Corona and its Impact on Energy Sector

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Government has finally announced a reduction in Oil prices of 15 Rs pe Liter in the wake of huge fall in international oil prices. The action comes almost one week before the standard announcement date and has been necessitated due to the Corona emergency. GoP has been and continues to be in search of way out for reducing or arresting the projected increase in gas and electricity tariff. This scribe has also been arguing the need for cheaper LPG rates at-least for the poor. In this space, we will discuss the prospects and impact of falling oil prices on Pakistan's energy sector-on both producers and consumers.

Oil

1. Oil prices had already come down much before Corona. Initially, there was Oil price war between the two major oil producers- Saudi Arabia and Russia- and then came Corona's impact of lowering demand and consumption. Pakistan's lower economic growth projections at 3% also had demand depressing impact .It is projected that, there would be a demand reduction of at-least 35% over the year.

2. Oil prices are at 29 USD/bbl when these lines are being written. Oil prices were at 60 USD a few months earlier which came down to 40 USD until last month. There are projections of Oil prices coming down as much as 10 USD/bbl. This would be a destructive price having negative impact on the sector and the world economy. Average sustainable production costs and prices are quoted at 40 USD/bbl.

3. Generally, Oil prices have had a salutary effect on Pakistan's economy and welfare conditions. GoP has announced a decrease of Rs 15.00 per Liter. More reduction is projected, if the fall in prices continues. Some people argue that more reduction was possible even at today's prices. However, GoP needs revenue. Its revenue will come down with economic downturn and it has to finance the emergency package, as it has announced a relief package of 1200 Billion Rs. It may be noted that by now India has not made any significant change in oil prices. Throughout this month of March, Indian prices have remained almost constant. In fact, Indian government has announce an increase in Excise tax on Petrol and Diesel by 8 IRs (16 Pk.Rs) per Liter. They will lower prices eventually but Indian government has already announced to shave off IRs 8.00 out of the projected decrease in oil prices. We have mentioned in an earlier piece that Oil prices in Pakistan are lower than in India.

Gas Prices

4. With Oil prices, gas prices have come down as well, although LNG prices are based on last three months oil prices slowing down the reduction rate. Qatar LNG landed price hovered around 10 USD/MMBtu, which is expected to come down to a level of 4 USD, although spot LNG prices have already come down to less than 4 USD. On the other hand, overhead costs of LNG have already increased due to underutilization. Last month only, one LNG ship landed at Pakistan Gas Port Limited

(PGPL) terminal as opposed to a normal of 6 ships. As a consequence, the LNG tariff at that terminal has increased to 2.2895 USD as opposed to the normal terminal tariff of 0.42 USD. Earlier gas shortages were being projected and there was an upbeat demand for new LNG terminals. This has already lost its shine and enthusiasm. It would give more time to GoP to sort out its policy options.

Coal

Coal appears to be the most expensive fuel these days around USD 30/bbl of oil equivalent, a few percentage points higher than Oil, while gas prices are under USD 20 Oil equivalent. There is no price war in Coal markets and there is steady coal demand in Asia coming out of Electric power plants. Please see the enclosed graph.

Electricity

5. Electricity demand may also go down by 25-30 % if the economic down-turn and Corona impact continues. Winter is gone with traditional low demand as low as 50% of the summer demand. Gas prices would reduce the cost of production. It is not yet clear, if coal prices would come down appreciably. Gas based electricity prices may go down by 25%.Due to decrease in demand, fixed charges would increase thus almost nullifying the effect of decrease in fuel prices.

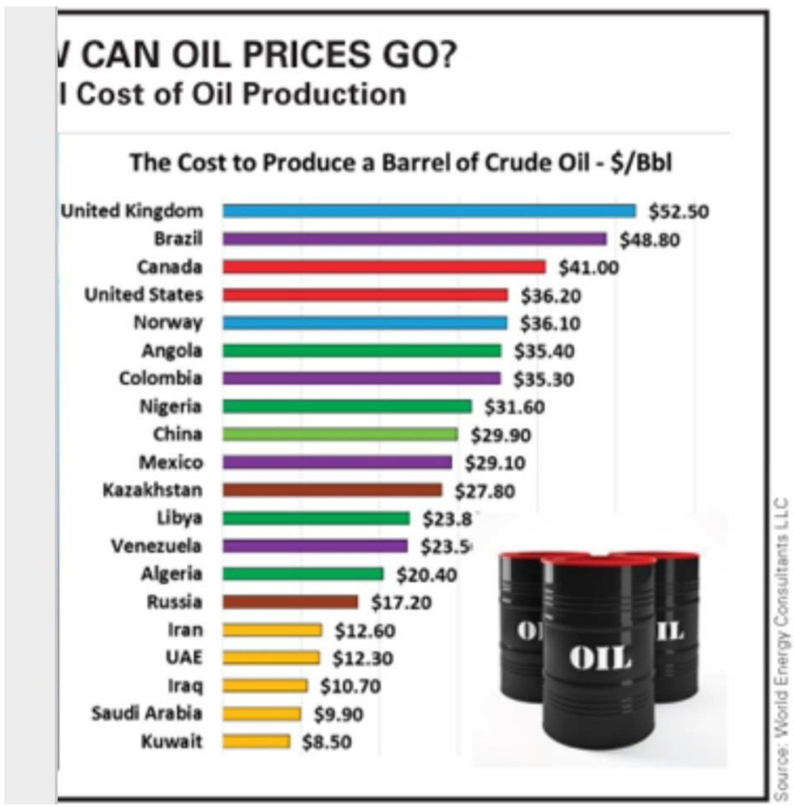
Local Oil Industry

6. There would be problems for local oil industry. Some local refineries have already shut down their units. Furnace Oil may come up again due to its lower price competing with gas. There was no lifting of Furnace oil by the power sector in the recent months. It has already started lifting Furnace Oil. However, the E&P sector would come under pressure as are all oil companies throughout the world. The two major bread earners are OGDC and PPL having significant government ownership. Last year, OGDC made a profit of 118 billion Rs and paid taxes of estimated 40 Billion Rs. at average Oil prices of 60-65 USD/bb/.Similarly, PPL generated net profit of 61.6 billion Rs and paid taxes to the tune of 23 billion Rs. .These two companies and others may go in loss depriving GoP of a total corporate taxation and other revenue of around 250 billion Rs. in addition to employment taxes. GoP may have to make changes to the current crude pricing formula which is based on landed costs of Brent Crude prices. Local production cost is estimated at around 30 USD/bbl. If oil prices go down below this level, GoP may have to introduce floor prices and to balance it, price ceilings may also have to be introduced. Fortunately, the Oil and non-Oil income of the two companies has averaged at 45 % of the total revenue. Gas prices have a floor and ceiling formula reducing the impact of downfall in oil prices.

Decrease in Oil imports and Current Account Deficit

7. There have been imports of around 18-20 million tons per year valued at 12-13 billion USD. Imports may come down by 30 %, although it would be the beginning of last quarter by the coming month. Yearly impact at reduced oil prices at 30 USD /bbl on the average may cause a reduction in oil import bill of 7-8 billion USD i.e. Oil import bill may come down to 4-5 billion USD only, something which has not occurred in the recent history. There may be additional one billion USD of lesser LNG imports.

8. Concluding, overall the impact of low oil prices on Pakistan's economy would be positive, although there may be some risks of reduction in remittance income and loss of revenue and profits in domestic oil industry. It may give some space to the government to arrest inflation and offer welfare oriented consumer tariff for energy items other than oil. While Corona effect may last beyond one year, Oil prices may eventually recover partially after touching a new low which has yet to come***.(The writer is former Member Energy, Planning Commission)***



OGDCL Cost Analysis-rough cut-2018-19		Qty	per year	Rate -USD/unit	Mn.USD
crude oil	bbls/day	40810	14283500	50	714.175
Gas	Mmcfd	1014	354900	2.5	887.25
Lpg	mt/d	802	280700	300	84.21
Sulphur	mt/d	55	19250	100	1.925
Sales Revenue	million rs	261481	261481		1687.56
Profit margin	million Rs.	53			
Production cost	Million Rs.	47	122896		792.877871

Source: OGDC Annual Report 2018-19

Energy Consumption Pakistan 2017-18-MTPA
Oil and Gas Sector

	Production	Imports	Exports	Consumption	M.S.%
Gas	29872574	7492597		37341627	57.17
Crude Oil	4367729	10679770	383317	14764198	22.60
Petroleum Products		13781798	1181047	12157821	18.61
LPG	617577	435665		1054006	1.61
Total	34857880	32389830		65317652	100.00
Market Share-%	53.37	49.59			

Source: HDIP year Book 2017-18