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Factors influencing finance on IPP projects in Asia: A legal framework to reach the goal

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Abstract

To capture faster economic growth in power sector, concerned efforts from the government for developing an appropriate legal framework is essential. It should be noted that government's involvement in independent power producer (IPP) project is a prerequisite for its development which eventually has significant influence on the financial structure of a project. This research discusses and identifies various issues that the government needs to deal with from selected case studies. Four IPP projects in Asia from India, Pakistan, Indonesia and China are evaluated and examined. The issues examined are related to Sovereign support policy, involvement of financial institutions and export credit agencies, purchase agreements, and credit enhancement mechanism. This study constitutes an attempt at providing a competitive strategy that will help government to develop a legal framework for IPP project financing.

Keywords: Government guarantee; Independent power producer; Project company; Public private partnerships; Sovereign support

1. Introduction

The role of power sector becomes vital for the economic development of a country [1]. Especially, in Asia, government considers this issue very critically in economic viewpoint but failed to make credible promise due to political instability and financial constraints. Government can affect private infrastructure investment as a financier, supplier, customer, competitor, or regulator [2]. Government's involvement can occur in federal, state or even local level which influences the investment policy for infrastructure. Any element in a country's policy framework that jeopardizes financial structure becomes a stumbling block for investor consortia, making project either more expensive or simply impossible because of increased risk. In many developing countries, therefore, successful implementation of financial structure requires careful review of business environment for investments and, if necessary, reform of policy framework underlying it. New financial structures often need to be designed, laws need to be amended and/or new legislation created and adopted, and regulatory oversight functions must be established and strengthened. According to Gonzales [3], a careful structuring of terms and conditions of the financing deals could pave a way to the formulation of a workable model. A consistent regulatory policy is therefore required even with multiple changes of government parties. In public private partnership (PPP) project, though most of the stakeholders are from private side and may be one or two bodies from public side such as Central Government, State Government and/or government owned agency, but they have profound role and can influence financial structuring. The role and involvement of government in financial structure of PPP project can be best understood from the Fig. 1.

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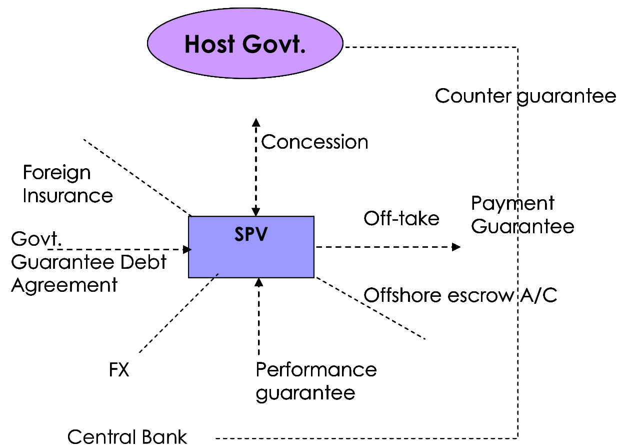

Fig. 1. Government's involvement in IPP project.

2. Overview of projects

2.1. Dabhol power project, India

The first privatized independent power producer (IPP) project in India. The Government of India and Ministry of power had invited EDC (Enron development corporation) to set up this project. Dabhol power company (DPC), a special purpose vehicle (SPV) worked as a nodal agency for bringing together private investors and concerned government agencies for the project. It was a 2015 MW project which would be connected to Maharashtra state electricity board (MSEB) grid through 440 KV transmissions [1] (See Fig. 2).

2.2. Laibin B power project, China

Laibin B was the second phase project of Laibin power plant, which involved investment, financing, design, construction, procurement, operation and maintenance and transfer of a 2X350 MW coal-fired power plant. The project company (SPV) was consisted of Electricite de France (EDF) and GEC Alsthom backed by COFACE, France's export credit agency. Guangxi State Government ensured fuel supply and power purchase guarantee [4].

2.3. Paiton1 power plant, Indonesia

This was the first independent power project financed in Indonesia. PT Paiton Energy Company (Paiton1) was organized to finance, construct and own Indonesia's first large private power project at a cost of roughly US $ 2.5 Billion. It was a 30 yrs contract with PLN. The economic downturn and political changes in Indonesia after 1998 caused severe problems to the project. The devaluation of local currency also adversely affected the sponsor's ability to service the foreign debt. The contract was then renegotiated [5].

2.4. HUBCO power plant, Pakistan

Hub power company (HUBCO), a public limited company incorporated in Pakistan was established to produce 1292 MW thermal power in the province of Baluchistan at a total cost of US $ 1.833 billion. The lenders considered the equity as the protection for their loans and commitments towards the project. World Bank and a consortium of foreign banks and agencies were committed to finance the project. National Development finance corporation (NDFC) was appointed to the lead bank to arrange long term loans and also the administrator of private sector energy development fund on behalf of the Government of Pakistan (GOP). The power generated would be sold to WAPDA [6].

Table 1 shows the general information of the projects.

3. Methodology

The study has attempted to analyze government's role and involvement in four IPP projects in India, China, Indonesia and Pakistan. Qualitative research is done based on case studies published in journals, books, and through the Internet. The project contracts were signed during the

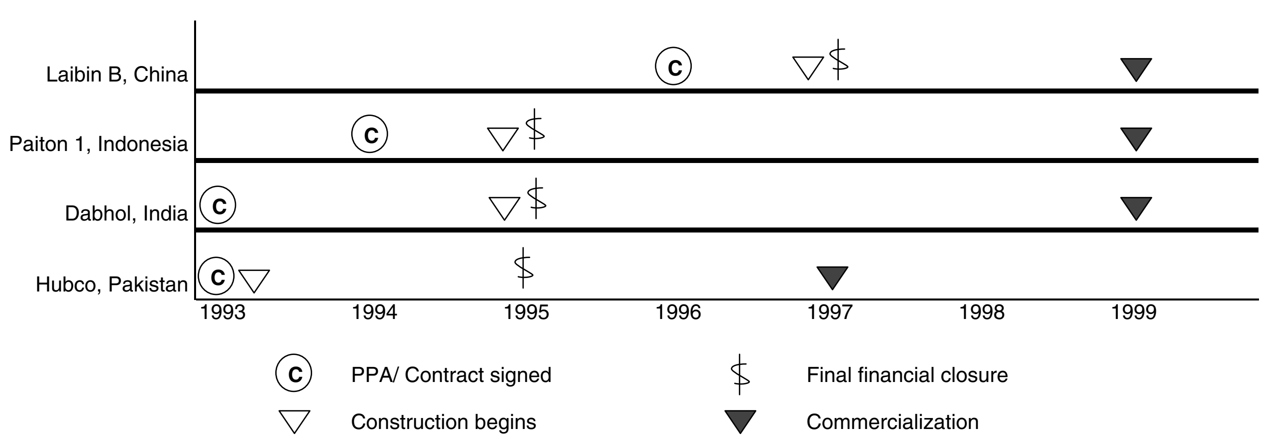

Fig. 2. Project phases.