Fuel, munitions and food: the mounting toll of Trump's Iran war

Conflict is reverberating across the US economy at cost of hundreds of billions of dollars in lost output

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Donald Trump's Iran war is ripping across the US economy at a cost of hundreds of billions of dollars in lost output, as soaring fuel prices, rising borrowing costs and supply chain snags erode Americans' prosperity.

While early estimates by the Trump administration have put the direct price tag to US taxpayers at $25bn, economists foresee a far larger toll once the full military bill and higher financing costs are considered.

"The budgetary costs that have been announced are really just the tip of the iceberg," said Linda Bilmes, a Harvard professor and expert on the cost of US conflicts. "It might not be felt immediately — you can patch something up for a while. But the scale of this financially is such that you can't cover it up forever."

The conflict comes at a time when Trump's popularity is already near record lows, fuelled in part by a worsening cost-of-living crisis that has left many Americans struggling to make ends meet.

"War remakes the economy in really fundamental, profound and expensive ways," said Justin Wolfers, professor at the University of Michigan. "I'm not for a moment saying it's not worth it — that's a judgment based on what you think the benefits of war are. But if you want cheap gas and more groceries, this is the wrong way forward."

The Pentagon's $25bn estimate

The Pentagon has burned through years' worth of costly missiles and air defence interceptors during the conflict, which it says has been the primary driver of its $25bn estimate for the cost of the war.

US defence spending was already shooting up even before the crisis began, with Trump announcing plans to raise spending by around 50 per cent to $1.5tn between the current fiscal year and 2027. Those figures do not include the effects of the war.

The Pentagon plans to have the White House submit a supplemental request to Congress, but the amount has not been determined yet.

Status of crucial US munitions

Munition	Unit cost	Pre-war inventory (estimated)	Use in war (estimated)	Delivery time (months)
Tomahawk	$2.6mn	3,100	1,000+	47
JASSM	$2.6mn	4,400	1,100+	48
PrSM	$1.6mn	90	40-70	46
SM-3	$28.7mn	410	130-250	64
SM-6	$5.3mn	1,160	190-370	53
Thaad	$15.5mn	360	190-290	53
Patriot	$3.9mn	2,330	1,060-1,430	42

The budget and future supplemental requests represent "a lot of money" and it is "going to have economic knockdown effects", said Carlton Haelig, a defence fellow at the Center for a New American Security think-tank.

Haelig added, however, that the defence industry would "take years" to turn the new orders into new weapons "at the scale they're envisioning with this budget".

While defence boosts output, economists say the money would be better spent on education and infrastructure, which have higher so-called “multiplier effects” and a greater impact on Americans’ prosperity.

A $35bn fuel price tag

The closure of the Strait of Hormuz, through which a fifth of global oil supply flowed prior to the war, has pushed up US petrol prices by more than half to $4.55 a gallon, marking the most severe fuel shock of any G7 economy.

Diesel — a vital input for America’s industrial economy — has risen by a similar margin to $5.66, just shy of its all-time record of $5.82.

As of Friday, American consumers had paid an extra $35bn in petrol and diesel costs since the war began, according to Brown University’s Watson School of Public Affairs. That equates to about $268 per household or about the cost of a week’s groceries.

“The total cost of Nasa’s annual budget is $25bn, so we are well past that now,” said Jeff Colgan, a political science professor at Brown.

“It screams out what else we could have done with this money if we weren’t wasting it on extra fuel costs associated with a war that most Americans don’t seem to want in the first place.”

Research published this week by the New York Fed found that, while households in the top third by income distribution had barely cut back at all on petrol use, those in the bottom third were now consuming 7 per cent less, resorting to carpooling and public transport to deal with the economic hit.

Still, higher fuel prices are a net positive for at least one group: US oil producers. The country is shipping more than it ever has and exporters brought in a record $214bn in March.

“The people who benefit are the owners of the oil and gas wells in the US that are getting higher prices — but those tend not to be poor people,” said Joseph Gagnon at the Peterson Institute for International Economics.

Jet fuel, meanwhile, has risen by more than 70 per cent, driving up the cost of airfares and placing huge strain on the airline industry. The war has already hastened the demise of budget carrier Spirit Airlines.

The $200bn loss from higher interest rates

In late February, before the conflict began, investors expected the Federal Reserve to cut US borrowing costs by a quarter-point twice this year.

But any support the US central bank could have provided to ease strains in America's lacklustre labour market now appears to be off the table, as soaring fuel prices drive inflation to a three-year high of 3.5 per cent to levels well in excess of rate-setters' 2 per cent goal.

Lower interest rates fuel demand, driving up investment and consumer spending, and boosting growth. Wolfers estimates the Fed's inability to cut interest rates by half a percentage point will have a substantial hit. "That one channel alone adds up to about $200bn worth of lost output," he said.

Higher rates are also costing would-be American homeowners dearly. The average 30-year mortgage rate — the industry standard — is now 6.37 per cent, up from 5.98 per cent before the conflict began.

Bilmes warned that the eventual bill could also be "quite destabilising" to taxpayers at a time when the costs of financing the US government deficit are creeping higher and higher.

"In 2003, when we went into Iraq, we were spending 4 per cent of the budget on paying interest on the debt. And now we are already paying 15 per cent," said Bilmes. "So that puts a pretty big squeeze when you're already paying 15 cents of every tax dollar on interest — and then we're simply adding on more."

The mounting costs of chinks in supply chains

The New York Fed's monthly gauge of global supply chain pressures is now at its highest level since the coronavirus pandemic.

Shortages in some raw materials are beginning to emerge, while the costs of shipping metal containers around the world at short notice have jumped.

"Even the Transatlantic from North Europe to US East Coast — which does not call at Asia transshipment hubs or Middle East ports — short-term freight rates have surged 56 per cent from end-February," said Peter Sand, of shipping data specialists Xeneta. "The crisis is still very much present — it has simply migrated from the regional to the global level."

Austan Goolsbee, president of the Chicago Fed, said this week that, despite the shocks of the Covid era, many manufacturers in his industry-heavy district were still heavily reliant on "just-in-time" delivery.

"At any given moment, all the parts, components and supplies are not sitting in a warehouse somewhere. They're on a truck or on a ship or on a plane being sent," Goolsbee told journalists on Wednesday. "So the price of fuel makes a huge direct difference on the transportation costs of their supply chain."

The impending ripple effect on food costs

Economists expect a roughly six-month lag until the higher costs of diesel translate into a noticeable rise in grocery prices, with perishable goods such as fruit, vegetables, meat and seafood, which rely on refrigeration and rapid distribution, likely to lead the way.

"Those are what I would call the canary in the coal mine in terms of where we would expect to see higher prices show up," said David Ortega, a food economist at Michigan State University.

There are already signs that the higher price of diesel is having an effect on input costs. Bank of America tracked a jump of 7.9 per cent in the costs borne by packaged food and beverage companies in March.

The hit from diesel is set to be compounded as farmers shell out on higher fertiliser costs. The price of nitrogen fertiliser, much of which is produced in the Middle East, has risen more than 30 per cent since the war began, which could curb crop harvests over the coming year as farmers cut back on fertiliser, shrinking food supply and driving up costs.

The impact of the Iran war on food prices is expected to be less than what followed Russia's full-scale invasion of Ukraine, a critical agricultural supplier to the world. Grocery price inflation surged to more than 13 per cent in August 2022.

Still, economists warn it is the latest blow to a sector that has been rocked by Covid, the Russia-Ukraine war, tariffs and the impact of immigration policies on labour supply, each fuelling inflation for US consumers. Food costs have risen about 30 per cent in the past six years.

"This is the latest shock that the agrifood system has faced in the past few years," said Ortega. "We're looking at a bit of a perfect storm here."