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What the Iran War Means for Europe's Energy Sector

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Comparisons with the Russian invasion of Ukraine have been inevitable as the conflict in Iran has raged over the past few weeks. However, while most European countries were heavily reliant on Russian natural gas, the curtailment and destruction of energy supply from the Persian Gulf is less direct and severe for Europe.

Roughly 10% to 15% of European oil comes from the region (primarily Saudi Arabia and Iraq),[1] and only 4% of natural gas supply,[2] although some countries like Italy and Belgium have much greater exposure to Qatari LNG (~40% to ~45% of their LNG import).[3]

Similarly, natural gas provides ~17% of European power (again with much higher percentages in a few countries like Italy, the Netherlands and the UK), in contrast with the U.S. where it accounts for over 40% of power generation output and capacity. Does this rather limited dependence on Persian Gulf energy, and more specifically natural gas, mean Europe has largely been spared any real impacts from the conflict?

The answer is a resounding "no" because of the way European energy markets operate. As a result of competition between Europe and Asia for flexible LNG cargoes, pricing is determined by which market is willing to pay more at any given moment. Notably, the Iran conflict has had the distinct impact of creating both a physical supply shock and a crisis bidding environment that has spanned both markets. This has severely affected the availability of physical supplies in Asia, a primary destination for Gulf LNG flows. European impacts have been primarily price-related, as they compete with Asian markets for available supply, rather than involving physical scarcity. In this environment, average European natural gas prices have increased by ~70% (100% at the recent peak). So far, this has had minimal impact on power prices in most European countries (Italy excepted) as power generators have drawn down gas storage, but Europe's energy-intensive industries like metal, glass and chemicals have experienced substantial pressure on their share prices (~20% declines for steel makers) and Europe is now entering its critical gas storage refill season with exceptionally low storage levels.

How will Europe respond in the near- and medium-term to this latest crisis, and what will it mean for the European energy sector going forward? In the immediate term, Europe has a limited but consequential set of options.

1. Will this lead to extended supply of Russian gas into Europe?

Possibly, depending on the duration of disruption. Europe has rapidly weaned itself off Russian gas since the invasion of Ukraine, with import share dropping to 13% in 2025 from ~40% in 2021. Under current European Union law, this is set to continue to decline over the next two years to approach zero Russian imports. This supply has been replaced by LNG, led by the U.S. (~25% of gas imports), while Qatari LNG only accounted for ~4% of total gas imports in 2025 (impacts also vary by country; Italy, for example, imported ~45% of its LNG from Qatar in 2024).[2,3] If the price surge remains acute, there will be considerable debate within Europe about whether it can undo four years of progress on

[1] EU imports of energy products - latest developments - Statistics Explained - Eurostat
[2] Where does the EU's gas come from? - Consilium
[3] Italy Natural gas, liquefied imports by country | 2024 | Data

Russian energy and geopolitics just to avoid the potential cost and risk of U.S. LNG as Asia competes for supply in the spot market, where prices have increased from 10 $/MMBtu to 25 $/MMBtu in the past month. As Europe faces a tighter gas market heading into storage refill season, there may be some discussion of delaying Russian LNG phase-outs as a way to offset Iran war impacts.

2. Will the Iran war lead to delays to decarbonization targets?

Probably, but subtly. Decarbonization targets were already under scrutiny in recent months given their impact on export competitiveness and consumer affordability. The Iran war has triggered serious near-term discussions, mostly by Germany's Minister of Economy and Energy, on potential adjustments or even suspensions. Near-term measures are focused on managing carbon price levels and volatility, including providing free allowances to industry, front-loading allowance issuance and increasing funds for stabilizing carbon prices. The potential for this intervention, combined with earlier political pressure for ETS reform along with reduced demand due to higher electricity prices, has (ironically) led to relatively flat carbon prices since the start of the war.

3. Will governments step in to subsidize industry and/or consumers?

Yes. Industrial energy subsidies have already been under discussion after the EU updated state-aid rules in 2025, most notably in Germany. If gas prices continue to rise, noting they reached 6x current levels in February 2022, additional subsidies for the most energy-intensive industries (metals, glass and chemicals) may emerge. Cuts to electricity prices are also under discussion. The question is the sustainability of these subsidies, given starkly competing exigencies of affordability for export competitiveness and the need to retain fiscal and monetary stability. More fundamentally, blunting price signals that reflect scarcity also removes a powerful tool for addressing energy security threats.

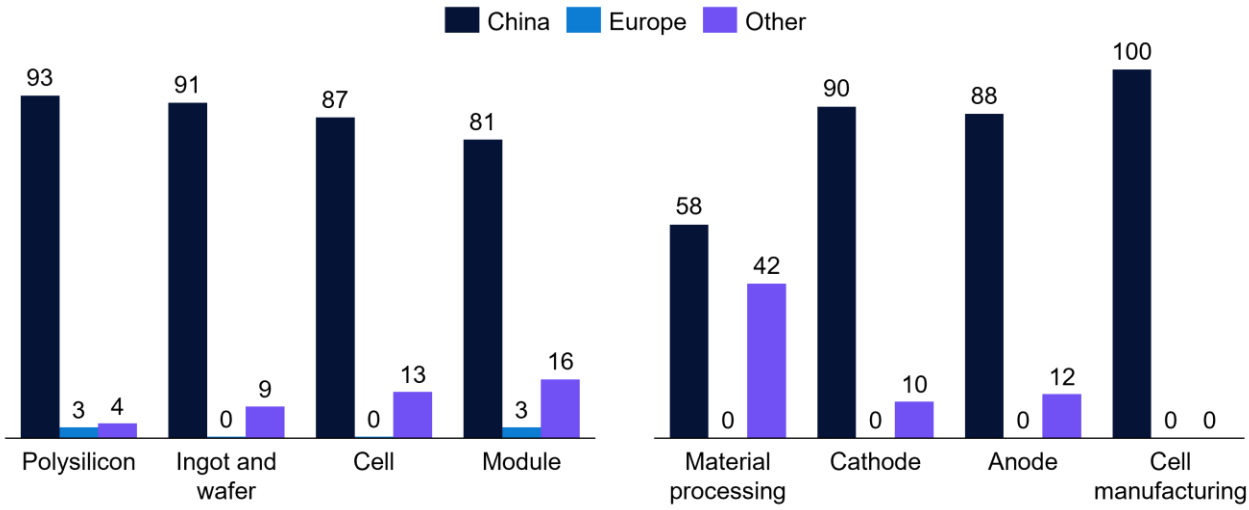
Medium-Term Implications

Self-sufficiency became a prominent theme in 2025 European politics as the U.S. increasingly appeared to pursue its perceived national interest unilaterally, without regard for the wishes of its European allies. The Iran war and Strait of Hormuz closure extends this theme from defense to energy.

This will mean reducing overall reliance on energy imports, as well as reducing the concentration of import exposure to particular countries or regions. For the most part, the Iranian conflict should serve to accelerate this process by improving political support for measures viewed as enhancing affordability for consumers and exporters, as well as regional security. Key trends are likely to include:

- **Reshoring renewables and storage** would provide a purely domestic source of energy by mitigating Chinese control of renewable supply chains (especially solar and storage). Current progress has been slow (see Figure 1 below), but the proposed EU Industrial Accelerator Act may finally provide a supportive solar and storage manufacturing environment.

Figure 1: 2025 solar (left) and Li-ion storage (right) supply chain concentration [%][4,5]



[4] Reshoring Solar Manufacturing to Europe - SolarPower Europe
[5] China's hold on the lithium-ion battery supply chain: Prospects for competitive growth and sovereign control - ScienceDirect

- **Reviving nuclear** power generation would significantly insulate domestic electricity production given the much longer fueling cycle of fission versus hydrocarbon-based generation (with supply measured in years versus days of storage). In the medium term, the greatest potential may lie in restarting mothballed units (~2 GW in Belgium) and extending operating licenses (up to ~5 GW). Construction of new units at existing plants could represent another ~30 GW (~30% of current capacity), but even under accelerated permitting and construction regimes, this would be unlikely before the early 2030s. The construction of small modular reactors will also be unlikely in this decade. Even further out is fusion, which European governments are investing in relatively aggressively (led by the UK and Germany with £2.5B and €2B committed, respectively, among others).

- **Accelerating electrification of space heating and transportation** eliminates exposure to imported hydrocarbons. Adoption of heat pumps has been limited by high electricity prices compared to gas and consumer resistance to retrofitting. A combination of higher relative prices for natural gas and renewed political resolve could overcome the stalled adoption rate. In the case of transportation, unlike the U.S. case where EV adoption fell from its 10% peak in 2024, electrification has continued to grow across most European countries throughout this decade, reaching ~25% of new car sales in 2025. The resulting challenge for Europe from its successful electrification push will be to fund and execute grid upgrades (assets, regulations and operations). These are overdue both at the distribution level, to support this load, and at the transmission level to integrate yet more renewables reliably and eliminate persistent transmission constraints between countries.

- **Insulating natural gas supply** from geopolitical price and supply risk will be an obvious lesson from the past few years but challenging to accomplish. Significantly boosting European oil and gas production, primarily in Norway and the UK, is possible. But those resources' relatively high lifting and total production costs may require some form of policy underwriting (e.g., price floors and/or changes in tax and royalty regimes) to induce investment. Accelerating pipeline and interconnection capacity to North Africa and Cyprus will provide more economical sources of supply but will face significant diplomatic and regulatory challenges, as well as their own geopolitical risks. The most obvious action to reduce geopolitical-related supply risk may well be to further diversify LNG sources, reducing the dominant (~45%)[2] share of the U.S., perhaps with higher shares from Algeria, the Atlantic coast of Africa (Nigeria, Angola, etc.) and very ironically, eventually Qatar.

In some respects, the European energy system reflects a rare, positive instance of the "law of unintended consequences." An intense commitment to decarbonization, combined with the recent geopolitical and economic shock of the Ukraine war, has set Europe on the path to a more resilient energy system. Addressing regulation-induced complexity and fragmentation, through administrative and capital market reform, would be another positive, if less likely, outcome of this most recent crisis.

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