**CPEC: phases and challenges**

Nasir Iqbal

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The China-Pakistan Economic Corridor (CPEC) is widely considered a turning point for both Pakistan and the region. It is an important stimulus for Pakistan, and promises rapid economic growth, massive infrastructure development, 700,000 new jobs in the next ten or fifteen years and the creation of special economic zones along the way.

After four years of Phase I of CPEC, Pakistan is now ready to enter Phase II. Some 27 projects are planned within the framework of Phase II. This phase emphasizes industrial cooperation, agricultural development and trade promotion. The tourism sector is also expected to expand during this phase. These initiatives are very promising for the expansion of job opportunities for local residents. The agricultural and tourism industries are considered the backbone of future growth.

But the key question remains unanswered: is Pakistan ready to reap the potential benefits of CPEC? Does Pakistan have enough soft infrastructure to attract investments in the industrial sector, especially in the special economic zones (SEZs)? It is clear that Pakistan may not have developed the fundamentals needed to realize all the benefits of Phase II of CPEC.

There are three prerequisites that are needed to reap the potential benefits of industrialization and tourism: human capital (HC), rural connectivity (RC) and a business environment (BE) that will attract foreign direct investment (FDI) and tourists. The current status of these prerequisites is poor.

First, the situation of human capital (HC) is lagging in Pakistan compared to other regional countries. HC has a large payoff for economic growth: between 10 and 30 percent of the differences in per capita income are attributable to cross-country differences in human capital.

The HC indicators, particularly education and health, show miserable progress in Pakistan compared to the rest of the South Asian region. According to the 2019 Human Development Report, Pakistan’s human capital index (HCI) was below average by region and income group. Pakistan ranked 152, while India ranked 129, Bangladesh 135 and Sri Lank 71 of the 189 countries. Pakistan has one of the lowest rates, within the region, of female participation in the workforce.

Second, local road and transportation networks are underdeveloped. Well-developed rural roads are needed to connect growth-generating sectors in different regions and achieve a wider distribution of economic benefits. They are also a prerequisite to the development of remote and/or environmentally difficult areas. Infrastructure investments in rural areas lead to higher farm and non-farm productivity, employment and incomes. Rural connectively with SEZs is key to creating opportunities for the poor to raise their economic status – a precursor of inclusive growth.

Nationally, approximately 60 percent of the Mouza (a type of administrative region similar to a town) are less than a kilometre from a sealed road and 67 percent of the Mouza have good transport connections on the same radius. But in CPEC districts, road and transport connectivity is woeful: only 4 percent and 23 percent of the Mouza in Kohistan, for example, have road and transport connectivity respectively; and the story is similar in other districts.

Third, FDI inflows are constrained by an unfavourable business environment. According to the Doing Business 2020 report, Pakistan ranked 110 out of 190 economies in terms of doing business, improving 11 notches from the Doing Business 2019, while India ranked 63, Nepal 94 and Sri Lank 99. Even within South Asia, Pakistan ranked fifth out of eight countries. Indicator-wise data reveals that getting electricity (ranked 123), paying taxes (ranked 161), trading across borders (ranked 111) and enforcing contracts (ranked 156) are the most seriously low-performing indicators.

In order to improve upon the indicators, institutional frameworks – such as political stability and an independent legal system – play an imperative role. Unsurprisingly, the quality of institutional frameworks in Pakistan is very poor. Pakistan is in the third percentile for political stability and absence of violence or terrorism, where 0 is the least desirable and 100 the most desirable rank, according to data from the World Governance Indicator by the World Bank 2019.

South Asia as a region ranked in the 29th percentile, compared with Europe and Central Asia (ECA) that is ranked 62nd and East Asia Pacific (EAP) that is ranked 66th. In the government effectiveness indicator, Pakistan ranked in the 26th percentile while South Asia and ECA are in the 36th and 69th percentiles, respectively. In control-of-corruption indicators, Pakistan ranked in the 23rd percentile while South Asia and ECA are in the 34th and 63rd percentiles respectively. The situation is similar for rule of law and regulatory quality indicators.

To maximize the potential benefits of CPEC, Pakistan needs to improve upon the three prerequisites, in all of which it is currently underperforming. First, Pakistan needs to invest in development institutions that require restructuring to improve legal frameworks, to implement rule of law and to ensure political stability. Political stability would be critical to the success of any developmental project and accountability process. While political instability undermines growth processes, it creates investment uncertainties, discourages international investors and de-motivates tourists.

The government is making concentrated efforts to implement reforms and positive impacts on the ease of doing business, where there is some good news. However, these reforms may not produce the desired results until we have a stable political environment to promote government effectiveness.

Second, the development of local road and transport systems should be part of the CPEC agenda. Without creating local connectivity, the roads and SEZs may not produce the desired economic growth and employment. Provincial governments should actively plan and develop local roads and transportation networks.

Third, the development of human capital through formal education and technical training should be streamlined, especially in deprived districts. The government should design area-specific training courses to cater to local needs. For this purpose, an assessment study can be conducted to understand local needs and business opportunities. Despite having a basic education, we lack the professionalism to provide services efficiently. Therefore, in addition to the amount of education, it is necessary to focus the quality of education to produce professionals in all sectors.

Without the implementation of an integrated institutional framework, establishment of a local road and transport network or developing area-specific human capital, the fruits of Phase II of CPEC may never materialize.

The writer is associateprofessor at the PakistanInstitute of Development

Economics (PIDE).

Email: dr.iqbaln@gmail.com