Fall in International Crude Oil Prices

Why in News

Recent fall in international crude oil prices has reversed a **six-month trend** of **rising auto fuel prices** which saw the prices of petrol and diesel hit all-time highs across the country.

- The price of **Brent crude** has **fallen under USD 63 per barrel from a high of USD 70 per barrel in early March 2021**.
- Two crude oils which are either traded themselves or whose prices are reflected in other types of crude oil include **West Texas Intermediate (WTI) and Brent**.

Key Points

- **Oil Pricing:**
    - Generally, the **Organization of the Petroleum Exporting Countries (OPEC)** used to work as a cartel and fix prices in a favourable band.
        - **OPEC is led by Saudi Arabia**, which is the largest exporter of crude oil in the world (single-handedly exporting 10% of the global demand).
        - **OPEC has a total of 13 Member Countries** viz. Iran, Iraq, Kuwait, United Arab Emirates (UAE), Saudi Arabia, Algeria, Libya, Nigeria, Gabon, Equatorial Guinea, Republic of Congo, Angola, and Venezuela.
    - OPEC **could bring down prices by increasing oil production and raise prices by cutting production**.
    - The **global oil pricing mainly depends upon the partnership between the global oil exporters** instead of a well-functioning competition.
    - Cutting oil production or completely shutting down an oil well is a difficult decision, because restarting it is immensely costly and complicated.
        - Moreover, if a country cuts production, it risks losing market share if other countries do not follow the suit.
    - Recently, OPEC has been working with Russia, as **OPEC+** to fix the global prices and supply.
        - In 2016, OPEC allied with other top non-OPEC oil-exporting nations to form an even more powerful entity named OPEC+ or OPEC Plus.
- **Reason for the Fall:**
    - **Resurgence in Covid Infections:**
        - A recent resurgence in **Covid-19 infections** coupled with a decision by OPEC+ to **increase crude oil production** has contributed to a fall in crude oil prices.
            - OPEC+ has announced a **phased withdrawal of production cuts** which would see total crude oil production by the group of countries rise by 1.1 million barrels per day by July 2021.

- **Recovery in Supply:**
    - The **recovery in supply without a similar recovery in demand** has contributed to the recent correction in crude oil prices and that supply cuts were difficult to maintain for oil-producing countries given the global macroeconomic situation.
        - Recent US data has also indicated that **gasoline inventories are rising faster** than the fall in crude oil inventories raising concerns of waning demand for petroleum products.
        - **US crude oil production capacity has recovered to about 11 million barrels per day** after abnormally cold weather in February 2021 forced US crude oil output down to 9.7 million barrels per day.
- **Impact on India:**
    - **Current Account Deficit:**
        - The **decrease in oil prices will decrease the country's import bill,** and will help in reducing its **current account deficit** (excess of imports of goods and services over exports).
            - According to estimates, a **one-dollar increase in crude oil price increases the oil bill by around USD 1.6 billion per year**.
            - **India imports 80% of its crude oil** requirements.
    - **Inflation:**
        - The **decrease in crude prices could also also further decrease** inflationary pressures that have been building up over the past few months.
        - This will increase the space for the **monetary policy committee** to ease policy rates further.
    - **Fiscal Health:**
        - If oil prices would have continued to increase, **the government would have been forced to cut taxes on petroleum and diesel** which might have caused **loss of revenue** and **deteriorated its fiscal balance**.
        - The revenue lost will erode the government's ability to spend or meet its fiscal commitments in the form of budgetary transfers to states, payment of dues and compensation for revenue shortfalls to state governments under the **Goods and Services Tax (GST)** framework.

Brent and West Texas Intermediate (WTI)

- **Origin:**
    - **Brent crude oil originates from oil fields in the North Sea** between the Shetland Islands and Norway.
    - **WTI is sourced from US oil fields,** primarily in Texas, Louisiana, and North Dakota.
- **Light and Sweet:**
    - Both oils are relatively light, but **Brent has a slightly higher API gravity, making WTI the lighter of the two**.
        - **American Petroleum Institute (API) gravity** is an indicator of the density of crude oil or refined products.
    - **WTI with a lower sulphur content** (0.24%) than Brent (0.37%), is considered **"sweeter"**.
- **Benchmark Prices:**
    - **Brent crude price** is the international benchmark price **used by the OPEC** while **WTI crude price is a benchmark for US oil prices**.

    - Since India imports primarily from OPEC countries, **Brent is the benchmark for oil prices in India**.
- **Cost of Shipping:**
    - **Cost of shipping for Brent crude is typically lower,** since it is produced near the sea and it can be put on ships immediately.
    - **Shipping of WTI is priced higher** since it is produced in landlocked areas like Cushing, Oklahoma where the storage facilities are limited.

Source: IE