



Chief Minister's Policy Reform Unit



VALUING NATURAL GAS: IMPLICATIONS FOR PROVINCIAL ECONOMIES

March 01, 2014

INTRODUCTION & BACKGROUND:

Chief Minister's Policy Reform Unit, Government of Balochistan, organized a presentation on "Valuing Natural Gas: Implications for provincial Economies" March 01, 2014 at Quetta Serena Hotel that was attended by a large number of stakeholders, including ministers, MPAs, party office-bearers and members from academia, law and other fields. The objective of the presentation was to sensitize concerned stakeholders about the facts and figures of gas resource and its actual value. The presentation was chaired by Dr. Hamid Achakzai, Minister for Planning and Development.

STRUCTURE OF THE WORKSHOP:

The presentation was made by Mr. Haris Gazdar, a well-known Economist and Researcher working on social policy and political economy issues. Though this was a technical subject, it was presented in common language for the ease of understanding, as majority of the participants had no background in economics and in dealing with figures. The presentation session was followed by question and answer session.

PROCEEDING OF THE WORKSHOP:

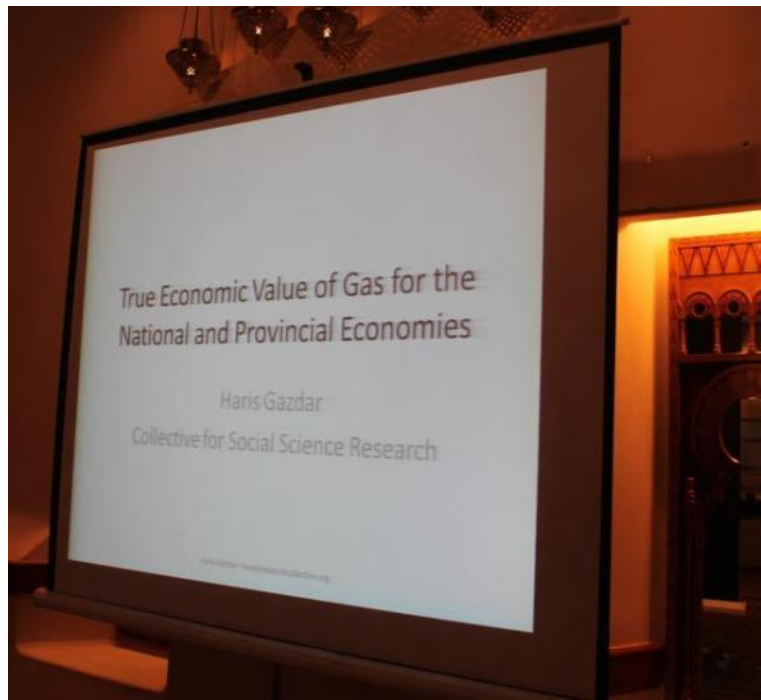
The workshop started with the recitation of Holy Quran. After that Dr. Kaiser Bengali, head of CMPRU, formally welcomed the participants and in his opening remarks, expressed the view that this workshop will define the political strategy of Government of Balochistan in the stance of Oil & Gas. He said that for the last 50 years, gas prices have remained low and we have been using gas as freely as water. Resultantly, gas producing regions bear the major loss and gas consuming regions gain a substantial subsidy. Low gas price has also not encouraged conservation and now there is a serious shortage of gas, requiring import at high cost in foreign exchange.



"This workshop will define the political strategy of Government of Balochistan in the stance of Oil & Gas."

PRESENTATION BY MR. HARIS GAZDAR:

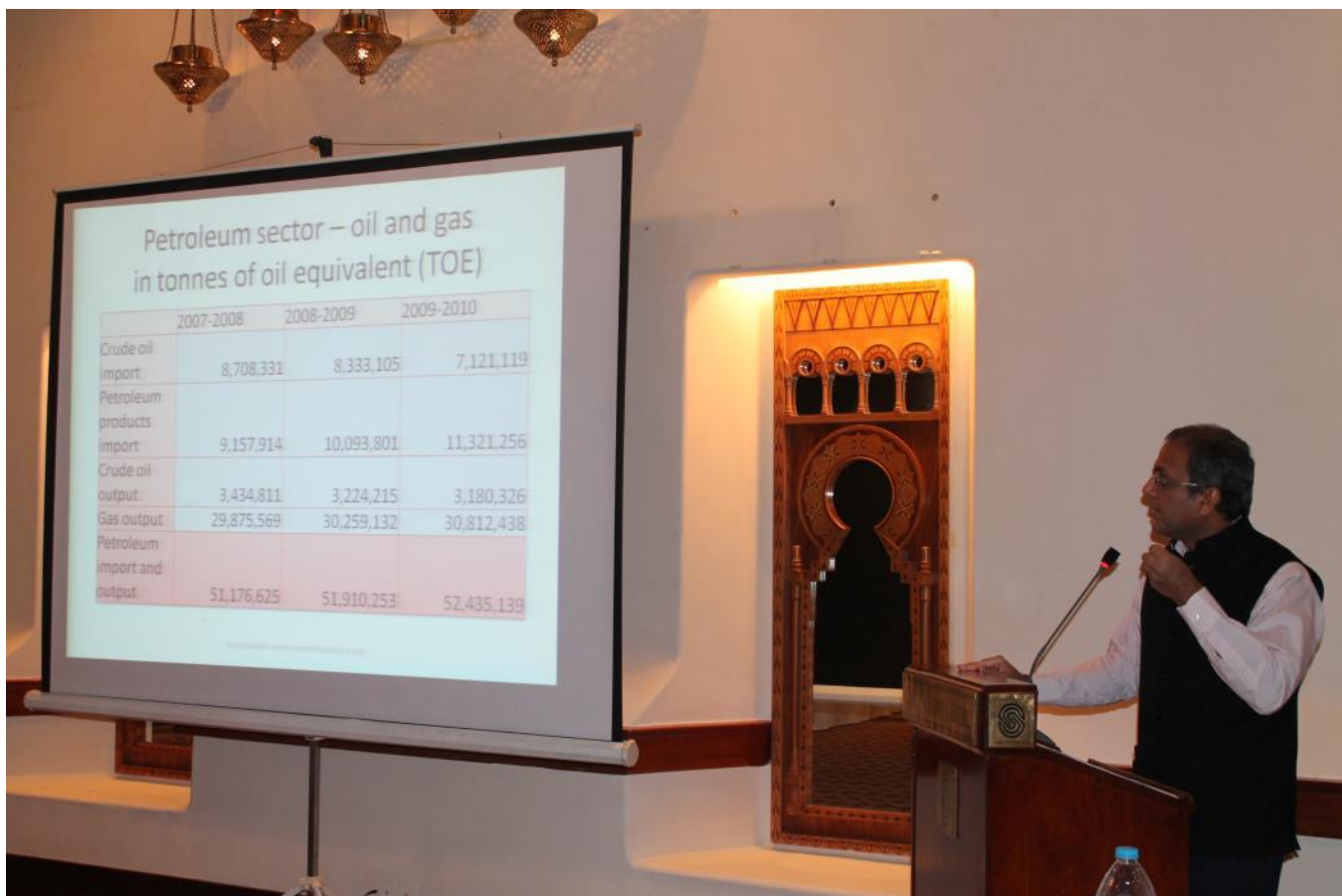
The political and economic scenario of Pakistan is now changing and after the 18th amendment there is a paradigm shift from authoritarian centralization to democratic federalism. Now the masses are aware that in order to better manage the resources provinces cannot be



ignored. He said that gas resources are undervalued and this situation is further worsened by the subsidy that government gives to different

sectors and companies. Every natural resource has its economic value and if we under value any natural resource then its implication on economy are adverse. In Pakistan, gas price is determined, not by the market, but by the gas policy of the federal petroleum ministry and has remained far below alternative valuations – i.e. India Qatar and Henry Hub. The extent of undervaluation of Gas prices can be seen from the fact that if alternative international prices were used, the contribution of gas in GDP would be 9% as against 0.5% at present. Now the important point to consider is that if Pakistan thinks of purchasing gas from abroad, it will have to pay the international rate, which is more than 3 times the rate in the country.

Mr. Haris Gazdar's power point presentation is annexed as Annexure 2.



QUESTION ANSWER SESSION:

The most frequent question asked was about different prices of Gas among provinces. Why Balochistan Gas has low value as compared to other provinces. Mr. Haris explained that every well head operates under different policies and in Balochistan being the first in gas supplies has majority of the wells operating on the prices that were set long ago. Dr. Kaiser Bengali explained that older gas wells have zero depreciation costs and is thus valued lower. Balochistan wells are older than in Sindh or Khyber-Pukhtunkhwa.

Mr. Usman Kakar from PKMAP asked that why there is a difference between the rate at which gas is supplied to fertilizer companies and domestic users and is there any data available regarding our total gas production and usage. He further asked about Pak Iran Gas pipe line and the line from Turkmenistan to purchase gas. Answering this, Mr. Haris Gazdar said that there are different subsidy rates for different sectors as fixed by federal government. As far as Turkmenistan is concerned, that was the alternate option given by external powers in order to isolate Iran. He said that every option can be considered in the welfare of the country and provinces should have their say in this kind of decision making.



Mr. Muhammad Ayaz from University of Balochistan asked that if re-evaluating gas price can have negative impact on GDP. Doing so, will increase the input cost and then what will be the overall impact on output prices. Mr. Haris Gazdar explained that though input cost will increase, but its overall impact will be for short time period and in a long run the country's economy will grow. In one way or other we have to assign due economic value of gas; otherwise, there will be severe crises, he said

Advocate General Mr. Nazim-ud-din asked about the provincial role in all the steps involved in Gas exploration and its supply. Mr. Haris Gazdar replied that till the 18th Amendment, all the agreements with companies were made by federal government; the provincial government only issues the NOC issuance; so there was no major role of provincial governments. Post 18th Amendment, the situation is different.

Mr. Nagi Senior Lawyer of Balochistan said that Article 172(3) began with words, "Subject to existing commitments ..." and asked about the extent of existing commitments prior to the 18th Amendment and commitments made post-18th Amendment. This was a question to be put to the federal government.

SUMMING UP:

Dr. Ishaque Baloch, Policy Coordinator of CMPRU, said that the 18th Amendment will greatly benefit the province. Now all the existing policies should be reviewed in the context of 18th amendments. For this reason this kind of workshop is very useful as all stakeholders sit together and see what we have achieved and what should we do further to implement the 18th Amendment in its true spirit. He further added that now all agreements regarding exploration should be made with the mutual consent of federal and provincial governments. Regarding the

royalties issue, he said there should be a policy whereby a part of the Royalty is shared with the district from where natural resources is extracted for the welfare of local community there. At the end he thanked Mr. Haris Gazdar for his valuable presentation and the participants for their worthy inputs.



CONCLUDING REMARKS BY MR. HAMID ACHAKZAI:

Dr. Hamid Achakzai, Minister for Planning & Development, praised the efforts of Chief Minister's Policy Reform Unit for arranging this useful and much needed presentation and the quality and importance of information provided. He said these kind of events are very useful and one of few in which all major party heads and stake holders sit together to talk about serious issues.

He said after a long struggle of 65 years, now the province has got their rights and now we should exercise the powers that our Constitution has given to us. Pertaining to the price issue he said that it is not acceptable that Balochistan buys food at full international prices and sells gas at one third the international price.



ANNEXURE 1: PROGRAMME



Presentation on “Valuing Natural Gas: Implications for Provincial Economies”

March 1st, 2014

Programme

Time	Activity	Resource Person
10:30- 11:00	Registration of participants	CMPRU staff
11:00- 11:05	Recitation of Holy Quran	Najam-ul-Haque
11:05-11:15	Welcome address and Introduction	Dr. Kaiser Bengali
11:15- 12:15	Presentation on “Valuing Natural Gas: Implications for Provincial Economies”	Mr. Haris Gazdar
12:15-01:15	Question Answer Session	All Participants
01:15-01:45	Concluding remarks by Chief Guest	Dr. Hamid Achakzai
01:45-01:50	Vote of thanks	Dr. Ishaque Baloch
01:50	Lunch	

ANNEXURE 2: PRESENTATION SLIDES

True Economic Value of Gas for the National and Provincial Economies

Haris Gazdar

Collective for Social Science Research

Haris Gazdar - www.researchcollective.org

Gas and Reform

- Historical background
 - Politic trend – authoritarian centralisation to democratic federalism (Rabbani 2012)
 - Economic context – state monopoly to market-orientation – 'free resource'
- Natural resource rent
 - Efficiency – ownership does not matter, price does, no 'free resource' – standard economics
 - Equity – ownership and disbursement is entirely a political matter – rent and conflict (Collier et al, Bjorvatn)
- Crossroads in historical terms
 - Will the trajectory of political reform collide with the logic of economic reform, and how might they help each other?

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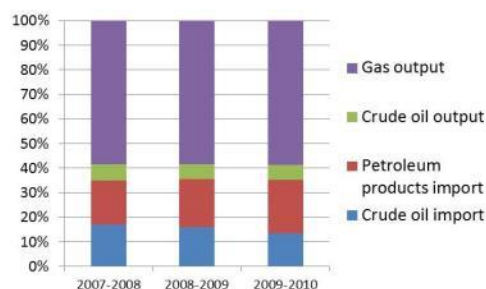
Petroleum sector – oil and gas in tonnes of oil equivalent (TOE)

	2007-2008	2008-2009	2009-2010
Crude oil import	8,708,331	8,333,105	7,121,119
Petroleum products import	9,157,914	10,093,801	11,321,256
Crude oil output	3,434,811	3,224,215	3,180,326
Gas output	29,875,569	30,259,132	30,812,438
Petroleum import and output	51,176,625	51,910,253	52,435,139

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Share of domestic and imported oil and gas – TOE

Source: Calculations based on Pakistan Energy Yearbook, various



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Why think about price?

- Natural resources have economic value
- Shortages imply market is not clearing
- Most commodities and many services are now traded
- Economic value becomes pertinent once we start talking about ownership and distribution of a resource.

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Ways of valuing gas

- Presently, in Pakistan's national income accounting gas value is based on its well-head price
 - This price is determined by the gas policy of the federal petroleum ministry
 - It has remained far below alternative valuations – i.e. an implied subsidy
- Alternative ways of measuring the economic value of gas through the market price – given that Pakistan does not yet import gas options are:
 - Tonnes of Oil Equivalent (TOE) – what the country actually paid for equivalent energy units imported in shape of oil in a given year
 - India-Qatar average – the average price neighbouring India paid in a given year for LNG imports from Qatar
 - Henry Hub – a market for mostly internal trading of gas within the US

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Gas price in Pakistan in comparative perspective (Rs per million BTUs)

Sources: Calculations based on Pakistan Energy Yearbook (various), Broad College of Business (2010), Mundi Index

	2007-2008	2008-2009	2009-2010
Power*	254	359	389
Industry	252	339	382
Domestic**	93	102	118
Fertilizer fuel	252	339	382
Transport (CNG)	291	427	504
Fertilizer feed***	71	86	93
Commercial	283	393	464
Cement	335	454	536
Weighted average	223	304	340
Price- TOE	1,014	1,002	1,132
Price- India/Qatar	503	937	1,012
Price- Henry Hub	525	463	360

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Reasons and implications of prices being far from their economic value

- What is behind this situation in Pakistan
 - Well-head prices are policy-driven – link with economic value is weak – 2001, 2007 policies
 - Policy rationale
 - Mandate of federal petroleum ministry
 - Supply of gas at lowest possible price and volatility
 - While ensuring profitability
- But implications
 - Demand AND supply distortions
 - Not only in gas sector, but across economy
 - And political implications too

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Extent of undervaluation of gas, using alternative prices

Sources: Calculations based on Economic Survey (various), Bengali and Sadaqat (2005), Pakistan Energy Yearbook (various), Broad College of Business (2010), Mundi Index

Alternative price for gas		2007-2008	2008-2009	2009-2010
TOE (tones of oil equivalent)	Rupees, billion	1,085	1,064	1,215
	Share of GDP	11%	9%	9%
India-Qatar average for the year	Rupees, billion	513	991	1,079
	Share of GDP	6%	9%	8%
Henry Hub average for the year	Rupees, billion	538	459	334
	Share of GDP	6%	4%	3%

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Gas production as % of GDP

Sources: Calculations based on Economic Survey (various), Bengali and Sadaqat (2005), Pakistan Energy Yearbook (various), Broad College of Business (2010), Mundi Index

	2007-2008	2008-2009	2009-2010
No adjustment	0.5	0.5	0.5
TOE	11.5	9.3	9.3
India-Qatar	5.7	8.7	8.3
Henry Hub	5.9	4.3	2.9

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Gas production as % of provincial GDP –reference 2009-2010

Sources: Calculations based on Economic Survey (various), Bengali and Sadaqat (2005), Pakistan Energy Yearbook (various), Broad College of Business (2010), Mundi Index

	Punjab	Sindh	Khyber-Pakhtunkhwa	Balochistan
No adjustment	0.1	1.2	0.2	2.0
TOE	0.9	20.7	4.0	33.5
India-Qatar	0.7	16.2	3.1	26.1
Henry Hub	0.2	4.5	0.9	7.2

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Undervaluing of gas in terms of provincial GDP – 2009-2010

Sources: Calculations based on Economic Survey (various), Bengali and Sadaqat (2005), Pakistan Energy Yearbook (various), Broad College of Business (2010), Mundi Index

	Punjab	Sindh	Khyber-Pakhtunkhwa	Balochistan
TOE	0.8	19.3	3.7	30.9
India-Qatar	0.6	14.8	2.8	23.6
Henry Hub	0.1	3.2	0.6	5.1

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Provincial GDP as % of Pakistan – reference 2009-2010

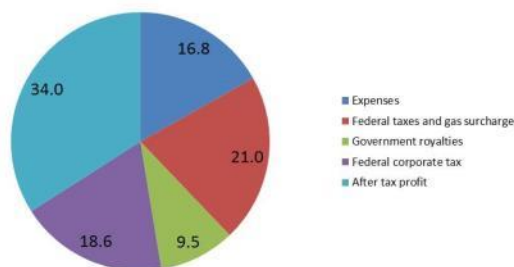
Sources: Calculations based on Economic Survey (various), Bengali and Sadaqat (2005), Pakistan Energy Yearbook (various), Broad College of Business (2010), Mundi Index

	Punjab	Sindh	Khyber-Pakhtunkhwa	Balochistan
No adjustment	51.0	31.8	11.8	5.4
TOE	47.3	34.9	11.2	6.6
India-Qatar	48.1	34.2	11.4	6.3
Henry Hub	50.3	32.4	11.7	5.6

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Typical example of distribution of gas producer's sales revenue (per cent)

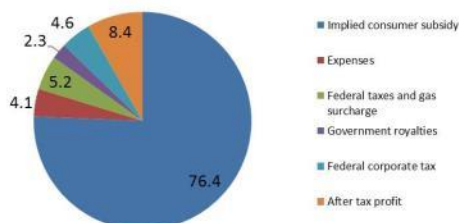
Source: PPL Annual Report 2008



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Distribution of the economic value of a unit of gas (per cent) – assuming TOE value

Source: Authors' calculation based on PPL Annual Report, and Pakistan Energy Yearbook 2010



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Way forward

- Economic reforms
 - Measurement is important – provincial governments and civil society can start this work
 - Energy reform will have clear winners and gainers, and serious bottlenecks – hence political issue
 - Model of other resource rich countries becomes relevant – invest resource rents in social programmes
 - Again, agenda for government and civil society
 - Gas price issue can no longer be wished away
 - Imports
 - Privatisation agenda?

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Inevitable questions

- Political issues
 - Who should own production and distribution companies?
 - Or who should have a say on price
 - And, how should profits/rents be distributed
 - Nightmare scenario if other reforms (i.e. privatisation, deregulation etc) not cognizant of constitutional and political issues
 - Preparing the political ground – or allowing things to drift?

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ANNEXURE 3: ATTENDANCE SHEET



Chief Minister's Policy Reform Unit (CMPRU)

Attendance Sheet

Event: Presentation by Mr. Haris Gazdar on "Valuing Natural Gas, Implications for Provincial Economies"

Date: March 1st 2014 at 10.30 Am

Venue: Quetta Serena Hotel, Qilla Saifullah Hall

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