

## Government finally pedals on oil reforms, albeit partially

*The Financial Express*  
June 26, 2010

*Author: Gokul Chaudhri, Partner*

The Economic Survey in 2009 set the ball rolling for the much-needed reforms in the downstream oil and gas sector of India. The resultant constitution of the expert group headed by the Planning Commission member Kirit Parikh was required to advice on viable and sustainable system of pricing of sensitive petroleum products. The announcement of the expert group was met with skepticism given the history of several aborted attempts to reform the fuel subsidies.

In January 2010, the expert group recommended market-linked prices for petroleum products. The key suggestions included---decontrol of petrol prices with immediate effect, followed by diesel; partial increase in price of PDS kerosene by Rs 6 per litre and domestic LPG by Rs 100 per cylinder; impose windfall tax on blocks awarded to state-run oil companies ONGC and OIL on nomination basis for financing under-recoveries incurred on account of domestic LPG and PDS kerosene; and providing cash subsidy from the Union budget for meeting the remaining gap. The prime minister responded to the recommendations by constituting an empowered group of ministers (eGoM); the two central issues to be deliberated upon by the eGoM were (a) degree of decontrol; and (b) the timing of implementing such decision.

Very much on expected lines “a bare minimum decontrol” was agreed, as the eGoM deregulated the relatively less controversial petrol prices and maintained a status quo on the sensitive petroleum products with moderate upward price revisions. The eGoM decided to revise upwards the price of petrol by Rs 3.50 per litre; diesel by Rs 2 per litre; Kerosene by Rs 3 per litre; and LPG by Rs 35 per cylinder.

Deregulating petrol prices is a progressive decision that the government has taken towards oil reforms; deregulation of petrol prices is expected to help existing oil companies as these will now be free to decide the selling price of petrol. Further, out of the under recoveries incurred on account of sale of sensitive petroleum products, petrol accounted for 8% of the under recoveries.

Under recoveries are expected to scale down as a result of deregulation of petrol prices. The attempt of the eGoM is to chip away at the problem. While, on the one hand petrol prices have been deregulated, on the other hand, the government has deferred the reform process by announcing only a partial increase in prices of other sensitive petroleum products. The larger share of under recoveries is still on account of three petroleum products vis diesel (34%), Kerosene (PDS) (30%) and LPG (Domestic) (28%). Under recoveries on account of these three petroleum products was earlier estimated at Rs 67,800 crore. With partial price revision on these products, it is expected to scale down under recoveries by only 22% (i.e. Rs 146 billion), still leading to under recoveries to the tune of Rs 53,200 crore.

### Our Locations:

<b>Bangalore</b> +91 80 4032 0000	<b>Mumbai</b> +91 22 3021 7000	<b>New Delhi</b> +91 11 3081 5000	<b>Chennai</b> +91 44 4298 7000	<b>Singapore</b> +65 6408 8004
<b>Bahrain</b> +973 1364 6676	<b>London</b> +44 20 7849 6100	<b>New York</b> + 1 212 880 6499	<b>Santa Clara</b> +1 408 834 4699	

New investments in the downstream sector are likely to remain sluggish given the governments deferment on deregulating diesel prices. Crude oil prices are currently stable, and the concern is if the reform agenda will continue to be pursued should there is a sharp rise in oil prices or a strong political opposition

**Our Locations:**

<b>Bangalore</b> +91 80 4032 0000	<b>Mumbai</b> +91 22 3021 7000	<b>New Delhi</b> +91 11 3081 5000	<b>Chennai</b> +91 44 4298 7000	<b>Singapore</b> +65 6408 8004
<b>Bahrain</b> +973 1364 6676	<b>London</b> +44 20 7849 6100	<b>New York</b> + 1 212 880 6499	<b>Santa Clara</b> +1 408 834 4699	