

Analyses & Comments by BR Research

### **Power tariffs to go considerably higher**

The Central Power Purchasing Agency (CPPA) has submitted its Power Purchase Price Forecast report for FY20. Of the multiple scenarios used to come up with forecasted demand and price projections, the CPPA has recommended the actual demand based projections to be considered as basis, for Nepra's approval, the hearing of which is scheduled for September 25, 2019. Recall that notifying revised power tariffs for FY20 by September end, is one of the IMF structural benchmarks.

The CPPA's forecasted power demand for FY20, based on actual energy demand for previous five years, is the one the Agency considers to be the closest to reality. Based on the scenario, electricity demand in FY20 is projected at 132.2 billion units, which is around 8 percent higher than the previous year, and does seem a fair reflection of ground realities.

From what It appears that the electricity is going to be priced significantly higher in the next tariff announcement for FY20, as the Power Purchase Price (PPP) for FY20 is slated to go to at least Rs12.1 per unit. This is Rs2/unit or 20 percent higher from the previous PPP of Rs10.02 per unit. Assuming all other variables constant, expect the consumer tariffs to go higher by the same magnitude. Given the government's policy to absolve the bulk of domestic consumers using up to 300 units from price hike, the burden could invariably fall on other consumer categories, to the tune of 30 percent. The allocated subsidy in the budget does not cover for more than Rs1.2 per unit as subsidy, which means the government will have no option but to pass on the hike to other sectors.

Bear in mind these numbers are based on actual demand, and not the units sold. When accounted for 15 percent allowable transmission and distribution losses, the PPP goes up to Rs14.63 per unit. Add the distribution margin, approximately at around Rs1.5/unit, and the total cost of electricity would be around Rs16/unit. A subsidy of Rs1.5 per unit, would still mean, the tariffs go up significantly.

It is to note that the CPPA has used rather lenient assumptions, with a high upside risk. The rupee dollar parity has been assumed at 150 for FY20, which seems to be on the lower side, by at least 7-8 percent, if not more. And this has a direct bearing on the PPP, especially the capacity payment component of the equation, which has the lion's share in the PPP at Rs6.67/unit. The CPP is estimated at Rs907 billion, but could well go beyond Rs1000 billion, should the dollar move unfavorably from the base case assumption of 150.

Secondly, the energy price component of the PPP also seems to be carrying an upside risk, as the price for gas is assumed at Rs729 per mmbtu. This seems rather absurd, as the last price revision had already taken the gas price for power consumers to Rs824/mmbtu. With a sizeable share of 16.4 percent in the generation mix for FY20 – an 11 percent deviation from actual price could also result in fuel price adjustments, on the higher side, every month.

Whichever lens you use, power is going to get pricier. And if you are thinking that FY20 may just be one tough year, and things will get better from thereon, you are in for a major disappointment. The CPPA report shows the PPP going higher and higher, from FY20 till FY25, despite a sizeable reduction in energy price component. The real deal is the capacity price component, which is slated to go to as high as Rs8.29 per unit by FY25. Say thanks to the lopsided take or pay contracts added in the not-so-distant past. Energy availability it is then. Affordability can wait (at least another five years)!