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The power blackmail

Without giving competitive bidding in power a fair trial, some have proclaimed its non-viability, says Uttam Gupta

EVEN as attention is focussed on what the Maharashtra government will do to the Dabhol power project, the core issues raised in this case must come under a thorough public scrutiny; for these are not peculiar only to Dabhol, but are relevant to majority of the other PPAs. Even the broad guidelines which various state governments are using as benchmark for laying down the essentials of the purchase agreement tantamount to a virtual surrender to private power generators.

The government's policy of providing for a return of 16 per cent at a plant load factor (PLF) of 68.5 per cent is fraught with possibilities of unprecedented profiteering for the generator and serious financial loss to the SEBs. It implies that all elements of fixed cost are allowed to be recovered at a capacity utilisation of 68.5 per cent. In the case of Dabhol, the installed capacity of the first phase being 695 mw, the normative level of power generation, for the purposes of allowing fixed charges, is 476 mw. If tne plant produces this much of electricity, it will be able to fully discharge its obligations towards interest, repayment of loans (coming essentially from depreciation) and other fixed expenses.

Generation of electricity beyond the level of 476 mw will yield a clear bonus towards these charges and correspondingly, add to the profitability of the company. According to newspaper reports, the price at which Dabhol is expected to sell electricity under the PPA to MSEB is about Rs 2.40 per kwh. How much out of this is towards the fixed charges, including the capital related charges, is not known? Apart from the overall investment cost, this will depend on a host of other factors like the financing pattern, interest on loans tied up from various sources, allowable rate of depreciation, methodology for allowing other elements of fixed cost etc. However, to understand the implications, there is an indirect way of looking at it.

We could subtract from Rs 2.40 per kwh the variable cost which is predominantly the cost of fuel. Dabhol proposes to use LNG or alternatively, naphtha. At the prevailing rates, the landed cost of imported naphtha is about Rs 6,000 per tonne. That is the value of 10 million k cal of energy; or Rs 6 for 10,000 k cal. About 2000 k cal of energy is required to generate one unit of power. On this basis, the cost of fuel would be about Rs 1.20 per kwh. Take it off from Rs 2.40, the balance will approximate the fixed charges.

Now, what the agreement means is that on every unit that is generated above the 68.5 per cent level, the profits of Dabhol will increase by Rs 1.20. And the designing, lay out, sizing of plant and equipment and process parameters are such that the PLF can go up to as high as 90 per cent. The plant is based on imported fuel and has dedicated infrastructure including an exclusive jetty to receive and handle (cost included in the project). This, in turn, will ensure continuous and uninterrupted supply of fuel. Demand too is fully assured as under the PPA, MSEB is obliged to take the entire quantum of electricity generated by Dabhol.

Detailed scrutiny of various MOUs by the CEA has brought to light cases of substantial padding of cost. This is true of Dabhol as well. Because of this, the profitability at each level of PLF gets artificially inflated. This cascading effect could be another major source of profiteering.

The philosophy behind any normative system of pricing is that it provide incentives for doing better and penalise for doing badly. Much depends on the norm itself. In this case, when it is known that the plant can produce at 90 per cent and sell without any risk, why fix its tariff at 68.5 per cent PLF and legitimise a clear-cut bonus over a vast range of 21.5 per cent in the garb of improvement in efficiency. Why not fix the norm at 80 per cent and give the benefit to the consumer by way of corresponding reduction in tariff.

This is not without precedent. In fact, in respect of gas based fertiliser plants under the administered pricing scheme, the capacity utilisation norm for price fixation in the case of ammonia plants was raised from 80 per cent to 90 per cent in 1988. This was in recognition of their ability to operate at higher rates than the plants based on naphtha/fuel oil.

Guaranteed super normal profits (allowed to be freely repatriated without any exchange risk) to the generator mean corresponding loss to the MSEB. And, this arises on two counts. First, the MSEB will not be able to realise, from the consumers, the rate it pays to the Dabhol. This is simply because there are a large number of consumers, such as in agriculture and households, who have to be supplied at subsidised rates. Consequently, even if the board charges exorbitant rates from the industrial users, it will not be able to realise, on a weighted average basis, a price that would fully cover its purchase price.

Second, to the extent the obligatory lifting of the entire electricity generated by Dabhol results in reduced generation/PLF of the board's own power plants, the latter's effective cost of generation will increase. This, in turn, will result in losses on the sale of electricity from its own plants.

Finances of the SEBs apart, have we cared to assess the impact of resultant high power tariffs on the viability of a host of industries? Already, the power rates are unbearable and electricity supplied from plants like Dabhol, would make matters worse. What will happen to the rate of inflation? What will happen to our cost competitiveness, particularly in the context of export promotion?

It has been argued, in some quarters, that some power, though at a high cost, is better than no power at all. But, what makes us believe that more power will come only when we agree to highly exploitative and discriminatory conditions? During the last four years, since power was thrown open to the MNCs, despite the offer of a virtual honeymoon to them, how much investment has come? Not even a single power plant! Clearly, what matters is not just what we offer, but, more importantly, how we act and what is our approach.

Till date, there is no clear-cut power policy. An investor has to assemble various pieces to arrive at his own interpretation. Most of the deals/negotiations are being conducted in a non-transparent fashion. Besides, as many as twenty clearances are required before any project can get the green signal. That means protracted delays, sometimes, even permanent blockades.

In January, 1995, the power ministry made competitive bidding mandatory for all fresh projects. Though belated, it was a good decision. It makes the process transparent and allows for the possibility of securing the best terms. There can be no compromise on this as any soft pedalling at the time of selection means perpetual loss. But, there is criticism that very few developers have come through this route. Without giving it a fair trial, we seem to be jumping to conclusions.