Summary

The Iran War has raised gas prices by about a dollar a gallon. That's not a serious hit for people in the upper part of the income distribution, but lower income people spend a high percentage of their income on gas. Especially for people in the bottom third or so of the distribution, the impact is significant. Increased gas prices are especially significant because other prices are also rising, tightening the squeeze on budgets. Gas prices aren't likely to go back to normal for months.

Commentators seem bemused by the intense political reaction to gasoline prices, which are up by about a dollar a gallon due to the Iran war. No doubt the reaction is accentuated because gas prices are highly visible. People buy gas frequently and even more frequently see signs posting the prices. But to a greater extent than many in the upper income distribution appreciate, the actual economic pain is very real.

Brookings researchers have unpacked the reasons. Over three-quarters of American workers use a car to get to work, and over 90% of shopping and errands involve cars. The length of the average trip has gone up from eight miles in 1985 to over eleven today, due largely to sprawl. In many areas, public transit is not a real option.

Because of the war, the median household earning $72,000 in post-tax income with two drivers is seeing a $72 increase in gas spending per month, which comes to 1.2% of income. Of course, some people drive a lot farther, especially in rural or exurban areas. Still, for people in the upper parts of the income distribution, this shouldn’t upset their budgets so much.

For the lower parts of the income distribution, however, the impact is much more painful. People in the bottom 20% of the income distribution spend about a tenth of their income on gas, so the ramp-up in gas prices is a bigger budgetary hit. As the Brookings researchers explain, for people in the bottom quintile, an extra $72 a month is equivalent to about a 5% paycut. People from the next quintile (20-40% of the distribution) spend only half as much of their budget on gas, but it’s still quite significant. And this is happening at a time when other prices are going up as well, partly due to the increased cost of diesel. It’s also coming at a time when people were already very glum about their economic prospects.

Gas prices are not likely to return to their old level this year. Even if the straits of Hormuz were opened tomorrow, it would take weeks for oil to reach market by tanker. Moreover, there has been considerable damage to oil and gas infrastructure in the Middle East, which could take many months to repair. More damage may be coming if fighting reignites. U.S. oil production has been slow to increase, since oil companies are unsure whether high prices will continue for the years required to pay for pricey new wells. Current price increases presumably won't be permanent, but the problem isn't going to go away quickly and might well get worse.