

# The economics of CPEC

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IN a country where negativity and cynicism reign supreme, critics and detractors of all kinds are revered, and emotional outbursts and fabricated stories dominate the air waves and social media, it is difficult to present a dispassionate analysis of national issues.

Since China announced the China Pakistan Economic Corridor (CPEC), more time and energy has been spent in finding faults, poking holes and raising doubts based on speculation and conjecture. Had this investment been announced in another developing country, the national reaction would be: how do we plan to ensure maximisation of benefits to the economy? What are the weaknesses and deficiencies in the existing set-up we need to overcome? But this type of thinking is not in our DNA. We are either in a mood for celebration and self-congratulations or outright condemnation and depiction of exaggerated pitfalls.

There are three types of reservations against CPEC. First, those who believe that this whole endeavour is designed to benefit Punjab to the neglect of the three smaller provinces. Fanning parochial and ethnic prejudices, doubts are created about the narrow impact of these projects. Second, that the country would be saddled with costly external loans and outflows forcing Pakistan to go for another bailout. Frightening numbers such as totals of \$110 billion are floating around. Third, some Baloch youth believe that they would become a minority in their own province. Mistrust and not perceived economic gains underlies such anxiety.

The government has not helped matters as it has not placed all the data and information about capital structure, detailed sources of financing, project sponsors etc pertaining to CPEC, in the public domain.

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## There are three types of reservations against CPEC. How can we address them?

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This article, to allay some of the reservations, proposes that the Planning Commission and PIDE use the well-established framework of cost-benefit analysis to evaluate and monitor the net benefits of CPEC projects. Benefits can be of three kinds: (a) direct, measured by incremental contribution to gross value added in energy and infrastructure. Assuming energy elasticity of greater than one, a two per cent growth in energy production and usage would increase GDP by more than 2pc from the current level (b) indirect, measured by the multiplier effect of activities resulting from the direct demand of goods and services and (c) induced effects or externalities: eg bringing in roads and electricity may make some economic activities feasible and reduce outmigration of skilled labour from those areas. Costs can be of four types: (a) direct costs associated with investment in electricity generation, transmission and distribution or construction of roads; (b) indirect costs: large scale investment projects create scarcity premiums and domestic prices of some goods and services are bid up. These premiums get reduced when competition sets in; (c) unavoidable incremental costs: in the absence of the required amount of domestic supplies of quality and specifications, imports have to make up the shortfall; and (d) avoidable incremental costs: proper planning, coordination and active management can substitute high-cost inputs by low-cost inputs keeping quality intact.

Net benefits are thus estimated as the difference between the discounted flow of aggregated benefits and the discounted flow of all types of costs over the given time horizon. This calculation is not straightforward and is beset with many conceptual, empirical and measurement difficulties. The most problematic area is the aggregation of easily quantifiable direct benefits or costs with estimated indirect and induced benefits and costs. The latter are sensitive to the assumptions on which they are based. Economists, by setting up monitoring experiments, discover new data that helps in fine-tuning and refining the original estimates. The outcomes therefore depend upon minimisation of avoidable costs and expansion of induced benefits thus enlarging the quantum of net benefits.

The avoidable costs phenomenon can be illustrated with the help of two examples. If the Chinese managers, skilled and technical staff continue to be deployed throughout the duration of the project, the unit cost of labour after taking into account the expatriate wage premium, security, housing and mobility expenses would be relatively much higher compared to a situation where preponderantly Pakistanis were employed. If the government makes advance plans for these positions to be transferred to Pakistanis over a staggered period through training, on the job apprenticeship, attachments and under study assignments supervised by Chinese trainers, cost savings would be substantial and net benefits much larger. This requires coordination, target setting, monitoring and outsourcing to vocational and technical training institutes, private providers and the provincial governments.

Similarly, it is guesstimated that at least 100,000 additional trucks would be needed to transport construction materials, movement of export-import trade and increased volume of goods. If investment in the sub sector is not carried out well ahead of the CPEC projects' peak load demand, the prices of trucking would escalate, putting Pakistani exports at a competitive disadvantage. The cost matrix of CPEC projects would also move upwards thus increasing the indirect costs. However, if Pakistani truck manufacturers are provided ballpark figures they can invest in expansion of existing capacity in tandem with the suppliers of parts and components. Indirect benefits would increase through creation of new jobs in the industry and efficiency gains from the economies of scale.

On the benefit side, it must be ensured that the most dynamic and enduring benefits from CPEC accrue to the people living in the deprived districts of Balochistan and southern KP. The opening up and integration of these districts with the unified national market of goods and services would make their fisheries, mining, livestock, horticulture and other activities economically feasible, creating incomes and jobs and helping lift them out of poverty. Roads and electricity are precursors for broad-based development as they minimise post harvest losses, waste and spoilage of perishable agriculture commodities, reduce the cost of delivery to market towns, and confer purchasing power in the hands of farmers who then use it to buy consumer goods, generating a second round of economic activities in these districts

By playing a more active role in maximising the benefits to the people of deprived districts and containing avoidable costs, the government would be able to allay a lot of misapprehensions and doubts.

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