

CURRENT AFFAIRS

QUESTION NO: 2

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

Capacity Payments:

Definition: Capacity payments are fixed payments made to independent Power Producers (IPPs) to ensure that electricity generation capacity is available, whether or not the electricity is actually produced.

Purpose: These payments are designed to cover the fixed costs of power plants, ensuring that they remain operational and ready to meet demand, especially during peak periods.

Capacity payments are fixed charges paid to IPPs to ensure that power generation capacity is available, regardless of whether the electricity is used. This model, which was designed to attract investment in the 1990s, has now become a burden due to several factors:

Over capacity:

Pakistan's electricity generation

capacity now exceeds its actual demand, meaning that consumers are paying for unused electricity. This is primarily due to generous terms offered to IPPs, which have resulted in a capacity far beyond what is required, especially during non peak times.

Background:

First major chunk of installed IPP in 1994 and then the following years 2005, 2011, 2014 but in those times the leaders didn't gave long term solution but used local solution to shortage of electricity such as big generators were installed that run at Coal, diesel, and LNG.

Peak times: and loads:

In winters there is less demand of electricity than in summer which is more than double. about 28000 MW plus demand per day in summers 2022 to 2023. July. where as in winters from Jan 2023 - Jan 2024 the demand was below 14000 MW

Peak months include May, June, July, August.

Moderate seasons include March, April, September, October, November

In winters including month of Dec, Jan, February requires less electricity.

If Pakistan is not even able to buy 1 MW of energy but still Pakistan has to pay 35% which is capacity payment.

In 2023 June there was a loan of 200 - 300 million \$ loan on Pakistan of capacity payment but now in 2024 4000 trillion Rps loan is on Pakistan.

Devalue of Rupees:

Since, Pakistan has to pay in dollars the price of per unit electricity. But the rupee is devalued but still have to pay in dollars though dollar value is rised. This had led to increased payments to IPPs, further driving up electricity costs.

Circular Debt:

The high value of cost of electricity, driven by capacity payments, has contributed to a growing circular debt problem. This debt arises when the government fails to pay power producers, which then struggles to pay fuel suppliers, creating a vicious

Cycle that drives electricity prices even higher.

Current rate of Electricity:

Pakistan's government, led by shehbaz sharif, has raised the electricity base tariff for domestic consumers to PKR 48.84. This increase approved by NEPRA, excludes those using up to 200 units per month for three months

Recommendations:

1- Renegotiate IPP contracts:

The government should consider renegotiating contracts with IPPs, focusing on reducing capacity payments and adjusting terms to be more aligned with current demand and economic realities

2- Diversify Energy Sources:

Increasing the share of renewable resources in the energy mix could help reduce dependence on expensive fossil-fuel-based IPPs and lower overall electricity costs.

3- Improve Efficiency:

Enhancing the efficiency of electricity distribution and reducing transmission losses can help lower costs for consumers.

4- Strengthen local manufacturing:

Encouraging local manufacturing of energy equipment could reduce costs related to imports and mitigate the impact of exchange rate fluctuations.

5- Reforming the Power Sector:

Strengthen regulatory oversight to ensure that IPP contracts are fair, transparent, and in the public interest.

5.1) Debt management:

Implement strategies to manage and reduce the circular debt in the power sector, which is exacerbated by high capacity payments.

Conclusions

While capacity payments are initially intended to ensure energy security, they have now become a significant factor in the high cost of electricity in Pakistan. Addressing this issue requires a combination of policy changes, contract renegotiations, and shift towards more sustainable energy resources.