Power sector needs holistic reform

CHANDRAJIT BANERJEE

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.

Solutions to fuel supply issue would involve drastic coal sector reforms, including opening it up for competition.

The Prime Minister's decision to look into the problems of the power sector is a timely and welcome step. In recent years, with demand outstripping supply, the woes of the sector are assuming crisis proportions. The inability to supply regular electricity to several hundred millions of people, and to industry, severely hobbles the country's aspirations for rapid and inclusive growth.

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

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 FY 2012 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.

An additional issue is that CIL signs five-year Fuel Supply Agreements while Power Purchase Agreements are for 25 years, thus placing generators at risk. CIL also guarantees only 50 per cent of coal linkages although developers need 80-85 per cent availability to recover capacity charges.

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 interiors, 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.

OPENING UP TO COMPETITION

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 needs to reconsider several issues to expand coal mining. 'Pooled pricing' of domestic and imported coal should be considered. Sale of coal through e-auction 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. The funding gap in the Eleventh Plan is estimated at over Rs 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 such as permitting long-term funds from insurance companies, raising of foreign currency loans by banks, and allowing banks to raise funds without attracting minimum reserve requirements such as SLR and CRR.

WEAK FINANCES

Third, the weak finances of distribution utilities and their poor efficiency record remains a challenge in the power sector. Accumulated losses have crossed Rs 70,000 crore and would go up to Rs 1,00,000 crore in the next two years. This is primarily due to the increasing gap between average cost of supply and average realisation per unit from Re 0.54 per unit in FY08 to Re 0.86 in FY10.

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 AT&C (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, 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 R-APDRP programme and greater clarity on direction of reform, such as distribution franchise vis-à-vis private monopoly, is required urgently.

TARIFF REVISION

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-six years, and a few for as much as a decade, for political expediency, while on an average, costs have risen by 8 per cent. State electricity regulatory commissions are to bring tariffs within 20 per cent of cost of supply by fiscal 2011, 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 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 such reform, India will continue to lag behind its inherent growth potential. Hopefully, the Committee of Secretaries will set the power sector on a new growth path.

(The author is Director General, CII. The views are personal)

blfeedback@thehindu.co.in