

THE EFFECT OF ROLLING BACK PETROL PRICES



vEcoSys

The Effect of Rolling Back Petrol Prices



THE EFFECT OF ROLLING BACK PETROL PRICES



While Petrol prices seem to be running away astray, what one must understand that causing “Bharat Bandh” and other protests and eventually rolling back prices does not help the situation.



THE EFFECT OF ROLLING BACK PETROL PRICES

For example, if India sells 100 units of produce at Rs 1000.

This means as long as India spends

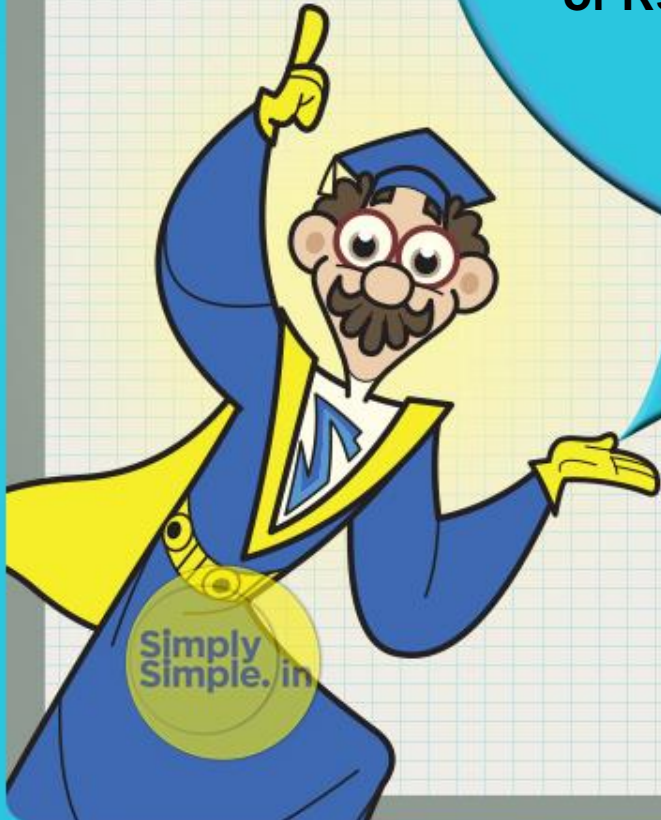
Rs 1000, it can recover it by selling the 100 units.

At this stage the economy is balanced.



THE EFFECT OF ROLLING BACK PETROL PRICES

Now, let's say India sells a liter of petrol at Rs 50 instead of Rs 75 (its true value) thus making a loss of Rs 25 per liter.



THE EFFECT OF ROLLING BACK PETROL PRICES

To compensate for this Rs 25 loss, India will either borrow Rs 25 or print currency of Rs 25. Whatever be the case, for the additional Rs 25, India does not produce any goods. The number of units continues to remain at 100. In the absence of any real production, India will recover the Rs 25 from its citizens by spreading the loss across the 100 units.



THE EFFECT OF ROLLING BACK PETROL PRICES

So, the system had 100 units and was sold at Rs 1000. However, due to the loss, an additional Rs 25 (borrowed money or printed currency) was added into the system.

So while the units remained 100, the money in the system became 1025. While the price per unit in the previous situation was $1000/100 = \text{Rs } 10$, now the price per unit would become $1025/100 = \text{Rs } 10.25$.



THE EFFECT OF ROLLING BACK PETROL PRICES

This is how the recovery takes place across all the units. In other words, the value of the rupee goes down because the same number of units is now purchased at a higher amount.

A very similar thing is happening in India. People are spending more than they are producing. This is causing fiscal deficit or a gap between what we spend and what we earn. So naturally, the value of money is eroding in the economy as explained in the earlier example.



THE EFFECT OF ROLLING BACK PETROL PRICES

India does not produce enough petrol and therefore imports because petrol is an essential commodity. As shown in our earlier example, the increase in petrol prices is not being passed on to the end consumer. Had the increase been passed on to the consumer, the system might have self regulated itself by way of the consumer and reducing the consumption because of higher prices.



THE EFFECT OF ROLLING BACK PETROL PRICES

Since the price rise does not get fully passed on, the demand for petrol remains unabated and India has to import more quantity of petrol. This naturally leads to more paper money (or borrowing) in the economy without a commensurate increase of real goods in the economy. This means that the price of goods in the economy increases to offset the loss of petrol sales.



THE EFFECT OF ROLLING BACK PETROL PRICES

Thus, instead of fewer people paying for the increase in the price of petrol, now they pay by way of higher prices of goods. This is what is commonly called inflation. So in essence, by rolling back prices, the people at large may not benefit as they are hit by inflation which erodes the value of their money.



THE EFFECT OF ROLLING BACK PETROL PRICES



Hope you have understood

The effect of rolling back petrol prices.

Thinking of Investment

Contact

vEcoSys



DISCLAIMER

The views expressed in this lesson are for information purposes only and do not construe to be any investment, legal or taxation advice. The lesson is a conceptual representation and may not include several nuances that are associated and vital. The purpose of this lesson is to clarify the basics of the concept so that readers at large can relate and thereby take more interest in the product / concept. In a nutshell, Professor Simply Simple lessons should be seen from the perspective of it being a primer on financial concepts. The contents are topical in nature and held true at the time of creation of the lesson. This is not indicative of future market trends, nor is vEcoSys IMF Pvt. Ltd. attempting to predict the same. Reprinting any part of this material will be at your own risk. vEcoSys IMF Pvt. Ltd. will not be liable for the consequences of such action.

**Mutual Fund investments are subject to market risks,
read all scheme related documents carefully.**

