

HOME ([HTTP://WWW.INFRACIRCLE.IN/](http://www.infracircle.in/))

OPINION ([HTTP://WWW.INFRACIRCLE.IN/CATEGORY/OPINION/](http://www.infracircle.in/category/opinion/))

REVERSE SWEEP ([HTTP://WWW.INFRACIRCLE.IN/CATEGORY/OPINION/REVERSE-SWEEP/](http://www.infracircle.in/category/opinion/reverse-sweep/))

February 2, 2017 | Saurabh Chandra (<http://www.infracircle.in/author/saurabhchandra/>)

| infra@vccircle.com (<mailto:infra@vccircle.com>)

Don't repeat Air India episode in merging oil companies



The setting up of two new caverns for storage of crude oil at Chandikhole in Odisha and Bikaner in Rajasthan is a step in the right direction. Photo by Reuters.

The highlight of the finance minister's Budget speech with regard to the energy sector was the proposal "to create an integrated public sector oil major that will be able to match the performance of international and domestic private sector oil and gas companies."

The rationale for integration across the value chain of the oil and gas industry was: "It will give them capacity to bear higher risks, avail economies of scale, take higher investment decisions and create more value for the stakeholders."



This proposal is sought to be implemented through consolidation, mergers and acquisitions. A proposal that needs to be handled with great care if it is to be taken to its logical conclusion. Lest the spectre of the botched up merger of Air India and Indian Airlines raises its head again. Not the least are personnel issues emanating from differences in hierarchical structures and work cultures. These if left unresolved continue to fester and have the potential to negate the gains of merger.

Its success would however be judged primarily by the distance travelled towards achievement of the target set by the Prime Minister – a 10% reduction in the country's oil and gas import dependency by 2022.

Exploration, Development and Production (EDP) of oil and gas is the key. This needs state of the art technology for EDP in difficult areas and management of producing reservoirs. Such technology is largely available with the private international oil companies. The 'oil major' would be able to meet the country's expectations only if it is able to develop and acquire cutting edge technology to become a technology company, a necessary condition for reversing the trend of falling crude oil and gas production. BP, Chevron and ExxonMobil are large and successful because of their technological prowess.

Similarly, for the downstream industry, the gap in Gross Refining Margin (GRM) amongst public sector companies on one hand and the international and domestic private refiners on the other would require not only technological upgradation but also adoption of the best management practices. Only a higher score on these parameters can justify scale upgradation.

The setting up of two new caverns for storage of crude oil at Chandikhole in Odisha and Bikaner in Rajasthan is a step in the right direction. It is necessary for the energy security of the country. This would however require the government to fund the purchase of crude oil to fill these caverns. A commitment for adequate budgetary provision for this purpose at the opportune time needs to be given.

Upstream producers were hopeful of a reduction in the ad valorem cess of 20%. A retention at this level would disappoint them since rising crude oil prices had taken the payable amount above Rs.4500 metric tonne (MT), which was being levied earlier. However, a reduction in basic customs duty on liquefied natural gas (LNG) from 5% to 2.5% would be helpful in lowering the carbon footprint.

The progress towards development of vibrant solar energy sector continues. The announcement of the second phase of solar park development for setting up an additional 20,000 megawatt (MW) capacity is another step in this direction. The viability and sustainability of the Solar Mission is also dependent on the health of the discoms and their ability to purchase solar power.

Thermal generation remained the mainstay of the power sector. While thermal power grew by 6.9% during April-September, 2016, the generation from hydel and nuclear plants was marginally lower during this period. However the distress in the electricity sector continues. The Economic Survey 2016-17 draws attention to this. According to it plant load factor (PLF) declined to 59.6% during April- December, 2017 from 62% during the same period last year.

Meanwhile, merchant tariffs for electricity sold in the spot market were about Rs.2.5/kilowatt hour (kwh) far below the breakeven rate of Rs.4/kwh. Meanwhile, captive power generation on expensive and polluting liquid fuel continues. The root cause of low PLF co-existing with power shortages leading to reliance on high cost captive power generation while lower priced spot market power has no takers, is the financial condition of the electricity distribution companies (discoms) in several states. This is basically a governance problem arising out of a reluctance to raise tariffs and reduce line losses in a euphemism for power theft in these states.

It would have been useful if the Economic Survey had analysed the progress of the Ujwal Discom Assurance Yojana (UDAY) initiated for improving the state of discoms, with a view to improving its implementation in these states through mid-course corrections.

It is also pertinent to mention that one factor responsible for the low GRM of public sector downstream oil companies is their reliance on captive generation of power for refining operations. While 100% village electrification by 1 May, 2018 is a laudable objective, availability of electricity remains a major concern in many states.

As enumerated by the finance minister in his Budget speech, this sector so critical for growth and which exemplifies cooperative federalism, needs a policy and systems based administration and transparency and objectivity in decision making to restore its health.

*Liked the story? **Subscribe** (<http://www.vccircle.com/infracircle/subscribe-to-newsletter>) to our daily and weekly newsletter, *InfraReads*, to keep track of India's infrastructure space.*



(<http://www.infracircle.in/author/saurabhchandra>)

SAURABH CHANDRA
([HTTP://WWW.INFRACIRCLE.IN/AUTHOR/SAURABHCHANDRA](http://www.infracircle.in/author/saurabhchandra))

Saurabh Chandra is the chairman of Multi Commodity Exchange. He is also former petroleum secretary, government of India and secretary in the department of industrial policy and promotion.

RELATED ARTICLES