

‘Irrational’ energy policies

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Pakistan has historically possessed some of the highest power tariffs in the region, which have not only hindered competitiveness over the years, but also raised pertinent questions about affordability. Our country’s energy tariffs have not been commensurate with the income levels of the general population, nor with regionally prevailing tariffs. Despite unreliable energy supply and higher tariffs, the textile sector has been operating at full capacity and receiving increased orders, leading to the revival of non-operational units, and the creation of new jobs. Textiles have been heavily supporting the economy, yet the industry’s profitability is being hampered by illogical energy tariff hikes and policies. In the past, the textile sector commended the Prime Minister for making Pakistan’s energy tariffs competitive with those in Bangladesh and India, but the current rate is 9 cents/Kwh which is well above average of 7 cents in the region.

The government has offered to offset the high energy tariffs with a DLT package, but this is an unsustainable solution as only direct exporters can benefit from it, whereas 80% of textiles comprise the chain as pictured below (Figure 1). Given the higher energy tariffs of our region, a domestic producer will not opt for local inputs while they can import them cheaply and without duty through DTRE and Bond. This policy, if followed through, will lead to rapid deindustrialization.

Exporters faced the brunt of the pressure from high energy tariffs, thereby facing a reduction in market share and leaving Pakistan far behind its regional competitors. This is also one of the prime reasons for the stagnation of exports, a fact which was duly acknowledged by the government when it announced regionally competitive tariffs back in 2018. However, over the last few months, there have been promising levels of export growth and positive impacts on industrial expansion and job creation. Minister for Commerce and Investment Abdul Razzak Dawood recently tweeted that the country’s exports have crossed the 2-billion mark in four consecutive months. Our exports for Jan 2021 are up by 8% to \$ 2.14 billion, compared to \$ 1.98 billion in Jan 2020, according to provisional figures. The exports for Jul-Jan 2020-21 have increased by 5.5% to USD 14.245 billion as compared to USD 13.507 billion during Jul-Jan 2019-20. Our cumulative exports for seven months of FY 2020-21 are showing a rising trend. The impact of this export growth on Pakistan’s economic stability cannot be overemphasized.

Exporters have achieved this feat despite difficulties, leading to a great degree of textile sector expansion. Value-added exports, including readymade garments, knitwear and other major exports have been showing substantial increases in both quantity and value. Large Scale Manufacturing (LSM) in Pakistan grew by 14.5 per cent in November 2020 as compared to the same month in 2019, data released by Pakistan Bureau of Statistics (PBS) showed. It is important to note that the SBP data is depicting a 5% drop in Textile exports whereas the PBS data is showing 10% enhanced exports over the last six months up to December 2020. The difference is entirely due to a disconnect in realization of proceeds and the change in terms of payment from suppliers due to COVID-19.

Pakistan’s electricity is currently in surplus: an excess of approximately 7,000 – 8,000 MW. The government seeks compliant consumers who will consume a mere 3,000 MW of electricity at a 9 cents/kWh tariff. As per a NEPRA’s notice from the previous month, 2.5 cents is the cost of fuel for thermal

power projects, while the rest is the fixed cost including debt servicing, management, etc. If we take 9 cents as total cost and deduct 2.5 cents from it, the remaining 6.5 cents is still available as a contribution towards capacity payments/fixed costs. The point to note is that whatever the cost, grid power is unreliable, with variations both in voltage and frequency, which result in substantial losses of production (in excess of 10%) in the newer electronic-based machinery. The industry has therefore made substantial investments and set up captive power so as to produce its own reliable and stable electricity. Even at a regionally competitive tariff of 7.5 cents, the government would be able to generate an excess of Rs.150 billion contributing to fixed costs. Ensuring the smooth flow and availability of electricity to all is the responsibility of the government, and this is certainly not the case at present.

The textile industry agrees with the government's intent to utilize the installed generation capacity of the country, as this is a suitable strategy to minimize the impact of past illogical policies. The transition from gas-based power to grid electricity could have, however, been better managed through a phased shifting of the load from captive power to the grid, while keeping the competitiveness of the industry intact through reasonable power pricing which would not increase the cost of doing business. Moreover, the integrity and quality of grid-supplied electricity can be ensured by taking on one industrial area at a time, and upgrading and modernizing the distribution system with appropriate quality controls, to ensure that the industry's power supply is stable and uninterrupted.

Furthermore, the inconsistent regulation between NEPRA (responsible for regulation of the power sector) and OGRA (responsible for the regulation of oil and gas sectors) sends mixed signals to consumers and investors, and creates disharmony in pricing strategies between gas and electricity. Additionally, since both are sources of energy, the misaligned tariffs on gas and electricity create opportunities for arbitrage in the system. To rectify this matter, prices must be set in equilibrium at \$6.5/MMBTU for gas and cent 7.5/kWh for electricity as one of the measures in establishing an efficient system design.

More issues are in store for the industry since the government has decided to suspend gas to industrial units, in an effort to tackle circular debt through enhanced usage of currently shut power plants, as well as to encourage electricity consumption and limit/control capacity payments. The supply of gas will continue to EOUs, even though the textile sector has rejected the proposal of moratorium of gas, and refused to use grid electricity. Suspending gas supply to industry at this stage where there has been an unprecedented growth in exports will hurt Pakistan's economy severely. Apart from production losses that'll compromise industry's and eventually Pakistan's credibility in performing orders, there will be adverse consequences from reduced exports, unemployment and loss on already made investments. The negative impact of moratorium on supply of gas will be far greater than making 450 MMCFD natural gas available for utilization to the power sector. To make matters worse, there is blatant discrimination wherein the industries falling in the jurisdiction of KPK and Sindh are likely to obtain a stay-order under Article 158 against the decision and will continue availing the gas supply, however, consumers in Punjab, having 70% of installed capacity, will suffer.

A key principle of industrial competitiveness is that unjust taxes and inefficiencies are removed and efforts are made to facilitate exports by the provision of internationally competitive inputs. Regional competitors easily capture market share with facilitation from their respective governments, while Pakistani industry flounders to get its voice heard. The current pricing would ensure that any move towards a free market would be stillborn. The cost of inefficiency would have to be borne by the consumers. Without the provision of a sufficient and continuous power supply at reasonable rates, it will be impossible to achieve

sustainable long-term growth rates. The matter can only be dealt with through the establishment of a competitive energy market, and until that happens, it is the government's responsibility to maintain reliable supply and keep rates at the internationally competitive level. There is a need to structurally reassess the power sector in Pakistan, which has consistently failed to provide reasonable prices or reliable supply, nor to remain consistent with the government's objectives.

Apart from being contrary to the principles of a market, an unwarranted reversal in competitive energy pricing would mark the beginning of a downward spiral for Pakistan's export industry, exports and ultimately the road to economic growth. One can picture the same problems recurring in a vicious cycle, from struggling before international donor agencies for additional loans, to struggling for the rollover of existing loans and deposits at the State Bank of Pakistan. The only path to sovereignty and economic growth for Pakistan is by a rapid increase in exports and the ability to compete in the international arena. It is high time those in power view the scenario from this perspective and reassess the broad consequences of the policies they propose.

Pakistan's energy crisis has persisted for decades, and power shortages are estimated to have cost Pakistan the equivalent of at least 3-4% of GDP each year since 2008, in direct output losses alone. In addition, the impact on jobs has been severe, especially in the industrial sector. We must remain cognizant of the fact that electricity is perceived as a fundamental "right" and consumers are not willing to pay for it (Burgess et al., 2020). This notion, coupled with Pakistan's unreliable supply, poor service, and weak infrastructure translates into Pakistan's energy sector, and as a consequence the economy and industry, being stuck in a "bad equilibrium."