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Rising Crude Oil Prices and Household Consumption in India: A Keynesian Perspective

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Abstract: *The price of crude oil is a huge external shock for India as it is highly dependent on imported crude oil and the price of the crude oil is directly linked to the domestic economy. Even though the macroeconomic consequences of oil-price movements have been well documented, little research has focused on the indirect consequences of oil-price changes for the demand for household consumption, in the form of cost-push inflation and reductions in real purchasing power. This study seeks to redress this by exploring the relationship between the growth in crude oil prices and household consumption in India as per Keynesian consumption function and cost-push inflation mechanism. This study is descriptive and conceptual research and is a secondary study that involves the study of secondary data related to Brent crude oil price, domestic fuel price, transportation and freight, consumer price inflation, and current account deficit. Instead of the primary household sample, estimates reported (and secondary evidence) are used to analyze the impact of the oil-price shock on the household purchasing power and consumption. The results confirm, in part, the theory that as crude oil prices rise, so do all prices for fuel, transportation, logistics and food, ultimately impacting the real disposable income of households. The resulting loss of purchasing power should limit household consumption, including lower and middle income households. The novelty of the present study is in the idea of considering a rise in crude oil prices as an indirect or "hidden" tax on the consumption of households and the incorporation of the cost-push inflation channel and Keynesian consumption behavior. The study finds that ongoing higher oil prices have significant implications on welfare of households and require specific fiscal and policy measures.*

Keywords: Crude Oil Prices, Household Consumption, Keynesian Consumption Function, Cost-Push Inflation, Purchasing Power, CPI Inflation, India.

I. INTRODUCTION

Crude oil is an essential part of transport, logistics, industry and home services, agriculture. As a result, fluctuations in international crude oil prices have ramifications beyond the energy industry. A rise in the price of crude oil can lead to higher import bill, inflationary pressures, and lower purchasing power of the households for an economy which imports crude oil like the Indian economy.

According to the source, the price of Brent crude rose from around US$93 per barrel in early June 2026 to nearly US$97 due to geopolitical tension because of uncertainty over supply and the Strait of Hormuz. The article also mentions that India imports about 88% of its crude-oil needs and that rising crude prices can drive up the cost of oil

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imports and current account deficit. This impact is enhanced by a depreciation of the rupee as most of the crude imports are in dollar terms.

Overall, the effect of the household impact is mainly via the cost-push inflation channel. The increased cost of transportation and logistics travel caused by higher fuel prices causes increases in food, consumer goods, and essential services.

The main transmission mechanism investigated in this study is:

Crude Oil Price ↑ → Fuel Costs ↑ → Transportation and Logistics Costs ↑ → CPI Inflation ↑ → Real Disposable Income ↓ → Household Consumption ↓

The study thus investigates a link between the oil-price shock and the Keynesian Consumption Function and whether the available evidence is consistent with the theoretical prediction of the reduction in household consumption with a decline in real purchasing power.

II. LITERATURE REVIEW

The impact of oil price shocks on inflation and the transmission of the oil price shock to macroeconomics.

Crude oil prices are a significant external factor for oil importing economies as fluctuations in international energy prices can impact domestic production expenses, inflation, trade balances and make up for household purchasing power. The economics of oil-price changes has been a focus in the literature so far. Hamilton (1983) has made the point that oil-price shocks are important for economic fluctuations, and Kilian (2009) has shown that the impact of a price change on the economy depends on whether the price change is due to a supply disruption or to a global aggregate demand or to an oil-specific demand shock.

More recent research continues to confirm the importance of the oil-price–inflation transmission mechanism. In a recent study on crude oil prices and the Indian situation for 2009–10 to 2023–24, Kundu, Tewari and Bhattacharyya (2025) estimate that a rise of 10% in the global crude oil prices will push up the headline inflation in India by about 20 basis points. Their results also stress the importance of taxation of petroleum products and government intervention in the regulation of domestic pass-through. (Reserve Bank of India)

This evidence is significant to India as it does not only make an impact on the price of petrol and diesel but on the economy as a whole. Fuel is a significant input for transportation industry, logistics sector, agriculture and manufacturing. This means that price increases in crude oil could have second-round effects on the prices of food and other consumer goods. The international literature also shows that fuel-price increases have more far-reaching and lasting inflationary effects on developing economies. (ScienceDirect)

The household budget constraint is related to cost-push inflation.

Crude oil can be transmitted to the living standards of households via the cost-push inflation channel. When crude oil prices rise, the cost of fuel and transportation goes up, which in turn leads to a rise in the cost of goods and services production and distribution. This means that, even if the nominal family income doesn't go up, the family will be paying more for a house.

This mechanism is directly related to the Keynesian consumption theory. The Keynesian Consumption Function is represented by:

$$C = a + bYd$$

It is represented by the equation: C = a + bYd, where C is consumption expenditure, a is autonomous consumption, b is the marginal propensity to consume, and Yd is disposable income.

The important thing to remember is that consumption is tied to purchasing power and not just to dollars and cents. When the price of crude oil rises and inflation rises, but the income of households does not rise in tandem with the price of crude oil, then real disposable income decreases. The households need to spend more of their income on essential expenditures and have less money to spend on discretionary expenditures.

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This mechanism is confirmed by recent international studies. Increased fuel prices have a negative impact on household purchasing power and fuel-price inflation spreads widely, disproportionately affecting developing economies, as the World Bank analysis of fuel-price transmission indicates. (ScienceDirect)

The study looks at energy prices and household consumption in India.The study examined energy prices and household consumption in India.

A recent key study that directly addresses the issue of energy-price shocks and their transmission to household consumption in India is that of Priya and Sharma (2024). They employ a large dynamic panel of Indian households and discover that shocks to energy prices have negative effects on overall household consumption and on the individual expenditure components. They found that expenditure on relatively elastic categories - such as services and durable goods - is more likely to see larger drops than to see less, whereas relatively inelastic categories - like food and fuel - are more likely to see less. They also find that household responses to energy-price volatility are greater. (ScienceDirect)

This study is relevant to the present study, as it goes beyond the traditional oil-price–inflation relationship, and looks at the household-consumption channel. However, it focuses on energy-price shock, in general, not on a severable sequence of theory of the oil price shock, cost-push inflation, and real income reduction, and an adjustment of consumption.

Other recent works by Bhattarai, Chatterjee and Udupa (2025) give additional support to the Indian study. The authors analyse the distributional impacts of the shocks to global food and oil prices, with monthly panel data of household consumption and income. They conclude that oil-price shocks have negative consumption effects and that these effects are linked to different wage-income effects. The study, therefore, offers valuable evidence of the impact of global price shocks on households through both price and income channels. (Federal Reserve)

Household Heterogeneity and Consumption Adjustment.Household Heterogeneity and Consumption Adjustment.

This impact of higher crude oil prices is not expected to be the same for all households. Households with restricted ability to spend on essentials have lower buffers to absorb increases in essential spending. As a result they can cut their discretionary spending, delay purchases of durable goods, decrease their recreational and restaurant spending, or savings can be diverted.

A recent IMF study also reinforces the significance of household differences in their reactions to external price changes. In the context of global fuel price and food price shocks, Martin, Adam and Gollin (2025) show how significant spatial variations in the consumption response can occur, and how important transportation costs and supply-side effects are. (IMF)

Likewise, recent IMF research on external price shocks indicates that increases in import prices can lead to higher inflation, lower real wages, and lower consumption, particularly for poorer households that find it harder to insure against external price shocks. The results support the view that an oil-price shock is not only an energy-market shock, but also a potential shock to household welfare.

A study of the Food Security and Poverty in Rural areas of Maharashtra Household Consumption Research was carried out in Maharashtra.

The present study is built upon the foundation laid by the literature that has developed on the trends of household consumption in Maharashtra. Jagannarayan and Prasuna (2024) discuss household consumption before and after COVID-19 in the paper entitled Shifting Patterns: Analyzing Household Consumption in Maharashtra Before and After COVID-19 to understand how household expenditure changed prior to and following the pandemic, and to emphasize the role of income, health considerations and spending priorities in distinguishing essential and non-essential consumption. (Informatics Journal)

Likewise, Jagannarayan and Prasuna (2024) attempt to map the money moves of the household by examining the expenditure behaviour of the household on food, health, and leisure among rural and urban households in the Amravati area using the CMIE Consumer Pyramids Household Survey 2019-2021. They show that income and household size,

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because of the influence they have on expenditure, are important determinants of expenditure and that the distinction between rural and urban consumption behaviour is important. (European Economic Letters)

Jagannarayan and Prasuna (2025) analyzed the consumption practices of women headed households during the COVID-19 lockdown in Maharashtra, a relevant contribution. The study uses CPHS data and regression analysis to show that income, age, gender, education and household size were factors affecting food expenditure during the lockdown. The study also identifies the importance of adaptive budgeting and prioritising essential consumption in times of economic insecurity. (The ASPD)

Such studies are particularly relevant for the current research since it proves that socio-economic characteristics and economic conditions affect household consumption in Maharashtra. They tend to focus on income and demographic changes or on energy price shocks from around the world, however, not on disruptions due to the pandemic. Thus, they serve as the foundation for the household-consumption framework, which will be developed within the present crude-oil framework.

Jagannarayan's later writings develop this theme. For instance, her study of leisure spending in Mumbai on households in the city (2026) finds that income, occupation and household size have significant effects on discretionary leisure spending among urban households. These findings corroborate the argument that an oil-price shock can affect the composition, not just the overall amount, of household consumption, and that there are differences in the responsiveness of expenditure categories to household economic conditions.

Research Gap

It is obvious from the literature that three important relationships are clearly established: oil prices affect inflation, inflation affects real purchasing power and income and economic shocks affect household consumption. India's recent research has also started to directly analyse the impact of energy price shocks on household consumption. These strands are, however, not well connected.

The present study aims to fill this gap and conceptually define the transmission mechanism as:

Crude Oil Price Shock → Cost-Push Inflation → Real Income Reduction → Consumption Adjustment

The novelty is linking up the international macroeconomic energy shock to household level consumption decision, via real disposable income loss. The present study is focused on the theoretical channel that links crude oil to cost-push inflation and then to household purchasing power, whereas Priya and Sharma (2024) show that energy-price shocks have a negative impact on household consumption and Bhattarai et al. (2025) highlight the heterogeneous response of households to global energy and food price shocks. (ScienceDirect)

The three studies by Jagannarayan and co-authors offer useful complementation since they show that consumption in Indian households is related to income, household characteristics, expenditure category and economic circumstances. In this context, the present research contributes to this literature on household consumption by considering crude oil prices as an external shock to the macroeconomies.

Novelty of the Present Study

The main contribution is the combination of macroeconomic energy economics and the theory of household consumption. The impact of crude oil is felt through fuel and transportation costs, as well as the costs of logistics and food, and thus is considered an indirect or “hidden tax” on household consumption.

The study therefore turns the lens away from:

Crude Oil Price → Inflation

to:

Crude Oil Price → Cost-Push Inflation → Real Disposable Income → Household Consumption

This home-based interpretation also offers a more compelling theoretical account of how continued price rises might be more constraining on discretionary spending and impact economically disadvantaged households. It also provides a foundation for future empirical testing with data at the household level for CPHS or time-series econometric analysis.

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From this home-based viewpoint, there is a more comprehensive theoretical basis for why an ongoing increase of oil costs could be particularly limiting on discretionary spending and affect economically disadvantaged families. It also provides a clear foundation for additional empirical analyses at the household level, using either the CPHS or time-series econometric approaches.

Theoretical Framework

Keynesian Consumption Function

The basic principle of the study is the Keynesian Consumption Function. The conventional relationship is: $C = a + bY_d$

C is consumption expenditure, a is autonomous consumption, b is the marginal propensity to consume and Y_d is disposable income.

The Keynesian framework implies: $\partial C/\partial Y_d > 0$

Therefore an increase in disposable income will lead to growth in consumption.

But if there is a shock to oil prices, the overall level of prices can rise without the overall level of nominal household income. Thus becomes significant the purchasing power of income.

Real disposable income can be represented as: $Y_r = Y_n/P$

where Y_r is real disposable income, Y_n is nominal disposable income and P is the general price level.

Thus: Y_n = constant, $P \uparrow \Rightarrow Y_r \downarrow$

An extended Keynesian consumption function can therefore be specified as:

$C = a + bY_d - cP$ where $c > 0$.

This formulation indicates that consumption rises as the level of disposable income rises, and decreases as the general price level rises.

Cost-Push Inflation

The other theoretical basis is the cost-push inflation mechanism. A rise in crude oil prices leads to a rise in fuel and transportation prices and this in turn leads to a rise in the cost of goods and services being transported in the economy.

The transmission mechanism is:

Oil Price ↑ → Input Costs ↑ → Transportation Costs ↑ → Product Prices ↑ → CPI ↑

Higher crude prices are said to impact household budgets in big ways via transportation, logistics, food, and essential services, among other channels, according to the source article.

Research Gap

The link between oil prices and inflation is explored in many studies but the current analysis is particularly interested in the household-consumption mechanism. It links the macroeconomic oil-price shock to the household via the following chain:

Crude Oil Price Shock → Cost-Push Inflation → Real Income Reduction → Consumption Adjustment

This provides a household-level interpretation of a macroeconomic energy shock.

Hypotheses Development

H1: An increase in international crude oil prices has a positive effect on India's consumer price inflation. $\beta_1 > 0$

H2: An increase in consumer price inflation negatively affects household real purchasing power. $\beta_2 < 0$

H3: Real disposable income has a positive effect on household consumption expenditure.

$\beta_3 > 0$

H4: An increase in crude oil prices has a negative indirect effect on household consumption through the inflation channel.

Oil Price ↑ → CPI ↑ → Real Disposable Income ↓ → Consumption ↓

H5: Rupee depreciation amplifies the inflationary effect of international crude oil price increases.

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III. RESEARCH METHODOLOGY

The research type of this study is descriptive and analytical research using secondary data. The source material includes observations and estimates on Brent crude price, fuel prices, freight costs, CPI inflation, food inflation, and current account deficit.

The variables suggested to be used in formal empirical testing are crude oil price, CPI inflation, real disposable income, household consumption, exchange rate, household income and household characteristics.

The principal consumption model is:

$$C_t = \alpha + \beta_1 Y_{rt} + \beta_2 CPI_t + \beta_3 OIL_t + \beta_4 EXR_t + \varepsilon_t$$

where C_t represents household consumption, Y_{rt} represents real disposable income, CPI_t represents consumer price inflation, OIL_t represents crude oil prices and EXR_t represents the exchange rate.

The expected coefficient signs are:

$$\beta_1 > 0, \beta_2 < 0, \beta_3 < 0$$

The crude-oil inflation model is:

$$CPI_t = \alpha + \beta_1 OIL_t + \beta_2 EXR_t + \beta_3 GDPG_t + \varepsilon_t$$

The expected relationship is: $\beta_1 > 0$

For household-level research, the model can be extended as:

$$C_{it} = \alpha + \beta_1 Y_{it} + \beta_2 CPI_t + \beta_3 OIL_t + \beta_4 HHSIZE_{it} + \beta_5 URBAN_i + \varepsilon_{it}$$

The proposed mediation mechanism is:

OIL PRICE → CPI → REAL DISPOSABLE INCOME → CONSUMPTION

The indirect effect can be expressed as:

Indirect Effect = (Oil Price → CPI) × (CPI → Real Income) × (Real Income → Consumption)

Because the supplied article does not provide a sufficiently large raw household or time-series dataset, the present study does not claim formal econometric validation of these equations.

IV. DATA ANALYSIS AND INTERPRETATION

Crude Oil Price Movement

The source material reports the following Brent crude prices:

Period	Brent Crude (US$/barrel)
31 March 2026	103.97
Early May 2026	102.00
28 May 2026	94.08
1 June 2026	93.26
3 June 2026	96.81

Source: Reuters, Trading Economics and ICE Futures Europe, as reported in the source article.

Between 1 June and 3 June 2026, Brent crude increased from US$93.26 to US$96.81.

The percentage increase is:

Percentage Change = [(96.81 - 93.26) / 93.26] × 100

Percentage Change ≈ 3.81%

The source material attributes the increase to geopolitical risk premiums, supply uncertainty and concerns about possible disruption to oil flows through the Strait of Hormuz.

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Transmission to Household Budgets

The reported transmission estimates are:

Transmission Channel	Reported Impact	Household Effect
Petrol and diesel	Approximately ₹7.5/litre increase	Higher commuting expenditure
Freight transport	Approximately 2.8% increase	Higher delivered prices
CPI inflation	Approximately 36 basis points	Lower purchasing power
Future CPI risk	Up to approximately 48 basis points	Higher family costs
Current account deficit	Approximately 0.3% of GDP per US$10 oil increase	Greater macroeconomic vulnerability
Food inflation	Logistics costs passed to consumers	Higher grocery expenditure

The reported estimates are from CRISIL, Ministry of Petroleum and industry estimates cited in the source article.

The evidence supports the following transmission:

Oil Price ↑ → Fuel Price ↑ → Freight Cost ↑ → Food and Consumer Prices ↑ → CPI ↑

Inflation and Purchasing Power

The CPI is a measure of inflation and purchasing power.

If fuel-price increases continue it could push headline CPI inflation up by around 36 basis points and as far as 48 basis points, according to the source article.

The article also mentions the evidence from RBI that inflation can rise by around 20 basis points with a sustained rise in oil prices by 10%.

The theoretical relationship is therefore: $\partial CPI/\partial OIL > 0$

This provides preliminary support for H1.

The effect on real purchasing power can be expressed as: $Y_r = Y_n/P$

Therefore: $P \uparrow \Rightarrow Y_r \downarrow$

When nominal income does not increase proportionately with prices, households experience a decline in real purchasing power.

The source article notes that income growth may not keep pace with rising prices and that middle-income households face pressure from housing, education and healthcare costs.

This is consistent with: $\partial C/\partial CPI < 0$ and therefore provides preliminary support for H2.

Current Account and Exchange Rate

Opening the door to inflation and Purchasing Power

The rise in fuel prices in recent months could add around 36 basis points to headline price inflation, according to the source article, though the impact could be as great as 48 basis points if prices continue to rise.

The article also cites RBI evidence, which suggested that if oil prices increase by 10 per cent, the inflation will rise by around 20 basis points.

A rise in crude oil prices also raises India's import bill and can lead to a strain on the current account. The source material estimates that an increase in oil prices of about 0.3% of GDP will contribute to the current account deficit for every US$10 per barrel increase in oil prices.

The exchange-rate mechanism is:

Oil Price ↑ → Import Bill ↑ → External Balance Pressure ↑ → Rupee Depreciation → Domestic Oil Cost ↑

This creates an additional inflationary channel and supports H5 theoretically.

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Discussion

The results show that an increase in crude oil prices is both a macroeconomic and household issue. The effect starts in the energy market, but trickles through the economy.

The most crucial thing about real purchasing power is that it decreases. Transportation and logistics costs are higher when oil prices are higher and so are the cost of goods and services. When household income grows at a lower rate, the real disposable income decreases.

The Keynesian Mechanism may thus be stated as:

Real Disposable Income ↑ → ***Consumption*** ↑

while an oil-price shock produces:

Oil Price ↑ → ***CPI*** ↑ → ***Real Disposable Income*** ↓ → ***Consumption*** ↓

The final statement of the original article that crude oil is a "hidden tax" on consumption is then in harmony with the long-embedded Keynesian concept. The impact of higher oil prices isn't felt as one more household tax but rather is spread out over transportation, food, housing, deliveries and other goods and services.

This impact is likely to be especially strong on households that are on a tight budget. These households will have fewer opportunities to cut back on non-essential goods and services, and hence larger welfare losses in the event of an increase in the prices of essential goods and services.

Practical Implications

The findings have a number of implications for the policy makers.

Inflation management: Oil-price inflation is an external supply shock. The price shock is not a problem of monetary policy, and coordination of monetary, fiscal and supply-side policies is important in the face of the underlying price shock.

Household protection: When the cost of essential goods and transportation is significantly increased by continuing oil price rises, vulnerable households may need specific protection.

Diversification of energy sources: Higher reliance on renewables, alternative fuels, electric mobility and public transport will limit the risk of India to international crude price volatility.

Exchange-rate management: For the purposes of minimizing the importation of oil-price increases to the domestic market, the exchange-rate is important because the majority of crude imports are in dollars.

Supply chain efficiency: Enhancing transport and supply chain efficiency can help curb the pass-through of fuel price increases to food and consumer prices.

Theoretical Implications

The paper is a modification of the traditional Keynesian Consumption Function, in order to explicitly include the price level: $C = a + bY_d - cP$.

It therefore links consumption with both nominal and changes in purchasing power.

In addition, the study incorporates the theory of Keynesian consumption with cost-push inflation theory:

Cost-push inflation is a problem that arises when oil prices change.A problem that can arise due to oil price changes is cost-push inflation.

This gives a common language for understanding how an international commodity-price shock may ultimately impact the welfare of households.

The evidence points to the direction of the proposed relationships; however, no formal statistical testing of the entire model has been done as there is no source data that provides the raw household or time-series observations needed.

Conclusions and Directions for Future Research.

One of the major external vulnerabilities of India is the price rise of crude oil. Their impacts are not restricted to the price of gasoline but also reach the transportation and logistics sectors, food prices, inflation and the current account and the purchasing power of households.

The study relates these effects with the Keynesian Consumption Function and suggests that the effects of crude oil on household consumption are mainly through the cost-push inflation and real-income channels.

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Theoretical Framework

Crude Oil Price ↑ → CPI Inflation ↑ → Real Disposable Income ↓ → Household Consumption ↓

The principal empirical model is: $C_t = \alpha + \beta_1 Y_{rt} + \beta_2 CPI_t + \beta_3 OIL_t + \beta_4 EXR_t + \varepsilon_t$

with expected relationships: $\beta_1 > 0$, $\beta_2 < 0$, $\beta_3 < 0$

The available evidence provides preliminary support for the theoretical framework, particularly for the relationship between crude oil prices, inflation and purchasing power. However, the complete Keynesian consumption mechanism requires formal econometric testing.

Future research should therefore use monthly or quarterly Indian data on crude oil prices, CPI, real disposable income, private consumption expenditure and the INR/USD exchange rate. ARDL/ECM, VAR/SVAR and household-level regression models can be used to establish short-run and long-run relationships. Household-level research should additionally examine whether the impact differs by income group, household size and rural-urban location.

A particularly useful extension would be to test the mediation pathway:

Oil Price → CPI → Real Disposable Income → Household Consumption

Such research would move the present study from preliminary theoretical validation to formal empirical validation of the Keynesian consumption mechanism in the context of crude oil price shocks in India.

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