



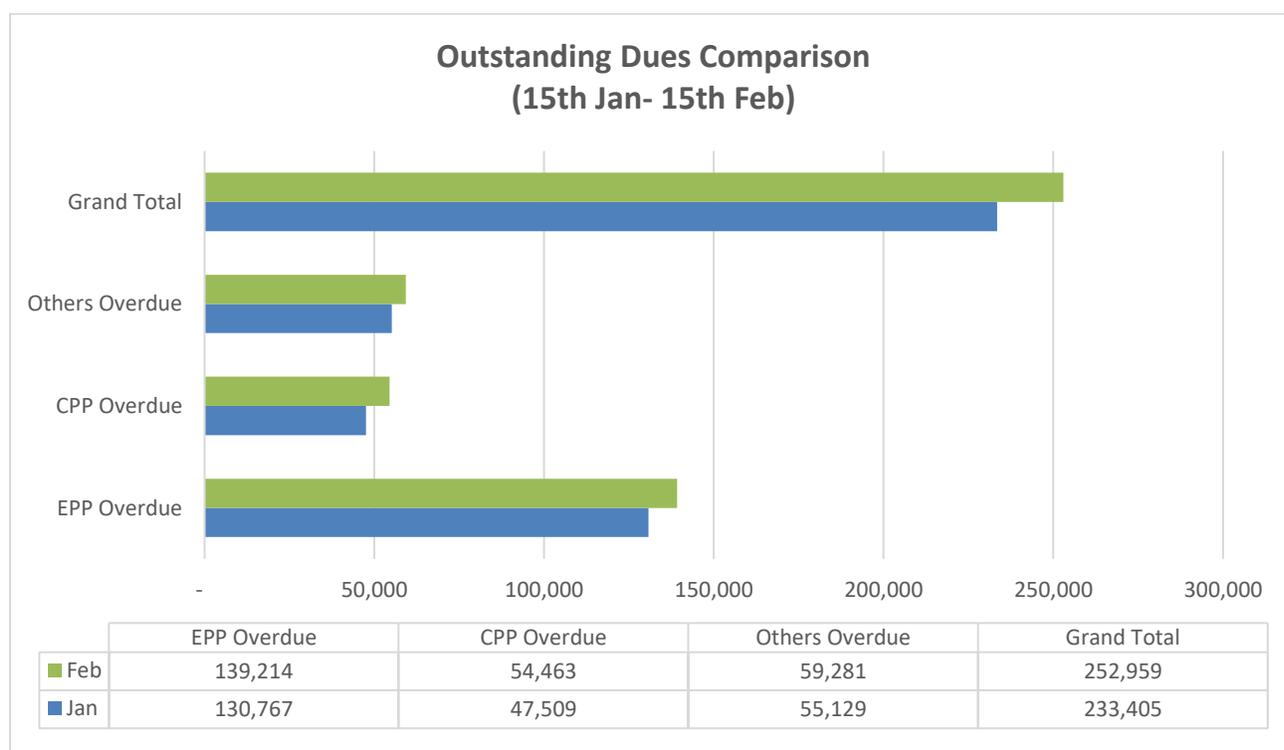
INDEPENDENT POWER PRODUCERS ASSOCIATION

MONTHLY NEWSLETTER

Welcome to the twelfth edition of Independent Power Producers Association (IPPA) Newsletter. The newsletter is published on a monthly basis to ensure regular dissemination of information to Member IPPs and other stakeholders, and also to provide a platform to discuss issues pertinent to the energy sector of Pakistan. We would like you to send us your feedback and comments on how to improve the monthly newsletter.

Monthly Infographics

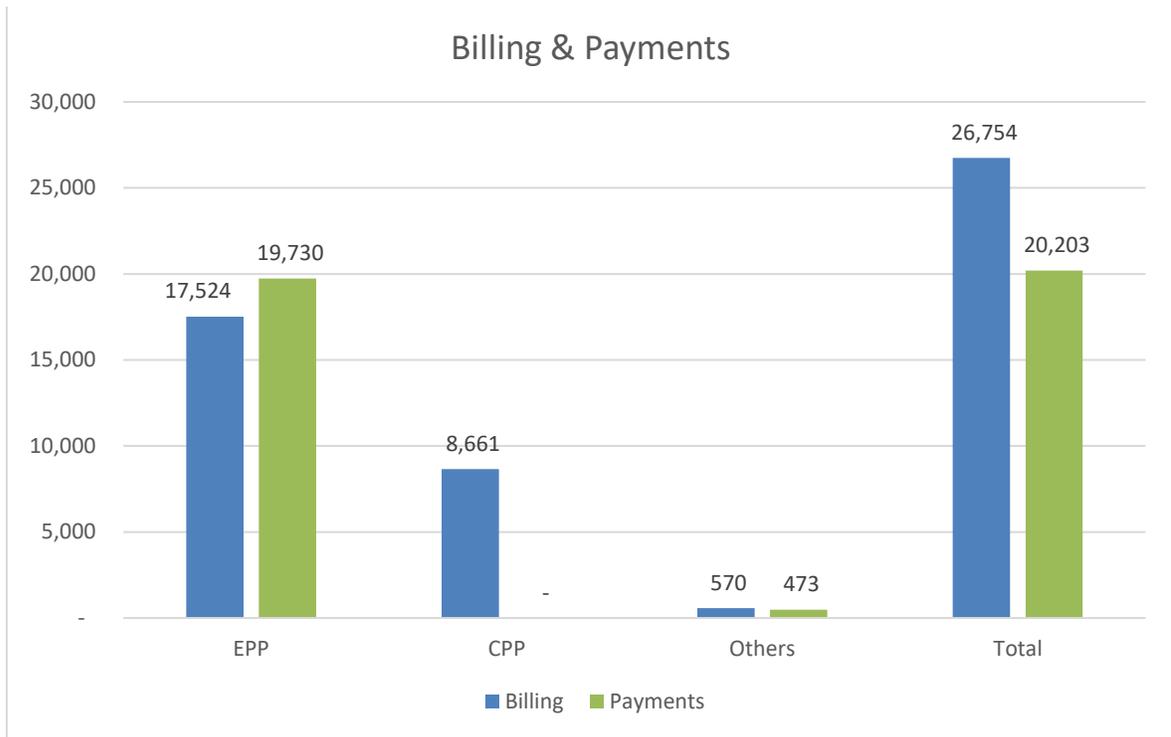
Outstanding Dues as of 15th February, 2018 in PKR Millions



Source: Member and Subsidiary IPPs

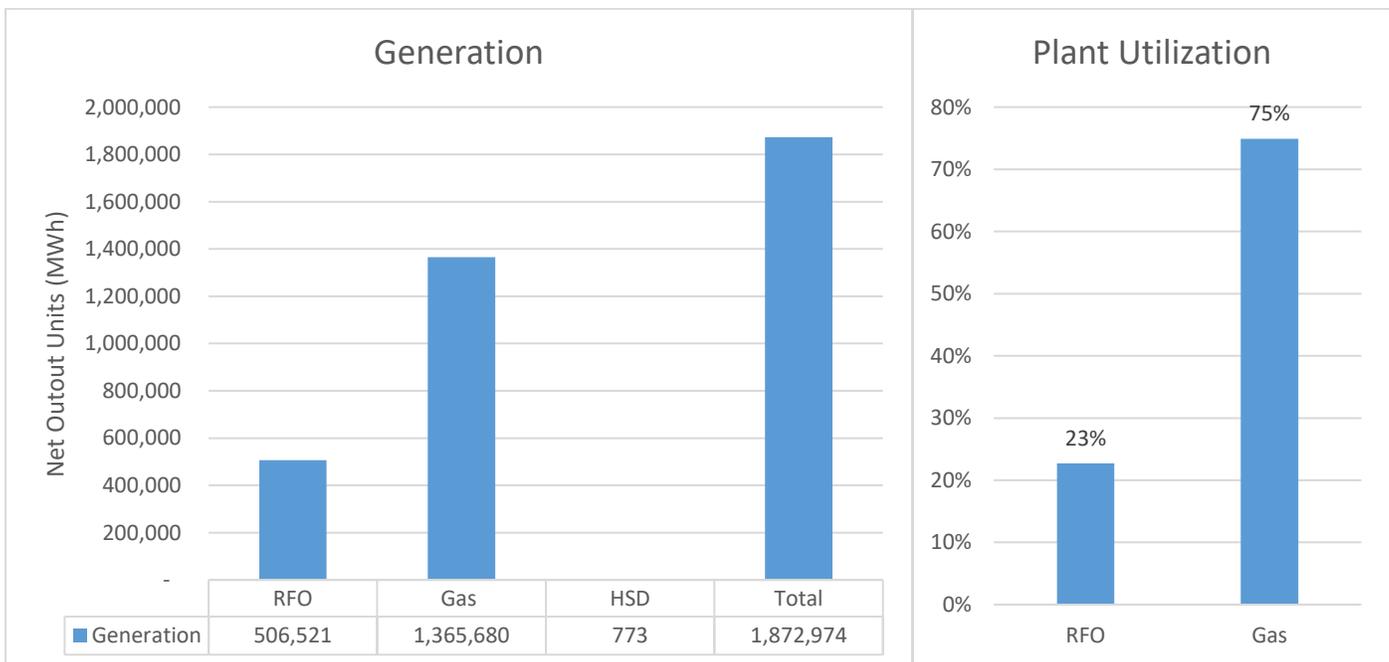
Monthly Infographics

Billing and Payments in February 2018 in PKR Millions



Source: Member and Subsidiary IPPs

Net Generation and Plant Utilization in February 2018

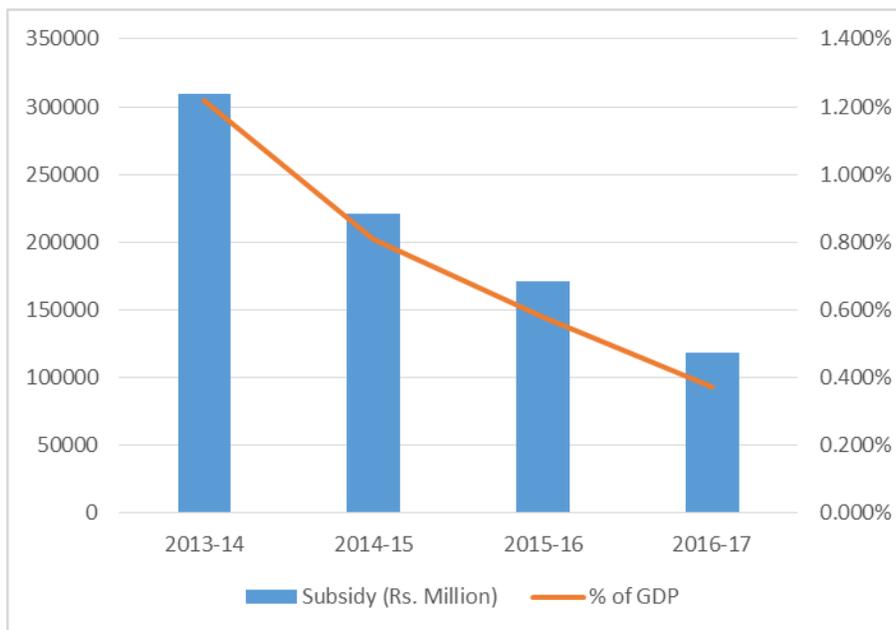


Source: Member and Subsidiary IPPs

Discussion: Electricity Subsidy

The official figure for circular debt has soared to 750 billion rupees, i.e. 56% higher than the amount inherited by the current government five years ago¹. This is an alarming situation calling for an urgent need to formulate comprehensive and dynamic long-term policy. The root cause of circular debt is cash flow crunch. There are several factors responsible for this discrepancy, including transmission and distribution losses, inefficient energy mix, subsidies and cross subsidies between the efficient and inefficient DISCOs, tariff and subsidy conflicts between the provincial governments and the DISCOs etc. However, this edition will focus on electricity subsidy.

Despite a downward trend in electricity subsidy, still, 0.37% of the GDP is used to provide subsidies to WAPDA/PEPCO and KESC (Federal Budget, 2017-18). As evident below, there has been a subsequent percentage decline in the subsidy reduction since 2013-14. Due to the adverse financial and welfare impact, even International Monetary Fund (IMF) has advised Pakistan to completely eliminate electricity subsidy².



Source: Data from Federal Budget (2013-17)

Financial Impact of Electricity Subsidy

The largest component of electricity subsidy is allocated to Tariff Differential Subsidy (TDS). Distribution companies (DISCOs) across Pakistan buy electricity from CPPA-G at different rates and have varied cost of operations. However, consumers across all distribution companies are charged a uniform rate. This gap between NEPRA approved rates and GOP notified rates is bridged through TDS.

However, the fiscal constraints faced by the Ministry of Finance impede its ability to make timely subsidy payments resulting in a liquidity crunch in the power sector. The incomplete and delayed

¹ 'Circular Debt' - Business Recorder

² 'IMF for ending inequitable subsidy on electricity tariff' - Khaleeq Kiana

subsidy payments is one of the major grievances of the power division of the Ministry of energy³. From a financial stand point, electricity subsidy is unsustainable and more like a never-ending vicious cycle which keeps getting bigger and bigger, exacerbating the circular debt situation. According to Federal Budgets, from FY 2013-14 to FY 2016-17, more than 819 billion Rupees have been spent on power sector subsidy alone. Moreover, if the current subsidy structure is maintained, the aggregate subsidy obligation may also increase with the increase in the supply of electricity. Therefore, unless the electricity subsidy for consumers is eliminated, the circular debt will keep building up.

Welfare Impact of Electricity Subsidy

It is often argued that even if granting electricity subsidy is not financially prudent, it is still necessary to continue the subsidy regime to benefit the poor households. This is a legitimate argument in the context of a developing country like Pakistan where a significant portion of the population does not have the purchasing power to consume electricity at unsubsidized rates. However, as the consumers are categorized into groups based on their consumption, and consumers from lower consumption slabs are provided with the subsidy, the welfare argument is hinged on the assumption that electricity consumption is related to household welfare

To explore the validity of this very assumption, World Bank carried out a study based on data from Pakistan Survey of Living Standards (PSLM), National Socio-Economic Registry (NSER) and monthly electricity consumption figures from DISCOs. The study concluded that the electricity consumption and welfare are weakly related⁴. The figure below also shows a relatively uniform consumption pattern across most income deciles. Majority of the consumers from most of the income deciles consume less than 300kWh/month which reflects that the consumption pattern is not indicative of financial status⁵.



Source: “Residential Electricity Subsidies in Pakistan: Targeting, Welfare Impacts, and Options for Reform”, by Walker et al.

Moreover, the consumer tariff is uniform throughout the year. Whereas, the consumption patterns change dramatically with variation in the seasonal temperatures. This uniform subsidy structure fails on two levels. First, during winter seasons, as the electricity consumption decreases, 13 percent of rich

³ ‘Circular Debt’ - Business Recorder

⁴ ‘Residential Electricity Subsidies in Pakistan: Targeting, Welfare Impacts, and Options for Reform’ - Walker et al.

⁵ ‘Residential Electricity Subsidies in Pakistan: Targeting, Welfare Impacts, and Options for Reform’ - Walker et al.

households fall into the lifeline subsidy slab⁶. Second, during the summer season, as the electricity consumption increases, poor households are no longer eligible for lifeline tariff⁷. This leads to the misallocation and poor targeting of electricity subsidy.

This poor welfare impact of electricity subsidy is not limited to Pakistan. Many countries adopt Inclined Block Tariff (IBT) and offer quantity based subsidies like Pakistan. In IBT, electricity price varies over several steps. Tariff increases as the consumption moves on to the next tariff slab⁸. Far from having a progressive impact, these subsidies in most cases do not even have a neutral impact. International evidence suggests that such subsidies have highly regressive benefit incidence⁹. This shows that the current subsidy structure is systematically flawed hence, it is bound to not only fail to achieve its welfare objectives but also in most cases worsen the situation.

Policy Recommendations

The core ingredient of any successful policy regime is strong political will. As discussed earlier the financial and welfare impact of electricity subsidy is poor. Several countries have been able to implement electricity reforms while curtailing the anti-government sentiment¹⁰. Therefore, the government should not have apprehensions towards subsidy elimination reforms.

However, it should be noted that successful policy reforms require a futuristic approach and long-term planning. Till date, the reduction in electricity subsidy has been done without any concrete supplemental measures. First, there is a need to bridge the communication gap between the public and policymakers. World Bank also carried out qualitative research to understand the public's attitude towards this issue. Research shows that the quality of electricity service provided is also important to consumers as is affordability. Respondents also showed a willingness to accept an increase in consumer tariffs if such reforms were supplemented by an increase in quality of service¹¹. A public relation campaign should be launched before enforcement of subsidy elimination. It should dispense awareness that electricity is currently subsidized, therefore increase in tariffs does not mean that the consumers will be overcharged but rather they will be charged the true cost of generation, transmission, and distribution. Moreover, they should also be assured that this will help in improving the overall quality of the service. When the public will witness improvement in the electricity sector as a result of these reforms, the public opposition will significantly drop. Moreover, the campaign should also address the concerns of the poor households who previously received subsidy but will not be able to maintain the same level of electricity consumption after the subsidy reform.

Concerns of these households can be addressed by providing them alternate social security network which does not have a regressive impact. One feasible and effective option is to give direct cash transfers to low economic households¹². Pakistan already has a safety net scheme i.e. Benazir Income Support Programme (BISP) in place. It targets the 15-20% of the poorest households in Pakistan¹³. Additional cash amounts can be dispersed through this program to mitigate the impact of increased tariff due to subsidy elimination. This will be a cost-effective solution as the framework of BISP is already in place.

⁶ 'Residential Electricity Subsidies in Pakistan: Targeting, Welfare Impacts, and Options for Reform' - Walker et al.

⁷ 'Residential Electricity Subsidies in Pakistan: Targeting, Welfare Impacts, and Options for Reform' - Walker et al.

⁸ 'Utility Subsidies as Social Transfers: An Empirical Evaluation of Targeting Performance' - Komives et al.

⁹ 'Utility Subsidies as Social Transfers: An Empirical Evaluation of Targeting Performance' - Komives et al.

¹⁰ 'Case Studies on Energy Subsidy Reform: Lessons and Implications' - Clements et al.

¹¹ 'Residential Electricity Subsidies in Pakistan: Targeting, Welfare Impacts, and Options for Reform' - Walker et al.

¹² 'Residential Electricity Subsidies in Pakistan: Targeting, Welfare Impacts, and Options for Reform' - Walker et al.

¹³ 'Residential Electricity Subsidies in Pakistan: Targeting, Welfare Impacts, and Options for Reform' - Walker et al.

However, it may be argued that some households may not qualify for BISP while they may require some assistance in the wake of subsidy elimination. In this regard, one-off cash transfers may be offered to such households during the initial period. These alternate measures of providing support, instead of current subsidy structure, will save huge sums of money which are lost currently due to misallocation of resources.

Moreover, simultaneously concrete measures should be taken to reduce the cost of electricity to the end consumer, so that in the future minimum help may be required from the government to help the poor households in purchasing electricity.

Our Members

	Member IPPs	Primary Fuel	Alternate Fuel	Gross Capacity (MW)	Net Capacity (MW)
1	The Hub Power Company (Tehsil Hub)	RFO	HSD	1292	1200
2	Pakgen Private Limited	RFO	-	365	350
3	Lalpir Private Limited	RFO	-	362	350
4	Kohinoor Energy Limited	RFO	-	131	126
5	TNB Liberty Power Limited	GAS	HSD	235	211
6	Uch Power (Private) Limited	GAS	-	586	551
7	Rousch (Pakistan) Power Limited	GAS	HSD	412	395
8	Habibullah Coastal Power (Pvt.) Co.	GAS	HSD	140	126
9	Attock Gen Limited	RFO	HSD	165	156
10	Atlas Power Limited	RFO	HSD	225	214
11	Nishat Power Limited	RFO	HSD	200	195
12	Nishat Chunain Limited	RFO	HSD	200	195.6
13	Liberty Power Tech. Limited	RFO	HSD	200	195
14	Orient Power Company Limited	GAS	HSD	229	213
15	Saif Power Limited	GAS	HSD	229	209
16	Sapphire Electric Company Limited	GAS	HSD	225	209
17	Halmore Power Generation Co. Ltd.	GAS	HSD	225	209
18	Engro Powergen Qadirpur Limited	GAS	HSD	227	217
Subsidiary IPPs					
19	Hub Power Company Ltd (Narowal)	RFO	-	220	214
20	Uch-II Power (Pvt) Ltd	GAS	-	404	375.2
21	Saba Power Company (Private) Limited	RFO	-	134	125.5

Upcoming Topics

April

Lack of Reliable Data

Established in 2010, IPPA serves as an advisory body for Independent Power Producers (IPPs) in Pakistan. IPPA liaises with the government and related departments such as NEPRA, SECP, WAPDA, CPPA-G, NTDC and PPIB and also serves as a facilitator between various IPPs and stakeholders within the power sector.

If you have any suggestions or feedback, kindly write to us at feedback@ippa.com.pk