Is CPEC Phase 2.0 a Game Changer for Poverty Reduction in Pakistan?

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Pakistan has now entered the next phase of the China-Pakistan Economic Corridor (CPEC) Phase 2 to deepen bilateral relations through strategic collaborations, transformative socio-economic projects, and advanced technological transfer.

Industrial cooperation, agricultural development, and trade promotion are key components of this phase. To accelerate industrialization, the government has planned the establishment of special economic zones (SEZs) in each province. Nine SEZs have already been identified across the country, offering competitive incentives such as income tax exemptions and customs duty exemptions on imports. Additionally, the tourism sector is expected to expand under Phase 2. These initiatives hold promise for job creation and poverty reduction by generating employment, supporting local businesses, and enhancing income generation, particularly in underdeveloped regions.

However, a crucial question remains: Is Pakistan equipped to maximize CPEC's potential for inclusive economic growth and poverty alleviation?

While CPEC brings substantial investment opportunities and promises of job creation, several concerns persist:

- Will these opportunities be accessible to underprivileged communities, or will the benefits remain concentrated among industrial elites?
- Do both foreign and domestic investors have confidence in Pakistan's economic stability, security, and policy consistency?
- Does Pakistan have a stable regulatory framework and a skilled workforce to attract and retain industrial investments in SEZs?

These structural challenges could hinder Pakistan's ability to translate CPEC investments into sustained economic growth and poverty reduction.

KEY PREREQUISITES FOR ECONOMIC GROWTH AND POVERTY ALLEVIATION

To fully harness the potential benefits of industrialization, tourism, and poverty reduction, Pakistan must focus on three critical prerequisites: human capital (HC), rural connectivity (RC), and a safe business environment (SBE). These factors are essential for attracting foreign direct investment (FDI), promoting tourism, and driving economic growth. However, Pakistan's current status in these areas remains weak.

1. Human Capital Development

Pakistan lags behind its regional counterparts in human capital development. According to the 2021

Human Development Report, Pakistan's Human Capital Index (HCI) ranks 144th out of 189 countries, significantly behind India (116), Bangladesh (123), and Sri Lanka (71). Additionally, Pakistan has one of the lowest female workforce participation rates in the region. A shortage of skilled labor could impede the success of SEZs and industrial expansion under CPEC.

To bridge this gap, Pakistan must invest in vocational and technical training programs aligned with CPEC-related industries, improve education infrastructure in underdeveloped regions, and implement targeted policies and incentives to encourage female workforce participation. With the right policies and investments, Pakistan's growing working-age population can become more skilled, productive, and capable of earning higher incomes, provided the economy generates sufficient quality jobs under CPEC.

2. Rural Connectivity and Infrastructure

Pakistan's underdeveloped road and transportation networks limit economic opportunities for underprivileged communities. Well-developed rural roads are crucial for linking growth-generating sectors across different regions and ensuring the equitable distribution of economic benefits. They are also essential for the development of remote and environmentally challenging areas. Investments in rural infrastructure can boost both farm and non-farm productivity, generate employment, and raise incomes—key factors for poverty alleviation.

However, rural connectivity with SEZs remains weak, raising concerns about whether CPEC-led industrialization will truly benefit the poor. Nationally, 60% of Mouzas (a regional unit similar to a town) are located within one kilometer of a paved road, and 67% have good transport links within the same radius. However, the situation is far worse in CPEC districts. For instance, only 4% of Mouzas in Kohistan have road connectivity, and just 23% have transport links. Similar gaps exist in other districts, making it unlikely that SEZ-led industrialization will create employment opportunities for rural populations without targeted infrastructure investments.

These connectivity challenges reinforce the risk that CPEC's benefits will remain concentrated in industrial hubs and urban centers rather than reaching underprivileged communities. Without an integrated rural transport strategy, industrial investments in SEZs may struggle to attract a local workforce, and rural populations may remain excluded from the economic gains of CPEC Phase 2.0.

3. A Safe and Business-Friendly Environment

Foreign direct investment (FDI) inflows remain constrained by an unfavorable business environment. According to the World Bank's Business Ready (B-READY) 2024 report, Pakistan falls into the fourth quintile, indicating persistent challenges in fostering a conducive investment climate. The report assesses economies across three key pillars: Regulatory Framework, Public Services, and Operational Efficiency, covering ten critical topics for investment and business operations. Pakistan's ranking highlights its struggle to create a stable and predictable business environment compared to regional peers.

This unfavorable business climate is particularly concerning for CPEC Phase 2.0, which relies on FDI, industrial expansion, and trade growth. Poor business conditions deter both foreign and domestic investors, limiting the potential for job creation within SEZs and other CPEC-related projects.
Additionally, weak institutional frameworks exacerbate these challenges. Essential governance structures—such as political stability, an independent legal system, and regulatory efficiency—are critical for attracting investment and ensuring long-term industrial growth. However, according to the World Governance Indicators (WGI) 2024, Pakistan ranks alarmingly low in these areas:

- Political stability and absence of violence/ terrorism: 6th percentile
- Government effectiveness: 26th percentile (compared to 36 for South Asia and 69 for Eastern Europe & Central Asia)
- Control of corruption: 23rd percentile (compared to 34 for South Asia and 63 for
- Eastern Europe & Central Asia)

Pakistan also scores poorly in rule of law and regulatory quality, further eroding investor confidence. Without institutional reforms, the country risks failing to leverage CPEC investments for sustainable economic growth and poverty reduction. Strengthening governance is critical to ensuring that SEZs attract long-term industrial investments, create jobs, and promote inclusive development.

To ensure that CPEC Phase 2.0 leads to meaningful poverty alleviation, Pakistan must strengthen its institutions, enhance rural connectivity, and invest in vocational training, particularly for low-income and rural populations. A well-functioning business environment—complemented by inclusive economic policies, will be essential in transforming CPEC from merely an investment corridor into a true engine of sustainable economic growth and poverty reduction.

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