

CPEC: Moving Beyond Infrastructure to Economic Reforms

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The first phase of the China-Pakistan Economic Corridor (CPEC) primarily focused on infrastructure development, with investments of over \$25 billion in road networks, port development, and power generation. Nearly 1,500 kilometers of highways were built, and power generation units adding 8,000 MW to the national grid were established.

Despite these infrastructure developments, a critical question arises: Why have they failed to deliver the expected economic benefits? Instead of reducing poverty and raising living standards, Pakistan's poverty rates have increased, and its per capita income has remained stagnant at around \$1,400 since the launch of CPEC in 2015. In contrast, competing countries have made significant gains. For instance, between 2015 and 2023, Bangladesh's per capita income doubled from \$1,236 to approximately \$2,400, while India's rose from \$1,590 to \$2,485 during the same period (Macrotrends).

A key reason for Pakistan's lagging macroeconomic performance lies in its failure to modernize policies alongside infrastructure. While the country invested in physical infrastructure (hardware), it neglected critical structural reforms (software). Pakistan halted its reform process in 2004 and began reversing earlier reforms from 2008 onwards. This trend intensified after 2014, leading to a decline in exports as a percentage of GDP. Exports peaked at 15% of GDP in 2003 but have since fallen to just 10.48%—far below levels seen in comparable economies.

International institutions like the World Bank and IMF have repeatedly warned of the consequences

of Pakistan's failure to reform its trade policies. A 2022 IMF report¹ described Pakistan as “a very closed economy compared to other emerging and developing economies, with net exports often acting as a drag on growth.” Similarly, a 2020 World Bank study² highlighted Pakistan's high trade barriers, noting that its tariffs are almost twice the global average and three times higher than those in East Asia and the Pacific. Pakistan ranks as the world's seventh-most protected economy, as measured by the Overall Trade Restrictiveness Index (OTRI).

The Pakistan Tariff Policy 2019-24³ acknowledged that while the world's fastest-growing export economies reduced import tariffs over the past decade, Pakistan increased them by 11%. Regulatory duties further raised effective tariff levels, making Pakistan's average weighted tariff the highest among 70 countries with over \$20 billion in annual exports. Despite this recognition, no remedial action was taken due to fears that lowering tariffs would reduce revenue collection.

Pakistan's failure to integrate with the global economy stands in stark contrast to the experiences of its neighbors and even its close ally, China. During the 1980s, China's trade grew at an annual rate of 12%, and its share of global exports rose from less than 1% in 1980 to 1.9% in 1990. This transformation was driven not just by infrastructure development but by structural reforms focused on global integration. Pakistan, however, has not adopted similar strategies, leaving its economy stagnant despite significant infrastructure investments.

¹ <https://www.elibrary.imf.org/view/journals/002/2022/027/article-A006-en.xml>

² World Bank. 2020. Modernizing Trade in Pakistan: A Policy Roadmap. © World Bank

³ <https://www.commerce.gov.pk/wp-content/uploads/2019/11/National-Tariff-Policy-2019-24.pdf>

The second phase of CPEC must take a fundamentally different approach, prioritizing policy reforms over infrastructure expansion. Pakistan must learn from China's dismantling of trade protectionism and focus on reducing both tariff and non-tariff barriers. High import duties inflate production costs, making exports less competitive globally. Lowering tariffs would grant local industries access to cheaper inputs and advanced technology, enabling them to integrate into global supply chains and drive economic growth.

Non-tariff barriers, such as complex regulations, inefficient customs clearance, and excessive documentation, further hinder trade. Streamlining these processes through automation, transparent policies, and harmonization with international standards would enhance trade efficiency and attract foreign direct investment (FDI).

Pakistan should actively integrate its economy into Chinese supply chains, leveraging its existing free trade agreement (FTA) with China. However, the current FTA is shallow, covering only 8.4% of Pakistan's exports and 27.28% of its imports. As a result, less than 5% of the bilateral trade increase can be attributed to the FTA. Whereas Pakistan's bilateral trade since the signing of FTA increased from \$3.5 billion to \$19 billion, India's trade with China surged from \$13 billion to \$116 billion in 2023.

Pakistan should also look at some other developing countries which underwent deep integration with their much larger neighbouring economies. For example, Turkey has integrated its economy with the European Union through a Customs Union, eliminating tariffs on manufactured goods. This has significantly enhanced Turkey's integration into European supply chains, with EU-Turkey trade reaching a record high of nearly \$215 billion in 2023. Similarly, Mexico's elimination of tariffs on manufactured goods has embedded its industries within U.S. supply chains, leading to bilateral trade exceeding \$800 billion.

Pakistan's limited trade integration has constrained its ability to produce and export more complex goods. Ranked 93rd out of 145 on the Economic Complexity Index (ECI), Pakistan's export basket remains dominated by low-value textiles and agricultural commodities like rice. Greater integration with China could enable a transition to high-value, knowledge-intensive products such as electronics, pharmaceuticals, and machinery. This shift would enhance export revenues, strengthen global competitiveness, and reduce reliance on volatile commodity markets.

To achieve this, Pakistan should focus on acquiring advanced technologies and getting its work force better skilled. Deeper integration with China can accelerate this transformation. Additionally, Pakistan should focus on emerging industries like electric vehicles,

advanced battery technologies, and solar energy—sectors where China leads globally. Collaboration in these areas would facilitate technology transfer and help Pakistan build a competitive edge in the green economy.

A strategic shift toward investment-driven growth is also crucial. Excessive borrowing has increased financial burdens and diverted resources from productive investments. By attracting FDI, promoting exports, and encouraging industrialization, Pakistan can create a self-sustaining cycle of economic growth, reducing dependence on international financial institutions.

In conclusion, the second phase of CPEC must prioritize policy reforms, global integration, and investment in high-growth sectors. While China can support Pakistan's industrialization by relocating some industries, long-term progress depends on Pakistan's ability to implement reforms that enhance productivity, investment, and economic resilience. By learning from China's experience and adopting similar strategies, Pakistan can unlock the full potential of CPEC and achieve sustainable economic growth.

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