

Rao, Geetha

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Sent: Monday, January 22, 2001 1:54 PM
To: geetha.rao@do.treas.gov
Subject: India/Dabhol Meeting



Dabhol PPA - DC
Talking Points...

Geetha,

My apologies for the delay in sending this material. I have lost both my regular assistant and my temp so I am a bit overwhelmed.

John Hardy will be attending the meeting tomorrow at 3. His SS# is [(b)(6)] and birthdate is [(b)(6)]. If you could remind me of the address of the meeting I would appreciate it. I managed to lose that as well.

John and I have a brief agenda: 1) we want to update you on Dabhol and 2) we want to discuss way in which the USG may become involved in encouraging market reform necessary to extract value out of our generating asset. Specifically, we want to focus on reform at the Indian federal level that will be necessary to deliver power to customers other than MSEB.

We look forward to meeting you tomorrow.

(See attached file: Dabhol PPA - DC Talking Points.doc)

Dabhol Power Company
January 10, 2001

Events

- The State of Maharashtra Chief Minister Deshmukh announced during the winter session of the State Legislature that Phase II of the Dabhol Project was to be reviewed. Allegations were made that the high Dabhol tariff was the cause of the Maharashtra State Electricity Board's (MSEB) financial difficulties.
- The Government of Maharashtra (GOM) will appoint a committee of experts to reexamine the Dabhol Power Purchase Agreement, a 20-year PPA to the single buyer MSEB.
- MSEB is currently in arrears for the Dabhol November bill in the amount of Rs 148 Crores (1,480,000,000 Rupees).
- Phase II of the Dabhol project is 80% complete, with 55% of the equipment on site and \$400 MM remaining to be disbursed out of \$2.6 billion.

Facts About Dabhol

- By providing 2184 MW gas fired power plant, built to international standards with related gas facilities, DPC is creating substantial opportunities for the development of a modern industrial corridor in south central Maharashtra
- So far, Dabhol has contributed over Rs 1600 crore to the national and state exchequers and has brought in Foreign Direct Investment of over Rs 10,000 crore (\$2.5 billion) into the country
- In building the facilities, DPC has provided valuable employment to area residents. DPC contractors on the site currently employ approximately 15,000 workers. A hospital, school and other community services have been provided to area residents by DPC

Issues

Expert Committee. DPC will cooperate with the GOM-appointed Expert Committee. That does not mean, however, that the PPA will automatically be renegotiated. To allow the time for such review, three things must happen: (i) DPC must continue to fulfill its generation obligations under the PPA; (ii) MSEB must pay the money owed to DPC; and (iii) the project lenders must continue to disburse funds to finish Phase II of the project.

Cause of MSEB Financial Difficulties. Dabhol is not the cause of MSEB's financial difficulties. Those difficulties are due to a number of factors, among them:

- The need for meters to measure electricity distributed to end users.
- The high rate of losses. MSEB currently has approximately 30% losses, a large part of which is due to theft.
- The State's continuing to grant subsidies on a political basis and not compensating MSEB therefor.
- The State's not allowing MSEB to disconnect nonpaying customers.
- The large cross subsidies built into the tariff structure.

Power Shortage. India is in need of power. The Minister of Power has recently stated that India needs 10,000 MW of new generation. (The state of Maharashtra itself faces a continuing shortage of power (approx. 2000 MW) resulting in large areas facing load shedding and blackouts.)

Foreign Direct Investment. Because India lacks the funds to construct needed power infrastructure, foreign direct investments are needed. Failure to honor contractual commitments or to respect the sanctity of contracts will serve to discourage such investment.

Distribution Reform. The long term solution is to institute reforms quickly. Reforms that are particularly pertinent to the financial distress suffered by the SEBs are:

- State Electricity Boards must be unbundled into three business units (generation, transmission and distribution) and be made accountable for their performance via corporatisation.
- Professional management teams rather than bureaucrats must run the power sector companies.
- Improvements to the infrastructure are critical. Losses cannot be reduced until electricity is metered, those using power properly billed, the funds billed properly collected, customers disconnected for nonpayment, and those responsible for theft of power prosecuted.
- The State must allow MSEB to run its business in a professional manner rather than as a political vehicle. Thus, subsidies must not be granted unless the government is willing to pay for them.
- Finally, the tariff structure must be rationalised so that the costs of distribution of power to the various customer classes are reflected in the tariffs.

The Dubbed Tariff. The tariff is not an absolute number but is a formula. The tariff at which DPC power is sold to MSEB is comprised of two cost factors, a fixed capacity charge and a variable energy charge. The per unit cost of DPC power, in turn, depends on the quantity of power actually drawn by the MSEB, prevailing international crude oil prices, and the rupee/dollar exchange rate. Depending on fluctuations in these variables, the tariff can go either up or down. A more representative way of judging tariff is on an annual average.

From May 1999 to October 2000, MSEB's off-take from DPC was an average of 60 %, resulting in an average tariff of Rs. 4.94. If during that period the off-take had been 90 %, the average tariff would have been Rs. 4.02. Looking ahead, the recent drop in international fuel prices (which affects the price of naphtha) will result in a decrease in the tariff. With the commissioning of the second phase of the project by end 2001, when Liquefied Natural Gas (LNG) is used as fuel, the tariff will be further reduced another 20-25% (assuming 90% off-take, prevailing foreign exchange rates and international fuel cost remaining within \$21-28.)

It is not true that the tariff was Rs. 28 per unit during last summer. Rather, a Rs 7.80 figure was recorded for the monthly cycle bill of July 2000 – a figure based on a low dispatch level of 33 %, naphtha price of \$ 306/MT and at an exchange rate of Rs. 45.35 per dollar. On the other hand, had MSEB dispatched DPC at 90% during the same period, other factors remaining identical, the tariff would have worked out to Rs. 4.31 per unit. (Capacity charge Rs 1.88 plus energy charge Rs. 2.43).

Financing

Costs. Total project cost is \$3 billion (Phase I \$1.1 billion; Phase II \$1.9 billion).

Total Debt. Total project debt is \$2 billion (Phase I \$600 million; Phase II \$1.4 billion).

Indian Debt. Of the \$2 billion project debt, \$1.2 billion is Indian debt, consisting of direct loans and guarantees. (Because the Japanese, U.S. and Belgium Exim Banks take no direct risk, the Indian banks guaranteed their loans.)

Other Foreign Government Lenders. Japanese Exim Bank; Belgium Credit Agency, U.S. Exim Bank, and Opic, the latter also providing political risk insurance to shareholders.

Other Lenders. 40 other international banks are involved in the loans for the Dabhol project.

Fuel Supply. Both the Oman and Abu Dhabi governments are involved in providing fuel to Dabhol. The Oman facilities are 60 percent owned by the Government and 30 percent owned by Shell.

LNG Tanker. The tanker is owned by Shipping Company of India, Mitsui and 15 percent by Enron.