

# Petroleum Prices

## Why they are so important for our Economy

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**P**etroleum prices are always a cause of concern for everyone. Will the Central government oblige and reduce the taxes or will the State government come forward? When will they be brought under the ambit of GST and how much help in stabilizing its prices?

For understanding petroleum pricing in India: We have to break it into following aspects:

The central and state governments tax collection on the petroleum sector in the last few years is as follows:

Year	2014-15	2015-16	2016-17	2017-18 (P)
1. Contribution to Central Exchequer (in crore) through Tax/ Duties on Crude oil & Petroleum products	1,26,025	2,09,354	2,73,225	2,84,442
2. Contribution to State Exchequer (in crore) through Tax/ Duties on Crude & Petroleum products	1,60,526	1,60,114	1,89,587	2,08,893
3. Total Contribution of Petroleum Sector to Exchequer through Tax/ Duties (1+2)	2,86,551	3,69,468	4,62,812	4,93,335



1. Petroleum prices component
2. Issues of under recovery and oil bonds during UPA
3. Revenue to Central and State governments from the petroleum section.
4. Alternative Sources of energy and future planning for reduced dependence on oil.

Petroleum products pricing is always a contentious issue. It has a large impact on inflation and also a major source of revenue for the Central and State governments, we import about 80% of our consumption needs. An increase of one dollar in the international price of crude oil increases the cost of our petrol and diesel by Rs. 0.50/ litre and one rupee fall in exchange rate against US dollar increase the cost by Rs 0.65/litre of petrol and diesel. We can conclude that the prices of petroleum products are determined in India by external factors. India imported 256.32 million metric tonnes of crude oil and petroleum products in 2017-18 and paid Rs. 6,52,896 lakh crore

Earlier under Administered Price Mechanism (APM) followed by UPA, petrol and diesel prices were not market determined. Steep increase in international prices of oil used to put severe pressure on the oil marketing companies (OMC). Still their retail prices were kept below the cost, resulting in under-recoveries for OMCs. Between the year 2004 to 2014, the total under-recoveries was to the tune of Rs. 8,53,628 crores.

When the international crude prices were increasing, during the period of 2004-08 the subsidy by the government on petroleum products became insufficient. Since the fiscal position of the Government was very bad, there was no scope for increasing the subsidy. The government started issuing 'oil bonds' to the OMCs instead of giving cash subsidy. These interests bearing Oil bonds were not even reflected in the Budget provision by the UPA Government, resulting in distortion of fiscal deficit figures. During 2005 to 2010, oil bonds for Rs. 1,42,202 crore were issued, with rate of interest on them ranging from 7.33 to 8.4 % per annum repayable up to 2024-25 by successive

The energy mix of our consumption is:

Sl. No.	Source	Share (in percentage)
1.	Coal and Lignite	46.28
2.	Crude Petroleum	34.48
3.	Electricity from hydro, nuclear and other renewable sources	12.75
4.	Natural Gas	6.49

**BAD FISCAL PRUDENCE UNDER UPA GOVERNMENT RESULTED IN INCREASING OF THE INTEREST RATES AFFECTING BORROWING AND INVESTMENT IN THE ECONOMY AND HIGHER INFLATION FOR THE COMMON MEN. WHILE THE PETROL AND DIESEL PRICES WERE ARTIFICIALLY KEPT LOW, PEOPLE WERE PAYING HIGHER PRICES FOR ALMOST EVERY OTHER THING.**

governments in the future. This was a case of postponing current liabilities on the future generation.

Bad fiscal prudence under UPA government resulted in increasing of the interest rates affecting borrowing and investment in the economy and higher inflation for the common men. While the petrol and diesel prices were artificially kept low, people were paying higher prices for almost every other thing. The burden sharing mechanism devised by the UPA government had also led to a depletion of cash reserves of oil companies like ONGC, GAIL and OIL and destruction of their intrinsic market value.

The argument that high taxed on petroleum product in India needs to be brought down to control the spiralling prices has to be closely looked into.

Firstly, this revenue is required for catalysing India's economic growth, for building infrastructure for better quality of life and providing social security to the poor classes and in the backward areas. Secondly, large component of Central government duties on petroleum products i.e. 42% of the Basic Excise Duty is given to State governments and 60% of the balance 58% of the Basic

Duty is spent on Centrally Sponsored welfare schemes in the States i.e. total amount transferred to the States by the Centre is  $(42+34.8)= 76.8\%$  of the Basic Excise Duty. It is also estimated that a one rupee reduction in the excise duty at the Centre would reduce revenue collection by Rs 14,000 crores.

Increase in the petroleum prices has different effect on the tax collected by the Centre and the States, which also has to be analysed properly. In a decontrolled regime now being followed in India, any change in international crude price is passed on to the consumer. Higher prices are likely to reduce consumption. The taxes imposed by the Centre are specific tax, i.e. fixed in terms of Rs per unit. So, if the consumption falls, the tax collected by the Centre goes down. The States, however, levy ad valorem taxes i.e. percentage based on prices and therefore with the increase in petroleum prices, its tax collection does not fall even with fall in consumption. Therefore, if the taxes on petroleum products have to be reduced in wake of the rising international prices, it should be done by the States first than by the Centre.

The solution to this teething problem on the long-term basis, is to change the share of petroleum products in energy consumption mix (34.48%, year 2015-16) We need to generate more energy from coal and lignite (46.28%), which and also focus on electricity generation from hydro, nuclear and other renewable sources like wind and solar (12.75%). Shri Narendra Modi government is working on this line. In the coming years we will definitely see a fall in the contribution of petroleum products in the overall energy share in our consumption.