The NATIONAL INTEREST FOUNDATION

The Economic Impact of the Ongoing Red Sea Crisis

The ongoing Red Sea crisis in which Yemen's Houthis have been attacking commercial shipping vessels traveling through the seawater inlet over the past several months has had a significant impact on trade, shipping, and the global economy. The Red Sea is one of the world's most densely-packed shipping channels and sits south of the Suez Canal, a key trade route connecting Europe to Asia and East Africa. Approximately 12% of global trade passes through the Red Sea, including 30% of global container traffic. Due to the high volume of goods and supplies which utilize the inlet, any delays or interruptions can have a serious effect on gas prices and the availability of products on the worldwide market. The crisis has caused an array of major shipping companies to suspend traffic through the Red Sea, and has forced many ships to be diverted around the Cape of Good Hope, on the southern tip of Africa, increasing journey time by up to two weeks. Back in mid-December, oil giant BP even decided to pause its transits as well. Additionally, insurance risk premiums for sailing through these high-risk areas have also been on the rise. As a result of the crisis and its ramifications, global trade itself fell by 1.3% between November and December.

Economic experts have outlined some of the most noteworthy impacts stemming from the Red Sea crisis. Trade between Asia and Europe, for example, has faced a massive effect because of the Suez Canal serving as such a vital gateway between the two regions. In recent months, the rate for a 40-foot container from North Asia to Europe has skyrocketed more than 600%. Shipping costs between Asia and the United States are also spiking, with these rates ballooning by 137% and 131% respectively for the same size containers between North Asia and the East Coast and West Coast of the United States. According to analysts, the increases in global shipping costs could also exacerbate consumer price inflation in the coming months if they lead to higher final goods prices. Commentators have also been keen to point out that the degree of the overall economic impact of the Red Sea disruptions will ultimately depend on how long the threat carries on. Since consumer prices change relatively slowly, it might take months for them to react to the rising shipping and transportation costs.

The potential threat to energy prices is also considerable because the Red Sea, especially via the Suez Canal, is a huge connecting point between Europe, Asia, and Africa, and a location where much of Europe's energy supply travels through during normal times. In the aftermath of BP's decision to suspend shipments through the Red Sea, oil prices rose nearly 2%. Prior to this, oil prices had fallen for seven consecutive weeks – the longest stretch of unbroken declines since late 2018. If the Houthi attacks in the Red Sea began to be targeted towards oil tankers and bulk carriers, this would particularly have detrimental consequences on energy prices and the global economy at-large. A prospective spike in energy prices might in turn have substantial spillovers to other commodity prices as well. Higher container transport costs, which have been almost twice the level that they were back in early December, could also boost world inflation.

In response to the ongoing Red Sea crisis, the United States assembled a multilateral naval security task force to carry out patrols in an attempt to safeguard vessels against attacks named *Operation Prosperity Guardian.* The military operation has shot down Houthi drones and intercepted missiles launched at transiting ships. The Houthis have carried out dozens of attacks on commercial vessels since mid-November. Since the U.S.-led operation to protect against the attacks was launched, it has been estimated that around 1,500 merchant ships have safely transited the waters of the Red Sea. This week, U.S. Secretary of State Antony Blinken warned that there will be consequences for the continued Houthi attacks in the Red Sea. This followed Tuesday's reports of the U.S. Navy shooting down 21 Houthi missiles and drones launched from Yemen, in one of the largest Houthi attacks to take place in the Red Sea over recent months. On Wednesday, the United Nations Security Council passed a U.S. and Japan-led resolution condemning the Houthi attacks on merchant and commercial vessels in the last two months. The resolution was adopted despite abstentions from Russia and China. Then yesterday, the U.S. and the U.K. launched strikes against Houthi military targets in Yemen, hitting various strategic sites there in an effort to disrupt the Red Sea attacks. The Houthis have vowed retaliation, and while it remains to be seen what transpires in the coming days and weeks, the risk of further escalations in addition to the continued economic and diplomatic fallout, are certain to only increase the longer the crisis carries on.