

IISD-TERI Workshop on Energy Subsidies in India: Summary report

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On August 28th, 2012, IISD-GSI and TERI co-hosted a workshop for media and civil society on “Fuel Subsidies: Getting to Grips with the Pros and Cons of Higher Prices”. The workshop was well attended with over 30 participants, of which half were journalists including from the Business Standard, CNBC – TV18, Business Today, Business World and MINT.

The purpose of the workshop was to brief media and selected civil society organisations on the key findings and policy recommendations of the joint research project, and to facilitate a discussion amongst journalists on key issues relevant to their reporting of fuel subsidy reforms.

The workshop was divided into three sessions:

Session 1: Opening remarks

- This session started with an introduction to the workshop by *Kerryn Lang, GSI Project Manager at IISD*. Kerryn provided the international context for the workshop discussions, noting that globally fossil-fuel subsidies are worth \$500 - \$600 billion per year, predominantly for subsidizing energy consumption in developing countries. Kerryn noted that although the negative impacts of these subsidies are widely understood, many developing countries face similar challenges in overcoming political opposition to reforms and implementing more effective measures to support the poor. Kerryn introduced the project partners and the key research topics.

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- *Leena Srivastava, Executive Director, TERI*, then gave the opening remarks. Leena's comments focused on India's energy challenges, including the myriad of negative impacts of fuel subsidies and the need for reform. Leena emphasised that India's fuel subsidies are causing distortions along the entire value chain and these are not only resulting to significant economic and fiscal impacts, but also leading to investment choices that are preventing the development of renewable energies.
- *Paranjay Guha Thakurta, distinguished journalist and political commentator*, then gave an in-depth overview of the political and practical challenges facing reform of India's fuel subsidies. Paranjay began by emphasising that food and energy security were the two biggest issues facing the country. As India has become dependent on imported crude oil which is subject to high price volatility, it has major implications for India's economy as a whole. And subsidies for fuel exacerbate this problem. Paranjay highlighted the following key issues for each type of subsidized fuel:
 - Kerosene – As long as there is a large price difference between kerosene and diesel, the Government will not be able to stop diversion. There is little information on how much kerosene is actually being diverted (estimates range between 25% - 50%) and who's using it. The black market is so profitable and powerful that the "kerosene mafia" are willing to kill investigators. This is very difficult to address through governance measures. Need to increase prices but find other ways to support the poor.
 - LPG – As LPG is mostly consumed by middle- to higher- income households, they can bear the burden of increased prices. The Government has raised possibility of capping the number of subsidized cylinders allocated per household but it's not clear whether this will be feasible to monitor and enforce.
 - Diesel – the reform of diesel subsidies is more complex because it used as an input to a wide range of economic activities and therefore price increases will have cascading effect throughout the economy. However this needs to be weighed against the impacts that a higher fiscal deficit (as a result of maintaining subsidies) has on inflation.
- *Discussion points included:* It was noted that these issues need to be addressed within the context of i) fragmented policy-making and ii) distortions in pricing systems across sectors. One participant highlighted the fact that fuel subsidies are more costly than food subsidies, which is significant when considering food security issues.

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There was some discussion around the concept of ‘under-recoveries’ and the need to clarify exactly how these contribute to the subsidy estimates. There was also acknowledgement that there appears to be a real lack of political will to reform subsidies at present and this may or may not improve post elections.

Session 2: Presentation of key findings and policy recommendations

- *Mukesh Anand, NIPFP* gave an overview of his research on the impacts of diesel price reforms on key economic sectors. These key sectors include:

Sector	Percentage of total diesel consumed in 2010-11
Transport:	
Road	60.4%
Railways	4.0%
Water	0.9%
Aviation	Negligible
Industry (registered manufacturing)	10.5%
Power Generation	8.2%
Agriculture, Forestry and Fishing	12.2%
Miscellaneous	3.6%

He calculated that to eliminate under-recoveries, diesel prices would need to be increased by approximately 25 percent (although this figure fluctuates). Mukesh’s analysis estimates that raising diesel prices by 25 percent would increase the inputs costs of key sectors as follows:

Large public transport operators	8%
Goods/Freight transporters	10%
Rail transport (freight and passenger)	2.5 – 3.5%
Industry (fuel consumers)	0.25%
Agriculture	
Wheat	2.75%
Sugar cane	0.75%

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In addition, a 25 percent increase in diesel prices would result in a general price rise of 1.2 percent. Mukesh recommended that the Government should gradually increase diesel prices to reduce the price gap and the resulting distortions between gasoline and diesel prices.

- *Anmol Soni, Research Associate, TERI* presented research on how a cash transfer scheme could be designed to support the reform of kerosene and LPG subsidies. Anmol noted the inefficiencies and estimated levels of diversion within the distribution systems for subsidized kerosene and domestic LPG. She then outlined some of the key design elements for a cash transfer scheme, including i) identification and targeting, ii) determining the amount and frequency of cash payments, iii) delivery mechanisms and iv) monitoring and evaluation. Anmol then highlighted the study's recommendations:

Short-term actions:

- Undertake more pilot studies to test the provision of direct cash transfers
- Undertake a value for money and cost benefit analysis of the transfer schemes
- Cap subsidized LPG cylinders per household

Medium- to long- term actions:

- Introduction of country-wide cash transfers, contingent on the finding of pilot studies
 - Cash payments should be indexed to price levels
 - India's financial inclusion needs to be increased
 - LPG prices should be gradually decontrolled
 - Supply chain of PDS kerosene and domestic LPG needs to be improved
 - The BPL surveys needs improvements in its design
- *Ramesh Jalan, UNDP* then provided a few comments noting that India's energy consumption doubles every 20 years. Within this context, subsidy reform is needed to help reduce India's energy consumption and to move towards improved energy technologies such as smart grids.
 - *Discussion points included:* There was some debate over appropriate pricing mechanisms (trade parity vs export parity pricing) and taxation (ad valorem vs specific taxes) for diesel.

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There was some discussion around whether implementing a cap on subsidized LPG cylinders per household would be a relatively quick and simple way to reduce subsidies. Although there is debate as to what number the allocation should be capped at, it was suggested that the Government could start with a high allocation (e.g. 10 cylinders per year) and gradually reduce this over time. An issue was also raised over whether cash transfers should be given to men or women in the household, noting that it is less likely to be misused if granted to women. Food stamps were raised as another alternative to cash transfers. One participant also noted that there will be inefficiencies in any system but that the “perfect should not be the enemy of the good” – i.e. even though cash transfers may also have some leakage, it could be a significant improvement on the current public distribution system for kerosene and food.

Session 3: The hidden costs of subsidies

- *Anumita Roychowdhury, Centre for Science and Environment* presented a wide range of impacts of diesel subsidies for the automobile sector. Anumita demonstrated how diesel subsidies are distorting the automobile market with the sale of diesel cars (small and large) reaching an all-time high, while demand is still growing and will overtake the sale of petrol-based cars.

She explained the impacts of this ‘dieselization,’ notably that it is undermining India’s energy security, increasing local pollution causing major public health issues, and exacerbating greenhouse gas emissions. Anumita recommended eliminating fuel subsidies as a key step to reducing diesel consumption and moving towards advanced ‘clean’ diesel technologies.

- *Discussion points:* There were many questions on the technical information presented. Anumita discussed the complexities of the issue, in particular how interest groups can use technical language, facts and figures that the general public do not understand to defend their industries and the subsidies that support them. She noted that it can be very difficult for journalists and others to fully understand the complexities of the issues and search out balanced views. There is a need for more robust and easy-to-digest information on the environmental impacts of economic policy. Researchers, journalists and civil society need to collaborate to build public and policy understanding on these issues.

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- *Kerryn Lang, IISD* closed the discussion noting some of the key issues that had been highlighted throughout the day. Despite how much the issue of fuel subsidies is discussed in the media there is still a significant lack of information on critical issues like i) the rate of diversion of subsidized kerosene (anywhere between 20-50%), ii) comparison of inflationary impacts as a result of maintaining subsidies/increasing the fiscal deficit vs removing subsidies either in one price hike or gradually. However there are a range of short-term measures that the Government can take including i) increasing diesel prices by small amounts, regularly, ii) capping the allocation of subsidized LPG cylinders per household and iii) expanding the number of pilot studies for replacing PDS kerosene with direct cash transfer, such as that in Alwar. But in the long-term, market-based pricing should be the ultimate goal with complete removal of government interference in the pricing mechanism. There is some question over whether there is sufficient political will to reform subsidies, with inconsistent messages from government reported in the media almost daily. If no reforms are implemented soon, the period immediately after the 2014 elections could be a good time to implement reforms when the government is at its most popular. In the meantime, researchers, journalists and civil society can support the process by filling information gaps, raising public awareness and building policy understanding of these complex issues.

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