

No, we don't need IPPs

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Tiger is doubtful whether open tenders are the best way out for future independent power producers or IPPs. He would like to question the very concept of IPPs instead. Do we really need IPPs and are they the way to keep power prices competitive? No, on both counts says Tiger. Read to find out why.

In one of its many snoozes after large meals, a bolt of inspiration came to Tiger. Is it really necessary to have independent power stations (IPPs) in the first place? Would it not be possible to have open tenders without IPPs? Why give a middleman IPP the right to mint money at our expense?

Let's look at and revisit this concept of IPPs which came into play when YTL Power was awarded the first one back in the 1990s, in the wake of utility Tenaga Nasional Bhd's (TNB) nationwide blackout. This set the stage for a new, but unnecessary, industry.

And let's examine in broad terms what this entailed to see if it could have been structured differently. Basically, the deal gave YTL Power the right to sell power directly to TNB at a certain rate which has not been fully disclosed. If TNB did not want the power it pays a capacity charge.

(Oh, by the way, since then YTL Power never got any contract for power in Malaysia until recently but has got itself into a bit of a pickle when its managing director Francis Yeoh said he would like to see the disappearance of cronyism in Malaysia. Read about it here.

This resulted in a backlash against YTL Power, which had just received a directly negotiated bid for a 1,100-1400 MW plant estimated to cost RM6 billion. Its two partners were to be TNB and Johor Sultan-controlled SIPP Power Sdn Bhd. Stung by the criticisms, YTL Power said it was withdrawing from this and will submit its bid for an open tender for the same project.)

Back to the 1990s, that lack of disclosure prevents outsiders, basically us public, from taking apart the figures, examining them closely and inferring how much of a good

deal (most privatisations were great deals – for those who got them that is) it was for YTL Power.

Suffice to say it was a good deal. The internal rate of return (IRR, which measures the returns over the life of the project) at 16% was considered extremely good for a project with very little risk while there are construction margins too.

It resulted in a spawning of other IPPs, making billionaires out of some people and causing a huge dent in profitability at TNB who had to give up market share of its power generating business when hitherto it was a monopoly.

It did not matter too much that it was a monopoly because it was government owned anyway until it was listed later when the government divested some of its stake. The government continued to be a major shareholder of TNB and treated it like a stepchild while it took care of IPP interests through iron-clad contracts.

TNB was often not allowed to recover increases in power costs but the IPPs through contracts were allowed to pass on all cost increases to TNB. Not surprisingly the IPPs thrived while TNB went through a long period of depressed earnings clearly out of favour with the very government which owned it. It lost billions in market value. Sad, but true.

How could this have been done differently? Let TNB continue to own all power facilities – if it gets too big, break it up according to types of business, namely power generation, transmission and distribution, and regionally.

The government can still have major stakes in the companies but they can then be independently run and compete with one another. There is no need to give out lucrative power purchase and construction contracts to private individuals and companies or cronies.

TNB should then be required to have open tenders for the power plants, inviting everyone from all over the world and cutting the bloodsucking middlemen out altogether. Why should TNB get others to buy equipment from Siemens or Mitsubishi or whoever else when it can deal directly with them?

The construction of the IPP too can be similarly tendered out to save on costs. Right now, the IPP decides who will build the plant and often the construction costs can be

inflated to the benefit of the parties undertaking construction. YTL Group, for instance, has a construction arm.

If further privatisation is required, then TNB can think in terms of outsourcing the running of the IPPs to others. But considering TNB's own track record and the fact that IPPs often used TNB staff to run their operations, that may not even be necessary.

That way, TNB can pass the savings on margins to the consumers instead of inserting a middlemen layer called IPPs who suck out the margins from TNB and consumers and increase the cost of electricity.

The key to this is not, as everyone seems to repeat almost parrot like, the government getting out of business, but the government empowering its own companies, encouraging competition, getting best prices from around the world and getting rid of rent-seeking activities which put valuable, income earning assets too cheaply into private hands.

A multitude of sins have been committed in the name of privatisation and greater efficiency. But most times privatisation has meant an increase in prices way beyond efficiency increases. Open tenders help mitigate this but they are not sufficient. Can anyone tell me what are construction and other margins in IPP projects? Silence?

If initial prices are high and inflated and the deal structured such that it is great deal in terms of this inflated price, a double whammy is imposed on the ultimate consumers of power.

The entire system needs to be changed – no, it needs to be dumped.

Yes, the IPPs don't have the good deals of the first generation ones anymore, but it is still a pretty good deal and a very safe one at that. Anyone who gets it does stand to become a billionaire and those who get it again will stand a chance of increasing their billions!

We should not have IPPs anymore – instead we can have a single efficient utility, or if necessary power companies all competing with each other via the break-up of TNB. In the process we will pay less for power.

But that's not likely to happen because of..... yes you guessed it, cronyism. We couldn't agree with Francis Yeoh more.

GRRRRR!!!

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