

Oil price may once again fall below \$45 per barrel: How does it bode for India?




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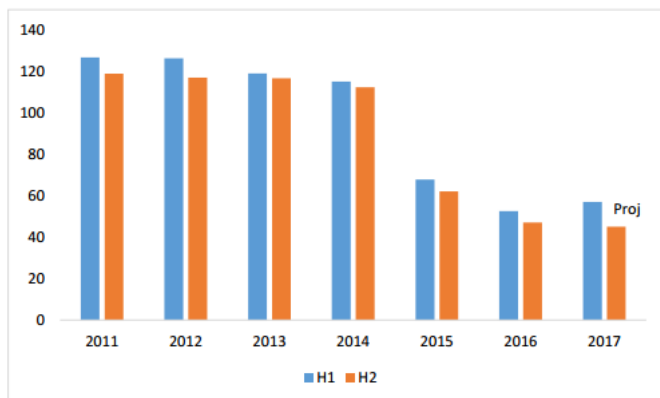
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Since the start of financial year 2017-18, there has been significant decline in the crude oil prices.

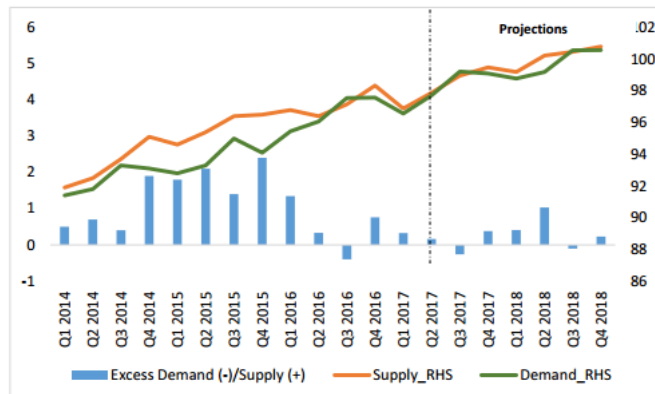
Price of crude oil has fallen more than 15% in recent weeks to around \$48 per barrel.

Graph 1: Crude oil prices (\$ per barrel)



Source: EIA, SBI Research

Graph 2: Crude oil - Demand and Supply (million barrels per day)



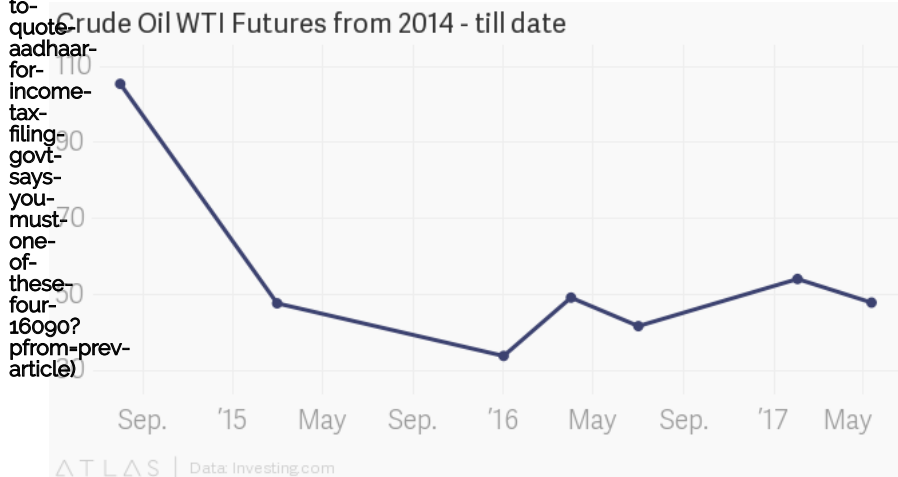
OPEC and other major producers had been enjoying higher prices since agreeing in November to slash production, a strategy designed to rid global markets of excess supply. But now the strategy appears to be not working.

After November 2016, US West Texas Intermediate and Brent Crude reached to \$54.01 per barrel and \$56.82 per barrel.

Since mid-2016, US crude production rose by 10% to 9.3 million barrels per day (bpd) which close to the output of top producers like Russia and Saudi Arabia.

The US Energy Information Administration raised its forecast on 2017 U.S. crude-oil production to an average 9.31 million barrels per day in 2017 and 2018 output at 9.96 mn bbl/day.

Analysts at State Bank of India said, "Interestingly, our analysis of past few years (since 2011) indicate that oil prices in the second half are always lower than to the first half of that year."



Oil prices on an average were around 6% in second half of FY17, which is less than compared to first half of the financial year. Till date, the average crude oil prices are at \$54 per barrel (maximum: \$57).

Brent Oil Futures performance from 2014 - till date



SBI said, "Given the current trend in non-OPEC oil production, we believe that crude oil prices may dip below \$45 level shortly or even lower than that."

Care Ratings said, "The market believes that a further six-month extension of cutting back on output may not be enough. The cartel could however, reverse course and increase production in an effort to squeeze US producers out of the market."

Falling crude prices is good for India.

A decline in prices would lead to decline in petrol and diesel prices and thus easing inflation as crude oil accounts for 10% of the India's wholesale inflation index -- the WPI.

Since the start of financial year 2016-17, WPI has been rising consistently, so much so that in February it reached to a 4-year high due to rise in fuel inflation (21.0%) and lower base in the previous year's index. (http://www.zeebiz.com/india/news-dont-want-to-quotes-aadhaar-for-income-tax-filing-govt-says-you-must-one-of-these-four-16090?pfrom-prev-article=print)

For India Inc too falling oil prices bode well. Fast moving consumer goods sector is already facing hard times. Therefore, any decline in crude oil prices comes as a positive for the sector as input cost will come down due to easing fuel prices.

Aviation: Lower crude oil prices comes as an opportunity for aviation firms as they expect reduction in jet fuel prices which accounts for nearly 50% of airlines' operating cost. There are directly linked with international crude prices. The aviation turbine fuel (ATF) prices has increased by 38% year-on-year and 11% quarter-on-quarter (QoQ) basis in fourth quarter ended four March 31, 2017, as per ICICI Securities.

Paint: Drop in crude prices means cheer to paint firms like Asian Paints, Berger Paints and Kansai Nerolac. As per reports, titanium dioxide and other crude derivatives such as PAN and PENTA together form about 40-50% of total input costs for these companies. A 10% fall in these inputs prices will add up to 7-10% in their earnings.

SBI added, "We believe Saudi Arabia has now realised production cuts need to be implemented for at least 12-18 months to reduce the inventory glut. This would only serve to boost US shale production further, and cause a major decline in Saudi's already falling market share"

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