How the war in Ukraine affects the price (and subsidy) of gasoline



Is the war in Ukraine affecting gasoline prices and subsidies? How long will the increase in oil prices affect global markets?

Héctor Magaña, research professor at the Center for Research in Economics and Business at Tec de Monterrey's State of Mexico campus, shared his opinion and vision on the matter with CONECTA.

"The oil ban is one of the sanctions that the United States and several European Union countries have imposed on Russia.

"This situation has **lowered the supply of this resource** in the global market, which has resulted in an **increase in its price**," said the professor.



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Oil price increase

Magaña said that the war in Ukraine does not directly affect the price of the gasoline that we consume in Mexico, but there are negative effects in our country due to the rise in the price of oil. He went on to explain:

"Mexico is no longer one of the **world's largest oil producers.** PEMEX's production has decreased year after year and, consequently, our country **exports less oil.**

"Therefore, higher oil prices don't contribute significantly to public revenue. Mexico imports more gasoline than it produces so, to meet the demand for fuel, the country buys gasoline from other markets."

As oil is the **main input for the production of gasoline**, the researcher explained, if its price increases, consumers will have to pay a higher price for it.



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Mexico and the gasoline subsidy

Oil prices worldwide **have continued to rise** and, according to the researcher, one of the great challenges for the authorities in Mexico, and worldwide, is **the uncertainty of not knowing how long this situation will last.**

"The first strategy implemented by the Mexican authorities was to reduce the special tax (IEPS) on gasoline to prevent its price from rising significantly.

"But if the trend of increasing oil prices **continues indefinitely**, the current administration has declared that a **subsidy could be used to mitigate the increase in fuel prices** since it has practically eliminated IEPS on gasoline," he said.

To keep offering a subsidy, the Mexican government will have to rethink the expenditure budget, said the academic.

"However, doing this could affect some public programs in that they will receive fewer resources than originally planned. Some projects will even have to be suspended until the situation improves.

The longer the war in Ukraine lasts, the more complicated it will become to keep subsidizing gasoline Mexico.- Héctor Magaña

The professor said that **the world situation due to the war in Ukraine is quite complex**; on the one hand, public finances in Mexico **will stop receiving the income** expected from IEPS on gasoline.

"(...) and on the other hand, the public administration must allocate resources to subsidize the price of gasoline, resources that weren't included in the expenditure budget for the current year," he said.

According to the researcher, the prolongation of the conflict in Ukraine and the sanctions against Russia could cause **more public programs in Mexico to suffer budget cuts**,

"Resources are limited, and it will become more complicated to continue subsidizing gasoline in our country.

"Worst case scenario: some public programs may be suspended if the authorities consider that the gasoline subsidy should remain in place until the price of oil normalizes," said the researcher.



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Actions taken due to the high price of oil

Héctor Magaña talked about some of the actions that other countries have taken to mitigate the increase in the price of oil in a scenario where the **war between Russia and Ukraine** continues **for months or years.**

"The United States has released part of its oil reserves and several OPEC members have agreed to increase oil production to cover the number of barrels not purchased from the Russian market, thereby increasing the available supply.

"However, the above has had little impact on international markets and the price of hydrocarbons keeps increasing," said the professor.

Héctor asserts that so long as there is a limited supply of oil, the outlook is unlikely to improve, at least until the war ends and Russian oil can once again be marketed internationally.



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The professor added that we should also **keep an eye on inflation** because Mexico had already been suffering significant inflation **before the conflict between Russia and Ukraine.**

"One of the goods that contributes most to a general increase in prices is precisely **gasoline**. "Which is why the current federal administration is **taking measures to mitigate the increase in fuel prices,**" he concluded.

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