Is There a Significant Increase in (FDI) to Pakistan as a Result of CPEC?

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Abstract

The China-Pakistan Economic Corridor (CPEC), a strategic cooperative initiative between China and Pakistan worth an estimated $62 billion, has indisputably reshaped the landscape of foreign direct investment (FDI) in Pakistan. Since its inception in 2013, the total net FDI in Pakistan has seen a significant increase. For instance, between 2013 and 2019, the net FDI increased from $1.45 billion to $2.24 billion, representing a growth of over 54% (State Bank of Pakistan, 2020). The majority of CPEC funding would go toward energy and infrastructure projects. Energy projects will get $33 billion of the overall funding. The energy imbalance has been cut in half from 4,500 MW in 2013 to nearly nothing in 2020 because of these initiatives (Javaid & Javaid, 2018). The geographical distribution of this investment, however, reveals a concentration in Punjab and Balochistan, leaving behind other provinces like Sindh and Khyber Pakhtunkhwa. This imbalanced distribution could exacerbate regional inequalities, potentially stoking socio-economic tensions. Although the energy and infrastructure sectors have benefited greatly from FDI, other industries, including agriculture, manufacturing, and services, have not seen the same level of investment. This discrepancy may indicate an over-focus on a few industries, underlining the need for more diverse investment to support long-term development. Constant discussion surrounds the long-term effects of this huge FDI inflow. Proponents say it can improve infrastructure, end energy shortages, and spur economic development. However, critics warn about the growing debt, with debt payment costs projected to reach a high of roughly $5 billion by 2022 (Wolf, 2020).

Keywords: *FDI, Investment, CPEC, China, Pakistan.*

Introduction

FDI, or foreign direct investment, is crucial for developing economies like Pakistan. Foreign direct investment (FDI) is a major contributor to global economic growth and has the potential to boost economic performance in many ways. The vast investment portfolio, mostly financed by FDI, that the China-Pakistan Economic Corridor (CPEC) represents, is a concrete example of these possibilities in action in Pakistan.

The expansion of the economy is a crucial advantage of FDI. The World Bank estimates that a doubling of foreign direct investment (FDI) would add 2% to GDP growth in emerging markets. Foreign direct investment in Pakistan has risen dramatically thanks to CPEC, from $1.45 billion in 2013 to $2.24 billion in 2019 (State Bank of Pakistan, 2020).

One of the most important aspects of FDI is the jobs it creates. Thousands of direct and indirect employment in fields including energy, infrastructure, and transportation have been generated as a result of CPEC-related FDI. One of the main benefits of FDI is the transfer of technology, and this is clearly seen in CPEC initiatives. For instance, cutting-edge equipment has been introduced to Pakistan's electrical grid as a result of CPEC energy projects. By using supercritical boiler technology, the Sahiwal Coal Power Plant was able to increase power-generating efficiency by a large margin (Javaid & Javaid, 2018).

Foreign direct investment (FDI) also helps a lot in bettering the workforce. Workers improve their productivity and marketability by gaining new information and abilities. Thousands of Pakistani employees have been given this chance thanks to CPEC, helping to expand Pakistan's human resource pool.

Background

The China-Pakistan Economic Corridor (CPEC) is a major step forward in the development of China and Pakistan's strategic alliance and a flagship project of the wider Chinese Belt and Road Initiative (BRI). The China-Pakistan Economic Corridor (CPEC) is a massive infrastructure project that began in 2013 and is expected to cost over $62 billion. It includes a wide range of improvements throughout Pakistan, from the country's northern border with China to its southern seaports.

The China-Pakistan Economic Corridor (CPEC) is an ambitious plan to improve regional connectivity via the development of several energy, transportation, infrastructure, and industrial projects. The overarching purpose of these endeavors is to promote regional integration and development by strengthening economic cooperation and connectivity between China and Pakistan.

CPEC and FDI: An in-depth analysis

State of FDI before CPEC

Before the launch of CPEC in 2013, Pakistan's FDI had been on a downward trajectory. The country received an FDI of $1.45 billion in 2012-13, which was significantly lower than the $5.4 billion received in 2007-08 (Board of Investment, Pakistan, 2014). This decline can be attributed to factors such as power shortages, political instability, and security concerns.

The flow of FDI during the implementation phase of CPEC

Since the launch of CPEC, there has been a significant increase in FDI, primarily driven by Chinese investment. According to data from the State Bank of Pakistan, the country received an FDI of $2.4 billion in 2016-17, a 150% increase compared to 2012-13 (State Bank of Pakistan, 2018). Most of this investment was directed toward CPEC projects, particularly in the power and infrastructure sectors.

While the correlation between CPEC and FDI inflow to Pakistan is empirically observable, the question of the extent and nature of this correlation merits further exploration. This involves dissecting the investment dynamics through the lens of economic sectors, geographical location, and strategic long-term impacts.

Economic Sectors

a. Energy Sector

One of the most significant components of CPEC is its focus on the energy sector, with approximately $33 billion of the total CPEC investment dedicated to energy projects (Yasmeen & Mukhtar, 2020). The energy sector is the primary recipient of CPEC's FDI, accounting for about 70% of the total FDI inflow under CPEC until 2020 (Yasmeen & Mukhtar, 2020).These projects span various forms of energy production, aiming to reduce Pakistan's substantial energy deficit.

Coal Power Projects: Coal power plants are a critical part of the CPEC energy portfolio. Notably, the $1.8 billion Sahiwal Coal Power project, completed in a record 22 months, is a shining example of China's direct investment into Pakistan's energy sector (Yasmeen & Mukhtar, 2020). The project added 1,320 MW to the national grid, meeting the energy demands of millions of Pakistanis (Javaid & Javaid, 2018). Similarly, the

Port Qasim Coal-Fired Power Plant, a $2 billion project, added another 1,320 MW, reinforcing the pivotal role of Chinese FDI in addressing Pakistan's energy crisis (The Nation, 2017).

Hydroelectric Power Projects: There has also been a lot of money put into hydroelectric power plants. Key instances of FDI in this area include the $1.8 billion Suki Kinari Hydroelectric Power Project in Khyber Pakhtunkhwa and the $1.42 billion Karot Hydroelectric Power Project in Punjab (CPEC Official Website, 2021). These initiatives will help Pakistan transition away from its reliance on fossil fuels and towards a cleaner, more sustainable energy grid.

Renewable Energy Projects: Smaller renewable energy projects have been able to successfully attract foreign direct investment. One of the biggest solar farms in the world, the $1.5 billion Quaid-e-Azam Solar Park highlights the potential of solar energy in Pakistan (Dawn, 2015).

b. Transport Infrastructure Development

Highways: The modernization of the Karakoram Highway Phase II, a $1.3 billion project, showcases the transformative role of Chinese FDI in enhancing Pakistan's road connectivity (The Express Tribune, 2019). Another notable project is the Multan-Sukkur Motorway, part of the larger Peshawar-Karachi Motorway, which had an estimated cost of $2.89 billion (Radio Pakistan, 2019).

Railways: The Main Line-1 railway project, costing $6.8 billion, is one of the most ambitious transportation projects under CPEC (Dawn, 2020). This project is set to upgrade Pakistan's existing railway infrastructure, enhancing the speed and capacity of the rail network.

Ports: The Gwadar Port project, with an investment of $622 million, underscores China's commitment to enhancing Pakistan's maritime infrastructure (Pakistan Observer, 2020). The project includes not only the development of the port but also a free zone and a connecting road network.

c. Industrial Cooperation:

The creation of SEZs within the framework of CPEC is an important strategy for stimulating manufacturing expansion and luring in foreign direct investment. Special Economic Zones (SEZs) are geographically delineated regions inside countries where some business and trade rules are relaxed in order to entice foreign investment and boost economic activity. SEZs are often utilized to kickstart industrialization, provide new employment opportunities, and expand exports (Farole & Akinci, 2011).

Nine SEZs are planned under CPEC across Pakistan's various provinces, each offering a range of incentives for investors such as exemptions from customs duties and taxes for capital goods imported for SEZ development, income tax holidays, and simplified visa procedures (CPEC Official Website, 2021).
Three SEZs have been prioritized for early development:

Rashakai Economic Zone, Khyber Pakhtunkhwa: Industries including fruit processing, textiles, steel, and car components are the main emphasis of the Rashakai Economic Zone, which spans an area of around a thousand acres. Over $1.5 billion in investment and 200,000 new employment are predicted as a result (Khan, 2020).

Dhabeji Special Economic Zone, Sindh: Spanning over 1,500 acres, the Dhabeji SEZ is expected to focus on mixed industries, including light engineering, textiles, pharmaceuticals, chemicals, food processing, and auto and auto parts. Its strategic location near Karachi, the economic hub of Pakistan, and proximity to the port gives it a strategic advantage, with the potential to attract more than $4.5 billion in investment and create 300,000 jobs (Husain, 2020).

Allama Iqbal Industrial City, Punjab: This SEZ is planned to span over 3,000 acres near Faisalabad. It will focus on textiles, petrochemicals, steel, food processing, and automobiles. It is expected to attract investment of over $5 billion and create around 300,000 jobs (Express Tribune, 2020).

These SEZs hold considerable promise in boosting FDI in Pakistan by creating an enabling environment for business, thereby stimulating industrialization and job creation. However, the success of these zones will depend on effective governance, the provision of quality infrastructure, and the country's ability to attract and retain investment.

Geographical Perspective

From a regional perspective, it's clear that the effects of CPEC on FDI are unevenly distributed across Pakistan, with the Punjab and Sindh provinces benefitting the most. Both provinces have seen a significant rise in FDI inflows, primarily in the energy and infrastructure sectors.

Punjab is the largest province in terms of population and has a strategically important geographical location. The Sahiwal Coal Power Plant, a flagship CPEC project, is an example of substantial FDI into the region. This $1.8 billion project was funded mainly by Chinese companies, such as the Huaneng Shandong Ruyi (Pakistan) Energy (HSR), and has enhanced Punjab's power generation capacity (Warraich, 2016).

Further, Faisalabad's Allama Iqbal Industrial City, part of the Special Economic Zones (SEZs) under CPEC, is set to attract massive investment. It's being promoted as a global hub for trade and manufacturing, and according to the Faisalabad Industrial Estate Development and Management Company (FIEDMC), it's expected to attract over $5 billion of FDI (The Nation, 2020).

Sindh, particularly Karachi, has also significantly benefited from CPEC. Infrastructure projects like the Karachi-Lahore Motorway and the upgradation of the Main Line-1 (ML-1) railway have attracted substantial Chinese investment.

Moreover, the Thar Coal Power Project in Sindh, valued at around $2 billion, has bolstered the energy sector in the region (Dawn, 2018). This project, again largely funded by Chinese companies, showcases how CPEC has increased FDI in Pakistan.

The Dhabeji SEZ, located in Thatta near Karachi, is another flagship project under CPEC, designed to attract significant foreign investment. The SEZ, spread over 1530 acres, is expected to host manufacturing industries, logistics hubs, and other businesses, thereby becoming an attractive destination for FDI. However, it's worth mentioning that provinces like Balochistan and Khyber Pakhtunkhwa have seen relatively less FDI, primarily due to their geographical remoteness, security issues, and less developed infrastructure. The success of CPEC in boosting FDI across all of Pakistan, therefore, relies heavily on addressing these disparities and promoting an equitable distribution of projects.

Long-term Perspective

The completion of CPEC projects carries significant potential for future Foreign Direct Investment (FDI) in Pakistan. This potential lies primarily in the energy, transportation, and industrial sectors, as these have been the focus of the CPEC initiative.

Energy Sector

With a significant portion of the CPEC budget allocated to energy projects, the completion of these initiatives could further attract FDI. Given the need for regular maintenance and upgrades, investors may be drawn to continuous involvement in the energy sector. Also, with the increasing global shift towards renewable energy, Pakistan's focus on wind and solar projects under CPEC may attract environmentally conscious investors in the future.

Transportation Sector

The development of transport infrastructure, such as highways, railways, and ports under CPEC, is also expected to boost FDI. The improved connectivity may entice businesses related to logistics, warehousing, and supply chain management. For instance, the completed Karakoram Highway Phase II and the proposed railway mainline (ML-1) could make Pakistan an attractive investment destination for multinational freight companies.

Industrial Sector

The establishment of Special Economic Zones (SEZs) under CPEC is expected to serve as a major attraction for future FDI. SEZs, by offering tax breaks, simplified regulatory procedures, and infrastructure support, encourage businesses to invest. An example is the Rashakai SEZ, where China's Century Steel is reportedly investing $366 million (Board of Investment, 2021).

The successful completion of CPEC projects will likely enhance Pakistan's global image as an investment-friendly country. This enhanced reputation could stimulate additional FDI inflows beyond those directly related to CPEC.

However, the realization of this potential also depends on the resolution of challenges such as political stability, security concerns, regulatory transparency, and ease of doing business. Thus, it is crucial for Pakistan to continue improving its business environment and investment policies to make the most of the opportunities offered by CPEC.

Pessimists, however, express concerns over the mounting debt, transparency, and the economic viability of these projects. They argue that the repayment obligations could strain Pakistan's already fragile economy. Furthermore, concerns over the lack of transparency and fears of becoming overly reliant on China have also been raised (Khan et al., 2020).

Recommendations

Given the analysis above, Pakistan can take several steps to further increase Foreign Direct Investment (FDI) and maximize the benefits of the China-Pakistan Economic Corridor (CPEC):

Invest in Human Capital: To ensure a sustainable influx of FDI, Pakistan needs a skilled workforce that can meet investors' needs. Investment in education, vocational training, and skills development should be a priority.

- Strengthen Legal and Regulatory Frameworks: A well-defined, transparent, and consistent regulatory environment is essential to attracting and retaining FDI. Pakistan should continue improving its legal framework and making its business regulations more transparent and straightforward.
- Improve Infrastructure: While CPEC has greatly improved infrastructure, particularly in Punjab and Sindh, more remote regions require similar attention. Better infrastructure can attract more diversified FDI across different regions of Pakistan.
- Security and Political Stability: Security concerns and political instability often deter foreign investors. It's crucial to maintain and improve the security situation and political stability to reassure investors.
- Leverage Special Economic Zones (SEZs): SEZs, with their incentives such as tax breaks and simplified regulatory procedures, can be significant attractors of FDI. Efficient management and marketing of these zones, alongside ensuring their completion in a timely manner, are vital steps.

- Promote Green Energy Investments: Given the global shift towards renewable energy, promoting green energy projects could attract FDI from environmentally conscious investors.
- Expand Bilateral Investment Treaties (BITs): BITs can encourage FDI by providing legal protection to foreign investors. Pakistan could consider expanding its network of BITs, particularly with countries known for outbound FDI.
- Improve Ease of Doing Business: Implementing reforms to simplify business registration, taxation, property registration, and contract enforcement processes can significantly improve Pakistan's ease of doing business rank, thereby making it more attractive to foreign investors.

Conclusion

In conclusion, the China-Pakistan Economic Corridor (CPEC) has undoubtedly enhanced the Foreign Direct Investment (FDI) landscape of Pakistan, reflecting the transformative potential of such large-scale infrastructural projects. It has amplified opportunities, especially in the realms of energy, transportation, and industrial cooperation, thereby significantly shaping the country's economic prospects.

However, the influence of CPEC is not uniform, which is evident from the disparities across various regions. The benefits have been predominantly skewed towards provinces like Punjab and Sindh, underscoring the need for a more inclusive strategy that extends these advantages across all provinces, particularly Balochistan and Khyber Pakhtunkhwa.

The potential for future FDI as CPEC projects reach completion is promising, presenting a myriad of opportunities for both domestic and foreign investors. Nonetheless, for this potential to translate into actual, far-reaching benefits, Pakistan needs to adopt a comprehensive approach that addresses the pressing challenges of the time - human capital development, robust and transparent regulatory frameworks, infrastructure improvements, enhanced security, and ease of doing business.

In essence, while CPEC has indeed facilitated a surge in FDI in Pakistan, further amplification of this trend depends significantly on how well Pakistan manages the intricate web of economic, political, and security concerns. If addressed meticulously, these challenges can transform into opportunities, enabling Pakistan to maximize the benefits of CPEC, thereby fostering sustainable economic growth.

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