

The Center for Economic Renewal, Growth, and Excellence (CRECE, for its Spanish acronym) and Intelligent Economics have partnered to bring you ***The Road to Prosperity Newsletter***. This periodic publication offers concise yet comprehensive economic analyses, providing insights for informed policy decisions that advance free entrepreneurship and economic freedom in Puerto Rico. From industry overviews to policy impacts, each issue is crafted to be an essential source of information with a primary emphasis on Puerto Rico's recovery efforts post-María and post-COVID, complemented by insights into U.S. and global trends.

The Cost of War: How the Iran Conflict Is Hitting Puerto Rico's Economy

I. THE OIL SHOCK: SCALE AND CONTEXT

The U.S.-Israel war against Iran, which began on February 28, 2026, has triggered the largest oil supply disruption and energy crisis in modern history. Before hostilities began, Brent crude, which is the international benchmark, traded near \$73 per barrel. On April 30, the price reached a 4-year peak at \$126, a surge of more than 70% in less than two months. March alone saw one of the largest single-month price jumps on record, with Brent gaining 51% as Gulf output collapsed and exports stalled. The near-complete closure of the Strait of Hormuz, ordinarily a conduit for roughly one-fifth of the world's oil and natural gas supplies, is the primary driver. Goldman Sachs estimates that exports through the chokepoint have fallen to just 4% of normal levels.

While Puerto Rico's local fuel prices track WTI (the U.S. crude oil price benchmark) more closely than Brent, monitoring Brent matters because it is the reference price for roughly two-thirds of internationally traded crude. The World Bank projects Brent will average \$86 per barrel through 2026, up from \$69 in 2025. This is the most significant energy price spike since Russia's invasion of Ukraine in 2022.



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II. THE PRICE TAG FOR PUERTO RICO

The first channel through which the war affects Puerto Rico’s economy is gasoline prices. Puerto Rico does not import oil directly from the Gulf, but local prices respond to global benchmarks. For three crude oil price scenarios, the table below quantifies the pass-through to retail gasoline prices and the resulting aggregate cost burden on Puerto Rico's economy:

Oil Price Increase	Impact on Gasoline Prices (per gallon)	Impact on Gasoline Prices (per liter)	Annual Aggregate Impact
+\$10/barrel	+\$0.32	+8.4¢	~\$350 million
+\$20/barrel	+\$0.63	+16.7¢	~\$700 million
+\$30/barrel	+\$0.95	+25.1¢	>\$1 billion

Source: Authors’ calculations.

WTI has risen roughly \$35 per barrel since the war began, rising from approximately \$72 to above \$106 per barrel. This means that the annualized aggregate impact of higher fuel costs in Puerto Rico could exceed \$1 billion, directly affecting households, consumers, businesses and other sectors that depend on transportation.

Electricity is the second channel. Puerto Rico generates approximately 62% of its electricity from petroleum-fired plants. PREPA and LUMA adjust the Fuel Charge Adjustment (FCA) quarterly to reflect changes in oil prices. This results in higher electricity rates for consumers and businesses within months. Following Russia’s invasion of Ukraine, the fuel-cost portion of electric rates jumped from 15 to 22 cents per kilowatt-hour in a single quarter. A comparable or even greater adjustment is expected in 2026 given the scale of the current shock. Moreover, ongoing debt restructuring negotiations with PREPA bondholders could put more pressure on rates, which could rise to more than 30 cents/kilowatt-hour, adding to the elevated cost of living in Puerto Rico.

The third channel is imports. Puerto Rico imports more than 80% of the goods it consumes, including 85% of its food supply. Higher fuel costs raise shipping, insurance, and logistics expenses throughout the supply chain. In January 2026, Puerto Rico imported over \$4 billion in goods. Consumer goods such as food and beverages, as well as industrial materials, will all carry higher embedded transport costs under the current oil price environment. These costs are ultimately passed through to consumers.

The impact of sustained price increases at this scale transcends costs: they also alter economic behavior. Economists refer to this as demand destruction: the process by which consumers and businesses reduce consumption in response to persistently higher prices, thus compressing economic activity in ways that can outlast the initial shock.

In Puerto Rico, the sectors most directly exposed include:

- Restaurants and food service, where higher food import costs and electricity bills compress profit margins and force price increases that reduce foot traffic
- Entertainment and leisure, where discretionary spending is typically the first casualty of household budget pressure
- Apparel and retail, where shipping and logistics costs are passed through to consumers in the form of higher prices
- Transportation, where fuel costs directly drive operating expenses for trucking, delivery, and public transit, with knock-on effects across local distribution networks

Beyond domestic consumption, two sectors central to Puerto Rico's economy—tourism and pharmaceuticals—face their own pressures, though through different channels:

- **Tourism.** Higher jet fuel costs result in more expensive fares, which reduce visitor arrivals, particularly from the U.S. mainland, Puerto Rico's primary source market. Goldman Sachs estimates that global jet fuel demand has already fallen roughly 3.6 million barrels per day from pre-war levels.
- **Pharma.** Puerto Rico's pharmaceutical exports totaled \$24.7 billion in 2024, representing 88% of total exports. Although this sector is less exposed to domestic demand shocks, it faces rising input and logistics costs that could affect margins and investment decisions.

Meanwhile, recent economic performance on the Island has been weak: the Economic Activity Index (EAI) grew just 0.5% in 2024, contracted 0.4% in 2025, and has continued a downward trajectory early in 2026. In addition, consumer confidence and retail sales in non-essential categories are softening. Layered onto this weakness, the current oil shock elevates the downside risk to growth.



III. WHAT PUERTO RICO CAN CONTROL

Puerto Rico cannot prevent geopolitical shocks or control global oil markets. However, it can reduce the extent to which its own policies amplify their impact. Here's where pursuing greater economic freedom comes to play. Economies with fewer barriers to production, investment, and trade adapt faster when external conditions deteriorate, because they have more room to maneuver. Two areas are most relevant for Puerto Rico:

1. **Tax response.** Quick governmental response to price shocks requires a simple tax structure to allow the implementation of fast and targeted relief mechanisms. In this sense, greater economic freedom means having fewer distortive layers. Recent proposals to temporarily suspend the 'second crudita' tax on petroleum products and revise the inventory tax would be steps in the right direction. The 'crudita' is a per-barrel excise on petroleum products entering Puerto Rico, currently \$15.50 per barrel, with a 2015 add-on (the 'second crudita') making up \$6.25 of that total and originally tied to Highways and Transportation Authority (HTA) debt.
2. **Local production.** Puerto Rico imports 85% of its food despite having a favorable climate and fertile land. Yet, the agricultural sector represents less than 1% of gross domestic product (GDP). Easing regulatory barriers to investment and production could unlock capacity in agriculture, food processing, and light manufacturing, thereby reducing the import dependence that magnifies external shocks.

The Iran conflict is a reminder that global instability is a recurring feature of the economic environment, not a temporary exception. Economies that are freer, more productive, and less dependent on outside supply chains are better equipped to absorb these shocks. Puerto Rico must accelerate progress in that direction.

Economic activity showed no real growth in 2025

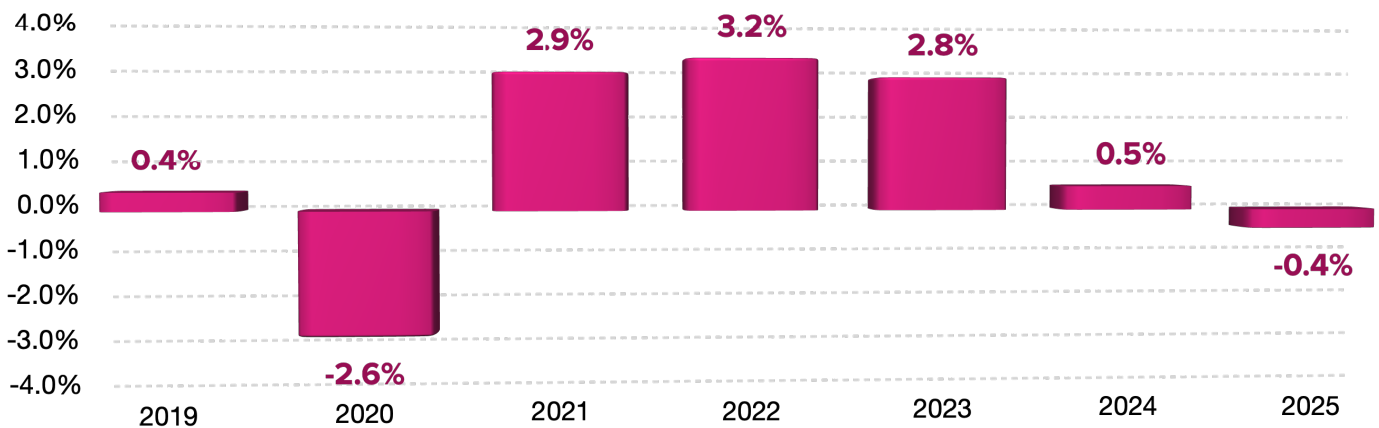
Puerto Rico’s Economic Activity Index (EAI) shows that, while the economy succeeded in rebounding from the sharp disruption caused by the 2020 pandemic, it has steadily lost strength in recent years. In 2021 and 2022, the index expanded 2.9% and 3.2%, respectively. Growth was driven by the economy’s reopening after pandemic lockdowns, stronger consumption, and the injection of federal recovery and stimulus funds. In 2023, the EAI posted a solid 2.8% gain, underscoring the resilience of economic activity post-COVID-19. The deceleration documented above for 2024 and 2025 has continued into 2026, with the EAI growing just 0.3% year-over-year in January and contracting 0.6% in February.

This recent trajectory suggests that Puerto Rico is entering a phase of stagnation, with the local economy going from a period of rebound to a period of weak and fragile growth.



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ECONOMIC ACTIVITY INDEX
Year-over-year % change

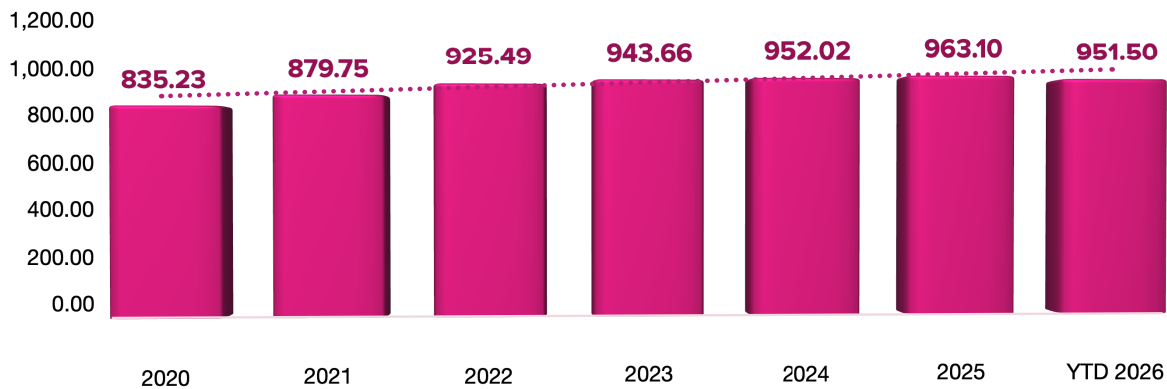


Source: Puerto Rico Department of Economic Development and Commerce.
Note: 2026 includes January and February.

Employment remains strong

Nonfarm employment reached 963,100, rising by 11,000 jobs—or 1.2%—in 2025 compared to 2024. That was a stronger pace than in 2024, when payroll employment increased 0.9% from 2023. Growth was led by government, leisure and hospitality, educational and health services, and trade, transportation, and utilities. On the other hand, employment in professional and business services and manufacturing contracted. The unemployment rate rose from 5.4% in 2024 to 5.7% in 2025, with about 70,000 people unemployed at year-end. Labor force participation improved modestly to 45.4%.

NONFARM EMPLOYMENT



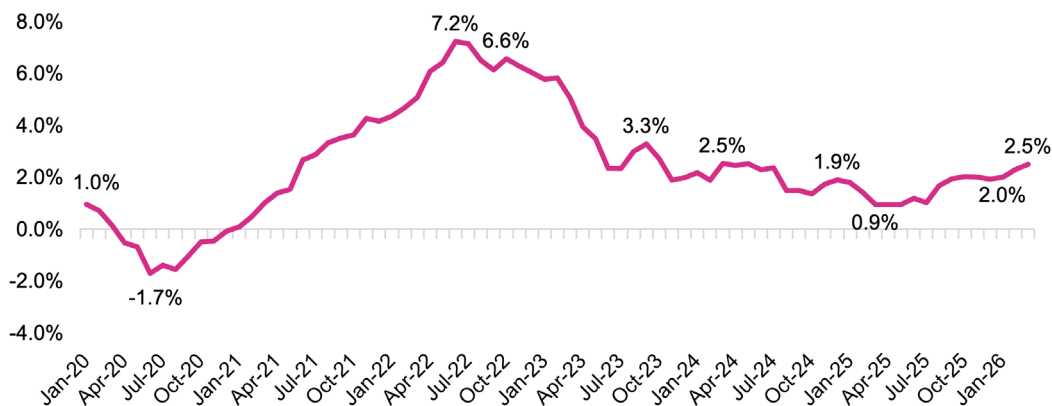
Although year-over-year data point to a strong labor market, month-over-month growth is starting to stagnate.

Source: Puerto Rico Department of Labor.
Note: 2026 includes January and February.

Cost of living continues to increase

Inflation in Puerto Rico ended 2025 at a moderate 1.5%, well below the sharper increases of prior years, but accelerated through the first quarter of 2026—climbing from 2.0% in January to 2.3% in February and 2.5% in March, the highest reading since early 2024. Rising gasoline prices, tariffs on imported goods, and persistent cost pressures across the economy all point to the risk of additional price acceleration. In Puerto Rico, where households are already highly exposed to imported inflation, this puts more pressure on purchasing power.

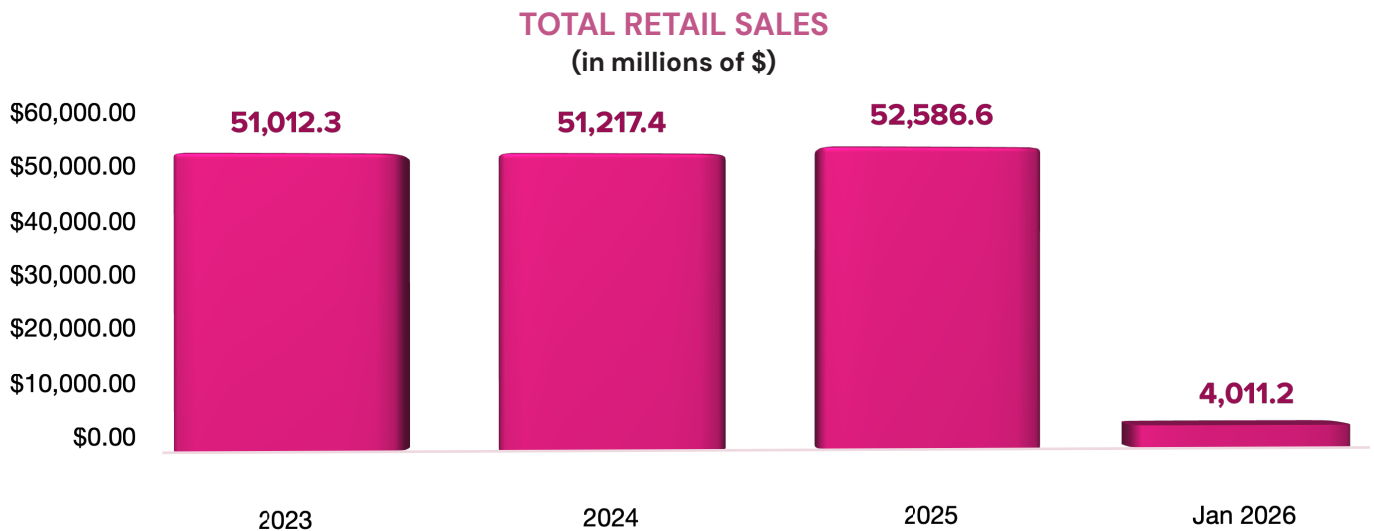
INFLATION



Source: Puerto Rico Department of Labor.

Retail sales remained positive in 2025, but performance varied across categories

Puerto Rico’s retail sector posted modest growth in 2025, with cumulative retail sales for the calendar year increasing 2.7% compared with 2024. In 2025, total retail sales reached \$52.6 billion, signaling resilient consumer spending despite emerging challenges in the economic environment.



Source: Puerto Rico Department of Economic Development and Commerce.

That said, performance across retail categories was far from uniform. The strongest gains were in cosmetics, beauty products, and perfumes (+14.2%), new and used motor vehicles (+13.2%), and restaurants and alcoholic beverage establishments (+10.6%). By contrast, the largest declines were in lawn and garden equipment (-6.2%), department stores and miscellaneous retail (-5.3%), and fuel distributors (-4.4%).

In January 2026, retail sales totaled \$4.01 billion, falling -1.7% compared to January 2025. The sharpest reductions were seen in gas stations (-35.3%) and department stores (-11.5%). On the other hand, restaurants (+0.7%) and supermarkets (+3.6%) reported increased sales.

