

3. Oil Economy– International Relation

Fearing de-dollarisation– On the U.S., oil and the petrodollar. The global oil market is witnessing a shift from the U.S.-dominated Petrodollar system toward de-dollarisation, driven by sanctions and geopolitical fragmentation, with nations exploring local currency settlements. Simultaneously, structural changes in oil trade—distinguished by sweet/sour and light/heavy crude varieties—and the push for energy transition are redefining energy security for import-dependent economies like India.

1. The Petrodollar System and De-dollarisation

A. The Petrodollar System

Definition– The global practice where international oil trade is primarily priced and settled in U.S. dollars.

Origin (Early 1970s)– emerged after the collapse of the Bretton Woods system.

The Deal– Negotiations between the U.S. and Saudi Arabia led to an agreement where oil-exporting countries would price crude exclusively in U.S. dollars.

Quid Pro Quo– In exchange, the U.S. provided security guarantees and financial access to these nations.

Global Norm– This arrangement was adopted by OPEC, making it the global standard.

Significance– Links energy markets with global finance. Transforms oil from a mere commodity into a pillar of international monetary power.

Current Status

1. Approximately 80% of global oil trade is still settled in dollars.
2. Sustains constant international demand for U.S. currency.
3. Allows the U.S. to finance large fiscal/current account deficits.
4. Enables the U.S. to exercise geopolitical influence via sanctions and financial controls.

B. De-dollarisation

Definition– The process by which countries reduce their dependence on the U.S. dollar (USD) in trade, reserves, and finance.

Drivers– Recent U.S. sanctions on Russian energy and engagement with Venezuelan oil have accelerated concerns over dollar dominance.

Mechanisms

1. Using alternative currencies.
2. Bilateral settlement agreements.
3. Creating regional financial mechanisms.

Objectives

1. Enhance monetary sovereignty.
2. Reduce exposure to U.S.-led sanctions.

2. Crude Oil– Basics and Extraction

A. Definition and Composition

Nature– Naturally occurring, non-renewable fossil fuel.

Composition– Primarily hydrocarbons formed from buried organic matter under heat and pressure over millions of years.

Significance– Provides approximately 30% of the world's total energy supply.

B. Extraction and Processing

Extraction– Drilled from underground reservoirs (land or seabed), often found alongside natural gas and saline water.

Processing– Transported to refineries for distillation.

End Products– Petrol, diesel, Aviation Turbine Fuel (ATF), Liquefied Petroleum Gas (LPG), and petrochemical feedstocks.

3. Types of Crude Oil

The market categorizes crude oil based on density (Light/Heavy) and sulphur content (Sweet/Sour).

Feature	Light Crude Oil	Heavy Crude Oil	Sweet Crude Oil	Sour Crude Oil
Characteristics	Low density; flows easily.	High density; high viscosity.	Low sulphur content (<0.5%).	High sulphur content (>0.5%).

Refining	Cheaper/easier to refine.	Requires complex techniques (coking/hydrocracking); higher cost.	Fewer pollutants; less corrosion to equipment.	Technically challenging; requires desulphurisation.
Yield	High proportion of petrol, diesel, aviation fuel.	More residual products.	Meets environmental standards easily.	More polluting.
Key Sources	USA (Shale), North Sea (Brent), Nigeria, Azerbaijan.	Venezuela (Orinoco), Canada (Oil Sands), Mexico, Middle East.	USA (WTI), North Sea (Brent), Libya, Indonesia.	Middle East (Saudi, Iraq), Canada, Venezuela, Russia.

4. Global Oil Trade and Benchmarks

A. Major Benchmarks

Brent Crude– Light and sweet; sourced from the North Sea. The most widely used global benchmark for waterborne crude.

West Texas Intermediate (WTI)– Light and sweet; key U.S. benchmark; heavily traded in North America.

Dubai/Oman– Prices Middle Eastern oil for Asian markets; often linked to Brent.

OPEC Reference Basket– Used by OPEC for pricing decisions.

Western Canadian Select (WCS)– Heavy, sour benchmark for Canadian oil.

Regional Benchmarks– Bonny Light (Nigeria) and Urals (Russia).

B. Key Organisations

OPEC (Organization of the Petroleum Exporting Countries)

1. Founded– 1960.
2. Goal– Coordinate policies, stabilize markets, ensure fair prices.
3. Members (12)– Saudi Arabia, Iran, Iraq, UAE, Kuwait, Venezuela, Nigeria, Algeria, Libya, Congo, Equatorial Guinea, Gabon. (Angola withdrew in Jan 2024).

OPEC+–

1. **Formed**– 2016.
2. **Composition**– 12 OPEC members + 10 non-OPEC nations (includes Russia, Mexico, Kazakhstan, Oman).
3. **Function**– Coordinate production levels to influence the global market.

C. Top Producers and Reserves

Rank	Top Producers	Top Reserves
1	United States	Venezuela
2	Saudi Arabia	Saudi Arabia
3	Russia	Canada
4	Canada	Iran
5	Iraq	Iraq

5. Current Global Oil Market Scenario

A. Structural Changes

Geopolitical Fragmentation– Intensified by the Russia–Ukraine conflict. Western sanctions disrupted supply chains, pushing buyers (India, China) to alternative settlement mechanisms.

Oil Quality Mismatch– The U.S. produces light sweet shale oil but has refineries designed for heavy sour crude, driving its interest in Venezuelan and Canadian oil.

Market Volatility– Driven by West Asia conflicts, OPEC+ decisions, and climate disruptions.

B. Energy Transition

Demand Shifts– Rapid EV growth (especially in China) is weakening future oil demand.

State Intervention– Governments now use strategic reserves and export controls, reducing the role of pure market-driven pricing.

C. De-dollarisation Trends in Oil

Non-Dollar Trade– Russia accepts rubles/yuan; China uses yuan for Gulf/Russian oil.

BRICS Initiatives– Discussions on alternative payment systems and local currency trade.

Bilateral Arrangements– India using rupee-based frameworks and third-currency settlements for Russian oil.

Weaponisation of Dollar– U.S. sanctions on Iran/Russia have incentivized parallel systems like China's CIPS.

6. India's Position in the Oil Economy

A. Vulnerabilities

Import Dependence– Over 85% of crude is imported.

Economic Impact– A \$10/barrel rise in prices can increase CPI inflation by 25–35 bps and reduce GDP growth by 20–30 bps.

Strategic Storage Gap

1. Current SPR– Covers ~9–10 days.
2. Total Cover (SPR + Industry)– ~70–75 days.
3. International Benchmark (OECD)– 90 days.
4. Target– Increase SPR to ~11.83 MMT (approx. 22 days of demand).

B. Mitigation Strategies

Source Diversification– Moving beyond West Asia to include Russia, U.S., and Africa.

Energy Mix Shift– Non-fossil capacity to exceed 50% of installed electricity capacity by mid-2025. National Green Hydrogen Mission targets 5 MMT annual capacity by 2030.

Biofuels– Promoting ethanol blending, bio-CNG, and biodiesel.

Conclusion

The petrodollar system is weakening due to geopolitical fragmentation, active de-dollarisation by major economies like Russia and China, and the global energy transition. Oil trade is increasingly defined by currency politics rather than just market fundamentals.

Source– <https://www.thehindu.com/opinion/editorial/fearing-de-dollarisation-on-the-us-oil-and-the-petrodollar/article70491351.ece>