

Policy Imperatives for CPEC:

By Ishrat Husain

Most of the discussion about CPEC has so far focused on the financing and indebtedness in the future but the success of this initiative lies in the successful interaction between investment, institutions and policy. What kind of policies are needed to maximize benefits and minimize costs to the country. There are several but at least six areas need careful design and execution.

Energy Policy:

The addition of 10000 MW of electricity that is scheduled to become available to the National Grid by 2018 would overcome the energy shortages. However, it may create unintended adverse consequences for the public finances and liquidity of the companies involved in the energy supply chain if other components of energy policy are not put right. The Circular Debt that has now become a perennial problem would get worse if the gap between the purchase price of power paid by the DISCOs and the sale revenues collected by them is not bridged. The uniform tariff rate, the Transmission and Distribution losses and energy thefts, the discrepancy in the amount billed and the amount recovered, and the growing account receivables underpin this problem.. Unless the DISCOs are either privatized or restructured to become commercial organizations free from political interference, this growing circular debt would end up widening the fiscal deficit. The cost of generation to the end users can be reduced if competitive energy markets and energy exchanges are set up, auctions are held for tariff determination and multiple buyers are introduced instead of the present single buyer model. The NTDC would recover only the Wheeling Charges for the use of their transmission infrastructure.

Industrial Policy:

The Special Economic Zones (SEZs), Industrial parks etc to be set up along the Corridor should be open to Pakistani firms on the same terms as to the Chinese. Any incentives given to the Chinese would be equally applicable to all investors. Land is to be allotted on long term lease rather than outright purchase. The leases should be auctioned only to genuine, pre-qualified and screened bidders to eliminate land grabbers and speculators. In Balochistan, some portion should be reserved for local investors wherever it is feasible to do so without the right of alienation. The lease should incorporate a provision that the allotment of land would be cancelled if the project is not operational within three years... All infrastructure works – power, gas, water, roads, effluent plants, amenities – should be in place before the possession is passed on.

Pre-Feasibility studies should be carried out by the Zone authorities through expert Consultancy firms or universities, to provide base line data and information about the kind of projects that can be established in different zones.

Trade Policy:

External payments on account of repatriation of profits and debt servicing of CPEC projects would put pressure on the Current Account. Exports have to grow at least 15 percent annually to meet these new obligations and remittances have to increase at their historical level. Exchange rate has to be managed deftly to stimulate new export products, new firms, and penetration into new markets, but ensuring that prices of imports of capital goods, machinery and equipment are not hiked up to make new investments unattractive. Pakistani and other foreign companies winning competitive bidding should receive the same tax treatment to ensure level playing field.

Free Trade Agreements have to be renegotiated to preserve the comparative advantage of Pakistani exports and tariff quotas introduced to safeguard against material injury to Pakistani manufacturers. Import tariff rates have to be gradually reduced to enable Pakistani companies to participate in global supply chain.

Foreign Exchange Regime:

The current foreign exchange Regime is becoming too restrictive, for making timely payments to suppliers, vendors, and financiers. Further restrictions would only divert inflows towards informal channels, resulting in a vicious cycle. As inflows through official channels recede, and the demand for outflows through banking channels at interbank rates rise, the State Bank of Pakistan (SBP) would have to further tighten external payments, prolong the timing and disallow certain genuine payments to conserve their reserves.

As more payments are pushed to the kerb market, the differential between the official and open market rates would widen. Exporters and remitters would channel their earnings at the higher open market rate, reducing the supply in the interbank market. The increased demand by importers and other consumers of foreign exchange at the lower official rate would lead to a demand-supply disequilibrium.

Market sentiment plays an important role in the determination of exchange rate, and any hint that outflows on account of payments to the Chinese would lead to further restriction in foreign exchange regime would erode the confidence of the market players

Financial Policy:

Commercial banks should finance Pakistani Companies either stand alone or in joint ventures with the Chinese companies in collaboration with the Infrastructure Development Fund that would carefully scrutinize the proposals from potential investors, calculate the future cash flows, and carry out scenario analysis for risk mitigation.. For the small and medium enterprises working either as sub-contractors to the large firms, or providing goods and services for the CPEC projects, or setting start-up businesses, the existing Funds set up by DFID, USAID etc. should be geared up to meet this demand.

In Balochistan , Southern KP, GB , urban and rural infrastructure projects that link the main highways and motorways under CPEC with the communities should be given priority by the respective governments in the allocation of the Provincial Development budgets.

Skill Development Policy:

One of the prospective benefits for CPEC projects for Pakistan would be the training and development of skilled manpower. Plans have to be made to assess the long term manpower requirements, both for construction as well as operational phases of CPEC projects.

In light of this assessment, different categories and different levels of training programs have to be designed and then assigned to credible pre-qualified providers. Particular attention should be given to train the youth from the backward districts of the country, starting with Gwadar all the way to the Karakoram Highway.

A number of private and non-profit organizations are actively engaged in quality vocational and technical training, mainly in Karachi and Punjab. These organizations should be invited to set up similar facilities in other parts of the Country, where CPEC projects are being executed.

In addition to this formal training, internships and attachments with the Chinese companies working on the projects should be made an integral part of the curriculum. IF there is one lasting legacy for which

CPEC should be remembered it is this investment in producing skilled and trained technical manpower of different levels of expertise.

The other missing link in which Pakistan is weak is the institutional capacity for which a separate analysis would be required.