

THE OIL CRISIS IN INDIA

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"People must come to accept private enterprise not as a necessary evil, but as an affirmative good."

—Eugene Black

THE OIL CRISIS—THE WAY OUT

By

Prof. Guruprasad Murthy*

In India the oil crisis has assumed a serious proportion. It is, therefore, necessary to recast national energy policy in general and oil policy in particular. We are in a super crisis as far as oil is concerned. Since the West Asian War, the problem has become very critical in view of price escalations and also quantity cuts from which India initially was not exempt. Subsequent communication that India will be exempt from quantity cuts does not justify any complacency on our part. Political and economic measures have to be identified to successfully surmount the problems on hand. Economic policy measures would involve locating the critical or key point to the oil crisis prior to and subsequent to the West Asian War. Foreign exchange being a critical resource, the Government has always been suggesting the need to scale down exchange allocations for crude oil and oil products. Before the West Asian War, the proposed reduction was of the order of Rs. 50 crores (immediately) against an allocation of Rs. 400 crores for the current year. A reduction of Rs. 300 crores in the Fifth plan period was also being planned. However, the West

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Asian War and its concomitant adverse effect on factor market and also the possibility of reduced supplies (either due to exchange shortage, or diversion by oil companies or government access to supplies being limited) call for immediate quantity/price controls on oil products if increased allocation beyond the sustaining capacity of our external account is to be avoided.

The increasing prices of crude, as was obvious even before the West Asian War, will be a permanent burden on and obstruction to the process of our economic development. A 17 per cent increase in the price of crude by the OPEC (Organisation of Petroleum Exporting Countries) on October 17, 1973, will place a severe strain on our exiguous foreign exchange resources. And OPEC will continue to exert such pressure, war or otherwise (as evident ever since its inception), to take full and even undue advantage of its fast depleting natural wasting capital asset. The impact of the 17% increase will take the price of crude per barrel from \$3 to \$3.58. The imports of crude alone is likely to cost us an additional amount of Rs. 25 to 30 crores worth of foreign exchange per annum. Of course, there is some uncertainty of the base with reference to which the 17% increase is to be computed. It is believed that the 17% increase is to be computed with reference to a base of \$5.1 per barrel and not \$3.65. However, the price per barrel of light Iranian crude has gone up from \$2.995 to \$5.091; Arabian from \$3.011 to \$5.119 and Libyan from \$4.604 to \$8.925. This trend will continue and the price of crude may go upto \$10 per barrel very soon. The crude price takes the increase in October, 1973, alone to 44 cents per barrel. And every cent increase means for us Rs. 90 lakhs of foreign exchange. In November 1973, the price of crude went up again by 6 cents a barrel. However, in view of the confusion, the additional burden of crude price increase is estimated in the range of Rs. 114 to Rs. 200 crores by Government and the oil companies. The earlier increases were in accordance with the Teheran Agreement of 1971. The increase effective

from January 1, 1973 was of the order of 2.5 cents a barrel plus an additional increase of 5 cents a barrel. Again, because of a participation agreement in 1972, the tax paid cost increased by 9 to 10 cents per barrel. Over the last two years, crude prices have gone up by at least 150 per cent till the West Asian War. Since then the situation has worsened. The future is still worse because the OPEC regard recent crude price increases as reasonable and attribute price increase to world-wide inflation, currency depreciation, an elastic demand for oil and concentration of supply in the Middle East. In addition, collective resurgence of economic nationalism of theocratic Sheikdoms and depletion of oil reserves will render price increase of crude oil inevitable. The latter phenomenon exists in the very idea of the OPEC. Particularly, the OPEC has insisted that the theoretical posted price should be greater than market price by 40%. The market price and posted price would once again be in spiralling escalation. The West-owned oil companies have also indicated the shift of a preponderant portion of increase in tax-paid cost to India. They have also specified unspecified quantity cuts (except Shell). ESSO has intimated a rise of 95 cents per barrel against the increase of \$1.27 per barrel of Arabian Light and a rise of 98 cents per barrel against the increase of \$1.15 per barrel of Arabian Heavy. In the latter case, the company will absorb 17 cents and in the former case 32 cents per barrel of the indicated increases in tax paid cost. Burmah Shell has notified a price increase of 90 cents per barrel against the increase in tax paid cost of \$1.27 per barrel. The company will absorb the balance of 37 cents per barrel. Caltex notified an increase of \$1.08 per barrel effective from October 16, 1973. However, while Caltex and ESSO have given indications of cuts in quantities of crude imports for whatever reason, the Burmah Shell have been relatively fair*. While the increase in price by these

* Latest information reveals that FSSO is unlikely to cut crude supplies to India. Nevertheless complacency is unwarranted. Moreover foreign exchange is a critical resource.

companies is subject to the behaviour of factor market and the sulphur content of crude, the future is uncertain in terms of their participation with the objectives of Indian economic policy. The net effect of all this is an annual outgo of foreign exchange to the extent of Rs. 400 to Rs. 500 crores, including petroleum products, against the plan to scale down the outgo by Rs. 50 crores for the current year against oil and oil products. If further disaster is to be avoided some sort of controls are a must.

The way out of the oil crisis is good management which means that the government should Manage by Objectives and Manage for Results. Results would mean effectiveness (i.e., accomplishment of intended goals), and efficiency (i.e., refers to the ratio of results to resources). The problem areas that can be identified for initiating either response action or response corrective action are .

1. Economic Management (Market mechanism and conscious direction and the impact of the choice or combination on the objectives and results).
2. Social Management (Impact of Economic Management on society and supplementary or complementary action needed to subserve economic management and eventually the results and objectives).
3. Technology Management (Substitution effect in the short and long run and also advanced technology for exploration programmes and its impact on objectives and results).
4. Political Management (Its impact on objectives and results).
5. Police Management (Role of vigilance in identifying anti-social elements *ex ante* and its impact on objectives and results).
6. Foreign Investment Management (Its impact on objectives and results in the short and long run, respectively).

The above classification is used as a convenient point of departure to attempt a "Scientific Management Approach" to politico-economic and socio-economic problems pertaining to the oil crisis.

Economic Management

In order to cope up with the present oil crisis, the Government has resorted to the market mechanism, in lieu of conscious direction of resources. The increase in prices of oil products, except Naptha which is a feed stock in fertiliser plants and an essential item for our agriculture, is intended to curb consumption and redress thereby the imbalance between the demand for and supply of crude oil and/or foreign exchange.

Will the price increase of petrol produce the intended results? The answer is, unfortunately, in the negative. It is clear by intuitive reasoning, trial and error and logical economic analysis that the intensity of the demand is a curicus amalgam of spurious (speculation), semi-spurious (precaution) and non-spurious (transaction) factors. These factors viewed in juxtaposition with the marginal utility of purchasing power, the economics of black money, inflation and the socio-psycho profile of the petrol consuming entities give the impression that there is an attraction to prodigal dispensation of wealth, a temptation to conspicuous consumption and an inclination to ostentatious display of opulence. The interaction of the social, economic and psychological factors causes repulsion from austerity, rectitude and discipline. A price increase of petrol is, therefore, an impotent instrument, inadequate prophylactic and inappropriate policy measure to effectively remedy the situation. Government policy must take cognisance of the fact that the objectives of economic policy measure are to reduce quantities consumed and incidentally raise revenues and subserve other objectives. A merely revenue-oriented policy is rather preposterous in this case. And inspite of a fervent plea in "The Economic Times" (October 20, 1973) by the author to eschew the doctrinaire approach of using price

increase as an exclusive measure, the government till now has refrained from petrol rationing for uncertain reasons. The market mechanism will be ineffective and inefficient in making demand for petrol responsive to price increases unless black money is weeded out and income tax legislation suitably amended and honestly administered or the price hike is more.

The imposition of rationing is claimed to create administrative difficulties. Since June 1973, the idea has been pushed from pillar to post. However, the impact of the absence of rationing is to be identified with the following factors :

- a) precluding the country the privilege of managing the oil import bill with limited foreign exchange which can be used for other purposes;
- b) actively inviting the possibility of a fundamental disequilibrium on the external account especially in the light of the foodgrains imports, crude oil price increase and improvements in our foreign exchange reserves being notional;
- c) causing shortage of naphtha and thereby laying a sound foundation for food shortage which means more foreign exchange requirements, higher food prices and further decline in the standard of living of the ordinary man; the opportunity cost of one litre of petrol is 10 kilograms of additional foodgrains. A 25 per cent cut in petrol consumption means about 6 million tonnes of foodgrains due to increased naphtha produced;
- d) developing a series of physical imbalances in the economic system as a result of active financial problems on the external account thus giving fillip to the already decelerating process of economic growth;
- e) a total jeopardy in case of war or other similar contingency at home and the resultant adverse

political, social and economic impact. Comparing factors (a) to (e) with administrative difficulties (which in terms of Costs are predominantly fixed) it is clear that even an intuitively computed cost benefit calculus justified the introduction of petrol rationing long back. The ordinary man and the country have to pay a high price for managerial incompetence and administrative delays or it is a declared objective of decision-makers to play into the hands of vested interests which forestalled rationing initially (to avoid inconvenience) and postponed it eventually to take full and undue advantage in the long run by speculative demand. Thus the objective seems to be to leave enough time interval to allow speculation and precaution demand to operate to the detriment of the masses who have to be the ultimate victims of the impact of government policy [factors (a) to (e).] The cost of administering petrol rationing has to be weighed against the direct impact on the country's economic viability, political vulnerability and social instability, and of course the ultimate impact on the cherished socio-economic objectives of economic policy.

The objective of rationing is to curb consumption, and it may operate in one of the following ways :

- a) Dual pricing by allowing essential sectors necessary austere level quantities at regulated price (including excise) and leaving the remaining quantities to the open market with the entire increase in price in the open market being an excise duty.
- b) Dual pricing by allowing predetermined minimum quantities (austere level) to all sectors, at a regulated price (including excise) and leaving the remaining to the open market, with the entire price increase in the open market being an excise duty.

- c) Dual pegged price which will make available to all sectors the minimum quantities (austere level) at a lower pegged price (including excise) and remaining at a higher pegged price (including excise).
- d) Predetermined minimum quantities at regulated price (including excise) with no quantities left to the open market.

The advantage of the first method is that the cost of administering the non-essential sector is virtually zero. No rationing card or coupon system is necessary. However, the linkages (forward and backward) should be appropriately plugged. Also the possibility of theft and pilferage which may induce the anti-social elements to transfer the commodity from essential sectors to non-essential sectors should be, at least now, properly policed. Although, the open market price will be very high, the government's objective of curbing consumption will be served *ab initio*. Its penchant for revenue, which should be secondary, may also be served. Distribution to essential sectors will take place at petrol pumps where the vehicles have to be registered whereas for the non-essential sectors the quantities can be distributed at selective petrol pumps. The tax element of price increase may act as a fillip to inflation if increase in revenue is not followed by proportionate and simultaneous scaling down of expenditure in possible segments. The economic activity of petrol pumps will however be hit considerably; especially some members of the vulnerable sections may lose their jobs.

Also, a classification of petrol consuming entities into essential, and non-essential sectors is a necessary condition.

In the second method, ration cards will have to be issued to car owners. Coupons or cards supported by registration at a petrol pump with a marginal "ration fee" will be preferred. The quantities made available at regulated price should not exceed the number of cars registered at a petrol

pump. The open market price will once again be high and either people will refrain from consumption (objective accomplished) or pay the price (revenue increase due to tax element of price rise and also inflation control). There is once again the danger of pilferage, misappropriation, linkage effects and problems of reduction in petrol pump activity and unemployment.

In the third method, dual pegging will have the advantages of regulated price (with tax element) for minimum quantities and higher regulated price for quantities consumed above the specified minimum. The only advantage is that the price rise in the open market is controlled with the resultant loss of revenue and increased possible control over inflation. However, dual pegging will mean total substitution of the market mechanism by bureaucratic fiat. All the other disadvantages exist.

In the fourth method, the open market is abandoned *in toto* and a predetermined quantity is made available. Consumption is curbed, and revenue increase restricted, relatively, to the incremental tax element of the regulated price and quantities consumed. The disadvantages of nefarious behaviour and adverse side impact will still exist. But the cost of not introducing controls is greater than the cost of introducing controls. *Ipso facto*, cost of control is less than benefit inasmuch as the choice is between the devil and the deep sea.

The price of kerosene has been increased because of the possibility of adulteration of kerosene with petrol. In the first place, an increase to the tune of 28 paise per litre will increase the monthly cost of a hurricane lamp by 70 paise and that of a wickstove by Rs. 3.5. The marginal utility of money to the ordinary man is so high and real purchasing power so little that his vulnerability is being increased. The reduction in the price of kerosene to the extent of 10 paise however reveals the *ad hoc*, arbitrary objectives of the November 3 price increase.

If diesel using entities are declared essential sectors and diesel is given in adequate quantities at regulated prices and the non-essential sectors buys it in the open market (if it is not rationed) the possibility of adulteration affecting the public transport/or the essential sectors in urban and rural areas is eliminated. If entities other than public transport use diesel the possibility of adulteration can be minimised by rationing diesel. In fact, the price of kerosene should be reduced because, it would set in a marginal disinflationary force. and kerosene is available on rupee payments.

Social! Management

The effectiveness and adequacy of attempts to resolve the crisis in general and petrol rationing system in particular will be greatly influenced by the promptitude and thoroughness with which supplementary measures and complementary action are achieved in the set-up in which the controls are intended to give results. The suggested measures are:

- (a) Identify impact of controls :
 - (i) The controls will have the immediate impact of reducing the quantities consumed and also boosting revenues to the exchequer to the extent of the tax element of price increase and consumption volume.
 - (ii) The adverse impact is in terms of taxi trade being rather badly hit and aggravation of the unemployment problem.
 - (iii) In order that the taxi trade is not adversely affected, rationing must be supported by measures which divert demand from private cars to taxis. This could be done by restrictions on travelling by private cars, partially or otherwise, which would immediately divert demand in favour of

taxis. Institution supported vehicles should be asked to divert executive travel in favour of taxis on a joint basis so that untoward consequence of unemployment and or hardship to the taxi trade is forestalled while austerity in petrol consumption is simultaneously achieved. The number of persons allowed in a taxi may be increased to 5. Strict enforcement of meter rates at all hours is essential.

- (iv) Restricted number of working days in a week in Government and elsewhere will result in the saving of petrol. This will relatively ease the pressure on public transport.
- (v) If weekend private car travelling is temporarily suspended the twin objective of austerity and minimisation of the adverse side impact of petrol rationing can be achieved.
- (vi) The adverse impact on people working in the petrol pump stations should be solved by creating employment (assuming labour mobility) in sectors responsible to improve public transport and automobile industry should alter the product mix in favour of vehicles for public transport (buses, large sized taxis and lorries). The Central Road Fund plus the revenue raised by increase in price of kerosene and petrol should be put to active productive use. Inflationary forces will not therefore get a momentum.
- (vii) Superfluous use of oil-based energy or any other form of energy should be discouraged. In this connection there is considerable scope for curbing consumption in the field of civil aviation, which accounts for a sizable amount of fuel. Again, the Government which is responsible for nearly 60

per cent of petrol consumed should initiate austere measures based on enlightened self-restraint.

Technology Management: This would involve an attempt at altering the demand structure of energy away from oil based energy and also increasing other sources of energy.

Supply Position: While reduction in quantities of petrol and other forms of fuel can be brought about by autotas and technology permitting substitution effect, supply position should be taken cognisance of in the following fashion : (a) Diversification of sources of crude by tapping Indonesian, USSR and other possible crude sources; (b) Activating ventures to undertake oil exploration programmes at home and abroad especially Bangla Desh; (c) Agreements to procure crude for rupee payment and bilateral barter deals should be explored.

Police Management: Pilferage and misappropriation seems to be an accepted way of life. A rather high amount of oil is pilfered in the dock area when the process of bunkering is in operation. Urgent drastic action by the authorities will save the country from further disaster.

Foreign Investment Management: The objective of policy towards the foreign oil companies should be oriented. as it has been so far, to assure ourselves of the crude supplies, and as far as possible not to scare foreign investors from making useful contributions to national economic development. Moreover, in times of war, active, lively, friendly contacts with West owned oil companies is more useful than any one else as far as oil is concerned. At the same time, a policy design and de jure organisational relationship which prevents a step-motherly treatment to India is a necessary condition if the idea of outright nationalisation of the oil companies in India is to be ruled

out now or in the near and remote future. This is a problem area, very sensitive where political wisdom and economic assessment have to operate after taking into consideration the long run interests of India.

CRUDE OIL REQUIREMENTS AND IMPORTS (Million Tonnes)

Government Imports	8.25
Burmah Shell	3.75
Esso	2.75
Caltex	1.25
Indigenous Supply	<u>7.00</u>
	<u>23.00</u>

(Source : " Oil Statistics Journal ")

PRODUCTION OF PETROLEUM PRODUCTS IN INDIA

Product	Thousand Tonnes			
	1965	1970	1971	1972
Gasoline & naptha	1493	2766	2810	2862
Kerosene	1425	2912	2995	2813
HSDO	1665	3763	4356	4598
LDO	766	1024	1065	1010
Fuel oils	2618	4239	4098	3688
Others	1146	2473	2905	3237
TOTAL	9113	17177	18229	18208

(Source : "Oil Statistics Journal")

PRODUCTION OF MOTOR VEHICLES IN INDIA (1972)

Cars	38,828
Jeeps	12,518
Commercial Vehicles	38,702
Motor Cycles	47,561
Scooters	64,731
Three Wheelers	9,790

GROWTH OF THE PETROLEUM INDUSTRY IN INDIA

YEAR	CRUDE OIL Production (Thousand Tonnes)	PETROLEUM PRODUCTS Production (Thousand Tonnes)	PETROLEUM PRODUCTS Consumption (Thousand Tonnes)	IMPORTS		EXPORTS (Rs. crores)
				Crude Oil Products (Rs. crores)	TOTAL	
1950	259	211	3320	—	51.84	51.84
1955	347	3024	4818	24.31	60.53	84.84
1960	454	5741	7784	40.57	40.02	81.59
1965	3022	9113	12279	40.38	44.73	85.11
9701	6809	18459	18734	102.36	30.53	132.89
1971	7185	18229	20640	139.88	43.4	183.37
1972	7373	18208	22547	144.01	56.77	200.78

THE OIL CRISIS AND ROAD TRANSPORT

By

Dr. F. P. Antia*

We are in the midst of the worst-ever oil crisis. The problem of escalating crude oil prices will remain with us. Considering that our foreign exchange reserves are considerably eroded by foodgrains imports and the rising costs of maintenance imports, we just cannot afford the luxury of an imports-based, oil-biased energy policy.

Our import of crude and other petroleum products cost us Rs. 55.5 crores in 1950. This increased to Rs. 81.6 crores in 1960 and further to Rs. 132.6 crores in 1970. By 1972 this jumped to Rs. 200.4 crores and is estimated to shoot up to 460 crores in 1973. Our crude imports, currently, amount to 16 million exclusive of 4 million tonnes of other petroleum products. Our internal petroleum resources account for only a third of our total consumption. The scope for enlarging the indigenous petroleum resources is limited in the short run. But our industry, power generation systems and transportation are heavily dependent on oil. Let us hope our Bombay High venture will strike oil, which in our case will be as good as striking gold.

Given these parameters, a more sophisticated, selective policy of regulated consumption, rather than a blanket rise in prices through enhanced excise duties, is called for. Admitting that consumption would have to be reduced by 25% over the pre-West Asia conflict levels, there is scope

* The author is an eminent authority on transport economics and is actively associated with several organisations in this field.

ior evolving a production and welfare-oriented policy. Even within the reduced levels of consumption, a system of two-tier pricing will become necessary. Incidentally, we have to reduce and rationalise consumption through a pragmatic adaptation of road development policy as well as regulation and taxation of commercial road transport.

The use of a car is not always an unproductive luxury or a social misuse of funds by idle rich. In the case of a business man, a civil servant, an engineer, an industrialist, a professional man like an advocate or a doctor, it is essential as he uses it for productive work essential to the community at large.

It adds a new dimension of productivity to his time and contributes to the national income. The same cannot be said of the use of a car for sending children to school, when alternative school buses or public services can provide this service. On the other hand, use of cars for visits to cinemas, etc. must attract luxury level taxation. Here too we must remember that our cumulative tax burden on petrol at 84.3% before the recent hike is already the highest in the world. Leaving it to the Government to classify, I shall submit that socially indispensable (as that of a doctor) and economically productive (as that of an industrialist or professional) uses must not be subject to the recent excise duty rise. Roughly, two-thirds or three-quarters of the consumption of petrol by these classes should not attract the recently raised excise duty although they may well be asked to pay the 7 paise rise in cost of crude.

There is a sound economic justification for this. We are in a self-perpetuating inflation. So raising the costs of transport, whether petrol or diesel, will stimulate further the already intense cost-push inflation. We are even more vulnerable as the majority of car owners are reported to belong to the Public Sector. So a non-selective rise in petrol price will only push up non-plan, non-developmental expenditure. Instead of stabilising prices and underwriting growth, this will add further fuel to the inflation and sap

the reserves of vitality in the economy. Again this will act as a damper on generation of additional employment as the tempo of general economic activity will decline, not to mention the halting expansion of road transport, an employment-rich sector.

Also we can rationalise the consumption of petrol and diesel through appropriate road development policies. The neglect of our roads is imposing on the nation's motor fleet avoidable excess in the consumption of fuel by 25%. Scheduled road maintenance will scale down this excess consumption. This involves no foreign exchange and will create additional employment. Again, better roads will speed up the traffic facilitating higher traffic output at lowered levels of fuel consumption.

Coming to trucks carrying goods, poor roads preclude us from resort to trailerisation. Trailerisation delinks the power unit from the body and applies the principle that pulling a load is easier than carrying it. Further, through multiple use of trailers, this maximises journey time and traffic output. More significantly the power unit is engineered to haul heavier loads but at a substantially less consumption of fuel. So per ton km. of traffic the consumption of fuel will be reduced by over 40%. But poor maintenance, inadequate road crusts, weak bridges and culverts, even on arterial roads, prevent us from reaping the fuel economy and productivity benefits of trailerisation. So all-round road improvement is the first necessity. Truck-trailer units have more axles than the conventional truck. So long as the number of axles get the gross laden weight evenly distributed and within permissible weights, the truck-trailer will not impair the road surfaces.

By tailoring road programmes through scheduled maintenance and elimination of road deficiencies we can cut down fuel consumption, facilitate enhanced traffic output and release extra truck chassis for export, not to speak of the additional employment absorbing millions of unskilled labour.

A study by the Operations Research Group, Baroda, has revealed that 62% of the domestic transport of exports cargo to the ports go by road. If we raise the duties on petrol or diesel, domestic haulage costs of exports too would rise. This will raise the prices of our goods in foreign markets. Unlike the petroleum producing countries, we are not in the happy position to dictate the price to the foreign buyers of our goods.

Raising the excise duties on petrol and diesel being non-selective, would prove to be counter-productive. Our aim is to do something more than merely curbing consumption of petroleum products. We must attain fuel economy and optimisation of output of goods and services. There is a very strong reason to bring down the excise duties to the October 1973 level for all socially desirable and economically productive uses of fuel. Goods and passenger transport operations, whether in the public or private sector, merit judicious reduction of excise duties, as their costs exercise an impact on the price level. A dual-price system and rationing with issue of coupons for essential uses can be considered.

We can tide over this crisis. But we must be willing to overhaul our transport policy, rationalise operations and adopt a selective approach.

SELLING PRICES OF PETROL AND H.S.D. (PER LITRE)

Year and percentage of increase	Petrol H.S.D. Oil	Prices increases Due to :
1962	00.67 00.51	
1965 (25.8)	00.86 00.74	Excise Duty.
1967	00.98 00.78	
1968 (1.5)	00.99 00.79	Company Prices increased.
1969 (1.3)	1.06 00.79	Excise Duty.
1970 (1.3)	1.16 00.79	Excise Duty.
1970 (1.6)	1.16 00.79	Company Prices increased. Retail trade absorbed increase, except 93 Octane.
1971 (29.5)	1.36 00.79	Excise Duty.
1971 (29.5)	1.39 00.82	Crude prices increased.
1971 (1.7)	1.42 00.83	State Sales Tax.
1972 (1.4)	1.43 00.83	Octane rating from 79 to 83.
1973 (1.3)	1.52 00.83	Excise Duty and Sales-tax on percentage basis.
1973 (11.6)	1.55 00.86	Crude Prices & Sales Tax.
1973 (22.8)	1.67 00.87	Crude Prices & Excise Duty.

(Source: Petrol Dealers Association, Bombay)

The views expressed in this booklet are not necessarily the views of the Forum of Free Enterprise.

"Free Enterprise was born with man and shall
survive as long as man survives."

—A. D. Shroff
(1899-1965)
Founder-President,
Forum of Free Enterprise.

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