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Mexican Consumers Pay More at the Pump Despite Sharp Drop in Global Oil Prices

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While gas prices have fallen sharply in the US since the last quarter of 2014, Mexican consumers started 2015 by having to pay more at the gas pump despite a significant decline in international prices. The American Automobile Association (AAA) said US consumers were paying an average of US$2.26 per gallon for regular unleaded gasoline on Jan. 1, 2015. In Mexico, the price at the pump was 13.57 pesos (US$0.92) per liter, the equivalent of about US$3.50 per gallon. The price of premium was 14.38 pesos (US$0.97) per liter, which is about US$3.66 per gallon. Diesel sold at 14 pesos (US $0.94) per liter at the start of the year, the equivalent of US$3.55 per gallon.

The discrepancy is attributed to a mechanism implemented by former President Felipe Calderón and the Congress in 2008 to stabilize gasoline prices at a time when international gas prices were very high (SourceMex, Jan. 16, 2008). Through this scheme—used for the last time on Jan. 1, 2015—the government provided direct subsidies for gasoline while recovering some of those costs through gradual increases in the price of gas sold at the pump. Between 2008 and 2013, the administration disbursed about US$852 billion to subsidize gasoline prices.

The subsidies were invisible to the Mexican public, but consumers certainly noticed the gasoline taxes that were imposed on a monthly basis, beginning in January 2008, which led to the term gasolinazo. Because of the monthly taxes, which were intended to fund programs for states and municipalities (SourceMex, Sept. 19, 2007), gasoline prices have increased by almost 96% for unleaded regular (known as Magna), 69% for Premium, and 142.1% for diesel in the past six years.

Price-stabilization scheme, low refining capacity mostly to blame

The government's need to create this scheme was partially the result of Mexico's lack of refining capacity, which has forced the state-run oil company PEMEX to import roughly 40% of the gasoline consumed in Mexico and left the country more vulnerable to international price swings.

The scheme was favorable when international gas prices were high, which was the case between 2004 and 2008. The Mexican government kept the system of subsidies and retail taxes in place even when international prices dropped significantly in mid-2008 to close the year at about US$32 per barrel. While prices eventually rebounded above US$100 per barrel in subsequent years, a sharp downward swing occurred in the fourth quarter of 2014, as a standoff between US producers and the Organization of Petroleum Exporting Countries (OPEC) resulted in a glut of oil. In the last quarter of 2014, the price per barrel of Brent oil fell from US$102 to US$70.5, while a barrel of West Texas crude oil fell from US$90 to US$66.

Observers noted that the price controls that Mexico has exerted for the past several years had become a disadvantage for a country that has traditionally been one of the world's top producers of crude oil. "In the US, the price of fuel is determined by supply and demand, while the price of gasoline in Mexico has continued to increase because the price is controlled by the government," said the daily business newspaper El Economista.

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The contrast in policies created marked differences in gasoline prices along the US-Mexico border on Jan. 1, 2015. Even though gas prices are typically much lower in Mexican states bordering the US than they are in the interior, there was enough of a gap in prices to prompt some Mexican consumers to cross into the US to fill their tanks. The daily newspaper Excélsior reported that gasoline stations in the Texas cities of San Antonio and McAllen were selling regular unleaded gasoline at an average of US$1.70 per gallon at the start of the year, compared with a cost of 7.97 pesos per liter (about US$2.05 per gallon) in neighboring Tamaulipas state.

The situation was similar on the western end of the US-Mexico border, with prices in the San Diego area more attractive to Mexican consumers despite the imposition of a new environmental tax on gasoline by the state of California. "I remember when the situation was the reverse, when [US residents] were coming to Tijuana to fill their tanks," a Tijuana resident told Excélsior, referring to 2008, when gas prices in Southern California hovered around US$5 per gallon.

Many residents of Baja California do fill up their tanks in California, but they do this in conjunction with other activities. "In general, [residents of our state] are crossing into the US for other purposes, primarily to go shopping," said economist Alejandro Díaz Bautista of the Colegio de la Frontera (COLEF). "While they are there, they take advantage of the difference in prices to fill up their tanks."

Changes coming

The rise in gas taxes that went to effect on Jan. 1, 2015, marks the end of the gasolinazo. President Enrique Peña Nieto decided to continue with the subsidy-taxation policy employed under Calderón during the early part of the administration in an effort to ensure little market disruption while awaiting the approval of energy reform. When energy reform was approved in 2013 (SourceMex, Dec. 18, 2013) and specific rules set in 2014 (SourceMex, Aug. 6, 2014), the administration took steps to phase out the gasolinazo. "Mexico cannot remain the same," the president said in a national address on New Year's Day. "We have to make changes for the good of all."

Under the plan announced by the Peña Nieto administration, there will cease to be a single price for gasoline and diesel, and instead a ceiling will be imposed, allowing consumers to acquire the fuels at below maximum prices as competition between gas stations brings prices lower.

"The government will be setting a maximum price from now until 2017 ... (but) there will be competition among transport companies, storage operators, service stations," deputy finance secretary Miguel Messmacher said in an interview.

Under the energy reforms implemented last year, the government will remain directly involved in the fuel market through the end of 2017. In 2018, full competition will be allowed including private management and ownership of gasoline stations.

"In three years, the PEMEX monopoly on franchises will cease to exist, and service stations will be able to acquire franchises of other brands of gasoline," columnist Adrián Ortiz Romero Cuevas wrote in the online news site Tiempo en Línea. "In this way, the PEMEX logo will cease to be the only one in existence, and we could see other brands of fuel, something we have never seen in Mexico."'

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Messmacher said the tax reforms approved by Congress and enacted in 2014 (SourceMex, Oct. 23, 2013, and Nov. 20, 2013) will provide the federal government with sufficient nonpetroleum income in 2015 to fund the federal budget, eliminating the need for monthly taxes on gasoline.

As part of the change, the government will also end the subsidy of 35% on the price of gasoline, meaning that the global market will now provide the reference price for gasoline sold in Mexico. Some analysts say this change could create some problems down the road. "So if the cost of fuel rises in the global market, the immediate consequence is that it will also rise in Mexico," Romero Cuevas wrote in Tiempo en Línea.

Romero Cuevas said there is no way the Mexican oil market can reduce the impact of global trends as long as Mexico continues to import 40% of its gasoline. Even if prices remain stable or decline, he said, the chances are slim that Mexico would see any significant reduction in prices unless competition increases significantly in Mexico. The energy reforms could bring new capital into Mexico's refinery sector, but this could take a few years to become a reality.

While Congress welcomed the end of the gasolinazo, members of opposition parties questioned why the final price increase at the beginning of 2015 was even necessary, even though the price increase was only 1.9% instead of the projected 3%.

Sen. Dolores Padierna, one of the leaders of the center-left Partido de la Revolución Democrática (PRD) in the upper house, suggested the increase would affect the cost of fuel and transportation, which would raise the cost of foodstuffs and other products purchased by the general population. "This new increase is going to have a general impact on prices, but especially those that are part of the basic basket of goods," said the PRD senator.

Sen. Silvia Garza of the conservative Partido Acción Nacional (PAN) pointed out that the trucking industry, which moves about 80% of the cargo in Mexico, would feel a major impact. Like Padierna, Garza worried about the impact on the pocketbooks of ordinary Mexicans. "Because of the low salaries that our workers receive, many families will not be able to compensate for this increase in costs," said the PAN senator.

Legislators also worried about Mexico's competitive disadvantage relative to other countries. "With this new increase, the price of gasoline in Mexico will be 23.5% more expensive than in the US," said Padierna. [Peso-dollar conversions in this article are based on the Interbank rate in effect on Jan. 7, 2015, reported at 14.78 pesos per US$1.00.]

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