# IMF programme and energy crisis

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**Pakistan has less than US$3 billion in foreign reserves, enough to finance less than three weeks of imports. It owes more than US$9 billion in principal and interest payments in the next few months. Even if the principal payments are deferred through negotiations, payments on account of debt servicing will remain.**

Leaving aside domestic debt, the markup on foreign debt in the current fiscal year stands at Rs 511 billion. Beyond that, the Pakistani rupee has dropped to a historically low value by almost Rs 100 in a year.

Imports are not coming in, disrupting supply chains, and forcing industries to stop production. Industries are laying off workers amid more than 27% inflation. Pakistan needs to get the deal done with the IMF to keep its economy going.

The most critical issue facing Pakistan and became the central point in Pakistan-IMF discussion is the staggering US$15 billion energy sector circular debt — US$ 9.6 billion in the power sector, and the remaining in the gas sector.

After holding critical talks under the ninth review of the 23rd IMF Extended Fund Facility arrangement, the IMF states about enhancing energy provision by preventing further accumulation of circular debt and ensuring the viability of the energy sector.

Pakistan is in dire need of deep and long-overdue structural reforms in the energy sector. Yet again, for reducing the energy sector deficit, the ultimate solution coming out from IMF-Government negotiations, it seems, is the increase in electricity tariffs by 33%, equivalent to Rs 7.65 per kWh in the average base tariff, in addition to quarterly adjustments — not different from the earlier suggested solutions.

As discussed in a PIDE commentary on the 23rd IMF Programme for Pakistan, why do we always emphasize increasing prices and passing the burden on to consumers without worrying about structural energy issues? PIDE research has highlighted that tariff increases without structural changes lead to more inefficiencies and sector losses.

No realization at the government level that an increase in tariffs expands the black hole in the power system, halting efforts to reduce aggregate transmission and commercial losses. Any tariff increases lead to a higher financial gap.

Apparently, average T & D losses were reduced in FY2022 compared to FY2021. But due to the increase in tariffs, the financial loss to the national exchequer increased from Rs 71 billion to Rs 123 billion. While the financial loss due to low recoveries increased from Rs 39 billion to Rs 170 billion.

In its press release, the IMF pointed towards reducing untargeted subsidies and scaling up social protection to help the most vulnerable and those affected by the floods.

> Over the last ten years, energy subsidies have exhausted fiscal resources immensely. Reportedly, the IMF also discussed a reduction in energy subsidies for lower-slab consumers (300 units or less).

But the government resisted this move, obviously for political reasons. The burden of tariff increase will be on high-end consumers.

About half of the total electricity consumed is in the domestic sector. The tariff structure is progressive for domestic consumers. On average, 75-80% of domestic consumers use 300 or fewer units of electricity.

There is ample evidence that the households opted for options to remain in lower slabs, for instance, two to three meters in a residential premise dividing load, tampering with meter or electricity theft, or payment of a fixed amount to the lower staff of a company.

Now houses with net-metering facilities have also reduced their billed units to less than 300. In other words, those consuming less than 300 units are not necessarily lifeline or low-end consumers. Then what's the point in protecting these at the cost of consumers falling under high slabs?

The energy tariffs are already high due to governance issues, operational, financial, and commercial inadequacies, inept policies, and sub-optimal energy mix.

The policymakers try to cover all these inefficiencies through subsidies or by charging a higher tariff to industry, commercial and high-end residential consumers.

Why not equally distribute the burden of costs of energy service and target the actual lifeline consumers through scaling up the social protection program, as pointed out in the IMF press release?

Industry, with a consumption share of 26% in total, is the second largest recipient of tariff-related subsidy, and rightly so. This sector (along with the commercial sector and high-end domestic consumers) is cross-subsidizing 75-80% of domestic and all agriculture consumers. Thus, compromising its international competitiveness.

Only increasing tariffs (in the past) has not resolved the circular debt. Eliminate all subsidies and cross-subsidies. Although, easier said than done politically. But that's the solution. Without doing it, it would be challenging to obtain fiscal discipline.

The best way is to move from increasing block tariff to a flat linear tariff without slabs and consumer differentiation. It will not only minimize inefficiencies but will have a positive impact on the sector's financial health.

It will hurt poor households. Unlike tariff differential subsidies, direct cash transfers through social protection schemes is a better welfare alternative. In the same manner, small agricultural consumers can be protected.

The elimination of cross-subsidy will bring down industrial tariff automatically.

Until or unless a tariff structure in which service costs are not recovered from all consumer categories indiscriminately is not implemented, fiscal challenges for the government will remain.

Besides, the power sector needs decentralization of decision-making and management overhaul. Sector issues, such as line losses and bill collection, need to be resolved by the DISCO management instead of the centralized energy ministry.

Once all companies are made responsible and accountable for all their decisions and finances, it will improve the financial viability of the power sector. Pre-paid smart meters are a must not only for bill transparency and demand management but also for enhancing the sector's economic viability.

The same goes for the gas sector, where domestic resources are going down speedily. Pumping in money will help only for the time being. Pakistan should de-regulate the natural gas sector and liberalize the pricing structure.

The government must begin passing LNG costs to consumers. Otherwise, the circular debt will continue to inflate, as in the power sector.

Why do we need IMF to put our house in order? We can do it ourselves if we have the will.