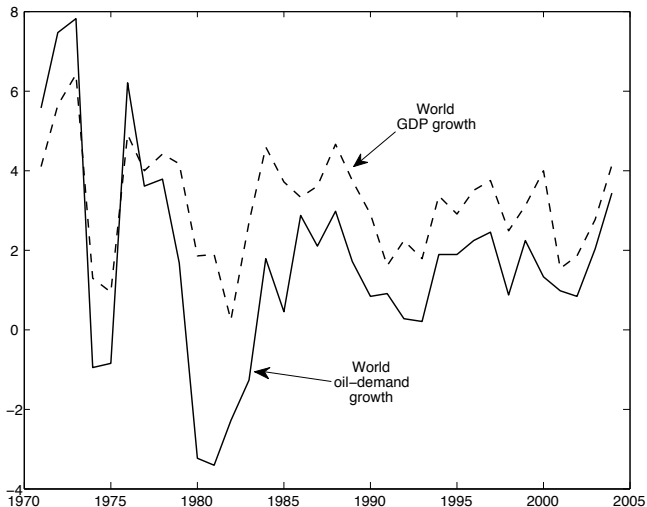
It's Not All About China

Contagion + Petrodollar Flows Have Contributed Substantially to Bubbles & Inflation



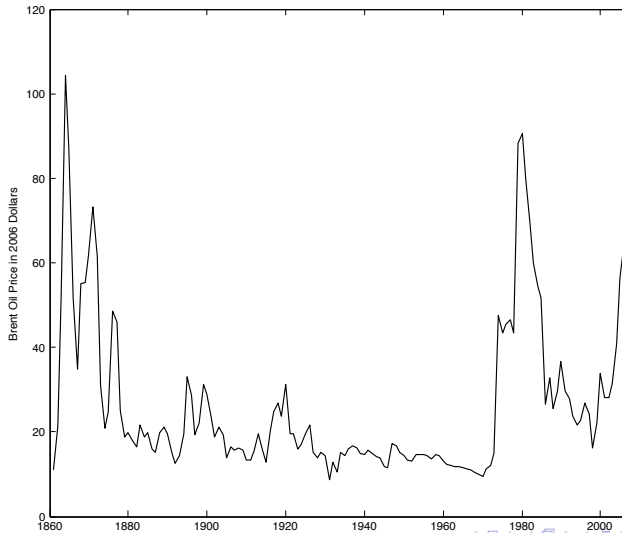
Self-Perpetuating Cycle, Magnified during Financial Crises

Reduced Long-Term Dependence on Oil?



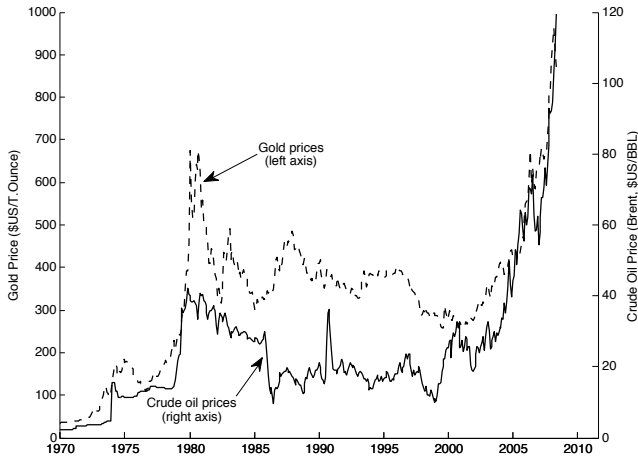
Coincidence of High Oil Prices with Financial Crises

Currency & Banking Crises Severest 1850s-70s, 1970s-



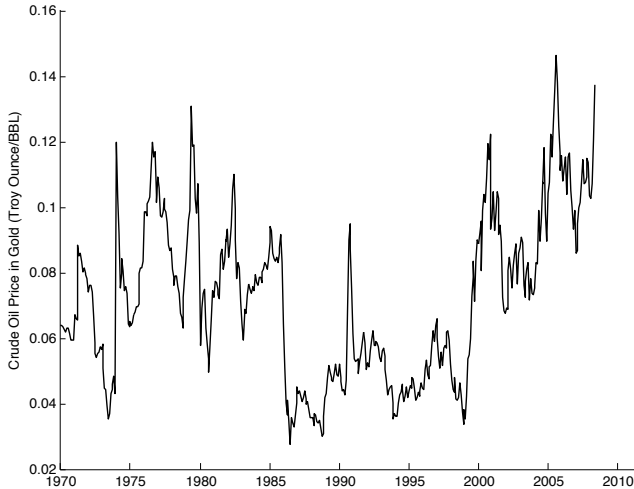
Post-Bretton Woods

Declining Real Oil Prices Precede Jumps



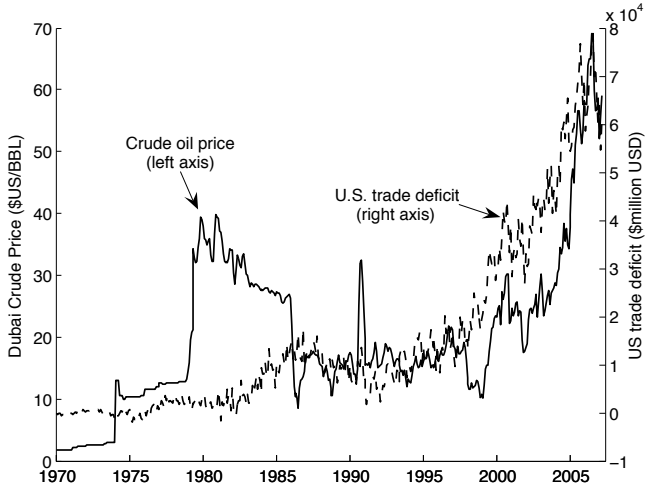
Post-Bretton Woods

The Gold Price of Oil



Post-Bretton Woods

Trade Deficits, Debts, Debased Dollars, and Oil



Fast Solutions (Cheap Money) and Long-Term Crises

Long-Term Solutions Are Known: Political Will Is Lacking

- Stop inflation before it becomes uncontrollable
 - Requires Volker resolve
- Gradual transition from Dollar-system – checks and balances
 - Bretton Woods III
- Reduce dependence on hydrocarbon fuels, esp. in transportation
 - Environmental dividends
- Increase absorptive capacities of Asia – reduced saving rates
 - Increase U.S. savings rates, balance growth and stability
- Increase absorptive capacities of Middle East – education & reform
 - Reduce geopolitical risks that amplify the petrodollar cycle

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