Natural gas — IV

Need for regulatory body

Uttam Gupta

THE increase in gas prices in recent years, has led to a substantial increase in the cost of production and, consequently, higher subsidy having to be paid under the RPS. Further, the increase in prices which would inevitably follow in the event of adopting the equivalence principle at current cost of alternate fuels/feedstock, will raise subsidy to mind-boggling proportions and make the situation unsustainable.

The adverse implications of the developments of the last two years are showing up but there is hardly any sign that the Government is picking up the warning signals. Far from undertaking a damage limitation exercise, it plans further policy changes which will only aggravate the situation. The proposed move to deregulate the hydrocarbon sector, including freeing the price of gas, is one major step in this direction.

Given the monopolistic nature of the gas industry, the shortage of gas and the emergence of new contenders, including those who can pay any price, the gas companies are bound to increase prices steeply, making the commodity available to those who are prepared to pay. From this angle, the fertiliser industry will be seriously handicapped as the farmers do not have the unlimited capacity to pay. Under the present system of administered pricing this would increase subsidy to unsustainable levels in the eventual decontrol and would sound the death knell of the industry.

This would be detrimental to the interests of the gas companies as well. The fertiliser industry, with a share of 40 per cent of total gas production, is the biggest consumer of gas. In the event of this industry being unable to take the bulk of its present consumption, because it cannot afford a price that would satisfy gas companies, the latter too would suffer a serious financial loss. Besides, it would also result in under-utilisation of the gas supply and distribution infrastructure.

Urgent attention is needed to salvage the situation. At the outset, the government must set at rest any speculation regarding the deregulation of the pricing and distribution of gas by announcing that the existing administered arrangement will continue.

Having cleared the uncertainty on this front, the Government should categorically spell out the policy on allocation of gas. This policy statement cannot be based on who is willing to pay and how much. Instead, it has to be viewed in the context of national economic considerations. Fertilisers should be assigned top priority as in the past. Contractually committed quantities, including the requirements for steam generation and captive power, should be made available to all existing gas-based plants.

Supplies for facilitating the future development of the industry have also to be ensured. In this context, according to the Eighth Plan working group on fertilisers, the demand for nitrogen for the year 1999-2000 has been projected at 12.5 million tonnes. As against this, and after taking into consideration the contribution to the production capability from projects currently under implementation and expansion schemes, the likely production by 1999-2000 will be about 9.2 million tonnes. This leaves a deficit of 3.3 million tonnes nitrogen uncovered.

After taking into account the incremental contribution from phosphatic fertilisers to cover the projected P205 deficit and providing for reasonable supplies through import of urea, about 1.8 million tonnes nitrogen will have to be made good by adding about four million tonnes equivalent of additional urea capacity. On the basis that about 750 cubic metres of gas are required for producing one tonne of urea (this includes the requirements for steam generation and captive power), the total requirement of gas to support this capacity (four million tonnes) will be about three billion cubic metres per annum. Unless this much extra gas is available, the additional urea capacity cannot be supported.

Presently, about four million tonnes per annum of urea capacity is from plants based on naphtha. Because of the higher price and lower conversion efficiency vis-a-vis gas, the feedstock/fuel cost in these plants, and consequently the cost of production, is higher. This additional cost is being supported by subsidy from the Government under the Retention Pricing Scheme. However, in a situation of ultimate decontrol of urea and concomitant abolition of the subsidy scheme, there could be a serious threat to the continued viability of these plants. In the context of the overall increasing demand and resultant high deficit, the country cannot afford to lose this capacity. The only way of ensuring their continued viability would be to facilitate their switchover to natural gas which would require an additional about 3 billion cubic metres of gas per annum.

The contracts for the supply of gas to fertiliser plants should be made equitable, fair and non-discriminatory. The gas companies should refrain from imposing one-sided and unfavourable terms and taking any unilateral action that would deviate from and violate the spirit of the agreement.

The Government may set up a gas regulatory authority (somewhat on the lines of the regulatory commission in the US) which should provide broad guidelines with regard to major aspects of pricing and distribution and also monitor the implementation and working of various arrangements. The functioning of the authority should be transparent and adequate opportunity should be given to the major user industries, including fertilisers, for projecting the implications of various proposals.

Finally, the prices of gas should be fixed in a fair and reasonable manner. All the anomalies pointed out by the JPC regarding the fixing of the basic price of gas and the transportation charges should be removed and the necessary downward adjustments in the prices made. Besides, various taxes and duties such as royalty on gas, central sales tax and sales tax should be removed to prevent a cascading effect on the prices charged to the plants.

(Concluded)

(The author is Chief Economist, The Fertiliser Association of India.)