

SLEA QUARTERLY ECONOMIC REVIEW

Abreast of contemporary issues on economic lens

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Message from the President of the Sri Lanka Economic Association (SLEA)

I am delighted to share with you our fourth e-newsletter, "SLEA Quarterly Economic Review" (SQER). This publication is the brainchild of the SLEA's Economic Research Committee (ERC), headed by Dr. Malraj B. Kiriella. I praise the ERC for their initiative and the committee members' untiring efforts in this worthy endeavor.

The SQER is a quarterly publication that contains an analytical discussion of contemporary economic issues faced by Sri Lanka, including their root causes, consequences, and policy prescriptions. The SQER covers both contemporary macroeconomic and sector-specific issues in the economy. The ERC organizes discussion forums with subject experts to gather first hand knowledge, which is then synthesized and compiled. The fourth issue consists of current status of IMF rescue programme and debt obligation, exchange rate appreciation and power sector reforms.

I hope you will enjoy our publication and feel free to share it with your network. If anyone wants to subscribe, they can email us at slea.office@gmail.com. If you no longer wish to receive this publication, please click the unsubscribe link at the bottom of the SQER.

Rev. Prof. W. Wimalaratana

SLEA President

Power Sector Reforms: Challenges and the Way Forward

Background

Power sector reforms have been undertaken by many developing countries. These reforms have generally led to the development of the power sector in countries where those were implemented. However, progress at physical, economic, and institutional levels has recorded mixed results, particularly in the areas of market structure, private participation, and regulatory framework. The electricity supply industry emerged in 1900-1950s and the electricity sector reforms began in the 1990s in Europe and 2000-2010 in Asia. In the early years of Sri Lanka's Independence, its power sector operated as a government department. In 1969, the Ceylon Electricity Board (CEB) was established, serving as the state's public service utility and regulated by the Ministry of Power and Energy as a vertically integrated monopoly. The CEB carried out all the functions of electricity generation, transmission, distribution, and retail supply, without any competition at any level. Since the early 1980s, countries with very different levels of income have had a wide range of experiences with power sector reforms. The sector was restructured in 1996 with the entry of the private sector in thermal generation. The next step was to unbundle the Ceylon Electricity Board (CEB), the government-owned monopoly, and establish an independent regulatory commission. In 2002, the Public Utilities Commission of Sri Lanka (PUCSL) and the Electricity Acts were approved. (ADB)

Current Status & Risks

Power sector reform experts believe multiple reasons led to the prevailing high cost of electricity. Accordingly, the high level of dependency on imported fossil fuels, which comes at a high cost, the absence of a transparent competitive procedure in purchasing electricity from the private sector, long delays in the expansion of the power generation capacity, and poor payment records of the CEB for high-risk premiums demanded by investors are the most noticeable.

Sri Lanka has a non-competitive procurement procedure that has been functioning for the past 31 years. The procurement of generation, which is being processed without a competitive process, and the procurement price for renewable energy is highly debatable. With a different view on the new Electricity Act, energy sector expert highlighted that weaknesses in accountability and transparency issues plague the reform process. There are rules, acts, and regulations to regulate costs, prices, and tariffs, weaknesses in accountability and the quality of commercial service by the regulators always hamper the process. Energy sector experts reiterated the issues in the regulatory systems and bureaucracy in management leading to the shortcomings in the system, which should be addressed and that the new electricity reforms will be a failure if poor governance in this sector is not rectified. The public is denied information on electricity reforms in Sri Lanka as those are not openly discussed. A long-term generation expansion plan does not address the shortage of supply, lack of

accountability, and inefficient procurement due to corruption issues. The management is heavily politicized, and the political interference of state-owned enterprises should be gotten rid of to manage the sector professionally and profitably. Also, energy sovereignty has to be looked at as the ownership of energy systems is alienated. It was suggested that unbundling into entities is not the answer to proper management as it will create multiple bureaucracies.

Way Forward for Sri Lanka

The cost of electricity and minimizing dependency on imported oil and other fossil fuels with renewable energy, competitiveness, efficiency improvement, and enforcing managerial accountability of transmission and distribution should be among the key objectives to develop the sector experts establishing a legal and institutional framework, including the inclusion of private sector investments, effective regulation with transparency, developing supply value chains, and allowing the consumer to select the energy supplier and source of energy through open access and competitive markets in line with global trends and technology were suggested, along with new electricity reforms to ensure long-term power development.

Recommendations

The vision should be to obtain cheaper electricity with the correct technology, professionalism, and a recognized international plan. Power sector reforms in Sri Lanka, including the evolution of the power sector's structure, policies and regulations toward reforms, and obstacles limiting reforms should be well-studied and planned before being executed. The outcomes of reforms are examined to the extent possible, by analyzing the trends in a set of commonly agreed and internationally accepted social, economic, and environmental indicators. Full liberalization of the electricity market is still a few years away and must wait until the regulator (PUCSL) displays the ability to supervise the current structure and implement the regulatory instruments that are already in place. The currently approved tariff methodology ends in December 2015, by which time a new methodology including the limited opening of the wholesale market should be discussed and prepared for implementation. As stipulated in the Electricity Act 2009 and in the National Energy Policy 2008, full cost-based pricing should be achieved for all customers, with targeted subsidies strictly limited to the very poor and provided through means other than electricity charges. This is an essential prerequisite to any new reforms.

Resource Persons: Dr. Pradeep Perera, Head of the Power Sector Reform Secretariat at the Ministry of Power and Energy

Dr. Tilak Siyambalapitiya, Managing Director of RMA Energy Consultants

Professor Lalithasiri Gunaruwan, Professor in Economics at the University of Colombo.

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