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India Raises Petrol and Diesel Prices by Rs 3 -- OMC Under-Recovery and West Asia Crisis

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ECONOMY

GEOGRAPHY

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WHY IN NEWS:

State-owned oil marketing companies (OMCs) – Indian Oil Corporation (IOCL), Bharat Petroleum Corporation Limited (BPCL), and Hindustan Petroleum Corporation Limited (HPCL) – raised petrol and diesel prices by **Rs 3 per litre** each effective May 15, 2026. This is the **first upward fuel price revision in over four years**, triggered by global crude oil prices crossing **\$110 per barrel** amid the West Asia conflict and Strait of Hormuz disruption fears.

BACKGROUND – INDIA'S FUEL PRICING ARCHITECTURE

India moved from **administered pricing** to a **market-linked dynamic pricing mechanism** in 2010 (petrol) and 2014 (diesel). Under this system, OMCs are expected to revise retail prices **daily** in line with the 15-day rolling average of international crude prices and the rupee-dollar exchange rate.

How Prices Are Set

COMPONENT	DETAIL
Base price	15-day average of relevant crude benchmark (Dubai/Oman blend for India)
Freight + OMC margin	Adds logistics, refinery margin
Central excise duty	Rs 19.90/litre (petrol); Rs 15.80/litre (diesel) – basic excise duty sub-component; total central levy is higher including AIDC and road cess
State VAT	Varies: 20-35% (petrol); 12-24% (diesel)
Dealer commission	~Rs 3.87/litre (petrol)

The Under-Recovery Problem

Despite dynamic pricing, OMCs **do not always pass on cost increases** – especially near elections or during political sensitivity windows. When they absorb the difference between their cost and the retail price, this is called an **under-recovery** (not a subsidy in the strict sense, since the government does not reimburse OMCs).

PERIOD	NATURE
April 2022	Last major hike (Rs 8/litre over two tranches)
May 2022 – May 2026	Prices frozen despite crude swings
2022-2024	OMCs benefited from crude crash below \$80; recovered earlier losses
2025-2026	West Asia escalation pushed crude above \$100; OMCs back in loss

By May 2026, OMCs were collectively losing approximately **Rs 1,000 crore per day** at pre-hike retail prices.

THE WEST ASIA CRISIS – SUPPLY-SIDE SHOCK

Strait of Hormuz Risk

The **Strait of Hormuz** is the world’s most strategically important maritime oil chokepoint:

- Located between **Iran** and **the Oman peninsula**
- Width at narrowest: **~34 km** (21 nautical miles)
- **~21% of global petroleum liquids** transited through it in 2023 (IEA estimate)
- India imports approximately **88-89% of its crude oil** requirements; roughly **60-65% of India’s crude imports** transit through the Strait of Hormuz

KEY CRUDE SUPPLIERS TRANSITING HORMUZ	INDIA’S IMPORT SHARE (APPROX.)
Saudi Arabia	~16% of India’s crude basket
UAE	~7%
Iraq	~22% (largest single supplier)
Kuwait	~5%

If Iran were to close or disrupt the Strait, India’s **crude supply chain** would be severely affected.

Global Crude Price Impact

DATE/EVENT	BRENT CRUDE APPROX.
Jan 2026	~\$72/barrel
West Asia escalation (April 2026)	~\$89/barrel
Strait of Hormuz disruption signal (May 2026)	~\$113/barrel peak

INDIA'S ENERGY SECURITY – KEY INSTITUTIONS

Strategic Petroleum Reserves (SPR)

India maintains **underground strategic petroleum reserves** at three locations, operated by **ISPRL (Indian Strategic Petroleum Reserves Limited)** – a special purpose vehicle under the Ministry of Petroleum and Natural Gas:

LOCATION	CAPACITY	STATUS
Visakhapatnam, Andhra Pradesh	1.33 MMT	Operational
Mangaluru, Karnataka	1.5 MMT	Operational
Padur, Karnataka	2.5 MMT	Operational
Total Phase I	5.33 MMT	Operational
Chandikhol, Odisha (Phase II)	6.5 MMT (planned)	Under development
Padur expansion (Phase II)	2.5 MMT (planned)	Under development

At India's current consumption (~5 MMT/month), **Phase I reserves provide roughly 9-10 days of oil security.**

India became an **IEA Associate Member in 2017** (not a full member – full membership requires OECD status). IEA members are expected to maintain **90 days of emergency oil stocks**; India falls short of this benchmark.

FISCAL AND MACROECONOMIC IMPLICATIONS

The Dual Bind

PRESSURE	EFFECT
Hike prices	Direct inflationary impact (transport costs, logistics, food prices in 2-3 weeks)
Freeze prices	OMC losses mount; crowding out of public investment; potential government bailout needed

WPI and CPI Linkage

- **WPI for Fuel and Power** had already spiked to **+24.71%** in April 2026 (wholesale prices)
- Every **Rs 1/litre hike in diesel** adds approximately **0.1-0.2%** to the CPI (food, transport cost transmission)
- The Rs 3 hike is expected to add **~0.3-0.5% to CPI** over the next 2-3 months

Government's Fiscal Tool – Central Excise Duty

The Centre has a lever: **cut central excise duty** on fuels to absorb the crude shock. In November 2021 and May 2022, the Centre cut excise duty by Rs 5-8/litre. However:

- These cuts cost the Centre approximately **Rs 1 lakh crore per year** in foregone revenue
- Current fiscal deficit target: **4.5% of GDP (2025-26)** – limited headroom
- The RBI has been cutting rates (easing cycle since February 2025); a sharp CPI uptick could force the MPC to **pause or reverse rate cuts**

UPSC RELEVANCE

GS Paper 3 – Economy and Environment

Key arguments:

- India's reliance on administered/semi-administered fuel pricing creates a **political economy problem** – OMCs lose money before elections, then hike prices after. This distorts market signals and creates fiscal cliff risks.
- The **energy security vulnerability** exposed by Strait of Hormuz risk is structural: India must accelerate SPR Phase II, renewable energy transition, and crude import diversification
- The **WPI-CPI transmission lag** (2-3 months) means the May 2026 hike will show up in CPI data only by July-August 2026 – just as the RBI reviews its easing cycle

GS Paper 3 – Geography

- Strait of Hormuz: geography, chokepoint significance, Iran's leverage
- India's crude import basket and geopolitical exposure

Keywords: OMC under-recovery, dynamic fuel pricing, Strait of Hormuz, ISPRL, Strategic Petroleum Reserve, WPI fuel and power, CPI transmission, LPG price, central excise duty on fuel, IEA Associate Member.

Indian Oil Corporation (IOCL – largest, under Ministry of Petroleum), BPCL, HPCL; together control ~90% of India's fuel retail network.

Between Iran and Oman; ~34 km wide at narrowest (21 nautical miles); ~21% of global petroleum liquids transit; only alternative is the 1,200-km Abqaiq-Yanbu pipeline (Saudi Arabia) and UAE's Abu Dhabi Crude Oil Pipeline (1.8 million bpd capacity).

Indian Strategic Petroleum Reserves Limited; SPV under MoPNG; Phase I (5.33 MMT) operational at Visakhapatnam, Mangaluru, Padur; Phase II (Chandikhol + Padur expansion) under development.

Under-recovery = gap between cost price and retail price absorbed by OMC (no government reimbursement). Subsidy = direct government payment to compensate the gap (as was done for LPG/kerosene pre-2014 reforms).

Paris-based; founded 1974 post-oil crisis; full membership requires OECD status; India is Associate Member since 2017; IEA members expected to hold 90-day emergency stocks.

Central excise + State VAT; Centre collects excise (Union List); states collect VAT (no GST on petrol/diesel despite GST Council discussions).

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