

**DEREGULATION OF THE DOWNSTREAM OIL SECTOR IS THE SOLUTION TO
THE PROBLEMS RELATED TO OUR ENERGY SECURITY**

On a daily basis, the blame game continues in the media with regard to who is responsible for the crisis facing the Oil and Gas sector. The Regulator gets blamed by the Industry (read Oil Marketing Companies or OMCs) for the mess that we see being played out. In the category of OMCs are the big 4 and the others, the so-called Emerging OMCs. Each has its own complaint to relate: it's like the proverbial Pot calling the Kettle black!

As we said goodbye to 2022 and welcomed 2023, we did not leave behind any problems but can look forward to more of the same (or worse) in 2023 unless and until we accept our shortcomings and, instead of living in denial, learn from them and chalk a way forward for what is good for our country. Facts cannot be brushed under the carpet at the altar of expediency, political or otherwise.

The Country's Financial Challenges are well known and the subject of daily Media discussions: the pressures from the IMF, the volatile prices of energy in the international marketplace, the depleting indigenous natural resources, all impact the prices of commodities that are consumed by the common man who is hard put to meet the financial challenges resulting therefrom.

We do not have enough fiscal resources to meet our ever-growing needs of the basic essential commodities to keep our populace supplied. The poor segment of our population is growing and facing survival challenges on a daily basis

All our indigenous resources have dwindled and we continue to rely more and more on costly imports at a time when our Rupee/Dollar parity is seriously compromised and the international market keeps heading north due to factors beyond our control and dictated by wars, political upheavals, pandemics, and the vagaries of the market itself.

Our Local Natural Gas Resources are already seriously compromised: We have consumed ~70% of our Natural Gas Reserves. Unbridled consumption of CNG and ever-increasing imports of expensive RLNG are overburdening our already compromised financial well-being

All the recent developments on the international front as well as the local scene, and the resultant continuous increase in the price of Oil and RLNG, are adding to Pakistan's woes.

Oil and Gas is a key area we need to focus on as it impacts the entire national well-being. We import almost 85% of our Crude Oil and 70% of our Gasoline and 50% of our HSD needs.

What is needed is out-of-the-box thinking similar to the theme of the Turnaround Pakistan Conference of 28 May 2022. When I was asked to present a Paper on the Energy Scenario, I felt hopeful since the theme of the Conference sought out-of-the-box solutions to the problems facing our Nation, and my presentation focused on the same.

While the intent of the Conference was the need of the hour, the outcome has regrettably been the same as the fate of all such past conferences: more talk and no action! Especially in the Oil and

Gas sector, the most critical area that determines the cost of every commodity effecting the wellbeing of the common man.

The bottom line is: We need to resort to belt-tightening and relying more on indigenous resource

Maximum Use of Indigenous Energy Resource, Reducing Consumption and Minimizing Imports is the only solution

The recipe to follow? Minimize imports and maximize use of local energy resource; target consumption reduction on war footing and target the right transportation fuel specifications.

The situation at the country's borders and the fight against terrorism being addressed by our valiant Armed Forces, furthermore, requires a National strategy that ensures timely and without-disruption POL supplies especially for the Armed Forces.

The challenges faced by the Downstream Oil Sector of Pakistan fall into two basic categories: those that are the result of recent global developments and those that arise due to systemic fault lines.

In the former category are the international oil prices which have risen to phenomenal heights due to pandemics, wars and such. Since Pakistan depends heavily on imports of Oil, these have a direct impact on the Refineries' and OMCs Cost of Sales and thereby their bottom lines.

In the second category are the OMC and Dealer Margins which have been regulated since long. The current OMC Margin is manifestly inadequate to cover the costs incurred by an OMC. Various independent studies including those by the Pakistan Institute of Development Economics (PIDE) confirm that revision of Margins to a more logical formula than that prevailing is a must. Margins dictate the investments that will come in to cater for the short, medium and long-term infrastructure needs to match the growth in the Sector. Only a decent market-based Margin will lead to the investments needed not only in the traditional fossil fuels but also in the future hybrid/electric vehicles and their hookups at the OMC forecourts.

The Oil Sector of Pakistan is highly regulated:

- The Sector Margins (OMC Margins and Dealers Margins) are fixed by the Government
- The Price of Fuel for the Consumer is fixed by the Government

The Government needs to get out of the business of price regulation and allow the market itself to determine what the consumer pays at the forecourt/retail outlet. Instead of the leading OMC being forced to purchase the transport fuel (Petrol and Diesel) from the traditional source (as per government diktat), OMCs must be allowed to procure from more competitive sources rather than being tied to one source. Let them fix their prices based on their own costs and let real competition set in. We have long suffered from fear-of-the-unknown whilst taking such decisions. No OMC should be afraid of real competition. That is what Deregulation is all about.

The only area where the Government must be involved is the setting of the product specification. These should be in line with government policy and uniformity as well as the right fuel for the right consumer must be ensured. The 2/3 wheelers must be supplied product that is genuinely required by their engines and not for the high-end consumer driving the 4-wheel drive. The latter can afford to pay for a higher cost but the poor segment of society must benefit from a reduced price. This is where we will also be in line with what the IMF is saying; subsidies must benefit the poor segment and not the rich!

Is Deregulation the answer? Let us examine this here.

What is de-regulation? Simply put, it is the removal of government regulations. The objective is to allow the Industry to operate its business more freely, make decisions efficiently and remove corporate restrictions. Implemented correctly, it assists in improving innovation, entrepreneurship, competition and efficiency.

However The Bottom Line is:

It must lead to lower prices for the customer and to improved quality of product

At this point the natural tendency would be to cite examples of successful de-regulation outside Pakistan: the Airline Industry, Telecommunication, and Trucking are generally termed success stories in the countries where they were successful.

However, the success of de-regulation is closely linked to the ground realities in a given country. Transparent Sharing of Data is a key factor in effective oversight of the switch to Deregulation. One must also ensure that the POL supply chain suffers zero/least impact due to the switchover from regulation to deregulation. Rather than copying what happened outside Pakistan, one must focus on what will work in our country.

While Deregulation has been the subject of concerted debate in Pakistan since over a decade, one of the main reasons that it has not been successful is the sensitivities of the local environment, political as well as technical in nature.

The first product to be deregulated was Furnace Oil in the 1990s. Based on the experience of Furnace Oil, a phased deregulation of other refined product was to follow. That has not happened. Political expediency has overshadowed any serious move towards further deregulation.

One element especially of note is the Inland Freight Equalization Margin (IFEM) through which the cost of transporting Petrol and HSD incurred by the OMC is compensated with the objective (as the name suggests) of equalizing the price the consumer pays throughout the length and breadth of Pakistan. For Deregulation, the IFEM would need to be abolished. Here, too, the Industry will find its own way to minimize cost of transportation instead of benefiting from a seriously flawed system which is also subject to gross misuse. We need to find a way around this fear of the unknown. We cannot sacrifice the benefits of deregulation at the altar of political expediency. Where there's a will, there's a way!

Even after Deregulation, the role of the Watchdog must continue by the Regulator (OGRA, Ministry of Energy) to ensure that the benefits pass on to the Consumer.

Deregulation does not preclude the role of the Regulator who has the primary responsibility related to Policy.

There is a misconception that by instant Deregulation the role of the government will completely end.

The role of the Regulator and the Policy Maker must not end with Deregulation. A watchdog must still ensure that the real benefits of Deregulation are being passed on to the Consumer and issues such as cartelization, adulteration, product quality improvements are adequately addressed. Otherwise the impact will be totally contrary to the Objective

Both the Regulator and Policy Maker will still need to achieve answers to:

What is the Benefit to the Policy Maker?

What is the Benefit to the Consumer, the ultimate beneficiary?

Deregulation, in the writer's opinion, is the only way to counter the fault lines and bumps that strew the path faced by today's oil supply chain!

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