5 November 2007

KUALA LUMPUR, Nov 5 (Bernama) -- The government has reiterated several times that there would be no increase in the price of oil or gas products for the year 2007.

But the reprieve is expected not to last long as we enter the new year and as global fuel prices continued to surge.

Oil prices added nearly US$12 a barrel since the start of October and reached US$93.80 (about RM313) a barrel last Monday (Oct 30) and US$96.24 (about RM321) on Nov 1. Some reports have also mentioned that oil prices could break the US$100 mark if risk factors influencing the sharp rise are to continue.

International Trade and Industry Minister Datuk Seri Rafidah Aziz was quoted as saying on Nov 1 that "it is not viable to continue to maintain a petrol subsidy at the current level and that the government is studying how much of the oil price increase should be passed on to industries, the commercial sector and the public."

FACTORS CAUSING PRICE SURGE

According to Anthony Dass, Head of Research, Inter-Pacific Research, the current increase in oil price is mainly due to the mismatch between demand and supply.

He added that demand for oil has been strong in view of the sustainable global growth.

"I am looking at 4.9 percent growth for 2007 and 2008, underpinned by a more broad-based growth. As a result of the strong global growth, inventory level has been extremely thin.

"Hence, any adverse shock news, be it due to fundamental or geopolitical issues is causing knee-jerk response to oil prices," Dass told Bernama.

The latest alarming geopolitical tension in the Middle East is between Turkey and Kurdish rebels in northern Iraq. Analysts had attributed heightened tensions between the two as one factor behind the continued surge in global oil prices besides the cold winter weather and rising production costs.

Qatari Oil Minister Abdullah al-Attiyah was quoted by a foreign news agency recently as saying that the US$90-plus oil price was a result of "politics and speculation and not due to a supply shortfall".

He also told reporters at an international energy conference in London that "the market is out of control".

HEAVILY SUBSIDISED

On the home turf, it is generally known that the fuel products sold in the country is heavily subsidised by the government. The fact is, the government is actually overly-burden by these subsidies.

Subsidy in this context is the money paid by the government to a producer or a seller of a product so that the retail price of the product is kept low as compared to its actual cost or market price. This move is actually to lessen the burden shouldered by consumers.

The amount of subsidies that need to be forked out by government depends on consumption of fuel products. For example if more petrol is used, the higher would be the subsidies borne by government.

Ministry of Finance Parliamentary Secretary, Datuk Seri Dr Hilmi Yahya was recently quoted as saying that the government had to bear subsidies to the tune of RM16 billion for the first eight months of this year due to the rising global price of crude oil.

He however stated that the oil price increase is still manageable even though the price hike has pushed inflation rate this year from five percent last year to seven percent.

When the government increased the retail prices of petrol, diesel and Liquefied Petroleum Gas (LPG) by 30 sen on Feb 28, 2006, the move had allowed the government to save about RM4.4 billion annually.

Prime Minister Datuk Seri Abdullah Ahmad Badawi told a media conference a day after the increase was announced that government would utilise the money saved for development projects including to improve the nation's public transportation services.

PRICE DISTORTION

Market analyst Dass argued that as long as government maintained subsidies for fuel products, there would be a strong price distortion that could pave the way for economic inefficiency.

He said Petronas should have been given the room to remove the subsidy in the years when Malaysians were enjoying strong growth and strong purchasing power.

"I guess if we had done it at that time, it would not have caused serious concern as what we are looking at today," he said, adding that a slowdown in the country's economic growth is likely to occur should the government continue to subsidise the oil price.

His reasoning was that there would be less funds allocated for development purposes due to what he called as 'opportunity cost' between subsidy and economic growth.

SUBSIDY IS BAD

Prof Dr Tan Eu Chye of Economics and Administration Faculty, University of Malaya shared Dass's concern over the subsidy issue.

"Subsidy could remain so long as it is sustainable. Too much subsidy is bad as it means the price would not reflect the actual economic cost and this would lead to wasteful over-consumption and causing undue pollution of the environment," he told Bernama.

Prof Tan went further to say that the spiraling oil price coupled with the US subprime (housing loans) crisis heightened the risk of a global economic stagflation (stagnation and inflation).

"Given that Malaysia is an oil exporter and that the government is in a fiscal position to offset to some extent the external shocks, the impact on the Malaysian economy could be contained.

"Nevertheless, the rakyat should always brace themselves for any eventuality. If there is any increase in the price of petrol and gas, they should not react but appreciate it as a universal problem instead. It is healthy to tighten belts when the need arises and let market force takes its course," he further explained.

STILL LOW

The 30 sen sharp increase in 2006 for the retail price of petrol, diesel and LPG has put the retail price of the RON97 premium petrol in Peninsular Malaysia to be sold at RM1.92 per litre, petrol RON92 at RM1.88 per litre, diesel at RM1.581 a litre and LPG at RM1.75 per kg.

Without the government's subsidy and tax exemption, retail price of RON97 in Peninsular Malaysia should be at RM2.46 per litre, RON92 at RM2.37 per litre, diesel RM1.98 per litre and LPG at RM3.21 per kg.

Still the price for the RON97 petrol for example is very much lower compared to that in neighbouring countries like Thailand (RM2.52), Philippines (RM2.21), Singapore (RM4.15) and Indonesia (RM2.30).

With the current surge of the crude oil global price, it looks like the government is left with not much choice but to make the dreaded move. In a nutshell, costlier fuel products would seem to be the most logical thing to be adopted by the government.

IMMINENT HIKE

In short, Malaysian consumers in general has to brace for another hike whether they like it or not and they may well be greeted some time in the new year of 2008.

Dass anticipated the price of petrol could jump between 15 sen to 30 sen per litre, depending on the global crude oil price.

As for gas (referring to gas supplied by Petronas to Tenaga Nasional Berhad), he projected the new price level to be around RM10 to RM15 for each million British Thermal Unit (mmbtu) supplied by Petronas to Tenaga Nasional as compared to the current rate of RM6.40.

"Tenaga Nasional's contract with Petronas expired in 2005 but Petronas is still supplying gas to Tenaga Nasional at the old subsidised rate.

"Tenaga Nasional may have to buy the gas at a new rate and when that happens, Tenaga Nasional would be under pressure to transfer the cost to consumers, meaning electricity tariff may have to be increased," said Dass.

By Melati Mohd Ariff

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