Distribution Utility Financial Restructuring - Is it just postponing the crisis?

T&D Conclave 2012
## Agenda

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Section 1

Status of the Crisis
Background

- Even after reforms in electricity sector in the past (beginning 2001), the SEBs failed to function on sound commercial principles;
- Discoms borrowed heavily for system strengthening & managing growing loads leading to financial burden as revenues didn’t increase proportionately;
- SERCs, which were formed to bring autonomy in tariff-setting, could not be completely de-politicised and tariffs were not cost-reflective;
- Further, to meet increasing revenue deficits due to rising fuel/ power purchase costs & tariff constraints by SERCs, the discoms borrowed heavily – leading to problem of debt entrapment;
- Deteriorating health of discoms impacted the growth of overall sector:
  - Commissioning of new generation capacity was impacted as discoms didn’t have enough resources to procure incremental power;
  - Investments in T&D went down – leading to increase in T&D losses;
  - Debt servicing was impacted, having major impact on financial sector – possibility of huge NPAs in financial sector
**Snapshot of power sector crisis**

- Total losses of SEBs/discoms in FY 11 ≈ Rs 62k crore (without subsidy); & Rs 42k crore (on subsidy recd. basis);
- All-India gap between ACS & ARR (average revenue without subsidy) in FY 11 ≈ 0.68 Rs/kwh ;
- Average AT&C Losses for FY 11 ≈ 26%; however several states have AT&C loss > 40%

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**Financial Loss (in Rs Crore)**
- Loss abv 3k Cr
- Loss btw 1k – 3k Cr
- Loss btw 0 – 1k Cr
- Profitable states

**Gap btw ACS & ARR (in Rs/kWh)**
- Gap abv 1 Rs/kWh
- Gap btw 0.5 – 1 Rs/kWh
- Gap btw 0 – 0.5 Rs/kWh
- Surplus states

**AT&C Loss (in %)**
- 40% & above
- 30 – 40%
- 20 – 30%
- Less than 20%
• Networth of the discoms have deteriorated:
  - Rajasthan, Uttar Pradesh, Andhra Pradesh, Haryana and Madhya Pradesh have a deteriorating networth.
  - Punjab & Tamil Nadu show improvement in networth as a result of equity infusion and transfer of relatively clean balance sheets to successor utilities on unbundling of PSEB and TNEB.

Section 1 – Status of the Crisis

Impact on Discoms

Networth (in Rs Crore)

Source: PFC Performance Report for State Power utilities - FY 2008-09 to FY 2010-11
Impact on Discoms

- Due to rising revenue deficits, investments have declined; while borrowings from banks/FIs/ market sources have increased rapidly:
  - Discoms in Rajasthan, AP, MP & Haryana are worst hit - as investments are dipping; borrowings continue to rise, having negative impact on health of discoms;
  - Tamil Nadu and Punjab present an increase in investments due to equity infusion at time of unbundling;
  - Increasing borrowings at higher interest rates, further add to the crisis in power sector.
Impact on lenders (banks/FIs/Bonds/others)

- The Banking sector’s short term exposure to Discoms is estimated at Rs. 1.5 -1.7 trillion as on 31st March 2012;
- It represents 3-3.6% of Banking credit and 45-52% of total power credit;
- Large part of these loans is taken to fund cash losses of Discoms;
- Any slippage on part of the discoms to repay these loans would create a huge NPA for the banking sector.

![Exposure of Short Term lenders as on 31.03.2010](image1)

![Exposure of Long Term lenders as on 31.03.2010](image2)

Section 2
Contours of the Central Financial Restructuring package
**Salient features**

- Scheme envisages turnaround of sector within next 3 years;
- State Govt would takeover 50% of O/s STL (incl. payables for power purchase) as on 31 March 2012 during next 2-5 years & provide support for interest & principal repayment for taken-over liability;
- Taken-over STL would be converted into bonds backed with government guarantee, moratorium of 3-5 years & repayment in 10 years;
- Balance 50% would be restructured into long term loans by lenders with moratorium on principal repayments upto 3 years, lenient repayment terms & waiver of penal interest;
- Central Govt. would provide additional support through TFM:
  - *Matching grant on accelerated reduction in AT&C loss targets in case gap between ARR & ACS is reduced by more than 25% within first 3 years*;
  - *Reimbursement support of 25% of principal repayment in case state govt. takes over entire 50% of O/s STL*;
- Lenders to finance operational losses & interest for first 3 years on a diminishing scale & remaining to be financed by State Govt.
Outline of the FRP scheme

Utilities
(Short term debts-1.9 Lakhs Cr)

State government
(50% loans)

Discoms to issue bonds with state Gov guarantee

Capital reimbursement support for state Gov taking 50% ST liabilities

Grant on AT&C loss reduction-metering, PPP, etc

Regulatory assets liquidation

Tariff rationalisation

3 yr moratorium on principle

Lenient repayment terms and removal of penal interest

Finance operational losses at diminishing scale for next 3 yrs

Lenders
(50 % loans)

Debt restructuring

State government (50% loans)

Lenders (50 % loans)

Utilities
(Short term debts-1.9 Lakhs Cr)

State government (50% loans)

Lenders (50 % loans)

Utilities
(Short term debts-1.9 Lakhs Cr)

State government (50% loans)

Lenders (50 % loans)
## Roles & responsibilities

### State Govt
- Takeover of 50% of O/s STL & provide support in interest & principal repayment;
- Finance remaining operational losses for next 3 years;
- Clear all O/s dues from Govt. deptt. before 30.11.12;
- Arrears of subsidy to be paid off & future subsidies to be paid upfront;
- Pre-paid meters be installed in all Govt. deptt.
- Form SLMC for monitoring progress at state level & submit reports to CLMC

### Discoms
- Get the FRP in-principally approved by SERC & lenders;
- Ensure 100% consumer metering;
- Reduce AT&C losses;
- Accounts for FY 11 to be audited by 30.11.12 & for FY 12 by 31.01.13;
- Tariff petition should be filed on time;
- Prepare plan for increasing private participation in distribution segment

### SERC
- Issue Tariff Order for FY 13 before FRP approval;
- Tariff Order for next FY to be issued by 30.4.13; while tariffs should be applicable from 1.4.13;
- Ensure recovery of legitimate costs of discoms including recovery of power purchase & fuel adjustment through FSA;
- Must plan to liquidate Reg. Assets within a period of 3 years
- Gradually reduce cross subsidy

### Central Govt
- Provide additional support through TFM to reduce burden on State Govt;
- Ensure necessary clearances are made from RBI, DFS for smooth implementation of scheme;
- Monitor progress of the scheme to ensure targets are met

### Lenders
- Restructure 50% of O/s STL into long-term loans for providing liquidity support;
- Finance operational losses for next 3 years in diminishing scale;
- Waive off penal interest (if any);
- Provide in-principle approval to the FRP prepared by the Discoms;
**Scheme milestones**

<table>
<thead>
<tr>
<th>31 March 2012</th>
<th>31 December 2012</th>
<th>2015</th>
<th>2017</th>
<th>2022</th>
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<tr>
<td>One-time take over by State Government of 50% of outstanding STL including payables for power purchase as on this date.</td>
<td>Validity of the scheme closes on this date.</td>
<td>Moratorium period of 3 years starting 2012 ends in 2015.</td>
<td>The takeover of the liability by the State Government from Discoms gets completed by issuance of special securities in the first 5 years; a</td>
<td>The balance 50% of the loans would have been restructured.</td>
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<tr>
<td>Discoms to convert these into Govt backed bonds for issue.</td>
<td>Discoms can send in their participation till this date.</td>
<td>Discoms do not have to repay any principal amount on their loans till this year.</td>
<td>Repayment &amp; interest payment to be made by State Government till the date of takeover.</td>
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PwC
Section 3

Diagnosis of FRP Scheme 2012
## Impact on Stakeholders - Success

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<th>Short-term</th>
<th>Medium-term</th>
<th>Long-term</th>
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<td><strong>State Govt</strong></td>
<td>Increase in fiscal deficit – outstanding payments to discoms &amp; new interest liabilities</td>
<td>Principal Repayments</td>
<td>Reduce burden due to discom turnaround</td>
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<td><strong>Central Govt</strong></td>
<td>Matching grant for accelerated AT&amp;C loss reduction to discoms</td>
<td>Reimbursement Support on principal repayments</td>
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<td><strong>Discoms</strong></td>
<td>Increase in liquidity - Reduction in acc. Losses, interest payments &amp; repayment moratorium</td>
<td>Repayments of restructured loans</td>
<td>Achieve Financial turnaround</td>
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<td><strong>Lenders</strong></td>
<td>Forego immediate cash inflow through restructure of loans</td>
<td>Finance of operational losses for next 3 years</td>
<td>Improvement in liquidity – recovery from Discoms; avoid NPAs</td>
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## Impact on Stakeholders – Failure

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<td>Increased burden due to increasing operational losses</td>
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<td><strong>Central Govt</strong></td>
<td>Matching grant for accelerated AT&amp;C loss reduction to discoms</td>
<td>Reimbursement Support on principal repayments</td>
<td><strong>Additional support?</strong></td>
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<tr>
<td><strong>Discoms</strong></td>
<td>Increase in liquidity - Reduction in acc. Losses, interest payments &amp; repayment moratorium</td>
<td>Repayments of restructured loans</td>
<td>Increase in borrowings for financing deficit</td>
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<tr>
<td><strong>Lenders</strong></td>
<td>Forego immediate cash inflow through restructure of loans</td>
<td>Finance of operational losses for next 3 years</td>
<td>Danger of NPAs &amp; liquidity crunch</td>
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Is it similar to the 2001 structuring?

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<th>Similarity/Negatives</th>
<th>Differences/Positives</th>
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<tr>
<td>The targets have been set but there is no penal mechanism to reprimand the outlier discoms. No strong emphasis on the monitoring of the reform process.</td>
<td>The new FRP scheme comes with riders — annual rationalisation of rates, reducing aggregate technical and commercial losses, timely release of subsidy by state governments, regular metering of supply and bringing private participation in distribution.</td>
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<td>No emphasis on the training and development of the manpower has been proposed. Developing the sense of belonging towards the discom is necessary for every employee to contribute towards loss reduction and performance improvement.</td>
<td>Responsibility for the discoms’ CEOs and various govt. offices has been set.</td>
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If such basic requirements are not met with, we are simply postponing the inevitable through redoing financial restructuring after a decade. This all with lead the discoms to a situation worse than they were in 2001, when the earlier restructuring was done.
The road ahead

It is very important that the discoms meet the targets set for them in the FRP. Some of the key drivers which can contribute to the success of the scheme are:

• Requirement of political will: Unless the state govts. clean up their debt to the state discoms and release subsidy on time, the realisation of the targets will be difficult for the discoms. The govt should allow the discoms to take stern action against defaulters/electricity thieves.

• Focus on training of the discom employees to evolve a sense of belonging towards the discom in order to improve their performance.

• The regulatory commissions should allow all justified cost to the discoms and ensure that the gap between ACS and ARR is met.

• A monitoring committee be formed in each discom comprising of representatives from the entire hierarchy to look after the monthly progress and raise alarms whenever a deviation is observed.
Thank You