

CERC notifies final tariff regulation FY24-29



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Utilities

The Central Electricity Authority (CEA) has issued final terms and conditions for Tariff Regulation FY24-29. The draft regulation was released in January 2024. The final regulation is in line with the draft, with a few adjustments to the normative plant availability factor (PAF) for capacity charge recovery and normative plant load factor (PLF) for PLF incentive. We note the incentive for off-peak power has been raised by 5 paise/kWh. We believe the final regulation will have a favorable impact on NTPC, NHPC, and SJVN while they are expected to have a limited impact on Power Grid.

ROE of regulated assets remains consistent with that outlined in the draft regulation

Return on equity of regulated assets remains steady with the proposals outlined in the draft regulation. For thermal and transmission projects, ROE is set at 15.5% while for hydro projects, it is at 16.5%. ROE has been relatively stable across tariff periods, indicating the Central Electricity Regulatory Commission's (CERC) preference for regulatory permanence. However, there are adjustments for new projects. For transmission projects commissioned after April 2024, the base rate for ROE will be 15%, and for new pumped storage projects, it will be 17%. ROE of new thermal projects remains unchanged at 15.5%. We do not expect a slight decrease of 50bp in ROE of transmission projects to have a significant impact on Power Grid Corporation of India (PGCIL), as most new projects are being added through tariff-based competitive bidding (TBCB). Conversely, an increase of 50bp in ROE of pumped storage projects is likely to attract sizeable investments in this sector. We expect companies, such as JSW Energy, NHPC, and SJVN, to register positive benefits.

NAPAF for recovering fixed charges and NAPLF for PLF incentive revised up from the draft

For power plants that are more than 30 years, normative PAF for fixed cost recovery and normative PLF for PLF incentive was proposed at 80% in draft regulation vs 85% earlier. This adjustment would have allowed earnings to be based on an additional 5% each for PAF and PLF. However, normative PAF and PLF each has been revised to 83% in the final regulation, resulting in earnings based on an additional 2% each PAF and PLF. Although the draft based PAF and PLF would have yielded more positive benefits, this adjustment is still positive for NTPC, which possesses ~15GW of thermal capacity aged over 30 years.

Incentive during off-peak hours increases 5 paise per unit in the final regulation

The proposed incentive for generation stations is set to be 75 paise/kWh for energy produced during peak hours and 55 paise/kWh for energy generated during off-peak hours, given that the generation levels are above normative levels. In the draft, the incentive for off-peak hour generation was proposed at 50 paise/kWh. This upward revision of 5 paise per unit is expected to fare positively for NTPC. The CERC has introduced a grid balancing incentive. In the draft regulation, the proposed incentives were up to 1% of annual fixed cost (AFC) for thermal assets and up to 4% of AFC for the hydro plants. However, the incentive for the hydro plants has been revised down to 3% of capacity charge approved for a given year.

O&M annual cost escalation revised down from the draft regulation

The CERC has set a special allowance applicable to plants that are more than 25 years old and not choosing additional capitalization for repairs & modernization at INR1.075 mn/MW/year during FY24-29. This marks a 13% increase over the preceding five years (INR 0.95 mn/MW/year during FY19-24). Initially, in the draft, the CERC proposed an annual inflation rate of ~5.9% for operations and maintenance (O&M) expenses, a sharp rise from the previous tariff period's 3.5%. However, this has been revised down to ~5.3%. This downward revision may be viewed as a negative, as companies are currently experiencing inflationary pressures in their O&M cost.

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