Discoms on the cusp of transformation

Opening up power distribution to competition will not only enhance efficiencies but also give consumers more choice

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The Ministry of Power's initiative to privatise power distribution companies in Union Territories (UTs) and a further announcement by the Finance Minister in the Budget on the distribution sector are welcome steps for strengthening the weakest link of power sector value chain. The following two major initiatives will have far-reaching implications on Discoms.

First, the announcement of tabling of the Electricity (Amendment) Bill 2021 in this Budget session. Once approved, this amendment will have a transformative impact by removing monopoly in the distribution sector — for example, de-licensing of the distribution business and providing customers with more choices to select power supplier.

There would be many power suppliers or distribution companies in one licensed area, including existing ones which will own network and charge wheeling costs to the new distribution companies as State Regulatory Commissions register them. The incumbent Discom will also share existing long term power purchase agreement (PPAs) with new entrants.

It would be interesting to see how new business models evolve, considering current high commercial loss levels and unreliable network that does not guarantee a 24x7 power supply. This model is presently working in European countries wherein losses are limited to technical losses, and the network is highly reliable with enough redundancy in the system.

Additionally, consumers have smart meters to facilitate quick switch-over from one distribution company to another. New entrants are likely as distribution companies strive for customer acquisitions by clubbing various other services to create value for consumers. It will not be surprising to have companies having more in-depth customer insight from other domains like telecom, gas or even transportation to join race for distribution services.

Innovative solutions

The incoming distribution companies are likely to offer innovative solutions and financing options for services like rooftop solar, battery storage and demand response management using time-of-day metering to attract new customers. These solutions will lead to reduction of customers' monthly bills. These acquisition strategies will also lead to the diversion of customers from incumbent distribution licensee to new ones.

While on one side, new distribution companies will ask for more reliable power from the existing Discom, on the other, State Discoms, due to their operational inefficiency and high loss level may sink deeper into the red. As a result of the higher autonomy provided to the Regulatory Commissions under the new Electricity (Amendment) Bill, regulators will not allow an increase in wheeling charges due to inefficient operational performance by the incumbent licensee.

In the offing More power to consumers

Second, a bailout package of ₹3 lakh crore is planned in the Budget for ensuring Discoms improve their operational efficiency. It is essential to use this package to incentivise State governments to privatise existing distribution licence business which has failed to bring down their AT&C (aggregate technical and commercial) losses and improve customer service delivery despite many bailout packages offered by the government since the Accelerated Power Development Programme in 2001.

The privatisation of Discoms has not gained much ground due to political unacceptability in the last few decades. While private players bring efficiency into the system, their investment to improve system reliability and higher operating expenses (opex) in the initial period lead to an increase in tariff and is not politically acceptable.

However, a closer look at the present scenario indicates that this is the best time to privatise utilities while ensuring that tariff does not increase for the next decades. Consumer tariff consists of two components — power purchase cost, which is 75-80 per cent, and distribution cost (about ₹1.5-2), which comprises capex financing, employee and maintenance costs.

Historically, most Discoms have entered in long-term PPAs that will expire over the next five years and get replaced with renewal power and purchase from the open market. Thanks to surplus generation in the country, the power prices are expected to remain lower than existing long-term power agreement prices, and the average portfolio cost of Discoms will come down. This will help in tariff reduction to the end-customer.

In the last decade, a fair amount of funding has been extended from the Centre to State governments through various schemes, and every household is connected to the primary system. An essential requirement is ensuring reliability and continuity of supply through proper maintenance, better governance, and having management systems in place. This will lead to growth in consumption, reduction in opex, and lower distribution cost per unit, thereby push retail tariff downward.

Another factor favouring reduction in tariff is a commitment to loss reduction by the private entities. The same should be taken care of in the transfer scheme, wherein gain due to over-achievement is shared in a specific ratio. The proposed bailout package should now enable the State government to take a bold step towards privatisation and ensure the neutralisation of any unwarranted upswing in tariff hike for the first five years after privatising.

In light of the proposed Electricity (Amendment) Bill, it is an opportune time for States to think innovatively and take steps to merge intra-State transmission with the distribution network in licenced areas and monetise the same.

Creation of competition in the proposed Bill will enforce distribution companies to bring new technologies and customer-centricity to optimise operations.

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