Expecting an Upswing

Financiers' views

As the conventional power segment continues facing fuel supply and execution-related challenges, financiers are betting on renewable energy. Favourable government policies, regulatory support, and shorter gestation periods of projects are likely to drive investments in the renewables segment over the next few years. The conventional power segment, meanwhile, is expected to witness merger and acquisition deals as debt-ridden companies sell their assets. *Power Line* invited the industry's financial experts to share their views on the sector's accomplishments and the future investment outlook...

What were the sector's most significant achievements in the past one year?

Aditya Aggarwal

Integration of the NEW grid with the southern grid: Transmission and distribution remain the sector's biggest pain points. As much as 30-35 per cent of the power generated in India is lost during transmission and distribution. The recent power crisis in Uttar Pradesh and Delhi, and the recent power tripping in South Mumbai bear testimony to India's dilapidated transmission infrastructure.

A lot of thermal power plants in Chhattisgarh, Jharkhand and Odisha have been forced to sell power in the short-term market of late, on account of the unavailability of transmission corridors to evacuate power to the southern states. The interconnection of the southern grid with the northern grid, with the commissioning of the Raichur-Sholapur line, was an important feat in this context. The integration will help balance out demand and supply, and help transfer power from the eastern and western regional grids to the southern region during periods of peak demand.

Capacity addition: A significant number of power plants planned in the Eleventh Plan have been commissioned in the past 12 to 18 months. Over 12,500 MW of capacity was commissioned in 2013-14, of which about two-thirds was contributed by the private sector. However, this capacity addition has come through after a fair share of execution challenges, including delays in land acquisition and cost overruns. A lot of these plants continue to face teething troubles, such as challenges related to fuel availability and fuel logistics, corridor unavailability, and plant-specific technical issues.

Capacity addition in the renewable energy sector is continuing, but at a slower pace. In 2013-14, 3.6 GW of grid-connected renewable energy capacity was added. Interestingly, the solar sector contributed 26 per cent of the renewable capacity addition. Going forward, the solar sector's share in the renewable energy mix could increase further, driven by lower capital costs and faster execution time.

Wind energy capacity addition had taken a beating briefly due to the discontinuation of accelerated depreciation (AD) benefits and lack of clarity on generation-based incentives (GBIs). The reintroduction of the AD benefits and the GBI scheme would certainly help restore some of the lost momentum of wind capacity addition.

Consolidation and mergers and acquisition activity: Debt-laden infrastructure companies have been trying to sell assets and deleverage for some time. The sector has seen some consolidation, with the Adani Group's acquisition of Lanco Udupi and Reliance agreeing to buy Jaiprakash Hydropower Limited's hydropower assets. Strategic foreign players have also shown interest, as is evidenced by GDF's and Sembcorp's acquisitions. Many more operational or near-operational power plants are also likely to be put up for sale.

Aditya Aggarwal
Partner,
IDFC Alternatives

D.R. Dogra
Managing Director and
Chief Executive Officer,
CARE Ratings

Andrew Jeffries
Energy Head (India),
South Asia Regional
Department,
Asian Development Bank

D.R. Dogra

In the past one year or so, the Indian government and other stakeholders have announced various measures to improve the fundamentals of the domestic power sector. These include:

- Formation of the CCI to enable greenfield infrastructure projects to secure various clearances on time.

- Introduction of the financial restructuring plan (FRP) to improve the commercial viability and liquidity profile of distribution entities.
- Formation of a model fuel supply agreement (FSA) and signing of a firm FSA by Coal India Limited (CIL) for projects to be commissioned before March 2015.
- Compensatory tariffs for competitively bid imported coal-based projects and a price pooling mechanism to dilute the impact of the high price of imported fuel.

Though there has been some progress by way of the announcement of these measures, the actual implementation of many of them is still pending. The sector continues to face challenges; however, the biggest achievements in the past one year have been the execution of firm FSAs by CIL and the relative improvement in the liquidity profile of distribution entities in key states due to the implementation of the FRP.

Andrew Jeffries

Some notable achievements were:

- Adding over 22 GW of new capacity in the generation segment over the past year.
- On the transmission front, the synchronous connection of the southern region to the central grid (via the 765 kV Raichur-Sholapur transmission line) under the national integration scheme.
- In October 2013, the first international grid integration between India and Bangladesh (for which the Asian Development Bank [ADB] provided funding to the Bangladesh government) is a first step towards a more integrated South Asian power grid.
- In the distribution segment, the discom restructuring scheme was important for recognising and addressing the distressed financial position of some of the state utilities, although the successful resolution of this matter will not happen overnight as it is a multifaceted challenge.

Do you see a qualitative improvement in the sector's outlook, in light of the steps taken by the new government?

"Poor financial health of state utilities, fuel supply issues, evacuation constraints, faulty bidding frameworks and execution challenges have brought the investment cycle in the conventional power sector to a grinding halt."

Aditya Aggarwal

Aditya Aggarwal

The decision to integrate the three ministries of coal, power and non-conventional energy will hopefully ensure coordinated decision-making and faster implementation of projects. It is still too early to judge the impact of the steps that have been taken. However, the government has made announcements in the right direction, specifically in the areas of:

- Environmental clearance process: Fast-tracking the environmental clearance process will not only help new power projects but, more importantly, it will also help kick-start production from CIL's mines, which is stuck for want of environmental and forest clearances.
- Boosting domestic coal supplies: The government has made announcements about augmenting CIL's production and rationalising coal linkages. The government has also prioritised coal supply to more efficient supercritical power plants over that to older, inefficient power plants.
- Initiatives on infrastructure financing: The Union Budget 2014-15 made a slew of announcements regarding financing. The proposed 5:25 structure will allow banks to loan money to developers for 25 years, with the option of resetting or transferring the loan to another bank or financial institution after five years. The exemption of long-term bonds from statutory liquidity requirement and cash reserve ratio requirements will ease the process for banks to deploy lower-cost capital to finance infrastructure. The introduction of infrastructure investment trusts will help developers churn their equity from operational assets. While some of these measures will help the power sector in the short to medium term, the issue of fuel supply needs to be addressed holistically.
- Private sector participation in mining: It is no secret that production from CIL has not kept up with demand. CIL's output has been woefully inadequate to meet the fuel demands of the country. While imported coal prices have softened recently, the economics for plants that are in the hinterland does not work out, due to the high associated logistics costs. A longer-term sustainable solution would entail the private sector having a greater role in coal mining.
- Pooling of imported coal: Given that CIL alone cannot meet the country's coal requirements, it is imperative to implement a pooled price for coal and to amend power purchase agreements for allowing pass-through in the price of coal.
- Stranded gas power plants: More than 20,000 MW of gas capacity is stranded for want of gas. A gas price pooling mechanism needs to be formulated, which will provide succour to these stranded assets. Also, immediate clarity on gas pricing is essential in order to incentivise the production and exploration of gas by private sector players.

"The new government's decision to put power, coal, and new and renewable energy under one minister will allow better exploration of integrated solutions across the three interrelated segments."

Andrew Jeffries