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# Reforming ONGC Videsh for India's energy security

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## EXECUTIVE SUMMARY

ONGC Videsh Limited (OVL) is the overseas arm of ONGC, India's primary nationalised oil company. OVL can and must play a critical role in ensuring India's energy security, which must involve actually securing increased oil and natural gas supplies for the country. Energy security is a bottleneck for India to get back to high economic growth, and OVL needs comprehensive reforms in order to truly contribute to this goal.

In a global oil market that is increasingly captured by nationalised oil companies (NOCs), the role of OVL only increases in prominence. Consequently, OVL must move beyond focusing on acquisition of acreage and drilling rights alone, to examining the entire supply chain of getting oil and natural gas to India. This requires a more strategic approach to acquisitions, which are currently driven by the imperative to rapidly reinvest profits and cash surpluses, so as to prevent their being appropriated by the government to subsidise loss-making domestic public sector undertakings (PSUs).

This policy brief proposes six strategies for OVL to secure deposits, extraction, supply routes and technology. OVL can build technological competencies by entering into joint ventures with market leaders and use it to unlock greater reserves at home. OVL can also enter swap deals and reciprocal arrangements to bring major oil companies (both nationalised and international) to India. To secure more reliable and inexpensive supplies and reliable supply routes, OVL should concentrate on countries where it enjoys unique leverage or soft power advantages. OVL can collaborate with other NOC competitors and avoid being lured into bidding wars with them. It should also cultivate alliances and bidding consortia with private sector players, both domestically and internationally. Finally, OVL should ensure that political risk is comprehensively accounted for, and develop contingency plans for disruptions in supply or supply routes.

This brief also raises certain aspects of domestic policy as necessary counterparts to these reforms. Investment, taxation and pricing of oil and natural gas in particular must be consistent and transparent to help to restore investor confidence in India, and critical sea lines of communication (SLOCs) must be secured.

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# 1. INTRODUCTION

## 1.1 Energy is key to economic growth

India's national interest, and even national security, is premised on achieving high economic growth. The challenges posed by stubbornly high inflation, poor industrial growth, and a sluggish and debt-ridden global economy can be met only by a resurgent and economically strong India.

Energy is a key component of such economic growth. India's "Energy Elasticity of GDP" ratio stands at 0.8[1]; a 10 percent growth in GDP would require 8 percent growth in energy supply. This ratio is adversely affected by increased expenditure on imports of fossil fuels, especially if their prices rise as well. Some writers have proposed, in response, that India achieve "Energy Independence" (self-sufficiency in energy supply). Such proposals, while correctly emphasising the role of oil and natural gas imports in energy security, remain more visionary than practical.

India does not enjoy such geological largesse as Brazil or Russia. Technological innovations in renewable energy, nuclear power, and indigenous extraction capacity have not yet reached a stage of viability at scale. Critical sectors – transport, aviation, fertilisers, power generation – continue to depend on supplies of oil and natural gas. India will thus rely on petroleum imports for the foreseeable future.

A more pragmatic definition comes from the erstwhile Planning Commission's Power & Energy division[1]:

> "Energy security is defined in terms of reasonable assurance of access to energy and relevant technologies at all times with an ability to cope with sudden shocks…it only means an ability to meet reasonable requirements with reasonable assurance of stable supply or an ability to pay for import needs."

This definition provides multiple standards – meeting import costs, access to energy supply, access to relevant technology, ensuring stability of supply, and insuring against supply shocks. Profitability (to offset import costs) is thus only the minimal threshold for claiming that an investment promotes energy security; OVL currently contributes only in this minimal sense. With adequate foresight and planning, however, OVL can operate so as to secure supplies, technology, supply routes and insure against shocks as well.

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[1] "Power and Energy", Planning Commission of India, 2014. goo.gl/XGhfme

### 1.2 A Framework for thinking about strategic options

Strategic measures offer benefits beyond mere financial returns, or at least offer financial benefits disproportionate to their costs, potentially by leveraging other forms of influence to expand such returns. In the context of energy security, investments may meet strategic goals in one (or more) of four ways:

- **Securing deposits:** to secure a reserve of petroleum resources that was hitherto unavailable or inaccessible, so as to directly increase fuel available to or in India, which reduces dependence on imports correspondingly.
- **Securing extractors:** to secure a fuel supplier, so as to assure India of a reliable supply of fuel in times of shock, or at rates more advantageous than market price (through a long-term supply contract, or any other arrangement).
- **Securing supply routes:** to secure the pipelines or sea routes along which India must transport such fuel, whether OVL-produced, discounted or purchased at market price. Overlaps directly with territorial and maritime security concerns.
- **Technology:** to access, acquire or develop the technology necessary to access deposits that are otherwise unreachable due to geological or ecological constraints. This includes not only physical equipment and intellectual property, but also training and expertise in the use of such equipment or techniques.

This policy brief suggests six reform measures for OVL's operations. Each of the measures proposed potentially secures at least two of the above strategic objectives. These reforms are not uniformly applicable in all contexts; each has its advantages and challenges, but they can be layered in a mutually complementary fashion, and supported by India's diplomatic or soft power leverage as needed. It is most useful to think of them as tactics, which form a part not only of energy security policy, but of India's broader diplomatic and economic outreach strategy.

## 2. PROPOSED REFORMS

### 2.1 Build Technological Competencies:

*OVL should enter into joint ventures to gain access to and experience in operating advanced technologies & methods. This can also help domestic exploration efforts by ONGC.*

*Secures:* Deposits, Technology
*Goal:* Improve recovery from domestic reserves

In India and globally, reservoirs are ageing. New reserves are harder to find, or "tight" – geologically and technically difficult to access. Technological solutions to the problems of declining yields and tight reserves represent the future of extraction. With shale touted as a game changer[2] and a bridge fuel[3] in India, it would be worth seeking out technological competencies to access shale reserves or other forms of hard-to-access oil and gas.

Key players in this field include Brazil's PetroBras, which has invested significantly in in-house Research and Development (R&D) [4] efforts, specialising in ultra-deepwater[5] operations. China has built up substantial expertise in improved/enhanced oil recovery (IOR/EOR) by entering Joint Ventures (JVs) with market leaders in the field[6]. ONGC has also invested in R&D efforts, associating with centres at various universities; EOR and reservoir management skills have developed indigenously. This is an advantageous position from which to suggest an exchange of skills, trainers or technical expertise, especially where it relates to extraction of shale oil or gas.

The key challenge here is that these technologies are typically proprietary, and – especially where an IOC is the patent-holder – purchasing ownership of such technology is likely to be prohibitively expensive. Still, the competency to operate them is critical as well. It is only a matter of time before other players also reverse-engineer or innovate similar solutions. Where such technologies have been valued, OVL can also offer to invest a greater share of financial capital in exchange for gaining preferential access to them.

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[2] Rakteem Katakey, "First India Shale Gas Seen in 4 Years, China Output Nears", *Bloomberg*, May 17, 2012. goo.gl/XnS5pm

[3] Elliot Brennan and Silvia Pastorelli, "India's Shale Gas Boom: Dream or Reality?" The *Diplomat*, June 18, 2013. goo.gl/8NLxqh

[4] Matt Moffett, "How a Sleepy Oil Giant Became a World Player", Wall Street Journal, Aug 30, 2007. goo.gl/8wQklv

[5] Joel Parshall, "Petrobras: A Legacy of Growth, Continuing & Accelerating", *Journal of Petroleum Technology (Company Profile Series)*, (August 2010): 26-29.

[6] Daojiong Zha, "China's Perspective: The Quest for Energy Security", in *Crux of Asia: China, India & the Emerging Global Order*, ed. Ashley J. Tellis and Sean Mirski, (Washington DC: Carnegie Endowment for International Peace, 2013)

### 2.2 Enter into Swap Deals and Reciprocal Arrangements:

*OVL should pursue swap deals and farm-in/farm-out agreements, where the reciprocal condition for OVL investment is for the JV partner to invest in India.*

*Secures:* Deposits, Technology
*Goal:* Complement Indian efforts to explore and develop domestic reserves.

Recent rounds of the National Exploration and Licensing Policy (NELP) auctions, where firms bid for permits to explore and develop various acreages in India, have seen very limited international participation. Swap deals would be one avenue to stimulate international investment in Indian oilfields. OVL's side of the swap – the acreage it invests in internationally – could also be used to increase the portfolio of profitable prospects available to the potential oil investor, for instance by applying locational advantage for mutual benefit. (OVL could sell the oil it produces further afield, in exchange for closer suppliers providing equivalent quantities of oil to India.)

There are a number of major IOCs that India would like to attract to domestic oilfields. The Chinese variant of the swap deal is instructive: NOCs will invest in important IOC-run projects overseas, and those IOCs will enter JVs to develop acreage in that nation. There is also the option of farm-in/farm-out agreements[7], where OVL picks up stakes in NOCs' existing projects in exchange for that NOC picking up an equivalent stake in ONGC projects. Ideally, these JVs start with the foreign partner as the operator, but transition to being locally run. This can be used to attract technical expertise needed in particular areas, without requiring Indian firms to acquire the technology outright. (For example, farming out an operating interest in ultra-deepwater exploration blocks to PetroBras.[8])

There are a number of challenges: locational swaps are difficult, because the territorial state has first buyer's right, and India's supplier states rarely need to buy oil; they may still work where such a supplier has obligations towards a state where OVL operates, which OVL could fulfil at reduced transport cost/time. As far as using swaps to bring IOCs to India is concerned, the domestic investment environment (e.g. clarity on capital gains tax) is a major factor; pending reform, some manner of special dispensation could be made for companies investing in Indian oilfields through this channel.

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[7] "ONGC and Petrobras announce swap agreements and entry of Petrobras in India", OVL Press Release, 4 Jun 2007. goo.gl/Zrk68B

[8] Rajeev Jayaswal, "Petrobras eyes stake in OVL's Brazilian assets", *Economic Times*, 29 Aug 2008. goo.gl/nTlVUP

### 2.3 Invest in markets where India has comparative advantage:

*OVL should target markets that competing NOCs find inhospitable for political reasons, or where India enjoys greater diplomatic influence or soft power.*

*Secures:* Extractors, Supply routes
*Goal:* Cultivate preferential-rate suppliers, by leveraging India-specific advantages.

NOCs often face criticism from IOCs for bringing political leverage to bear[9]. While all NOCs do enjoy advantages that IOCs do not[10], OVL is yet to win a bid where it was not the highest bidder. Where, for instance, OVL and Chinese NOCs have submitted competing bids, Chinese offers of developmental assistance (unrelated, of course) have tended to tip the scales. The lesson from these experiences is that OVL should play to Indian strengths, or at least capitalise on competitors' weaknesses.

The most plausible approach would be to approach nations historically unfriendly to competitors, but amenable to Indian participation. Chinese NOCs are OVL's most common competitors; identifying countries where political factors preclude Chinese participation and focusing on such countries for investment is an option worth exploring. ONGC believes Bangladesh may be one, but that is something of a special circumstance[11]. The littoral states of the South China Sea provide an ideal opportunity, but there is also substantial political risk involved, as OVL found out when it sought to lease acreage from Vietnam[12]. OVL could also exploit India's links with Taiwan, investing in those African states which still maintain relations with Taiwan instead of China.

Caution is needed[13] as OVL has fared poorly – picking up projects CNPC and RosNeft deemed too marginal, and may do better in states too stable for those firms instead[14]. This approach also explicitly requires close coordination between OVL, its parent Ministry, the Ministry of External Affairs[15], and potentially with Indian or Indian-origin private players who are established in those markets and can serve as intermediaries there.

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[9] Nina Poussenkova, "Lord of the Rigs: Rosneft as a Mirror of Russia's Evolution", The James A. Baker III Institute for Public Policy of Rice University (2007).

[10] Martin Chulov, "BP consortium wins historic deal for Iraqi oil", *The Guardian*, 30 Jun 2009 goo.gl/DWUPSM

[11] Shine Jacob, "'Diplomacy' draws OVL to Bangladesh", *Business Standard*, 20 April 2013. goo.gl/O5QM4i

[12] Anilesh S. Mahajan, "World Wide Woe", *Business Today*, 19 Aug 2012. goo.gl/y2u6n6

[13] Pratim R. Bose, "ONGC charts out plans to cut losses on Imperial Energy", *Hindu Business Line*, 16 December, 2011. goo.gl/p8ubHl

[14] Nitin Pai, "Playing the Energy Game against China", *Yahoo! News*, 7 July 2010. goo.gl/pXzknL

[15] PIB, "New Division of Energy" Answer to written question in Rajya Sabha, Ministry of External Affairs, Government of India, 6 September 2007. goo.gl/5zrizo

### 2.4 Make better use of bidding consortia and similar arrangements:

*OVL should explore ways to develop shared value with competitor NOCs; in particular, to avoid being driven into escalating auctions against each other.*

*Secures:* Extractors, Supply routes
*Goal:* Bring down effective per-unit fixed cost in acreage or infrastructure acquired.

States or companies auctioning off acreage or stakes in oilfields have been known to encourage competition between NOCs in an effort to push up bidding prices. Unofficial or "leaked" knowledge of highest bids received can be an effective tack to generate higher offers. OVL and Chinese NOCs have been played off into offering inflated bids – or sweetened bids with *post facto* offers of assistance on top – as a result[16].

Again, the nature of competition makes this approach focus on Chinese NOCs. Joint Sino-Indian offers preclude sellers from playing OVL and these NOCs against each other to push up bids. OVL's strategy in Iran may be replicated to take advantage of China's vast leverage where possible: picking up stakes left over after the Chinese bid on the same terms as the Chinese, which secures for OVL bids the softer terms the Chinese NOCs ensure through offers of Chinese development assistance.

In addition, anywhere west of Central Asia, the construction of east-flowing and/or port-bound pipelines (such as from South Sudan to Kenya) is beneficial to India and China alike. In such cases, OVL may even rely on China's unwillingness to suspend its own production and shipments from jointly developed fields – a geostrategic argument for diversifying into fields approached by Chinese NOCs.

If this approach becomes a predictable pattern, however, China is likely to react – not necessarily in the market, but perhaps in how it communicates its unofficial expectations to other governments; or it may simply exercise its first right of refusal. As in Iran, this approach must be used immediately after a successful bid, when the competitor has temporarily exhausted its resources; it will only work where the acreage on sale is vast. Ideally, it should be combined by bidding in one or more consortia, and then seeking stakes in similarly-assessed acreage in that country after an agreement on the primary sale is concluded.

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[16] Sascha Müller-Kraenner, "China's and India's Emerging Energy Foreign Policy", German Development Institute (DIE) Discussion Paper 15/2008, 2008. goo.gl/PosVTW

### 2.5 Cultivating Alliances:

*OVL should improve its bidding power by expanding consortiums to include not only foreign NOCs, but also Indian and/or foreign private investors.*

*Secures:* Deposits (in case of swap deals), Extractors, Supply routes
*Goal:* Expand the portfolio of successful bids, ideally also expand domestic exploration.

Investing in oil and natural gas involves managing diverse risks. Constructing a diversified set of consortia enables joint participation at varying levels of associated risk, with a specialisation in terms of upstream, midstream and downstream stages based on the competencies and priorities of each member of each consortium.

India has various energy cooperation agreements, including inter-governmental agreements with Russia[17] and Brazil[18], as also with the EU and the USA.[19] OVL has worked, with varying degrees of success, with the NOCs of Venezuela, Colombia, Iran, Syria and Malaysia[20] and has long-standing business relationships with other NOCs, such as those of Qatar and Saudi Arabia. Any of these could be leveraged through joint ventures, cooperative bidding, farm-in/farm-out arrangements, swap deals, shared pipeline or port development, etc. Private sector co-operation has also been invited, most recently in Myanmar.[21] Regulatory and financial caps on the size of bids from OVL and other NOCs can be most immediately bypassed by forming such consortiums, as also through public-private partnership (PPP) bids. This can complement external alliances, including by bidding through multiple consortia.

This strategy has no particular downside. It is premised on finding shared value with suitable partners – IOCs, NOCs, and domestic or foreign private players – and is limited only by the regulatory restrictions on and relationships with each partner. If OVL cooperates with any one player across a wide enough range of projects, risks could be spread out in relation to that complete portfolio instead of any single one, an additional form of hedging that some such players may find attractive.

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[17] ENS Economic Bureau, "India, Russia sign IGA on oil & gas, differ on timeline", *Indian Express*, 22 December 2010. goo.gl/F8awJc

[18] "IBSA Summit commits to energy cooperation", *ESI Africa.Com,* 19 November 2007. goo.gl/3ZhsrF

[19] Michael A. Levi, Elizabeth C. Economy, Shannon K. O'Neil and Adam Segal, Energy Innovation: Driving Technology Competition and cooperation Among the United States, China, India, and Brazil (New York: Council on Foreign Relations Press, 2010).

[20] "Iran Offers Gas", *The Telegraph*, 27 May 2013. goo.gl/XI5iMx

[21] Shine Jacob, "OilMin wants a united front to beat China in Myanmar", *Business Standard*, 31 May 2013. goo.gl/MhrxaH

### 2.6 Incorporate Political Risk Factors:

*OVL should account for political risk in a holistic fashion (beyond insurance alone), including the effect of disrupted supply, security of supply routes, and opportunity cost on investment.*

*Secures:* Extractors, Supply routes, Technology

The impact of political risk on production is typically addressed by insuring oilfields and pipelines, which may include some coverage for loss of production. Given the political scenario in various states where OVL seeks to invest, however, the severity of potential disruption tends to be underestimated. OVL's assets in Sudan, for instance, are insured against political risk[22], but have managed only sporadic production for years due to the prolonged civil war scenario in the region. New Delhi had to send a special envoy to establish some kind of normalcy in the region, then a new envoy to address disruptions in South Sudan since July 2013[23]. OVL experiences in Sudan, Iraq, Libya and Syria do not inspire confidence in the prospect of consistently realising production, let alone profits, from such disrupted climes.[24]

This is primarily an internal question, although it may lead to specific arrangements with insurance firms, supplier states or friendly states along supply routes. Beyond insuring investments against damage or disruption, comprehensive assessment involves considering the economic impact of reduced supply, or finding alternate suppliers (especially if a long-term supply contract is disrupted). It also involves ensuring that such effects are priced into the investment decision, especially how the opportunity cost of the investment is affected by prolonged disruption.

While this approach can limit the downside OVL may face, it is limited by its very nature. All risk analysis is predictive; the margin for error is considerable. Given the propensity for upheaval in the regions where OVL operates, the most practical solution may only be to engage in adequate scenario planning and ensure that contingency plans are prepared against various eventualities. As a stop-gap measure, parties responsible for stability in those regions may be asked to arrange or at least compensate for the technical training / experience opportunities OVL anticipated for its personnel in that location.

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[22] Anupama Airy, "ONGC Seeks Political Risk Cover For 2nd Phase Of Sudan Investment", *Financial Express*, April 28, 2004. goo.gl/LNvuGC

[23] Alex Lawler, "Middle East, Sudan Turmoil Cuts Into World Oil Supply", *Energy Tribune*, 30 July 2013. goo.gl/xiG5DC

[24] Ajay Modi and Jyoti Mukul, "OVL invokes force majeure clause for Libyan block", *Business Standard*, 02 Apr 2011. goo.gl/rssZTq

## 3. DOMESTIC AND INTERNATIONAL CONTEXT OF OVL OPERATIONS

### 3.1 India is increasingly reliant on imports

OVL's role in energy security attains significance precisely because India's domestic consumption of fossil fuels has risen sharply[25,26], reaching 219 million tonnes (MT) of crude oil (a 40 percent increase over 2007-08) and 54 billion cubic metres (BCM) of natural gas (a 25 percent increase over 2007-08). Domestic production of crude oil has remained all but flat, increasing barely 10 percent over the same period. Production of natural gas peaked in 2010-11 at 52 BCM, but has again fallen to 41 BCM of natural gas in 2012-13. That shortfall, particularly of crude oil, necessitates ever-growing imports.

**Figure 1A. Effective Price of Oil & Natural Gas Imports**
**Rupee Crores, Constant 2012 Prices**
**Per Million Tonnes Oil Equivalent (MTOE)**

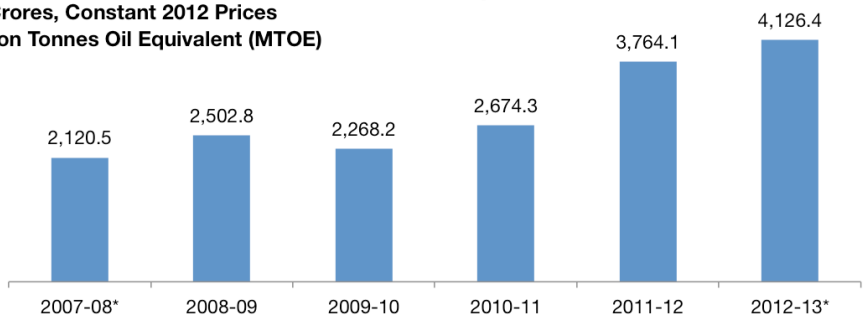
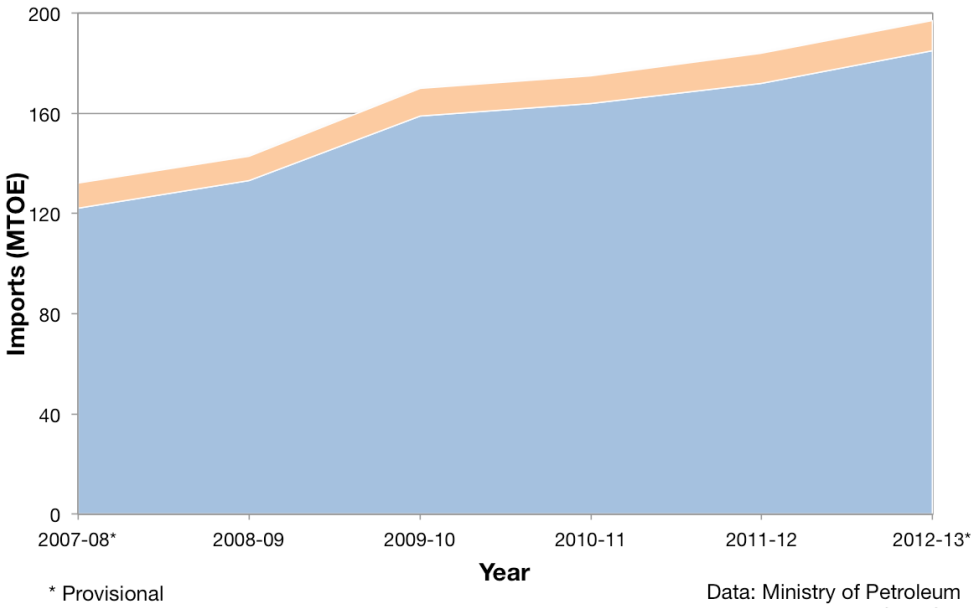



**Figure 1B. Size of India's Oil and Natural Gas Imports**




* Provisional

Data: Ministry of Petroleum and Natural Gas, GoI

[25] "Indian Petroleum and Natural Gas Statistics" Ministry of Petroleum and Natural Gas, 2012-13. goo.gl/qgtdfk

[26] "Energy Statistics 2013" Ministry of Statistics and Programme Implementation, Government of India, 2013 goo.gl/rsDW6G

In FY 2012-13, India imported 185 MT of crude oil, and another 10 MT of Liquefied Natural Gas (LNG); valued at over Rs. 800 lakh crores[27], this represents 33 percent of import expenditure in that year. India exported 48 million tonnes, or approximately Rs. 250 lakh crore worth of refined petroleum products. Net imports of petroleum were thus worth over Rs. 550 lakh crores – more than half of India's trade deficit in that year. Imports have risen by 50 percent over 2007-08 figures; the price of these imports has almost doubled from the 2007-08 figure, crossing Rs. 4,000 crore[28] per million tonnes of oil.

No significant expansion in domestic supply is anticipated before 2020 at the earliest, given the long exploration-to-production time-lag. Demand for petroleum products, on the other hand, will grow over the same period. The trend of rising imports can thus only continue in the short-to-medium-term. It is in this context that any measures taken to address, service, offset, manage and eventually mitigate this demand for imports become of crucial importance.

### 3.2 Geopolitically, India is a minor player

Secure energy access acquires geopolitical significance precisely because geography has not been kind to India. Pakistan straddles Central Asian / Middle Eastern gas pipeline routes to India. Pakistan's own complicated relationship with Afghanistan hinders the proposed Turkmenistan-Afghanistan-Pakistan-India (TAPI) pipeline, but India and Pakistan have a common problem when it comes to the Iran-Pakistan-India (IPI) pipeline[29]: neither can meet Iran's demanded price for the gas.

China, India's major rival in this field, has cornered gas production in Myanmar, from fields developed with joint Sino-Indian[30] investment, as the proposed Myanmar-Bangladesh-India pipeline route negotiations languish. Meanwhile, China and Russia recently resolved a long-standing border dispute[31], with China funding the construction of the massive trans-Siberian pipeline through contested regions of Manchuria[32].

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[27] i.e. 8000 billion rupees.

[28] In 2012 Rupees / not adjusted for inflation.

[29] PTI, "Turkmenistan gas to cost $10/mmBtu", *Economic Times*, 13 Dec 2010. goo.gl/uh1VHQ

[30] K. Yhome, "The Geopolitics of China's New Energy Route", *East Asia Forum*, June 2013. goo.gl/69rVPm

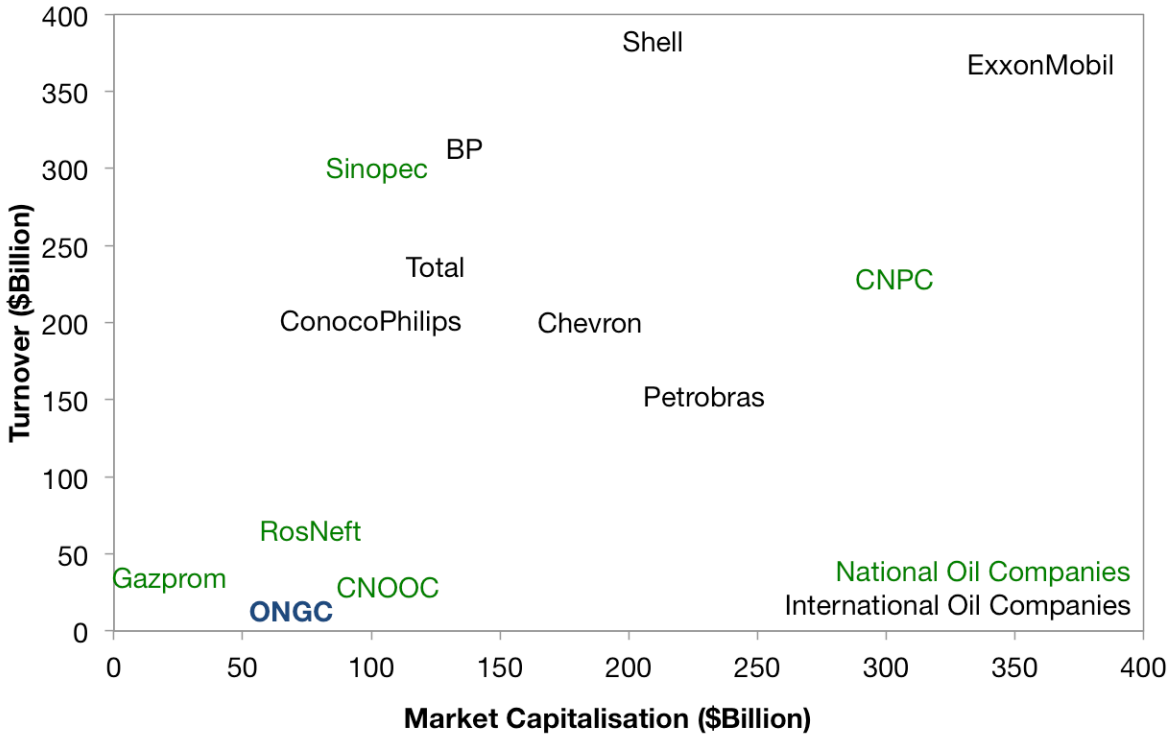
[31] Stephen Blank, "Pipeline to Nowhere: The Beijing – Moscow Dance Continues", *World Affairs*, March/April 2012. goo.gl/Y7lcnB

[32] Andrew E Kramer, "Rosneft to Send $60 Billion Worth of Oil to China", *New York Times*, 20 Jun 2013. goo.gl/ZZmk1I

China is also investing aggressively in its Central Asian neighbours, increasing investments in the Middle East and Africa, and even bid for Iran's Chabahar port[33]. These steps potentially decrease China's dependence on the Straits of Malacca, through which practically all Chinese oil imports flow today[34].

In the global oil market, NOCs are displacing the 'super major' international oil companies (IOCs), reflecting the effectiveness of political leverage on the bidding process[35]. A typical bid will involve a consortium of IOCs, NOCs and domestic investors, only one of whom is designated the operator; companies may bid together on some occasions and against each other on others; NOCs of the same country may bid in different configurations through rival consortiums.

**Figure 2. ONGC Market Capitalisation and Turnover compared to other major oil companies (2012 Billion $)[36]**




Data: Vikram Singh (2012)

[33] Amitav Ranjan, "As China offers funds to Iran, India set to fast-track Chabahar pact", *Indian Express*, 1 July 2013. goo.gl/ktCwFm

[34] Zha Daojiong, "Oil Pipelines from Myanmar to China: Competing Perspectives", RSIS Commentaries 74/2009, July 2009. http://goo.gl/gFE4EQ

[35] "Supermajordammerung", *The Economist*, August 3, 2013. goo.gl/5WyFjJ

[36] Vikram Singh, "BRIC National Oil Companies", unpublished, draft shared by the author, 2012.

Even ONGC, the largest Indian oil company, barely approaches the scale of other NOCs and IOCs; it is the smallest even among the BRIC countries' NOCs. In terms of market operations, Indian firms are price-takers; any acquisition of acreage or sales of oil that ONGC or OVL may carry out are at too small a scale to affect the global market. This point appears to have been internalised, as OVL's investment decisions seem to be driven mostly by internal political economy.

### 3.3 NOCs invest to avoid appropriation of cash surplus, not to secure supply

NOC investment decisions (very rationally) incorporate the imperative of reducing any cash surplus available for appropriation[37]:

> "Impetus [for NOCs to explore foreign sources] comes not from concerns about energy security, but rather from the need to invest cash surpluses & resources before they are appropriated as dividends or forced discounts… (they are) no different from their private counterparts, which in the face of regulatory & political risk choose to invest overseas rather than in more risky climes at home. In fact (for NOCs) the risk of appropriation of surpluses by the majority shareholder (the state) being far higher, they can afford to be more aggressive in bidding for acreage overseas."

Exploration, pipeline and refinery projects come with discretionary spending ability for the NOC in question. If their profits are channelled to Ministry supervision, a lesser amount of funds are left at the NOC executives' discretion. This is a strong argument for disposing of captive funds before they accrue to a higher level of hierarchy.

In India, NOC profits cross-subsidise oil marketing companies (OMCs), which sustain losses due to domestic subsidies on petroleum products. The government's direct share of this subsidy has been below 10 percent; in 2011-12 it was only about Rs. 30,000 crores, as against a total subsidy of over Rs. 500 lakh crores. Importing at market prices while selling at a discount places a dual burden on the economy[38]; the brunt of which falls on NOCs. Therefore, mere acquisition or running of assets like exploration blocks, oil fields, pipelines or refinery abroad does not boost energy security.[39]

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[37] Sunjoy Joshi, "India's Perspective: The Search For Energy Security", in *Crux of Asia: China, India & the Emerging Global Order*, ed. Ashley J. Tellis and Sean Mirski, (Washington DC: Carnegie Endowment for International Peace, January 2013). goo.gl/37h4VH

[38] Niranjan Rajadhyaksha, "The trade deficit and India's weakening energy security", *Livemint*, 20 April 2012. goo.gl/jfrFQh

[39] Shebonti Dadwal and Uttam Sinha, "Equity Oil and India's Energy Security", in Strategic Analysis Vol. 29 No. 3, (New Delhi: Routledge, July 2005).

Further, the profitability of an asset is necessary but not sufficient while deciding to acquire and run new assets.

OVL's operations cannot be called strategic merely because sales from some acquisitions could offset import costs. Any profit-making investment could make that claim, and there are safer and more productive options than oilfields. OVL was set up with the mandate to secure overseas energy supplies for India, must be particularly strategic in its approach; acquisitions must be selected to secure benefits above and beyond mere market rents or operations.

### 3.4 International investors must be reassured about regulatory and political risks

Just as OVL and other NOCs must learn to look beyond their internal political economies, India's energy sector policies too must shift to rewarding genuine progress, rather than protecting existing players or special interest groups. One key concern is restoring investor confidence in India as a secure destination for investment. Strategies premised on attracting external participation to boost domestic production will still fail to attract major IOCs and foreign NOCs unless the government can urgently signal that this sector is a priority area, and one whose development it takes seriously. Measures to improve infrastructure, especially ports, pipeline, transport and storage facilities, may serve as such a signal.

The importance of pricing structures has also long been acknowledged[40]; different levels of resource extraction are viable at different price points. At market prices, all except the technically most difficult reserves – 'tight' oil and gas – will be operationalised; any given level of regulated prices will see a corresponding level of development. The key point is not price itself, as much as it is stability and certainty in pricing[41]. Related concerns include taxation policy, delays in granting clearances, and the willingness to reopen pricing debates after agreements have been signed, all of which create an undesirable degree of volatility.

Finally, given India's heavy reliance on the Straits of Tiran–Arabian Sea route for transhipment of oil and natural gas imports, we must maintain the security of critical sea lines of communication (SLOCs) in this region.

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[40] Sanjay Dutta, "Oilcos told to share cost of Terror Security", *Times of India*, 4 Oct, 2007. goo.gl/BGmtSY

[41] Anne-Sophie Cobeau, "Natural Gas in India", International Energy Agency Working Paper (Paris: International Energy Agency, 2010). goo.gl/MTbHhs

## 4. CONCLUSION

To be said to truly contribute to India's energy security, OVL cannot only earn foreign exchange to offset import payments, but must act strategically by securing deposits, extractors, supply routes and technology. To this end, OVL can gain technological competencies through joint ventures with market leaders, to better access domestic reserves, simultaneously using swap deals and reciprocal arrangements to bring major oil companies to explore Indian reserves as well. OVL can secure more reliable and inexpensive extractors and supply routes, and can target countries where India enjoys unique leverage or soft power advantages. To hold down overall fixed costs on acquisitions, OVL must avoid being lured into bidding wars against other NOC's; rather, it can consolidate resources and risk appetites by forming bidding consortia with these NOC's, as also with private sector players, both domestically and internationally. Finally, OVL can ensure that political risk is comprehensively accounted for through contingency planning, including salvaging training or equipment when production is disrupted.

As the overseas arm of ONGC, operating in a global market that is increasingly captured by NOCs, OVL's role in ensuring India's energy security cannot be understated. This role must be more than mere market operations; it must actively secure increased oil and natural gas supplies for the country. "Energy Security" can be a convenient narrative, but OVL must move beyond focusing on acquisition of acreage and drilling rights alone if it is to change that narrative into a real and substantial contribution. This requires a more strategic approach to acquisitions than the current rush to rapidly reinvest profits and cash surpluses, so as to prevent their being appropriated by the government.

Finally, while this brief is focused on OVL in particular, certain broader domestic policy measures must accompany these reforms to truly unleash their potential. Investment, taxation and pricing of oil and natural gas in particular must be consistent and transparent to help to restore investor confidence in India, and critical sea lines of communication (SLOCs) must be secured. Energy security will remain a bottleneck to India's economic growth, making these measures an urgent priority.

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