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Increasing capacity payments to IPPs has made electricity hyper expensive. Critically evaluate the statement and give recommendations.

PROLOGUE

"Increasing capacity payments to IPPs has made electricity hyper expensive. Crony capitalism in Pakistan's energy sector is evident in the expensive IPP agreements that disproportionately benefited politically connected individuals and entities. Fixed capacity payments to IPPs, circular debt, lack of transparency in contracts, over-contracting power generation capacity relative to actual demand have made electricity hyper expensive. To make electricity affordable it is vital to diversify country's energy mix; furthermore, there is dire need to renegotiate IPP contracts, improve energy efficiency, strengthen ~~demm~~ regulatory oversight, address circular debt.

GENESIS OF IPPs IN PAKISTAN

The genesis of IPPs in Pakistan can be traced to the **Private Power Policy of 1994**. Under this policy, private investors were allowed to set up power generation projects under long term take-or-pay power purchase agreements at extremely attractive rates.

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CRONY CAPITALISM IN IPP AGREEMENTS

Crony capitalism in Pakistan's energy sector is exemplified by the expensive IPP agreements that have disproportionately benefited politically connected individuals and entities. These agreements were often negotiated under non-transparent conditions, where conflicts of interest and insider influence led to signing of contracts with overly generous terms, including high guaranteed returns and capacity payments. Through these deals some politicians and their allies secured ownership stakes or favourable contract terms.

CRITICAL EVALUATION

CAPACITY PAYMENTS TO IPPs

Capacity payments are fixed payments made to IPPs to ensure that they have the ability to produce a certain amount of electricity, whether or not that capacity is fully utilized. These payments are intended to cover the fixed costs of power plants including capital recovery and maintenance

OVERCAPACITY AND UNDERUTILIZATION

Pakistan has over-contracted its power

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generation capacity relative to its actual demand. This overcapacity means that even when power plants are underutilized, the government still has to pay the full capacity payments. This inefficiency directly translates into higher costs, which are passed on to consumers in the form of higher electricity tariffs.

IMPACTS ON ELECTRICITY PRICES

The high capacity payment have indeed contributed to making electricity expensive. The fixed costs associated with capacity payments are embedded on the overall tariff structure. As the demand for electricity fluctuates, the cost per unit of electricity can rise sharply if the capacity payments are not spread out over a sufficiently large volume of consumed electricity.

LEGECY CONTRACTS AND LACK OF TRANSPARENCY

Many of the agreements with IPPs were signed at the times of energy crisis, where the priority was to rapidly increase generation capacity rather than ensuring cost efficiency. This led to signing of contracts that are now seen overly generous to IPPs. There is also criticism over the lack of transparency in these contracts and some have questioned whether the

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terms are fair and sustainable in the long run.

CIRCULAR DEBT

The high cost of electricity, driven by capacity payments and other factors, has contributed to Pakistan's notorious circular debt problem. When consumers and distribution companies are unable to pay for electricity, it creates a backlog of unpaid bills that affects the entire supply chain. This financial strain exacerbates the cost issues in the sector.

RECOMMENDATIONS

RENEGOTIATION OF IPP CONTRACTS

The government should consider renegotiating the terms of Power Purchase Agreements (PPAs) with IPPs to align the capacity payment with actual demand. This could involve paying in PKR (adjusting the currency dom denomination of payments, revising return on equity, or extending the contract periods to spread out the costs.

DIVERSIFICATION OF ENERGY MIX

Reducing reliance on expensive fossil fuel based IPPs by increasing the share of renewables in the energy mix

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can help lower operational costs once established and do not require capacity payments.

IMPROVING ENERGY EFFICIENCY

Investing on energy efficiency measures, such as upgrading the transmission and distribution network to reduce line losses can help power the overall cost of electricity. Reducing technical and non technical losses would decrease financial burden on the energy sector.

STRENGTHENING REGULATORY OVERSIGHT

The National Electricity Power Regulatory Authority (NEPRA) should enhance its oversight and ensure that any new PPAs are aligned with long-term interest of the country. This includes transparent bidding processes and ensuring that contracts are not overly favourable to IPPs at the expense of consumers.

ADDRESSING CIRCULAR DEBT

The government should implement a comprehensive plan to address circular debt: including improving bill collection efficiency, reducing subsidies that distort pricing, and ensuring timely payments across

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the energy supply chain

CONCLUSION

The statement that increased capacity payments to IPPs have made electricity hyper expensive in Pakistan is largely accurate but it is part of a broader set of issues in the energy sector. To address these challanges, a multifaceted approach is required including renegotiation of contracts, diversification of energy mix, improving efficiency and transparency in the sector. These measures, if implemented effectively can help stabilize electricity prices and reduce the financial burden on the economy.

US-China rivalry is shaping into increasing currency war where US wants the continuation of dollarization of international trade while China wants to dedollarize it. Analyze

The US-China rivalry is increasingly being played out in the realm of global finance, particularly through their competing efforts to either sustain or diminish the role of the US dollar in international trade. This struggle reflects broader geopolitical and economic tensions between the two superpowers, each seeking to influence the global economic order in a way that aligns with their strategic interests.

THE US PRESPECTIVE: MAINTAINING DOLLAR HEGEMONY

The US has long benefitted from the dollar's status as the world's dominant reserve currency. The dollarization of international trade means that a significant portion of global transactions, particularly in commodities like oil and gold, are conducted in the US dollar. This provides several advantages for the US:

ECONOMIC POWER AND INFLUENCE

The dollar's dominance allows the US to exert significant influence over global trade and finance. It provides US with the ability to impose economic sanctions effectively, as many international transactions involve US financial institutions or dollar dominated exchange.

LOWER BORROWING COSTS

The demand for dollars keep US interest rates lower than they might otherwise be, reducing the cost of borrowing for the US government and businesses.

TRADE DEFICIT MANAGEMENT

The US can sustain large trade deficits more easily because other countries are willing to hold dollars in the reserves, effectively lending the US money by purchasing US Treasury bonds.

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THE CHINESE PESPECTIVE : DE-DOLLARIZATION AND FINANCIAL SOVEREIGNTY

China, on the other hand, sees the dollar's dominance as a constraint on its economic and political sovereignty. Dedollarization the process of reducing reliance on the US dollar in international trade, is a key component of China's broader strategy to reshape the global financial system in a way that diminishes US influence and enhances China's own economic security.

DEDOLLARIZATION AND CHINA'S AMBITION OF A NEW WORLD ORDER

Dedollarization is a critical component of China's ambition to establish a new world order, as it seeks to challenge the dominance of the US in global financial and geopolitical spheres. By reducing reliance on US dollar, China aims to promote the yuan as a viable alternative for international trade and finance, thereby increasing its influence in global economic systems. De-dollarization will allow China to create a more multipolar world order where power is more evenly distributed among major global powers. Moreover it will give China a position to shape rules and norms of international order.

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BREAKING THE DOLLAR'S GRIP: CHINA'S TACTICAL MOVES TOWARDS GLOBAL DEDOLLARIZATION

CURRENCY SWAP AGREEMENTS UNDER BRICS

China has signed currency swap agreement with approximately ~~20~~ 40 countries of the world including BRICS counries. These agreements are aimed at enhancing financial cooperation and reducing reliance on US $ dollar. China and Russia have made a currency swap agreement of 150 billion yum in 2014, India and Japan in 2018, South Africa and China in 2015, UAE and India in 2018. These agreements are part of BRICS's strategy to enhance trade relations and reduce dependence on Western financial systems.

ESTABLISHING THE CROSS-BORDER INTERBANK PAYMENT SYSTEM (CIPS)

To facilitate Yuan's internationalization, China has developed the Cross-border Interbank Payment System (CIPS). It was launched in 2015 as an alternative to US dominated SWIFT system. CIPS allows global banks to clear and settle cross-border Yuan transactions directly without the need for a dollar intermediary. As of 2023, CIPS has expanded its network to include hundreds of financial institutions worldwide, including major internat

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banks.

BRICS AND NEW DEVELOPMENT BANK

New Development Bank (NDB) established by BRICS, aims to provide an alternative to Western-dominated financial institutions like World Bank, IMF. It offers loans and financial products in currencies other than dollar. This supports the broader goal of creating a ~~m~~ world where dollar is not the sole dominant currency.

CHINA'S EFFORTS TO DITCH PETRODOLLAR SYSTEM

China's efforts to ditch the petrodollar system are closely linked to the pursuit of a more balanced and multipolar global economic system. The petrodollar system, where oil is predominantly traded in US dollars, has been a cornerstone of dollar's global dominance, reinforcing US economic and geopolitical power. China is world's highest energy demand center then comes India. China wants to buy in local currency. ~~Putin's~~ Xi's visit to Middle East in 2022 was instrumental where it was decided that China ~~will~~ would buy oil from gulf countries on local currencies.

ROLE OF BRI IN DEDOLLARIZATION

Many projects under BRI are financed by China in Yuan. This not only supports

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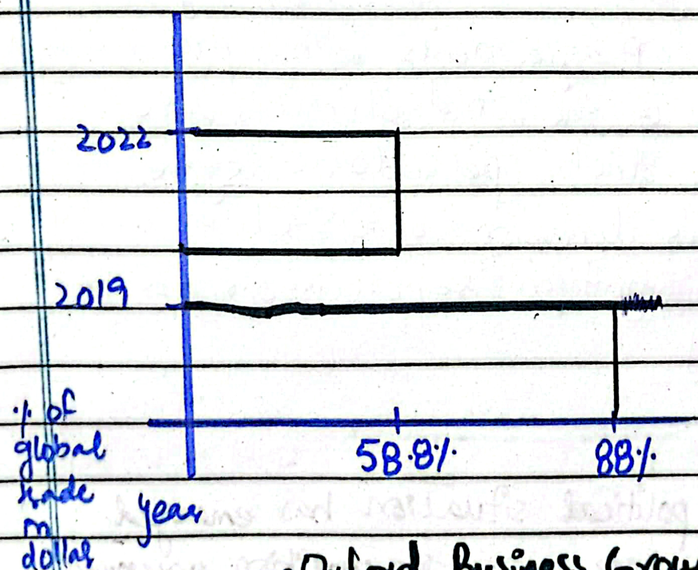
supports the internationalization of Yuan, but also integrates these countries into China's economic sphere, further diminishing their reliance on the dollar.

DEDOLLARIZATION EFFORTS YIELDING FRUITS

The efforts of China to dedollarize the world economy are yeilding fruits. According to a report by **Oxford Business Group 2022**, 88% of global currency trade in 2019 was in US dollars, but by 2022 this share dropped to 58.8%.



• Oxford Business Group

In 2022, Saudi Arabia and Turkiye traded Russian and Chinese goods in yuan and ruble. In August 2023, India and UAE started settling bilateral trade in their local currencies. New Dehli purchased

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a million barrels of crude oil in Indian rupee. On 20 December 2023, Russian Deputy Prime Minister told that in 2023, 95% of Russia-China trade was done in ruble and yuan.

CONCLUDING REMARKS

Currency war has emerged as one of the most significant dimension of US-China rivalry. China want to dedollarize the world economy while the US is working to maintain dollar's hegemony. China's dedollarization efforts are yeilding fruits as global trade in dollars is reduced to 58% of the total global trade. China has signed currency swap agreements with approximately 40 countries of the world. China is also working to ditch petrodollar regime.

In short, this dimension of US-China rivalry will have significant repercussions for the US economy.