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Question over sharing spare power cost resurfaces

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THE question of how independent power producers (IPPs) should share the cost of maintaining the country's spare capacity has surfaced again as excess capacity is expected to increase dramatically in the next two years.

Currently, Tenaga Nasional Bhd bears the entire cost of maintaining spare capacity that could account for as much as half the country's installed capacity in 2004.

This is made worse by the fact that demand for electricity is slowing and it may crimp earnings of the national power company.

In contrast, IPPs are protected from the vagaries of demand thanks to favourable power purchase contracts that assure them stable returns over the agreement period.

"Tenaga is currently stuck with burdensome contracts that provide no comfort when demand for electricity is lower.

"For IPPs to share the risk of reserve margins in a meaningful way is to be exposed to lower revenue when demand is lower," said an analyst of a foreign research outfit.

Power purchase agreements (PPAs) stipulate how much Tenaga will pay for per kilowatt-hour of electricity to IPPs over a fixed-time period. The price comprises capacity payments that take into account the plant's development cost as well as returns that will be made by an IPP.

Capacity payments make up two-thirds of the price and the rest is energy payments or what Tenaga actually pays for the amount of power it buys. A major feature of a contract is that an IPP must maintain a certain availability rate, where it has to ensure that about 80 per cent of the plant's capacity is always ready to be despatched to Tenaga.

Because of the PPAs' structure, IPPs are insulated from fluctuations in demand and need only to focus on cost efficiency to improve profit margins. Tenaga, on the converse, is fully exposed to operational as well as demand risks.

Demand for electricity this year is not expected to grow as much as 14 per cent achieved last year, as the economy slows down in tandem with the slowing global economic growth.

Tenaga is also likely to lower its demand growth forecast for next year as the economy is projected to grow by 5 per cent compared to an earlier prediction of 6 per cent.

Back in July, Prime Minister Datuk Seri Dr Mahathir Mohamad called on IPPs to share the burden of maintaining costs of spare capacity, suggesting they lower the price of power that is sold to Tenaga. Although PPA prices subsequently declined, they do not really address how IPPs can help share the costs of spare capacity in times of slowing demand.

"Going forward IPPs cannot expect to get high capacity payments. Rather than have a guaranteed amount of payment, capacity payments could probably be lowered and possibly introduce an element of fluctuation where a stronger demand results in higher revenue and vice versa," the analyst added.

Of course, this is easier said than done.

Currently, IPPs can sell power only to Tenaga. If, for example, Tenaga agrees to pay an IPP to ensure only a 60 per cent availability rate, it needs to offset the lower revenue by selling the remaining capacity.

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