

IMPACT OF GLOBAL MELTDOWN ON PETROLEUM SECTOR IN INDIA

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Indian Petroleum Industry

The **Indian Petroleum Industry** is a case in point for exhibiting the giant leaps India has taken after its independence towards its march to attain a self-reliant economy.

During the Independence era of 1947, the Indian Petroleum Industry was controlled by foreign companies and India's own expertise in this sector was limited. Now, after 60 years, the Indian Petroleum Industry has become an important public sector undertaking with numerous skilled personnel and updated technology that is comparable to the best in the world. The vim and the achievement during these years is the growth of productivity in petroleum and petroleum-based products. Even the consumption has multiplied itself nearly 30 times in the post-independence era.

An important advancement in the petroleum industry came with the Industrial Policy Resolution, 1956 which signified the promotion of growth of industries. The ONGC originally set up as a Directorate in 1955, was transformed into a Commission in 1956. In 1958, the Indian Refineries Ltd., a government undertaking, came into existence. The Indian Oil Company (IOC), also a government undertaking, was set up in 1959 with the purpose of marketing petroleum-related products. Indian Oil Corporation Ltd. was formed in 1964 with the merger of the Indian Refineries Ltd. and the Indian Oil Company Ltd. Presently, 17 refineries operate under the Indian Petroleum Industry.

Growth of the Indian Petroleum Industry:

- 1 During 1947-57, 3 refineries were set up in Mumbai and Visakhapatnam by transnational oil corporations doing business in Indian
- 1 During 1957-67, another 3 refineries were established in Guwahati, Barauni, and Koyali by Indian Refineries Ltd.
- 1 During 1967-77, 2 more were set up in Chennai by Iranian companies and in Haldia by Indian Oil Ltd.
- 1 During 1977-87, 2 more refineries were commissioned. The one at Bongaigaon was the first to have an amalgamated petroleum refinery-cum-petrochemicals unit. The other was established at Mathura.
- 1 During 1987-97, 2 more were set up at Nagapattinam and Mangalore.
- 1 During 1998-2007, refineries at Panipat and Numaligarh were set up.

Major Players:

OIL AND NATURAL GAS CORPORATION

It is a public sector petroleum company in India, contributing 77% of India's crude oil production.

Revenue (2006): \$ 10.5 billion

Employees: 41000

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HINDUSTAN PETROLEUM CORPORATION LTD. 1952:

The Company was incorporated in the name of Standard Vacuum Refining Company of India Limited on July 5, 1952

INDIAN OIL CORPORATION LTD.

It is India's largest commercial enterprise, with a sales turnover of US \$36.537 billion.

A wholly owned subsidiary company, Indian Oil Corporation Ltd. is the 19th largest petroleum company in the world.

BHARAT PETROLEUM CORPORATION LTD.

It is the 3rd largest oil company in India owned by the Government of India.

Revenue (2005): \$17.613 billion

Employees: 12400

IMPACT OF GLOBAL MELTDOWN:

- 1 Due to the lower international crude prices, the oil companies' losses on kerosene and cooking gas too have come down to Rs 17.26 per litre on the sale of every litre of kerosene and Rs 148 per cylinder, respectively.
- 1 The companies were losing nearly Rs 30 on each litre of kerosene and Rs 333 per cooking gas.
- 1 Based on the average international oil price in the second fortnight of November, the state-run firms earn a margin of Rs 44 crore per day on petrol and Rs 42 crore a day on diesel. They, however, lost Rs 66 crore a day on sale of kerosene and Rs 29 crore per day on cooking gas.
- 1 The fall in international oil prices will result in lower revenue loss on fuel sales this fiscal. The companies will end 2008-09 with Rs 109,190 crore revenue loss, Rs 92,853 crore of which has already been accounted for in the first half of the fiscal.
- 1 The profit being earned on petrol and diesel would not be enough to wipe out the net losses of the three firms reported in the second quarter ended September 30, 2008.
- 1 Indian Oil posted its largest-ever net loss of Rs 7,047.13 crore in the July-September quarter.
- 1 BPCL posted a net loss of Rs 2,625.17 crore in the second quarter on top of an Rs 1,066.70 crore loss in the April-June period,
- 1 While Hindustan Petroleum reported Rs 888.12 crore losses in the first quarter and another Rs 3,218.92 crore in the second quarter.

Meltdown Effect

The overall growth in the world consumption of oil has been marginal. From 84.9 million barrels per day in June 2007, the world consumption barely rose by 0.22 mbpd to 85.12 mbpd in May 2008, a miniscule 0.26 percent rise. However, even in the so-called "oil guzzling" economies of china and India, the increase in consumption has been average. India's consumption has been increasing around 6% in 2007-08. But since India's overall consumption is much less than that of the US and china, the increase in consumption is comparatively insignificant. Clearly, there has been no significant growth in the world oil consumption to warrant the runaway prices.

The slide in global crude prices from their stratospheric level began only in the last couple of months, since the onset of the global financial market meltdown and a looming recession in developed countries. The fall in crude prices followed the general downtrend in commodity prices the world over and this got further accentuated by the apprehension of a slowdown in manufacturing activity across countries, which is turning out to be real than apparent.

The public sector OMCs (Oil Marketing Companies) source their products from the refineries on import parity basis which then becomes their cost price and the difference between the cost price and the sale price signified the under-recoveries of the OMCs. The under-recoveries for 2008-09, originally estimated at Rs 2.45 lakh crore in June 2008 when the global crude prices ruled the highest, are currently estimated at Rs 1.47 lakh crore based on the prices of the second half of October 2008.

The Hot Oil:

Of course, the prices of crude oil have been on an upward trend since 2002, but the rise has been gradual from around \$20 per barrel at the beginning of 2002 to \$70-75 per barrel in mid 2006 after which the prices corrected till they touched the \$50 per barrel level in January 2007 and the least \$45 per barrel in the 2008.

But, thereafter oil has been on fire, scorching of households across the globe. The desperation over runaway oil prices is high, especially so in countries like India, where the multitudes have got used to getting petrol, diesel, LPG and kerosene dirt cheap since ages, thanks to the subsidy largesse.

Subsidy Scheme

- 1 The kerosene price, for instance, has hovered at around Rs 9.05/kg since 2005 and the government has extended the PDS kerosene and domestic LPG subsidy scheme 2002 and freight subsidy (for far-flung areas) to March 31, 2010.
- 1 The point to ponder is on each litre of PDS kerosene during the year 2007-08 (April to December 2007) the subsidy was Rs 16.02, of which the oil companies bore Rs 15.20 and the contribution from the Government budget was 82 paise.
- 1 In case of domestic LPG, the per cylinder subsidy amounted to Rs 201.67 during the reference period, of which the contribution from the government budget was Rs 22.58 and the amount borne by the oil companies was Rs 179.09.
- 1 A recent House Panel report of the Ministry of Petroleum & Natural Gas states that a massive amount of Rs 73,250 crore was collected by the Government from the cess slapped on indigenous crude since the introduction of the Oil Industry (Development) Act, 1974 till end-December 2007, out of which a paltry sum of Rs 902.40 crore was disbursed to the Oil Industry development Board (OIDB).

Who Benefits From Subsidies?

So, who is the beneficiary of the government's largesse? Obviously, all sections of the society, including the rich, middle class and the poor! The government subsidizing the kerosene, which is mainly used by the poor for cooking on kerosene stoves and for lightning lanterns in villages. But one fails to understand the rationale behind subsidizing diesel and LPG which are mostly used by middle, upper middle and affluent classes. The huge subsidy on domestic LPG is not used by the poor, but by the middle, upper middle and affluent classes, who can easily afford Rs.648 per cylinder (without subsidy). Also diesel used in cars (including Mercedes!) and other vehicles used by the affluent sections of society needs no subsidy.

The average subsidy per selling unit on Domestic LPG & PDS (Public Distribution System) Kerosene works out as under:-

Year		Domestic LPG	PDS Kerosene
		Rs./Cylinder	Rs./Litre
2002-03		67.75	2.45
2003-04	At 2/3 rd level	45.17	1.63
2004-05	At 1/3 rd level	22.58	0.82

CRUDE OIL PRICES

2008

January	\$84.70	July	\$126.16
February	\$86.64	August	\$108.46
March	\$96.87	September	\$96.13
April	\$104.31	October	\$68.50
May	\$117.40	November	\$49.29
June	\$126.33	December	
		2008 Average	\$96.80

2007

January	\$46.53	July	\$65.96
February	\$51.36	August	\$64.23
March	\$52.64	September	\$70.94
April	\$56.08	October	\$77.56
May	\$55.43	November	\$86.92
June	\$59.25	December	\$83.46
		2007 Average	\$64.20

If the cost price of petrol per litre is Rs 58.90, following is the break up of cost calculated by the government.

Basic Price:	Rs 28.93
Excise duty:	Rs 14.35
Education Tax:	Rs 0.43
Dealer commission:	Rs 1.05
VAT:	Rs 5.5
Crude Oil Custom duty:	Rs 1.1
Petrol Custom:	Rs 1.54
Transportation Charge:	Rs 6.00
Total price:	Rs 58.90

Company Basic Price calculation - Considering that the current price of crude oil is \$107 (on September 22) per barrel, cost of per barrel in RS will be $107 \times 45.40 (1\$ = \text{Rs}45.40) = 4858$.
 One barrel consists of approximately 160 litres. So Price of crude oil per litre will be $4858/160 = \text{Rs}30.36$
 (It is the cost of crude oil per litre).

Petrol cheaper by Rs.5 a litre, diesel by Rs.2 as on 6th December 2008

Date	Petrol	Diesel	Kerosene	LPG
Feb16,2007	42.85	30.25	9.09	294.75
June 6,2007	43.52	30.48	9.09	294.75
Sept 27,2007	43.52	30.48	9.15	294.75
Feb 15,2008	45.52	31.76	9.15	294.75
June 6,2008	50.56	34.80	9.15	346.30
July 18,2008	50.62	34.86	9.15	304.70
Dec 5,2008	45.62	32.86	9.15	304.70

Conclusion:

Though oil prices are depressed now, the long-term prognosis is one of expensive oil. Once the global economy rides out the current storm and growth returns to the developed economies, oil prices are bound to bounce back. When that happens, India, which depends on imports for three out of every four barrels that it consumes, could find itself in a similar situation as the last two years. Therefore, whichever way one looks at it, this is the best opportunity in a long time for the government to free prices. Soon, it will announce a cut in domestic fuel prices.

Simultaneously, it should free itself of the burden of fixing prices and transfer the responsibility to the oil companies. If current fortunes hold, who knows, the oil companies may even have the chance to further cut prices in the near future.

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