

Oil Prices and Indian Economy

*Note: Editorial written for Economic Journalist: 2000 **

The rise in crude oil prices has affected the Indian economy quite significantly in the current year. While this rise has led to a relatively high inflation rate in WPI terms it is also impacted current account deficit of the country on the other. The contribution of fuel, power, light and lubricants group to the annual inflation as on January 27,2001 on point-to-point basis was very high since overall WPI based on point-to-point basis rose to 8.2 percent while it was only 2.4 percent excluding the above group of commodities. The current account deficit is also expected to grow to 1.5-1.7 percent of GDP in the current year, as compared to only 1.1 percent in the previous year.

In more specific terms, domestic crude oil production during first 8 months of the current year registered an increase of only 0.4 percent compared to the same period last year. On the other hand, the consumption of petroleum products including imports by private parties during first 8 months of the current year was 0.8 percent lower at 62.2 million tonnes in comparison to the same period last year. Thus even though total consumption of petroleum products in the current year was a little lower, galloping international prices of crude oil made all the difference in the inflation rate on the one hand and deterioration in the current account on the other.

As for natural gas, production in the first 8 months of the current year had shown an increase of 4.4 percent compared to the same period last year at 19.62 billion cubic metres (bcm). Even this increase did not help very much in curbing the deterioration in current account as well as inflation scenario.

Need to Crcale Self Reliance

While India had reached a figure of 50 percent self-reliance, and even more, in the 1980s, the level of self-reliance has been declining for sometime. It was only 33 percent in 1999-2000 and is expected further to go down to as low as 30 percent in the current fiscal year 2000-2001. As a consequence of this realization of the deterioration in the petroleum sector contribution to the national economy, government is taking steps to increase domestic production of crude oil by offering blocks under the new exploration licensing policy.

The rise in oil prices abroad is however not a phenomenon only of the current year. The overall price of crude oil had also increased in the previous year albeit at a much lower rate. The cumulative effect of 2 years' rise in oil price scenario, however, has had quite a negative effect on the Indian economy and perhaps on economies of most other developing countries.

Some discerning economist has suggested that future of the world lies with only two types of economies, those using frontier level technologies and those with considerable resources under the crust of their lands. Economies using middling technologies such as India's have limited future. If this be the scenario options are on the one hand to go all out to discover some more economic resources under the crust of our lands and on the other to move forward towards frontier technologies. The sooner we do that the safer our future will be.

Oil pool deficit is also a matter of concern. Years ago corridor gossip in the North Block used to be that budget is floating on oil. Today, the scenario has changed almost completely and to an extent it appears to be sinking under oil. There are enough indicators that government will have to deal more firmly with the prices of petroleum products than hitherto it has had the courage to do. The more it places the task of pricing into private hands the less politically exposed government will be to changes in the price management without much political fall out. It will also help better demand management by keeping demand and supply in automatic and continuous balance, without loss of time.

We are hopeful that our forward-looking Finance Minister will initiate some steps in this direction in the forthcoming budget and lay down guidelines for gradually doing away with petroleum products subsidies which currently find a place under administered prices regime.

* S.P. Ahuja
Hony. Director-CERPA