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"The Hamlet Syndrome in Infrastructure" (S L Rao)

In recent months, the Appellate Tribunal for Electricity and the Central Electricity Regulatory Commission have begun to undo the damage done to the electricity sector over the years by central and state governments. All infrastructures are in the nature of public goods. The attempt must be to make them available, accessible and affordable to all. They have developed largely with government funds, and the framework is of dominant government ownership, control and management. As a result they are subject to political (populist) influences.

With escalating demand governments do not have the resources to invest as needed. Public-private partnership contracts have come into vogue. Contracts and their execution often witness clash between politics and economics, resulting in delays, lockup of funds, and possibly infructuous investments. Delays on any account hinder economic growth and peoples' well-being. Since at most 20% of investments are as equity, the balance 80% is debt. The danger of default with such large sums as are involved in infrastructure investments could seriously hurt the economy.

To ensure fairness and transparency the contracts are bid and awarded competitively. Since lenders want confidence that the output will be sold at a price that enables their loans to be repaid, the debt funds require forecasts for the life of the project. For this purpose, the tariff bids are for the life of the project, between 25 and 30 years. The contract provides for escalation in the bid if one or more specified elements of cost change over the period. However, the contract period involved is long and not all contingencies are foreseen in the contract. When they occur they make the whole project unviable. The bidder wants a renegotiation and the buyer is against it. These disagreements result in projects getting much delayed, even stranded, a growing occurrence in indie as it has been In Latin America.

.. Indeed, central and state governments have been responsible for its present dismal state, further aggravated by the venality and incompetence in the central government's handling of related areas. Coal, oil and gas, imported and domestic have been bottlenecks leading to stranded capacities and vast investments in power becoming unproductive. Lack of clear policies and speedy clearances-of land acquisition, environment and forests-and many administrative hurdles, have resulted in delays and locking up of funds. Large fluctuations in the exchange value of the Rupee, higher interest rates, unforeseen rises in fuel prices, have led to higher fixed and variable costs of power projects. With tariffs being fixed within a levelised framework for 25 years, the negative impact on project balance sheets, has been devastating.

It is these uncertainties and their consequent effects on costs that have led to some of the largest power projects in the world wither not being completed or causing huge losses to the promoters. Imported coal and the unilateral increase in prices promulgated by the Indonesian government, the sudden rise in domestic coal prices by Coal India, delays in land acquisition and various clearances by governemtn departments, rises in interest rates, the dharp decline in the foreign exchange value of the Rupee resulting in substantial increases in Rupee costs of external borrowing and of imported equioment, have played havoc with the plans of TATA in Mundra, Reliance Power in Krishnapattnam, Adani in Mundra, GMR, and others.

The recent CERC order on a petition by Adani has agreed that many of these unforeseen events and costs have made the project unviable. It therefore has appointed a committee to review the project, the impact of these events on costs, and recommend a solution. CERC had the option to declare that these higher costs could not be foreseen and were a non-naytural economic force majeure that must be compensated. That would have been within the purview of the contract and the Electricity Act, 2003. CERC has instead taken powers under its tariff determination powers. This could lead to long liigation.

The objective must be to prevent stranded capacities. infructuous investments, and increase the supply of power. A suggestion that the project developer who has invested in Indonesian coal mines must share the extra profits from higher coal prices to lower the additional cost of coal to the Indian project appears an unjust proposal. Government delays in giving various clearances must be charged to government. Coal India must enter into firm contracts on prices or build escalation clauses. Variations in Rupee values in foreign exchange, like interest rates, are a business risk that the promoter must bear. It might have been prudent to provide for escalations in the contract.

What is clear is that the present contracts for power are difficult to implement. A levellised tariff for 25 or 30 years, for a project in which Rs 20000 crores or more has been invested, cannot ever forecast the changes that might take place and affect future costs. If banks require guaranteed offtakes, the agreement with buyers must be for the [eriod of the loan, usually 15 years, and not more. If it has to be more there msut the well-thought out terms for renegotiation. The idea of tariff based competitive bidding is attractive. However, when bidders are aggressive in bdding, they create the problems now being experienced. The contractor must therefore have a floor price below which a bid will not be considered. This will at least ensure that some bids we have seen (for example, Secunderabad metro), especially for roads and metros, do not get considered even though tariffs are low.

In conclusion we myst note that the present problems have come about because we are trying to fit private parties into government frameworks. These give governemtn the control over the tariff, the major material costs, and allow them to influence costs by delayed permissions. Instead, the role of government must be reduced. Items like (domestic and imported) coal, gas, etc, must have their prices determined on the Exchange, and not by government agencies. If the end product (power, tolls on roads, metro fares, etc), have to be made affordable to socially wek groups, that must be done independently by the government. It must not beincluded in the project revenues.

In the absence of government recusing itself from these matters, the Regulators are taking over. Until they come to decisions, we losr many

years and crores of Rupees invested in building capacities that are not producing. (1065)