Analysis

The Financial Express

NEW DELHI • MONDAY, NOVEMBER 10, 1997

Fleecing consumers and producers

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AFTER a lull of about two and a half years, the government has once again raised the price of natural gas. It has decided, in principle, to link basic price of domestic gas to international price of a basket of fuel oil (FO) and set the former at 55 per cent of the latter during 1997-98, per cent in 1998-90 and per cent during 1999-2000. Thereafter, it proposes to examine the possibility of setting gas price at 100 per cent of FO world market price.

On this basis, from October 1, 1997, basic price at land fall point/on-shore gas has been increased from Rs 1,850 per thousand cubic meter (tcm) applicable for quarter-ending December 21, 1997. This works out to an increase of Rs 300 per tcm. However, after including royalty, central sales tax and local taxes - levied on an ad valorem basis - increase in cost to users will be about Rs 380 per tcm.

For users of gas in north-east region - hitherto enjoying a concessional price of Rs 1,000 per tcm - basic price is proposed to be set at 35 per cent of international basket of FO in 1997-98, 45 per cent in 1998-99 and 55 per cent in 1999-2000. On this basis, revised price is Rs 1,200 per tcm i.e., an increase of Rs 200 per tcm. After including taxes and duties, effective increase works out to about Rs 220 per tcm.

The basic price to users of gas along HBJ pipeline has also gone up from Rs 1,850 per tcm to Rs 2,150 per tcm. However, they will be affected much more as charge for transport through HBJ is up from Rs 850 per tcm to Rs 1,150 per tcm. The total impact after including additional royalty, CST and ST, will be about Rs 700 per tcm.

The ball does not stop here. The basic price is set to increase progressively to reach Rs 2,850 per tcm by the year 1999-2000. Corresponding to this, after including royalty/taxes and transport charge, on-shore plants will paying about Rs 3,500 per tcm and those along HBJ, Rs 4,500 per tcm. These will be Rs 1,300/1,400 per tcm higher than existing level i.e., prior to October 1, 1997.

Ironically, while the Shankar Committee wanted Rs 2,850 per tcm to be reached in five years from now, the government has decided to achieve this level in three years only, it could be reached even earlier. This is because the price is linked to world market price of FO. Although, the latter has been more or less steady in fact a substantial increase henceforth is not ruled out.

The government of India has decided not to allow any more naphtha allocation to independent power producers (IPPs) as well as new fertiliser projects. This will induce shift to FO specially for power and resultant increase in import demand leading to higher prices. Moreover, by prescribing a band of Rs 2,140-2,850 per tcm, the government has virtually lent legitimacy to increase in price of gas to maximum limit any time.

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The increase in gas prices will significantly increase production cost of fertilisers. Taking the 600 cubic-metre need for producing a tonne of urea the cost of production of plants located on-shore e.g., KRIBHCO Hazira, RCF Thai, GSFC, Baroda etc., will increase by about Rs 230 per tonne and that of HBJ plants by about Rs 420 per tonne. The industry, on the whole, will have to shell out about Rs 420 crore per annum.

Corresponding to the basic price of Rs 2,850 per tcm, the increase in production cost will be about Rs 780 per tonne for on-shore plants and Rs 850 per tonne for HBJ units. The additional burden on industry under this scenario will be almost touching about Rs 1,000 crore per annum.

Under retention pricing and subsidy scheme (RPS), above will lead to corresponding increase in subsidy. However, reimbursement of the same is likely to be delayed leading to liquidity problems. This is because an additional budget allocation to cover increase in requirements is unlikely to be made as the government would not wish fiscal deficit to go out of control. There will be loss of profit as well as on delayed payments, no interest is paid.

Manufacturers of decontrolled complex phosphatic fertiliser who use domestic ammonia based on natural gas, e.g., Deepak Fertilisers and Petrochemicals, GSFC etc. will also be affected. Unlike urea which is covered by RPS, these producers' will remain unprotected as under the scheme of ad hoc concession, while concession amount is uniform - linked to price of imported ammonia - even selling price is also uniform.

The new structure of gas price is devoid of any valid reason not to talk of upholding principles of equality and justice. The linkage to price of FO is illogical and seriously flawed. Fuel oil is no substitute for gas. While, utility of latter is primarily for its chemical value and is used in manufacture of fertilisers and other petrochemicals, former is useful mainly for its heat value and most suited for power generation. In India, only 13 per cent of total N capacity is based on FO, against 50 per cent on gas. The world over, N capacity is mainly on gas; there is hardly any plant on FO.

Pricing of gas has to be on its own based on reasonable cost of production taking into account weighted average cost of gas from all fields. This principle was even suggested by the JPC (1992) which found serious anomalies in prevailing structure of gas price - latter was based on Kelkar Committee formula of linking price to FO. Unfortunately, bypassing JPC recommendation, the same anomalous system is being continued.

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