Third Party Evaluator's Opinion on Improvement in Power Grid Project

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Relevance

Of the eight designated substations for which the project was to procure and install additional transformers, five had to be installed in different locations. In two of these five cases, the reason was lower than predicted power demand due to (a) the economic slowdown occasioned by the 1997 Asian financial crisis, and (b) the overly optimistic load forecast contained in the Power Development Plan (PDP).

The wide difference between projected and actual electricity consumption was the result of both failing to meet GDP growth targets and assuming a very high income elasticities of demand for power. While the Asian financial crisis could not have been anticipated, the GDP growth targets were much higher than actual rates based on postwar historical experience. Similarly, the income elasticities of demand used in the projections (in the range of 1.53) were much higher than observed historical levels. This reviewer alerted the Department of Energy on this in mid-1993 (having been asked to review3 the draft PDP); the comments were referred to the National Power Corporation (NPC), but NPC stuck to its highly optimistic forecasts. The result was a significant expansion in power generating capacity, much of it through BOT contracts with Independent Power Producers (IPPs) under take-or-pay arrangements at high levelized prices, the effects of which continue to plague the sector up to now. By the latter half of the 1990s, many IPPs were operating below their expected capacity factors. Most analysts agree that some of the BOT projects should have been deferred or even cancelled.

The project nevertheless maintained its relevance because by the late 1990s, NPC's financial health was beginning to suffer, and the project offered relief with its very generous concessional terms. The project also allowed sufficient flexibility in the choice of location (with five of the eight original sites replaced, based on exigencies at the time). This would not have been easily arranged with other donor partners. The substantial cost saving with the project (appraisal vs. actual) similarly belies the perception of some high Philippine government officials that JBIC projects are generally expensive, over-designed, and supplier-driven.

Sustainability

The Evaluation Report documents vividly the project's effectiveness in enhancing the stability of power supply in the areas concerned and the corresponding positive impact of this improved reliability on consumers, particularly industrial users. A significant threat to the sustainability of project benefits, however, is NPC's deteriorating financial condition. In 2002 the return on rate base (RORB) was only 0.2%, way below the minimum 8% that NPC has committed in its loan covenants; the net income to net worth ratio was -43.7%; the debt-to-equity ratio was 95:5. The poor financial performance is partly due to a change in account conventions; starting in 2002 foreign exchange losses on loans and IPP obligations had to be booked immediately and in full, instead of being spread out over the remaining life of the obligations. But much is also due to NPC's inability to adjust tariffs to reflect actual costs.

The 2001 Electric Power Industry Reform Act (EPIRA) was initially expected to launch a sector reform program that would make the industry more competitive, with the private sector given a bigger role. NPC privatization, however, is suffering delays; even if the NPC assets were sold on time, there would remain some P200 billion in unpaid loans. There is also a problem with IPP contracts signed after 2000. It can only be hoped that all these issues get resolved soon, or the country will once again suffer a power crisis.