

# Developing Electricity Market

Afia Malik



On November 12, 2020, NEPRA has approved the detailed design and implementation plan of Competitive Trading Bilateral Contract Market (CTBCM) of electricity. NEPRA has given the timeline of 18 months for preparation and implementation. The model envisages that all the future contracts for the sale/purchase of electricity will be bilateral between the parties, that is, sellers - generation companies and buyers - distribution companies or bulk power consumers.

Pakistan's power sector does need a market, no doubt. The basic aim of the reform model introduced in the early 1990s was to develop a competitive electricity market. Other reform measures including unbundling, deregulation and privatisation were merely transitory stages to move towards a free market. The idea was to achieve cheap pricing for consumers through competition in generation and supply and shift decision making from government to the market.

As part of these reforms, Pakistan unbundled its electricity sector into generation, transmission and distribution. Private investors were also allowed in the generation sector. But in the absence of competitive bidding, we ended up in long term contracts with sovereign guarantees.

The anecdotal evidence suggests that the performance of our electricity system is worse today than what it was in 1990s, when the reforms were initiated. One of the reasons quite possibly is that we left the reforms half way through. Secondly, we were not fully prepared to implement reforms when these were initiated; the restructuring was undertaken only in haste under influence of the donors. The result is in front of us - the end consumer tariffs are high, the government is still a decision-maker, and though we have a separate regulator but with insufficient authority.

In early reforming developing countries, the most successful were the ones with strong governments and political will for reforming the power sector. These countries established a competent and independent regulatory framework; eventually moving towards a free-market. In Pakistan, political and bureaucratic capture is strong; it resists any change.

The detailed design of CTBCM has been prepared by an international consultant for the Central Power Purchase Company (CPPA-G). Once again, the entire exercise is under the advice of the donors and consultants. The government has decided to develop a wholesale market in the next two years and the retail market in the next five years. Are we prepared for this structural change? Or will we repeat the mistake we committed over two decades ago?

The electricity market is complex; it needs a design, developed keeping in view the ground realities and after consultations with all the stakeholders. The stakeholders include not only the industry but also the politicians, judiciary and academia etc. A national consensus, which has not been developed so far, is essential before the envisaged reforms can be successfully undertaken.

The electricity wholesale market, to function efficiently, must meet the following pre-requisites:

A financially viable sector and a reliable payment chain are crucial for a market to function. The creditworthiness of all, in particular, distribution utilities is critical. Presently, the power sector is not fully solvent, its deficit, that is, circular debt, is rising continuously and has reached an all-time high of Rs. 2.4 trillion. The inefficiencies in the distribution sector are responsible for more than 50 pc of this deficit. High transmission and distribution losses and less than optimal recovery rates are adding to this deficit; besides increasing the tariff for compliant consumers.

A large power system with several buyers and sellers is required. Unfortunately, we do not have enough buyers and sellers to compete. On the generation side, all the independent power plants and even the three state-owned generation companies despite being inefficient are all under take-or-pay contracts – which guarantees 60 pc of payments (capacity charges) to generation companies even if the government fails to buy the electricity.

In the CTBCM, because of take-or-pay contracts, the distribution companies (DISCOs) would be required to provide a credit cover for future procurement of power. This will not be possible, given the current poor balance sheets of the DISCOs. If buyers, that is, DISCOs, are financially unsound how the envisaged wholesale and retail power market will function? Moreover, the benefits of competition are unlikely to pass to end-users if market power is concentrated either in the generation or in the distribution sector.

A transmission infrastructure with sufficient capacity to carry all the electricity generated is required. This unfortunately is not fully available.

A non-discriminatory governance structure for the market operator and system operator is essential. Though government owned, Central Power Purchase Company (CPPA-G) is an independent market operator but it has a clear bias favouring DISCOs.

Finally, a stable macroeconomic, political and social environment is necessary for the market to develop and function. Institutions play a crucial role in the success of any market, not just electricity. The dismal state of our institutions and governance failures need no mention.

The bottom line is that the current conditions are not feasible for the development of a full-fledged market in electricity. Our best bet then is to start with the 'wheeling of power' – electricity transmission from a producer to a user in the same balancing area or from one area to another. This would be a precursor to market development. NEPRA should facilitate 'wheeling' by discouraging the hurdle creating entities.

DISCOs being averse to competition are creating hurdles; CPPA-G is supporting them. An example is an increase (as suggested in CTBCM) in wheeling charges to incorporate the inefficiencies of DISCOs. Inefficiencies in DISCOs are due to mismanagement. Even if some IPPs were to agree, to revise their contracts from take-or-pay to take-and-pay; a massive increase in wheeling charges would discourage them. The market will collapse before formally taking off.

The electricity market is complex; it requires legal, financial and human capacity at every level. Build this capacity first.

*It is time for a sustainable energy policy which puts consumers, the environment, human health and peace first.*

**Dennis Kucinich**