

Gas Needs a New Pricing Meter



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It's been over two years since the Russia-Ukraine war sparked global commodity price shocks, primarily in natural gas. About half of India's LNG consumption is from imports. LNG spot prices rose from below \$10/MMBTU in 2021 to unprecedented levels, averaging \$30-35/MMBTU, fuelling widespread inflation.

Policy interventions employed to reduce the burden on consumers are increasingly causing pricing distortions in the country's gas markets, creating suboptimal outcomes for buyers and producers. Global gas prices have cooled to pre-war levels, and a review of pricing mechanisms is vital.

The profit-sharing New Exploration Licensing Policy (NELP) regime was formulated in 1998, and gas prices were linked to Brent crude benchmarks. This pivotal period saw an upsurge in private investments, most notably in Reliance's KG basin fields, and beginning of LNG imports in the early 2000s to meet skyrocketing demand. This

surge dipped in 2012 when high LNG and Brent-linked domestic gas prices hurt consumption. This led GoI to constitute the C Rangarajan Committee, which moved towards deregulating markets and pricing domestically produced gas at the six-month averages of four hubs: the US, Britain, Canada and Japan, with a six-month lag.

While consumer prices rose from earlier levels, it created predictability for consumers. Domestic producers saw improved realisation aligned with global markets. This equation was disrupted by the Ukraine war and LNG crisis. Demand for relief from high gas prices led to the Kirit Parikh Committee in 2022. It recommended linking prices to Brent, but also capped prices at lower value for gas produced from legacy fields of national oil companies (NOCs), which covers most of their production. These proposals are in place to date.

The assortment of state interventions in price mechanisms also comprises royalties on different types of fields, differing revenue-sharing arrangements across field categories introduced over decades, and price subsidies for specific geogra-

phies. With the Parikh committee's norms, production from private producers and newer fields of NOCs have become uncompetitive in sales, particularly to GAIL, the country's largest buyer and transporter of gas.

Yet, selling gas below the nominated price of \$6.50/MMBTU is not viable for most companies, as royalties are fixed to the nominated price. This leaves private producers attempting to sell to GAIL in a hard spot. These distortions are impacting revenue realisation for producers, which could otherwise be invested in exploration and capex to increase domestic production.

There are calls for revisiting the post-Independence cost-plus basis of gas pricing. But pricing methodology is derived from assessing the producer's costs, which would risk propagating gold plating. This is a morally hazardous practice where producers deliberately inflate costs to increase price realisation, as observed in many African petrostates with similar policies.

What could future policy look like? Pricing policy needs to be simplified and streamlined with global norms. Ensuring linkage to

rolling averages of global benchmarks like Brent or other global benchmarks, along the C Rangarajan committee recommendations, would sustain the balance between consumers and producers.

This should be implemented alongside more uniform gas pricing. One price could be benchmarked for LNG imports, another for domestically produced gas from regular fields, and one higher price for more difficult fields like ultra-deep and high-temperature high-pressure fields.

Such a structure would mitigate price multiplicity across the market and substantially alleviate market alterations. This could be implemented alongside other streamlining measures like pipeline tariff unification, GST inclusion, enhancing trade and sales on Indian Gas Exchange (IGX), and fast-tracking the ongoing development of the National Gas Grid to enlarge and unify the national gas market. The eventual target must be market-driven gas prices in the long run.

Policymakers aspire for gas to fulfil 15% of our energy demand by 2030. The time is ripe for gas pricing reforms to streamline the industry with global norms, safeguard consumer affordability and enhance India's energy security.

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