**Charter of energy?**

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As Pakistan suffers yet another ‘energy crisis’, it is worth asking what should be done to avoid history repeating itself all too frequently. To be fair, the recent commodity super cycle, compounded by the war in Ukraine, is stress testing even the more developed energy ecosystems worldwide. However, our sectoral fault lines are structural in nature and cannot be blamed on external factors alone.

It would, therefore, help to first understand the real issues and then try to develop a political-cum-bureaucratic consensus on a holistic solution beyond the ongoing binary debate on maintaining (or reversing) the current unsustainable power and petroleum subsidies.

First and foremost, Pakistan’s energy sector must be liberalized and run autonomously by regulated companies, private or public. This would be a paradigm shift in thinking and approach but does not mean granting cart-blanche to unscrupulous private cartels to ‘loot and plunder’ the common citizen, and create artificial supply shortages at will, as is sometimes feared.

For the state to cede political and pricing control of such essential service, it means restricting its role to consistent policymaking, alongside strengthening independent regulatory oversight of the licensees to enforce competitive consumer pricing, reliability of supply and a level playing field, as generally experienced in the telecom sector post liberalization. What that practically implies for the energy sector is illustrated by the following four propositions:

One, there is no reason for the prime minister of Pakistan to intervene in the market to set fortnightly petroleum prices when the same can be done more effectively on a petroleum commodity exchange matching supply and demand in real time, with PSO (the state-owned oil marketing company with the largest footprint) effectively setting the pricing benchmark. Whether it is for petroleum or electricity, a political government will always retain the policy toolkit to reduce indirect taxes and levies on various energy products or offer funded subsidies to targeted socio-economic segments of the population directly through its social welfare programmes (BISP/Ehsaas) or to the export-oriented industrial sector. If the market is deregulated, there may also be no need, for instance, to offer special incentives or subsidies to the local refineries to optimally invest in upgrading and modernizing their existing assets to enhance our energy security.

Two, the management of all state-owned power distribution companies must be handed over to the private sector, under a transparent process run by the Privatization Commission, alongside a more equitable financial and risk sharing arrangement with the provinces per the spirit of the 18th Amendment and the NFC Award. The federal government must finally realize that it cannot centrally run these local ‘last mile’ businesses from Islamabad whilst bearing 100 per cent of their financial burden. Let the private concessionaires be regulated and incentivized by Nepra, under a multi-year tariff regime, to invest in well-identified technical solutions to reduce the aggregate technical and commercial losses and improve customer service at these DISCOs.

Three, all new power projects, except perhaps hydro and nuclear, should henceforth with competitively tendered and their electricity traded on the upcoming power commodity exchange (CTBCM) and/or wheeled to private wholesale customers without any sovereign offtake guarantees. Policymakers, therefore, need to show some spine in resisting the rent-seekers’ desire to maintain status quo and finally discard the single-buyer model (chiefly responsible for the sector’s paralyzing circular debt) in favor of a market based multi-seller, multi-buyer structure.

Four, the state needs to get out of further LNG business and let the private sector procure the molecules internationally at its cost and risk, regassify those at the existing and future FSRU terminals, and sell the gas to industrial and commercial customers at deregulated prices via the Sui pipelines (under third-party access rules) or cryogenic bowsers. The federal government should only be concerned with the supply and allocation of locally produced natural gas per its stated socio-economic policy and constitutional provisions.

The dominant reason for the power sector’s debilitating circular debt is not DISCOs’ losses but the unaffordable, and continually increasing, input cost of generation due to various policy decisions from the 1990s onward. One can debate forever as to whether we contracted too much and too expensive IPP capacity under a take-or-pay arrangement, but that is all water under the bridge. The choice we now have is to either convince the IPP financiers to restructure their existing project debt by extending tenor and reducing margin, or to transfer a portion of such ‘stranded’ sectoral cost from the consumer electricity tariff into public debt. While there is no free lunch and the latter option may appear to be a zero-sum accounting ploy, it will however improve the competitiveness and sustainability of the overall power sector with potential collateral benefits for the entire economy.

If the energy market is properly liberalized under a regulatory framework, the public should benefit with cheaper and more reliable electricity and gas; however, some of our state-owned enterprises (such as DISCOS and the Suis) will go under if they remain obliged by the state to subsidize the leftover customers while continuing to bear the full economic burden of previous policy sins and errors. Such legacy, and indeed future ‘strategic’, costs should therefore be absorbed over the entire GDP as a budgetary line item. Building and maintaining a Strategic Petroleum Reserve infrastructure that could be used judiciously by the state during force majeure events, or to manage extreme volatility in the market as we saw during Covid-19, is another such example.

Finally, tacking climate change and achieving energy independence should be a key policy focus for the state. Not just for environmental but also economic and energy security reasons, we must develop and implement a holistic roadmap to achieving net zero carbon emission by 2050 or thereabouts. This goes beyond a 60 per cent renewable energy target by 2030; our aim should be close to 100 per cent power generation from wind, solar, hydro, and nuclear plants by mid-century. Green hydrogen (and associated ammonia for urea production) can also be part of the decarbonized energy mix as we are endowed with plentiful sunshine and wind in certain zip codes, the capital cost of electrolyzers is reducing worldwide, and international green financing is available for such ventures.

Even without subsidy support from the government, albeit under a policy framework, the private sector can launch e-mobility in the commercial space (buses, rickshaws, motorcycles) to reduce imported diesel and petrol consumption and pollution. Electrification of domestic and commercial space heating (via heat pumps or AC inverters) to save indigenous gas usage in the winters also requires appropriate differential pricing signals and green consumer financing options. Likewise, energy efficiency standards and conservation (via new building codes, for instance) already exist on paper but are not yet fully implemented. The World Bank and other multilaterals could finance the early buyout of existing oil-fired IPPs if the sale proceeds are ploughed back by their sponsors into replacement renewable energy assets under a Nepra-determined tariff regime.

There will, however, still be need for hydrocarbons in the hard-to-abate sectors of the economy. If there is one, and only one, additional energy project under CPEC, it should be to convert Thar coal into synthetic natural gas (95 per cent methane) and potentially other petroleum products. The technology already exists, with CO2 abatement, and at $25 per ton coal price the end-product should be competitive against imported LNG, if we can secure long-term concessional financing from China, alongside net FX savings in the long run. Concurrently, with imported coal at $300+ per ton, it is also critical for us to expeditiously link the existing imported coal power plants to Thar via railway lines.

In conclusion, there are no magic solutions or low-hanging fruits to instantaneously ‘fix’ the energy sector. What we need is clarity and buy-in on a few fundamental governance principles and a granular roadmap and set of work streams implemented consistently over the next 3-5 years to make this sector a net positive contributor to the national economy while providing affordable and reliable energy products and services to the people of Pakistan.

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