

MEXICO – Macroeconomic Risks of Energy Shocks

- ▶ The macroeconomic consequences of the ongoing conflict in the Middle East will depend on the conflict's duration, global escalation, and the degree of disruption to supply chains. Drawing on earlier episodes, we identify the main transmission channels and plausible fiscal and monetary outcomes.
- ▶ If international energy prices spike while the government contains domestic pump prices through subsidies, short-term headline inflationary effects can be muted. We identify two channels of impact. First, the gasoline channel where subsidies dampen short-term inflation. We estimate that a 10% increase in oil prices would raise headline inflation by roughly 0.1 percentage points over the first six months. Second, the exchange-rate channel, where the correlation between international oil prices and the real exchange rate is low, and exchange-rate pass-through to inflation is minimal—especially in the presence of a negative output gap.
- ▶ Higher fertilizer prices also pose upside risks to the inflation outlook. We expect the initial impact to materialize in protein prices around mid-2026, driven by feed cost pass-through. By summer, food inflation is expected to broaden across categories.
- ▶ Considering all possible scenarios, Banxico should wait before easing policy further. In the May 26 meeting, the central bank should shift its inflation risk balance to the upside to incorporate the geopolitical conflict. In addition, the oil shock may also prevent easing by the Fed, which somehow limits Banxico's elbow room. Given the new volatility environment, it seems likely that policymakers will opt to remain on hold for now at 7.0%. We continue to expect a terminal rate at 6.5% in 2026, with rates likely to remain at that level through 2027.

This study examines Mexico's evolving position in the global oil market from a macroeconomic perspective and synthesizes historical evidence on how past energy shocks—whether price-driven or supply-driven—have transmitted to the Mexican economy. We use those lessons to assess the likely macroeconomic and fiscal consequences of the current energy disruption stemming from the Iran war.

Mexico is no longer an energy powerhouse

Over the past four decades Mexico has undergone a structural shift from an oil-centric economy toward manufacturing-led growth. Trade liberalization, maturation and natural depletion of legacy fields, and weak investment in upstream capacity have all contributed to this transformation.

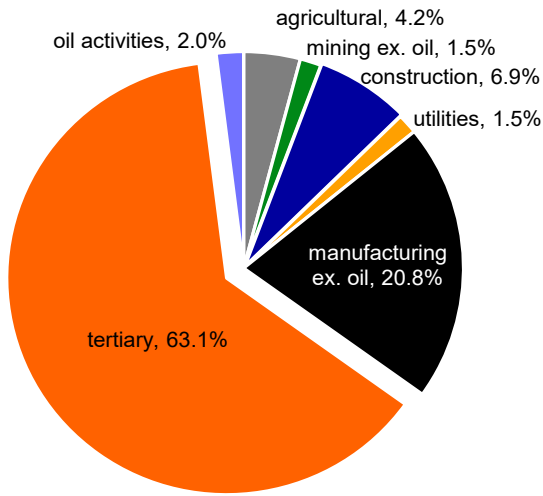
Oil production has declined steadily, reaching record lows in 2025. Falling output from mature fields was not offset by new discoveries or sufficient capital expenditure; operational inefficiencies further compounded the decline (see [Pemex and sovereign risk](#) for a deeper discussion). By 2025 oil-related activity contributed roughly 2% of GDP, while manufacturing accounted for about 21%. Ten years earlier oil activities represented approximately 6% of GDP and manufacturing 18%.

Mexico has been a net oil importer since 2014 and remains highly dependent on imported refined fuels and natural gas. In 2025 the oil trade balance recorded a deficit of USD 25.6 billion, the largest in two years. Petrochemical products now represent about 8% of merchandise exports, down from 15% a decade ago. The United States supplies roughly one million barrels per day of refined petroleum products to Mexico—around 70% of domestic consumption of gasoline, diesel and jet fuel.

Domestic natural gas production has declined, leaving electricity generation increasingly reliant on U.S. pipeline imports. Approximately 60% of Mexico's natural gas demand is met by shale gas piped from the Eagle Ford region in Texas, creating a critical dependence for Comisión Federal de Electricidad (CFE) and the wider power sector.

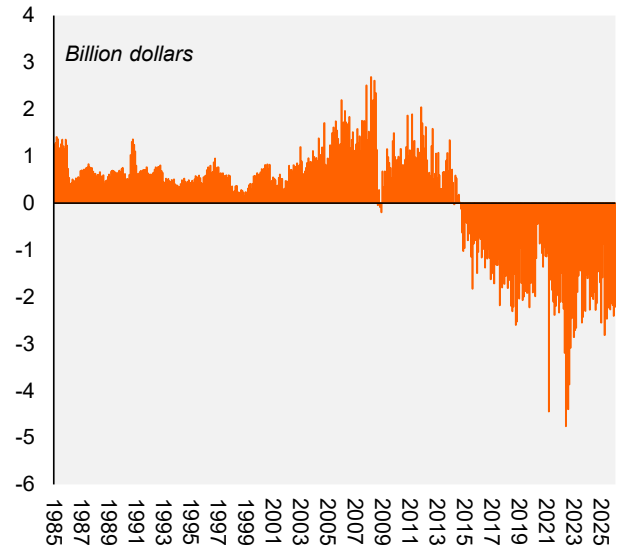
The fiscal significance of oil has diminished markedly. Oil revenues fell from an average 44.1% of budgetary revenues in 2008 to 10.8% in 2025, while tax revenues—boosted by the 2014 tax reform—rose to 73.4% of total revenues in 2025. This reallocation reduces the automatic fiscal buffer that oil windfalls once provided.

Sectors in 2025 (% total GDP)



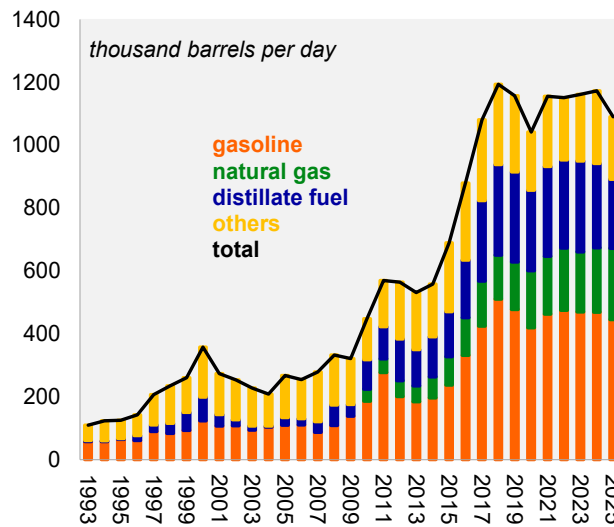
Source: INEGI, Itaú

Oil trade balance



Source: INEGI, Itaú

US Exports to Mexico of Crude Oil and Petroleum Products



Others include residual fuel oil, pet. coke, lubricants.

Source: EIA, Itaú

Historical energy shocks and their transmission in the economy

Limited strategic reserves¹ and heavy reliance on U.S. supply hubs amplifies vulnerability to external shocks — particularly when prices surge along the U.S. Gulf Coast.

An example of a supply shock in the economy is the natural gas shortage between the second quarter of 2012 through the second half of 2013—partly driven by Pemex’s increased gas use for enhanced oil recovery amid high crude prices²—forced industrial energy curtailments. Empirical work (Alcaraz & Villalvazo, 2016) estimates that a 10

¹ Official data is scarce; however, a rough estimation is about 15-20 days of emergency stockpiles.

² WTI stood at 91.82 USD/bbl. in 2012 and 98.42 USD/bbl. in 2013.

percentage points increase in gas shortages reduces manufacturing output by 0.32%. At the peak shortage in 2Q13, seasonally adjusted quarterly GDP would have been about 0.28 percentage points higher absent the disruption.

Another shock occurred in February 2021 when extreme winter weather in Texas froze pipelines and prompted the U.S. to prioritize domestic gas consumption, curtailing exports to Mexico. The resulting gas and power disruptions hit northern and central manufacturing hubs: in the 1Q21 industry contracted 0.3% QoQ, utilities fell 19.7% QoQ, and manufacturing dropped 0.3% QoQ.

The beginning of the Russia–Ukraine war in February 2022 produced a global energy price shock that pushed fuel costs sharply higher and fueled inflation worldwide. The Mexican government partially insulated consumers by subsidizing domestic fuel prices. Mariscal and Miranda (2024) estimate that subsidies reduced the effect on the output gap by roughly 0.6 percentage points, limited headline inflation by up to 4.4 percentage points, and prevented an additional 4.3 percentage-point rise in the policy rate at the peak.

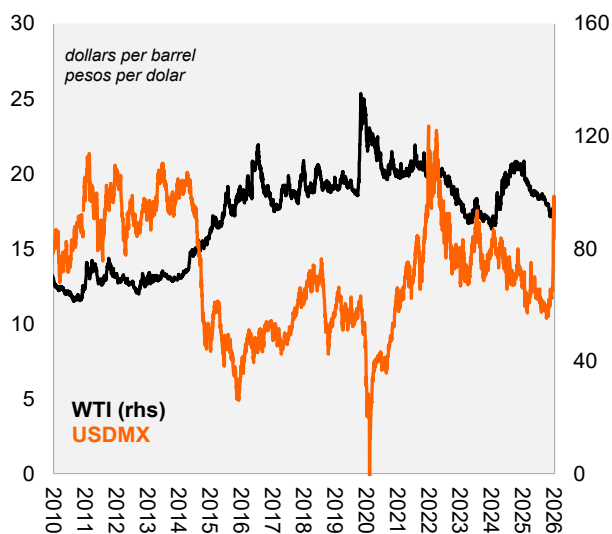
On the fiscal front, higher international oil prices had a dual effect on revenues. While they raise government and Pemex revenues, they simultaneously increase the cost of subsidies on fuels, eroding projected tax collections. In 2022 incremental oil revenues of 394.5 billion pesos (≈USD 15 billion, 1.3% of GDP) were almost entirely offset by gasoline subsidies of 395.4 billion pesos.

The ongoing conflict in the Middle East: transmission channels and scenarios for Mexico

The macroeconomic consequences of the ongoing strife in the Middle East will depend on the conflict’s duration, global escalation, and the degree of disruption to supply chains. Drawing on earlier episodes, we identify the principal transmission channels and plausible fiscal outcomes.

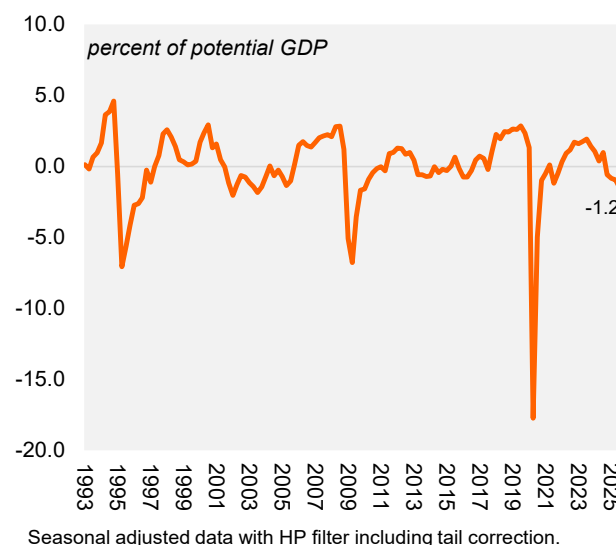
If international energy prices spike while the government contains domestic pump prices through subsidies, headline inflation effects can be muted in the short run. We identify two channels of impact. First, the gasoline channel where continued price containment (e.g., a maximum domestic price agreement at 24 pesos per liter) dampens short-term inflation. We estimate that a 10% increase in oil prices would raise headline inflation by roughly 0.1 percentage points over the first six months under such a policy approach. Second, the exchange-rate channel, where the correlation between international oil prices and the real exchange rate is low (≈0.11), and exchange-rate pass-through to inflation is minimal—especially in the presence of a negative output gap—reducing a second-round inflationary mechanism.

WTI and USDMXN



Source: Xx, Itaú

Output gap estimate



Source: INEGI, Itaú

The 2026 Budget assumes a crude price of USD 54.9 per barrel; each additional dollar per barrel translates into roughly 11.6 billion pesos (≈0.04% of GDP) in extra government revenue. **If the average crude price reaches USD 90/bbl, ceteris paribus, additional revenues could approach 400 billion pesos (≈1.4% of GDP).**

However, this gross benefit will be substantially eroded if the government expands fuel tax incentives or subsidies to shield domestic prices. Unlike 2022, fiscal consolidation constraints today limit the scope to finance large-scale subsidies without material trade-offs elsewhere in the budget.

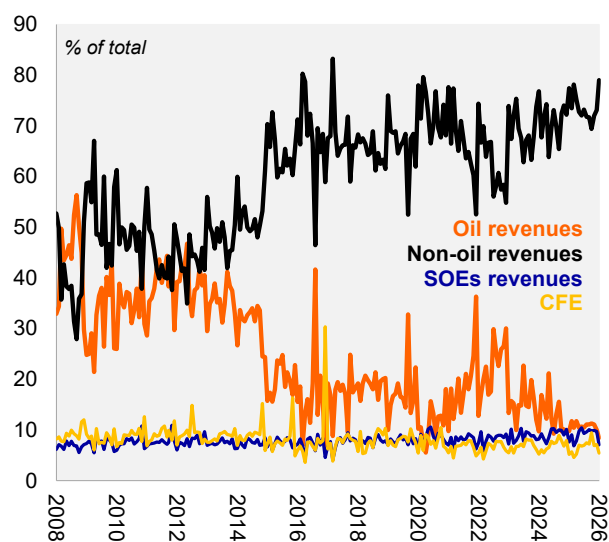
An extended or intensifying conflict could lead to higher prices associated to supply disruptions. U.S. policy priorities—protecting domestic supply chains and industrial stability—could lead to export curtailments during episodes of scarcity, replicating the transmission mechanisms observed in 2013 and 2021. Such actions would risk power-generation shortfalls, industrial disruptions, and acute fiscal pressure from simultaneous revenue swings and subsidy demands.

Higher fertilizer prices are also relevant. Roughly one-third of global fertilizer trade flows through the Strait of Hormuz, exposing supply to potential disruptions. Mexico remains particularly exposed, importing approximately 75% of its fertilizer demand; in 2025, fertilizer imports reached close to 3.8 million tons.

Mexico’s urea import cycle typically peaks between April and June—a key seasonal window that now aligns with rising supply risks from the ongoing Middle East conflict, which would expose domestic producers to both price volatility and potential shortages. The issue is compounded by persistently high urea prices and restrictions on Russian imports, limiting inventory build-up. We expect the initial impact to materialize in protein prices around mid-2026, driven by feed cost pass-through. By summer, food inflation is expected to broaden across categories.

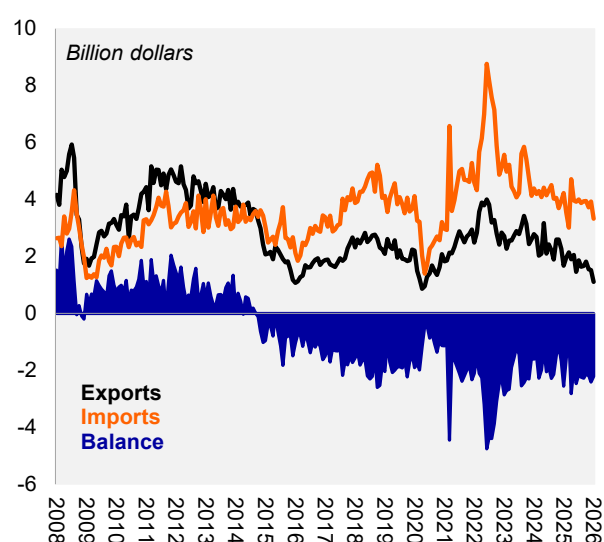
Considering all possible scenarios, Banxico should wait before easing policy further. In the May 26 meeting, the central bank should shift its inflation risk balance to the upside to incorporate the geopolitical conflict. In addition, the oil shock may also prevent easing by the Fed, which somehow limits Banxico’s elbow room. Given the new volatility environment, it seems likely that policymakers will opt to remain on hold for now at 7.0%. We continue to expect a terminal rate at 6.5% in 2026, with rates likely to remain at that level through 2027.

Government revenues



Source: MoF, Itaú

Oil trade balance



Source: INEGI, Itaú

Conclusion

Protracted and severe energy shocks place sustained strain on Mexico’s economy and public finances. Current policy efforts to raise domestic gasoline production are necessary but seem insufficient in the near term. Fiscal constraints, limited openness to private investment in the energy sector, and institutional weaknesses that undermine business confidence impede a rapid supply-side response and perpetuate reliance on refined imports.

Temporary consumer subsidies can blunt headline inflation but do not resolve underlying supply constraints. Price suppression during supply shocks tends to sustain elevated consumption while incentivizing suppliers to divert volumes to higher-priced markets or reduce deliveries—creating electricity disruptions, natural gas shortages and mounting fiscal burdens.

Policy priorities should include diversifying import sources and routes; accelerating investment in domestic refining and gas production under transparent and investor-friendly rules; and strengthening fiscal frameworks to manage volatile oil revenues without resorting to ad hoc subsidies. These measures would help Mexico better insulate growth and public finances from future energy shocks.

Julia Passabom
Mariana Ramirez

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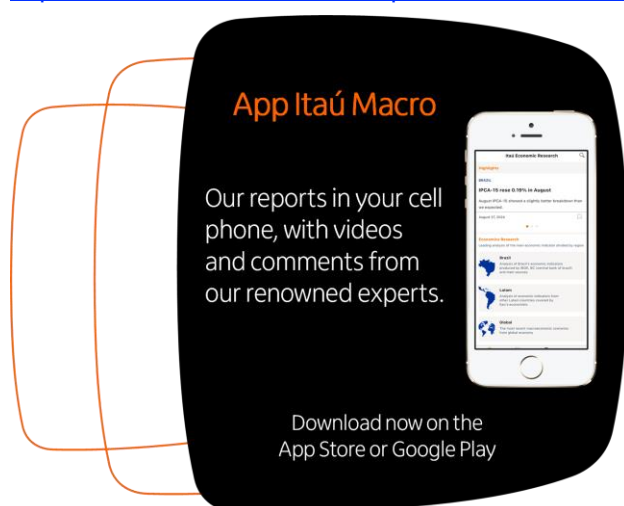
Mariscal, Rodrigo and Miranda, Axel (2014), “The Macroeconomic Impact of Fuel Price Controls and Excise Tax Subsidies in Mexico. Working Paper - Last update: September 2024.

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Mario Mesquita – Chief Economist

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