Power: The web of debt*

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The state of Jharkhand has reportedly stopped payments to the Damodar Valley Corporation (DVC) for the 700 MW of power the later supplies it every day. The evident reason is that it has not been able to cover payments for the power it acquires from the generators and supplies to its customers, resulting in deficits that are covered with debt that it is no longer able to service. A consequence of this would be an inability to purchase power from the generators, increasing their losses and affecting the debt they in turn owe the banks. With this debt being a significant share of the incremental advances of banks in the recent period, they too will have to be recapitalised by the state, based on its own borrowing, resulting in a peculiar web of debt.

This conundrum arises in a context where, as a result of the “reform” of the power sector, the three activities of generation, transmission and distribution that were undertaken by the state electricity boards (SEBs) were unbundled as a prelude to privatisation, which it was claimed would do away with unsustainable inefficiency, and high costs and losses in the power sector. In practice, the private sector was interested mainly in generation where price setting was liberalised to accommodate the interests of the debt-financed investment of major players. As of 2016, while state government owned generation capacity was around a third of the total, that in the private sector stood at 42 per cent of the total. Transmission remained with the states not least because of poor private interest, and distribution could be handed over to private players, particularly Reliance, only in Orissa and Delhi, where low-agricultural consumers were absent or unreached.

The consequence of this division of labour between the public and private sectors was that the payments due for acquisition of power by the distribution companies from the generation companies under power purchase agreements (PPAs) falls short of the net revenues generated from distribution. While transmission and distribution losses are part of the problem, such losses have fallen from 28 per cent to around 18 per cent of output since 2001. The principal issue is that the prices at which power is sold to different sections to make it affordable is far too low to cover unit costs in the form of prices paid to generators and costs incurred in transmission and distribution. This requires the state or central governments to cover the implicit subsidy with resources mobilised though taxes, which they have failed to do. The net result has been a pile up of debt that is transferred periodically to the government, and, in the case of Jharkhand, has resulted in default.

This is of significance because a little more than a year back, in an effort to wipe out the debt of around $4.3 lakh crore accumulated by the power distribution companies (discoms), the NDA government launched a new programme identified by the acronym UDAY, which stands for Ujwal Discom Assurance Yojana. Involving a tripartite agreement between the central power ministry, the state governments and the discoms, the scheme was aimed at relieving the distribution companies of the interest burden due on their accumulated debt, and creating an environment where they could restructure themselves to do away with losses and make their operations sustainable.

The central government scheme announced with much fanfare, had four principal components. It allowed state governments to exceed the borrowing limits set on them and issue bonds either in the market or to banks and financial institutions holding discom debt to mobilise resources to take over 75 per cent of that debt accumulated as on 30 September 2015. This was to be done in two phases over as many years: with 50 per cent of discom debt absorbed in 2015-16 and another 25 per cent in 2016-17. Since interest rates on these bonds were much lower than the 14-15 per cent applicable to discom debt, the burden on the states was less than what they would have carried if they chose to service the latter debt themselves. Second, discom debt not taken over by the state government was to be replaced by public sector banks with state guaranteed loans bearing an interest rate of not more than the bank's base rate plus 0.1%. Third, states were required to fund future losses of the discoms in a graded manner, starting from 5 per cent in 2017-18 and going on to 10, 25 and 50 per cent over the three years ending 2020-21, so that they did not quickly accumulate additional debt that was unsustainable. And, finally, through efficiency improvements and tariff adjustments to cover reasonable costs, the discoms were to reduce and do away with losses, so that their dependence on debt and state bail-outs were reduced.

The beneficiaries of the restructuring were not just the distribution companies and the states. It included the power generation companies, the ownership of many of which had at the margin shifted in favour of the private sector either through their own investments or through public-private partnership projects. These projects were given relative freedom (subject to ceilings set by newly established regulatory authorities) to price their power to cover costs and provide for a margin, and were mandated to enter into power purchase agreements (PPAs) with the distribution companies, which required the latter to lift a specified quantum of power at a pre-specified price. So long as the discoms entered into these agreements and paid their dues the power generation companies were in the black and could service the loans they had obtained from the commercial banks (largely public and occasionally private) that had been encouraged to finance a part of their investments.

The whole scheme was based on one important premise: that the power distribution companies, or the State Electricity Boards, would become profitable in the course of a year or two, through improved efficiencies in transmission and distribution realised through modernisation, reduced leakages and theft and adjusted tariffs. That assumption has been belied, not least because power distribution companies have not been able to significantly raise the tariffs they impose on their clients, particularly households and agricultural consumers. Since, on the other hand they have had to pay high prices to the generation companies, who are now independent providers, losses were inevitable. The ambition of UDAY remains unrealised.

Jharkhand is only one example. The success of UDAY is measured using 14 operational and financial parameters, including reduction in technical and commercial losses, reduction in gap between per unit cost of power supply and revenue, household electrification, smart metering, and the distribution of LED lights, besides profit and loss. In October last year the Economic Times reported that, “Haryana, Gujarat, Bihar, Punjab and Rajasthan have fulfilled (only) 30-45 per cent of the commitments made under UDAY… Uttar Pradesh, Bihar, and Jharkhand need (ed) improvement with below 30 per cent progress.” And Jammu & Kashmir lagged far behind with a score of just 15%.

The net result is that distribution companies began reporting losses. The problem is not really the inefficiency of the public sector SEBs, as illustrated by the experience in the two states (Orissa and Delhi) where distribution has been privatised. In Orissa, the Electricity Regulatory Commission faced with failure of the three distribution companies owned by Anil Ambani's Reliance to meet agreed commitments and their refusal to comply with orders, chose to cancel their licences. And in Delhi, once again the Anil Ambani-controlled BSES Rajdhani Power Limited (BRPL) and BSES Yamuna Power Limited and the Tata-owned New Delhi Power Limited, all PPP projects with a 49 per cent state stake, have been found to have indulged in financial irregularities to the tune of Rs. 8,000 crore. They inflated power purchase costs and underreported revenues and overcharged consumers. In the process, they have been able to survive, but at the expense of their clients.

The SEBs that have not been able to do this, have notched up losses and debt resulting in a situation where they are unable to buy as much power as is available from the generation companies. With new PPAs not being signed, utilisation has fallen, and according to reports as much as 25,000 MW of capacity is now lying idle. That affects the profits of the generation companies and their ability to service their debt to the banks, which have accumulated large volumes of non-performing assets. Clearing that would increase the debt of the central government, which sought to transfer the debt of the SEBs onto the state governments. That seems to be closing a peculiar circle of debt.

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