

## **Cut in Oil Price**

### **Why in News?**

Saudi Arabia has cut the oil prices and declared its intention to increase output well beyond what the oil market can absorb currently.

### **Why did Saudi cut the price?**

- The Organisation of the Petroleum Exporting Countries (OPEC) and Russia (the largest non-OPEC producer) failed to reach an agreement to deepen existing production cuts to cope with the falling demand.
- So, the Saudi Arabia has cut the oil price.
- Already teetering from the impact of the corona virus, global markets received a shake with the fall in price.
- This is so as oil prices crashed overnight consequent to the price fall.

### **What will happen now?**

- The oil market is now set to witness the rare conjunction of a demand and supply shock which is bad news for prices.
- Fears of a fall in demand following the outbreak of COVID-19 had already depressed oil prices.
- The possibility of the market being flooded with excess production from Saudi Arabia and Russia will unfortunately lead to a supply shock.
- There is still a downside to prices from current levels especially if Russia joins the battle with Saudi Arabia and decides to hike its own output.

### **How this news is perceived?**

- A fall in prices is good news for major consumers such as India and China which depend on imports for a major part of their oil needs.
- But, it may be bad news for the big oil companies and the smaller shale oil players who are highly leveraged.
- A collapse of these shale oil producers may set off defaults in the bond markets, setting off its own non-virtuous spiral.
- With stock and bond markets already in turmoil, the price war now set off in oil is only going to make the markets more volatile and murkier.

### **How will India be impacted positively?**

- For India, the sharp dip in oil prices is good news, for now.
- This will reduce the oil import bill at a time when merchandise exports are likely to suffer due to the freeze in the developed economies.
- This will keep the current account deficit balanced.
- The fall in fuel prices will also drag down headline inflation giving the Reserve Bank of India elbow room to cut rates.

### How will India be impacted negatively?

- The Centre's disinvestment programme to sell the Bharat Petroleum Corporation Limited (BPCL) could run into headwinds.
- The company's valuation may drop.
- So, the big oil companies, which are expected to bid for BPCL, may either shy away from it or their bids may be much lower than expected.
- Eventually, the government may increase the excise duties to compensate for the loss from disinvestment proceeds.
- Any such decision is unlikely to go down well with India's consumer middle class.

Source: The Hindu

### Quick Facts

#### Organisation of the Petroleum Exporting Countries (OPEC)

- OPEC is a permanent intergovernmental organization of 13 **oil-exporting developing nations**.
- It was founded in 1960 by five countries namely Islamic Republic of Iran, Iraq, Kuwait, Saudi Arabia and Venezuela.
- In accordance with its Statute, the mission of the OPEC is to coordinate and unify the **petroleum policies** of its Member Countries.
- It should ensure the **stabilization of oil markets** in order to secure an efficient, economic and regular supply of petroleum to consumers.