



PAUL R. PORTNEY

Why \$2/Gallon Gas Is Still a Good Deal

This letter will probably reach you in late July or early August—often referred to in the United States as “peak driving season.” For this reason, you may be in no mood to hear me say that we shouldn’t be complaining unduly about the recent increases in the price of gasoline. In fact, stop reading right now if you think the country needs gasoline price controls or, at the very least, a vigorous congressional investigation into prices at the pump. My message here will only spoil your day.

For at least three reasons, even gasoline at \$2.10/gallon (the average retail price in the United States at the time of this writing) is *not* the calamity that the media and many politicians make it out to be. First, when adjusted for inflation, gasoline is 25 percent less expensive today than it was in 1981, when it hit \$2.79/gallon. (Over this same period, real per capita income in the United States rose nearly 60 percent.) In fact, gasoline costs less today in real terms than it did in 1918 (when Henry Ford’s Model Ts had to be refueled at \$3.00/gallon). To put it differently, we still work many fewer hours to fill up our cars today than we have during most of the gasoline era.

Second, as anyone knows who’s ever rented a car in Europe or Japan, gasoline looks positively dirt cheap, even at current prices, when compared to other Western industrial countries. There motorists pay \$4–5/gallon and have for a long, long time. (Taxes explain all the difference, incidentally.) True, population density is greater in Europe and Japan (so that people drive less far on an average trip than in the United States), and public transit is much better developed in most European and Japanese cities, thus making the impact of higher gasoline prices there less dramatic

than they would be in the United States. That’s one reason why, in fact, the Europeans have elected to tax gasoline so heavily—it’s not as painful, or politically unpopular, as it would be here.

There’s a third reason why we shouldn’t complain too much about the price of gasoline: it probably should be higher than it is now, especially if we factor in the high and growing costs of traffic congestion. The current price of \$2.10/gallon covers the cost of the crude oil used to make gasoline (about \$0.86/gallon), the cost of refining, transporting and marketing it (about \$0.81/gallon) and the federal, state and local taxes levied on it (which average about \$0.43/gallon). But it does *not* include any of the “external” costs associated with climate change, oil import dependence, or traffic congestion. These external costs may be harder to express in dollar terms than the costs of exploration, production, refining, and marketing, but they are real nonetheless. (See Ian Parry’s attempt to value these costs in the summer 2002 issue of *Resources*.) Painful as it may be to be paying more at the pump, we’re probably still not paying the full social costs associated with our use of this extraordinary versatile and valuable fuel.

I hope you enjoy this issue of *Resources*, and thank you for your interest in RFF. ■

Paul R. Portney