

PAKISTAN'S ENERGY SECTOR CHALLENGES



ECONOMIC POLICY
& BUSINESS
DEVELOPMENT



Pakistan's power sector has evolved from a fundamental economic driver into a systemic liability threatening national economic stability. The sector currently faces multiple critical challenges including expensive surplus electricity generation, escalating capacity payments, and unsustainable fiscal pressure that collectively impede economic growth and industrial competitiveness.

Current policy responses have proven counterproductive and structurally unsound. Gas prices for captive power generation have been increased to Rs 4,291 per MMBTU (\$15.38), with further increases planned to reach Rs 6,000 per MMBTU (\$21.5) by August 2026. This policy artificially renders industrial self-generation uneconomical rather than addressing the fundamental inefficiencies in the national grid system. Such measures undermine competitiveness in key export sectors including textiles and cement manufacturing, sectors vital to Pakistan's economic stability.

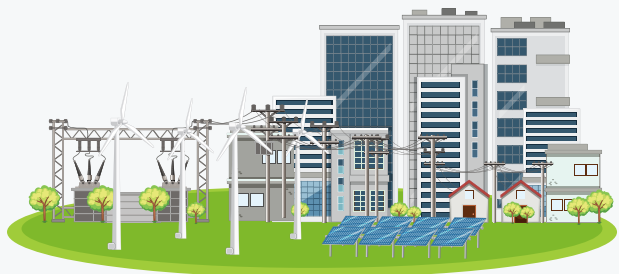
The current policy approach contradicts global market trends, as Pakistan paradoxically imports expensive LNG at \$10-12/MMBtu while curtailing domestic gas production that costs less than \$4/MMBtu. SNGPL's management of surplus RLNG—deferring Qatari cargoes, offloading Eni cargoes, and diverting 250 MMCFD into the pipeline network—directly contributes to the gas sector's circular debt, which now exceeds Rs. 2.7 trillion. The proposed bank consortium arrangement for Rs. 1.275 trillion with a Debt Service Surcharge of Rs. 3.23 per unit may provide temporary relief but fails to address the structural causes of debt accumulation.

Simultaneously, significant barriers have been erected against renewable energy adoption. Recent regulatory changes have slashed purchase prices for excess solar electricity from Rs 27 to Rs 10 per unit, replaced net metering with gross metering, and imposed GST on self-consumed solar power. These policy reversals have extended investment recovery periods from 3-4 years to over a decade, effectively halting progress in a sector that had achieved significant momentum with 226,000 net-metering consumers and projected installed capacity of 4,124 MW.

The fiscal implications extend beyond the power sector itself. The Petroleum Levy, already maximized at Rs 60 per liter, faces pressure for further increases to cross-subsidize electricity tariffs. This approach creates market distortions while failing to address the core structural deficiencies: transmission and distribution losses averaging 16.5% nationwide (with certain distribution companies like PESCO and SEPCO exceeding 35%), capacity payments surpassing Rs 2 trillion, and circular debt exceeding Rs 2.4 trillion as of end 2024.

The reform imperative has gained additional urgency following recent commitments to the International Monetary Fund (IMF) made in early 2025. The government has pledged to maintain cost-reflective tariffs, halt new electricity and gas subsidies, and implement a comprehensive Circular Debt Management Plan. This plan will convert Rs 1.252 trillion of circular debt to CPPA debt through bank borrowing, repaid via a Debt Service Surcharge over six years. A temporary subsidy mechanism funded through the Petroleum Development Levy will provide interim tariff relief while structural reforms take effect. These IMF commitments create an external accountability framework that could accelerate implementation of necessary reforms, with technical assistance from the World Bank and Asian Development Bank supporting these efforts.

Six critical reform pathways must be prioritized for meaningful sectoral transformation:



First, the single-buyer model must be replaced with a **competitive electricity market structure** allowing direct transactions between generators, distributors, and consumers.



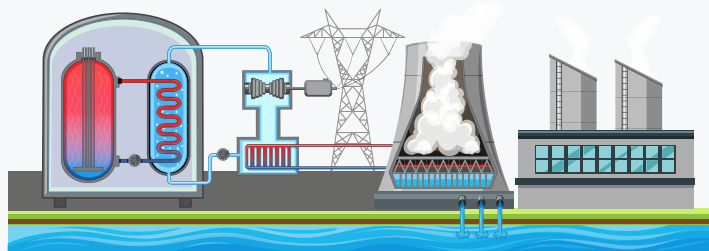
Third, **strategic rebalancing** of the generation mix away from the current 60% dependence on imported fuels (RLNG, coal, and furnace oil) toward indigenous and renewable resources.



Fifth, establishment of **policy coherence** that recognizes decentralized generation & renewable adoption as complementary to grid modernization rather than threats to be suppressed.



Second, aggressive reduction of technical and commercial losses through **smart metering infrastructure**, improved billing systems, and fundamental distribution company reforms.



Fourth, implementation of the **Weighted Average Cost of Gas (WACOG)** pricing at the national level, offering a mixed price of local and imported gas to consumers like captive industry who have the appetite and need to buy WACOG-based gas. This approach would save Pakistan's gas infrastructure while creating a balanced and sustainable gas market.



Sixth, implement transparent **Third Party Access** protocols enabling private B2B arrangements while diversifying procurement beyond G2G deals. RLNG pricing for industry should reflect actual costs without cross-subsidies or inflated charges, restoring competitiveness as global LNG markets transform with 170 MTPA of new capacity by 2030

It is crucial to recognize that market-oriented reforms are complex and presuppose a power system that is already largely developed, adequately governed, and financially secured. Countries like Colombia, Peru, and the Philippines achieved positive outcomes from power sector reform because they met these basic conditions before embarking on liberalization.

Peru's experience is particularly instructive—after fully restructuring its power sector by 1994, it attracted approximately \$16 billion in private investment over 20 years across generation, transmission, and distribution networks (World Bank)¹. The creation of an effective sector regulator and wholesale power market institutions drove efficiency to best-practice levels and significantly reduced energy costs.

The economic consequences of inaction are severe and potentially irreversible. Without these structural reforms, Pakistan risks continued economic stagnation, deteriorating industrial competitiveness, and worsening fiscal imbalances.

The power sector's transformation must be recognized as a national economic priority requiring immediate, coordinated policy intervention across multiple domains to create a sustainable energy ecosystem capable of supporting Pakistan's economic development objectives.

¹ <https://www.worldbank.org/en/news/feature/2019/09/10/rethinking-energy-reforms-in-power-hungry-world>