

Analysis of the Kirit Parikh Committee Recommendations

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Kirit Parikh Committee recommendations are positive, but implementation is the key

An experts group, headed by former Planning Commission member Kirit Parikh, submitted its much awaited report on pricing policy for four major oil products, namely, petrol, diesel, kerosene and LPG.

The committee has recommended that prices of petrol and diesel to be market-determined, both at the refinery gate and retail levels, whereas the prices of kerosene and domestic LPG can be partially raised by Rs 6 per litre and Rs 100 per cylinder respectively. For kerosene and LPG, the committee has recommended linking fuel prices with per capita income and selective allocations to poorer families through smart cards linked with unique identities (UID) project.

The committee has accepted the subsidy formula proposed by Oil and Natural Gas Corporation (ONGC) aimed at reducing burden of oil companies. The formula suggests an incremental rate of taxes on higher crude oil price realization from the nomination blocks of ONGC and Oil India Ltd (OIL). The proposed subsidy sharing formula shall keep the government's subsidy contribution from budget in the range of Rs 19,780-23,340 crore at various crude price levels. A summary of recommendations and their impact has been provided in Annexure.

According to **D.R.Dogra**, Managing Director & CEO , **CARE Ltd**. " The impact on the oil and gas industry, if any of the recommendations by the committee is implemented, will be extremely positive" The complete deregulation of auto-fuels and sharp hikes in the prices of cooking fuels would help the government in reducing fiscal deficit and thus curtail its borrowings. The three public sector oil marketing companies, namely, Indian Oil Corporation, Bharat Petroleum Corporation Ltd and Hindustan Petroleum Corporation Ltd, would be able to reduce their under-recoveries considerably. However, the complete deregulation may prompt private players such as Reliance, Essar and Shell to re-open their retail fuel outlets, putting pressure on market share of public sector oil marketing companies (OMCs). In the past, the entry of private players in retail fuel market had resulted in an

erosion of about 10 per cent in the market share of public sector OMCs. The proposed hike in prices of cooking fuels coupled with reduction in allocation of kerosene under the public distribution scheme (PDS) by 20 per cent would reduce under-recoveries by about Rs 16,454 crore, whereas, the auto-fuel deregulation would avert Rs 13,997 crore of under-recoveries.

In the opinion of **CARE Research**, this is a landmark report, but implementation is the key. Although the report is in line with the wish-list of most of the market participants, implementation of the recommendations needs to be keenly watched for. "The situation is tricky for the Government, as it needs to strike a balance between reducing the subsidy burden on the public sector oil and gas undertakings, reducing the fiscal deficit and managing the current inflationary scenario, given the economy being in the process of revival and attempting to restore its buoyancy" added **Mr Dogra**. It may be noted that similar kind of recommendations made by the Chaturvedi committee in 2008 were rejected by the government. Also, practicability of the selective allocations to poorer families through smart cards linked with UID project also needs to be evaluated by the government keeping in view the infrastructure requirement for the same. Although diesel is a major contributor to the total under-recoveries, its deregulation needs to be carefully evaluated as the agriculture sector (consuming 12 per cent of diesel) and transport industry (consuming 40 per cent of diesel), the backbone of the Indian economy, are the major consumer of the fuel.

Annexure

Summary of Recommendations by the Kirit Parikh Committee

Fuel	Pricing	Reasoning	Under-recoveries
Petrol	Market-determined both at the refinery gate and retail levels. Price hike of around Rs.7/litre and Rs. 23/litre at the oil price of \$80/bbl and \$120/bbl respectively.	1) Small impact on inflation. 2) Primarily used by the upper 2-3% of household. 3) Incentive to increase vehicle efficiency by 20%.	Nil if recommendations are accepted. No comments on calculation methodology.
Diesel	Market-determined both at the refinery gate and retail levels.	1) Agricultural Sector (12% consumption) - Adjust MSP to account for rise in prices. 2) Trucks and LCV (40% consumption) - Incentive to increase efficiencies. 3) Industrial users would be able to fully-pass on increased price, resulting in similar inflationary impact as subsidies. 4) Car owner - No social reason to subsidize.	Nil if recommendations are accepted. No comments on calculation methodology.
	An additional excise duty on a diesel vehicle to bring it at-par with petrol driven cars. At the current levels of usage, an additional excise duty payable amounts to about Rs.80,000/year.	Differential taxation on petrol and diesel causing more usage of diesel. Petrol and Diesel tax should bring on parity.	
PDS Kerosene	Price of PDS kerosene be raised by Rs.6/litre (~66% hike) to around Rs. 15/litre and should be revised every year in-line with per capita agricultural GDP at nominal prices.	Only 1.3% of rural household use PDS Kerosene for cooking purpose. Among the poorest 4%, 60% use PDS Kerosene for lightening purpose.	No comments on calculation methodology.
	Rationalize distribution of PDF Kerosene to BPL families to 2 litres per month. Promote rural electrification, LPG distribution for lightening purpose.	Out of the current norm of 5 litres/household per month, most of the households use only 3.5 litres per month.	Reduction in allocation by 20% would reduce subsidies by Rs. 3,484 crore.
	Distribution of PDS Kerosene to BPL families through smart cards with biometric identification linked with UID project.	Reduced adulteration. Estimates suggest 35% or more of PDS kerosene is diverted for unauthorized purposes including adulteration.	Increase in price by Rs.6/- on the reduced quantity would reduce subsidies by Rs. 5,390 crore.
	Bring down the all india allocation by at least 20%.		
LPG	Increase the price of domestic LPG cylinder (14.2 kg) by at least Rs. 100. The price should be periodically revised based on the per capita income.	1) High unintended uses. 2) Rural households resort to alternative fuels. 3) Subsidies to the targeted group such as the BPL rural households can be delivered as entitlements or through direct cash transfers to be given to the woman of the household.	No comments on calculation methodology. Increase in price by Rs.100/cylinder would reduce subsidy burden by 7,580 crore.
Subsidy Sharing	Accepted the formula proposed by ONGC, involving incremental tax rates on higher crude oil price realization from the nomination blocks.		The formula shall keep the government's share in the range of Rs 19,780-23,340 crore at various crude price levels.
Taxation	No comments	Government is currently preparing roadmap for the introduction of the Goods and Services Tax (GST) with effect from 1st April, 2010.	
	No windfall taxes		

Source: Compiled by CARE Research