
1. Battle to Set Oil Prices

Prelims Syllabus: Economics

Mains Syllabus: GS-II Effect of Policies and Politics of Developed and Developing Countries on India's Interests, Indian Diaspora.

Context:

- The global economy, grappling with the COVID-19 pandemic, is now facing an energy war, with crude oil prices crashing in the international market. Crude oil prices crashed, as the Organisation of the Petroleum Exporting Countries (OPEC) and its alliance partners failed to reach any consensus on cutting back production to levels that would enable prices to Remain Stable.

COVID-19 and its Impact on Oil market:

- There has been a spectacular fall of around 30% in crude oil prices.
- The International Energy Agency (IEA) has scaled down global demand for oil, a move not taken by the energy watchdog since 2009.
- Demand for oil had already weakened owing to the global economic slowdown, and this weakening has become more pronounced due to the COVID-19 pandemic, which has hit China's economy and reduced consumption by the world's largest importer.

US - Russia: Capturing the Market:

- The U.S., as the largest oil producer today, has stayed away from the OPEC-plus arrangement, hoping that production cuts by OPEC-plus countries will help it increase its market share.
- Russia refused any production cuts, unleashing an energy war with Saudi Arabia.
- Russia's decision to reject any production cuts is driven directly by its strategy of denying market share to American shale oil producers.

American Shale:

- The American producers rely on higher prices in the range of \$50-\$60 to remain profitable because of higher production costs.
- At \$31 per barrel, not more than five American shale oil producers can remain profitable at current prices.
- President Donald Trump has scrambled to put together a rescue package for the shale oil companies.

Sanctions on Rosneft:

- Russia also remains resentful of sanctions imposed on Rosneft, which is building the gas pipeline project Nord Stream 2 across the Baltic Sea, carrying Siberian gas to Germany, a major consumer.
- This pipeline was delayed due to opposition from Denmark's environmental activists and could not be completed before the U.S. sanctions kicked in.
- Moscow has accused Washington of using geopolitical tools for Commercial Reasons.

Saudi Arabia and Russia:

- Both Saudi Arabia and Russia depend heavily on oil revenues — upwards of 80% of export revenues accrue from crude oil.
- Both are also fighting to retain market share.
- It has been reported that Saudi Arabia has agreed to supply crude oil at lower rates to refiners in India and China, two primary customers, but refused to supply to other refiners in Asia.
- This will impact on India's oil procurement from the U.S.
- Can Russia and Saudi Arabia sustain the energy war for long? -
- Saudi Arabia's production cost is the cheapest in the world and it can ramp up production to around 12 million barrels a day.
- By offering discounts, it can undercut other producers, including Russia. Domestic considerations also matter.

Benefit to Importing Countries:

- Lower crude oil prices are not necessarily bad news for oil importing countries like India, which is the world's third-largest importer of crude oil and the fourth largest importer of LNG.
- Impact on the global economy: The global economy, already impacted by President Donald Trump's trade war with China and other countries, including India, and the COVID-19 pandemic, may find lower energy costs helpful in overall growth.

Benefits for India:

- From a high of \$147 per barrel in 2008, crude oil prices have fallen to around \$24 per barrel and may even go further southwards.
- India, with 80% of its energy requirements met by imports from the international market, stands to save ₹10,700 crores for every \$1 drop in prices.

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- While this may help manage the current account deficit, fiscal deficit and inflation.
 - If the cost of fuel at the pump is passed on to consumers, it will have a multiplier effect.
 - Lower cost will reduce transportation costs and boost demand.
 - The consumer, however, may not benefit much since the government may choose to use this financial windfall for other purposes, like bailing out banks which have been hollowed out by NPAs to leading Indian companies.

