



May 24, 2010

The Honorable Richard Holbrooke
Special Representative for Afghanistan and Pakistan
U.S. Department of State
2201 C Street NW
Washington, DC 20520

Subject: Open letter #3, U.S. development assistance to Pakistan's energy sector¹

Dear Ambassador Holbrooke:

This is the third in our series of open letters, through which we aim to provide constructive commentary and practical recommendations over the next year on the U.S. foreign assistance and development program in Pakistan. As with the [first](#) and [second](#) letters, this letter is meant not only for you but for your colleagues throughout the Administration, including in the White House and at USAID, as well as for interested readers in the policy and research communities. At the third meeting of the [CGD Study Group on a U.S. Development Strategy in Pakistan](#), we focused on what U.S. policies and aid programs would be most effective in addressing [Pakistan's energy crisis](#). We understand the administration's decision to support a major investment program in Pakistan's power sector. From a national security, diplomatic, and short-term stability perspective, [Secretary Clinton's announcement last fall of six energy projects](#) was a good first start in what we understand is a multiple-part signature energy program.

However the U.S. assistance program is also meant to address Pakistan's long-term development needs. With that in mind, I would like to make the following four points, guided by input from our study group members.

1. The real challenge of Pakistan's energy sector— beyond quick repairs and other programs to increase the supply of power in the short run—is to **work with the government of Pakistan on the institutional and pricing reforms** that will ensure the power sector does not constrain Pakistan's growth over the medium to long term. To strengthen the financial viability of the sector, the government of Pakistan needs to resolve the circular debt problem (in which importers or local producers are not paid by distributors who are not paid by users including government agencies, to simplify enormously) and overcome the political resistance to increasing power tariffs to adequate levels to ensure a commercial return to new investments. Further governance and institutional reforms are needed to address the corruption and patronage that are

¹ This open letter will be published on the Center for Global Development website (www.cgdev.org) and disseminated to relevant officials in the administration and Congress.

behind some of the fragmentation and lack of coordination that hamper the sector. Some members of the study group urge the creation of one single energy ministry and/or the appointment of a deputy prime minister to coordinate energy policy across the current tangle of at least seven major ministries and agencies, with conflicting interests, involved in the sector.

Given there is no alternative to government-led reform, we support strongly the apparent decision of the administration to work closely with the government of Pakistan in general and to develop programs in which most U.S. funding—for this and other sectors—flows to and through the government itself. Without progress led by the government of Pakistan itself on these institutional reforms, U.S. and other outsider spending on Pakistan’s energy infrastructure will never be sufficient to make lasting change.

While the United States may need to identify individual energy projects to ease current shortages, ideally these immediate steps will be part of an overall strategy agreed between the government and the major donors and creditors. For example, the government could be supported in announcing any future tariff increases will occur only if and when brown-outs have been reduced to pre-specified levels. This would clarify the need to improve services in the short run and help prepare the political ground for increased tariffs in the future, while also supporting those in the sector committed to the politically difficult structural reforms.

2. At the same time, the United States need not be out front in pressing for key institutional and governance reforms, but should **work with and through the other major donor partners**. We are concerned that the U.S. team is not taking full advantage of the experience, the ground capacity of the World Bank and the Asian Development Bank in the energy sector in Pakistan, and the broad interest in the donor consortium on Pakistan’s energy needs. Nor is the obstacle a lack of technical agreement on the nature or sequencing of critical reforms, which have been set out in Pakistan by the current government.²

It is true that past efforts by the World Bank and the Asian Development Bank to support fundamental institutional and demand-side reforms tell a dismal tale (for more, see our [background note](#)). Despite decades of policy dialogue with donors and billions of dollars in external assistance, the government of Pakistan has not been willing or able to implement key reforms. The challenge has been and continues to be political will. On the other hand, the United States’ renewed engagement comes at what may be an opportune moment politically for the government itself, given the depth of the crisis and the frustration of Pakistani citizens with the situation.

3. Beyond the [\\$125 million already promised for repairs and upgrades to Pakistan’s energy infrastructure](#), we encourage you to **commit more U.S. funds on Pakistan’s**

² A medium-term strategy has been defined (the so-called Integrated Energy Plan), commissioned by former Finance Minister Tarin and led by the Chairman of Pakistan’s Oil and Gas Development Corporation, although we have seen only summaries of the plan.

energy infrastructure only as and when the government of Pakistan is able to show progress on the tough financial and political reforms critical to attracting private investment to the sector. Increasing supply now is probably necessary to build public support for tariff increases and increase confidence in the government itself. But further large commitments by the United States to infrastructure and other measures to increase energy supply should go hand in hand with institutional and policy reforms by Islamabad. We say this not because the United States might have influence on what is a sensitive internal political issues—it probably does not—but because without home-grown and politically sustainable reforms, short-term fixes now can easily be reversed.

4. Finally **once again** I urge both the administration and the government of Pakistan to **be transparent about the approach to the energy crisis and to better educate the Pakistani public** about the need for it. For example, we urge the administration to agree with the government of Pakistan on simple and transparent benchmarks for progress on the fundamental institutional and pricing reforms, and to make these clear to the Pakistani and American public. Because the basic causes of Pakistan's energy crisis are not well understood by the Pakistani public, the United States should support efforts to engage civil society and the Pakistani public about what is causing the crisis and the reforms that are needed to resolve it.

Along with members of the study group, I recognize the challenge for both the administration and Government of Pakistan presented by the severity of Pakistan's energy crisis. We understand that there are plans this summer for delegations of U.S. officials to visit Pakistan for joint discussions on energy and other specific sectoral issues, in follow up to the [United States - Pakistan Strategic Dialogue](#) in March. In addition to this constructive dialogue between U.S. and Pakistani policymakers, we are hopeful that growing internal pressures within Pakistan will finally be able to break through the impasse on reform that external pressure has to date been unable to overcome.

I hope our letters are and will be helpful to you and your colleagues, and I welcome any comments from you or any of those working with you.

Sincerely,



Nancy Birdsall
President, Center for Global Development

Attachment: CGD Study Group on a U.S. Development Strategy in Pakistan

CGD STUDY GROUP ON A U.S. DEVELOPMENT STRATEGY IN PAKISTAN*

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** Study group members serve in their individual capacity; their affiliations are shown for identification purposes only. While the open letter draws heavily on the views expressed in the working group meeting, individual members do not necessarily endorse all policy recommendations contained in the open letter.*