CASE STUDY 02 OCTOBER 2013

Private Sector Participation: DABHOL POWER CORPORATION, INDIA

In 1991, Indian government introduced two major structural policy changes to spur economic growth. Government control over industrial licensing was decentralised and the economy was opened to more foreign investment, popularly known as Liberalisation Privatisation and Globalisation (LPG) policy. With a steadily growing population and mass urban migration and agglomeration, the power sector was critical to India's economic development. Given the importance of the power sector to India's economic development, the government decided to fast-track projects to induce foreign investment in this sector as part of a wider program of economic liberalisation. In May 1992 India invited Enron Corp (Houston-U.S. based energy company) to explore the possibilities of building a large power plant in Maharashtra. In a joint venture with U.S. companies General Electric and Bechtel, Enron created an Indian subsidiary, Dabhol Power Co. (DPC), which was 65 per cent owned by Enron.

On 20 June 1992, Enron and the Maharashtra state government signed a memorandum of understanding (MoU) to develop a 2,000 MW liquefied natural gas (LNG) fired power plant at Dabhol, 180km south of Mumbai. Neither central nor state government engaged in independent technical assistance or conducted a financial appraisal of the project and the main contract was concluded without competitive bidding of any kind. During 1995, there were state elections in Maharashtra and a new government came to the power. This new government scrapped off the plan of the power project claiming it to be infested with corruption and high costs. However, later in the same year the project was renegotiated. MSEB's stake was much higher than it had been in the initial contract. In May 1999, the first phase of the power plant was ready and begun operating.

Early Scepticism over the Power Plant

While many observers hailed the project and its promised benefits, some economists doubted its feasibility and some Indian citizens bridled at Enron's autocratic behaviour. In April 1993, a World Bank analysis questioned the project's economic viability, citing the high cost of importing and using LNG relative to other domestic sources of fuels. Because of those findings, the World Bank refused to provide funds for the project. Other critics charged that the project had not been open to competitive bids and that the deal was too costly. Some expressed concern over the terms of India's agreement to underwrite the project. With the World Bank declining to provide loans, India was forced to take on even greater risk. In 1993, the Prime Minister overruled objections from his own Finance Minister to give state guarantees for both foreign and domestic investors in energy projects. The guarantees could be counted by lending institutions as additional state debt.

The Problem Continued

Financing the project after World Bank's refusal was tough. In July, 1994, the U.S. government extended a helping hand by providing loan insurance and granting $100 million loan guarantee from the Overseas Private Investment Corporation (OPIC), for the project. For the first time ever, the then Indian government, in order to rescue the project, agreed to underwrite the liabilities of a private company. Meanwhile another issue arose, and this time it was environmental concern over importing and storing of LNG and other land and water acquisition issues. Though Enron, in a press release, vehemently denied all concerns over environmental and other ecological issues, the protests lead by the local farmers continued.

Phase-I: Operation of the plant begins

In the midst of the local protests and citizen unrest, the first phase of the Dabhol plant began its operation in the year 1999 and within one month MSEB raised concerns about its ability to pay a US$20 million monthly bill. Although MSEB had a relatively strong financial position among India's state electricity boards, it faced common longstanding financial problems, in part due to receiving payment for only a portion of the electricity that it supplied. Phase I of Dabhol consumed naphtha, a comparatively expensive fuel oil derivative, and crude oil prices had risen sharply in 2000. This was aggravated by a falling rupee, given that MSEB was bound to a US dollar denominated price. Faced with financial difficulties, MSEB sold half its 30% stake in DPC which it had acquired after the 1996 renegotiations, increasing Enron's shareholding in DPC to 65%.

With its single customer unable to pay for power, DPC invoked the central government counter-indemnity in February 2001 to recover US$17 million owed by MSEB since November 2000. The state government eventually paid the amount. DPC had few options if MSEB was unable or unwilling to pay or stopped taking power from Dabhol. Although electricity was in shortage throughout India, cross-state sales were hampered by poor infrastructure. Independent power projects wishing to sell outside their home state needed approval from the state of domicile as well as approval of the tariff by the consuming state's regulatory authority. Since 1999, Enron had tried without success to persuade the federal and Maharashtra governments to relax these rules so as to enable independent power projects to sell power to more than one state, but no relaxation was given.

Foreign creditor banks were now also concerned about MSEB's payment problems, not least since the central government's counter-indemnity applied only partially to Phase II and funds for its construction had ceased to be made available in March 2001 when construction was about 90% finished. Indian creditors, on the other hand, reduced interest rates on DPC's local currency loans to help avoid statutory provisioning for their loans. In April, DPC commenced arbitration proceedings in London and served notice of political *force majeure*. However, no settlement was reached between the parties.

DPC shuts and Ratnagiri Gas & Power Pvt Ltd (RGPPL) takes over

The millennium beginning proved to be an end for Enron's dream project in India. In December 2001, after failing through arbitration proceeding and exposure of Enron's financial and fraudulent accounting strategies in U.S., the corporation filed for bankruptcy protection. In 2004, Indian receivers took control of Dabhol Plant and the project was taken over by conglomerate that included public sector banks, MSEB, GAIL, NTPC and some financial institutions, named as RGPPL. However, this plant stopped its operation in 2006 due to lack of naphtha supply after it began its operation earlier that year, but in 2009, it began its operations once again and this time without any interruptions.

Dabhol Power Plant: Today

The 1940 MW Dabhol power project, situated in Ratnagiri district, is operated by an equal joint venture of GAIL and generation utility NTPC. GAIL is in charge of the LNG terminal, while NTPC looks after the generation. State run utility GAIL is also working on a makeover plan that hinges on doubling the capacity of Dabhol power project's gas import facility to 10 million tonnes a year. The Dabhol power project, after years of operational losses and shutdowns, is seeing a strong rebound, with its half yearly profits at Rs 220 crore during the fiscal year 2010. RGPPL the company that now owns the project made all six gas turbines operational in early 2010, achieving full capacity of 1,940 MW on March 31, 2010. The gas-based power project, which had registered a loss of Rs 600 crores in 2008-09, had notched up a marginal operational profit in the year-ended March 2010.

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