

# A template for power reform

CHANDRAJIT BANERJEE

**T**he power failures on two consecutive days is a telling commentary on the situation of the power sector in the country and drives home the point that the underlying issues behind the widening demand-supply gap for electricity need to be urgently addressed.

The problems in the power sector are multifarious, relating to fuel shortages, lack of adequate finance, poor financial health of distribution utilities, absence of cost-reflective tariffs and peaking power shortages. In addition, land acquisition, environmental clearances, and administrative delays too discourage investments.

Fuel availability has emerged as the most severe bottleneck for power generators. Although India is fortunate to have large coal reserves, coal production at 5 per cent growth has lagged power sector growth of 10-15 per cent in the last Five-Year Plan. For 2011-12 alone, the shortage is estimated at 100 million tonnes (mt). Also, for the 208 captive coal blocks allotted with a production potential of 657 mt per annum, the estimated annual production for the Eleventh Plan is only about 37 mt.

Resorting to imported coal is fraught with its own complexities as international prices have soared due to increased demand in India, and most power plants are in the interior, far from ports. Tariffs are based on domestic coal prices and there is little clarity on reimbursement to developers paying 70 per cent higher prices for imported coal. The availability of natural gas is equally uncertain, as it competes with sectors such as fertilisers and regasified LNG is thrice as expensive.

The shortage of coal and shortfall in the allocated gas from the Krishna-Godavari Basin has put a question mark on the future of many power projects with several thousand megawatts of power capacity lying stranded. For instance, approximately 50 per cent of the 35,000 Mw of coal-based power capacity which reached the commercial operation stage in the period between April 2009 and March 2012, is operating at 40-45 per cent utilisation. The situation is similar in the case of gas-based plants with about 7000 Mw of gas-based capacity lying idle.

Solutions to the fuel-supply issue would involve drastic coal-sector reforms, including opening it up for competition. The proposed Mines and Minerals (Development and Regulation) Bill also needs a rethink on several issues to expand coal mining. "Pooled pricing" of domestic and imported coal should be considered. The sale of coal through e-auctions must be permitted only after the demands of the power sector are met.

Second, financing is increasingly becoming constrained as banks are

reaching their power sector exposure limits. Funding gap in the Eleventh Plan alone was estimated at over ₹4 lakh crore. Foreign investors are deterred by the complexities of the power sector despite permission to invest 100 per cent. Pre-project procedural issues delay financial closure of projects. It is necessary to open new sources of funding such as permitting long-term financing from insurance companies, the raising of foreign currency loans by banks, and allowing banks to raise funds without attracting minimum reserve requirements such as SLR and CRR.

Third, the weak finances of distribution utilities and their poor efficiency record remains a challenge in the power sector. Accumulated losses of the utilities stood at close to ₹200,000 crore as of March 2012. State Electricity Boards are reluctant to raise tariffs and tend to cross-subsidise domestic and agricultural consumers by above-cost tariffs for industrial consumers. Combined with aggregate technical and commercial losses of about 28 per cent, about 40 per cent of power generated has little or no cost recovery, leading to unsustainable burden on paying consumers.

Again, the entry of private players in distribution would raise competition and reduce revenue leakage. Open

access for purchasing power from the open market must be promoted across all states. Automation and IT development is essential for the success of the R-APDRP (Re-structured Accelerated Power Development and Reform Programme) and greater

clarity on direction of reform such as distribution franchise vis-à-vis private monopoly is required urgently.

Fourth, the question of tariffs has to be revisited if the power sector is to be strengthened. Many states have not changed tariffs for five or six years, and a few for as much as a decade, for political expediency — while, on average, costs have risen by 8 per cent. State electricity regulatory commissions were to bring tariffs within 20 per cent of cost of supply by 2010-11, but most have not addressed the issue so far. This woeful scenario must be redressed through movement to full-cost recovery and a multi-year time-of-day tariff structure.

Finally, peaking power deficiency at the highest point of consumption hovers around 10-12 per cent and is expected to increase in the next few years. Independent peakers must be made attractive through peaking power tariffs that allow running on more expensive fuel. SEBs should be mandated to procure peaking power rather than resort to power cuts.

A holistic reform of the power sector with multi-sectoral approach has gained urgency. In the absence of this, India will continue to lag behind its inherent growth potential.

*The writer is director-general of CII*

**Shortages of coal and the shortfall in gas supply from the Krishna Godavari Basin has put a question mark over the future of many power projects**