

Europe's Second Energy Shock: Avoiding the Mistakes of 2022

Europe is experiencing the second major energy price shock in four years, triggered by the war in the Middle East. This development has revived a familiar policy question: how should governments respond to rising energy prices? The lesson from 2022 is to avoid broad-based fiscal interventions. Instead, the 2022 experience reinforces the case for a more disciplined approach: protecting vulnerable households, preserving price signals and limiting the overall fiscal burden. Such an approach is essential not only for fiscal sustainability and equity, but also for maintaining overall economic policy coherence (Amaglobeli et al., 2023).

Although the current geopolitical shock has strained global energy markets, its impact on Europe remains less severe than that of the 2022 shock. Brent crude oil prices in 2026 are projected to average around US \$95 (as of late May 2026), about 35% higher than in 2025 and close to the average price observed in 2022, and petroleum product prices have risen considerably. By contrast, European natural gas prices, as captured by the Dutch TTF benchmark, are projected to average €47.7 per MWh, about 30% above 2025 levels, but still well below the 2022 average of €121 per MWh. Should the crisis deepen, prices could climb higher: under the IMF's April 2026 *World Economic Outlook* "severe" scenario, oil prices could rise by 66% and European gas prices by 150% relative to 2025. Such a scenario could come with physical shortages of fuel, potentially disrupting some economic activity.

So far, EU households have felt the shock largely through more expensive transport fuels, which account for between 3% and 8% of household consumption spending, depending on the country (5% on average across countries). Looking ahead, under current pricing, the average EU household would lose approximately €375 (0.7% of consumption spending) in 2026 because of higher fuel and electricity prices; under the "severe" scenario, the average loss could rise to around €1,750 (about 3.5% of consumption). These magnitudes are well below the 8.5% recorded loss during the 2022 crisis.

Recent policy responses have again relied heavily on broad-based measures. While current fiscal costs – estimated at less than 0.2% of GDP – remain modest compared to a cumulative 2.5% of GDP in 2022-23, the composition of support raises concerns, particularly given the risk of rapid cost escalation under more adverse energy price scenarios (Celasun, 2026). The drawbacks of broad-based interventions, such as consumption tax cuts and price caps, can be assessed along several dimensions.

Distorted pricing. Broad-based support measures limit the pass-through of the increase in international prices to domestic consumers, weakening incentives for energy conservation and delaying necessary adjustments in both supply and demand. By contrast, targeted cash transfers allow prices to reflect scarcity conditions, thereby supporting efficient market responses.

Fiscal cost. Evidence from 2022 indicates that the absence of targeting significantly inflated fiscal costs, with approximately three-quarters of the total fiscal cost absorbed by measures that were either untargeted, price-distorting or both. As an illustration, International Monetary Fund staff estimates show that fully compensating the bottom 40% of households by income would have come at a cost of just 0.9% of GDP (Arregui et al., 2022). In other words, the limited use of targeting roughly tripled the bill relative to fully compensating the bottom 40% by income. During the cur-

David Amaglobeli, International Monetary Fund, Washington, D.C., USA.

Simon Black, International Monetary Fund, Washington, D.C., USA.

Oya Celasun, International Monetary Fund, Washington, D.C., USA.

Frederik Toscani, International Monetary Fund, Washington, D.C., USA.

rent shock, under the current pricing scenario, fully compensating the bottom 20% of households would cost 0.04% of GDP, rising to 0.19% of GDP in the severe scenario. This compares to costs of 0.2% of GDP from already announced measures, a significant part of which accrues to households. The contrast could hardly be starker.

Distributional implications. Broad-based measures that benefit all consumers may appear equitable. In reality, the equity argument for broad price subsidies is not merely weak – it is inverted. IMF staff calculations show that for every €100 of economy-wide price reduction, the richest 20% of households capture €34 via road-transport-fuel subsidies and €33 via electricity subsidies; the poorest 20% receive just €9 and €11, respectively. Untargeted measures are, in effect, regressive transfers from taxpayers to wealthier consumers.

Political economy. Broad-based support measures may be popular – with visible and immediate impact, such as lower prices at the pump. Yet they prove far harder to unwind, protracting the fiscal cost. Some of the relief measures introduced in 2022-23 are still in force, for example. By contrast, more limited and well-targeted support, combined with clear communication, can be equally effective at supporting vulnerable households while avoiding these pitfalls.

The 2022 energy crisis underscored that firms deploy a range of coping strategies in response to shocks – passing costs through to prices, as well as curtailing consumption, and accelerating efficiency investments (Amaglobeli et al., 2024). Preserving price signals is essential to incentivize such adjustments. Where support to firms is nonetheless deemed necessary, it should be temporary, carefully calibrated and narrowly targeted at viable but affected enterprises, rather than disbursed through broad subsidies (Ari et al., 2023). Importantly, firms already capture part of untargeted support provided to the economy, such as consumption tax cuts. Support should be conditional on investments that facilitate the energy transition, with eligibility criteria designed to limit adverse selection and, where feasible, private-sector co-participation. Care must also be taken to avoid distortions to international competition, prevent overcompensation where firms are already restoring profitability, and guard against double compensation when costs can be passed through and households are already receiving relief.

Europe has the tools and institutional capacity to respond to the 2026 energy shock effectively, with well-targeted support costing a fraction of untargeted measures and delivering clearer distributional gains. Examples of well-targeted support do exist. For example, Bulgaria introduced temporary, targeted transfers aimed at the bottom 20% of the income distribution, with recipients of means-tested social assistance enrolled automatically, while other applicants undergo eligibility verification based on administrative tax records covering income and vehicle ownership. Outside Europe, in Thailand, households registered in the social registry are automatically enrolled to receive targeted support.

What is now needed is political resolve: to acknowledge that the shock, while real, is manageable; to resist costly untargeted subsidies; and to focus support on those most in need, thereby avoiding a repeat of the regressive approach taken in 2022.

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