

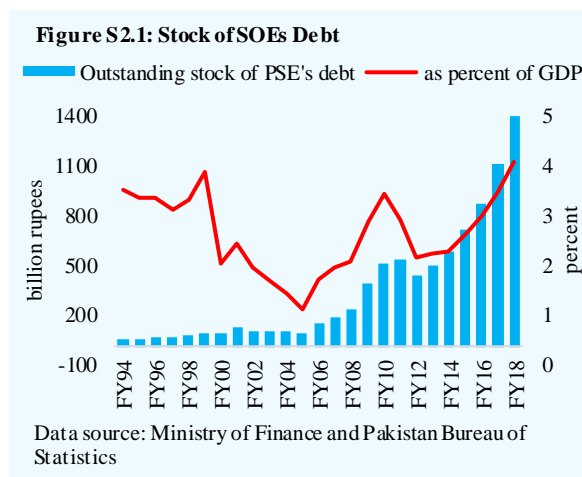
Special Section 2: Evaluating the Fiscal Burden of State-owned Enterprises in the Power Sector¹

S2.1 Introduction

The performance of state-owned enterprises in Pakistan is typically characterized by weak financial management stemming from poor governance, excessive staff recruitment and political interference in day-to-day operations. Over the past couple of decades, the consistent loss accumulation by some SOEs and their fiscal spillovers have prompted successive governments to initiate policy-oriented and institutional reforms in these entities. However, commitment issues have persisted. Privatization agendas were also formulated, but the progress remained lackluster due to recurring financial losses, non-viability of commercial operations and other structural bottlenecks.

In the absence of decisive policy actions, problems in financially constrained SOEs have exacerbated, leading to heavy debt accumulation by these entities

(**Figure S2.1**). This section intends to evaluate on a macro level the financial position of the SOE sector as a whole and provide perspectives on the assessment of actual fiscal burden these enterprises incur. The section particularly highlights the role of sectoral policies and overall business conditions in the power distribution sector, which has hampered the financial performance of associated SOEs.

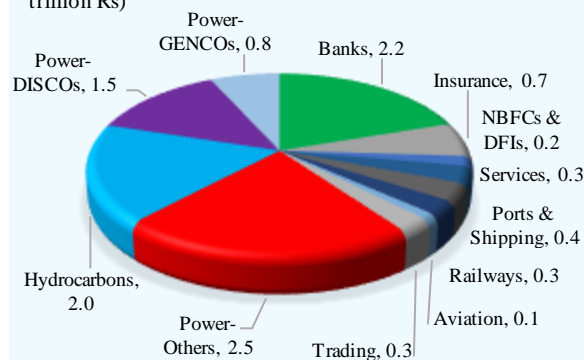


¹ This special section draws heavily from various published documents including “Circular Debt, Issues and Solutions” presented to Senate, different editions of “Federal Foot Print - SOE Annual Report” published by Ministry of Finance, different editions of ‘State of Industry Report’ by Nepra and financial reports of related entities. In addition, our discussions with National Electric Power Regulatory Authority (Nepra); Ministry of Finance, Power Holding Private Limited (PHPL), Central Power Purchasing Agency (CPPA), Islamabad Electric Supply Company (IESCO), Sukkar Electric Power Company (SEPCO) and commercial banks were useful in developing insights about the sector.

S2.2 Current size and aggregate financial position of SOEs

The aggregate assets of state-owned enterprises (SOEs) have increased by 11.3 percent CAGR between FY13 and FY16, and stood at Rs 11.5 trillion (US\$ 110.3 billion) at end June 2016. This large asset base, spread across 197 entities, is equivalent to around 40 percent of Pakistan's GDP (**Figure S2.2**). Energy predominantly constitutes the bulk of SOEs' business. Right from upstream activities (oil & gas exploration), these entities are engaged across the entire energy sector value chain in the country. Their involvement in financial business also remains strong, as public sector institutions (comprising 20 percent share in aggregate financial sector assets) continue to operate along with the private institutions. Transport, storage and communication is another area where SOEs are operating while also enjoying a near-monopoly in their segments, especially in the case of railways (Pakistan Railways – PR) and international aviation (PIA).

Figure S2.2: Sectoral Classification of SOEs' Assets (in trillion Rs)



Data source: Federal Foot Print 2015-16, Ministry of Finance

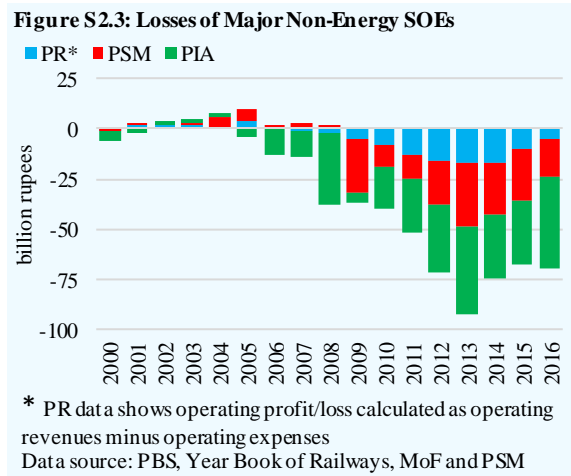
Table S2.1: Net Profit/Loss of SOEs
billion rupees

	2012-13	2013-14	2014-15	2015-16
Total SOEs	163.5	193.5	52.9	-44.8
Commercial	158.2	217.6	67.4	-43.9
1. Energy	225.6	256.5	125.0	6.0
Hydrocarbons	173.8	225	145.7	115.4
Power	51.9	31.5	-20.7	-109.4
2. Financial	19.3	32.6	36.3	34.5
3. Industrial & engineering	-24.6	-23.4	-25.7	-17.8
Pakistan Steel Mills	-28.4	-25.8	-25.7	-18.8
4. Trading	3.4	7.1	1.3	0.2
5. Services	-2.9	-3.8	-10	-6.6
6. Promotional & advocacy	1.4	1	3.1	1.8
7. Transport	-65.5	-54.3	-52.4	-62.8
PIA	-45.1	-30.7	-32.1	-45.3
Pakistan Railway	-30.5	-32.5	-27.2	-27.0
Non commercial	-	1.7	0.3	1.2
DFIs	5.3	6.2	5.6	7.4

Data source: Ministry of Finance

As shown in **Table S2.1**, the overall SOE sector had posted a net *profit* of Rs 410 billion between FY13-FY15. This performance owed primarily to healthy earnings of entities operating in the upstream energy and financial sectors, which more than offset the losses incurred by the entities operating in power distribution, industrial and transport sectors. However, the situation reversed in FY16, when the drag from loss-making entities increased significantly and more than offset the earnings of profitable entities (a sharp fall in global crude prices had led to a decline in revenues of oil and gas exploratory firms). This resulted in the net loss of Rs 44.8 billion in the aggregate SOE sector during the year. In terms of dispersion, however, more than 80 percent of the entities posted operating profits during FY16, whereas 55.6 percent were able to post strong bottom lines.

This basically suggests that, though large in size, losses in the SOE sector are limited to only a few entities. Among these, transport and industrial entities, such as Pakistan Steel Mills, PIA and Pakistan Railways, have posted persistent losses over the past decade due to overstaffing, operational inefficiencies, regulatory bottlenecks and lack of new investments (**Figure S2.3**). Policy-related issues are also partly responsible; their role is evident in sub-par performance of private operators in these sectors (especially aviation). The issues of service quality also crop up from time to time. While these entities are off the privatization list, structural revamping plans in these entities are being mullied over.



In the meantime, the most pressing issue that has emerged in recent years is of the circular debt, which has escalated financial constraints of the energy sector SOEs. As shown in **Table S2.2**, these entities have contributed the most to overall SOE debt accumulation as well as fiscal support over the past few years.

S2.3 Losses in some SOEs are high, but the aggregate fiscal burden needs careful assessment and attribution

The government provides details of its support to SOEs in an annual publication, “Federal Footprint – SOE Annual Report”. According to this document, the

support mechanism includes subsidies, loans and grants provided by the federal government to these entities. Guarantees are also included since these represent contingent liabilities of the government. However, in order to assess the overall impact of SOEs' financial health on the fiscal accounts, one must understand the nature and objective of this support and also account for the revenue stream that the government generates from the operational activities of SOEs.

First, the support: as shown in **Table S2.2**, subsidies are the heaviest item on government's books. The bulk of these subsidies are energy-related, and represent the government's policy decision to provide electricity to consumers at below-market price.

Technically, this expense comprises the difference between the Nepra-determined power tariff (based on the generation cost, margins, T&D losses of Discos) and the tariff notified by the government. It is important to highlight here that end-consumers, not the PSEs, are the beneficiaries of the subsidy [thus, it is not surprising to see that the K-

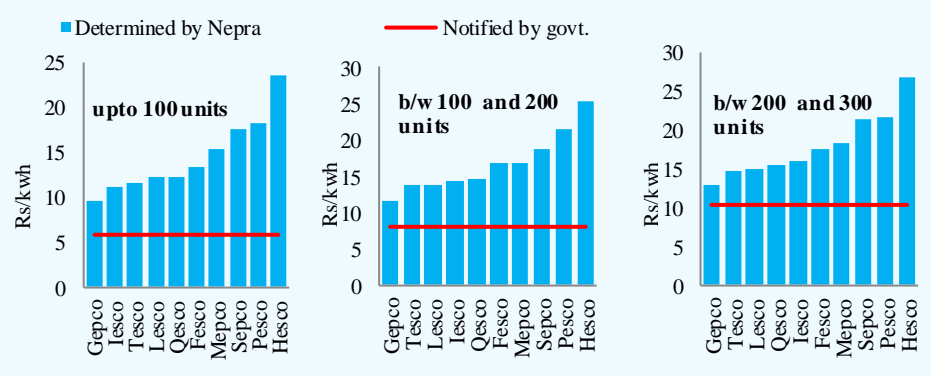
Electric, which is the only generation and distribution company in the *private* sector, was the recipient of one-third of total energy-related subsidies during the past 3 years]. This is because: (i) subsidies represent the government's effort to unify the electricity tariff across the country despite a wide disparity in Discos' efficiency levels; and (ii) these also shield consumers from the impact of high input costs and inefficiencies across the energy value-chain. As shown in **Figure S2.4**, for household consumers who consume up to 200 units of electricity, the government notifies the tariff at a level which is even lower than what Nepra determines for most efficient Discos. Certainly, political considerations make it hard for the federal government to pass on the impact of prevalent inefficiencies in the power sector value-chain to end-consumers.

Table S2.2: Annual Fiscal Expense on SOEs
billion rupees

	FY13	FY14	FY15	FY16
A. Loans	80.4	150.5	110.3	181.3
o/w Energy sector	29.6	57.5	29.0	80.2
B. Guarantees	123.6	99.7	154.8	128.5
o/w Energy sector	103.1	57.0	96.0*	114.2
C. Subsidies	281.2	271.8	229.3	223.1
o/w Energy sector	260.0	228.0	221.0	171.2
D. Grants to Pakistan Railway	35.4	33.5	37.0	37.0
E. Total support (A+B+C+D)	520.6	555.5	531.4	569.9
F. Fiscal expense (A+C+D)	397.0	455.8	376.3	441.4
as % of GDP	1.8	1.8	1.4	1.5
G. Total income/revenues	75.8	133.0	88.3	146.3
as % of GDP	0.3	0.5	0.3	0.5
Mark- income	12.3	67.0	14.2	57.7
Dividend income	63.5	65.9	74.1	88.5
H. Net expenditures (F-G)	321.2	322.8	324.0	295.1
as % of GDP	1.4	1.3	1.2	1.0
as % of FBR Revenue	15.7	13.6	11.5	8.7

*Since decomposition of guarantees was not available for the year, this number was calculated by subtracting guarantees to PIA from total guarantees (for other years, this amount was almost equal to guarantees to the energy sector)

Data source: Federal Foot Print SOE Annual Report, 2015-16, 2013-14, MoF, PBS

Figure S2.4: Difference b/w Tariff Determined by Nepra and GoP Notified Tariffs for Different Consumer Slabs

Data source: SRO 01 (I)/2019, Ministry of Energy, Government of Pakistan

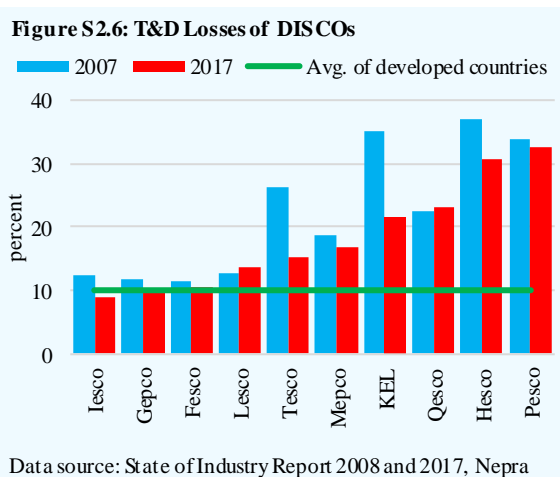
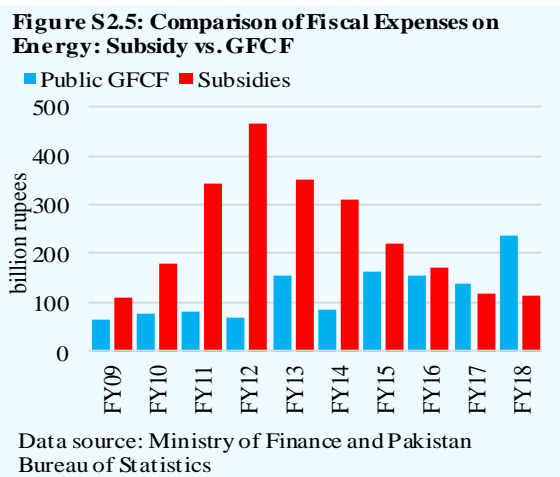
This practice of allowing untargeted subsidies has two negative fallouts. First, the unintended consequence of implementing a unified tariff across the country is that it feeds into inefficiency. Specifically, in the current scheme of things, Nepra penalizes inefficient Discos by allowing certain percent of transmission and distribution (T&D) losses to be included in the base tariff, with additional losses eating into the Discos' earnings. However, by absorbing Discos' losses via subsidies, the government alleviates public pressure on inefficient Discos to put their house in order. This practice also lifts pressures from inefficient power producers who continue to use more expensive fuels for thermal generation. On aggregate, this inter-Disco tariff differential subsidy constitutes 60 percent of the total subsidy expense budgeted for FY19 (**Table S2.3**).

Table S2.3: Subsidies Profile
billion Rs

	Revised Estimates		Budget
	2016-17	2017-18	2018-19
Subsidy to Wapda/Pepco	102.6	81.5	134.0
Inter-Disco tariff differential	91.0	57.5	105.0
Tariff differential for agriculture tube wells in Balochistan	1.7	0.0	5.0
To pick up Wapda/Pepco receivables from FATA	9.9	10.0	12.0
Subsidy to Wapda	0.0	14.0	12.0
Subsidy to K-Electric:	15.4	33.5	15.4
To pick up K-Electric's tariff differential	10.2	11.0	15.0
For tariff differential for agriculture tube wells in Balochistan	0.6	0.4	0.4
Subsidy to Discos & K-Electric on A/c. of industrial customers	4.7	22.1	0.0
Total power sector subsidies	118.0	115.0	149.4
Overall subsidies	169.0	147.6	174.7

Data source: Budget in Brief for Fiscal Year 2017-18 and 2018-19

The second fallout is that over the past decade, subsidies have eaten up the bulk of fiscal resources, leaving fewer resources for capacity expansion/upgradation (**Figure S2.5**). Although public investments picked up some pace between FY15 and FY18 (including FDI inflows), these were concentrated heavily in power generation. Expansion and up-gradation of distribution infrastructure (for instance, installing high voltage transformers and smart grids; discarding obsolete grids; ensuring safety protocols such as proper earthing and plugging current leakages) was mostly left for Discos to manage, who consistently underinvested in the area due to financial constraints, mis-governance, and commitment issues. As shown in **Figure S2.6**, no major improvement was seen in T&D losses in the distribution sector, except for the privatized K-Electric, and the company responsible for power distribution in tribal areas.



As far as loans to SOEs are concerned, it is clear that the bulk of loans to SOEs is actually PSDP spending by the government in strategically important sectors like roads, energy and transport. Specifically, the government's development expenditures in these sectors comprise of loans to the relevant entities. In FY16, for instance, half of the loans to SOEs were received by National Highway Authority for the completion of various public projects, such as Faisalabad-Khanewal expressway; Lowari tunnel and access roads; and CPEC funded Thakot to Havelian section. In the energy sector, major recipients of development loans were Neelum-Jhelum hydropower project and National Power Parks (for the

completion of LNG-based power plants in Baloki and Haveli Bahadurshah). Importantly, the mark-up that the federal government charges on development loans to SOEs is slightly higher when compared with the SOEs' cost of borrowing from commercial banks (**Table S2.4**).

Table S2.4: A Comparison of SOEs' Borrowing Cost from Federal Government and Commercial Banks

	Rate of mark-up chargeable on development loans by the federal govt.*	Weighted average lending rates on bank lending to non-financial PSEs (end June)**
FY15	10.53	6.8
FY16	7.37	6.66
FY17	6.5	4.98
FY18	6.62	7.04

Data source: *Notification No. F.8(2)GS-I/2018-196, Ministry of Finance, **State Bank of Pakistan

As for the revenue stream for the government, the two major sources from SOEs are mark-up income on government loans to these entities, and the dividend income from the profit-making entities. Combining these two sources, the government earned 0.4 percent of GDP on average between FY13 and FY16. This suggests that in overall terms, the actual (net) burden of SOEs on the fiscal account, which has been expensed out, was on average 1.2 percent of GDP and 12.4 percent of FBR's revenues during this period.

However, it is important to note that a major fiscal burden has not been expensed out yet: the guarantees. While notional amounts of government guarantees during the previous 3 fiscal years were large (**Table S2.4**), the real concern lies with their accumulated volume (PSE debt), which has touched 4 percent of country's GDP by end December 2018. It is important to recall here that the federal government encourages SOEs to borrow directly from commercial banks to finance their capex as well as working capital needs. However, the disaggregated data showed that nearly half of these guarantees (46.5 percent) merely represented cash flow constraints in the energy sector stemming from circular debt. At end December 2018, banks' exposure to Power Holding Private Limited (on whose books the bulk of circular debt is parked) increased to Rs 516.5 billion². To alleviate this burden, the government has recently issued Sukuks worth Rs 200 billion, following which the state-owned CPPA was able to make payments to power generation companies. However, such measures would be effective only in the short-term; for a sustainable functioning of the sector, a massive overhaul is needed as described below.

² In overall terms, energy sector entities constituted 73 percent of the total lending to SOEs by commercial banks at end December 2018

S2.4 Improvement requires a massive overhaul of the sectoral policy, not just SOEs' inefficiencies [Case Study: Public Sector Discos]

Disaggregated data shows that in the energy supply chain, the hydrocarbon sector comprised of oil and gas exploration firms, refineries and OMCs, has been making decent profits over the past decade. The margins, however, shrink once the focus is shifted towards the electricity generation and distribution sector, where most of the entities are making substantial losses (**Table S2.5**). When it comes to losses (and thus the need for fiscal support) incurred by Discos, the reasons typically boil down to the issue of managerial and technical inefficiencies prevailing in these entities.

Table S2.5: Net Profit/Loss of Key Energy Sector Entities
billion rupees

	FY13	FY14	FY15	FY16	FY17	FY18
OGDCL (67.5%)	91.3	123.9	87.2	59.97	63.8	78.74
Parco (60%)	13.1	10.4	13.6	18.8	NA	NA
GHPL (100%)	24.0	25.8	24.3	18.1	20.3	27.5
PPL (67.5%)	42.1	50.9	38.4	17.2	35.7	45.7
PSO (22.5%)	12.6	21.8	6.9	10.3	18.2	15.5
SSGC (53.2%)	0.4	-3.8	-5.4	-6.1	1.3	NA
Genco-II (100%)	-3.3	-2.4	3.8	-1.5	NA	NA
Genco-I (100%)	0.7	1.5	0.8	-2.4	0.7	0.3
Genco-III (100%)	-4.3	-5.1	-1.5	-3.9	0.7	NA
Wapda (100%)	20.5	23.2	33.3	19.5	17.0*	NA
NTDC (88%)	59.4	7.3	8.9	9.2	10.6	14.7
Gepco (100%)	7.1	-1.6	5.8	10.2	7.5	-5.0
Tesco (100%)	-5.1	-2.3	0.9	0.2	NA	NA
Iesco (100%)	10.2	22.7	2.7	-7.7	-11.9	-27.3
Mepco (100%)	11.9	9.9	9.8	-10.3	-17.9	-33.8
Lesco (100%)	13.8	10.4	-8.9	-11.2	NA	NA
Fesco (100%)	24.1	29.5	5.2	-13.3	-14.2	NA
Pesco (100%)	-32.5	-34.4	-15.1	-14.5	-19.4	-43.0
Sepco (100%)	-19.4	-14.8	-17.7	-21.7	NA	NA
Hesco (100%)	-16.5	-12.6	-19.8	-27.2	NA	NA
Qesco (100%)	-13.8	9.1	-35.1	-34.6	NA	NA

*Hydroelectric-Neptra regulated business. Figures in parenthesis represent government's share in entities
Data source: Ministry of Finance; Companies' Annual Reports

In particular, low recoveries, large T&D losses and governance problems have left little cash with these entities over the years that could have been invested for the up-gradation of transmission and distribution infrastructure. While this line of reasoning can easily be validated by poor financials of most Discos, it is equally important to highlight the role of the prevalent policy and regulatory practices in explaining some of the financial woes of the distribution sector. To understand this phenomenon, three major aspects stand out:

(i) Even the most efficient Discos are facing serious financial constraints:

The case in point is Islamabad Electric Supply Company (Iesco) and Faisalabad Electric Supply Company (Fesco). These Discos are incurring T&D losses equivalent to those in developed countries (**Figure S2.6**). On the recovery side also, Iesco and Fesco have appreciably high recovery rates of 92 and 97 percent, respectively. It is not surprising, therefore, that these two have consistently been

at the top positions on the regulator’s (Nepra) performance evaluation ranking, outperforming the only Disco operating in the private sector (K-Electric).

Despite the performance advantage, however, the entities incurred operating losses between FY16 and FY18. Importantly, these entities were enjoying steady net profits up till FY16, when their bottom-lines were hit by a snag in the determination of multi-year tariff (MYT). In

Table S2.6: Different Components of MYT Determination: Iesco’s Case

Adjustments	Requested by Iesco	Granted by Nepra
Return on rate base	18.85%	11.83%
Return on equity	19.0%	16.67%
Cost of debt	16.15%	3m kibor+2.75
Prior year adjustment (billion Rs)	1.0	-10.8
Additional recruitment	10,304 persons	None

Source: Various tariff petitions of Iesco extracted from website of Nepra

In 2015, Nepra introduced multi-year tariffs (MYT) for some profit-making discos in order to prepare them for privatization (**Box SS2.1**). Although these Discos had themselves requested for the MYT, they were dissatisfied with the notified tariffs, and filed a petition against the decision with Nepra (**Table S2.6**). Later, these Discos sought legal recourse for the reconsideration of notified tariffs; the government (Ministry of Energy) lodged a complaint in the high court on behalf of the affected Discos. In 2017, the court decided in favor of the enterprises, advising Nepra to revise the tariffs.

Importantly, for the years ending FY16, FY17 and FY18 when their tariff determination was under litigation, these companies had to bill their customers as per the tariff last notified (in 2015). This meant that the growth in electricity revenues could not keep pace with the expense on electricity purchase. After the court verdict, Nepra re-determined their tariffs (in September 2017), but marked the same as post-dated; the expenses of the past couple of years were ultimately borne by the enterprises, and they had to incur financial losses. By FY18, when the MYT regime was eventually revised, the net loss of Iesco had accumulated to Rs 46.9 billion between FY16 and FY18. Fesco, on the other hand, had incurred a cumulative loss of Rs 27.5 billion during FY16 and FY17 (it has withheld its financial statement for FY18).

This suggests that tariff determination and associated procedural delays also create financial challenges for Discos. As per the report presented in the Senate, titled “Circular Debt: Issues and Challenges”, delays in determination of consumer tariffs contributed almost a third to gross receivables of Central Power Purchasing Agency, which is responsible for power procurement for Discos.

Box SS2.1: Multi-year Tariff Regime

Under the “Regulation of Generation, Transmission and Distribution of Electric Power Act 1997” Nepra is responsible for determining tariffs and other terms and conditions for the entire electricity supply chain including generation, transmission and distribution. To determine tariffs of distribution companies, Nepra practices two different methods: (i) Single Year Tariff Regime (SYT) for annual tariff determination; and (ii) Multi Year Tariff Regime (MYT) for more than a year.

The MYT is a framework for regulating return/profits of entities over a period of time, keeping in view their projected revenue and cost stream. The methodology of MYT adjustment takes into account multiple factors, including future power purchase cost, transmission cost, and cost of capital. Specifically, the MYT is based on (i) indexation/adjustments of various components of distribution margin; (ii) targets of T&D losses; and (iii) future investments for the MYT period. Moreover, certain costs such as variation in power purchase price (PPP) and delay in notification leading to prior year adjustments (which comprise of under/ over recovery of the different components of tariff) are adjusted in a timely manner to ensure sustainability of operations.

Discos prefer to get MYT regime since: (i) MYT is considered less volatile and is subject to fewer intra period adjustments, which may reduce the frequency of revisions in base tariff and cost of capital; (ii) the MYT puts in place a performance-based tariff structure where Discos get benefits of improved efficiencies and lower T&D losses; (iii) it protects companies against uncontrollable risks, such as unexpected changes in PPP; and (iv) it reduces the frequency of regulatory protocols (e.g., time required for petitioning and hearings).

(ii) Qesco's recoveries are suppressed due to a 10-year long subsidy on tubewells, and delays in subsequent tariff notifications

Qesco is incurring one of the highest T&D losses and lowest recovery ratios of the power distribution industry. Over 75 percent of the electricity being supplied by Qesco is utilized by agriculture consumers for running tubewells. Between 2001 and 2010, a subsidy was given for tubewell connections: agri consumers were to pay Rs 4,000 per month of the bill, and the remaining amount was to be borne by Qesco, the government of Balochistan and the federal government in a ratio of 30:30:40, respectively.

With the completion of initially announced duration, the subsidy program ceased for a period of 27 months, but was later restored with effect from December 2012. Importantly, no clarification/notification was provided for the distribution of dues across farmers, Qesco, and the provincial and federal governments. Agri consumers were reluctant to pay their share of electricity bills beyond what they were burdened with during the subsidy regime, and therefore defaulted on their bills for these 27 months. This amount alone equals Rs 55.3 billion. Furthermore, subsequent billing was also affected as consumers were required to make their pending payments before they could pay their current dues. This meant that even if the consumers wanted to pay off current period liabilities, they were unable to do so without clearing the accumulated backlog.

The said notification regarding the proportion and liability of payments is still pending. It is pertinent to note here that the average recovery (3-year) ratio by Qesco before 2010 was 80 percent; this had come down to only 43.6 percent by end-2017. While agri consumers constitute the bulk of Qesco's defaulters, the Government of Balochistan and the federal government also collectively owe Rs 44.8 billion to the entity.

(iii) Enforcement issues³

The third aspect is the issue of electricity theft or low recoveries. Over 5.3 million electricity connections in Pakistan are getting electricity despite having defaulted on payments. At end June 2018, the outstanding balance of these defaults stood at Rs 404.8 billion, which makes up nearly half of the total receivables of Discos. These defaults are concentrated primarily in 4 Discos, including those operating in Quetta, Peshawar, Sukkur and Hyderabad. Furthermore, it appears that while recovery efforts on the part of these Discos are falling short, security conditions and law enforcement issues also impede collection process. Political considerations cannot also be ruled out when it comes to enforcing disconnections upon defaults.

In case of Sepco, for instance, the lack of cooperation from law enforcement agencies was important. Private sector receivables of this entity have been increasing at the rate of Rs 8-10 billion per annum for the past 3 years, primarily on account of theft, to stand close to Rs 84.6 billion at end FY18. In this regard, the distribution companies requested the help of law enforcement agencies to enable recovery and minimize losses from the affected and sensitive areas, but this did not help.⁴ Similarly, Peshawar Electric Supply Company (Pesco) also finds it difficult to take action against defaulters due to administrative and political obligations. Sometimes, the worst case scenario following permanent disconnection saw the company staff facing road blockages and attacks, and transmission towers being blown off.

In addition to this, distribution companies also have sizable proportion of pending receivables from provincial governments. The non-actualization of the amount for an extended period of time exacerbated the liquidity woes of these entities.

³ The issues highlighted and the data presented in this section have been taken from "Circular Debt: Issues and Solutions" authored by Senator Shibli Faraz, August 2018

⁴ After conducting a survey, Sepco found out that close to 400,000 illegal connections were operating in its jurisdiction. According to Sepco, 11,905 FIRs were lodged with local police between FY16 and FY18 (Jul-May), of which only 79 were registered.

S2.5 Unless the policy and overall business conditions change, a change in management of SOEs may not suffice

While too much emphasis is being given to privatization of Discos (and other SOEs), it is equally (if not more) important to devise a time-bound action plan to (i) shift towards efficient power generation; (ii) do away with costly and poorly targeted subsidies; (iii) address deficiencies in governance and regulatory infrastructure; (iv) remove price distortions; and (v) launch an effective crackdown against defaulters in security-wise challenging areas. While privatization might be helpful, its effectiveness will hinge on how the structural and political challenges facing these SOEs are addressed.

To bring down the Discos' T&D losses, heavy capital investments are required to phase out unreliable and old generation plants and replace low-voltage transmission and distribution lines. Therefore, the foremost step the government should take is to rationalize its subsidy outlay and expedite its investments in modernizing and revamping the distribution sector. Furthermore, both the federal and the provincial governments must step up their efforts and align their spending structures with the capital needs of the energy sector. Here, it is important to note that Discos are currently not in a position to undertake the needed up-gradation of their distribution infrastructure because of their persistent cash flow constraints. Over the medium-term however, Discos' reliance on PSDP can be reduced, and these entities should be able to seek financing based on the strength of their own balance sheets.

Furthermore, the involvement of provincial governments in the operational and managerial processes of the SOEs is also of significance. By facilitating loss recovery, provincial authorities can help the energy sector SOEs in tackling major financial issues, like theft and post-disconnection electricity consumption.

In sum, in order to improve the performance of the overall SOE sector, decisive action is required in the energy sector, along with a general improvement in the institutional governance of these entities. Efforts should particularly be taken to create an environment where the sector could be run on commercial basis, and SOEs operate independent of any political interference. In this context, a national consensus is required towards the formulation of a coherent energy sector policy, with a clear buy-in from all stakeholders at the government level.