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CHINESE INVESTMENT IN PAKISTAN: POSSIBLE IMPLICATIONS

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NOTE FROM THE EDITOR

While many laud the government for taking the initiative of China-Pakistan Economic Corridor (CPEC), some remain cautious of its possible drawbacks for Pakistan. What is important is to analyse what real impact Chinese investment has on our economy - both positive and negative. This month's issue shares the details of CPEC and highlights its implications for Pakistan.

In my commentary, I share with you the case of politicization of the credit market today where politically connected firms have better access to credit but worse is the fact that the federal government crowds out private sector, dominating 70% of the credit market. The case of circular debt and rising black economy in the property market is also explored.

In the end, we present the snapshot of the economy, which again is not very positive. The balance of trade is still declining with dwindling remittances. The LSM growth is also not up to its potential. One piece of good news is the improvement in Pakistan's doing business ranking, largely owing to improved access to credit and the introduction of an electronic "Web Based One Customs Platform" which facilitates the process of importing and exporting.

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Business Climate Review

by Ali Salman

The Business Climate Review sums up important developments spanning the entire federal government economic governance over the previous month. It discusses possible consequences of decisions, policies and regulations announced by the federal cabinet, regulators and Federal Board of Revenue for the business climate of Pakistan. The analysis is based on the idea that economic freedom is good for the business climate and any law that increases arbitrariness, red-tape, and government involvement is counterproductive. Also, we believe that the government should not choose winners and losers by legalizing exemptions or favors.

Politically Connected Families or a Rent Seeking Government- which is the bigger evil?

A new report by the World Bank reveals that politically connected firms in Pakistan received 45 per cent more credit than others between 1996 and 2002. Such loan recipients were less productive and had 50pc higher default rates, says World Development Report 2017.

This should be considered surprising, as the banks were being privatized extensively during this time period. In fact, one of the main reasons for their privatization was their excessive exposure to political lending under nationalization. One is reminded of a rather old but perhaps still relevant finding by Dr. Mehboob ul Haq, who had established, in 1960s, that almost two-thirds of commercial credit remained concentrated in the famous '22' families. The scale is very different now, and the number of 'selected' families has grown extensively but the question is whether we have come out of that structural bias in our lending systems or not. The World Bank report implies we have not.

One related fact which the World Bank report did not highlight, and perhaps will not, is how the government controls the credit market today. The federal government receives 70% of all commercial credit available today in the country! Depends on how what views this development, there cannot be anything more political than the government dominating the credit and then spending it to meet its own projects. Not even 22 or 2200 families!

Property Value in Black & White

A huge amount of black money is being pumped into the property market which

runs the risk of creating a real-estate bubble, a sub-committee of the National Assembly's Standing Committee on Finance claimed recently. A recent report by Pakistan Real Estate Investment Forum claiming that the property is heading towards a burst after imposition of FBR determined valuation has been disputed by a Parliamentary Sub Committee established on the subject.

According to a news item (Dawn, 7th February 2017), the members of the Committee have held that property market is becoming a safe haven for black money in the country and the investors demand unbacked by genuine customer demand is causing the prices to remain high.

This is not a new allegation. Property market in Pakistan has been long associated with the black money, tax evasion and unproductive allocation of capital. Part of this is caused by the lack of appropriate policy. The current policies impose unnecessary restrictions on vertical urban restrictions thus pushing the market towards horizontal expansion, which end up precious agriculture land and increases pressure on the city management. The market transactions are usually cash based for fear of documentation. Hence there is certainly a need of formalization of the market. However, these efforts should not lead to market depression in the long run. The role of FBR in value determination is questionable and will only invite more trouble, more red tape and more corruption. While taxes on incomes have to be paid by everyone the value of a transaction has to be market based.

Life goes in a circle for our energy planners

The circular debt is back in circulation though it never went away in reality. According to a news item (Express Tribune, 9th February 2017), it has again reached to Rs 370 billion. It is accompanied by the recent advertisements by the independent power producers indicating their intention to call sovereign guarantees if their payments are not cleared immediately. In the past, these calls have been responded by the knee jerk reaction. Government typically pays a small amount immediately, fixed nothing and then promises to pay more in future and then forgets. The reaction is likely to be the same this year.

As long as the government sticks to a central purchase system of electricity, where it is the sole buyer, the problem of circular debt will not go away. There is huge unmet demand in the electricity market of the country and much of it is actually able to enter into independent contracts and pay directly instead of central government. Unless we move to a wholesale market of electricity, we will not be able to solve the perennial energy crisis. The present government promised this and then forgot, much like it forgot to honour its commitments to IPPs.

MARKET ANALYSIS

Chinese Investment in Pakistan:
Possible Implications

Introduction

China's massive expansion into global markets has transformed the world's economic landscape. The largest country in the world by population has combined state-led economic regulation with steady liberalization over the last three decades, achieving massive growth rates to become the second-largest economy in the world. China currently makes up the second-largest share of the world's GDP at around 15%,[1] which is expected to increase to 20% by 2050. 2050 is also cited as the year when China is projected to overtake the USA as the world's largest economy.[2]

The effects of China's economic expansion are far-reaching, leading it to be viewed as "the factory to the world."[3] Chinese goods and companies are ubiquitous, which comes as no surprise considering how China became the world's largest trading nation in 2013.[4] The country's status as an economic giant is more or less undisputable.

What does China's economic activity mean for Pakistan? There is much talk of China surpassing the US and Europe in coming years, but developing nations such as Pakistan are likely to be affected just as much, if not more. China is Pakistan's biggest trade partner, with bilateral trade between the two countries reaching USD 18.9 billion in 2016, although the State Bank of Pakistan gives a much lower figure (USD 11.1 billion).[5]

The giant's latest and greatest involvement in Pakistan is the China-Pakistan Economic Corridor (CPEC), a 3200km trade route connecting China's Xinjiang region with Pakistan's Gwadar port.

Structure of the analysis

[1] World Bank, Data Bank, Accessed 20 March 2017, http://data.worldbank.org/indicator/NY.GDP.MKTP.CD.
[2] John Hawksworth, Rob Clarry, and Hannan Audino,"The World in 2050 – Summary Report," PwC, February 2017, http://www.pwc.com/gx/en/world-2050/assets/pwc-world-in-2050-summary-report-feb-2017.pdf.
[3] Alex E. Fernandez and Barbara Hogenboom, "China's Growing Economic and Political Power: Effects on the Global South," The Asia-Pacific Journal 5, no. 12 (2007): 1-19.
[4] Angela Monaghan, "China surpasses US as world's largest trading nation," The Guardian, 10 January 2014, https://www.theguardian.com/business/2014/jan/10/china-surpasses-us-world-largest-trading-nation.
[5] Nasir Jamal, "Mother China: A 'Chinese revolution' sweeps across Pakistan," Herald, 28 January 2017, http://herald.dawn.com/news/1153413.

The USD 57-billion-dollar initiative includes energy and infrastructure projects scattered across the country, the crescendo being the development of Gwadar.[6]

This report takes a look at China's investment climate and its previous investments in similar countries. In light of this, we will analyze what the future holds for Pakistan.

1. China's Trade and Investment Climate

China is currently engaging in a spate of overseas investments, approaching USD 1.5 trillion.[7] It is now ranked as the third-largest source of overseas investment, with 84.7 per cent of these investments taking place in developing and transition economies.

However, China did not always look abroad to facilitate its economy. Prior to 1978, China's economy was socialist and state-controlled, maintaining policies that insulated the country from international markets. The economy was poor, stagnant, highly controlled, and inefficient.[8]

China opened up to foreign trade and investment in 1979, implementing free market reforms. As part of its efforts to be more competitive globally, it joined the World Trade Organization in 2001. Since then, it has emerged as a key economic power – the world's largest manufacturer, trader, holder of foreign exchange reserves, and the world's largest economy (on the basis of purchasing power parity).[9]

As far as foreign direct investment (FDI) is concerned, China's inflows rose 6% in 2015, from the previous year, reaching USD 126.3 billion. This is mainly because of China's steady high economic growth and its growing domestic market.[10]

However, China bears a more restrictive foreign investment regime than its major trading partners, such as the United States. Even though it was the top destination for FDI in 2015, the government employed several protectionist measures, encouraging investment in some sectors of the economy, and prohibiting it in others. Industrial policies promote state-owned and other favourite firms. According to a report by the US Department of State, vague regulatory laws, shortage of qualified management and employees, increasing protectionism, and infringement of intellectual property rights are major challenges for companies looking to invest in China.[11]

China is performing remarkably well abroad as of now, but the future of Chinese overseas investments may be uncertain, though local investment in China could look up. In December 2016, Beijing announced plans to impose controls on the foreign investments of Chinese firms. This was after several companies started investing abroad in response to a dwindling domestic economy. Although foreign investment surged, inflows were stagnant, raising concerns about capital flight and declining domestic growth. Commerce minister Gao Hucheng announced that it would be made easier for foreign firms to invest in China, while decreasing Chinese firms' foreign spending.[12]

Results were seen as soon as January 2017, when China's overseas property purchases and investments experienced a slump due to the imposed controls. China's outbound investment fell 35.7% to

[6] Nasir Jamal, "The Cost of CPEC," Dawn.com, 12 march 2017, https://www.dawn.com/news/1320028/the-cost-of-cpec.
[7] "China Global Investment Tracker," American Enterprise Institute, https://www.aei.org/china-global-investment-tracker/.
[8] Wayne M. Morrison, "China's Economic Rise: History, Trends, Challenges, and Implications for the United States," Congressional Research Service, 21 October 2015, https://fas.org/sgp/crs/row/RL33534.pdf.
[9] Ibid.
[10] Bureau of Economic and Business Affairs, "2016 Investment Climate Statements – China," US Department of State, 5 July 2016, https://www.state.gov/e/eb/rls/othr/ics/2016/eap/254271.htm.
[11] Ibid.
[12] Rob Davies, "China to rein in outward investments as domestic growth stalls," The Guardian, 26 December 2016, https://www.theguardian.com/business/2016/dec/26/china-to-rein-in-foreign-investment-as-domestic-growth-stalls.

its lowest in 16 months.[13] The long term repercussions are yet to be seen.

2. China and Pakistan – A history of trade and investment

Pakistan and China have a trade history almost as old as Pakistan itself, with the two countries trading since 1949. The first trade agreement between the two countries was signed in 1963, however, when they both granted each other Most Favoured Nation (MFN) status, cementing their commercial and trade ties.[14]

However, this did not give a very significant boost to trade, as the value of traded goods stood at just USD 1 billion in 2003, compared to the USD 6.2 billion trade between China and India, even though their trade relations were established in the late 1990s.[15] China's late entry into the global market, as well as Pakistan's prior policies of connecting with open market economies, is cited as a reason for the slow burgeoning of trade between Pakistan and China. This called for a further strengthening of trade relations. A Preferential Trade Agreement (PTA) became operational between the two countries in 2004, while a Free Trade Agreement (FTA) was formalized in 2007.[16]

This caused a surge of bilateral trade, with the value of traded goods reaching USD 14 billion in 2013. This figure is expected to reach USD 20 billion or more by 2020.[17] Though Chinese goods did enter Pakistan prior to the signing of the FTA, smuggling routes were often used. The FTA sought to address this by decreasing import taxes on both sides of the border and removing other administrative hurdles. Nevertheless, a significant disparity still remains between official and unofficial trade figures, indicating that smuggling is still prevalent.[18] In any case, trade swelled, with Chinese products flooding Pakistani markets. Currently, the trade volume between the two countries between 2000 and 2015 stands at more than USD 100 billion, while contracts worth more than USD 150 billion have been signed over the same period.[19]

Chinese investment in Pakistan similarly displayed slow initial growth. China-Pakistan trade had been growing steadily in the years leading to 2005, from USD 1 billion in 2000 to USD 4.5 billion in 2005. However, most of this trade was in China's favour, so Pakistan sought to attract Chinese investments in the industrial sector in order to address this imbalance by increasing Pakistan's FDI. Although FDI did increase by around 600% between 2000 and 2005, very little of this was from China. Unfortunately, China was not forthcoming with investing in Pakistan. Although political meetings consisted of much talk of facilitating investment in Pakistan, such plans were not put into practice for a long time, and Chinese investments in Pakistan remained low.[20]

More recently, in 2015, Chinese President Xi Jinping formally announced a USD 46 billion investment in Pakistan (now USD 57 billion), in the form of the China-Pakistan Economic Corridor (CPEC). Since then, Chinese investment in Pakistan has seen a major boost. The following section takes a closer look at Chinese investments in Pakistan under CPEC.

3. The Current Scenario: CPEC

The initial announcement of the massive figure of USD 46 billion was met with

[13] Yawen Chen, "China's overseas property purchases, investments slump as capital controls bite," 16 February 2017, http://www.reuters.com/article/us-china-economy-fdi-idUSKBN15V0DB.

[14] Nasir Jamal, "Mother China: A 'Chinese revolution' sweeps across Pakistan," Herald, 28 January 2017, http://herald.dawn.com/news/1153413.

[15] "India Imports," World Integrated Trade Solution, Accessed 21 March 2017, http://wits.worldbank.org/CountryProfile/en/Country/IND/StartYear/2001/EndYear/2005/TradeFlow/Import/Indicator/MPRT-TRD-VL/Partner/CHN/Product/all-groups

[16] Fazal-ur-Rehman, "Pakistan-China Trade and Investment Relations," Strategic Studies, 12 January 2011, http://issi.org.pk/wp-content/uploads/2014/06/1299822989_45060000.pdf.

[17] Nasir Jamal, "Mother China: A 'Chinese revolution' sweeps across Pakistan," Herald, 28 January 2017, http://herald.dawn.com/news/1153413.

[18] Ibid.

[19] "Pakistan and China relations: 65 years of friendship to strategic partnership," Pakistan Today, 15 May 2016, http://www.pakistantoday.com.pk/2016/05/15/pakistan-and-china-relations-65-years-of-friendship-to-strategic-partnership/.

some skepticism, as economic relations between China and Pakistan were historically poor. The government, on the other hand, displayed much optimism at such a large investment. Through the beginning of 2015, the debate centered on whether the project would take off at all, as previous talks had rarely translated into action.[21]

CPEC is part of the Chinese 'One Belt, One Road' initiative, which will extend to South and Southeast Asia, the Middle East, and Europe, linking China to the world through a network of roads, railways, ports, and pipelines.[22]

In April 2015, when CPEC was finalized after the first announcement in 2013, 51 Memorandums of Understanding were signed between China and Pakistan. These covered eight projects and five joint energy projects. In addition to the much talked about energy and infrastructure undertakings, several agreements included social, economic, technological and cultural partnerships. These include exchanges in television and radio. Furthermore, the Industrial and Commercial Bank of China opened a branch in Lahore, the countries jointly set up the China-Pakistan Joint Cotton Bio-Tech Laboratory, and a China Culture Center was established.[23]

However, the current stage of CPEC focuses largely on energy, infrastructure, and industrial cooperation. Some major projects include a 1320MW coal-fired power plant in Thar, a 900MW solar energy park in Bahawalpur, construction of the Karachi-Lahore Motorway, and the development of the Gwadar port, all of which are currently underway.[24] In fact, a Chinese company has land use rights to some 280 hectares of land in Gwadar, for a period of forty-three years. This signals the long-term nature of the phase of Pakistan-China relations inaugurated by the CPEC.[25]

What does this level of investment from China – involving massive funds, Chinese companies, and multiple long-term projects – mean for the future of Pakistan? What can we expect from the next few years? An examination of the results of Chinese investments in other countries would be instructive at this point.

4. Looking ahead: Implications for Pakistan

The implications of CPEC for Pakistan may be both positive and negative, as commentators often highlight.

Whether the positives will outweigh the negatives cannot be said with much certainty yet. Chinese investments have sprung up fairly recently, so long-term analysis of their effects may be difficult to gauge, with a lot of commentary on China being informed by emotion and suspicion.[26] Nonetheless, this report will make an effort to consolidate the possible implications of such large-scale Chinese investment for Pakistan.

The Positives

Ishrat Husain, former State Bank Governor and Public Policy Fellow at the Woodrow Wilson Centre in Washington, tends to view this Chinese investment in a relatively favourable light. Husain rightly points to Pakistanis' deep-seated cynicism as the reason why mentions of CPEC are not often met favourably. Certainly, there will be numerous positives associated with the entry of an economic powerhouse such as China, a country which has successfully pulled more than 800 million of its citizens out of poverty.[27]

[20] Fazal-ur-Rehman, "Pakistan-China Trade and Investment Relations," Strategic Studies, 12 January 2011, http://issi.org.pk/wp-content/uploads/2014/06/1299822989_45060000.pdf.
[21] Andrew Small, "CPEC – Corridor of Uncertainty," Herald, 10 February 2016, http://herald.dawn.com/news/1153330.
[22] Ishrat Husain, "Corridor of Power," Herald, 2 June 2015, http://herald.dawn.com/news/1153156.
[23] Raymond Lee, "The Strategic Importance of Chinese-Pakistani Relations," Al-Jazeera Centre for Studies, 3 August 2016, http://studies.aljazeera.net/en/reports/2016/08/strategic-importance-chinese-pakistani-relations-160803101555719.html.
[24] "CPEC-Energy Priority Projects," China Pakistan Economic Corridor, http://cpec.gov.pk/energy.
[25] Ibid.
[26] Thilo Hanemann and Daniel H. Rosen, "China Invests in Europe: Patterns, Impacts and Policy Implications,"Rhodium Group, June 2012.

1. Development of rural areas: Major developments are expected to occur in backward areas on the Gwadar-Kashgar motorway, for example. Three proposed motorways are part of this plan, which will pass through areas of Sindh, Balochistan, and Khyber Pakhtunkhwa. These will have the effect of linking many backward areas to the rest of Pakistan.[28] This may lead to much development of rural areas, giving citizens greater access to healthcare and education facilities as well as jobs. Ahsan Iqbal is quick to point out that CPEC is unlike previous mega-projects, as it is inclusive and is based on improving historically disadvantaged areas such as Balochistan.

2. A possible end to load shedding: The massive energy infrastructure to be constructed under CPEC is expected to hugely benefit Pakistan as well. All in all, the CPEC energy projects are adding 10,000MW to the national grid by 2030 and are the basis behind the sitting government's promise of ending load-shedding by 2018. This development alone is enough to propel the economy forward with growth rates not seen in decades.[29]

3. Economic benefit: The overwhelming benefit of these Chinese investments is expected to be economic in nature. Foreign direct investment from China, as with any FDI, should have the effect of increasing the welfare of both producers and consumers. Chinese firms will have the benefit of exploring a new market in the form of Pakistan, while Pakistani consumers will be exposed to more choices of goods, lower prices due to competition, and new and innovative products. FDI, ideally, will also bring in more jobs and tax revenues.[30] A study found that Chinese direct investors created about 45,000 jobs in the European Union as of 2012.[31] Former KCCI Chairman and President Employer's Federation Pakistan, for example, foresees the establishment of warehouses, port activity, industry, hotels, etc., particularly in Balochistan, which is expected to be a key beneficiary.[31] This will hopefully give rise to a surge in new jobs for the local population.

Furthermore, as Ahsan Iqbal points out, CPEC's many routes mean a massive improvement in trade with other countries in the region. This is also likely to give rise to peaceful relations between countries because of improved trade relations.[33]

4. Knowledge spillovers: There are also expected to be knowledge spillovers due to FDI – Pakistani workers may be trained in new skills and technologies, and R&D activity may increase. Majyd Aziz expects new technologies and production techniques to be taken up in the textile industry, for example.[34]

Box: The Case of Sri Lanka

The Colombo Port City Project worth USD 1.4 billion, also falls under the One Belt, One Road initiative. The Chinese were handed a 99 year land lease to construct the mini-city, similar to China's 43 year lease in Gwadar. The negatives of Chinese involvement in Sri Lanka included:

- Millions in debt, with interest alone being USD 30 million a year
- More land leases to China, in return for easing loan conditions
- Friction in Sri Lanka's relationship with India, as China took over important ports near India

A few projects, such as a container terminal, did meet with success. But for the most part, China reaped more benefits than Sri Lanka.

[27] Ishrat Husain, "Corridor of Power," Herald, 2 June 2015, http://herald.dawn.com/news/1153156.
[28] Ibid.
[29] "Load shedding to end in current government's tenure, NA told," The Nation, 2 February 2017, http://nation.com.pk/newspaper-picks/02-Feb-2017/loadshedding-to-end-in-current-govt-s-tenure-na-told.
[30] Thilo Hanemann and Daniel H. Rosen, "China Invests in Europe: Patterns, Impacts and Policy Implications,"Rhodium Group, June 2012.
[31] Ibid.
[32] "Brief Recording," Business Recorder, 19 December 2016, http://epaper.brecorder.com/2016/12/19/17-page/829859-news.html.
[33] Ahsan Iqbal, "CPEC: A positive outlook," The Express Tribune, 28 August 2016, https://tribune.com.pk/story/1171552/cpec-positive-outlook/.
[34] Ibid.

The Negatives

According to economist Mushtaq Khan of Bank Alfalah, many Pakistanis do approach CPEC with some caution. CPEC is currently the largest foreign investment in Pakistan, but the burden of debt that Pakistan will face is still not clear. It has been aptly noted that official information on CPEC activities is not exactly forthcoming, as many Pakistanis have noticed the large number of Chinese citizens in the country, but are not entirely sure as to the nature of their presence in Pakistan.[35] Some fears associated with this level of Chinese investment are:

1. The loss of livelihoods: This is a negative externality that is certainly being faced due to CPEC and other Chinese developments in Pakistan. In a detailed investigative piece by Maqbool Ahmed for Herald, it was found that fishermen in Gwadar have lost a number of important fishing spots because of port construction. Furthermore, the tightening of security for Chinese personnel means that fish traders and fishermen have limited access to Gwadar's old fish harbor. New harbours are being built, but at a distance from Gwadar that will make them inaccessible for many existing fishermen. It was reported that some fishermen have already given up on their profession.[36] Another report found that a ceramics manufacturer shut down and had to fire 500 employees because of the influx of Chinese tiles in the market, sold at a price below the production cost of local tiles.[37]

2. Low returns: Abdul Hafeez Jamali, a professor at Habib University and a specialist in the anthropology of globalization and development, is skeptical of the success of CPEC. According to him, a mega project of this stature is seen as a way of achieving quick economic growth, but such projects do not have a high success rate. He cites the Lahore-Islamabad motorway, which is "generating much less revenue than anticipated at the time of its planning and construction."[38]

3. Heightened tension with India and within Pakistan: As in the case of Sri Lanka, highlighted in the box, India's opposition of CPEC may create more friction between Pakistan and India.[39] Tensions between China and India, coupled with hostility between Pakistan and India have compounded in the form of India's vehement opposition of the project. Pakistan may have to tread on eggshells as far as India is concerned, so as to not exacerbate tensions.

Furthermore, an issue that creates frequent roadblocks is interprovincial rivalry within Pakistan, with less developed areas fearing that most of the benefits of CPEC will accrue to Punjab. Several concerns about road networks have been laid to rest, with the motorways expected to pass through numerous impoverished areas. However, disputes are frequent and fuelled by the aforementioned lack of accurate information.

4. High security costs: Given Pakistan's precarious security situation, more than USD 20 million have been earmarked for training and arming a massive force to protect CPEC projects and workers from China.[40] Further security divisions are expected to be created. A recent development has seen the government attempt to add the cost of this security into consumers' utility bills.[41] The decision is yet to be finalized but shows how these costs can be become a burden for the common consumer.

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[35] Danish Hyder and Mushtaq Khan, "CPEC: The devil is not in the details," Herald, 11 January 2017, http://herald.dawn.com/news/1153597.
[36] Maqbool Ahmed, "CPEC: Hopes and fears as China comes to Gwadar," Herald, 14 March 2017, http://herald.dawn.com/news/1153685.
[37] Nasir Jamal, "Mother China: A 'Chinese revolution' sweeps across Pakistan," Herald, 28 January 2017, http://herald.dawn.com/news/1153413.
[38] Ibid.
[39] Jeff M. Smith, "China's investments in Sri Lanka," Foreign Affairs, 23 May 2016, https://www.foreignaffairs.com/articles/china/2016-05-23/chinas-investments-sri-lanka
[40] Mushtaq Ahmed, "China's role and interests in Central Asia: China-Pakistan Economic Corridor," 21 February 2017.
[41] "CPEC Security Cost," Dawn, 22 March 2017, https://www.dawn.com/news/1321981.

Conclusion

The preceding discussion reveals how China's overseas finance is becoming a force to be reckoned with. This holds special importance for developing countries such as Pakistan, where China is currently making a massive investment.

The exact results of CPEC and other Chinese investments in Pakistan are difficult to predict, as China is a relatively recent foreign investor. Possible positive effects include increased employment, a stronger economy, development of rural areas, a solution to the energy deficit, and positive knowledge spillovers.

On the other hand, experiences such as that of Sri Lanka act as a cautionary tale to Pakistan. Though government officials tout Pakistan's economic ties with China as a cure-all, Chinese investment and goods have the potential to put Pakistani companies out of business, exacerbate tensions within Pakistan as well as with India, and overall not yield as high returns as are expected from CPEC.

Whether the CPEC balance tips in favour of the positive or the negative is yet to be seen. Pakistan needs to implement widespread economic reforms to make sure that it reaps the benefit of CPEC, instead of simply financing debts. Pakistan's economic climate will be the deciding factor in whether the corridor plunges Pakistan into dire economic straits or launches it onto a more sustainable path.

SNAPSHOT OF KEY ECONOMIC INDICATORS

Outlook of Pakistan's Economy (July-March FY17)

The inflation rate as of Feb 2017 was 4.2%; it remained quite stable during the fiscal year, staying within 3.6-4.2%. The PSX-100 index rose from 41,300 on 1st November, 2016 to 48,970 on 24th March, 2017. During the month of January 2017, the index crossed the 50,000 mark for the first time in history. Pakistan has seen a 6% increase in FDI in 8m (FY17) compared to 8m (FY16). Portfolio investment in Pakistan improved by 496% 8-month (FY17) as against 8m (FY16).

The stock market performance however does not represent the true picture of the economy. Despite the soaring stock market, the balance of trade in goods and services both have deteriorated. The current account deficit has widened by 121% to $5.473 billion during the first eight months of FY17 compared to $2.482 billion in the same period of previous year.

Worker's remittances have declined by 2% in 8m (FY17). Remittances from each of the four major countries with expat Pakistani population- USA, UK, KSA, and UAE, have taken a dip.

LSM growth rate though positive, is still not good enough at 2.8% on MoM basis in Jan-17. Trade statistics show that exports of sugar and raw cotton have taken a massive hit whereas in sum, exports price growth remained -2%. While currency exchange rates have remained more or less stable, crude oil prices in the international market have steadily risen and in the domestic market, Pakistan too jacked up prices of petroleum products.

Overall, Pakistan's ease of doing business rank has improved from 148 in 2016 to 144 in 2017. The most improvement has been achieved in access to credit. Exporting and importing have been made easier by enhancing electronic "Web Based One Customs Platform".

Table 1: Economic Snapshot

Particular	Reporting Period	Value
T-Bill		**(%)**
03-M	Feb-17	5.9
06-M	Feb-17	5.9
12-M	Feb-17	5.9
PIB 10-years	Feb-17	8.1
6-M Kibor	Feb-17	6.1
Discount Rate	Feb-17	5.8
Inflation	**Feb-17**	**4.2**
External Indicatrors		**($ Bn)**
Export	Feb-17	2.4
Import	Feb-17	4.6
Trade Deficit	Feb-17	-2.2
Home Remittances	Feb-17	1.4
Current Account	Feb-17	-744
FDI ($ Mn)	Feb-17	123
Public Finance		**(Rs. Bn)**
Tax Collection	Sep-16	38
Direct Taxes	Sep-16	18
Indirect Taxes	Sep-16	20
Credit to Private Scetor (Rs. Bn)	As of Jan 17	4,369
LSM growth MoM (%)	Sep-16	2.8
FX Reserves ($ Bn)	10 Mar 17	22.3

Sources: SBP, Finance Ministry

Table 2: Key Targets and Projections

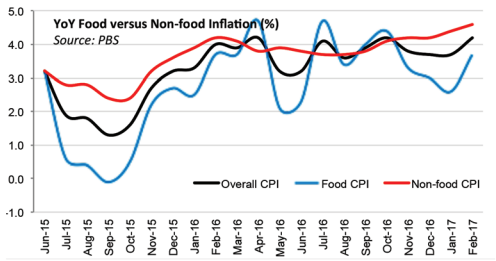
	Govt Target*	SBP Projection**	IMF Projection***	ADB Forecast****
		Percent		
Real GDP Growth	5.7	5.7	5	5.2
CPI- Full year average	6	4.5 - 5.5	5.2	4.5
		% change		
Export	n.a	n.a	4.1	n.a
Import	n.a	n.a	9.9	n.a
		% of GDP		
Current a/c Balance	n.a	n.a	-1.8	-1.2
Fiscal Balance	-3.8	n.a	-3.8	-5.3
Remittances ($ Bn)	n.a	n.a	20	n.a
Tax Revenue (Rs. Bn)	3,956	n.a	4,244	n.a

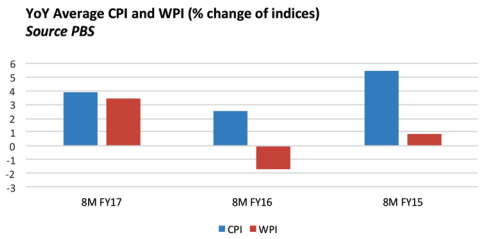
*Sources: *Budget in Brief 2016-17, **Monetary Policy Statement, ***IMF Country Report (June 2016), ****AsianDevelopment Outlook 2016*

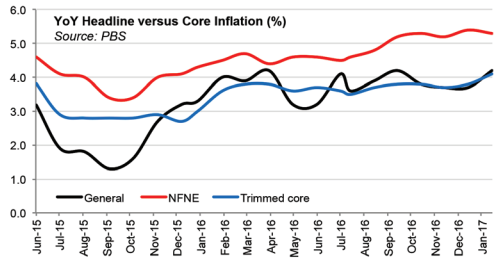
Table 3: Balance of Payment Account - Key Items Only

$ (Mn)	8M(FY17)	8M(FY16)	% change
Current Account Balance	-5,473	-2,482	n.a
Balance on Trade in Goods	-15,395	-12,133	
Exports of Goods FOB	14,051	14,339	-2%
Imports of Goods FOB	29,446	26,472	11%
Balance on Trade in Services	-1,986	-1,804	
Exports of services	3,529	3,637	-3%
CSF inflows	73	80	-9%
Imports of services	5,515	5,441	1%
	8M (FY17)	**8M (FY16)**	
Workers' Remittances	**12,363**	**12,677**	-2%
U.S.A	1516	1656	-8%
U.K	1446	1606	-10%
Saudi Arabia	3,573	3,834	-7%
UAE	2,761	2,807	-2%
	8M (FY17)	**8M (FY16)**	
Direct Investment in Pakistan	1285	1,212	6%
U.S.A	-7	-182	n.a
U.K	-50	-50	0%
Saudi Arabia	54	68	-20%
China	274	538	-49%
Portfolio Investment in Pakistan	650	109	496%
Equity	-355	-348	2%
Debt	1,005	457	120%

Figure 1: Trends in Inflation

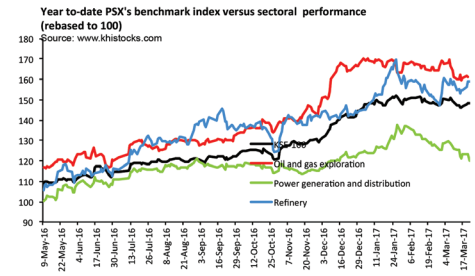


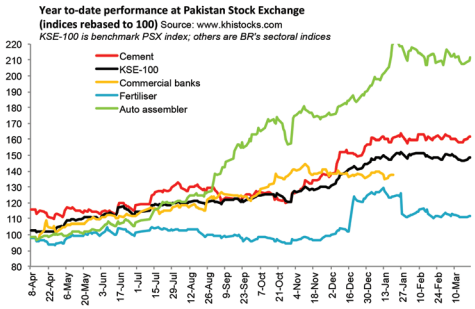




Source: PBS

Figure 2: Performance at Stock Market





Source: www.khistocks.com
KSE-100 is benchmark, PSX index, others are sectoral indices

Table 4: Key Export Categories: Percentage Year on Year Change (FY16)

KEY EXPORT CATEGORIES - PERCENTAGE CHANGE 8M FY17 over 8M FY16					
Commodities (units)	**Quantity (total)**	**Price ($ Mn)**	**Price (% change)**	**Quantity (% change)**	**ARP* (% change)**
Total	n.a		-2%	n.a	n.a
Food (M.T)		**2,209**	**-7%**	**n.a**	**n.a**
Rice	**2,413,340**	**992**	**-14%**	-11%	**-3%**
Basmati	**282,085**	**294**	**-26%**	-13%	**-15%**
Non-Basmati	**2,131,255**	**697**	**-8%**	-11%	**4%**
Sugar	**15885**	**34**	**-56%**	-90%	**-100%**
Textile	**n.a**	**8,183**	**-4%**	n.a	
Raw cotton (M.T)	**22,319**	**36**	**-48%**	-53%	**11%**
Cotton yarn (M.T)	**307,315**	**749**	**-19%**	4%	**-22%**
Cotton cloth (TH.SQM)	**1,260,905**	**1,428**	**-6%**	-14%	**9%**
Knitwear (TH.DOZ)	**78,481**	**1,532**	**-1%**	2%	**-3%**
Bedwear (M.T)	**234,564**	**1,410**	**1%**	9%	**-7%**
Towel (M.T)	**117,371**	**426**	**-12%**	-4%	**-9%**
Readymade garments (TH.DOZ)	**21,838**	**1,481**	**6%**	3%	**2%**
Art, silk & synthetic textile (TH.SQM)	**88,183**	**173**	**-5%**	-55%	**111%**
Petroleum products	**n.a**	**300**	**-6%**	n.a	
Naphtha (M.T)	**78,215**	**216**	**-7%**	2439%	
Other manufacturing goods	**n.a**	**2,310**	**-7%**	n.a	
Sports good	**n.a**	**350**	**1%**	n.a	
Football (TH.DOZ)	**2,040**	**128**	**-10%**	-10%	**0%**
Gloves (TH.DOZ)	**1,518**	**90**	**17%**	10%	**6%**
Leather tanned (TH.SQM)	**10,259**	**246**	**-11%**	-8%	**-2%**
Leather products	**n.a**	**309**	**-8%**	n.a	
Leather garments (TH.DOZ)	**540**	**208**	**-5%**	-10%	**5.0%**
Leather gloves (TH.DOZ)	**3,088**	**65**	**-8%**	-7%	**-1%**
Footwear (TH.Paris)	**6,373**	**59**	**-8.3%**	-19%	**13.6%**
Surgical goods	**n.a**	**244**	**-9%**	n.a	
Chemical & pharma products	**n.a**	**664**	**1%**	n.a	
Plastic material (M.T)	**100,624**	**234**	**-3%**	28%	**-24%**
Engineering goods (TH.NOS)	**n.a**	**115**	**-21%**	n.a	
Cement (M.T)	**3,440,466**	**185**	**-22%**	-14%	**-8%**
All other items	**n.a**	**779**	**9%**	na	

*ARP= Average Realised Price

Sources: PBS

Table 5: KEY IMPORT ITEMS - PERCENTAGE CHANGE 8M(FY17) over 8M(FY16)

Key Import Items - Percentage YoY Change FY16					
Commodities (units)	**Quantity (total)**	**Price ($ Mn)**	**Price (% change)**	**Quantity (% change)**	**APR* (% change)**
Total		11,724	10%		
Food Group (M.T)	**n.a**	**3,477**	**17%**	**n.a**	**n.a**
Tea	145,714	361	5%	22%	-14%
Palm Oil	1,673,121	1,149	8%	-6%	15.0%
Pulses	781,126	523	63%	23%	33.0%
All other food items	n.a	1,087	24%	n.a	n.a
Machinery Group	**n.a**	**4,576**	**12%**	**n.a**	**n.a**
Power generation	n.a	758	3%	n.a	n.a
Textile Group	n.a	415	35%	n.a	n.a
Electrical	n.a	803	-8%	n.a	n.a
Telecom	n.a	612	-25%	n.a	n.a
Transport Group	**n.a**	**1,608**	**39%**	**n.a**	**n.a**
Road Motor	n.a	1,144	38%	n.a	n.a
CBU Heavy Vehicles	n.a	62	85%	n.a	n.a
CBU Motor cars	n.a	113	78%	n.a	n.a
CKD Heavy Vehicles	n.a	359	160%	n.a	n.a
CKD Motor cars	n.a	367	-5%	n.a	n.a
Other transport	n.a	91	249%	n.a	n.a
Petroleum Group (M.T)	**n.a**	**6,768**	**15%**	**n.a**	**n.a**
Petroleum Products	9,388,410	4,144	16%	50%	-23%
Petroleum Crude	5,275,798	1,778	-7%	38%	-33%
Textile Group (M.T)	**n.a**	**2,112**	**1%**	**n.a**	**n.a**
Agriculture Group (M.T)	**n.a**	**4,567**	**1%**	**n.a**	**n.a**
Metal Group	**n.a**	**2,180**	**-3%**	**n.a**	**n.a**
Iron & Steel (M.T)	2,114,298	1,223	-5.3%	11%	-15%
Miscelleanous Group	**n.a**	**755**	**20%**	**n.a**	**n.a**
All other items	**n.a**	**2,580**	**8%**	**n.a**	**n.a**

n.a = not available; PBS does not release data *ARP= Average Realised Price

Sources: PBS

Figure 3: Trends in Exchange Rate

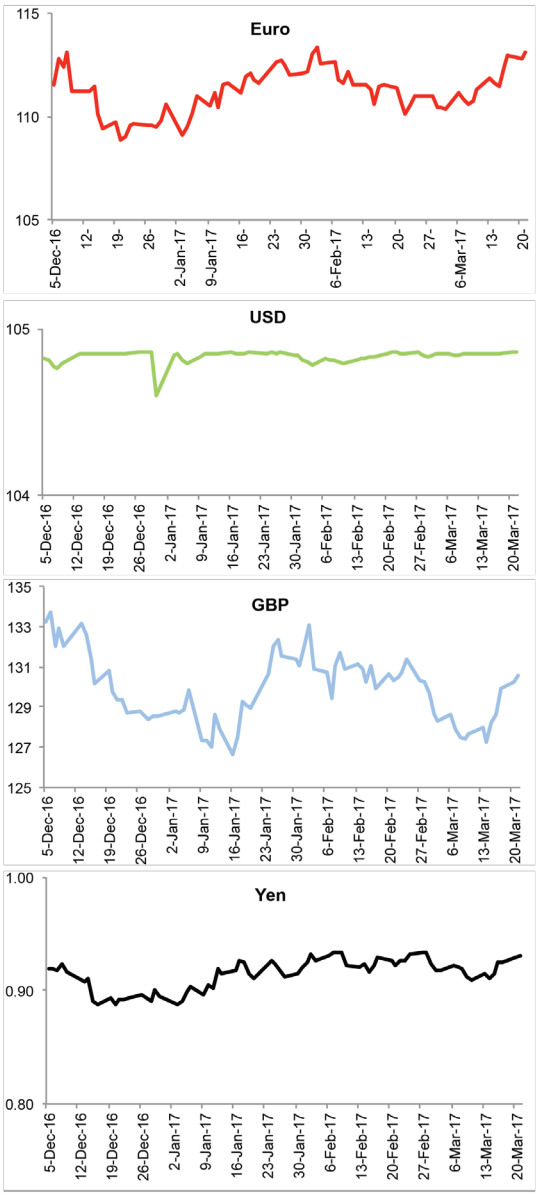
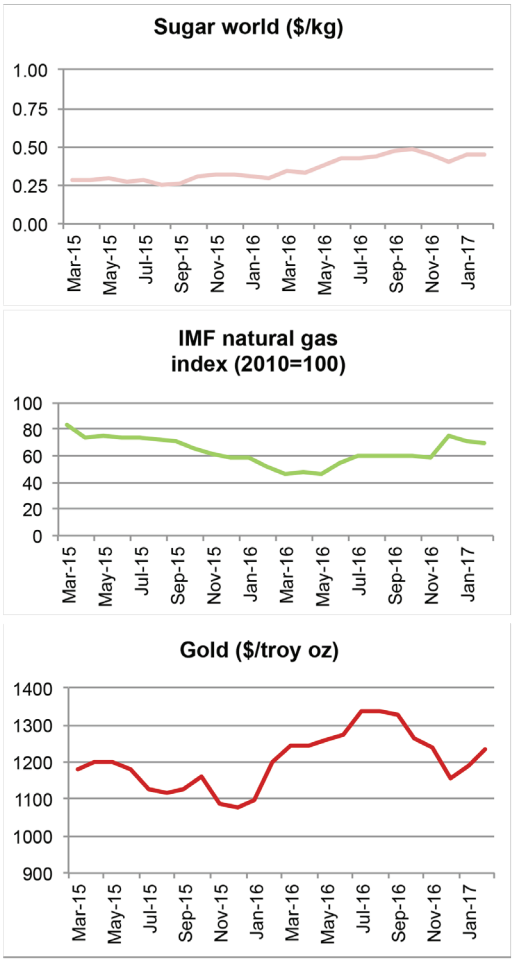


Figure 4: Key Commodities World Market



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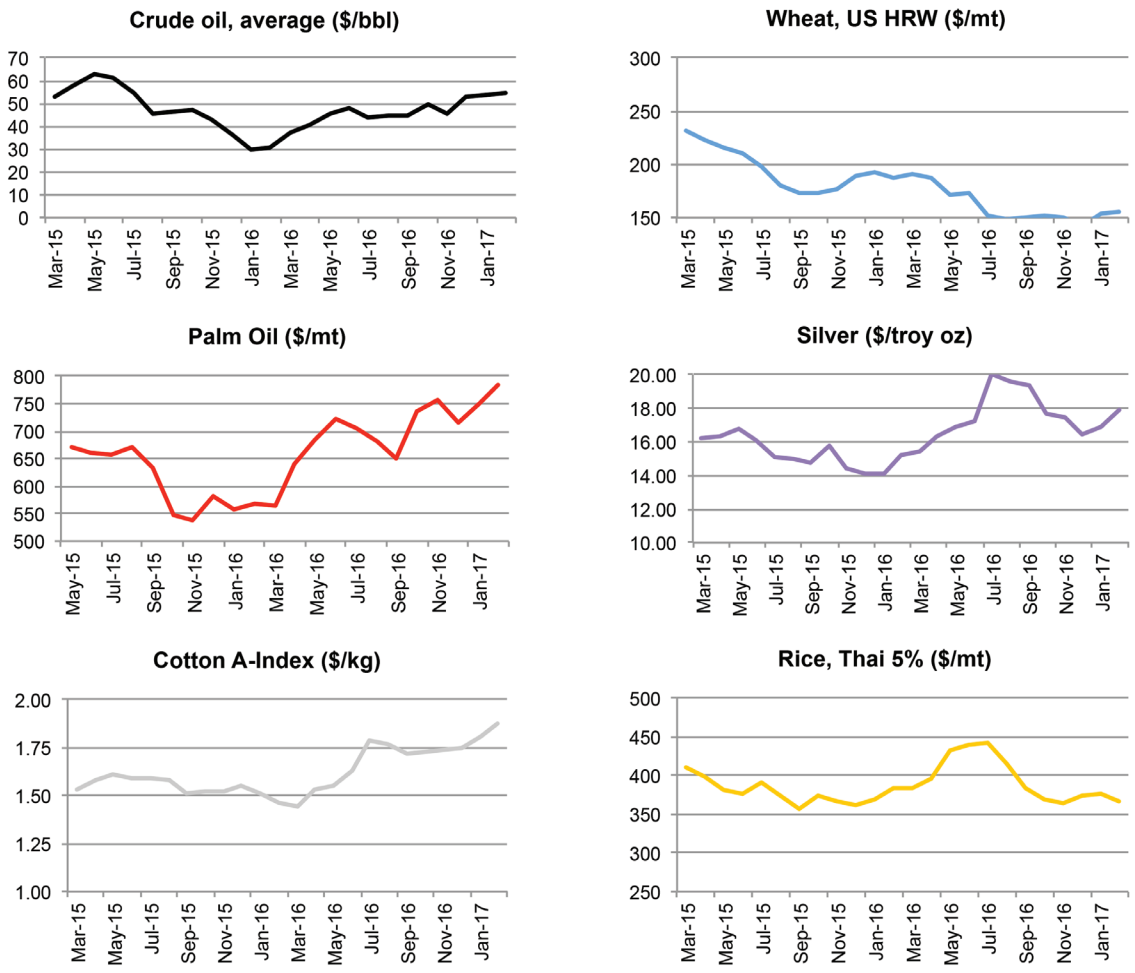


Table 6: Ease of Doing Business Index

Doing Business Rankings - Key Indices only								
	Starting a business	Dealing with construction permits	Getting electricity	Registering property	Getting credit	Trading across border	Paying taxes	Enforcing contracts
Pakistan	141	150	157	169	82	172	156	157
India	155	185	26	138	44	143	172	172
Bangladesh	122	138	187	185	157	173	151	189
Singapore	6	10	10	19	20	41	8	2
Vietnam	121	24	96	59	32	93	167	69
Turkey	79	102	58	54	82	70	128	33

Source: Doing Business

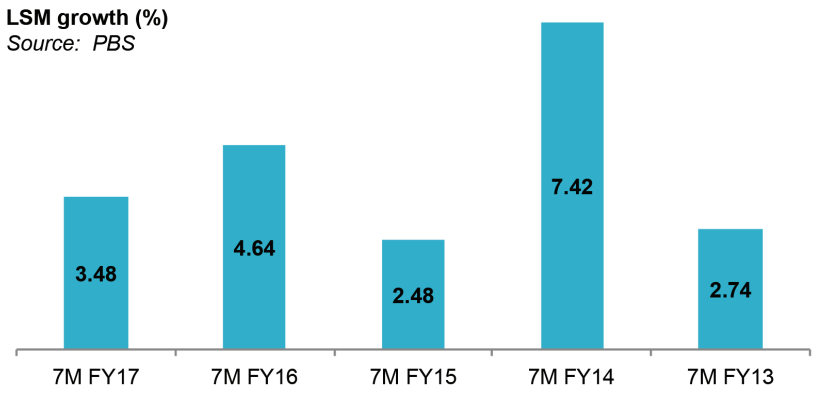
Performance of Large and Medium Scale Enterprises

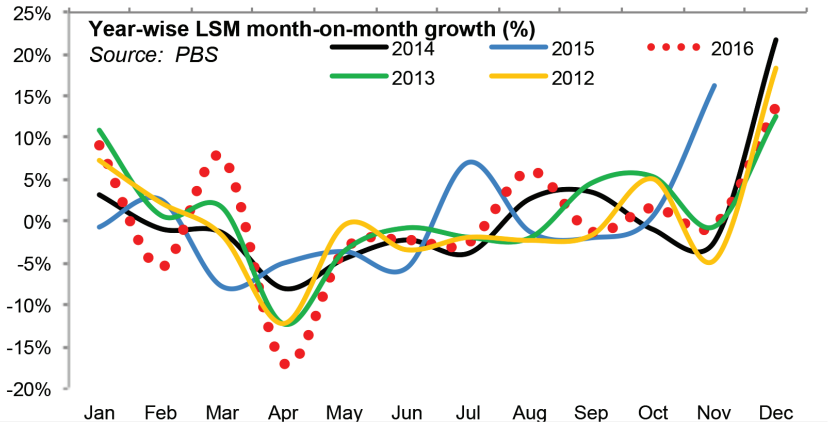
Major LSM Drivers

		Percentage change	
	Weight	5MFY17	5MFY16
Textile	20.92	0.02	1.03
Food, Beverages & Tobacco	12.37	3.78	4.89
Coke & Petroleum Products	5.51	-1.68	4.59
Pharmaceuticals	3.62	7.64	7.05
Chemicals	1.72	-3.60	11.67
Automobiles	4.61	5.57	32.26
Iron & Steel Products	5.39	14.53	-6.01
Electronics	1.96	14.52	-7.25
Leather Products	0.86	-17.85	1.12
Paper & Board	2.31	3.76	-18.17
Engineering Products	0.40	-5.86	-19.39
Rubber Products	0.26	0.47	10.04
Non-Metalic Mineral Products	5.36	10.48	5.95
Wood Products	0.59	-97.08	-23.48

Source: PBS

Performance of Large and Medium Scale Enterprises





Source: PBS

INDICATIVE TOPICS FOR PPR

01. Taxes

02. Credit Market

03. Capital Market

04. Investment Policy

05. Business Regulations

06. Civil Service Reforms

07. Research and Innovation

08. Tariffs and Trade Barriers

09. Inflation and Sound Money

10. State Owned Enterprises

11. Legal System and Property Rights

12. Human Capital, Labour Market and Regulations

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