14th OPEC and non-OPEC Ministerial meeting: April supply cuts and its Impact on India

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Overview

Since the last meeting convened by the OPEC+ group in the start of CY21 (5thJanuary 2021), crude oil prices have been on a rise and recovering even though the pandemic persists worldwide.

Oil prices have been on a rise due to restrained U.S. oil production, vaccine inoculation drive undertaken by various countries and additional stimulus packages in key economies. Brent crude oil price breached the USD 60/bbl mark after 13 months during February 2021. Oil prices were also impacted and have increased due to the winter storm in Texas (the largest oil producing state in the US) which led to US crude production to drop by more than 10% (or by 1 mb/d), while refining activities too suffered because of the freeze. Operations and facilities in the state have now resumed but not fully.

Oil prices have also increased due to the additional output cuts undertaken by Saudi Arabia in February 2021, which, is being continued in March 2021 followed by reductions followed/assumed by other members of the OPEC and its allies. Since the April 2020 meeting, OPEC and non-OPEC countries had withheld 2.3bn barrels of oil by end of January 2021, accelerating the oil market rebalancing.

In the January meeting, the cartel agreed to adjust the total production cuts to 7.125 million bpd for February and 7.05 mb/d for March.

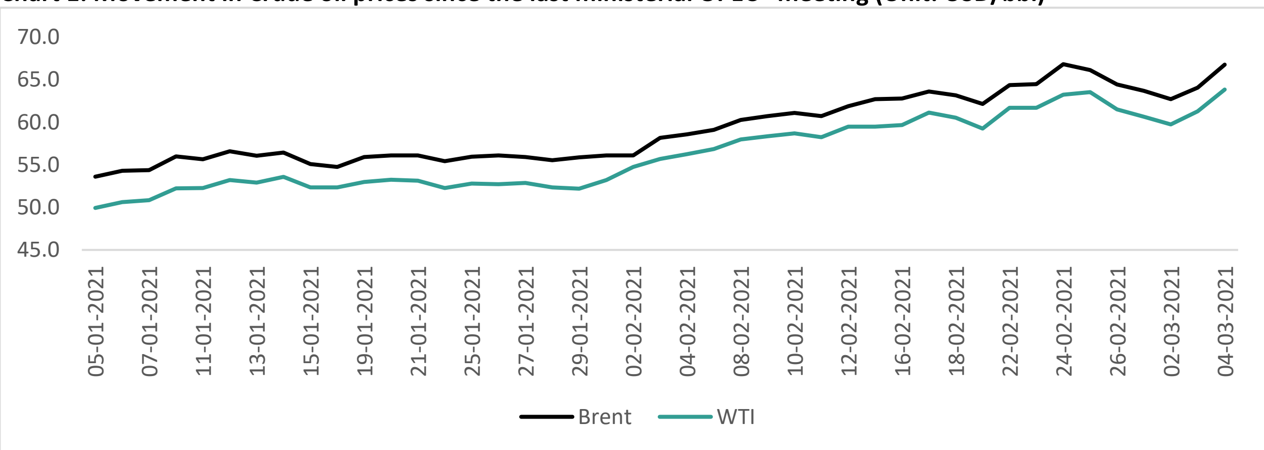
Table 1: OPEC+ Production Cuts (Unit: mb/d)

Dec-20	Jan-21	Feb-21	Mar-21
7.7	7.2	7.125	7.05

Source: OPEC, CARE Ratings
*mb/d million barrels per day

Verdict: OPEC+ members have decided to continue the production levels of March-21 for the month of April-21, with the exception of Russia and Kazakhstan, as they will be allowed to increase production by 130 and 20 thousand barrels per day respectively, due to continued seasonal consumption patterns. Saudi Arabia will be extending the additional voluntary adjustments of 1 mb/d for the month of April 2021 and participating members who have not been able to maintain and achieve its requisite quota of cuts will be allowed to achieve full conformity and make up for pervious compensation shortfalls till the end of July 2021.

Chart 1: Movement in Crude oil prices since the last ministerial OPEC+ meeting (Unit: USD/bbl)



Source: Bloomberg

Since the previous meeting held (January 5th2021) till date, Brent crude oil price has increased by 24.5% while WTI has increased by 27.8%. In the previous financial year, crude oil prices were on a downward trajectory since the start of CY20 due to the advent of COVID-19 in China and was falling further due to its spread in other countries from its epicentre. Post the announcement and decision taken during the 14th Ministerial OPEC+ meeting, crude oil prices have increased by 4.2%.

Concluding Remarks

Oil markets have been reacting positively with the supply cuts undertaken by the cartel and with US oil production too being restrained, with this OPEC has once again become the de facto controller of the oil markets. It was expected that the meeting would conclude with more supply being pumped in for April as demand has picked up, especially in Asia and particularly in China, which has recovered more quickly than other regions from the economic fallout from the pandemic but the cartel is still being cautious on the oil-based recovery. It will be crucial to see the reaction of the markets towards the on-going supply cuts considering the second wave of the pandemic and related lockdowns can put a damper on demand.

Price call

Price of crude oil will be elevated and **range between USD 65-68/bbl** creating a new base for oil prices. Vaccination programs against the coronavirus have been gathering pace, potentially leading to increased economic activity, more air travel and greater demand for oil this year and in addition, production growth from shale producers in the US is also expected to be restrained this year.

Impact on the Indian economy

The recent increase in oil price has not been favourable for the Indian economy considering how the country imports more than 80%-85% of its oil requirements.

- **Trade:** Increase in the oil price prevalent, on a macro level, with imports of million (3.9*365) barrels of crude oil during FY21, a dollar increase in prices on a permanent basis would increase the bill by roughly USD 1.4 billion per annum. India's crude oil import bill had come down by 8.7% during FY20 to USD 102.2 billion and currently value of crude oil imported has fallen by 46.3% during 10M-FY21 to USD 47.2 billion
- **Inflation:** Crude oil and its products have a weight of 10.36% in the WPI. Of this, crude oil and natural gas have a weight of 2.41% and mineral oils around 7.95%. With the exception of LPG and kerosene (with combined weight of 0.83%), the rest would be driven by market forces. Therefore, any increase in the price of crude oil would tend to impact the WPI inflation number commensurately. In case of the CPI the impact of crude oil prices is directly related to the pass through to transportation fuels which has weight of 2.39%. Thus increase in the crude oil prices will impact the WPI more than the CPI.
- **Government Revenues:** The current high price of petrol and diesel can be ascribed to the high taxes levied by the government coupled with an increase in crude oil price. Unless the government does not cut the taxes levied on petrol and diesel, prices of the auto fuel is expected to further increase from the high high's it is already at. Currently as of 1st March 2021, the government, centre plus states are able to collect around 161% taxes, (Excise Duty and VAT) on the base price of petrol and 124% in the case of diesel. Taxes now make up around 59% of the retail price of petrol 54% of the retail price of diesel.
    - Petrol price now is retailing at Rs 91.2 in Delhi, in Rs. 97.6 in Mumbai, Rs. 93.1 in Chennai and Rs. 91.4 in Kolkata, per litre, respectively. Current price of diesel in Delhi, Mumbai, Chennai and Kolkata, is Rs 81.5, Rs 88.6, Rs 86.5 and Rs 84.4 per litre, respectively.

Note: OMCs take appropriate decision on pricing of petrol and diesel in line with their international product prices, exchange rate, tax structure, inland freight and other cost elements. Oil firms consider the trade parity pricing which is based on the prevailing prices in the international markets. Retail prices of petrol and diesel in India are linked to their prices in the global markets. Prices of petrol and diesel in India are worked out based on the average of the trailing 15 days of benchmarked Arab-Gulf fuel prices, which move in tandem with global crude oil prices. The pricing formula involves 80% of import price and 20% export price of the fuel. Which means indirectly prices of petrol and diesel are correlated to that of crude oil. So one can say that the increase in crude oil price is leading to an increase in the price of petrol and diesel.

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