



**Resources
Future**

What works and what does not

Power Sector Restructuring Options in Pakistan

1: Only sell good electricity distribution companies

Myth: Only good electricity distribution companies can be privatized. Investors will dislike the bad ones and may not view them favorably.

Not always true: Bad distribution companies are more attractive for investors from loss reduction perspective. If provided with a performance-based model, investors are well incentivized to improve performance. The selection of any of DISCO's assets for divestment should be based on the diagnosis of the operational and financial performance of all assets, and its Performance Improvement Plans (PIP) establishing the baselines and targets for future performance improvements (e.g. losses). This diagnosis is also important to classify the DISCOs and determine which ones are ready to be privatized vs. requiring restructuring vs. more suitable for other models.

2: Transfer out to Provincial Governments

Myth: Transfer all DISCOs to respective provincial governments, who would be fully responsible for controlling theft, improving supply, customer service, augmenting the distribution infrastructure.

Not a real reform: There is no evidence that transfer to provincial governments will improve operational performance. This model also involves limited private sector investment and would not necessarily address some core issues of the sector, such as inefficiencies leading to circular debt. This model mainly devolves the responsibility of the DISCOs from the federal to the provincial governments, who will continue to absorb the losses, subsidies and debt of the DISCOs. It is also unclear if all provinces have the capacity to take on this responsibility.

3: Ensure cost recovery method of electricity

Recover cost of supply, set a target of eliminating cross-subsidies within 2-3 years; bulk of the subsidy should be provided through direct channels of targeted subsidy like Ehsaas program

Critical: This is necessary to ensure that the DISCOs recover their revenue requirements. A glide path or subsidy plan should be put in place to reach full subsidy elimination. This is to ensure that no new debts are added to DISCOs' books due to factors beyond their control. This requires that all subsidies are budgeted for, and updated on an annual basis, with a true-up at the end of the year if the required subsidies differ from budgeted.

4: Restrict Federal Government to merit order dispatch regime

*Restrict the federal government financing & ownership to transmission infrastructure with merit order dispatch regime;
Remove transmission constraints to increase supply of Power*

Important: This needs to be supported by transmission planning to ensure security of supply from a national perspective, which is not necessarily the incentive of the private sector. Furthermore, a strong system operator and dispatch regime is critical for an efficient power system.

Abolish all distribution exclusive license and allow private sector players to openly compete in the retail segment

Important: Introducing competition could reduce the risk of abuse of monopolistic market power, which can lead to lower quality and higher tariffs.

Control theft and increase recoveries, install AMI technology to control leakages before restructuring and privatization

Important but not a pre-requisite: Not necessarily a prerequisite for privatization; what is more important is the availability of regulations and judicial actions to treat theft and nonpayment. Furthermore, the private sector may be more effective in reducing losses if the right incentive is in place (e.g. performance-based model)

AMI - Useful, but not necessarily a prerequisite for privatization; such investment can be done by the private sector. Furthermore, given that AMI takes time, it can be first targeted to large customers to be most effective.

7: Break up DISCOs to make them operationally viable

Break up larger DISCOs and split DISCOs into smaller units along the lines of settled urban areas versus rural area

Not a pre-requisite: DISCOs should not be broken up simply because they are too large. The size of DISCOs matters less for privatization than their operational and financial conditions. Furthermore, splitting DISCOs along urban/rural lines may result in the concentration of customers that require high costs of connection/service and/or are difficult to enforce in the same DISCOs, making their operation challenging.

Condition of not firing any employee for a defined period of 3 years, together with a Voluntary Golden Handshake after that.

Important: Assessment of staffing and skills at the DISCO level, with actions for restructuring/restaffing is important for smooth privatization. It is expected that labor productivity would be one area that private sector involvement can help improve. Such condition would affect the financial situation of the company and may not be attractive to the private sector. Instead, the Government can put in place a retrenchment plan with sufficient benefits for affected employees.

Payment of Government arrears and ensure timely payment of public sector electricity bills in the future

Critical: Public sector accounts for a large share of receivables and the reform actions should include mechanisms to clear arrears and ensure systematic payment of bills to reduce the losses of DISCOs that are in the Government's control.

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