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POLICY **BRIEF**

NO. **016**

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KEY POINTS

- It is observed that while installed capacity has risen from 804.7mw/h in 1970 to 13,400mw/h in 2020, the size of electricity generated only increased from 176.6mw/h to 3,196mw/h over the period.
- While already privatized, government still expends huge amount of resources to cover shortfalls along the various value chains of the electricity sector.
- The sector needs to operate in a manner that minimizes costs and be free from unnecessary bureaucratic processes that may introduce other financial and non-financial costs to the citizens.

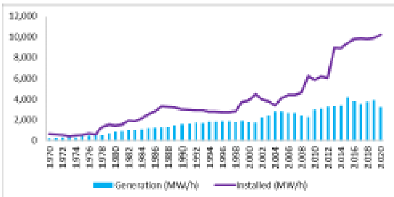
Can Nigeria Learn from the 'Failed' Privatization of its Electricity Sector?

The performance of Nigeria's power sector has been sub-optimal, despite various policies, interventions, and investments in the sec-tor. Figure 1 shows the trend of the country's electricity installed capacity and generation over the last 5 decades. It is observed that while installed capacity has risen from 804.7mw/h in 1970 to 13,400mw/h in 2020, the size of electricity generated only in-creased from 176.6mw/h to 3,196mw/h over the period.

Nigeria's electricity generation is very low, as most selected countries record higher values than Nigeria (see Figure 2). Also, countries such as Ghana, Kenya and Botswana with lower generation still have relatively higher per capita electricity generation than Nigeria. The sector has been grappling with problems around generation, transmission, distribution, incessant grid collapse and general ineffective infrastructural capacity. These problems are further compounded by low investment, policy inconsistencies, subsidy and an inefficient tariff regime.

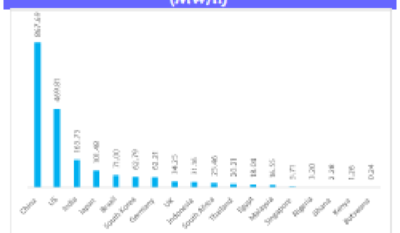
Over the years, successive governments have come up with re-forms, laws, policies and interventions toward solving Nigeria's electricity problems. One of such reforms is Electricity Power Sector Reform Act of 2005 which has the aim of deregulating the generation and distribution segments of the power supply market. These efforts have predated and birthed the privatization of the sector in 2013 and the handing over of the generation and distribution of power to the private sector, while the government retains the transmission.

Figure 1: Electricity Generation and Installed Capacity



Source: PHCN, CBN & ADSR Research

Figure 2: Electricity Generation of Selected Countries (MW/h)



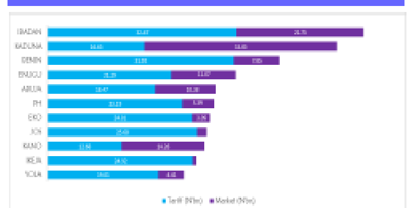
Source: EIA & ADSR Research

However, the general experience is that the Nigerian electricity sector has not witnessed the type of improvement envisaged and required to move the economy forward. This suggests that the privatization of the power sector has failed to achieve its major objective of delivering increased and efficient power to Nigerians.

It is interesting to also note that while already privatized, government still expends huge amount of resources to cover shortfalls along the various value chains of the sector, coming from the CBN Payment Assurance Facility (PAF), Federal Government Budget Allocation and World Bank Power Sector Remittance Or-der (PSRO) loan. Specifically, the PAF comes from the establishment of Nigeria Electricity Market Stabilization Facility (NEMSF) by the CBN worth N213 billion to mitigate the current challenges facing the power and gas sector, among others. The Nigerian Bulk Electricity Trading Plc. (NBET) is a Federal Government company set up, among others, to purchase electricity from the electricity Generating Companies (GenCos) and resell to the Distribution Companies (DisCos). NBET defines the Minimum Remittance Order (MRO) as the minimum remittance that a DisCo must make to NBET in relation to its invoice for grid distributed electricity received by the DisCo for a period. It is the rate at which the sector regulator determines the tariff is commercially viable to the DisCo.

To further illustrate the nature of the problem in the sector, data obtained from the NBET indicates that in 2021, DisCos' tariff shortfall amounted to about N251 billion while market shortfall is estimated at about N113.5 billion. Figure 3 shows the distribution of both shortfalls across the different DisCos. It is observed that Ibadan leads the chart with N34.47 billion and N21.75 billion tariff and market shortfalls respectively; and this is closely followed by Kaduna. A DisCo such as Kano has a high market shortfall relative to its tariff shortfall; while Ikeja, Jos and Eko have relatively low market shortfalls relative to their respective tariff shortfalls.

Figure 3: Tariff and Market Shortfalls of DisCos 2021



Source: NBET, ADSR Research

The figure therefore shows that government supports DisCos with relatively high tariff shortfalls while those with relatively high market shortfall will be highly indebted. Accumulation of shortfalls by the Discos over the years contributes to their high indebtedness and inability to meet some of their acquisition loan obligations to commercial banks.

In a bid to salvage the sector from total collapse, the Federal Government recently announced the takeover of four of the DisCos namely: Kaduna, Kano, Ibadan, and Port Harcourt. The government also inaugurated the board of the Nigeria Electricity Liability Management Company (NELMCO) to enhance the ongoing efforts to resolve liabilities relating to shortfalls for distribution companies, among other challenges plaguing Nigeria's electricity sector.

While it is important for government to step in and ensure that the DisCos perform sustainably with improved access to electricity by Nigerians, the country needs to properly define and be committed to its privatization philosophy. For instance, the National Development Plan (2021-2025) has, as government philosophy to *"…open opportunities for the private sector to be a major engine of growth."*

Learning from the experience of the privatized refineries which was reversed by a new administration in 2007 and the recent takeover of the DisCos, one strongly wishes future privatization exercise in the country are properly executed by determining the suitability of private sector operations for the relevant sectors or their aspects, attracting the right investors and implementing an effective framework for regulating private operators.

Government's plan to privatize some of its assets aims at transitioning Nigeria from public sector to private sector led economy. However, the recent takeover shows weakness in implementing the right policy and institutional framework to drive the exercise to success. Thus, future effort at privatization may suffer trust problem and may affect the success rate. Going forward, there is need for proper and effective policy and institutional framework that would eliminate policy inconsistency, ensures effective re-form implementation and proper capacity need assessment of investors to attract those with the right technical and financial capacities.

Moreover, the takeover also raises questions about the fate of the country's electricity sector in the short to medium term. Will the government just move in, stabilize the sector and move out and for how long? Or will it completely be under government control and what will the performance level be, and at what cost? Regardless of the approach taken, Nigeria and Nigerians need an electricity sector that generates, transmits and distributes electricity to power the economy. It is equally important that this is done in a manner that is efficient and devoid of unnecessary costs for sustainability.

Issues around investors' confidence should be managed discreetly; lest they become too cautious of dealing with the country in the future, particularly on long-term projects. Unnecessary issues of litigations can also be avoided, learning from the case of Ajaokuta Steel Company which stalled the development of the Company for many years with some financial penalties. In the current case, issues of litigation that may arise need to be well managed and resolved. Government needs to build investors' confidence in the sector. The new board of NELMCO, recently inaugurated, needs to deliver on its set mandate of settling the liability of the defunct PHCN to boost investors' confidence and attract the right ones to the sector.

As earlier depicted, the DisCos are currently experiencing huge tariff and market shortfalls; this needs to be addressed whether the sector is operated by the private sector or the government for a while. No doubt, government may bear some costs, but this should be for a defined period. The sector needs to operate in a manner that minimizes costs and be free from unnecessary bureaucratic processes that may introduced other financial and non-financial costs to the citizens.

If things are done transparently and efficiently, costs may be low and affordable to Nigerian who themselves may have little or no justification to push back on cost-reflective tariffs, especially if they get value. No doubt, the current supports are unsustainable, and they are more likely to disappear under a private-sector producer that operates efficiently and guided by the right policy and regulatory framework.

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