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A Review of the Budget Speech for F.Y. 2024/25: Highlights and Critiques for the Energy Sector

The Finance Minister of the Government of Nepal has presented the budget for the upcoming Fiscal Year 2024/25 which has allocated a total budget of NPR 57.50 billion (Nepalese Rupees Fifty Billion Seven Hundred and Sixty Million Only) for the energy sector. The following represents some of the key highlights and critics from the recent budget in the energy sector.

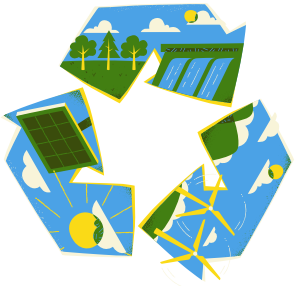
Development of Hydropower Projects

The budget has prioritized starting the construction of Dudhkoshi (670 MW), Nalsingal (417 MW), Naumure (280 MW), Ghunsa (77.5 MW), Simbhuwa (70.3 MW) hydropower projects to meet the electricity demand during the dry season.

In addition to identifying the list of hydropower projects to be developed, the Government has also focused on identifying the source of investment to finance some hydropower projects. Amongst the identified projects, Naumure (280 MW), Ghunsa (77.5 MW), Simbhuwa (70.3 MW) hydropower has been planned to be constructed by utilizing investment from individuals pursuing foreign employment.

The budget has continued to prioritize projects from the previous fiscal years including the development of Upper Arun (163 MW), Tamakoshi fifth (100 MW), Chainpure-Seti (210 MW) hydropower project under the "Public Hydroelectricity Program". The construction of Nalsingal (417 MW), Naumure (280 MW), Ghunsa (77.5 MW), Simbhuwa (70.3 MW) and Modi A (42 MW) hydropower projects are additional projects proposed in the current budget. The proposed budget has significantly continued with the projects which were supposed to start construction from the previous fiscal year. In the current pace of execution of projects, the likelihood of achieving 11,759 MW by F.Y. 2085/86 as stated in the 16 th Plan does not seem achievable.

One of the key highlights of the budget is to commence the engineering design of Karnali - Chisapani Hydropower Project (10,800 MW). The execution of the proposed Karnali-Chisapani Hydropower Project would align to the 16 th plan which prioritizes the construction of the reservoir-based and multipurpose electricity generation projects to meet the generation target. However, similar to other electricity projects, the likelihood of executing the project is also doubtful.



For context, the feasibility study of the last project was already conducted in 1989 and it has already been nearly four decades that the progress remains stationary. Since then, the Government has decided to conduct a fresh study of the project on several occasions and still no such progress has been made towards its execution. To achieve long-term electricity generation target of 40,000 MW by F.Y. 2100 (2101 B.S.), Government must avoid such delays in developing large multipurpose and reservoir hydropower projects like Karnali-Chisapani Hydropower Project.

Transmission Line

The development of transmission lines has also been a key focus with major projects including Hetauda-Dalkebar-Inaruwa; Khimti-Bahrabise-Lapshiphedi; Karnali Corridor; New Butwal – Gorakhpur; Inaruwa-Purniya; Dododhara-Bareli and Rasuwa-Kerung transmission line networks. The Government has set an ambitious target to nearly double the transmission line network by 2085/86 B.S. increasing it from the current status of 5,792 circuit kilometers to 9,356 circuit kilometers. The 16 th plan of the National Planning Commission also emphasizes the development of transmission lines to meet the requirements of internal consumption and the export of electricity, aiming to increase the current electricity consumption from 380 kWh to 700 kWh by 2085/86.

One way the Government proposed meeting this ambitious target is by facilitating private sector participation in the development of transmission and distribution lines. This also aligns with the recent reforms proposed in the Electricity Bill, which aims to facilitate private sector's involvement in the development of transmission lines.

Net Zero by 2045

The Budget has introduced programs to replace fossil fuels with renewable energy aiming to reach zero carbon emissions by 2045. For this purpose, specific focus has been given to the development of solar energy projects for electricity generation of 100 MW and research and development of green hydrogen. Recently, the Government has tried to develop the energy sector with mixed sources of energy, which over the last decade has mostly been limited to hydroelectricity. This proposed initiative of focusing on solar energy is a welcoming step towards an inclusive mix of energy sources in Nepal which thereby can decrease the over-dependency of the country on hydroelectricity. Furthermore, the shift to solar energy should be continued as a start for identifying additional sources of other renewable energy such as wind power, geothermal, green hydrogen. This would potentially pave the way for an effective strategy to reach the target of net zero by 2045.

As of June 11, 2024, Nepal's installed solar energy capacity stands at 68.38 MW and has issued survey licenses totaling a combined capacity of 662 MW for 33 projects, according to the latest data from the Department of Electricity Development. Significant developments in the sector include the recent tender issued by Nepal Electricity Authority for the development of 800 MW of solar energy, reflecting encouraging progress.

Way Forward

Overall, the current budget for the energy sector largely continues to mirror the previous budget. Some of the notable efforts in the budget are increasing the sources of financing and initiating steps towards increasing energy mix through solar projects.

Participation of private sector in the energy sector (both generation, and transmission) is crucial to harness maximum potential in this sector. To effectively implement the proposed engagement of the private sector in developing transmission lines and electricity generation projects, the government should facilitate various financial instruments being used by institutional investors in the global markets. Policy reforms should be designed to address key bankability risks (like termination payment) to increase sources of financing. This will support the key strategies of the 16th Plan to promote domestic, foreign, and bilateral investment in the development of National Pride Projects and development of transmission line projects by mobilizing innovative financial instruments.

Globally, institutional investors have been using different forms of financing models such as blended finance, thematic bonds, green bonds, and mezzanine instruments to balance higher bankability risks with potential upside. The Government should promptly coordinate with NRB and other regulatory authorities to enable investment from such innovative financial instruments. This will be a welcoming shift to the institutional investors who under the current regulation have been limited to finance projects only by way of a typical financing modality (i.e., either in the form of loan or equity). Increased stakeholder discussions including potential financiers are necessary to understand key bankability risks in Nepal.

There has been a provision in the budget to facilitate green bonds and other innovative financial instruments. However, this may not benefit institutional investors without legal reforms in the foreign investment and NRB Bylaws.

Similarly, the recent 16 th plan has proposed facilitating electricity trade by adopting an action plan and incorporating legal provisions enabling participation from the private sector in trading of electricity as one of the major strategies for energy sector.

For a better alignment of the budget for the development of the energy sector, going forward, the Government should shift from its current attitude of continuing the same budget and same strategies from the previous fiscal years with few adjustments. The Government needs to adopt a more comprehensive and reformative strategy to meet the expected policy targets in the energy sector.

On that note, revising the proposed Electricity Bill, which is currently tabled been in the House of Representative, is crucial. The following reforms can play a pivotal role:

1. Implementing a delicensing mechanism for renewable energy projects such as solar and wind, as well as captive energy projects to limit bureaucratic involvement and process allowing quicker development of renewable energy projects.
2. Implementing an inclusive framework that encourages private sector participation, including asset monetization, particularly in the areas of transmission and distribution networks. Asset monetization would allow private sector to take over performing assets and this would maximize utilization of these assets by harnessing efficiencies expected from the private sector and would also allow the government to recycle its assets and capital.
3. Private sector should be prioritized before public sector constructs and operates transmission and distribution infrastructure. So, construction of all new transmission and distribution infrastructure should be floated for private investment prior to competitive bidding or implementation through negotiation in certain situations. (B) Private sector involvement in construction of transmission assets have been recorded to be 25-30% lesser expensive than public sector in Latin American countries like Peru and European countries including UK. Further, the private sector is more likely to complete the construction of infrastructures on time and more efficient O&M can be expected from the private sector as it aligns with their commercial interest.
4. Key bankability risks should be addressed through the Electricity Bill to attract more private sector financing, especially foreign capital. Those bankability risks include issues like security creation, change in law protection, certainty on termination of licenses, and efficient land acquisition process. A certain standardized form of concession agreements would also be a step towards addressing these issues.