



# The Political Economy of the China-Pakistan Economic Corridor

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*Edited by*  
Bai Gao · Zhihong Zhen

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## CHAPTER 1

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# China-Pakistan Economic Corridor and the Belt and Road Initiative

*Bai Gao*

The China-Pakistan Economic Corridor (CPEC) is the pilot project of China's Belt and Road Initiative (BRI). This is China's first government-to-government project with an aim to comprehensively promote the economic development of another country along the Silk Road. As China's first overseas project with large-scale investment, CPEC has presented both the Chinese government and Chinese companies two major challenges: not only must they undertake an adjustment process to situate themselves within the foreign political, economic, cultural, and religious environments, but they must implement CPEC projects via Pakistani institutions and mechanisms which function under operational logics quite different from those at home. Analyzing the Chinese and Pakistani experiences during the early stage of CPEC can provide valuable insights that help us understand the political economy of the BRI.

There are five issues surrounding CPEC that are of importance to understand the BRI. First is the issue of China's and Pakistan's motivation

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for the implementation of CPEC. Essentially, we might ask how, at the international level, does China see its national interests as related to the economic development of an investment-receiving country, and how, at the domestic level, is Pakistan's economic development related to its political stability and national security? Second is the issue of terrorism. Can the promotion of economic development reduce terrorism in a country like Pakistan? Terrorist activities have become a major national security issue for many countries in recent years and are an issue of great concern among within the international community. Indeed, with its direct implications for public policy, the relationship between economic development and terrorism might be considered one of the most important and consequential subjects of academic research in the twenty-first century. The third issue is whether CPEC might trigger an influx of Muslim immigrants into China which some Chinese commentators view as a threat to national security. Over the past few years, populism and anti-immigration sentiment have formed part of the anti-globalization movements in western countries. Even in China, some commentators have expressed their worries online that certain CPEC projects, especially roads and railways, may lead to an influx of Pakistanis into China, changing the proportion of Muslims in the population and thus threatening China's national security. Fourth is the matter of the administration of foreign direct investment (FDI) while implementing CPEC. How ought China to work with the different political-economic systems and mechanisms in Pakistan? Or more specifically, how should China respond if the project is carried out under Pakistan's domestic political-economic systems and mechanisms in a way that differs from China's expectations, or even if the outcome of its FDI somehow goes against China's initial intentions? Finally, the fifth issue is China's investment and development plan's inclusivity. There is a risk that CPEC's benefits might not be shared equitably among all Pakistanis, which raises the question of whether China, as the principal investor of CPEC, should itself adopt the principle of inclusive development so that all social groups in Pakistan share the benefits of economic growth brought about by the CPEC projects.

China has already made heavy overseas investments through the BRI to promote economic development in developing countries. Now, China is faced with a serious question: Is such investment prudent if China neglects the social consequences of its FDI in recipient countries? An examination of the roots of the anti-globalization movements in developed countries indicates that the political sustainability of globalization largely depends

on whether globalization's benefits are shared among all social groups in a fair and equitable manner. If China continues to make FDI, but focus only on short-term political gains to the disregard of long-term social consequences, it will likely cause a political backlash in the recipient country and the outcome of the projects in that country will run counter to the investments' original intentions. For this reason, it is essential that China, when promoting a new international economic order amid the anti-globalization trend—as exemplified by CPEC and the BRI—adhere to the principles of socioeconomic justice and the shared benefits of economic development.

The remainder of this introduction will elaborate on the following five issues.

### 1.1 WHAT IS CHINA'S MOTIVATION FOR IMPLEMENTING CPEC?

Admittedly, there are several reasonable arguments against CPEC. Pakistan's geological conditions pose a significant technological and engineering obstacle. The China-Pakistan border is mountainous and roads and railways face threats including earthquakes and mudslides. Under these conditions, roads, railways, and oil pipelines constructed under CPEC projects will necessarily have very high maintenance and repair costs. Especially when compared to ocean shipping, inland transportation appears quite inefficient. Moreover, there are many poor, underdeveloped regions in China with inadequate infrastructure and that lack a social safety net; why should China make FDI in Pakistan instead of investing domestically?

While these arguments are reasonable, China apparently sees value in CPEC and the BRI which far exceeds any considerations about these economic costs or domestic factor.

A discussion of the CPEC project must begin with an analysis of China's motivations for the BRI more generally. Before the Chinese government officially announced the BRI in 2013, the idea to develop the Silk Road Economic Belt came about as a consequence of two important historical events. The first event was the 2008 global financial crisis. This crisis had an enormous impact on developed countries which had been China's traditional export markets. These countries were no longer able to absorb all of China's products. Prior to this, for the thirty years leading up to the BRI, China had exercised a "blue ocean" strategy in which domestic

economic development was promoted through the exportation of goods to Western countries via oceanic shipping. But after the 2008 global financial crisis, this strategy began to appear unsustainable. The second event was that the territorial disputes intensified between China and several neighboring countries amid the US' adoption of the "pivot to Asia" strategy in 2009. This placed immense additional strategic pressure on China, which in turn invigorated nationalist sentiment within China. Under such complicated historical circumstances, the westward "opening up" strategy with its aim to promote the economic integration of Eurasia by building the New Silk Road Economic Belt became an important hedging strategy through which China could promote free trade and maintain world peace [2].<sup>1</sup> To China, in the face of increasing economic difficulties, the essence of the BRI is to defend free trade by opening new international markets, identify new opportunities for economic growth, and create a hedge against market turbulence in developed countries. In addition, China considers a turn toward Eurasia as vital to the avoidance of direct conflicts with traditional sea powers because, in this way, it would no longer rely solely on the Asian Pacific region for its economic connection to the world, thereby maintaining world peace and reducing the intense geopolitical pressures of the Asia-Pacific region.

The BRI is geo-economic in nature. Traditional geopolitics characterizes international relations as a zero-sum game emphasizing conflicts of interest and competition among nation states. In contrast, geo-economics attaches importance to the shared interests and cooperation among nation states in international relations and emphasizes the search for win-win solutions. It holds that every country could gain more opportunities as long as they cooperate with each other to increase the size of the market. This perspective lies at the BRI: it is essentially a hedge against the strategic pressures put on China from the United States and its allies in the Asia-Pacific region. Hedging in this case is neither friendly diplomacy nor confrontation, but simply an option that induces cooperation by demonstrating the costs of non-cooperation.<sup>2</sup>

With long coastlines and vast inland territories, China's geological location boasts strategic advantages in geo-economics. Western China is

<sup>1</sup> Gao Bai, "Gaotie yu zhongguo 21shiji dazhanlue" (High-speed Rail and China's Strategy for the 21st Century), *Jingji Guanchabao* (*The Economic Observer*) (March 2011): 41–42.

<sup>2</sup> Gao Bai, "Gaotie yu zhongguo 21shiji dazhanlue" (High-speed Rail and China's Strategy for the 21st Century), *Jingji Guanchabao* (*The Economic Observer*) (March 2011): 41–42.



connected to Central and South Asia and is not far away from the Middle East where are located the world's main sources of oil, natural gas, and many other minerals. Connecting countries of abundant energy, resources, population, capital, and technology, Eurasian railways and roads can mobilize production factors and further improve the relative global economic status of these countries, and affect the future international political and economic order.<sup>3</sup> China may put itself in a strong and favorable position within the international political economy if it utilizes its unique geographic advantages to create a hedge for itself. To do so, China must build railways and other infrastructure to promote economic integration with the Eurasian continent and promote the economic integration of the Pacific Rim. For China, the twenty-first century can be either a Pacific century, or a Eurasian century, or both. If the Pacific countries are hostile to China, it can turn westward to promote the economic integration of Eurasia; if the Eurasian countries are hostile to China, it can turn eastward to facilitate the economic integration of the Pacific Rim. If both sides show goodwill toward China, it can develop simultaneously in both directions.<sup>4</sup>

Why did China select CPEC to be the BRI's pilot project?

Unlike other neighboring countries, Pakistan offers unique political support for CPEC that other countries do not. Since both China and Pakistan consider each other all-weather strategic partners, domestic political support for cooperation with China is very strong in Pakistan; in fact, Chinese cooperation as a national policy is unanimously accepted by all political parties in Pakistan and has historically occurred through both governmental and military channels. In addition, Pakistan's political relations with other major powers are not as close as those it has with China, so it is less likely for Pakistan to be influenced by other countries when implementing CPEC projects. Perhaps most importantly, the Pakistani government recognizes that CPEC is a once-in-a-lifetime opportunity for the country's economic development. In consideration of these international and domestic conditions, therefore, starting the BRI from the southern route of the Eurasian land bridge seems to be China's best choice.

<sup>3</sup> Gao Bai, "Gaotie yu zhongguo 21shiji dazhanlue" (High-speed Rail and China's Strategy for the 21st Century), *Jingji Guanchabao* (*The Economic Observer*) (March 2011): 41–42.

<sup>4</sup> Gao Bai, "Gaotie yu zhongguo 21shiji dazhanlue" (High-speed Rail and China's Strategy for the 21st Century), *Jingji Guanchabao* (*The Economic Observer*) (March 2011): 41–42.

Pakistan's geographic location is of great importance to China. Whether China's BRI will succeed depends largely on whether China can develop and maintain good relations with neighboring countries and gain political support from them. The importance of a country's geographic location lies in the fact that location is a precondition for both geopolitics and geoeconomics. Without first considering the geographical environment of international political economy, it would be impossible to assess the value of various BRI route options in the context of big power relations. For instance, if Sino-US relations were stable, Pakistan's value to China, either as a pathway to the Indian Ocean, or as a route across the Eurasian land bridge, would be relatively low. If such were the case, China could ensure its ocean shipping route through the Pacific and Indian oceans and it would not need a land path to reach the Indian Ocean, nor a route across the Eurasian continent. Similarly, Pakistan's value to China would also be relatively low if China and Russia had an established strategic alliance, because in this case, Russia, rather than Pakistan could serve as China's main route to enter the European market.

China has given top priority to its diplomacy with its neighbors because the geographic locations of these countries are important. When China assesses the prospect of investment in neighboring countries, their values are not judged simply by whether investment will generate immediate financial returns, but by the manifold long-term political and economic benefits. Moreover, it is easier for China to protect its FDI in the event it falls under threat when that investment is in a neighboring country.

Pakistan's geographic location bears unique significance for the BRI. Situated on the other side of the Himalayas in South Asia, Pakistan is both an important pathway for China to reach the Indian Ocean and a vital route connecting all of South, Central, and West Asia. Gwadar Port, merely 400 kilometers away from the Persian Gulf, puts both the Middle East and Africa within easy reach. This route greatly shortens the logistic distance of both Chinese exports to markets in South Asia, West Asia, the Middle East, and Africa, and facilitates the import of energy and raw materials from these markets back to China. When CPEC is completed, Pakistan and China will be further bonded economically and Gwadar Port, sustained by newly built roads and railways, can serve as a major port for ocean shipping from the western regions of China, equivalent to the Port of Shanghai or the Port of Ningbo-Zhoushan that serve Eastern China. Eventually, it is possible that Pakistan's supply chains could become bonded with China's in a manner similar to that of Vietnam and South

Korea, effectively making China a true Indian Ocean country. This would further enhance its economic cooperation with surrounding countries. Such a mutually beneficial relationship is vital if China is to maintain the driving forces of its economic growth in both the Asian-Pacific region and the Eurasian continent. CPEC has expanded the demand for Chinese goods from not only the nearby Xinjiang region and other western Chinese territories; indeed, but also other regions of China with a strong manufacturing industry. By opening new markets for these regions, China can gain some cushion time while it shifts its model of economic development from external-demand-driven to domestic-demand-driven.<sup>5</sup>

The southern route of the Eurasian land bridge through Pakistan serves as an effective hedge to the northern route through Russia and to the middle route through Kazakhstan. Although there are multiple routes between China and Europe, each has its own risks, depending on the countries through which they pass. The best way to minimize these risks is to maintain each route's availability while keeping them in a managed competition. Russia has been sanctioned by Western countries since the Ukraine crisis. Kazakhstan, which has been greatly affected, is therefore trying hard to facilitate China-Europe freight trains, under pressure of survival. So far, two routes have been put into operation, including the China-Ukraine water-land transshipment route via Kazakhstan, the Caspian Sea, Azerbaijan, Georgia, and the Black Sea, and the China-Iran route via Kazakhstan and Turkmenistan. More recently, the China-Turkey route via Kazakhstan and Azerbaijan has started trial operation. Because the northern and middle routes are doing well, the urgency to build the southern route via Pakistan has declined. Yet, if the Kazakhstan route encounters problems, Pakistan's value to China as an alternative to enter the Middle East and Europe will increase.

China also considers Pakistan an important channel through which to communicate with the Islamic world. The Silk Road Economic Belt passes through two geopolitical zones: one is the sphere of influence of the former Soviet Union, the other is the Islamic world. Pakistan has long been closely related some countries in the Middle East, especially Saudi Arabia and the United Arab Emirates (UAE). Pakistan has sent many migrant workers to these two countries. In addition, The UAE has been a major provider of aid to Pakistan, and Pakistan has been one of the major sources

<sup>5</sup> Gao Bai, "Gaotie yu zhongguo 21shiji dazhanlue" (High-speed Rail and China's Strategy for the 21st Century), *Jingji Guanchabao* (*The Economic Observer*) (March 2011): 41–42.

of mercenaries for Saudi Arabia.<sup>6</sup> Pakistan may help China to extend the China-Pakistan railway to Africa with supports from Saudi Arabia and UAE. After the Gwadar-Kashgar railway is completed, it will further extend westward into Iran. If Saudi Arabia and the UAE are willing to fund the construction of an underwater tunnel across the Hormuz Strait between Iran and Amman and a bridge between Yemen and Djibouti, then the China-Pakistan railway would reach Africa through Iran and the Arabian Peninsula. These above-mentioned railway projects will become important Asia-Africa land routes if they can be materialized.<sup>7</sup> One of Saudi Arabia's challenges is to adjust its economic structure while maintaining political stability in an effort to survive the increasing competition in the oil industry wherein the Caspian Sea region and the United States have become new energy sources. If a railway is built between Asia and Africa via the Arab peninsular, Saudi Arabia will have opportunities to develop new economic sectors to shoulder the economic pressures.

To China, if CPEC succeeds, it will set an example for other countries. As Pakistan's economic development increases due to China's FDI, other Indian Ocean countries such as Sri Lanka, Bangladesh, and Myanmar may follow suite to engage in economic cooperation with China.<sup>8</sup> In this sense, CPEC is considered a test for the BRI. China has never before been involved as deeply in international affairs as it is now through the BRI. Although China has provided aid to other developing countries for years, these projects were normally idiosyncratic, tailored to individual entities. CPEC is China's most ambitious project by far and the first government-level project that provides substantial economic support to a foreign country through massive investments in multiple industries. An in-depth analysis of CPEC's outcomes will offer valuable insights.

<sup>6</sup> Gao Bai, "Gaotie yu zhongguo 21shiji dazhanlue" (High-speed Rail and China's Strategy for the 21st Century), *Jingji Guanchabao (The Economic Observer)* (March 2011): 41–42.

<sup>7</sup> Gao Bai, "Shate wenti de zhongguo jie jue fangan" (China's Solution to the Saudi Problem), *Xinan Jiaotong Daxue Xuebao (Journal of Southwest Jiaotong University)* (July 2014).

<sup>8</sup> Gao Bai, "Shate wenti de zhongguo jie jue fangan" (China's Solution to the Saudi Problem), *Xinan Jiaotong Daxue Xuebao (Journal of Southwest Jiaotong University)* (July, 2014).

## 1.2 CAN THE PROMOTION OF ECONOMIC DEVELOPMENT REDUCE OR ELIMINATE TERRORIST ACTIVITIES IN PAKISTAN?

Although China plans to invest \$46 billion in CPEC, to what extent this investment will reduce terrorist activities remains a controversial issue with scholars, journalists, and policymakers holding different views. The relationship between economic development and terrorism is a social science research subject with significant policy implications in the twenty-first century, drawing major attention in the international community. There are two schools of thought on the relationship between economic development and terrorism. On one hand, some journalists who have done in-depth investigations argue there is a positive correlation between poverty and terrorism. Sharing such assumptions, some governments have made concerted efforts to eradicate the perceived breeding grounds for terrorism by promoting economic development or providing humanitarian aid in those countries most affected by terrorism. For example, during the War on Terror following the 9/11 attacks in New York City, the US government increased its economic assistance to countries thought to harbor terrorists. On the other hand, “a substantial amount of scholarship casts doubt on the purported nexus between poverty and terrorism.”<sup>9</sup> It is easy, then, based on the results of Western academic publications, for commentators to cast doubt on the BRI’s and CPEC’s ability to ameliorate terrorism.

With the sharp contrast between these two perspectives, we wonder why the conclusion of scholarly publications could be so different from that of journalists reporting on the ground and of the policymakers who intuit the connection and expend resources to deal with it? One explanation for this discrepancy is that there may be problems with the research methods of cited academic publications and an oversight in qualitative research on the subject.

Let us first consider those studies that find an insignificant correlation between poverty and terrorism. Adequacy can be an issue if studies use country-level analyses with partial, cross-border data sets collected from

<sup>9</sup>Jeff Burdette, “Rethinking the Relationship Between Poverty and Terrorism,” *Small Wars Journal* (June 19, 2014); <https://smallwarsjournal.com/jrnl/art/rethinking-the-relationship-between-poverty-and-terrorism#:~:text=U.S.%20Policymakers%20have%20generally%20accepted,are%20directly%20and%20causally%20linked.&text=Numerous%20empirical%20and%20anecdotal%20studies,connection%20between%20poverty%20and%20terrorism.>

different sources rather than complete data sets specifically designed to examine the relationship between poverty and terrorism. As Sanchez-Cuenca points out, conceptual ambiguity has led to no common ground for the selection of cases and measurement ambiguity in database coding rules has created controversies.<sup>10</sup> Second, the unit of analysis may be another issue. When GDP per capita and income inequality are used to explain either the cause of or the lack of terrorism, the underlining assumption can be problematic, not only because terrorist activities take place in both rich and poor countries, but also because terrorist activities are usually limited to a small group of people within a small geographic area within a given country. There is therefore no theoretical reason to think wealth, either at the individual level or even at the national level, would reduce terrorist activities.<sup>11</sup> Nevertheless, as Victoroff points out, even if we were to assume that a country's economic development level was not significantly related to terrorism in a particular country, such a conclusion would still fail to answer a more fundamental question: if inequality in wealth distribution were drastically reduced in a given country, would the number of terrorist activities remain the same? In other words, if the average income and expected future income of Palestinians and Israelis were identical, would there still be Palestinians willing to become a human bomb?<sup>12</sup>

Piazza argues that cross-border quantitative analyses have neglected a theory widely used in mainstream sociology, anthropology, and criminology, that is; the personal experience of ethnic, racial, and class discrimination may be used to forecast the probability of future aggressive behaviors and violent crimes. Personal experience can be difficult to quantify, especially from data not specifically designed to do so, resulting in a poorly operationalized independent variable. It is precisely this point that some qualitative studies, focusing on a single country or single terrorist group,

<sup>10</sup> Ignacio Sanchez-Cuenca, "Why Do We Know So Little About Terrorism?" *International Interactions* (Sept./Oct. 2014).

<sup>11</sup> Bryan Brophy-Baermann, "Democracy Causes Terrorism: Methodological Flaws, a New Approach, and a New Answer," *Journal of Pedagogy, Pluralism, and Practice*, (2014) 6 (1): 87-124.

Joseph K. Young and Michael G. Findley, "Promise and Pitfalls of Terrorism Research," *International Studies Review*, (2011) 13: 411-431.

<sup>12</sup> Jeff Victoroff, "Introduction: Managing Terror: The Devilish Traverse from a Theory to a Plan," in Victoroff, ed., "Tangled Roots: Social and Psychological Factors in the Genesis of Terrorism," *IOS Press* (2006): 10.

have underscored. However, this criticism is often ignored or treated as irreconcilable in the current cross-border quantitative studies. Consequently, there are virtually no studies that examine the relationship between terrorism and economic discrimination suffered by minorities. Piazza argues that when a minority has been marginalized in a society, it forms a “group grievance” that is often used by terrorists to recruit new members.<sup>13</sup>

Piazza operationalizes the concept of group grievance by measuring economic and social discrimination faced by a minority in employment, education, medical care and social services, formal and informal segregated areas of residence, and a lack of economic opportunities, as compared with other social groups. All these inequalities function as a catalyst for a minority group to oppose the government, the current economic situation, mainstream society, and majority groups and provide opportunities for terrorists to mobilize participation and recruit new followers.<sup>14</sup>

In short, the relationship between economic development and terrorism is far more complicated than either the poverty-terrorism hypothesis or its critics suggest. While economic development may not be solely sufficient to eliminate terrorism, it is an important and necessary condition.<sup>15</sup> Therefore, BRI projects should address disparity in economic development, not only among countries and regions, but also among social groups within a particular country or region.

For China, CPEC serves to reinforce national security along its western borders. Although terrorism has been haunting Pakistan for years, the country has not found an effective way to counteract it. China’s promotion of Pakistan’s economic development is in fact a form of comprehensive cooperation that represents a joint effort at counter-terrorism. If Pakistan becomes safer because of its economic development, the same strategy may be also effective in Afghanistan and other Central Asian

<sup>13</sup> James Piazza, “Poverty, Minority Economic Discrimination, and Domestic Terrorism,” *Journal of Peace Research*, (2011) 48 (3): 339–353.

<sup>14</sup> James Piazza, “Poverty, Minority Economic Discrimination, and Domestic Terrorism,” *Journal of Peace Research*, (2011) 48 (3): 339–353.

<sup>15</sup> Jeff Burdette, “Rethinking the Relationship Between Poverty and Terrorism,” *Small War Journal*, (2014) June 9. <https://smallwarsjournal.com/jrnl/art/rethinking-the-relationship-between-poverty-and-terrorism#:~:text=U.S.%20Policymakers%20have%20generally%20accepted,are%20directly%20and%20causally%20linked.&text=Numerous%20empirical%20and%20anecdotal%20studies,connection%20between%20poverty%20and%20terrorism>.

countries. In this sense, CPEC exemplifies a new anti-terrorism strategy adopted by China: instead of fighting against terrorism exclusively at home, China now actively invests in neighboring countries with the aim to curb the spread of terrorist activities by promoting economic development in these countries.<sup>16</sup>

A new study published in China shows that since the start of CPEC in 2013, Pakistan has not had any major political turmoil but has experienced a relatively long period of stability that the country has not seen in eighteen years. By investing heavily in Pakistan, China closely tied its own interest to Pakistan's national security. In an effort to counter terrorism more effectively and support the CPEC projects, Pakistan's army launched the Prophet's Sword operation. Since then, terrorist attacks and related casualties have been greatly reduced.<sup>17</sup> However, China, as the principal investor of CPEC, must help Pakistan reduce regional disparity and inequality in wealth distribution when promoting economic development in the country. Only when Pakistan achieves these two goals can it reduce or eliminate terrorist activities. When the benefits of economic development are shared by all social groups, the appeal of extremism may lessen.

### 1.3 WILL CPEC TRIGGER AN INFLUX OF MUSLIM IMMIGRANTS TO CHINA, THEREBY POSING A THREAT TO CHINA'S NATIONAL SECURITY?

Recently, an online post spread widely in China. It argued that CPEC would trigger a huge influx of Muslims from Pakistan into China, these Muslim immigrants would ally with local Muslims in China, and this would pose a major threat to the country's national security. Some readers considered this populist opinion reasonable, but its logic falls apart quickly under social science scrutiny.

Connectivity in transportation certainly provides convenient mobility to human beings, but like the relationship between poverty and terrorism, convenient transportation is a necessary but not a sufficient condition for mass immigration. Convenient transportation does not necessarily lead to mass immigration, and mass immigration can also be realized without

<sup>16</sup> Gao Bai, "China-Pakistan Railway: The Outline of China's Land Power Strategy," (April 2015), <https://www.guancha.cn/gaobai/2015-04-21-316648-s.shuml>

<sup>17</sup> Zhou Rong and Chen Xiaochen, "Zhongba jingji zuolang jianshe jinzhan chaoyuqi (CPEC Progresses Beyond Expectation), *Diyi Caijing* (*China Business News*) (April 2017).



convenient transportation. Indeed, the railway and roads between China and Pakistan, as laid out in CPEC, are designed mainly for freight transport. China-Europe freight trains have already made thousands of runs, and we have not seen any Chinese using the trains to smuggle themselves into Europe.

Immigration status can be classified as one of three types: legal entry and legal stay, illegal entry and illegal stay, or legal entry and illegal overstay. “Illegal immigrants” belong to one of the latter two types. In any case, the issue of immigration is the concern of the immigration authority, not the transportation agency that provides convenient transportation. In other words, it is a government’s immigration policy that affects the volume of immigration, not the convenience of transportation.

Legal entry requires a valid passport and/or visa. All countries have strict rules for visa issuance, and any person entering a foreign country is required to go through a border inspection. It is hard to imagine that China would issue millions of visas to people from another country without regard to these established rules and let its borders be overwhelmed by an influx of immigrants. Admittedly, despite strict border controls to prevent illegal entry, border controls cannot prevent illegal overstay. Nevertheless, the fact remains that preventing illegal immigration depends on a host country’s immigration policy, and has little or nothing to do with the transportation connectivity between two countries. China, the most populated country in the world, is connected to Europe by railway, and although many Chinese wish to immigrate there, no part of Europe is being overrun by Chinese immigrants. Moreover, there already exists a means for Pakistanis to “conveniently” enter China: the Karakoram Highway between China and Pakistan has existed for over 40 years and yet rampant illegal immigration as described in the online post has not occurred. And even more evidence of the illogic of that argument: China and the United States are separated by thousands of miles across the Pacific Ocean, yet there are a significant number of illegal Chinese immigrants in America. Africa, too, is thousands of miles from China, yet there are many Africans overstaying their visas in Guangzhou, despite the fact that there is no land transportation between China and Africa at all.

Countries that allow immigrants to live legally as permanent residents need corresponding policies and social structures to support those immigrants—policies that in the Pakistani case, China doesn’t have. The increase of the Muslim population in European countries is not due to convenient transportation, but those European countries’ immigration

policies. France, for example, in order to meet labor shortage during the economic recovery after World War II, voluntarily absorbed immigrants from its former colonies until the first oil crisis in the 1970s. As labor-based immigration came to an end amid the first oil crisis, family reunification became the only valid channel for immigration. In 2005, 70 percent of immigrants entered France for family reunification, and only 7 percent for work. At the same time, about 70 percent of these immigrants came from former colonies in North and West Africa, countries with which France already had a strong socio-political relationship, with Algeria and Morocco being the largest source countries. Today, Muslims account for 7 percent of the French population and rising, making France the EU member state with the largest Muslim proportion.<sup>18</sup>

China is unlikely to adopt a French-style immigration policy. Although France has taken an open attitude towards Muslim immigrants from Africa, it has not done enough to help them integrate into French society. As a result, the grievances between the second and third generations of Muslim immigrants are growing deeper and deeper. China is more likely to stay conservative and maintain strict immigration control while simultaneously actively promoting the economic development of its neighboring countries in an effort to eliminate or control both potential terrorist risks and immigration pressures. With an effective transportation connection, rising economic development, and a reduction in inequality brought about by CPEC development, Pakistanis will prefer to live and work in peace at home rather than migrate to China.

#### 1.4 WHILE IMPLEMENTING CPEC'S PROJECTS, HOW SHOULD CHINA INTERACT WITH VARIOUS DOMESTIC SYSTEMS AND MECHANISMS IN PAKISTAN?

Some authors in this study on CPEC came to an identical conclusion: if the implementations of BRI projects are left completely to the logic of political and economic systems of the recipient country, the political outcomes may run counter to China's original vision of the BRI. An overarching theme in this book is an analysis of the logic of Pakistan's domestic systems and mechanisms, and discussions of how they may affect the CPEC outcomes.

<sup>18</sup>Sally Marthaler, "Nicolas Sarkozy and the Politics of French Immigration Policy," *Journal of European Public Policy* 15, no. 3 (2008): 383.

In Pakistan, the Punjabis are the largest ethnic group and Punjab is the largest province. According to the rules of the country's electoral system, a province's seats in parliament are allocated in proportion to its population; thus Punjab is the most powerful province in Pakistani domestic politics. The Punjabi people are also the backbone of the Pakistani army because of their long warrior tradition. Clan politics also plays an important role in Pakistani politics. As a result, resource allocation at the national level always favors eastern Pakistan due to the region's enormous Punjabi population. Consequently, eastern Pakistan has become far more developed than western Pakistan. This means that if CPEC related funds and projects are allocated according to the logic of Pakistani politics, those resources are more likely to be channeled to eastern Pakistan.

Plains are the major landform in eastern Pakistan, well-suited for building communities and transportation infrastructure. In contrast, western Pakistan is mountainous and, while possessing abundant minerals, are less habitable. Sindh, a province in the southeast and home to the largest port city, Karachi, ranks number one in GDP among Pakistan's provinces. Sindh has the advantage of being on the country's coastline with the Indian Ocean, making Karachi the country's major commercial center. Economically speaking, eastern Pakistan is endowed with more production factors and better geographical conditions for transportation and logistics systems. According to the principle of resource allocation efficiency, which prevails in the investment decision of private companies, the eastern provinces of Punjab and Sindh are better investment destinations than the western provinces of Khyber-Pakhtunkhwa (also known as the Northwest frontier province) and Baluchistan.

For these reasons, as explained and forewarned by the articles in this book, there is a danger that CPEC investment may concentrate in eastern Pakistan, creating conditions that may run counter to China's original aspirations for CPEC.

One of the major goals of CPEC and China's FDI is to reduce terrorist activities in Pakistan by promoting economic development. Terrorist activities tend to concentrate in the west and northwest regions, where economic development has lagged behind the east and northeast regions. This disparity in economic development provides a favorable environment for terrorist forces to recruit new members. To counter terrorism, therefore, it is vital that China promote economic development in the west and northwest regions and share the fruits of CPEC with the people of those

regions. Only by developing the overall economy and reducing inequality can these regions overcome the scourge of terrorism and extremism.

If the implementation of CPEC were completely left to the logics of Pakistani domestic political economy, CPEC project resources would tend to concentrate in the east, thereby exacerbating the disparity in economic development between the eastern and western regions. The gap between the rich and the poor, already a major challenge to Pakistan, will grow larger, conflicts between the central and local governments and between different ethnic groups will grow more severe, and terrorists will become more active, forming a threat to both Pakistan and the CPEC project itself.

Another difference between Pakistan and China is the use and influence of mass media. Pakistani media are heavily influenced by English media. However, Chinese media always releases information in Chinese rather than in English, and is not involved in Pakistan's public discussions about CPEC. Moreover, Pakistan's NGOs are also deeply influenced by external forces. Once a dispute over CPEC occurs, it will be difficult for Chinese companies to manage the situation in comparison with what they can do back home.

### 1.5 SHOULD CHINA, AS THE PRINCIPAL INVESTOR AND IMPLEMENTOR OF CPEC AND THE BRI, ADVOCATE THE PRINCIPLE OF INCLUSIVE DEVELOPMENT SO THAT ALL SOCIAL GROUPS IN PAKISTAN CAN SHARE IN THE PROJECTS' ECONOMIC BENEFITS?

2016 witnessed Brexit and the election of a populist president in the United States, two major events that exemplified the trend of globalization reversal.

Anti-immigration sentiment and inequality caused by globalization were important issues in the Brexit debate.

Donald Trump became a candidate for president by defeating a group of establishment Republican candidates, and then became President-elect, by defeating the establishment Democratic candidate, Hillary Clinton.

Both during his campaign and after being elected, Trump made a series of remarks regarding the current international trade regime that had, in his view, dragged the world into chaos. He announced that the United States would withdraw from the Trans-Pacific Partnership (TPP), renegotiate the North American Free Trade Agreement (NAFTA), and

threatened to label China as a currency manipulator and impose a 45 percent tariff on all US imports from China. Trump also criticized the European Union, saying that it functioned as a tool of Germany, and that he supported Brexit and predicted that more countries would and should do the same: look out for themselves.

This trend of globalization reversal in developed countries was due to the accumulation of social tensions and conflicts that occurred during the globalization process. But many countries along the path of China's Belt and Road are still in the earlier stage of the globalization process or have even been excluded from it, so such social tensions and conflicts are only just now starting to accumulate. For this reason, the trend of globalization reversal may not become a truly global phenomenon and may leave China some leeway to cope with an international economic environment growing increasingly hostile to globalization. If implemented conscientiously, the countries involved in the BRI may not experience the pitfalls that lead to globalization reversal.

In developed countries, failing to share the benefits of globalization among different social groups led to the rise of the anti-globalization movement. These countries had opened their domestic markets, which led to the loss of jobs opportunities and worsened the inequality gap.<sup>19</sup> Even in the Chinese economy, a distinctive phenomenon has occurred in recent years: income from capital investment has increased far faster than wages, creating a real estate bubble in the so-called first tier cities that has significantly deepened the wealth disparity between the rich and the poor.

These are important warnings: when implementing CPEC and other BRI projects, China must be fully prepared in advance to avoid the troubles that both developed countries and China itself have gone through. If China invests in a developing country but neglects the potential long-term social problems and fails to take precautionary measures, its FDI will not only fail in its aim to promote economic development in recipient countries, but it will aggravate the ensuing crises and in fact damage local economies in the end. When CPEC was launched, it enjoyed support from every political party and interest group in Pakistan because it was recognized as a once-in-a-lifetime opportunity for Pakistan's economic development. However, if China fails to prevent CPEC from inadvertently worsening inequality in Pakistan, both countries' security situations will

<sup>19</sup>Gao Bai, "Quanqiuhua nizhuan jizhi" (Mechanism of the Globalization Reversal) *Wenhua Zongheng* (*Beijing Cultural Review*) (December 2016).

worsen, terrorist activities will increase, China will not see a return on its investment, and the promise of the BRI will not be fulfilled.

In the short term, production capacity cooperation may help China ease the pain of declining domestic demand. However, an exclusive focus on investment and economic growth while neglecting the issue of fair distribution of BRI benefits in recipient countries and the failure to prevent inequality will result in crises down the road. The results of this short-sightedness have already been demonstrated by the emergence of populism in western countries. On one hand, developed countries were the biggest winners of globalization because global production and outsourcing improved their productivity while free trade provided them with cheap consumer goods. On the other hand, the benefits of globalization were not shared equally among social groups which led to an eruption of social conflict and a populist trend toward anti-globalization. When a developing country suffers from stagnation, any investment is considered good for economic growth. But if an investor does not care about the long-term political consequences of that investment, serious problems will arise once the economy recovers or a regime shift takes place.

Involving more than sixty countries, the BRI will become more than a mere multilateral cooperation project; the resultant institutional arrangements will form part of future international economic order. The principle of inclusive development should be an indispensable feature of this new order. Since China is taking the lead in the construction of this new international economic order for the post-globalization era, its responsibilities are far more complicated and more consequential than those of any previous regional economic cooperation. While China ought to defend the principle of free trade, it must also loudly advocate for the fair distribution of development benefits brought about by international economic cooperation—not only at the country level but among the social groups within a given country. Although China does try to provide public goods to countries along the New Silk Road Economic Belt by building transportation infrastructures, this can only narrow the gap of economic development among these countries to a limited extent. In order to make BRI a sustainable project in the twenty-first century, China must actively advocate the fair distribution of development opportunities and use its FDI power as a bargaining chip to allocate economic benefits among different social groups in recipient countries. With this strategy, the BRI will also gain political support in recipient countries through its reputation as an advocate of economic fairness and socioeconomic justice.

In short, the analyses on the challenges confronted by CPEC in its implementation provide two valuable lessons for future BRI projects.

First, BRI projects must be concerned about not only economic growth but also fair distribution and socioeconomic justice. Of course, economic growth cannot solve all social problems, but if China simply pushes globalization and economic growth in recipient countries while failing to address the issue of fair distribution of economic benefits among all social groups, the BRI will encounter local political backlash. China should clearly define a strategy for the fair distribution of economic growth benefits and officially adopt it as a universal principle for its BRI projects. This is especially important in the post-globalization era.

Second, China should not give up its political responsibility in case a host country's domestic systems and mechanisms cannot realize the goals of fair distribution of economic benefits for BRI projects among different social groups. Rather, China should be prepared to exert influence on recipient countries through appropriate channels. China will not be able to ensure the sustainability of the BRI and the long-term interests of its FDI unless it can help recipient countries realize fair distribution and socioeconomic justice as they join the processes of globalization and economic growth via the BRI.



# Structural Factors of International Relations That Affect China-Pakistan Economic Corridor

*Xuemei Qian*

The conception of CPEC<sup>1</sup> can be traced back to the late 1990s, when Pakistani military was planning to build a domestic ring road. In the early twenty-first century, President Musharraf of Pakistan proposed to China

<sup>1</sup> According to the current planning, CPEC is about three thousand km long, starting from Kashgar, Xinjiang in the north of China, connecting Gwadar Port, Baluchistan in the south-west of Pakistan. CPEC boasts a four-pillar-framework of energy and transportation infrastructure construction, including roads, railways, oil and gas pipelines and optical cables. In April 2015, China and Pakistan signed more than thirty CPEC-related projects agreements, including eight road and railway projects, fifteen power grid projects, four coal mining and energy pipeline projects, and other industrial parks, ports, hospitals and telecommunication infrastructure projects.

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to jointly build an economic corridor.<sup>2</sup> It was made official when China's Premier Li Keqiang visited Pakistan in May 2013. The two countries signed the "Memorandum of Understanding on Building CPEC" on July 5th, 2013, and another fifty-one cooperation agreements and memorandums during President Xi Jinping's visit to Islamabad in April 2015. According to some estimates by the Pakistani side, the total investment of CPEC would reach approximately US\$46 billion.

Many Pakistanis regard CPEC as a "game changer," or even a "fate changer," expecting the three-thousand-km corridor to bring about fundamental changes to Pakistan. However, whether CPEC can really change Pakistan or to what extent can it change is a question that can only be answered when it is completed. And for now, the practical question is whether CPEC can be implemented successfully.

It is not simply a "yes" or "no" question. There is no doubt that China and Pakistan are all-weather strategic partners and share strong determination to build CPEC well. However, CPEC is not to be built in a vacuum. Its implementation will certainly be affected by various internal and external factors, and its success will also be measured in different ways. Among the existing literature on CPEC, few has discussed about how to measure its success. Most studies are focused on possible difficulties and obstacles that may occur while implementing CPEC, and analyses based on internal factors are more than those on external factors. The so-called internal factors mainly include the economic, political and security situations, as well as social and cultural environments of both countries. Besides, the challenges of terrorism, provincialism and social unity are also included. In theory, the external factors refer to all the international relations that might be involved in CPEC. However, current studies are mainly focusing on a few countries, especially India and the United States, etc.

The success of CPEC should be at least measured in three dimensions. First, all the CPEC-related projects should be launched as scheduled, instead of remaining in documents or disappearing automatically. Second, the CPEC-related projects should help Pakistan get through the current difficulties by improving its economic and social environment, and drive

<sup>2</sup>As recorded by Rizwan Zeb, a researcher at the Institute of Regional Studies Islamabad, when Musharraf first proposed the conception of today's CPEC to China ten years ago, he said that the Karakoram Highway was the "Eighth Wonder" in the world, and if China and Pakistan would together build energy pipelines and railways connecting each other, those would be the Ninth and Tenth Wonders. "Pakistan-China relations: Where They Go From Here?" *UNISCI Discussion Papers* 29 (May 2012): 45–58.

its economy into a fast lane of stability and development. Third, the implementation and operation of CPEC should ultimately consolidate China-Pakistan friendship, and even enhance the peace and development of the Central and South Asian region to a higher standard. But this will not be discussed in detail due to topic and length limitations. The main task of this paper is to study the structural variables of international relations that have affected or will affect the implementation of CPEC.

## 2.1 STRUCTURAL VARIABLES OF INTERNATIONAL RELATIONS

Above all, three points need to be clarified in order to understand the impact of structural forces of international relations that affect CPEC.

Firstly, the relationship between CPEC and the structure of international relations lies in two dimensions: one is the relationship between the parts and the whole, and the other is the relationship of interaction. On the one hand, as a product and symbol of China-Pakistan friendship, CPEC represents inter-national relations, or put it more specifically, the foreign relations of China and Pakistan respectively. As a part, it carries the DNA of the structure of international relations, which are always related to international cooperation, competition and confrontation among the relevant countries. On the other hand, CPEC will in turn shape the existing international relations of the region. However, this paper only discusses the impact of the international relations on CPEC, and the impacts of CPEC might have on international relations will be skipped here.

Secondly, is there a relatively stable structure in the constantly changing international relations? This paper would presume “yes”. According to a mainstream international relations theory, it is generally believed that the international society is a state of anarchy, but anarchy does not necessarily mean chaos and disorder. Neither it equals to no structure at all. In fact, it only means that there is no formal international government or true global controller. Even the theory of anarchism believes that society is based on self-organization, volunteer associations and mutual assistance.<sup>3</sup> And these organizations, associations and their mutual relations are by themselves patterns of structure.

<sup>3</sup>Cynthia Weber, *International Relations Theory: A Critical Introduction*, (Routledge 2014): 240.

CPEC was born in a dual structure. First, China has risen as the second largest economy in the world, and China's presence and actions beyond its border are watched by different countries to different extents. Second, since the August of 1947, South Asia has been caught by a strong and stable structure characterized by Indian-Pakistan rival and hostility. All other countries on the South Asian stage cannot but play within this framework, by either choosing side to deepen the hostile situation, or trying to reconcile the two and maintain certain balance. The confrontation between the United States and the Soviet Union during the Cold War was not an exception. In the 1950s and 1960s, Pakistan joined the Central Treaty Organization (CENTO) and the Southeast Asia Treaty Organization (SEATO) established by the United States, while India was close to the Soviet Union. From the late 1970s to the 1980s, the United States actively intervened in Afghanistan's Jihad against the Soviet Union with the help of Pakistan. The ongoing anti-terrorist war of the US has not changed this fundamental structure, either. Against this background, no matter how eagerly people hope CPEC to be a "fate changer," it can only live and grow within the existing framework of South Asian politics in the foreseeable future. Moreover, CPEC is not the single event in this region. It will certainly be affected by the international relations of the related countries.

Judging from the perspective of China-Pakistan friendship, CPEC is unique when compared with hundreds of friendly cooperation projects in the past, because some parts of it will become real geologic existence and the economic corridor will be there for a long time. The Karakoram Highway, praised as the "Eighth Wonder" of the world, will also be further upgraded under the framework of CPEC. Power grids and industrial parks, the key projects of CPEC, are likely to reshape the geo-economic relations in South Asia. And geographical re-constructure itself could be ranked as a geopolitical event. In this field, however, CPEC is not pioneer but a latecomer. Countries like India, the United States, Russia and Iran all had proposed their own strategic plans to develop energy pipelines and land transportation facilities in Central and South Asia. The difference is that CPEC is based on and supported by the friendly bilateral relations, by which it could be regarded as pilot in its peers. But it cannot go beyond the regional established geopolitical-economical structure.

One step further, the structural factors of international relations that affect CPEC can be divided into three categories. The first is historical factors, such as historical memories including long-term friendship or hostility, etc. The second is the relatively stable relationship among the main

actors, including bilateral, trilateral and multilateral relations. The third is a number of functional issues, such as geopolitical and geo-economic benefits, the framework of big powers and non-traditional security, etc.<sup>4</sup> Among these three categories, historical factors are the background for the latter two, but are also influenced and thereby updated by the latter two. Therefore, this paper chooses to mainly discuss two factors, one is the inter-national relations and the other is functional issues, which can be specified as five variables, namely, the inter-state relations, geopolitics, energy politics, connectivity politics and cognitive politics.

Thirdly, it should be noted that non-state actors such as multinational companies, sub-national ethnic groups, local armed forces and transnational terrorist forces, etc. are also quite active in South Asia. This article will skip them in that, to some extent, their impacts on CPEC can be roughly included into the states. And for now, there are two ways for such inclusion.

One is that non-state actors, acting as an internal cause, are subordinate to the relations between the two countries' governments and their internal rivals. The separatist, terrorist and extremist forces active along the corridor belong to this case. They may take CPEC as a new battlefield to fight against both states by impeding or destroying the project. However, their impetus to do so is not CPEC, but their resent or dissatisfaction with their governments. It is possible that various anti-government forces of both countries may join hands during the implementation of CPEC, forming the rival with the two governments as one side and the union of anti-government forces as the other.

Another is that non-state actors are subordinate to the broad international relations. In Pakistan, there have been some transnational extremist and terrorist forces for a long time. The composition and background of these forces are quite complicated. CPEC will provide them with new opportunities for making profits. Some of these forces may be affiliated or subordinate to a third country, becoming a strategic tool or agent thereof. In Balochistan, such signs have emerged already. The expansion of Daesh (ISIS) in the Pak-Afghanistan, which has evoked much concerns recently, also has such potential.

<sup>4</sup>Talking about the structure of international relations does not mean this structure is fixed. On the contrary, with the changes in international political life, these three pillars are changing.

## 2.2 INTER-STATE RELATIONS

The basic structure of inter-state relations has been existing long before the initiative of CPEC. It is the fundamental environment and framework for the implementation and operation of CPEC. There are two types relations that are crucial for CPEC: China-Pakistan bilateral relations, the tri-lateral relations formed by China, Pakistan, and the third-parties.

### 2.2.1 *China-Pakistan Bilateral Relations*

China-Pakistan friendship is not only the core driving force of CPEC, but also the decisive factor for its success. Recent discussions on CPEC are too concentrated on challenges and risks to have dwarfed this decisive factor. Commentators talked a lot about the conflicts and risks, or the benefits and effectiveness of CPEC. Some asserted that for China, CPEC will solve its Malacca dilemma and shorten its distance to the Persian Gulf. Also, CPEC will export spare capacity, expand overseas markets and acquire Gwadar Port, etc. They also claimed that for Pakistan, CPEC will boost its long stagnating economy, improve its economic condition and stimulate its take-off.

If we talk about CPEC without considering the overall framework and goals of China-Pakistan bilateral friendship, it might invite at least two risks. First, the political and economic benefits of CPEC are likely to be overemphasized, and people may regard CPEC merely as a temporary expedient for respective goals of China and Pakistan. Second, the two countries may put more effort in developing private sectors and less in maintaining bilateral relations, or give priority to economic relations over political one.<sup>5</sup> It is true that long-term and sustainable bilateral economic cooperation must be based on solid mutual benefits and win-win outcome, but if we simply interpret China-Pakistan relations as ordinary bilateral economic cooperation, it will do more harm rather than good in the long run, because it actually downgrades their all-weather friendship to ordinary bilateral relations.

Therefore, it is necessary to reiterate that China-Pakistan relations are the core variable for the success of CPEC. The political determination of

<sup>5</sup>The author noticed some signs while visiting Islamabad, Pakistan in May 2016. For instance, a Pakistani entrepreneur said in a speech, “The future of China-Pakistan relations doesn’t lie in the relationship between governments, but in the relationship between private sectors.”

both governments not only provides guarantee and necessary conditions for CPEC, but also help themselves overcome various internal and external obstacles in the construction process. However, China-Pakistan relations are closely watched and easily influenced by third parties under the more and more complicated international environment, therefore, it is impossible to maintain the friendship without efforts from both sides. One of CPEC's important goals is to further consolidate the bilateral relations of China and Pakistan. If the nature and goal of China-Pak relations would be changed significantly when CPEC is completed, then we could hardly call CPEC a success.

### *2.2.2 Trilateral Relations: China-Pakistan with Third-Party Participants*

From the perspective of economic geography, the major part of CPEC is located in South Asia, where there are many politically influential countries. Both China and Pakistan have established diplomatic relations with different countries, which means the overall China-Pakistan relations and the implementation and future operation of CPEC will definitely be influenced by third-party countries.

In the past few decades, kinds of trilateral relations have dominated South Asia with India-Pakistan relations lying at its core. Given the long-term hostility between India and Pakistan, it is difficult for other countries in the subcontinent to keep true neutrality and balance between India and Pakistan. When extraterritorial country enters South Asia, it will, more or less, have to enter trilateral relations or triangular relations with India and Pakistan. Taking the sophisticated international relations beyond South Asia into account, in the current South Asian arena, the number of triangular relationships among countries like Pakistan, India, China, the United States, Russia, Japan, Afghanistan, Iran and Saudi Arabia is almost equal to their mathematical result of permutation and combination. Most of the relations are actually or potentially related to CPEC, which is too complicated to be simply defined as positive or negative.

Still, the influence of third parties upon CPEC is not decisive. No third party can really reverse the process of CPEC except by launching military war against China or Pakistan. Up till now, no country has shown such intention publicly. With this in mind, we may find there are three ways for third party to exert impacts on CPEC: one is to influence China and Pakistan respectively through bilateral relationships; the other is to

cultivate its agents in China and Pakistan; and the third is to establish a triangular relationship with China and Pakistan. In addition, an extraterritorial country may also seek support from a South Asian state other than Pakistan.

Among all the third-party forces that may affect CPEC, India ranks number one. No matter in terms of geopolitical weight or capability to take actions, India's influence on CPEC is far stronger than the United States, Iran, Russia, Japan, or any other countries. For global powers like the United States, Japan, and Russia, South Asia is just one part of its interests. Since the end of the World War II, the United States has repeatedly come and gone. The remote geographical distance was, and will continue to be, an important reason. Sir H.J. Mackinder has pointed out that the physical geography imposes mandatory limitations on human activities.<sup>6</sup> Although transportation, communication and delivery techniques have advanced significantly in the twenty-first century, the Pacific and Indian Oceans will still be huge geographical boundaries in times to come. And this imposes certain restrictions on human activities. So far, the United States has been practicing checks and balances to China in East Asia. Over the past two years, the US-Indian relations have deepened significantly, which indicates that Washington intends to balance South Asian or even the entire Asia with India's support in the future. In 2015, India and the United States together announced a joint statement and expressed the determination to strengthen their global partnership, especially their strategic cooperation in the Indo-Pacific region.<sup>7</sup> Although India has never officially given up its "non-alignment" principle so far, Russia has already adjusted its policy toward South Asia, especially toward Pakistan, as a response to the changes of US-India relations.<sup>8</sup>

<sup>6</sup>H. J. Mackinder proposed that the United States was strong enough at the end of the 19th century, but it still chose to influence the balance of powers in Europe through Russia. H.J. Mackinder, *The Geographical Pivot of History*, trans. Lin Erwei and Chen Jiang, (Beijing: the Commercial Press, 2013): 50–51, 69.

<sup>7</sup>"U.S-India Joint Statement," (January 2015), <https://www.whitehouse.gov/the-press-office/2015/01/25/us-india-joint-statement-shared-effort-progre>.

<sup>8</sup>Russia's desire to "go south" can be traced back to the beginning of the 19th century but in vain somehow. Russia has significantly accelerated its "southward" pace since 2012. It has developed relations with Pakistan and Afghanistan actively, although India is still the key in its South Asian strategy. Noteworthy is that the US-India relations are warming in parallel with Moscow's efforts to strengthen relations with Islamabad and Kabul. From 2014 to 2015, despite the opposition of India, Russia sold MiG 35 fighter jets and Klimov RD-93 engines to Pakistan, and reached a bilateral defense agreement. At present, Russia continues

Among all the triangular or trilateral relations, China-Pakistan-India relationship influences CPEC the most for three reasons. First, the implementation of CPEC requires an overall peaceful environment, or at least a generally manageable environment in the region, in which India and Pakistan are of vital importance. Second, both CPEC and the Bangladesh-China-India-Myanmar Corridor (BCIM) are among the six major BRI corridors,<sup>9</sup> and both are regarded as pioneer projects of BRI, too. Although India has shown little interests in participating in BCIM or BRI, it is easy to tell that India is very concerned about CPEC. Third, India is the strongest power in South Asia. As India's economy continues to grow strongly in coming years, its political and economic status in international affairs will be further strengthened. That's why the United States and Japan, which are geographically far from South Asia, tend to increasingly rely on India in regional affairs in these years.

India is expanding its influence around the world and, therefore, attracting global powers. It is the connecting point for many triangular relations in South Asia. It will be reasonable to properly handle China-Indo-Pakistan relations, which is not easy for China despite that China-India relations have made considerable progress since the end of the twentieth century. In this context, CPEC will surely bear the burden of the hostility between India and Pakistan as well as the mutual mistrust between China and India.

### 2.3 GEOPOLITICS

For the construction of CPEC, geopolitics refers to at least three aspects: the geo-strategic values of South Asia itself, the Indo-Pakistan confrontation and the Kashmir conflict. In a sense, the Kashmir conflict is the crux and manifestation of the Indo-Pakistan rival, but its impact on CPEC will go beyond the scope of India-Pakistan relations, because CPEC, as scheduled, will pass through the controversial Gilgit-Baltistan region.

to put more investment in Pakistan's economy and infrastructure, including CASA-1000 and Karachi-Lahore pipelines.

<sup>9</sup>The BCIM, starting from Yunnan province, China, is planned to connect China, Bangladesh, India, and Myanmar. The rest four corridors include China-Mongolia-Russia, New Eurasian Continental Bridge, China-Central Asia-West Asia, and China-Indochina Peninsula corridor. They are called as "the first chapter of BRI Symphony" by some Chinese media.



### 2.3.1 *The Geo-strategic Values of South Asia*

South Asia boasts crucial geo-strategic values because its north-west part borders the Middle East, the world's treasure house of oil and gas resources. It is not only close to the Persian Gulf and the Arabian Sea, but also connects the Indian Ocean and the Pacific Ocean in the south with its far south end, and connects Southeast Asia in the east. Such geopolitical values are an important driving force for CPEC.

However, due to such important geo-strategic relevance, CPEC cannot go forward without external interference and pressures. Some suspicions about China's strategic intentions have already emerged. The strategic game among powers in South Asia is another challenge because big powers have never stopped coveting and scrambling for this region since modern times. During the Cold War, the United States contained the Soviet Union with all means, and the Central Treaty Organization and the Southeast Asia Treaty Organization were just two of its tools. Pakistan was the connecting point of these the two organizations. The White House had put pressures on Pakistan when President Musharraf was in power, trying to prevent Islamabad from handing over Gwadar Port to Chinese company for operation.<sup>10</sup> In recent years, the United States has devoted itself to developing a global partnership with India, making India the pillar of its Asia-Pacific strategy. And Russia has started to plan to go south since Peter the Great. The Soviet Union had good relations with India, and now, Moscow is trying to step up its relations with Pakistan while maintaining friendship with India at the same time. In 2014, Russia lifted the arms embargo on Pakistan and their bilateral economic cooperation has been significantly strengthened thereafter.<sup>11</sup>

Theoretically speaking, world powers could coexist with each other peacefully in any region. In recent years, China spares no efforts in promoting mutual benefit and win-win diplomacy. The so-called Cold War mentality, however, has been deeply rooted in some states. It was not

<sup>10</sup> Kiyva Baloch, "Can China's Gwadar Port Dream Survive Local Ire?" (December 2014), <http://thediplomat.com/2014/12/can-chinas-dream-of-a-pakistan-port-survive-local-ire/>. The Port of Singapore Authority (PSA) was entitled the rights to manage Gwadar port for 40 years in February 2007, but PSA voluntarily withdrew on January 30, 2013 due to huge deficit. After that, the operation rights of Gwadar Port were handed over to China Overseas Port Holdings Co., Ltd. for a period of forty years.

<sup>11</sup> Farhan Bokhari, "Pakistan Buys Initial Batch of Four Mi-35s," (August 2015), <http://www.janes.com/article/53758/pakistan-buys-initial-batch-of-four-mi-35s>.

originated from the competition and confrontation between the United States and the Soviet Union in the twentieth century, but a continuation of the ancient idea of zero-sum game. Although all countries have already been closely connected by economic globalization, the concept of a community with a shared future advocated by China still needs to overcome the political obstacles, among which the strategic mutual doubt among big powers is most dangerous.

### 2.3.2 *India-Pakistan Confrontation*

The most notable feature of the geopolitics of South Asia is that, on the one side, India takes the lead in terms of land area, population, economic strength, and development tendency, while on the other side, Pakistan, the second largest country of the region, keeps denying and refusing India's dominance. The hostility and confrontation between the two sides have lasted for about seventy decades. To make it worse, internal motivation to normalize the relations is nowhere in sight. The world has witnessed the two countries have been trying every effort to oppose and undermine each other in nearly all aspects of the social, political and economic life. Shortly after the launch of CPEC, it is frequently reported that India has taken secret moves in Balochistan to impede or destruct the projects. Islamabad and Rawalpindi have publicly condemned New Delhi for such actions on many occasions.<sup>12</sup>

Similar wars of words have never stopped between India and Pakistan since 1940s. Pakistan's accusations cannot be defined as conspiracy theory. They were not simply to discredit India, either. China and its growth are India's anxiety because New Delhi never get out of the shadow of the 1962 war. Pakistan's hostility is also a basic fact for India. As a result, India stays vigilant towards China-Pakistan friendship. It strategically believes that Pakistan is always trying to re-balance Indo-Pak's strength gap and undermine the sub-continent's geopolitical structure by allying with third players.<sup>13</sup> Through this prism, the foundation of China-Pakistan friendship has been deemed to be their common hatred against India. For instance, the so-called "Pakistan-China Axis" theory was popular in India in the late

<sup>12</sup>"India Criticized for Opposing CPEC," (June 2015), <http://www.dawn.com/news/1185887/india-criticised-for-opposing-cpec>.

<sup>13</sup>Gary K. Bertsch, Seema Gahlaut and Anupam Srivastava, (eds.), *Engaging India: US Strategic Relations with the World's Largest Democracy*, (New York: Rutledge, 1999): 223.

1960s. That theory nourished the famous “String of Pearls Strategy” after the end of the Cold War, saying China was intended to besiege India. Since CPEC was launched, India’s public opinion was whipped up once again by the old theory of the so-called “China-Pakistan Axis”.<sup>14</sup>

Pakistan is also on guard against India and has been trying its best to compete with it in terms of military, economic, diplomacy, etc. In recent years Pakistan suffered from economic recessions and stagnation, and the government is facing tremendous domestic pressures due to its lagging far behind India. Economic development thus became more and more important in China-Pakistan relations. In 1999, the two countries defined the economic and trade cooperation as the priority of their bilateral relations. In 2006, they signed the Preferential Trade Agreement (PTA) in 2003 and the Free Trade Agreement (FTA), bringing about rapid increase in bilateral trade. From 2000 to 2014, the trade volume between China and Pakistan increased from US\$794 million to US\$16 billion,<sup>15</sup> rising by more than 19 times. Over the same period, however, the trade volume between China and India increased from US\$2.9 billion to US\$71.6 billion,<sup>16</sup> more than 23 times’ growth. The main reason behind the difference was that India’s economy was greater in terms of size and strength. Still, this gap aroused concerns within Pakistan. Its media and scholars, aiming to narrow the gap between India and Pakistan, strongly suggested that China-Pakistan relations should strengthen its economic basis, particularly the economic and trade cooperation, as soon as

<sup>14</sup>G. L. Sharma, *The Pakistan-China Axis*, Calcutta: Asia Publishing House, 1968. For the new discussion after CPEC, see Andrew Small, *The China-Pakistan Axis*, London: Hurst, 2015.

<sup>15</sup>Musleh-ud Din, Ejaz Ghani, and Usman Qadir, “Recent Experience and Future Prospects of Pakistan’s Trade with China,” *The Lahore Journal of Economics, Special Edition* (September 2009): 87–110. The figures for 2014 are sourced from the Economic and Commercial Counseling Office of the Chinese Embassy in Pakistan: “A Brief Introduction to China-Pakistan Bilateral Economic and Trade Cooperation from January to December 2014,” February 5, 2015, <http://pk.mofcom.gov.cn/article/zxhz/hzjj/201502/20150200890010.shtml>.

<sup>16</sup>The figures for the year of 2000 are sourced from “China Customs Statistics,” quoted from “Analysis of the Development of Economic and Trade Relations between China and India” by Li Tianhua, *International Trade Issues*, no.1, (2004): 49–54. The figures for 2014 comes from the “India Trade Bulletin December 2014” by the Ministry of Commerce of China, [http://countryreport.mofcom.gov.cn/new/view110209.asp?news\\_id=43252](http://countryreport.mofcom.gov.cn/new/view110209.asp?news_id=43252).

possible.<sup>17</sup> CPEC was conceived accordingly to this request. The estimated investment of US\$46 billion of CPEC equals 20 percent of Pakistan's annual GDP, more than twice as much as the total foreign direct investment it has received since 2008. It is also estimated that US\$37 billion will be invested in Pakistan's domestic power grids,<sup>18</sup> aiming to help it pass its capital and power bottlenecks for economic development.

### 2.3.3 *Kashmir Conflict*

National territory and the borders are important parts of geopolitics. According to H.J. Mackinder's theory,<sup>19</sup> the South Asian countries' borders, except Maldives and Sri Lanka, are all set by arbitrary. As a result, lots of geopolitical conflicts took the roots such as disputes over territorial sovereignty, conflicts in rivers' water distribution, cross-border armed forces, etc. Among them, Kashmir conflict is most relevant to CPEC.<sup>20</sup>

Ever since their independence in 1947, India and Pakistan had been accusing each other of the illegal actions in Kashmir, which has led to two large scale wars. In the new century, India has blamed Pakistan repeatedly for supporting terrorists in Kashmir, which the United States has stepped in and identified Kashmir's anti-Indian forces like Lashkar-e-Toyba (LeT) as its foreign terrorist organizations (FTO). Currently, the land of Kashmir

<sup>17</sup>There are many comments in the Pakistani media. For academic analysis from Pakistan, see Farrukh Nawaz Kayani, Mumtaz Ahmed, Tahir Ali Shah, Umar Nawaz Kayani, "China-Pakistan Economic Relations: Lessons for Pakistan," *Pakistan Journal of Commerce and Social Sciences* 7, no. 3(2013): 454–462. For strategic analysis from Indian think tanks, see Sumita Kumar, "The China-Pakistan Strategic Relationship: Trade, Investment, Energy and Infrastructure," *Strategic Analysis* 31, no.5, 757–790, (<https://doi.org/10.1080/09700160701662278>).

<sup>18</sup>S. Mahmud Ali, "Pakistan's Year of Mixed Fortunes," (December 2015), <http://www.castasiaforum.org/2015/12/21/pakistans-year-of-mixed-fortunes/>.

<sup>19</sup>H.J. Mackinder, *The Geographical Pivot of History*, trans. Lin Erwei and Chen Jiang, (Beijing: Commercial Press, 2013): 30–38.

<sup>20</sup>Under the Anglo-Indian colonial government, the princely state of Kashmir enjoyed autonomy. The resolution on India-Pakistan partition passed in 1945 stipulated that the princely states have the right to decide their own future: either to join India, or to join Pakistan, or to maintain their independent status. On the eve of independence, both the Indian National Congress Party and the Muslim League wanted Kashmir. The Prince of Kashmir were Hindus, but most of the residents in the area were Muslims. In 1947, the two sides clashed over which country to join, which led to the intervention of both countries and thus triggered the first India-Pakistan war. In 1965, India and Pakistan fought fiercely again for Kashmir, forming today's Line of Actual Control (LoC).

is divided by the 1965 Ceasefire Line and controlled separately by the two countries.

China stays neutral on the Kashmir issue, and regards it as an dispute left over from history between India and Pakistan, hoping that the two countries will resolve it peacefully through consultation. As planned, CPEC will depart from Khunjerab Pass on China-Pakistan border, arrive at Islamabad via Gilgit-Baltistan (GB),<sup>21</sup> and then connect Gwadar Port in the south. The proposed projects within the Gilgit-Baltistan region include expanding and upgrading the old Karakoram Highway, building some railways, industrial parks, pipelines and hydropower facilities. India strongly opposed this plan. Its government lodged a formal diplomatic protest against China in 2014. When Prime Minister Modi visited China in May 2015, he expressed his concerns and worries about CPEC again. Indian domestic strategic analysts pointed out that these construction plans indicated that China, as a third party with great and direct interests of Kashmir issue, had formally intervened in the conflict.<sup>22</sup>

Such accusation is nothing new. In fact, protesting against China and Pakistan had become a daily routine of the Indian government to claim its sovereignty over Kashmir ever since China and Pakistan signed their bilateral border agreement in 1963. In the beginning, Delhi protested against China and Pakistan confirming their borders that include Kashmir. Then it made solemn representations against the Karakoram Highway project. Following that, it protested repeatedly against China's participation in building dams, roads and other infrastructures in Kashmir. It is foreseeable that India's blaming focus will shift to CPEC programs in the coming years.<sup>23</sup> Its

<sup>21</sup> Formerly known as the "Northern Areas," Pakistan changed its name to Gilgit-Baltistan by legislation in 2009, defining it "Special Zone". The disputes over the eastern, western and central routes of CPEC within Pakistan these years were about the route from Islamabad to Gwadar Port, not the part from Islamabad to Khunjerab.

<sup>22</sup> "Q. NO. 260. Projects of China and Pakistan in Neighbouring Countries," (December 2014), [http://www.mea.gov.in/lok-sabha.htm?dtl/24458/QNO260PROJECTS\\_PLUS\\_SPI\\_OF\\_PLUS\\_SPI\\_CHINA\\_PLUS\\_SPI\\_AND\\_PLUS\\_SPI\\_PAKISTAN\\_PLUS\\_SPI\\_IN\\_PLUS\\_SPI\\_NEIGHBOURING\\_PLUS\\_SPI\\_COUNTRIES.Editorial](http://www.mea.gov.in/lok-sabha.htm?dtl/24458/QNO260PROJECTS_PLUS_SPI_OF_PLUS_SPI_CHINA_PLUS_SPI_AND_PLUS_SPI_PAKISTAN_PLUS_SPI_IN_PLUS_SPI_NEIGHBOURING_PLUS_SPI_COUNTRIES.Editorial), "India's Objections to CPEC," (June 2015), <http://www.dawn.com/news/1185779/indias-objections-to-cpec>. Rumel Dahiya and Jagannath Panda, "A Tale of Two Disputes: China's Irrationality and India's Stakes," (June 2015), [http://www.idsa.in/policybrief/ATaleofTwoDisputesChinasIrrationalityandIndiasStakes\\_rdahiya\\_290615](http://www.idsa.in/policybrief/ATaleofTwoDisputesChinasIrrationalityandIndiasStakes_rdahiya_290615).

<sup>23</sup> An Indian think tank found that New Delhi's stance on the Kashmir issue seemed to be weakening: in the 1960s, it was a "stern representation," but now it has become an understatement of diplomatic protests and "reservations". Priyanka Singh, "The China Pakistan Economic Corridor and India," (May 2015), [http://www.idsa.in/idsacomments/TheChinaPakistanEconomicCorridorandIndia\\_psingh\\_070515](http://www.idsa.in/idsacomments/TheChinaPakistanEconomicCorridorandIndia_psingh_070515).

determination on Kashmir should not be underestimated. Modi has repeatedly expressed a strong stance on the border and territorial issues during his election campaign. When talking about the Zangnan issue (藏南地区, or the so-called “Arunachal Pradesh” by India) and the Kashmir issue, he criticized China’s expansionism and vowed that no force on the earth can encroach an inch of India’s land.<sup>24</sup> Modi’s way of expressing protests differed from his predecessors. In the past, Delhi used to complain through the foreign affairs department, but in 2015 Modi directly protested by himself, raising the issue to the highest political level between two states.

While implementing CPEC, China should not only deal with India’s diplomatic complains cautiously, but also guard against the all possible measures and actions it might take. Pakistani media has publicly criticized India for deliberately sabotaging CPEC since 2013 by instigating and supporting separatists in Balochistan.<sup>25</sup> It was no coincidence that India protested China’s aid in building infrastructures and facilities in the Gilgit-Baltistan region on the one hand, and conducted oil and gas exploration and development in the disputed waters of the South China Sea as invited by Vietnam on the other since 2011.<sup>26</sup> In short, India may crave for more weights by means of overt or covert checks and balances during the implementation of CPEC.

## 2.4 ENERGY POLITICS<sup>27</sup>

South Asia is geographically close to the oil-rich areas such as Iran and the Persian Gulf. It is also an ideal outlet for Central Asian energy exporting countries like Turkmenistan, Kazakhstan, and Russia. Connecting two major energy consumption and import regions of East Asia and Southeast

<sup>24</sup> John C.K. Daly, “India Unsettled by Proposed China-Pakistan Economic Corridor Through Kashmir,” *China Brief* 14, no.5 (March 6, 2014), [http://www.jamestown.org/single/?tx\\_ttnews\[swords\]=8fd5893941d69d0be3f378576261ae3e&tx\\_ttnews\[any\\_of\\_the\\_words\]=CPEC&tx\\_ttnews\[tt\\_news\]=42052&tx\\_ttnews\[backPid\]=7&cHash=2adf983d9d4ec272df948c627b9f517e#.VpiGOIk3ME](http://www.jamestown.org/single/?tx_ttnews[swords]=8fd5893941d69d0be3f378576261ae3e&tx_ttnews[any_of_the_words]=CPEC&tx_ttnews[tt_news]=42052&tx_ttnews[backPid]=7&cHash=2adf983d9d4ec272df948c627b9f517e#.VpiGOIk3ME).

<sup>25</sup> “India Criticized for Opposing CPEC,” (June 2015), <http://www.dawn.com/news/1185887/india-criticised-for-opposing-cpec>.

<sup>26</sup> Jyananth Jacob and ReshmaPatil, “Beijing Says Keep Off S China Sea, Delhi Unmoved,” (September 2011), <http://www.hindustantimes.com/delhi/beijing-says-keep-off-s-china-sea-delhi-unmoved/story-gtmH6WhDtbB6ODwLkKucI.html>.

<sup>27</sup> The “energy” mentioned in this paper refers exclusively to oil and natural gas, excluding nuclear energy, coal, shale gas and various clean energy sources.

Asia, South Asia bridges energy sources and markets, which makes it a stage for “Energy Politics in Central and South Asia”. The protagonists that have already appeared on the stage include all the South and Central Asian states like Russia, China, Iran, Qatar, Oman, and the ubiquitous actor around the world, the United States. With energy pipelines as its major component, CPEC is a latecomer to this stage of energy politics. This stage is based on the idea of, via the channel of South Asia, drawing the importing countries closer towards production areas and exporting countries closer towards markets. The connection between the importing and exporting countries is a natural product of the market rule. However, with the intervention of the United States, the connectivity between energy supply and demand has been distorted even blocked to a degree, eventually transforming energy economics into energy politics.

A typical example in this regard is the Iran-Pakistan-India Gas pipeline (IPI). The driving force behind IPI was that India and Pakistan needed to import energy while Iran wanted to export natural gas. The three parties began to discuss a joint project of pipeline in 1995, which they called the “Peace Pipeline”. Theoretically, the IPI project could combine India with Pakistan by sharing natural gas from Iran. Pakistan was willing to allow the pipeline passing through its territory before it reaches India, and India was also willing to entrust its energy import channel to Pakistan. The region would benefit from the *détente*. However, the IPI project went against American sanctions on Iran. As a result, the United States intervened directly. It imposed political pressure on Pakistan and provided financial aid as a supplementary, which proved to be successful in that the pace of Islamabad on IPI slowed down. At the same time, Washington negotiated with India for several times, and finally signed the US-India Civilian Nuclear Agreement in 2006. As an exchange, India withdrew from IPI project in 2009. The US-India Civilian Nuclear Agreement ostensibly seemed to be a perfect alternative to IPI, because it satisfied India’s urgent energy demand while maintaining US sanctions against Iran intact. But the real value of this agreement goes far beyond. It practically bypassed the Comprehensive Nuclear Test Ban Treaty (CTBT) and gave India the permission to be a nuclear state. It provided India with huge conveniences to possess nuclear weapons, laying the cornerstone for US-India global strategic partnership.

Pakistan was disappointed by Washington’s different treatments. It resumed the pipeline talks with Iran, although with India’s pulling out, the IPI was reduced to the Iran-Pakistan (IP) pipeline. The United States

kept pressure on Islamabad, threatening to impose sanctions against Pakistan. Knowing very well about this state's emergent power shortage, the United States attempted to persuade it to join the framework of the New Silk Road, which includes some energy projects like the Turkmenistan-Afghanistan-Pakistan-India Gas Pipeline (TAPI) and the Central Asia-South Asia Electricity Transmission and Trade Program (CASA-1000). All these projects were no more than a vision and, for the best, full of uncertainty in that the investment was not secured and Afghanistan, the key area the pipelines passed, was in chaos. As the domestic energy shortage in Pakistan got worse and worse, together with the pressure for fulfilling agreement from Iran, President Zardari finally launched a groundbreaking ceremony to construct the IP pipeline on March 11, 2013,<sup>28</sup> which was criticized by the United States immediately. As a matter of fact, the project stopped after the ceremony because Pakistan did not have the money to proceed. It is estimated that the total cost would be US\$1.5b to US\$1.8b.

After CPEC was launched, Pakistan expected China to aid the IP project, which was designed to connect South Pars, the largest natural gas field in the world, with a designed transmission capacity of 21.5 million cubic meters per day. China promised to take part in the pipeline. In 2015. The 700-km-long pipeline within Pakistan was divided into two parts, the part from Nawabshah in Sindh Province to Gwadar Port in Balochistan (over 600 kilometers) would be built by China, and the remaining part of about 80 km from Gwadar to the Iranian border would be constructed by Pakistan. As for the investment, China would provide 85 percent of the project fund in loans, and Pakistan would provide the remaining 15 percent.<sup>29</sup> The original IPI thus turned into the Iran-Pakistan-China (IPC) pipeline. Some analysts regarded IPC as an extension of CPEC.<sup>30</sup> So far, there are no signs showing India has interests to rejoin the pipeline project.

With the negotiation on the Iranian nuclear issue turned for the better, India started to find ways to strengthen relations with Iran actively. In

<sup>28</sup> By that time, 1100 kilometers of pipelines in Iran was reported to have been completed. Sajjad Ashraf, "The Iran-Pakistan Gas Pipeline: Pakistan's Energy Lifeline," (March 2013), <http://www.eastasiaforum.org/2013/03/27/the-iran-pakistan-gas-pipeline-pakistan-s-energy-lifeline/>.

<sup>29</sup> "China to Build Pakistan-Iran Gas Pipeline: Report," (April 2015), <http://tribune.com.pk/story/866893/china-to-build-pakistan-iran-gas-pipeline-report/>.

<sup>30</sup> Andrew Korybko, "Pakistan Is the Zipper of Pan-Eurasian Integration," (September 2015), <http://en.riss.ru/analysis/18882/>.



terms of energy relations, India re-explored the feasibility of building an Iran-Oman-India Deep-sea Gas Pipeline, also known as the Middle East-India pipeline. At the same time, it actively planned for a new gas trading mechanism among Turkmenistan, Iran and India. Both energy channels were designed to bypass Pakistan, which disclosed India's geopolitical considerations. It remains to be observed whether or not these projects can be completed, or what relationship they will have with the IP pipeline and CPEC in the future.

## 2.5 CONNECTIVITY POLITICS

Planning to build roads and railways to enhance the connectivity between China and Pakistan, CPEC is neither the first nor the only project in this regard. In the past 20 years, relevant states have put forward various connectivity plans, all of which are systematic in themselves whereas independent to one another.

India has longed for connecting Central Asia for a long time, which also coincides the desire of Russia and Central Asian states to go south to access the sea. Since India and Pakistan remain hostile to each other, all the go-north plans of India are designed via Iran, especially Iran's Bandar Abbas and Chabahar ports, which are, in fact, aided by Russia. In September 2000, India, Iran and Russia signed an agreement to jointly build the International North-South Transport Corridor (INSTC) in order to promote freight connectivity and trade cooperation among the members. But INSTC progressed very slowly and almost stopped from 2005 to 2012 due to various reasons. Restarted in 2012, INSTC has now expanded to 14 countries, covering the Indian Ocean, the Persian Gulf, the Caspian Sea Basin, and northern Europe,<sup>31</sup> and included both water and land transportation. INSTC is planned to start from Mumbai to the Bandar Abbas Port, and go northward by land to the Anzali on the south bank of the Caspian Sea, and then across the Caspian Sea by ferry to reach Astrakhan in Russia, and finally reach Central Asia and other European countries by railway. It is estimated that after its completion, the Eurasian freight distance will be shortened by 40 percent, and the cost will be reduced by 30 percent accordingly. At present, it takes 45 to 60 days to

<sup>31</sup> The other eleven members of INSTC are: Azerbaijan, Armenia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkey, Ukraine, Belarus, Oman, Syria, with Bulgaria as an observer country.

travel from Europe to Southeast Asia via the Suez Canal, and 25 to 30 days will do via INSTC in the future.<sup>32</sup>

Among India's efforts to connect Central and South Asia, its plan to combine Afghanistan via the Chabahar Port in Iran is most noteworthy.<sup>33</sup> India, Iran and Afghanistan are all very enthusiastic about this connectivity project, and India even defines it as "strategic necessity".<sup>34</sup> Afghanistan is eager to get rid of the current predicament that Karachi is its only outlet to the sea. Iran hopes to take this opportunity to develop its relatively backward Sistan-Baluchistan province, and to develop its Chabahar Port into a gateway and transportation hub for Eurasia as well. The arterial roads that connect India, Iran and Afghanistan have been built in the past decade. India has completed the 218-km-long highway from Delaram to Afghan southwest border city of Zaraji (Nimruz province). The 900-kilometer railway and highway are also under construction from Zaranj to the south, connecting the Chabahar Port via Iran's Mirak, Zabol and Zahedan.

Various connectivity plans will boost regional economy in the long run by accelerating the flow of economic factors, and will bring more development opportunities and ultimately promote a shared prosperity of the region. But people have different viewpoints. For instance, Indian media and government define its INSTC and other efforts to connect Central Asia as part of the New Great Game in Central Asian, which represents a battle for power, hegemony, profit, and resources.<sup>35</sup> CPEC is also deemed as a competitor in this game by Indians. In 2015, Indian strategic analysts suggested their government initiate an India-China Silk Route Corridor (ICSRC) project, which directly connects China, to offset the impact of

<sup>32</sup>Meena Singh Roy, "International North-South Transport Corridor: Re-energising India's Gateway to Eurasia," (August 2015), [http://www.idsa.in/issuebrief/InternationalNorthSouthTransportCorridor\\_msroy\\_180815](http://www.idsa.in/issuebrief/InternationalNorthSouthTransportCorridor_msroy_180815).

<sup>33</sup>In addition to INSTC, the Indian government is also concerned about three other transport routes passing through Iran to connect Central Asia. One is the Kazakhstan-Turkmenistan-Iranian-India corridor. Another is to extend the famous "Northern Transportation Network" (NDN) to the south and connect the Afghanistan-Iran-India transportation network. The third is the India-Iran-Afghanistan arterial road network.

<sup>34</sup>"India Accelerates Iranian Port Project after US-Iran Thaw," (November 2013), <http://indianexpress.com/article/business/business-others/india-accelerates-iranian-port-project-after-usiran-thaw/>.

<sup>35</sup>Indrani Bagchi, "India to Spread Tentacles into Central Asia via Iran," (March 2012), <http://timesofindia.indiatimes.com/india/India-to-spread-tentacles-into-Central-Asia-via-Iran/articleshow/12239197.cms>.

CPEC.<sup>36</sup> Some Pakistani scholars believe that India, Iran, and Central Asian states are worried about CPEC because it will bring a negative impact on the Chabahar Port and INSTC. “And they may take measures to impede CPEC out of such worries.”<sup>37</sup>

The competition between the Chabahar Port and the Gwadar Port has become a hot issue in Indian media in these years.<sup>38</sup> Chabahar, only 72 kilometers (44 nautical miles) away from Gwadar, is also a high-quality deep-water port. The Iranian government invited India to participate in developing the port in 2003. Until 2013, India’s involvement was quite limited. After CPEC was launched, however, India’s interest grew up obviously and the efficiency to develop the port got enhanced greatly. Connectivity became one of the priorities of Modi’s government.<sup>39</sup> In October 2014, the Indian government formally announced to participate in the Chabahar project, and promised US\$85 million for building two berths and container terminals in the port. According to one Indian media, both India and Iran governments believe that developing the Chabahar Port is an important way to increase their geopolitical weight against Pakistan, and to protect their common interests in Afghanistan and Central Asia. In March 2015, India and Iran signed a memorandum of understanding for developing the Chabahar Port, with the total investment of US\$195 million. In addition to the US\$85 million already invested, India would invest another US\$110 million. In May 2016, Modi signed a bilateral agreement for the Chabahar Port during his visit to Tehran, promising to invest US\$500 million in developing the Port<sup>40</sup> in order to accelerate the connectivity to Afghanistan, Central Asia and Russia.

<sup>36</sup> Stobdan, “The Need for Haste on Pakistan-occupied Kashmir: China Pakistan Economic Corridor Needs a Counter Strategy,” (October 2015), [http://www.idsa.in/policybrief/TheNeedforHasteonPakistanoccupiedKashmir\\_pstobdan\\_071015](http://www.idsa.in/policybrief/TheNeedforHasteonPakistanoccupiedKashmir_pstobdan_071015).

<sup>37</sup> Saima Perveen and Jehanzeb Khalil, “Gwadar-Kashgar Economic Corridor: Challenges and Imperatives for Pakistan and China,” *Journal of Political Studies* 22, no. 2 (Winter 2015): 351–366.

<sup>38</sup> Muhammad Zarrar Haider, “Maritime Compulsions of China Pakistan Economic Corridor,” *Defense Journal* 18, no.11 (June 2015): 20–23.

<sup>39</sup> “Iran Offers India a Bigger Role in Chabahar Port: Report,” (July 2015), <http://indianexpress.com/article/india/india-others/iran-offers-india-bigger-role-in-chabahar-port-reports/>.

<sup>40</sup> C. Raja Mohan, “Iran and India’s Road to Afghanistan,” (October 2014), <http://indianexpress.com/article/opinion/columns/iran-and-indias-road-to-afghanistan/>. Ashok K. Behuria and M. Mahtab Alam Rizvi, “India’s Renewed Interest in Chabahar: Need to Stay the Course,” May 13, 2015, [http://www.idsa.in/issuebrief/IndiasRenewedInterestinChabahar\\_BehuriaRizvi\\_130515](http://www.idsa.in/issuebrief/IndiasRenewedInterestinChabahar_BehuriaRizvi_130515). BBC News, “India and Iran Sign ‘Historic’ Chabahar Port Deal,” (May 2016), <http://www.bbc.com/news/world-asia-india-36356163>.

Shortage of investment is the biggest obstacle to all pipeline and road projects connecting Central and South Asia, including TAPI and CASA-1000 supported by the United States, INSTC jointly proposed by India, Russia and Iran, and India's efforts to connect Russia and Afghanistan through Iran, etc. Comparatively speaking, CPEC has its advantages in some aspects. For instance, compared with INSTC which involves more than one dozen of member countries, CPEC is easier to coordinate and implement in that the resources and strengths are more concentrated, and the base for cooperation is stronger as well. Compared with the Chabahar Port, CPEC has more investment, and the construction costs are lower<sup>41</sup> because China and Pakistan directly border each other on land. In fact, the Iranian President proposed a \$8 billion project to India in July 2015,<sup>42</sup> but Modi's government only offered a \$500 million construction agreement of the Chabahar Port after about one year's silence.

## 2.6 COGNITIVE POLITICS

Cognitive politics is manifested as gaps between understanding about CPEC by all parties whereas the core is the different attitudes and counter-measures thereof. It is natural to have different views on the same thing. But in the context of the so-called "China Threat Theory" and "Thucydides Trap", misunderstanding or over-interpretation may lead to serious political consequences. Similar tragedies happens repeatedly in international politics.<sup>43</sup> The cognition and attitudes of different countries towards CPEC resulted from complicated causes consist of practical interests, strengths, values, historical and cultural factors, etc. As complex and subjective as it is, human's cognition does not necessarily and cannot completely picture the reality. Once perception is formed, however, it becomes a structurally stable force which could be defined as bias or prejudice.

There are two major cognitive gaps concerning CPEC so far. One is the different understanding between China and Pakistan, and the other is the

<sup>41</sup> In terms of political risks, Baloch rebels and separatists also exist for a long time in Sistan-Balochistan Province of Iran, showing a rise in recent years.

<sup>42</sup> "Iran Offers India a Bigger Role in Chabahar Port: Report," July 18, 2015, <http://indianexpress.com/article/india/india-others/iran-offers-india-bigger-role-in-chabahar-port-reports/>.

<sup>43</sup> Robert Jervis, *Perception and Misperception in International Politics*. trans. by Qin Yaqing, Beijing: World Affairs Press, 2003.

over-interpretation by the international society. To some extent, some Chinese media played a role in building up the latter.

The gaps in understanding of CPEC between China and Pakistan lies in at least two aspects. Firstly, the Pakistani people share a high expectation for the corridor and believe it is the hope to change their lives. But for China, CPEC is just a project of BRI. Although being defined as BRI's flagship and model project, CPEC is affiliated to BRI. It is not an independent project. Secondly, the Pakistani people are generally excited about the estimated US\$46 billion investment, whereas in China, people tend to be more concerned about the hardships and risks CPEC might encounter and bring about. The volume of the CPEC investment is still other misunderstanding. The number came from private calculation. Someone concluded the total construction cost for the more than fifty projects of CPEC is US\$46 billion. Then this number was translated by Pakistani media as well as the politicians into "the total investment of CPEC" and got currency. China government did declare to build fifty plus projects within CPEC, yet has not officially stated the number, the source, and the composition of the investment.

These gaps in understanding are closely connected and will impact on CPEC for the long run. To a certain extent, they are reshaping Pakistan's domestic politics, and may influence the long-term bilateral relations between China and Pakistan significantly. The expectation of US\$46 billion has already activated various social and political forces in Pakistan. Actions and competitions for interests are spreading among political parties and provinces, private and public sectors, government and the military forces. Historical political contradictions and the emerging issues are challenging Islamabad and its governance capability. Pakistani people are expecting CPEC to change their destiny from now on. Some public servants have even expressed their optimism that when the corridor is completed, all problems in the country will be solved, including separatism, extremism and terrorism. In other words, CPEC has been regarded as a panacea for them. However, the experiences of China and many other states have already proven that economic development cannot solve some problems. In some cases, the new challenges that occur in the process of social and economic development are not only increase in amount, but also become more complicated and difficult to solve.

CPEC is widely over-interpreted in international society. It was originally and officially recognized by China and Pakistan governments as economic cooperation to promote bilateral investment and trade, thus

realizing a shared prosperity for the two states.<sup>44</sup> In the autumn of 2013, CPEC gained a new identity as the flagship and model project of BRI after China proposed the Silk Road Economic Belt and 21st Century Maritime Silk Road initiatives.

Later, the new identity of CPEC almost replaced the original one. Under the greater framework of BRI, CPEC was no longer interpreted from the perspective of China-Pakistan friendship, but was recognized as a part of BRI, which was defined as China's new diplomatic strategy by international society. As a result, many strategic analysts were busy digging, imagining and construing the so-called China's strategic intentions behind CPEC, as if China had conceived CPEC for a long time. Even in Pakistan, many commentators only focused on what strategic benefits China could obtain from CPEC, but never pointed out that it was originally proposed by General Musharraf. So did some scholars in China. In the context of the "China Threat Theory," would such statement really be conducive to the implement of CPEC and promote China-Pakistan relations? Probably not. In the past, most countries were accustomed to China-Pakistan friendship, and not very concerned about the status quo and prospects of Pakistan's economy. However, after the Chinese media clearly described CPEC as the flagship and model project of BRI, a lot of extra attentions were aroused therefrom.

Although both China and Pakistan governments have made it clear for many times that CPEC does not target any third party, international community are obviously not convinced. Robert Jervis points out that an actor who thinks himself will not pose a threat to others often assumes that others will understand that he has no hostility. But in fact, others may neither understand it nor believe it.<sup>45</sup> It is true especially for those countries lacking strategic trust in China and being hostile to Pakistan. Their prejudices, suspicions and speculations are part of the reality that CPEC must face. The point is that the influence of cognitive politics does not merely exist at the cognitive level in international politics; subjective doubts and suspicions often lead to preventive or preemptive policies and measures, which have shown signs in Balochistan for now and might be even worse in the future.

<sup>44</sup> "Li Keqiang Visits Pakistan: Building Economic Corridors and Seeking Win-Win Cooperation," May 24, 2013, [http://news.china.com.cn/live/2013-05/24/content\\_20149644.htm](http://news.china.com.cn/live/2013-05/24/content_20149644.htm).

<sup>45</sup> Robert Jervis, *Perception and Misperception in International Politics*, trans. by Qin Yaqing, (Beijing: World Affairs Press, 2003): 372.

### 2.6.1 *Countermeasures and Suggestions*

On March 28, 2015, the National Development and Reform Commission, Ministry of Foreign Affairs and Ministry of Commerce of the People's Republic of China jointly issued the *Vision and Proposed Actions Outlined on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road*, explaining the background, principles, framework, priorities and China's proposed actions of these initiatives. This document advocates that the OBOR should be jointly built through negotiation to meet the interests of all, and welcomes all countries and international and regional organizations to actively participate so as to create a better future.<sup>46</sup> The consensus of an open and inclusive environment and a community with a shared future still seems to be a vision at the moment. However, CPEC has already been put into practice, and cooperation and competitions are also getting started by both open and secret means among relevant countries.

We have to admit that the structural factors of international relations in South Asia have deep-rooted historical causes, which are not likely to get changed completely overnight. Nonetheless, social relations are always open to be reshaped. International relations are no exception. Therefore, China can and should take conscious efforts to improve international environment for CPEC, although such improvement neither comes from empty words and explanations, nor from bottomless concessions and compromises to the opposing forces. Based on the previous analysis, this paper puts forward the following suggestions.

Firstly, CPEC should be split from BRI in external communication and get back to its true nature of bilateral friendly cooperation to meet the following three goals.

1. To reiterate and emphasize the only factor that is completely conducive to implementing CPEC: the bilateral friendly relations between China and Pakistan. Remain true to the original aspiration and keep the mission firmly in mind by fundamentally consolidating the driving force.
2. To make sure that CPEC will eventually further consolidate China-Pakistan friendship. The author believes that this is one of the criteria for measuring the success of CPEC. The priority is to prevent CPEC from being misunderstood by public opinion, especially from

<sup>46</sup>Vision and Proposed Actions Outlined on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road, <http://www.mofcom.gov.cn/article/h/zongzhi/201504/20150400929559.shtml>.

being regarded as a tool of the so-called China's grand international strategy, or being interpreted as China's strategy to pass its excess capacity over to Pakistan. So far, there are comments saying that the bilateral relations have partially shifted from friendship to mutual interest, and development aid has also been described as pure strategic investment. Such interpretation and images will do harm to CPEC and, therefore, must be reversed as soon as possible. Or else China-Pakistan friendship would hardly get improved by the success of CPEC in the end, and might even get worse instead. It is crucial to highlight the friendship nature of CPEC again.

3. To split CPEC from BRI might help reduce excessive doubts and interference from the international community, thus reducing the external obstructions. Tying CPEC to BRI does not increase people's confidence and understanding of BRI. Instead, it arouses excessive attentions from the international society where many countries are suspicious of China's strategic intention, which is not conducive to the implementation of CPEC and BRI and China-Pakistan friendship in the long run.

Secondly, China should take efforts to communicate and coordinate with CPEC-related states like Iran and Afghanistan, and participate in energy and transportation infrastructure projects in these countries, so as to integrate the regional energy pipelines and connectivity plans. China should take actions to promote a shared prosperity, the development and peace of the region, and to promote win-win relationship with other states, thus shaping and improving regional international relations.

Thirdly, do not ever expect India change its attitude towards CPEC and BRI unless India-Pakistan relations could be normalized.

Needless to say, it will be optimal if China could get India's understanding and support for CPEC. But the gap between desire and reality is huge. The hostility between India and Pakistan is deep-rooted in the geopolitical structure of South Asia and can hardly be changed in the short run. In fact, with the progress of CPEC, it will be increasingly difficult for China to maintain diplomatic balance between India and Pakistan, for which China should get well prepared in advance.

India will surely continue to express its protests against CPEC. In the coming years, its protests will mainly focus on the Gilgit-Baltistan issue, cross-border dams and ecological environment, etc., which may take place anywhere by all means, publicly and secretly. CPEC will definitely be an important issue in China-India relations before 2030. Beijing must get



prepared to respond to the public complains by New Delhi in Modi's style. At the same time, it is essential to strengthen cooperation with Pakistan to meet various challenges so as to guarantee the smooth progress of CPEC.

China has proposed the Bangladesh-China-India-Myanmar Corridor (BCIM) and the Maritime Silk Road initiative, which are both ignored by India. China should be aware of the strategic plans that India might propose in the future to undermine CPEC.

China-India relations are loaded with historical burdens. In fact, even without IR elements like the negative influences from the United States and Japan, India's memory about the 1962 war is alive. Indian's perceptions about the so-called "Dragon vs. Elephant" are difficult to change. It has been repeatedly proven that no bilateral relations could go far and sound without similar efforts from both sides.

Of course, China will not follow Pakistan's way and be hostile to India, either. To construct CPEC does not mean China chooses to be enemy of India. India is China's important neighbor, and China-India relations should develop in a normal way. The growth of economic and trade relations and social and cultural exchanges between the two countries have strong vitality within both countries.

Fourthly, China should address cognitive gaps between Chinese and Pakistani peoples, and reach mutual understanding and consensus through enhanced communication.

China should pay special attention to the needs of Pakistan's social forces, trying to strengthen mutual understanding and cooperation between the Chinese and Pakistani enterprises. CPEC should be developed on the basis of China-Pakistan friendship, and nourish their friendship in return. Given the high expectations and political mobilization for CPEC in Pakistan, China should also pay attention to the impacts of CPEC on Pakistan's domestic politics, and prepare for possible scenarios.



# How Pakistan's Political System Works on China-Pakistan Economic Corridor: Political Dominance and Socio-economic Development

*Yao Huang and Yan He*

## 3.1 INTRODUCTION

By virtue of its geostrategic location, Pakistan is deemed by China as a key partner. Chinese President Xi Jinping's visit in April 2015 delivered Pakistan a handsome reward: the latter would receive investments worth 46 billion US dollars from China for the construction of China-Pakistan Economic Corridor ("CPEC"). According to its previous practices, China usually insists its principle of non-interference and takes in charge of capital and technical support in overseas investments. Yet Pakistan is a special case since it has remained as one of the world's poorest and most

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dangerous areas, and the majority section of the corridor is placed within Pakistan and set to cross areas that have a high frequency of terrorist attacks. Apparently, investing in Pakistan is a business with risks. The question is: on the condition that China follows the non-interference principle and relies on Pakistan's political operation to manage the resources in the corridor, will CPEC be able to reach its desired goals?

The existing literature has fully explored Pakistan's military dictatorship, Punjab's historical dominance, uneven fiscal distribution, and the rise of terrorism, but it seems that these issues were studied respectively. This chapter combines these issues, especially the current form of government, to examine the impacts of Pakistan's political system on CPEC. It is discovered that Pakistan's Punjab-dominated political system has led to an unbalanced allocation of fiscal resources, which has a direct effect on the rise of terrorism. Since terrorist attacks remain as the greatest threat to CPEC, the usually-practiced non-inference principle is worthy of discussion.

This chapter begins by revealing the political characteristics of Pakistan. The second section presents Pakistan's uneven revenue sharing formula driven by its political structure and discusses the provincial struggle for a fair distribution of fiscal resources. The third section highlights the link between unequal resource allocation and the rise of terrorism. Long-term economic stagnation and backward social development in poor provinces have paved the way for chaos. The last section of this chapter elaborates the benefits of CPEC as well as its major challenge—threat of terrorist attacks, and it also comments on China's role in alleviating Pakistan's instability.

### 3.2 LOPSIDED SHARING OF POLITICAL POWER

As the first state established after Second World War, Pakistan has undergone an intricate and daunting process of political development. Its geopolitical environment, vehement ethnic conflicts, and violence-plagued sectarian rivalries have haunted the country. What makes the situation worse is the military intervention. Moreover, decades of martial law have had negative consequences for the country's economic growth as well as social development, especially when compared with its neighbor India. However, in 2008, Pakistan's political development took a step forward democracy: the country started to exercise universal suffrage and formed a democratically elected government. Furthermore, in 2010, the

Eighteenth Amendment to the Constitution was passed, since which Pakistan's political system has changed from semi-presidential to parliamentary, and the power has been vested in the Parliament, or more precisely, in the representatives who carry out the interests of voters. Nonetheless, Pakistan's politics is still characterized by high centralization of power and the dominance of one province.

The Constitution of 1973 laid the foundation for the past four decades of Pakistani political development. It was undoubtedly more complete and developed, and it was regarded as "the best possible arrangement to accommodate the various political parties, political issues and demands, economic interests, parties' manifestos, and so on."<sup>1</sup> Indeed, the Constitution of 1973 has exerted the most profound influence on current political framework because it re-established a prime ministerial system in Pakistan. But the constitution also contributed to problems between the center and the provinces. The 1973 Constitution distributed legislative powers between the federal center and the provinces by adopting Federal Legislative List and Concurrent Legislative List. Accordingly, the former list included 67 subjects that the center was entitled to legislate by itself, while the latter had 47 subjects that both the center and the provinces could legislate. Most importantly, when the center and a province went into collision regarding a subject in the concurrent list, it was stipulated that the federal law should prevail regardless of chronological order. Thus vertically, the Federation's overall supremacy has constrained provincial autonomy, and this helps explain deepening grievances among provinces. Moreover, Pakistan is a highly centralized state since the federal government has centralized every aspect of the civilian bureaucracy. "The federal government controlled recruitment, training, posting, transferring, promoting and demoting of officers," and "...provincial governments felt helpless in the face of a centralist bureaucracy that managed the affairs of the provinces of their posting by giving priority to the interests of the federation," writes by Mohammad Waseem.<sup>2</sup>

Apart from the federal centralization, one province dominating all is another characteristic of Pakistan's politics. Punjab's dominance dates back to the nineteenth century. As Tan Tai Yong argues, Punjabis

<sup>1</sup>Hamid Khan, *Constitutional and Political History of Pakistan* (2nd edition) (Karachi: Oxford University Press, 2009): 374.

<sup>2</sup>Mohammad Waseem, *Federalism in Pakistan* (Lahore: Lahore University of Management Sciences, 2010), 12, <http://www.forumfed.org/pubs/Waseem-Fed-Overview.pdf>, accessed April 4, 2017.

established their exclusive position in the colonial India by providing most of the manpower in the Indian army from the late 1880s to 1947; their military participation rendered Punjab more influential than other provinces and known as “sword arm of the Raj”.<sup>3</sup> After the independence of Pakistan, the Constitution of 1973 further paved the way for Punjabization in Pakistan’s politics. Before 1971, East Pakistan accounted for approximately 55 percent of the population; however, the governing elites who were centered in the western part and enjoyed economic, political, and administrative superiority, hoping to achieve equal representation in the parliament as East Pakistan, were therefore determined to merge four provinces and territories of West Pakistan into One Unit in 1955 notwithstanding fierce opposition from Sindh, North West Frontier Province (“NWFP”, called Khyber Pakhtunkhwa after 2010), and Balochistan.<sup>4</sup> Prior to East Pakistan’s secession, Punjab was already virtually dominant in Pakistan, which evoked resentment from other ethnic groups. Apart from Bengalis’ active secessionism, separatist movements had also sprung up in Sindh, Balochistan, and NFWP.<sup>5</sup> When East Pakistan declared independence in December 1971, the center of gravity in the Federation shifted to Punjab, the most populous province with 57.36 percent of the population.<sup>6</sup> The result of one-prevails-all circumstance imposed considerable impact on the situation in the parliament. Aside from its overwhelming dominance in terms of political representation, Punjab has remained as the most educated area, the strongest economy, and the main source of senior officials in the crucial political and military sectors.<sup>7</sup> Therefore, it can be said that the Punjabis have been the dominant group in Pakistan and benefited in decision making at the federal level.

### 3.3 CONTENTIOUS FISCAL RESOURCE DISTRIBUTION

For a well-functioning federal system, a crucial precondition is having a reasonable distribution pattern of fiscal powers as well as a proper design for revenue gathering and allocation among federal units. Therefore,

<sup>3</sup>Tan Tai Yong, *The garrison state: the military, government and society in colonial Punjab, 1849–1947* (New Delhi: Sage Publications India, 2005): 17–18.

<sup>4</sup>Waseem, *Federalism in Pakistan*: 6–7.

<sup>5</sup>Stephen P. Cohen, *The Idea of Pakistan* (Washington, DC: Brookings Institution Press, 2004): 201.

<sup>6</sup>Ibid., 75.

<sup>7</sup>Ibid., 223–224.

intergovernmental distribution of fiscal resources and responsibility has always been a controversial issue for a federal state like Pakistan. In fact, as early as the colonial period, Punjab became dominant in the resource distribution as the British Raj gave most of its economic resources to Punjab in order to placate this dominant component of the army.<sup>8</sup> After Pakistan was established, with the help of its military and political power, Punjab designed a resource distribution pattern in its favour.

### 3.3.1 *Fiscal Mechanism: Provinces Rely on Federal Center*

As a result of federal centralization, Pakistan's central government is in charge of collecting approximately 90 percent of the revenues, while the provincial governments collect less than 10 percent of the revenue from some minor taxes assignments.<sup>9</sup> The federal government is also responsible for distributing revenues between the federation and provinces and amongst the provinces based on a revenue sharing arrangement called National Finance Commission ("NFC") Award, while the provinces take the responsibility of redistributing resources they receive from the center to local governments that are under their jurisdiction according to the Provincial Finance Commission ("PFC") Award, a resource-sharing revenue formula at the provincial level.<sup>10</sup> Figure 3.1 shows the structure of resource distribution in Pakistan.

As for the provinces, on the one hand, they get only a small portion of tax revenues due to their limited role in taxation, and they also have difficulty in generating non-tax revenues. On the other hand, they spend 30 percent of the total national expenditure but the federal government spends 70 percent.<sup>11</sup> Consequently, the financial deficit renders the provinces highly dependent on federal transfer and grants operated by the NFC.

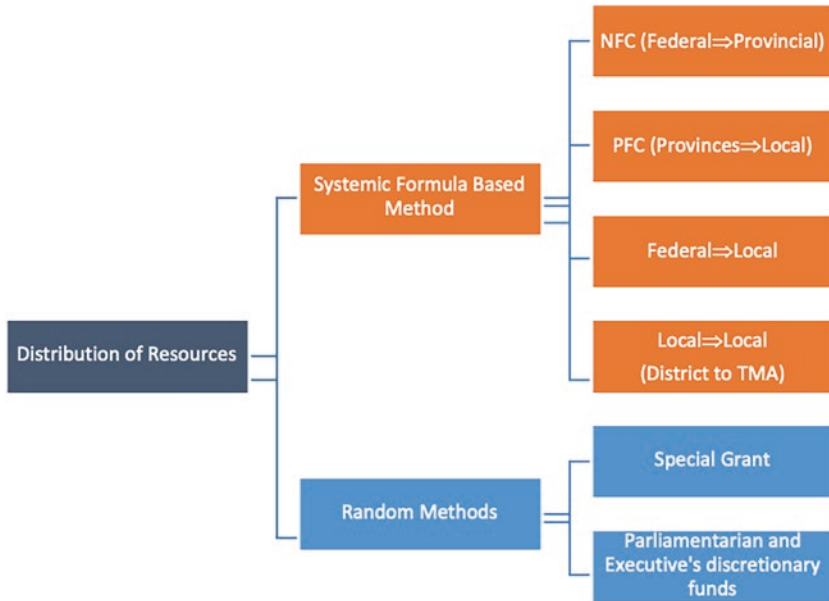
Functioning as a primary mechanism for vertical and horizontal inter-governmental resource sharing, NFC plays a critical role in Pakistan's resource distribution. What should be noticed is that the distribution of

<sup>8</sup>Tan, *The Garrison State*: 17–18.

<sup>9</sup>*Report of the National Finance Commission 2009* (Islamabad: National Finance Commission Secretariat, 2009), iii, [http://www.finance.gov.pk/nfc/reportofthenfc\\_2009.pdf](http://www.finance.gov.pk/nfc/reportofthenfc_2009.pdf), accessed July 21, 2017.

<sup>10</sup>Iftikhar Ahmed, Usman Mustafa, and Mahmood Khalid, "National Finance Commission Awards in Pakistan: A Historical Perspective" (Working Paper, Pakistan Institute of Development Economics, 2007).

<sup>11</sup>*Report of the National Finance Commission 2009*, iii.



**Fig. 3.1** Distribution of fiscal resources in Pakistan. (Source: Ijaz Nabi and Hina Shaikh, *Fiscal Federalism in Pakistan: A Radical Departure and Some New Challenges* (Lahore: Development Policy Research Center, 2010), 6)

taxes revenue has remained as a thorny issue between the federation and federal units and among the provincial governments for years. Given their excessive reliance on federal transfer and grants, provincial governments have asserted their rights to get a larger share of the divisible pool while the federal government has stood firm on its own interest. The distribution formula of the divisible pool has also provoked disaffection and animosity among the provinces, since the standard has used only one factor, namely population, for several decades, which benefited Punjab the most followed by Sindh, until the 7th NFC Award introduced different factors in 2009. Among several NFCs, only four awards were issued as a result of provinces' divergence on distribution formula since 1974. To be fair, long-term stagnation of issuing awards and ceaseless disputes over fiscal resource distribution arrangements have imposed a challenge to provincial economy, federal units' harmony, and even national unity.

### 3.3.2 *Population as the Sole Criterion*

As Fasihuddin stated, the current arrangement of revenue sharing in Pakistan between the federal and provincial governments is based upon pre-independence practice.<sup>12</sup> Punjab benefited from its large population in terms of resource distribution, since population had been used as the single criterion of divisible pool in the NFC awards before 2009.

Punjab has remained as the major beneficiary in both politics and fiscal resource sharing, whereas other stakeholders have suffered from criteria discrimination. Since federal transfers and grants can be regarded as the financial lifeline for provincial governments, three provinces, including Sindh, NWFP and Balochistan, have constantly demanded a balanced formula in revenue distribution, fighting with a muscular Punjab which has taken unwavering stand on population. While Punjab is the largest in terms of population, the other three provinces have different features: Balochistan is the least populated province but the largest in terms of area; Sindh is notable for its sea-port and related business; NWFP is the poorest and the most affected by terrorism. Their diverse needs have complicated the fiscal relationship. As a consequence, every NFC has been characterized by a struggle over the allocation of resources.

The basis of current revenue sharing was established by the 1973 Constitution under which it was made mandatory to form a new NFC every few years to review the distribution formula. The first NFC Award was announced by the Bhutto Government in 1974, whose divisible pool merely included income taxes, sales taxes and export duties and was allocated to federal and provincial governments at a ratio of 20:80. Since population was the sole criterion, Punjab got 60.25 percent of the provincial share, while Sindh, NWFP, and Balochistan received 22.50 percent, 13.39 percent, and 3.86 percent respectively. The second NFC was set up by President General Zia-ul-Haq in 1979 and the third one in 1985, but both of them did not establish a new award. The 1974 Award was thus continued till 1990, while the horizontal distribution proportion changed slightly after the population census in 1981, when the shares of Punjab, Sindh, and Balochistan were adjusted to 57.97 percent, 23.34 percent, and 5.30 percent, while that of NWFP remained unchanged.<sup>13</sup> A new

<sup>12</sup> Fasihuddin, "Seventh NFC Award implications for Balochistan", in *Balochistan: Rationalisation of Center-Province relations*, ed. M. H. Nuri., A. Ahmad., and F. Akram (Islamabad: Islamabad Policy Research Institute, 2010): 114.

<sup>13</sup> Ibid., 116.



award was finally given in the 1990 NFC. The divisible pool was expanded by embracing excise duties on tobacco and sugar, but the sharing between the Federation and the provinces was fixed at similar ratio and the horizontal portion was still divided on a basis of provinces' respective population, even though the provinces had appealed for a diversified formula. This fourth award also instituted "straight transfers from the federal to provincial governments of the development surcharge on gas, excise duties on gas and crude oil and net hydro-electric profits on the basis of collection," followed by the next NFCs.<sup>14</sup> This recognized the provinces' rights to be paid for the using of their natural resources, and therefore the total transfer they received increased to 45 percent of federal taxes revenues.<sup>15</sup> The fifth NFC was authorized in 1996 and its award was issued in 1997 after several contentious meetings. As a result, the share of provinces dropped to 37.5 percent while the federal government was assigned with 62.5 percent. There was however no change in the distribution formula and each province's respective proportion was unaffected. Even though royalties on crude oil, the development surcharge on natural gas, grants-in-aid (mainly for NWFP and Balochistan), and matching grants were given to provincial governments, the decline in the provincial share, along with internal and external shocks, damaged provinces' impaired economy.<sup>16</sup> The provincial share of divisible pool under different NFCs is shown in Table 3.1.

The sixth NFC was constituted in 2000 and reconstituted in 2003 but unable to finalize any award because of the divergent positions set by four provinces. On the one hand, all four provinces were unanimous in demanding a larger provincial share of resources in vertical distribution; on the other hand, the provinces held different opinions on the distribution criteria.

<sup>14</sup>Aisha Ghaus-Pasha, Hafiz A. Pasha, and Asma Zubair, "Fiscal Equalisation among Provinces in the NFC Awards," *Pakistan Development Review* 49, no.4 (2010): 570, <http://www.pide.org.pk/pdf/PDR/2010/Volume4/563-576.pdf>, accessed July 29, 2017.

<sup>15</sup>Usman Mustafa, *Fiscal federalism in Pakistan: The 7th National Finance Commission Award and Its Implications* (Islamabad: Pakistan Institute of Development Economics, 2011), 6.

<sup>16</sup>Ahmed, Mustafa and Khalid, *National Finance Commission Awards in Pakistan*: 8.

**Table 3.1** Provincial share of divisible pool under different NFCs (%)

<i>NFC</i>	<i>Federation: Provinces</i>	<i>Punjab</i>	<i>Sindh</i>	<i>Khyber Pakhtunkhwa ("KPK")</i>	<i>Balochistan</i>	<i>Total</i>
1st 1974	20:80	60.25	22.50	13.39	3.86	100
2nd 1979	20:80	57.97	23.34	13.39	5.30	100
3rd 1985	20:80	57.97	23.34	13.39	5.30	100
4th 1990	20:80	57.88	23.28	13.54	5.30	100
5th 1996	62.5:37.5	57.88	23.28	13.54	5.30	100
6th 2006 <sup>a</sup>	58.5:41.5	57.36	23.71	13.82	5.11	100
7th 2009	44:56 <sup>b</sup>	51.74	24.55	14.62	9.09	100

Source: Adapted from Usman Mustafa. *Fiscal federalism in Pakistan: The 7th National Finance Commission Award and its implications* (Islamabad: Pakistan Institute of Development Economics, 2011)

<sup>a</sup>Given provinces' failure to finalize recommendations, a special order was announced by President Musharraf in 2006

<sup>b</sup>The share of provinces would be 56 percent in the financial year 2010–2011 and 57 percent in the remaining years of the 7th NFC Award. Correspondingly, the federal share of the divisible pool would be 44 percent in the first financial year and decrease to 42.5 percent from the financial year 2011–2012 onwards

### 3.3.3 *A Turning Point: The 7th NFC Award in 2009*

The 7th NFC was constituted in 2005 and reconstituted in 2009. After fierce competitions over resource distribution formula, provinces showed their flexibility and finally reached an agreement. They signed the NFC report in the presence of the Prime Minister and Chief Ministers at Gwadar on the last day of 2009 and the Award was issued by the President Asif Ali Zardari in May 2010.<sup>17</sup> This NFC Award was a truly epochal achievement in Pakistan's history.

Firstly, success was achieved with unprecedented political consensus and the NFC process indicated a truly democratic development.<sup>18</sup> Secondly, provinces received more divisible pool transfers since their collective share was increased to more than 55 percent, while the federal government's share was reduced. Thirdly, progress was made in improving horizontal balance by introducing diversified criteria to distribution formula. Population lost its sole supremacy and its weight shrank to 82 percent, while poverty or backwardness, revenue collection or generation, and inverse population density were weighted at 10.3 percent, 5.0 percent, and 2.7 percent respectively. Fourthly, federal government's

<sup>17</sup>Fasihuddin, "Seventh NFC Award implications for Balochistan", 117.

<sup>18</sup>Marc-Andre Franche et al. Editorial to *Development Advocate Pakistan*, ed. Maheen Hassan (Islamabad: United Nations Development Programme Pakistan, 2015): 1.

collection charges for the revenue were decreased from 5.2 percent to 1 percent.<sup>19</sup> Fifthly, discretionary grants-in-aid to all provinces were abrogated but 0.66 percent of the annual provincial share was granted to Sindh to compensate for its losses because of the merger of 1/6th of General Sales Taxes in the divisible pool and NWFP was given additional 1 percent of the divisible pool for its expenses in the war against terrorism and in generation of hydro power.<sup>20</sup> Sixthly, the formula for Gas Development Surcharge computation was modified according to the demand of Balochistan, and the province was guaranteed to receive 9.09 percent of provincial share every year.<sup>21</sup>

The 2009 NFC Award presented a clear trend towards reasonable fiscal resource distribution in Pakistan. As shown, both the federal government and Punjab made a concession: The federal government's share of the divisible pool was reduced to 44 percent in the first financial year and to 42.5 percent in the following years; Punjab's proportion declined to 51.74 percent of the collective share. Simultaneously, the rights of smaller units to be paid for natural resources and their special needs were recognized. Briefly speaking, this Award not only assigned more resources to provinces but also invited structural development to horizontal allocation, which was viewed as a turning point in Pakistan's inter-provincial and center-provinces relations.

The four provinces have reached no consensus so far and consequently chose to extend the 7th NFC Award. Essentially speaking, the provinces' struggle over fiscal resource distribution stems from the imbalances of political power. As long as the power structure in Pakistan is lopsided, fights against inequality are hard to stop.

### 3.4 TERRORISM AND SOCIO-ECONOMIC DEVELOPMENT

Pakistan's fiscal resource distribution has demonstrated the frictions between the federal center and the provinces. Such an interdependent but also competitive relationship is based on a model: one's population proportion determines its political power in the state, which further dominates its assignment of resources. In view of the present distribution,

<sup>19</sup>Nasir Jamal, *Development Advocate Pakistan*, ed. Maheen Hassan (Islamabad: United Nations Development Programme Pakistan, 2015): 6.

<sup>20</sup>Muhammad Sabir, *Agenda for the 8th NFC: Lessons from the 7th NFC Award, Post-7th NFC Developments and Emerging Issues* (Karachi: Social Policy and Development Center, 2014), 2; Mustafa, *Fiscal federalism: Implications*, 8.

<sup>21</sup>*Report of the National Finance Commission 2009*, 20.

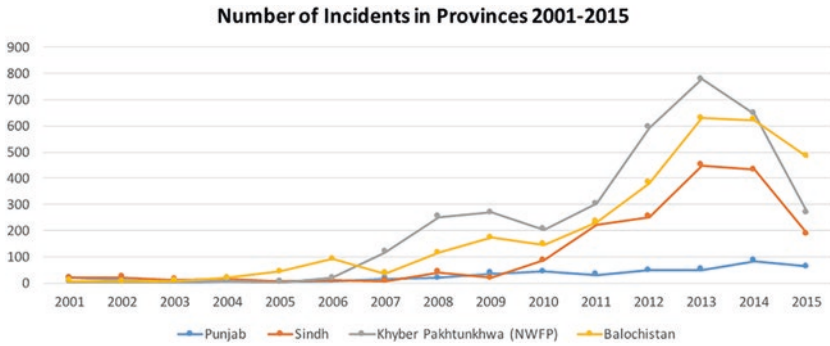
provinces with a demographic advantage, primarily Punjab and Sindh, prevail over others in the NFC. However, population-disadvantaged provinces, namely Khyber Pakhtunkhwa and Balochistan, are struggling against poverty and backwardness due to violent attacks and lack of funds. The newest distribution award with multiple criteria has been practiced for many years, but the reality is that Khyber Pakhtunkhwa and Balochistan.

Pakistan has suffered from accelerating terrorist attacks in recent years. The geographic distribution of incidents indicates that most of terrorist activities occur in Khyber Pakhtunkhwa and Balochistan, the poorest provinces in Pakistan. There are multidimensional causes of terrorism. It is accurate to say that internal sectarian hostility, religious extremism, Afghanistan's disorder, and external forces' involvement help explain the rise of terrorist attacks in Pakistan. However, it is also true that economic factors have contributed to the country's security deterioration.

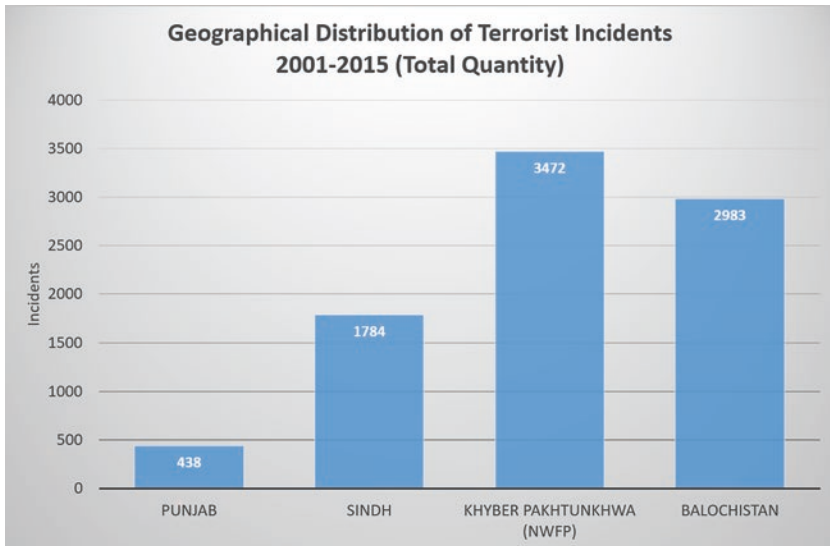
For decades, all provinces have been dependent on federal resource allocation. Unbalanced distribution has aroused resentment from the provinces in dire need of resources. People in these provinces have suffered from years of hardship, thereby venting their rancor through violence, which in turn inflicts a fatal blow on the provincial development. The turmoil in these underdeveloped areas makes it hard to generate revenues and available resources are therefore limited. In addition, these provinces have devoted the bulk of their funds to fight against terror, while socio-economic development has been placed behind. The poorer the provinces become, the more turbulent they get, which further invites economic consequences. As a result, the security issue intertwined with dire economy enters a vicious circle.

Figure 3.2 indicates that, terrorist attacks in the federal units started burgeoning in 2005. Before 2007, the numbers of incidents in the four provinces were all below 100; but during 2006, it shows clearly that Khyber Pakhtunkhwa (NWFP) had abrupt growth of incidents and surpassed Balochistan as the forefront of terrorism; beginning from 2008, the numbers fluctuated but all the provinces have suffered from increasing terrorist activities.

According to the geographic distribution of terrorist incidents in Pakistan from 2001 to 2015 as shown in Fig. 3.3, there are notable differences between provinces. Khyber Pakhtunkhwa has suffered the most with a total of 3203 incidents in this period; Balochistan ranked the second,



**Fig. 3.2** Number of incidents in provinces (2001–2015). (Source: By author, data from Global Terrorism Database, <http://www.start.umd.edu/gtd/>)



**Fig. 3.3** Geographical distribution of terrorist incidents (2001–2015). (Source: By author, data from Global Terrorism Database, <http://www.start.umd.edu/gtd/>)

while Sindh experienced nearly 1600 attacks. Compared to the other three provinces, Punjab was the least affected area assaulted by terrorism 375 times. Apparently, the distribution of incidents across time and place demonstrates that two provinces in the west part of Pakistan, Khyber Pakhtunkhwa followed by Balochistan, are the most deprived regions under the threat of terrors.

### 3.4.1 *Impacts of Unbalanced Resource Distribution on Terrorism*

Undoubtedly, Pakistan's deteriorating security and its west-centered feature have multifaceted incentives. "Terrorism not only has economic consequences, but also economic causes,"<sup>22</sup> thus in addition to understanding how internal and external religious extremism sparks the fire of terrorism, it is important to realize the influence of economic factors over social stability.

As the Global Terrorism Index (2015) analyzes, "terrorism in Pakistan has a diverse array of actors. While many of these groups are Islamist, there are also other organizations such as separatist movements for Baloch, the Bettani tribe and Sindhi people."<sup>23</sup> It is true that separatism has been rampant and plotted many terrorist incidents in Pakistan. Based on the research of Stephen Philip Cohen, the causes of separatism include uneven development, inequitable distribution of resources, a lack of representative political institutions, and an oppressive state apparatus.<sup>24</sup> In terms of political factors, as validated from the onset, Balochistan, Khyber Pakhtunkhwa, even Sindh are much less represented than Punjab in the state's decision-making center due to the population criterion and they are always overwhelmed in the Center-Provinces affairs by a strong federal center dominated by Punjab. Such weakness in political representation has generated feelings of being marginalized and oppressed. Economically speaking, no matter separatism or other kinds of extremism in Pakistan, their formation and development have been tightly connected with

<sup>22</sup>Mario A. R. Estrada et al. "The Economic Impact of Terrorism: A New Model and Its Application to Pakistan", *Journal of Policy Modelling* 37, (2015): 1066, <https://doi.org/10.1016/j.jpolmod.2015.08.004>, accessed May 14, 2017.

<sup>23</sup>"Global Terrorism Index 2015: Measuring and Understanding the Impact of Terrorism," *Institute for Economics and Peace*, November 2015, 23, <http://economicsandpeace.org/wp-content/uploads/2015/11/Global-Terrorism-Index-2015.pdf>, accessed May 11, 2017.

<sup>24</sup>Cohen, *The Idea of Pakistan*, 291.

disproportionate fiscal resources allocation and lopsided social and economic development.

This chapter shows that NFC as the primary resource transfer path bears a great responsibility. Owing to the fiscal centralization, provincial governments in Pakistan are highly dependent on federal transfers and grants, which implies that once the revenue distribution design is malapportioned, some of provinces will be short of resources they need to sustain development. As clarified in Sect. 3.2, the allocation of resources in Pakistan is in accordance with the NFC formula, and as a result of having less population, Khyber Pakhtunkhwa and Balochistan get a smaller share than the other two provinces in the east.

Table 3.2 below gives a better understanding of the federal transfers provinces received in the past financial years. The amounts Balochistan and Khyber Pakhtunkhwa received in the divisible pool distribution were far behind what Punjab and Sindh obtained. From 2007 to 2010, the combined shares of two western provinces were less than 20 percent of the total divisible pool. Sindh got much more than Khyber Pakhtunkhwa and Balochistan, but its amount was dwarfed by Punjab's overwhelming share. Starting from the financial year 2010–2011, less-populated provinces were granted greater amounts due to the enforcement of the 7th NFC Award. For example, Balochistan obtained 123.3 billion Rupees in financial year of 2013–2014, which was more than the 93.5 billion than it had had six

**Table 3.2** Transfers to provinces in divisible pool (Rs. billion)

<i>Transfers</i>						
<i>Financial Year</i>	<i>Punjab</i>	<i>Sindh</i>	<i>KPK</i>	<i>Balochistan</i>	<i>Total</i>	<i>Percentage of KPK and Balochistan in the total provincial share</i>
2007–2008	225.8	141.6	56.7	29.8	453.8	(19.0)
2008–2009	289.6	168.9	72.2	34.2	564.9	(18.8)
2009–2010	322.4	187.3	79.4	39.7	628.8	(18.9)
2010–2011	463.6	277.9	156.9	99.3	997.7	(25.7)
2011–2012	540.5	256.5	171.1	95	1063.1	(25.0)
2012–2013	568.2	269.6	179.9	114.2	1131.9	(26.0)
2013–2014	649.9	308.4	205.7	123.3	1287.3	(25.6)

Source: Pakistan Economic Survey, Ministry of Finance (Pakistan), <http://www.finance.gov.pk/index.html>

years earlier. Nonetheless, moderate modifications in distribution formula failed to shake the fiscal dominance of Punjab. The percentage of western provinces' systematic transfers stayed around 25 percent to 26 percent under the Award, which was only a quarter of the total provincial divisible pool. Such resource assignments are contrary to the principle of equality. Provinces with less population have fewer resources than big provinces to develop their economy and to invest in social sectors.

Table 3.3 selects the data of several financial years before and after the 18th Amendment from the economic surveys conducted by Pakistan's Ministry of Finance. As shown, in the financial year of 2007–2008 and that of 2008–2009, the taxes and non-taxes revenues Balochistan collected accounted for 6.6 percent to 6.7 percent of its total budget, while Khyber Pakhtunkhwa only made approximately 7 percent. Thanks to the 18th Amendment, more taxing power was released to provinces, and the proportion that provinces collected was able to increase. However, as the table demonstrates, their ability to generate their own fiscal resources was still restricted. As a consequence, it is difficult for the provinces to solve their socio-economic development issues.

Moreover, the provinces are not benefitting from having rich natural resources. As the largest gas producer producing more than 70 percent of the total gas production in Pakistan, Sindh only consumed approximately 46 percent of the gas it generated and the royalties it received were only 12.5 percent of total profits.<sup>25</sup> As the major hydro-electric power producing province, Khyber Pakhtunkhwa was not paid for this natural resource until 1991, and later it only received a small amount of payment under the influence of the central government.<sup>26</sup> Balochistan is the most extreme example. It is known that this least-populated province harbors abundant resources like gas, coal and minerals, but it is not the one to relish the fruits of resource exploitation. For instance, while most of Balochistan's gas was sold to other provinces at a very low price, merely 17 percent was consumed in the province and only one-sixth of its districts were covered by gas supply; moreover, as what Sindh and Khyber Pakhtunkhwa experienced, the royalties on gas the province received from the central

<sup>25</sup> Shaikh Abdul Rasheed, "Sindh Is Rich—Why Aren't Its People," *Nation*, April 16, 2015, <https://nation.com.pk/16-Apr-2015/sindh-is-rich-why-aren-t-its-people>, accessed May 21, 2017; Ijaz Nabi and Hina Shaikh, *Fiscal Federalism in Pakistan: A Radical Departure and Some New Challenges* (Lahore: Development Policy Research Center, 2010): 18.

<sup>26</sup> Nabi and Shaikh, *Fiscal Federalism: Radical Departure*: 18.



**Table 3.3** Balochistan and Khyber Pakhtunkhwa budget revenues (Rs. billion)

	<i>Balochistan</i>						<i>KPK</i>		
	2007–2008	2008–2009	2012–2013	2013–2014	2007–2008	2008–2009	2012–2013	2013–2014	
Total revenues	48.8	52.5	166.7	182.1	79.7	100.4	250.5	300.7	
Share in federal taxes	29.8	34.2	114.2	123.3	56.7	72.2	179.9	205.7	
Provincial taxes	0.9	1	1.2	2.8	2.4	3.9	8.1	11.7	
Provincial non-taxes	2.3	2.5	15.8	17.8	3.1	3.5	32.1	46.9	
All others	15.8	14.8	34	36.7	17.5	20.7	26.1	36.4	
Percentage <sup>a</sup>	6.6	6.7	10.2	11.3	6.9	7.4	16.0	19.5	

Source: Pakistan Economic Survey, Ministry of Finance (Pakistan), <http://www.finance.gov.pk/index.html>

<sup>a</sup>Percentage of revenues created by provinces in total provincial revenues

government was approximately 10 percent of total amount, which made people in Balochistan infuriate, thereby attacking several gas pipelines in order to prevent the federal government and other provinces from exploiting their natural resources; they targeted the supply routes to Punjab in particular, and industrial parks along the pipelines were forced to shut down.<sup>27</sup>

In fact, resentment over natural resources only partly explains some terrorist attacks. As Baloch leaders points out, the lack of development remains as an important cause of the province's grievances, for which the unfair resource distribution should be blamed.<sup>28</sup> As discussed above, on the one hand, provinces with less population were not able to get enough resources from the Federation; on the other hand, they were not granted with the authority to collect substantial revenues. The consequence is that insufficient and irregular fundings have led to the provinces' slow economic growth and also to their incapacity to deliver social service.

To further explore the impacts of unbalanced resource distribution over terrorism, geographic distribution of poverty worths a look as shown in Fig. 3.2. Governments' low spending on social development is one of the causes of the country's widespread poverty. As Arif Naveed and Nazim Ali assert in their report, over half of the population of Pakistan lives under the poverty line, and one-third of households are under the threat of poverty.<sup>29</sup> Western part of the country is clearly poorer, and the two poorest districts are located in Balochistan and Khyber Pakhtunkhwa.

In discussion of poverty and terrorism, Erin Connelly argued that these two subjects are interrelated.<sup>30</sup> The demographic structure of Pakistan shows that young people constitute the majority of population: 39 percent of the population is under 15 years old and 50.4 percent is under 19 years

<sup>27</sup> Alaiwah, "Constitutional Distribution of Natural Gas & Hydroelectric Power," *Never Mind* (blog), September 24, 2008, <https://alaiwah.wordpress.com/2008/09/24/constitutional-distribution-of-natural-gas-hydro-electric-power/>, accessed June 22, 2017.

<sup>28</sup> Ibid.

<sup>29</sup> Arif Naveed and Nazim Ali, Clustered Deprivation: District Profile of Poverty in Pakistan, *Sustainable Development Policy Institute*, September 2012, 27, [http://www.sdpi.org/publications/publication\\_details-358-36.html](http://www.sdpi.org/publications/publication_details-358-36.html), accessed July 4, 2017.

<sup>30</sup> Zahra Malik and Khalid Zaman, "Macroeconomic Consequences of Terrorism in Pakistan", *Journal of Policy Modelling* 35, (2013): 1106, <https://doi.org/10.1016/j.jpmod.2013.08.002>, accessed May 27, 2017.

old.<sup>31</sup> Comparing this, Pakistan's high youth unemployment rate, particularly in Khyber Pakhtunkhwa (13.6 percent in 2008–2009),<sup>32</sup> together with economic stagnation and an unfair distribution of resources, decreases the opportunity costs of participating in terrorist incidents.<sup>33</sup> Having no opportunities in poverty, young people are likely to be attracted by Madrassas associated with armed militant organizations which offer food, shelter, and a sense of group identity.<sup>34</sup> As SPDC's policy brief of Social Impact of the Security Crisis (2011) demonstrates, a large number of militants are from the lowest socio-economic segments of society, and most of terrorist activities have been implemented by young males in the country.

Therefore, it can be inferred that poverty has paved the way for extremism, which helps explain the high incidence of terrorism in Khyber Pakhtunkhwa and Balochistan.<sup>35</sup>

In general, the rise of terrorism in Pakistan is intertwined with the prejudiced resource distribution and economic stagnation, which is due to the highly centralized and one-province-dominant political system. Lacking political representation in national policy making makes it difficult for poor provinces to compete for resources. In the last decades, poor provinces have been in dire need of resources to fight against poverty as the NFC failed to distribute resources equally. The poorer the provinces remain, the more likely their inhabitants be attracted and involved in radicalism.

<sup>31</sup>National Institute of Population Studies (NIPS) and ICF International, *Pakistan Demographic and Health Survey 2012–13* (Islamabad and Calverton: NIPS and ICF International, 2013): 18.

<sup>32</sup>SPDC, "In Search of a Solution," in *Annual Review of Social Development in Pakistan 2009–10: Social Impact of the Security Crisis*, (Karachi: Social Policy and Development Center, 2010): 128.

<sup>33</sup>Muhammad Shahbaz et al. "An Analysis of a Causal Relationship between Economic Growth and Terrorism in Pakistan," *Economic Modelling* 35, (2013): 21, <https://doi.org/10.1016/j.econmod.2013.06.031>, accessed May 27, 2017.

<sup>34</sup>Akmal Hussain, "Terrorism, Development and Democracy: The Case of Pakistan," in *Terrorism in South Asia: Impacts on Development and Democratic Process*, ed. Sridhar K. Khatri and Gert W. Kueck (Colombo, New Delhi and Delhi: RCSS, Konrad Adenauer Foundation and Shipra Publications, 2003): 9.

<sup>35</sup>Rabia Sidat, "Policy Brief: Social Impact of the Security Crisis in annual review of social development in Pakistan 2009–10," *Social Policy and Development Center*, December 2011, 3, [http://www.spdc.org.pk/Publication\\_detail.aspx?sysID=707](http://www.spdc.org.pk/Publication_detail.aspx?sysID=707), accessed September 3, 2017.

### 3.4.2 *Has the 7th NFC Worked?*

With a larger share of revenues and multiple distribution criteria under the 7th NFC Award, provinces received a mass of additional resources, and they also obtained greater social sector responsibilities because of the 18th Amendment, therefore having more opportunities to make significant headway in socio-economic development in order to reduce poverty. However, the outcomes did not measure up to people's expectations. Key social indicators like the net primary school enrollment rate, infant mortality, and coverage of tap drinking water showed a degenerating trend instead.<sup>36</sup> It can be said that even though provinces were granted with a higher share of taxes, social sectors did not receive significant improvement.

Such worsening public service delivery has a few causes and effects. On the one hand, provincial governments are incapable of designing and implementing a larger social development portfolio, resulting in a waste use of resources; military strikes have been prioritized in anti-terrorism, leading to a shift of resources from social sectors to security-related expenditures; a substantial portion of the resources have been used on raising the salaries of provincial government employees.<sup>37</sup> On the other hand, the slowdown in the pace of social development has resulted in increasing level of poverty, and terrorism also risen after 2010. People's suffering from low income, poor education, and inadequate social services continues to provide a breeding ground for extremism and terrorism.

Provinces except for Punjab have determined to diversify distribution criteria in order to get more federal transfers and grants. They succeeded in the negotiation of the 7th NFC and received a several-fold increasing funding from the federation. If they had prioritized economic development and spent more resources in social sectors, poverty might have been mitigated, and then at least one of the causes of terrorism may be alleviated. Despite the increase in revenue, the weak provinces failed to make a change. Also, the continuing security crisis in Pakistan has proved that applying solely military forces to combat terrorism is far from enough. To assuage the violence in the country, it is necessary to realize the significant role of poverty alleviation in anti-terrorism strategy. Hence, it seems

<sup>36</sup> Ashfaq H. Khan, "Opinion: 7th NFC Award: Has It Worked?" in *Development Advocate Pakistan*, ed. Maheen Hassan (Islamabad: United Nations Development Programme Pakistan, 2015): 16–18.

<sup>37</sup> SPDC, "Initial Impact"; Sidat, "Policy Brief."

significant for Pakistan to achieve socio-economic growth and deliver the benefits fairly to all components of population.

### 3.5 CHINA-PAKISTAN ECONOMIC CORRIDOR

Pakistan's lopsided political environment and its severe security crisis have exerted negative impacts on foreign direct investment and economic development. This section tries to explore the question that will CPEC be able to reach its desired goals through analyzing from China's and Pakistan's perspectives.

The China-Pakistan Economic Corridor, as an essential component of One Belt One Road Initiative, was first proposed by Chinese Premier Li Keqiang when he visited Pakistan in May 2013. Two years later, during President Xi Jinping's April visit in Islamabad, China and Pakistan reached a consensus on the "1 PLUS SPI 4" arrangement, which not only prioritized the implementation of CPEC but also emphasized the construction of Gwadar Port, energy supply, and transport infrastructure as well as industrial partnerships.<sup>38</sup> There were 51 agreements in total, delivering 46 billion US dollars' worth of Chinese investments to Pakistan. As one of the slowest developing South Asian countries, Pakistan considers CPEC as a lifeline to stimulate its economy and promote its infrastructure.

As for the investor, given Pakistan's enormous geo-strategic potential, financing CPEC is in line with China's concerns. Yet such huge investments come with risks and obligations. Pakistan is known for its vulnerable security, and there are cases that militants have targeted Chinese investment projects and several Chinese got killed in terrorist attacks. Thus, the ongoing security crisis has posed a great threat to the construction of CPEC. Moreover, according to Pakistan's internal politics and its method of distributing resources, a large portion of Chinese funding is likely to flow to the power-holders and may not be able to reach where the need is greatest. If this happens, the gap between the rich regions and poor ones is likely to be further widened, which may enlarge the social instability and raise security risks for China's investments. Consequently, as the largest

<sup>38</sup>Tan Yifei, Wen Dao, Gong Jie and Nie Lubin, "Yidaiyilu Zhongba Jingji Zoulang Yangban" [One Belt One Road Initiative: The Model of China-Pakistan Economic Corridor], *21st Century Business Herald*, March 7, 2016, [http://epaper.21jingji.com/html/2016-03/07/content\\_33736.htm](http://epaper.21jingji.com/html/2016-03/07/content_33736.htm), accessed September 16, 2017.

foreign investor in Pakistan, China shall recognize the possible impacts by its massive economic infusion and incorporate the concepts of assisting Pakistan with poverty alleviation and relatively balanced economic development, making CPEC a better game-changer.

### 3.5.1 *The Motivations of China to Build CPEC*

Located on the shipping lanes of Persian Gulf, sharing borders with Iran, Afghanistan and India, and providing access to the sea for China, Pakistan has significant strategic value in terms of its geographical location. Therefore, as a rising economy, China is paying increasing attention to this traditional partner. By building a passageway connecting western region of China and the South end of Pakistan, China is able to reach the Indian Ocean directly, which makes it easier to get access to the Middle East, Africa, and even to Europe.

Admittedly, considering the severe security crisis in Pakistan, CPEC seems more challenging and high-risk than other corridors. China also announced its initiatives to build several Silk Road channels linking Central Asia, West Asia and Europe. For instance, according to the Xinhua News Agency, one of the channels was open on January 30th 2016 as the first cargo train from Illichivst, a southwestern port in Ukraine, via the Trans-Caspian International Transport Route, passing through Georgia and Azerbaijan, finally reached Kazakhstan in 15 days.<sup>39</sup> Another motivation was also achieved when the first train from Yiwu, a city in Zhejiang Province known for its large wholesale market, carrying thirty-two 40ft. containers of commercial products and travelling at a speed of 700 kilometers per day, via Kazakhstan and Turkmenistan, arrived at Tehran Train Station 14 days after its departure date January 28th 2016, saving 30 days compared to the normal sea voyage from Shanghai to Iran's Bandar Abbas port city.<sup>40</sup> The success of these routes seems to provide more reasons for not risking in Pakistan. However, if China manages to have a corridor

<sup>39</sup> Xinhua, "Ukraine-China Cargo Train on Silk Road Opens up Prospects for Trade Promotion," *Xinhua News*, February 1, 2016, [http://news.xinhuanet.com/english/2016-02/01/c\\_135062009.htm](http://news.xinhuanet.com/english/2016-02/01/c_135062009.htm), accessed September 5, 2017.

<sup>40</sup> Xinhua, "First Train from China to Iran Stimulates Silk Road Revival," *Xinhua News*, February 16, 2016, [http://news.xinhuanet.com/english/2016-02/16/c\\_135100997.htm](http://news.xinhuanet.com/english/2016-02/16/c_135100997.htm), accessed September 5, 2017.

across South Asia, it helps decrease dependence on Central Asia. Having alternative partners in Asia is one of China's strategic concerns.

In addition, the terrorism and separatism in Pakistan have a direct effect on China's domestic stability. As Louis Ritzinger says, "Elements of China's own Muslim Uyghur insurgency in its westernmost Xinjiang Uyghur Autonomous Region are reportedly tied to extremist networks in Pakistan and use the country's lawless western regions as a base of operations."<sup>41</sup> CPEC aims to build linkage between Balochistan's Gwadar Port and Xinjiang's Kashgar, expecting to fuel the economic development of underdeveloped areas along the corridor. The construction of CPEC also offers an opportunity for China to alleviate poverty and accelerate economic development in its northwestern region. Thus, the colossal investments may help the investor spur "economic growth and stability both at home and abroad, while strengthening its struggling ally."<sup>42</sup>

Last but not least, CPEC may assist China in diversifying its energy importing channels. As the one of the world's largest consumer and importer of oil and gas, China considers energy supply as one of its national security concerns; accordingly, China has to import approximately 4 million barrels of oil and LNG per day from the Persian Gulf oil states, heavily relying on the trade route that travels through Arabian Sea, Indian Ocean, Strait of Malacca, and South China sea, which is very insecure, time consuming, and high-cost.<sup>43</sup> Consequently, China has to find an alternative of current marine route, and CPEC seems to be a good option. By making use of the corridor that links with Chinese constructed and operated Gwadar Port, China's energy supply line can be much shortened as the oil and gas could be directly transferred through the land pipelines and reach the West of China.<sup>44</sup> CPEC enables China to be more flexible on distributing its energy imports, thereby strengthening its energy security.

<sup>41</sup> Louis Ritzinger, "The China-Pakistan Economic Corridor: Regional Dynamics and China's Geopolitical Goals," *National Bureau of Asian Research*, August 5, 2015, <http://www.nbr.org/research/activity.aspx?id=589>, accessed July 25, 2017.

<sup>42</sup> Ritzinger, "Regional Dynamics."

<sup>43</sup> Gulfaraz Ahmed, "The CPEC Opportunity," *Business Recorder*, February 25, 2016, <http://fp.brecorder.com/2016/02/2016022519778/>, accessed September 21, 2017.

<sup>44</sup> Ritzinger, "Regional Dynamics."

### 3.5.2 *Pakistan: Being a Beneficiary*

A longstanding challenge for Pakistan is to reach its untapped potential for socio-economic development. As a country lagging behind other economies in South Asia, Pakistan's GDP only achieved about 4 percent growth in the past few years. Problems such as the energy deficit as well as inadequate transportation and infrastructure have handicapped the country's economic and social progress. Thus since Chinese President Xi Jinping announced the \$46 billion move of CPEC in 2015, Pakistan has viewed the initiative as a rare opportunity to rewrite its fate.

It is clear that the government, military, and research institutes in Pakistan have placed high expectations on China's enormous investments. The CPEC initiative is seen as highly beneficial to this South Asian country. Accordingly, the CPEC consists of two segments. A sequence of transportation projects, including rails and roads linking up the northwest border of China and the south of Pakistan, are highlighted in the program. The other component is the establishment of special economic zones along the trade and transport route, comprising various energy projects.<sup>45</sup> The first phase of the corridor was said to be financed with approximately 46 billion dollars, distributing 34.4 billion to energy sectors, 9.8 billion to transportation infrastructure, 793 million to Gwadar Port, and 44 million to fiber optic projects, according to Pakistan's Ministry of Planning, Development & Reform. Therefore, approximately 70 percent of the investments are concentrated on power projects.

As analyzed earlier, the energy shortage has been a serious constraint to Pakistan's socio-economic development. China is trying to help its counterpart to solve this sticking issue by virtue of developing electricity facilities, including thermal, photovoltaic, wind, garbage power as well as hydropower. There are many power projects have been set up. For example, the first stage of Quaid-e-Azam Solar Power Park, a photovoltaic power station in the Cholistan Desert of Punjab, employing more than 2000 people to work for heavy machinery, power transmission lines, water pipes and pylons, was undertaken by Chinese company Xinjiang SunOasis; once the second stage is completed by another Chinese company Zongery, the industrial park will be able to generate 1000 MW of electricity,

<sup>45</sup> Engr Hussain Ahmad Siddiqui, "CPEC Projects: Status, Cost and Benefits," *Dawn*, July 13, 2015, <https://www.dawn.com/news/1194014>, accessed September 21, 2017.



adequate to power around 320,000 households.<sup>46</sup> The 720MW Karot hydropower station, another energy priority project about 30 miles away from Islamabad, receives funding of 1.65 billion US dollars from the Silk Road Fund.<sup>47</sup> It will provide more than 3.1 billion kilowatt hours of clean energy to the people in Pakistan as long as it is done by China's state-owned Three Gorges Corporation which is also entitled to develop a series of private hydropower projects, including the Kohala program in Azad Jammu & Kashmir, with the approval of Private Power and Infrastructure Board under the Government of Pakistan.<sup>48</sup> This Chinese corporation has been invited by Pakistani government to join the construction of wind power generation projects as well. The first wind power project of 50 MW is located in Thatta District, near Karachi the capital city of Sindh, and it has supplied the electricity since November 2014.

In addition to energy sectors, CPEC has emphasized building a complete network of transportation that would facilitate trade and communication in Pakistan. For instance, according to the news released by China's State-owned Assets Supervision and Administration Commission of the State Council, the largest transportation infrastructure project of CPEC, a 392-kilometer-long section between Sukkur and Multan as a part of the Karachi-Lahore Motorway, was contracted by China State Construction Engineering Corporation contracted on December 22nd 2015. The project will greatly improve the public transportation system in this most developed and populated area and further promote Pakistan's socio-economic growth. Moreover, the contract of Lahore Orange Line Metro Train Project was signed between leaders of both countries in April 2015. The 27-kilometer-long mass-transit project is financed by the Export-Import Bank of China and predicted to function in 27 months; since September 2015, local companies have started the piling for construction with the support of Chinese technicians.<sup>49</sup>

The considerable investments brought by the CPEC, whether in transportation or energy infrastructure, will boost unprecedented

<sup>46</sup> Zofeen T. Ebrahim, "World's largest solar park to light up Pakistan's future," *Dawn*, September 8, 2015, <https://www.dawn.com/news/1205484>, accessed September 21, 2017.

<sup>47</sup> Siddiqui, "CPEC Projects."

<sup>48</sup> Xu Wei, "Zhongba Qianle ZhemeDuo Xieyi Luoshi Sudu Feitong Xunchang," [China and Pakistan Have Signed Many Agreements and Made Rapid Progress], *Guancha*, February 17, 2016, [http://www.guancha.cn/Neighbors/2016\\_02\\_17\\_351285\\_s.shtml](http://www.guancha.cn/Neighbors/2016_02_17_351285_s.shtml), accessed September 21, 2017.

<sup>49</sup> Ibid.

socio-economic advancement to the people all along the route by creating a large sum of job opportunities and triggering local commercial growth.<sup>50</sup> In consequence, provinces are in competition for winning CPEC projects. Even though Sindh receive many CPEC energy projects as Punjab, its Representative Khursheed Shah believes that his province is being purposely neglected while Punjab is more preferred in the design of CPEC projects.<sup>51</sup> In terms of the design of transportation network, several political parties have questioned the CPEC planning, asserting “the ruling party is deliberately trying to alter the design of the corridor to favor the constituencies of its own MPs.”<sup>52</sup> Smaller provinces have also expressed their strongly opposition towards giving priority to the eastern route of CPEC. The government of Khyber Pakhtunkhwa warns that it will take extreme steps if the central government failed to prioritize the western alignment in the construction of CPEC.<sup>53</sup> Apart from protesting against the federal government’s preference for Punjab, the Balochis stressed their worries that CPEC projects may render their interests jeopardized and marginalized. Such fights among parties have exerted negative influences on CPEC. Although an All Parties Conference was held on January 15th 2016 to remove the reservations of political parties as well as of provincial governments, concerns remain unsolved.

### 3.5.3 *What to Do to Reduce Terror Threats?*

There is no doubt that the progress of CPEC could be derailed by many challenges, one of which is the menace of terrorism. Terrorists have directed attacks against key infrastructures and their employees to wreak economic havoc upon the federation. China, with various projects across Pakistan and thousands of Chinese technicians working and living in this

<sup>50</sup> Gulfaraz Ahmed, “The CPEC Opportunity,” *Business Recorder*, February 25, 2016, <http://fp.brecorder.com/2016/02/2016022519778/>, accessed September 21, 2017.

<sup>51</sup> Web Desk, “CPEC Benefiting Only One Province Will Bear Negative Results: Khursheed Shah,” *Tribune*, November 13, 2015, <https://tribune.com.pk/story/990623/cpec-benefiting-only-one-province-will-bear-negative-results-khursheed-shah/>, accessed September 21, 2017.

<sup>52</sup> Muhammad Daim Fazil, “The China-Pakistan Economic Corridor: Potential and Vulnerabilities,” *Diplomat*, May 29, 2015, <https://thediplomat.com/2015/05/the-china-pakistan-economic-corridor-potential-and-vulnerabilities/>, accessed September 21, 2017.

<sup>53</sup> Abdul Manan, “PM Forms Committee for Redressal of Reservations on CPEC,” *Tribune*, January 15, 2016, <https://tribune.com.pk/story/1028011/pm-forms-committee-for-redressal-of-reservations-on-cpec/>, accessed September 21, 2017.

region, is not exempted from terror threats. According to the news, three Chinese port workers were shot to death in a premeditated attack at Gwadar in May 2004; in February 2006, three Chinese engineers and their Pakistani driver got attacked by Baloch Liberation Army in a town near Karachi, when the workers left a local cement factory without being accompanied by their guards.<sup>54</sup> Chinese facilities have also been targeted by terrorist activists. In July 2013, four fuel trucks working for Chinese operations were destroyed by militants in Chaghi District, not far from Quetta the capital city of Balochistan; in March 2015, several tankers supplying oil for a Chinese company in the same area were set on fire and the drivers were kidnapped by an unknown organization.<sup>55</sup> Needless to say, the unstable security situation in Pakistan has severely undermined the interests of Chinese investors.

Even though Pakistan military has decided to form a special force with estimated 13,000 soldiers to protect the security of Chinese investments along the corridor, there are a few principles to bear in mind when dealing with the security challenge.<sup>56</sup> Reviewing the causes of instability in Pakistan, the country's Punjab-centric political system has greatly affected the balance of fiscal resource distribution and attributed to provincial resentment. If China relies on Pakistan's internal operation to allocate CPEC's resources, there is a likelihood that most of the resources would flow to the most populated Punjab. Khurshid Khan, Sindh's representative as the leader of the Opposition in the National Assembly, points out that benefits' only flowing into one province will have negative consequences, as smaller provinces will hold more grievances against Punjab.<sup>57</sup> Supposing that the corridor enhances the growth of only one stakeholder, socio-economic disparity between provinces would be further exacerbated, strengthening social basis for terrorism and inflicting more dangers to China's investments. Therefore, it is crucial for China to take the

<sup>54</sup> "China Workers Killed in Pakistan," *BBC News*, February 15, 2006, [http://news.bbc.co.uk/2/hi/south\\_asia/4716820.stm](http://news.bbc.co.uk/2/hi/south_asia/4716820.stm), accessed September 28, 2017.

<sup>55</sup> Kiyra Baloch, "Chinese Operations in Balochistan Again Targeted by Militants," *Diplomat*, March 27, 2015, <https://thediplomat.com/2015/03/chinese-operations-in-balochistan-again-targeted-by-militants/>, accessed September 28, 2017.

<sup>56</sup> Syed Raza Hassan, "To Protect Chinese Investment, Pakistan Military Leaves Little to Chance," *Reuters*, February 8, 2016, <http://www.reuters.com/article/pakistan-china-security-gwadar-idUSKCN0VH06F>, accessed September 28, 2017.

<sup>57</sup> Desk, "CPEC Benefiting."

appeals of weaker provinces' into consideration in terms of resource distribution and offer chances to all parts of Pakistan.

With the infusion of China's efforts, Pakistan's power crisis has been reduced, and its transportation network has been renewed, thus giving the country more economic potential. More can be done to reduce the threat of terrorism.

More social responsibilities should be considered in investments. Given the previous analysis of 7th NFC Award, provinces did not address social development issues notwithstanding the help of additional fiscal resources, but CPEC can make a change. Aiming to boost local communities' living condition, China is working with the Government of Pakistan to build schools and hospitals and provide a series of skill training programs in Gwadar. It is a good start but far from enough. Demand for education and health care is high among young people across Pakistan. If CPEC is able to offer more opportunities for the people along the routes in social sector, it will help improve the security of the region.

Employment is critical as well. In Balochistan, people have long-standing resentments towards the federal government for not getting their due share of its natural resources and lack of opportunities of schooling as well as medical aiding. Their frustration had been intensified as the past mega projects in this area neglected the natives' demand for jobs and attracted a host of non-Balochi settlers. Thus, it is likely for the locals to get scared by the arrival of CPEC. "We are not against the Gwadar deep seaport, CPEC or any other developmental project. But if it is meant to marginalize the native people like Red Indians then we would not allow it to happen," says Mir Kabeer Ahmad Mohammad Shahi, Senator of the ruling party in Balochistan, in an interview with *The Nation* in July 2015.<sup>58</sup> Clearly, to eliminate local people's reservations whether in Balochistan or other places, it is advisable to involve both locals and minorities in sharing the socio-economic benefits brought by the CPEC projects. By contributing more employment opportunities on a basis of equality, CPEC can enable local people to make a better life on their own efforts, which may help to eradicate the roots of instability.

In short, CPEC plays a pivotal role in China's strategic concerns and Pakistan's socio-economic development. In spite of being highly

<sup>58</sup> Shah Meer, "CPEC: A Bad Deal for the Baloch People?" *Diplomat*, December 30, 2015, <https://thediplotat.com/2015/12/cpec-a-bad-deal-for-the-baloch-people/>, accessed September 28, 2017.

celebrated at the governmental level, CPEC has a long way to go in convincing the public of Pakistan that the “P” in CPEC stands for Pakistan rather than for a single province (Nasir, 2016) and in decreasing security vulnerabilities.<sup>59</sup>

### 3.6 CONCLUSION

China’s emergence as a global player and its growing influence over neighboring countries is the subject of much discussion. The CPEC initiative is one of the best examples of China’s economic impacts. This huge investment, on the one hand, brings a golden opportunity for Pakistan to boost its competitiveness; on the other hand, it help China settle its own issues. In consequence, addressing the challenges that CPEC encounters is crucial to all the stakeholders.

Pakistan is one of the world’s poorest and least stable countries, and the risk of investing in this area is fairly high. As a legacy of constitutional design, the dominance of most populous Punjab in state affairs has stayed unchanged for years. Moreover, the country has experienced continuous conflicts in Center-Provinces relation, mainly reflected in fiscal resources distribution, as a result of the federation’s centralization. However, greatly influenced by unbalanced representation in the political system, NFC, the primary transfer path of fiscal resources in Pakistan, insisted a single distribution criterion that favored more-populated provinces, in spite of other provinces’ strong opposition. Decades of unbalanced resource allocation have enlarged the disparity of socio-economic development among provinces.

In addition to being caused by religious extremism, ethnic disputes, and external security environment, the rise of terrorist attacks seems associated with resource distribution. Years of uneven resource distribution determined by the one-province-dominated political system have contributed to the socio-economic stagnation in poor provinces. Insufficient funds have disabled governments in these provinces to facilitate their economic growth, let alone to invest in infrastructure or to provide qualified public services. People in poor provinces, particularly in Khyber Pakhtunkhwa and Balochistan, have suffered from limited income, low education levels, lack of medical care, and high unemployment, all of

<sup>59</sup> Abbas Nasir, “What’s ‘P’ in CPEC?” *Dawn*, January 9, 2016, <https://www.dawn.com/news/1231714/whats-p-in-cpec>, accessed September 28, 2017.

which motivate many young people to participate militant groups and even execute terrorist activities. Despite that the connection between poverty and terrorism remains controversial, it seems clear that developing economy in poor provinces and enabling all to share the economic achievements will help reduce social contradictions and extremism threats.

Given the previous practices of resource distribution, existing political system in Pakistan may place more CPEC investment projects in population-dominant areas, which is likely to intensify the sense of deprivation and marginalization among people in weak provinces. Furthermore, it is untenable to view eastern provinces as safe havens because CPEC's facilities and employees can hardly be exempted from threats of attacks regardless of their locations. Thus, CPEC shall be a chance for Pakistan to develop its economy evenly. It is significant for Chinese investors to recognize the features of Pakistan's internal politics and to avoid excessive concentration of CPEC resources. In addition to assisting in developing local transportation and energy sectors, aiding in local social development such as providing more schools, medical support and job opportunities to local communities is recommended.

What CPEC can do for the people who have suffered poverty and turbulence for years is more than GDP growth. An evenly socio-economic developed Pakistan is more forward to safety and stability. A corridor to peace will be win-win for both China and Pakistan.



# Research on the Relationship between Pakistan's Institutional Risks and China's Foreign Direct Investment in Pakistan from the Perspective of Bilateral Political Relations

*Dongkun Li*

## 4.1 INTRODUCTION

China and Pakistan have developed friendly bilateral political relations based on deep mutual trust since their establishment of diplomatic relations in 1951. On entering the twenty-first century, the focus of China-Pakistan bilateral cooperation gradually shifted from geopolitics to geo-economics under the changing international environment and the demand of domestic development. During President Xi Jinping's visit to Pakistan in April 2015, China and Pakistan signed altogether 51 bilateral agreements with a total investment of US\$46 billion. Having witnessed such a big increase in Chinese FDI in Pakistan, many scholars remain

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cautiously optimistic about this because of the high institutional risks in Pakistan. According to the World Bank's Worldwide Governance Indicators (WGI) which are commonly used to measure the level of institutions and governance capacity of a country, Pakistan is significantly below the world average level in aspects of corruption control, government effectiveness, political stability and control over violence and terrorism, laws and regulations and rule of law, etc. Among which, the value of Pakistan's political stability and control over violence and terrorism have been well below  $-2.5$  since 2008,<sup>1</sup> which indicates that Pakistan not only suffers from political instability, but also fails to control violence and terrorism. Even though in 2013 Sharif's popular government has realized a smooth transition for the first time since the founding of Pakistan, and the conflicts among the government, the military and the judicial department have eased up, Pakistan's political risks are still very high, only slightly better than Somalia and Syria. Nevertheless, Chinese FDI in Pakistan has shown a rapid upward trend at the same time. Taking the stock of FDI as an example, it surged from US\$36 million in 2004 to US\$3.736 billion in 2014, up by more than 100 times in a decade, with the average annual compound growth rate at 59.08 percent, much higher than the growth rate (34.73 percent) of China's total FDI stock over the same period.

Generally speaking, high institutional risks of the host country are not conducive to attracting foreign investors. However, Pakistan's high institutional risks fail to discourage Chinese investors, large-scale inflows of Chinese investments have continued to increase in recent years. How to explain the synchronous increases in both Pakistan's high institutional risks and Chinese FDI? Is it due to special preferences of Chinese investors in selecting investment locations, or any other factors as risk mitigators? Taking into account their all-weather friendship and mutual trust since the establishment of their diplomatic relations, this paper attempts to review the relationship between Pakistan's institutional risks and Chinese FDI in Pakistan from the perspective of bilateral political relations. As a positive signal, good bilateral political relations can not only build the confidence of China's FDI in Pakistan, but also form the impetus for both governments to promote bilateral investment, thus providing more favorable policies and greater opportunities for the Chinese investment. As the Belt and Road Initiative (BRI) rapidly enters into the implementation stage,

<sup>1</sup>Values are roughly between  $-2.5$  and  $2.5$ , with a lower value indicating a country's poorer performance on the index.



this paper will help to gain a more clear-headed and profound understanding of CPEC, and provide experiences and lessons for China to make FDI in countries with relatively high institutional risks along the Belt and Road.

For the rest of this paper, Part II discusses the theoretical relationship between the selection of investment destination of FDI and institutional risks of a host country; Part III explores the types of institutional risks faced by Chinese FDI in Pakistan and further analyzes the changing relationship between Chinese FDI in Pakistan and the level of institutional risks, as well as the characteristics of these changes from 2005 to 2014; Part IV examines in detail the impact of the bilateral political relations on mitigating risks of Chinese FDI in Pakistan, by reviewing the developing process of the bilateral political relations; and Part V focuses on the future prospect of Chinese FDI in Pakistan.

## 4.2 THE SELECTION OF A LOCATION FOR FDI AND INSTITUTIONAL RISKS OF A HOST COUNTRY

The selection of a location for FDI has always been one of the key issues in international business researches.<sup>2</sup> It was first systematically discussed by Dunning in his early Eclectic Theory of International Production. According to his argument, to select a location for FDI, you should not only consider the factors of natural resource endowments, human capital levels, infrastructure conditions and market potentials, but also the institutional environment. As a decisive factor to the effective market mechanisms and domestic transaction costs in a host country, the institutional environment also plays a significant role in making strategic FDI by multinational companies in the long run.<sup>3</sup>

Usually, FDI tends to flow into a host country with sound institutions, which can effectively reduce the economic costs. However, terrible institutions (such as severe corruptions, poor legal systems and unstable politics, etc.) are nothing different from levying additional corporate taxes and increasing operating costs of FDI, impeding multinational companies

<sup>2</sup>Buckley, J., "Is the International Business Agenda Running out of Steam?" *Journal of International Business Studies*, (2002) 33 (2): 365–373.

<sup>3</sup>Wei, Y.Q., Zheng, N., Liu, X.H. and Lu, J.Y., "Expanding to Outward Foreign Direct Investment or Not? A Multi-Dimensional Analysis of Entry Mode Transformation of Chinese Private Exporting Firms," *International Business Review*, (2014) 23 (2): 356–370.

from coming in.<sup>4</sup> Moreover, sound institutions can also greatly reduce uncertainties which deprive investors of their assets. According to Asiedu's research on FDI in Africa, the more political stability a country has, the more FDI it will receive. With uncertainties rising in a host country, FDI will also be postponed accordingly.<sup>5</sup>

In reality, emerging economies are showing a relatively high tolerance for a host country with high institutional risks, especially China. Buckley and Cheung et al. have found out that indicators such as political risk level and corruption degree of a host country are directly proportional to the inflow of Chinese FDI by means of panel data regression.<sup>6</sup> In regard to the discordance between the classic investment theory and China's investment practice, current studies provide explanations from two aspects. One is China's motivation for FDI. According to studies by Kolstad, Wiig and Ji Xiangbao et al., China prefers to invest in developing countries with rich natural resources despite the high institutional risks there.<sup>7</sup> They attribute this paradox partially to its strong demand for natural resources. However, as a latecomer, China has limited choices to make large-scale investment in natural resources and strategic assets across the globe. As a result, considering the current resource distribution and development possibility, Chinese FDI flows more to countries with both abundant natural resources and high institutional risks. The other is the institutional factor including the favorable and supportive policies from both home country and host country. Among them, the impact of bilateral political relations on FDI has drawn more and more attentions, because as an alternative political arrangement for a host country with high institutional risks, good bilateral political relations can often help both governments reach a series of practical cooperation agreements to reduce uncertainties of bilateral investment

<sup>4</sup> Aizenman, J., Spiegel, M.M., "Institutional Efficiency, Monitoring Costs, and the Investment Share of FDI," *Review of International Economics*, (2006) 14 (4): 683–697.

<sup>5</sup> Asiedu, E., "Foreign Direct Investment in Africa: The Role of Natural Resources, Market Size, Government Policy, Institutions and Political Instability," *World Economy*, (2006) 29 (1): 63–77.

<sup>6</sup> Buckley, J., Clegg, L.J., Cross, A.R., Liu, X., and Voss Z., "The Determinants of Chinese Outward Foreign Direct Investment," *Journal of International Business Studies*, (2007) 38 (4): 499–518. Cheung, Y.-M., Haan, J.D., Qian, X.W., and Yu, S., "China's Outward Direct Investment in Africa," *HKIMR Working Paper*, no. 13, (2011).

<sup>7</sup> Kolstad, I. and Wiig, A., "What Determines Chinese Outward FDI," *Journal of World Business* (2012) 47 (1): 26–34. Ji Xiangbao, "An Analysis of the Influencing Factors of China's Foreign Direct Investment from the Perspective of Institutions," *Journal of WTO and China*, no. 9, (2014): 98–108.

environment.<sup>8</sup> Moreover, with longer friendship and the higher degree of mutual trust, it is more conducive to establishment and improvement of bilateral rules, and easier for a foreign investor to make self-adaption to the institutions of a host country and to protect its own interests and rights there.<sup>9</sup> Meng Xing and Dong Youde did regression analysis with FDI panel data of 25 countries from 2004 to 2012. The result shows the Chinese investors' concern for a host country's institutional risks is closely related to the bilateral political relations of both countries.<sup>10</sup> Chinese multinational companies are more likely to invest in a host country which has good bilateral political relations with China. It can be concluded that the factors which affect the selection of location for Chinese FDI are often related to the characteristics of a host country and its bilateral relations with China, and these factors share significant heterogeneity. However, in most of the existing studies, it is usually recommended to examine the above-mentioned issues as a whole from a macro perspective, and few carries out in-depth analysis according to the practical situation of a specific host country. Therefore, it is difficult to grasp the changes in the nature of bilateral political relations between China and a host country. If we fail to make more detailed analysis of complicated dynamic relations and the inner mechanism and functioning way thereof, how can we provide more targeted decision-making reference for Chinese investors who are planning to invest in a specific host country?

In regard to this, based on the existing studies, this paper takes Pakistan as the specific host country, and hopes to make the analysis result more meaningful. First of all, with relatively high institutional risks and relatively low natural resource reserves, Pakistan is a highly trustworthy country of Four Good Relationship<sup>11</sup> and all-weather strategic partner of China. China always gives diplomatic priority to China-Pakistan relations,

<sup>8</sup> Pan, Z., and Jin, Z.K., "Bilateral Political Relations, Institutional Risk of Host Country and China's Foreign Direct Investment," *Finance & Trade Economics*, no. 6, (2015): 85-97.  
 Duanmu, J-L., "State-Owned MNCs and Host Country Expropriation Risk: The Role of Home State Soft Power and Economic Gunboat Diplomacy," *Journal of International Business Studies*, (2014) 45 (8): 1044-1060.

<sup>9</sup> Zhang, J.H., and Jiang, J.G., "Research on the Impact of Bilateral Political Relations on China's Foreign Direct Investment," *World Economics and Politics*, no. 12 (2012): 133-155.

<sup>10</sup> Meng, X., and Dong, Y.D., "Social and Political Risks and Chinese Enterprises' Location Selection for Making Foreign Direct Investment," *Journal of International Trade*, no. 4 (2015): 106-115.

<sup>11</sup> Countries of "Four Good Relationship" refer to good neighbors, good friends, good partners and good brothers.

meanwhile, Pakistan also regards their friendship as its cornerstone of foreign policy and a national consensus as well. China-Pakistan bilateral political relations are unique, so Pakistan is undoubtedly the best and typical target for studying the interactions and relations of these three factors, namely Chinese FDI, the institutional risks of a host country and the bilateral political relations. Secondly, located rightly at the intersection of the Silk Road Economic Belt and the 21st Century Maritime Silk Road (其他地方都使用的是 the Belt and Road), Pakistan is one of the most important partners of China to promote BRI. With the rising strategic significance of Pakistan, the importance of Pakistan as China's investment destination also increases, since it is possible for both countries to cooperate in various spheres. Therefore, we must make in-depth interpretation of Pakistan's investment environment, potential risks and mitigation thereof. It is a requirement for increasing opportunities for bilateral economic cooperation in the new era and guaranteeing Chinese FDI there. It is also the important practical significance of this study. Finally, although countries along the Belt and Road vary from each other significantly, more than half of them have high institutional risks alike. As BRI is rapidly entering its implementation stage, this study on Chinese FDI in Pakistan can also provide valuable references for Chinese companies to better invest in other countries with high institutional risks along the Belt and Road and realize China's strategy of Going Global.

### 4.3 TYPES OF PAKISTAN'S INSTITUTIONAL RISKS AND THE RELATIONSHIP BETWEEN THE RISKS AND CHINESE FDI IN PAKISTAN

#### 4.3.1 *Major Institutional Risks Faced by FDI in Pakistan*

Located rightly at the intersection of the Silk Road Economic Belt and the 21st Century Maritime Silk Road (大多地方使用 the Belt and Road, 是否需要统一?), Pakistan boasts an ideal geological location of vital strategic importance. However, Pakistan is not a peaceful place due to various institutional risks, such as party struggles, religious conflicts and terrorist activities, which appear to be the main factors that hinder foreign investors from investing in Pakistan.

Firstly, Pakistan suffers from poor political stability due to historical, political and ethnic issues. Since Pakistan adopts federalism, there is serious imbalance existing in the functioning of Parliament because the economic

development and population distribution differ greatly among all the provinces. For instance, in regard to the distribution of seats in the National Assembly, the Punjab province dominated by the Punjabi people has 183 seats alone, accounting for more than half of the total seats; the Sindh province dominated by the Sindh people has 75 seats; and provinces of Khyber-Pashtun dominated by the Pashtuns and Baluchistans dominated by the Baluchis just have 43 seats and 17 seats respectively. The dominance of only one province and one ethnic group has even escalated the political conflicts among all provinces and ethnic groups. As a result, these provinces divided by ethics and geographical locations tend to lack the sense of identity as Pakistanis and the loyalty to Pakistan as a whole.<sup>12</sup> Some provinces, striving for greater provincial autonomy to increase their own influence on national police-making, are having more and more conflicts with the federal government and other provinces. Besides, there are numerous political parties in Pakistan. Major parties including the Pakistan Muslim League Nawaz (PML-N), Pakistan Muslim League Quaid-e-Azam (PML-Q), Pakistan People's Party (PPP) and Pakistan Tehrik-e-Insaf (PTI, Pakistan Movement for Justice) constantly struggle with one another. The opposition parties even purposely provoke political conflicts to oppose the ruling parties through unconventional means which even lead to bloodshed. With imperfect democratic and political systems, Pakistan's politics has been turbulent for a long time. As another important force, the military also plays a key role in Pakistan's political arena. When a popular government is in power, the military exerts its influence on policy-making in an indisputable way. And during domestic political crises, the military even acts as the final arbitrator with considerable political authority.<sup>13</sup> The military even took over the power and established a military government in Pakistan's history. Between the federal government and provinces, among different parties, governments and the military, complicated conflicts directly cause the political instability in Pakistan.

Secondly, religious fights in Pakistan are another influential factor that leads to high institutional risks. Pakistan has a huge population of nearly 190 million, 97 percent of which believe in Islam. As the two main sects

<sup>12</sup>Ye, H.L., "Identity and Nation Building: Another Perspective of Pakistan's Security Dilemma," *South Asia report 2012-2013* edited by Chen Lijun, Yunnan University Press, 2013.

<sup>13</sup>Du, B., "An analysis of the Origin of the Politicization of the Pakistani Army," *International Data Information*, no. 6 (2016): 1-7.

thereof, Sunni and Shia respectively account for about 85 percent and 15 percent of Muslims in Pakistan. Furthermore, there are still branches within Sunni and Shia. For instance, Sunni has Barelvis, Deobandis, Modernist and Ahl-e-Hadith, while Shia has Twelver Shiism and Isma'iliyya.<sup>14</sup> Different religious sects not only have different doctrines, laws, ceremonies and cultures, but also political demands and material rights. Therefore, religious fights in Pakistan are considerably fierce, characterized by Sunni extremists' expulsion against Shiites and other minority sects. The struggle between Sunni and Shia appears to be the most prominent one. Pakistan Taliban did publicly describe Shiites and some minority sects as the "enemies of Islam and ordinary people," and call on the Pakistani people to attack them in the name of "jihad" (holy war). According to the report on violence against religious groups in Pakistan released by the International Association for Religious Freedom in August 2014, from July 2013 to June 2014, there were 122 cases of violent terrorist attacks against minority religious groups in Pakistan, resulting in at least 430 deaths. Among them, 54 attacks were against Shiites, accounting for 44.26 percent, and the death toll reached 222, accounting for about 51.63 percent.<sup>15</sup>

Finally, terrorism is no doubt the biggest threat to Pakistan's national security. Terrorist attacks are not only committed by terrorists, but also by rebels and religious extremists (see Table 4.1). The national rebels represented by the Balochistan Liberation Army and terrorists organizations represented by Tehrik-e-Taliban Pakistan (TTP) have gradually grown into major terrorist forces since 2005. Later, they launched destructive terrorist attacks more frequently in Pakistan.<sup>16</sup> According to the statistics of the *Pakistan Security Report* issued by the Pak Institute for Peace Studies (PIPS), there were more than six thousand terrorist attacks in Pakistan, and the total number of deaths thereof exceeded twenty thousand in 2007–2009 along.<sup>17</sup> Although the Pakistani government and the

<sup>14</sup>Du, B., "An Analysis of Religious Conflicts in Pakistan," *International Data Information*, no. 7 (2013): 35–41.

<sup>15</sup>"Tackling Manifestations of Collective Religious Hatred," International Association for Religious Freedom, <https://iarf.net/the-rise-of-religious-intolerance-side-event-at-un-hrc-2014/>, login time: October 13, 2016.

<sup>16</sup>Zhang, X.D., "Changes in Pakistan's Domestic Politics since the New Century," *South East Asian and South Asian Studies*, no. 2 (2014): 22–30.

<sup>17</sup>"2008–2014 Pakistan Security Report," PAK Institute for Peace Studies (<http://san-pips.com/index.php?action=pages&cid=free>), August 17, 2015.

**Table 4.1** Major terrorist organizations in Pakistan and the demands thereof

<i>Category</i>	<i>Name</i>	<i>Demands</i>
Islamic terrorist organization	Sipah-e-Sahaba Pakistan (SSP) Lashkar-e-Jhangavi	To fight against other sects, especially Shiites, Ahmadis, and Barelwis. To firmly crack down Shiites and establish a pure Deobandis state.
Pakistani Taliban	Tehrik-e-Taliban Pakistan (TTP) Tehreek-e-Nafaz-e-Shariat-e-Mohammadi (TNSM) Bajaur Taliban Taliban in North Waziristan	To implement al-Shari'ah law in Pakistan; To crack down the central government and the military, and establish Taliban regime in Pakistan.
Afghan Taliban	Haqqani Network Quetta Shura Taliban (QST)	To fight against NATO and Afghan army and get actively involved in the Afghan political systems.
Anti-Indian terrorist organization	Hizb-ul-Mujahideen (HM) Lashkar-e-Taiba	To integrate Kashmir into Pakistan and promote Islamic culture in Kashmir. To incite Indian Muslims to launch a religious revolution in India; to establish a Muslim-dominated country around Pakistan; to support al Qaeda to launch a global jihad.
Ethnic separatist terrorist organization	Balochistan Liberation Army	To realize the independence of Balochistan and establish a great Balochistan kingdom.

*Source:* Yuan Sha, "Analysis of the Evolution, Characteristics and Impact of Domestic Terrorist Forces in Pakistan," *South Asian Studies Quarterly*, Issue. 2, 2016, 33–41

military have put more anti-terrorism efforts since 2010, and the United States has also increased the frequency of unmanned aerial vehicle (UAV) strikes, somewhat reducing the number of terrorist attacks, Pakistan still remains one of the countries that are most affected and seriously damaged by terrorist attacks.

FDI usually has the characteristics of large investment amount, long return period and close relations with the economic and social situations of the host country as well. Therefore, FDI is highly influenced by the risk level of the host country. As for Chinese FDI in Pakistan, political instability caused by partisan struggles, social instability caused by sectarian struggles and terrorist activities are enormous obstacles impeding Chinese investors. It's worth mentioning that Pakistan has three major institutional

risks for Chinese FDI. Among which, the institutional risk caused by partisan struggles is relatively minor, because in Pakistan, the ruling party, the opposition parties, the military or the tribal leaders are all on friendly terms with China, which indicates that Pakistan's foreign policy for China and its FDI will not change significantly with the change of Pakistan's domestic regimes. The negative spillover brought by sectarian struggles continues to expand, which not only intensifies the social division in Pakistan, but also disrupts its social and economic order. What's more, sectarian struggles are more frequently committed in terms of violence and terrorist attacks, increasing the threat to Chinese FDI in Pakistan. Featured by its suddenness, uncertainty and mass destruction, terrorism has always been one of the key factors that affect the security of FDI and personnel, as well as the confidence of investors.<sup>18</sup> The causes of terrorism in Pakistan are very complicated. Partisan struggles and sectarian struggles are usually intertwined with one another, stirring up widespread political and social conflicts nationwide. As a result, terrorism has become the major institutional risk for Chinese investors to decide whether to invest in Pakistan or not.

#### *4.3.2 The Non-linear Relationship between Pakistan's Institutional Risks and Chinese FDI in Pakistan*

As a major form of Pakistan's institutional risks, how will terrorism affect Chinese FDI in Pakistan? Considering the fact that the FDI flow appears more sensitive to the changes of institutional risks of the host country, this paper depicts the relationship between the flow of Chinese FDI in Pakistan and number of terrorist attacks in Pakistan from 2005 to 2014 as follows (see Fig. 4.1).

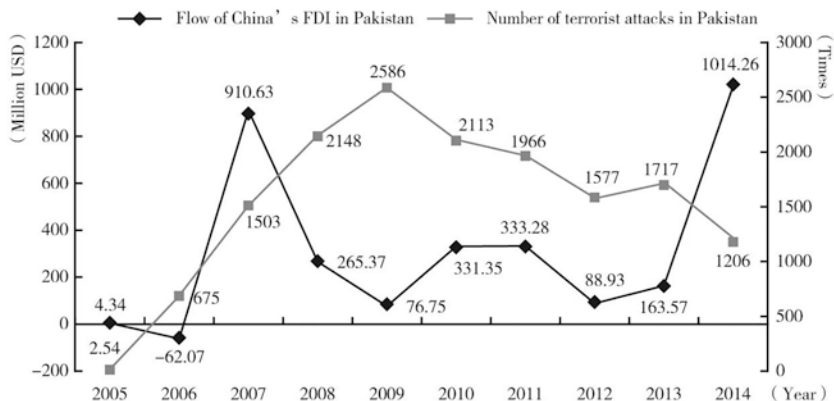
From Fig. 4.1 we can see the clear non-linear relationship between Chinese FDI in Pakistan and number of terrorist attacks in Pakistan. It can be divided into three phases according to the concrete changing trend.

##### 1. First phase: changing in the same direction (2005–2007)

The first phase was from 2005 to 2007, when the flow of Chinese FDI in Pakistan and the number of terrorist attacks in Pakistan were changing

<sup>18</sup>Ye, M.X., "On the Influence of International Terrorism on the World Economy," *Forum of World Economics and Politics*, no. 6 (2002): 64–67.





**Fig. 4.1** The flow of Chinese FDI in Pakistan and number of terrorist attacks in Pakistan from 2005 to 2014. (*Data source:* Statistical Bulletin of China's Outward Foreign Direct Investment and Pakistan Security Report)

clearly in the same direction. The number of terrorist attacks in Pakistan kept increasing from 2005 to 2007, and even doubled in 2007 on the basis of 2006. Meanwhile, Chinese FDI in Pakistan surged from US\$ -62.07 million to US\$ 910.63 million over the same period, increasing clearly together with the former. Under the background that both China-India and India-Pakistan diplomatic relations got much improved during this period, to promote bilateral economic development and geo-economic cooperation became the common desire of China and Pakistan in the twenty-first century. China-Pakistan Free Trade Agreement and China-Pakistan Five Year Development Programme were officially signed in November 2006, marking that the focus of China-Pakistan friendship has started to shift from political, diplomatic and security spheres to economic and trade cooperation. According to Chapter 9 of Free Trade Agreement, conveniences and protections should be provided for bilateral investors, and specifically points out that “if an investor of either side who invests within the territory of the other side has suffered a loss due to nationwide emergencies, uprisings, civil wars and riots or other similar events, the other side should be responsible for relevant restitution, compensation, indemnification or other countermeasures no less than treatment for investors of its own country or any third country.” This regulation has obviously increased the confidence and reduced potential risks of Chinese

investors to invest in Pakistan. At the same time, as one of the key projects of China-Pakistan Five-Year Program, Haier-Ruba Economic Zone was formally launched in November 2006, forming a new investment platform for Chinese enterprises. China Mobile acquired 88.88 percent of Pakistan telecommunication operator Paktel Ltd. for US\$460 million in January 2007, and later acquired the company entirely and spent hundreds of millions dollars to rebuild and expand the network facilities. In addition, a number of Chinese-invested companies were established in Pakistan, including Plum Qingqi Motorcycle Ltd., Haier and Ruba Group, SVA-Ruba Electronics, CMPak, Pak-China Joint Investment Company (PCJIC), etc. As of the end of 2007, the stock volume of Chinese FDI in Pakistan reached US\$1.095 billion.<sup>19</sup>

## 2. Second phase: changing in opposite directions (2008–2011)

The second phase was from 2008 to 2011, when the two factors went in opposite directions. The flow of Chinese FDI in Pakistan dropped dramatically in 2008 and 2009 because of the soaring terrorist attacks. To explain their relationship, we need to look back in 2007 when Pakistan's general election took place and political struggles intensified. The Red Mosque incident became a political watershed, providing a critical evidence for Pakistan's opposition parties and other religious groups to put pressure on the Pervez Musharraf government. Ayman al-Zawahri, the number two figure of Al-Qaeda, also incited Pakistani Muslims by video to retaliate violently against the government. Meanwhile, the judicial crisis caused by the fight between Musharraf and Iftikhar Muhammad Chaudhry, the Chief Justice of the Supreme Court, also appeared to be a tough problem. Although Musharraf got successfully re-elected with an overwhelming advantage in October 2007, the domestic crisis still remained unresolved. As domestic political situation grew more and more turbulent, he declared a state of emergency nationwide in November. The terrorist organization Tehreek-e-Taliban Pakistan (TTP) was established in December. As a result, the number of suicide bombings and terrorist attacks against the government and civilians increased rapidly. Furthermore,

<sup>19</sup>Economic and Commercial Office of the Embassy of the People's Republic of China in the Islamic Republic of Pakistan: China-Pakistan Economy and Trade, May 1, 2009, [www.mofcom.gov.cn/](http://www.mofcom.gov.cn/), <http://pk.mofcom.gov.cn/article/o/g/200905/20090506214883.shtml>.

Benazir Bhutto who served as Prime Minister of Pakistan was also assassinated, indicating the rapid development of domestic terrorist forces. In 2008, the new government of Yousuf Raza Gillani, jointly formed by Pakistan People's Party (PPP) and Pakistan Muslim League Nawaz (PML-N) didn't make things any better. Their political fight against Musharraf tended to be intensified, exacerbating domestic uncertainties. Musharraf was forced to resign from office in August 2008, PML-N also withdrew from the ruling coalition because of radical differences with PPP. The above-mentioned political events continued to bring negative impacts on Pakistan's anti-terrorist war and national security. Moreover, as Pakistan's security forces entered South Waziristan and the US also took drone strikes to fight the widespread extremism and terrorism, the security situation in Pakistan seriously deteriorated in 2008. According to *Pakistan Security Report 2008*, there were altogether 2148 terrorist attacks launched by terrorists, insurgents and sectarians across Pakistan in the year of 2008, up by 746 percent compared to 2005, causing 2267 deaths and 4558 injuries, higher than the total of the past three years. Furthermore, two Chinese engineers were kidnapped by Pakistan Taliban in August 2008, which severely destroyed the confidence of Chinese investors. Therefore, in 2008 and 2009, when the number of Pakistani terrorist attacks increased rapidly, the inflow of Chinese FDI in Pakistan slumped from US\$910 million to US\$77 million. This indicated that the inflow of Chinese FDI was largely impeded by the institutional risk in terms of terrorism when Pakistan suffered serious political instability.

### 3. Third phase: changing in the same direction (2012–2014)

The third phase was from 2012 to 2014. First of all, as the terrorist attacks decreased in 2012, Chinese FDI in Pakistan also decreased to a large extent. The reason for this might be that Chinese investors preferred to avoid risks rising from the deteriorating domestic security in Pakistan during its election in 2013. FDI from Germany, Saudi Arabia, and the United Arab Emirates also decreased likewise during the same period. According to the data from the National Bank of Pakistan, in the first five months of the 2012–2013 fiscal year (July–November 2012), Pakistan's net foreign investment decreased by 27.1 percent over the same period

last year.<sup>20</sup> Secondly, when the number of terrorist attacks bounced up in 2013, Chinese FDI in Pakistan increased significantly. 2013 was the election year of Pakistan and the overall security of the country got considerably worse. As the biggest terrorist force in Pakistan, Tehrik-e-Taliban Pakistan (TTP) made 645 attacks over fifty regions nationwide in 2013, resulting in the deaths of 732 civilians and 425 security soldiers. Especially in March and April before the general election, TTP launched 117 attacks against political leaders, government officials and other election-related targets, bringing serious impact on the campaigns of moderate secular parties.<sup>21</sup> The increasing terrorist attacks aroused complaints from all circles of society. The strong desire for a political change and economic growth of the Pakistani people spurred PML-N's victory in both national and provincial elections. PML-N had won 181 seats, more than half of the National Assembly, allowing them to form an independent cabinet. Its chairman, Nawaz Sharif, became the 27th Prime Minister of Pakistan, and the popular government had achieved a peaceful transfer of power for the first time in Pakistan. By allying with the Pakistan Muslim League Functional (PML-F), Awami National Party and other parties, its total seats in the National Assembly accumulated to 192, further consolidating its central ruling position. In the Punjab provincial assembly, PML-N won 294 of the 345 seats; and in Balochistan, it ruled together with other local parties, reinforcing its strength in local provinces. Under the strong leadership of PML-N, economic revitalization became the top priority of the new government. Sharif put forward the slogan of the Dream of Asian Tiger, and formulated an all-round revitalization plan, for instance, resolving the energy crisis, further developing the market economy, and increasing expenditures in infrastructure construction projects, especially railways, highways, hydroelectric stations and power grids, etc.<sup>22</sup> Sharif's economic development demands were highly compatible with China's development strategy to build new channels and strengthen China-Pakistan connectivity. In 2013, the Prime Ministers of both countries reached a consensus

<sup>20</sup> Pakistan's Foreign Direct Investment in the First Five Months of This Fiscal Year Decreased by 27.1 percent, [www.mofcom.gov.cn/](http://www.mofcom.gov.cn/), <http://pk.mofcom.gov.cn/article/jmwx/201212/20121208493638.shtml>.

<sup>21</sup> *Date source: Pakistan Security Report 2013.*

<sup>22</sup> Li, Q.Y., "The Reorganization of Pakistan's Political Party Territory and Its Influence," *Contemporary World*, no. 2 (2014): 67-69.

and agreement on the construction of CPEC, which further enhanced Pakistan's position in China's geo-economy. In the context of continuously deepening China-Pakistan bilateral relations, more and more practical economic cooperation agreements had been signed, and Chinese FDI in Pakistan kept increasing steadily, although the security situation in Pakistan still remained turbulent after the Sharif government assumed office. The domestic situation got even worse after Hakeemullah Mehsud, the leader of TTP, was killed by a US drone in November 2013.

Besides, the relationship between two factors showed new highlights in 2014. After Hakeemullah Mehsud was killed, TTP began to split from the inside. Moreover, Pakistani military launched the Prophet's Sword, a large-scale armed operation to clear illegal militants of Pakistan Taliban in North Waziristan, dramatically reducing the terrorist activities in Pakistan in 2014. At the same time, CPEC also sped up. For example, China Metallurgical Group and the Punjab government signed an agreement on exploring the Chiniot iron ore; China Mobile's Pakistani branch CMPak gained 3G and 4G licenses through bidding; China Harbour Engineering Company (CHEC) signed a US\$130 million construction contract of the Qasim Port in Karachi, Pakistan. All these new projects pushed Chinese FDI in Pakistan to a historical high of US\$1.014 billion, making China the largest source country of foreign investment.

It can be concluded that the relationship between Chinese FDI in Pakistan and Pakistan's institutional risks was non-linear: when the political instability appeared in Pakistan, especially during the election years, the institutional risks in terms of terrorism rose sharply and impeded Chinese investors significantly; and during the relatively stable ruling period, Chinese FDI showed a pretty high tolerance for Pakistan's institutional risks; as bilateral relations further deepened, Chinese FDI increased greatly in Pakistan, despite of the rising institutional risks of terrorism. As shown in Fig. 4.2, from 2005 to 2014, Chinese FDI increased by three times after the focus of China-Pakistan bilateral relations shifted and expanded from geopolitics to geo-economic cooperation. Furthermore, as time went by and Chinese FDI in Pakistan gradually accumulated, friendly political relations became more and more influential. Hence, when examining the impact of Pakistan's institutional risks on Chinese FDI, we must take the friendship as a key factor into account.

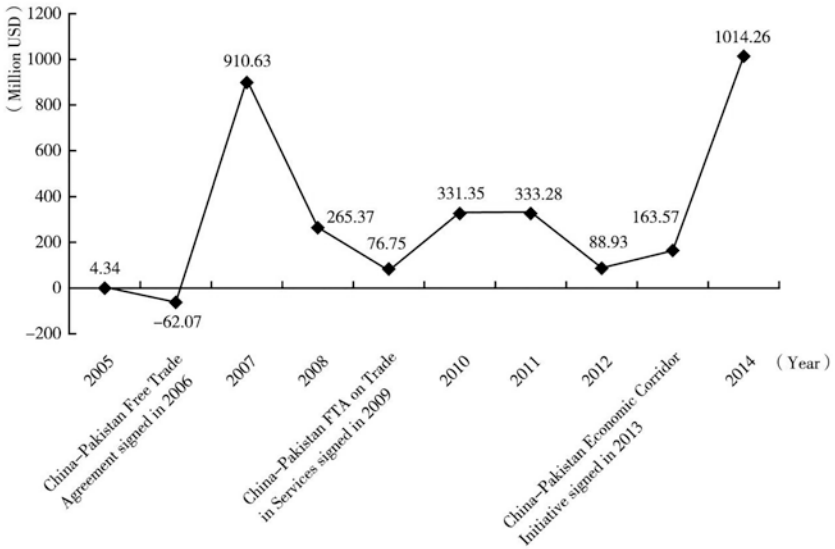


Fig. 4.2 Relationship between the important documents of China-Pakistan bilateral relations and Chinese FDI in Pakistan from 2005 to 2014

#### 4.4 THE EVOLUTION OF CHINA-PAKISTAN POLITICAL RELATIONS AND THE RISK-MITIGATING ROLE THEREOF

Ever since China and Pakistan formally established diplomatic relations in 1951, the two countries have formed friendly bilateral relations on the basis of deep mutual trust, the two sides paid high-level visits, signed agreements, issued joint statements and established strategic partnership. Under the changing international and domestic environment, the focus of bilateral cooperation also shifted from geopolitical spheres to geo-economic spheres, forming multi-dimensional cooperation channels, which played significant role in mitigating risks for Chinese FDI in Pakistan.

##### 4.4.1 *Bilateral Friendly Relations Shifting from Geopolitics to Geo-economics in an All-round Way*

China and Pakistan formally established diplomatic relations on May 21, 1951. Pakistan was the first Islamic country to do so. However, during the

initial period from 1951 to 1960, the two countries kept neither near nor far relations in a polite manner because of their different ideologies and arrangements. In the early 1960s, with the deteriorating China-India relations, the United States began to support India and alienate Pakistan in South Asia, which got strongly complained by Pakistan. Both China and Pakistan needed to stand up to the United States and beware of India, hence China-Pakistan political relations began to heat up. From the 1970s to the 1990s, leaders of both countries paid frequent visits on state affairs, gradually forming a stable all-weather friendship based on deep mutual trust and friendship.<sup>23</sup> However, throughout the second half of the twentieth century, the bilateral cooperation were mainly focused on political and security spheres due to the Cold War, and China's bilateral relations with countries including Pakistan, the United States, the Soviet Union and India. Meanwhile, the economic cooperation was not emphasized, so China-Pakistan political relations witnessed booms in political and military cooperation but stagnation in economic and trade cooperation.<sup>24</sup> Even in 1999, the bilateral import and export trade volume was merely US\$971 million, accounting for 0.27 percent of China's total trade volume; and China's contracted projects in Pakistan mounted to US\$306 million, accounting for 3.59 percent of China's total contracted amount.<sup>25</sup>

With the continuously improving international environment in the twenty-first century, China-Pakistan bilateral relations gradually shifted towards economic spheres. Besides, after officially joining the World Trade Organization (WTO) in 2001, China paid more attention to the development of bilateral and multilateral relations in economic and trade spheres. Among all neighboring countries of China, China's economic relations with Pakistan lacked relatively behind, as their bilateral diplomatic relations got improved notably, the gap grew even bigger. The total bilateral trade volume between China and India reached US\$2.914 billion by 2000, almost 2.5 times as much as that of China and Pakistan. The big gap became an important impetus pushing China-Pakistan bilateral political relations to shift to economic and trade spheres. In 2001, in response to Pakistan's request for aid, two countries met in Beijing and signed a

<sup>23</sup> Han, X.Q., "On the Evolution of China-Pakistan Relations from 1951 to 1965: From Neither Near nor far to De Facto Alliance," *Jiangsu Social Sciences*, no. 5 (2015): 137–146.

<sup>24</sup> Du, B., "All-weather Friendship and China-Pakistan Relations," *International Data Information*, no. 9 (2013): 27–32.

<sup>25</sup> The data of trade and project contracting in this paper are sourced from China Statistical Yearbook. Data on Chinese direct investment in Pakistan during this period are not available.

financing agreement for phase I of Gwadar Port project, and formally launched the joint construction the following year. During Pakistani President Musharraf's visit to China in 2003, leaders of the two countries issued the *Joint Declaration on the Development Direction of Bilateral Cooperation*, to further strengthen bilateral relations by deepening the all-weather friendship and all-round partnership. The declaration specifically pointed out that the two sides should guide economic cooperation and expanded bilateral trade and investment. During Premier Wen Jiabao's visit to Pakistan in April 2005, the two sides signed the *Treaty of Friendship, Cooperation and Good-Neighborly Relations between the People's Republic of China and the Islamic Republic of Pakistan*, announcing that China and Pakistan would further develop closer strategic partnership and start the negotiations on *China-Pakistan Free Trade Agreement*. A series of bilateral documents were signed later, including *China-Pakistan Free Trade Agreement in 2006*, *Agreement on Trade in Service of the China-Pakistan FTA in 2009*, and *Banking Business Service Protocol of the Agreement on Trade in Service of the China-Pakistan FTA in 2015*. In May 2013, Premier Li Keqiang proposed CPEC during his visit to Pakistan, aiming to push China-Pakistan economic cooperation to a new level by enhancing connectivity of both countries in transportation, energy and marine spheres. BRI was proposed and implemented after that, enhancing the significance of Pakistan and CPEC to a strategic height, and the bilateral political relations was officially upgraded to all-weather strategic partnership during President Xi Jinping's visit to Pakistan in 2015. During this period, the political relations got supported by both political and economic cooperation. On the one hand, from the geo-economic perspective, the political and social exchanges between parties, governments and all sectors were increasing greatly, laying a solid foundation of political and social mutual trust, which led to more trade and investment activities; on the other hand, from the geopolitical perspective, the deepening and expanding of political and military cooperation also required closer economic and trade relations. According to the National Bureau of Statistics of China, the bilateral trade volume reached US\$15.999 billion in 2014, an increase by 15.48 times compared to 1999; the stock of Chinese FDI in Pakistan maintained a rapid growth, too, up by nearly a hundred times during the decade from 2004 to 2014. The annual compound growth rate was 59.08 percent, much higher than the growth rate of China's total FDI over the same period (34.73 percent).



#### 4.4.2 *The Role of Friendly Political Relations in Mitigating Risks for Chinese FDI in Pakistan*

While China-Pakistan political relations kept deepening, with its focus shifting from geopolitical to geo-economic cooperation, on the one hand, the traditional friendship offered a solid foundation and guarantee for bilateral geo-economic cooperation, and fully exerted its positive marginal effect from the geopolitical perspective, so to speak the benefits brought by bilateral economic and trade relations increased as geopolitical relations went closer.<sup>26</sup> On the other hand, the internal interests of both countries were consistent from the geopolitical perspective, but different from the geo-economic perspective, thus forming multi-layer game relations.<sup>27</sup> To achieve the geopolitical and geo-economic goals, governmental departments should make overall arrangement of interests to fully exert enterprises' capacities. Currently, a series of economic and trade agreements have been signed, with the increasingly deepening China-Pakistan political relations, which provide official basis and guarantee for bilateral investment and trade. From non-governmental point of view, friendly political relations mean that Chinese FDI is highly accepted by Pakistan and greatly supported by China, and both sides enjoy high-level strategic connection, project arrangement and coordination. More importantly, as BRI and CPEC are proposed and implemented, the importance of strengthening bilateral economic cooperation has risen to a higher level. Therefore, it is a practical option to reduce risks faced by Chinese FDI in Pakistan by providing policies, funds and personnel, etc. We will discuss this from the following three aspects: China, Pakistan, and cooperation among local governments.

1. The home country (China): to guide investors, formulate policies and prevent risks.

As the home country of investors, China's central government has taken multiple measures to guide investors, provide supportive policies and prevent risks so as to enhance investors' capacity to control potential risks. In order to better analyze China's support measures for FDI in

<sup>26</sup> Yin, Z.H., "Geopolitics and International Regional Economic Cooperation," *Journal of Socialist Theory Guide*, no. 7 (2011): 105–107.

<sup>27</sup> Huang, R.W., "Evolution of Geo-theory and China's Path of Peaceful Development," *Contemporary International Relations*, no. S1 (2010): 18–25.

Pakistan, this paper collects 153 non-financial investment records approved and archived by the Chinese government from January 1st, 2004 to June 15th, 2015 on the website of the Ministry of Commerce of PRC (see Table 4.2). These investment activities reflect the intentional guidance and supportive policies by the Chinese government to a certain extent.

Firstly, state-owned companies play a leading role in investing in Pakistan. As the implementer of the Chinese strategies, state-owned companies with strong financial strength and solid risk control ability are the most important investors. As shown in Table 4.2, among 153 investment records in Pakistan, fifty-two were state-owned companies (solely state-owned or state-holding companies) and nine joint stock ones transformed from state-owned companies, and the proportion of state-owned companies or multinational corporations with state-owned background<sup>28</sup> was 39.87 percent, indicating that China guides and encourages state-owned companies to invest in Pakistan, setting an example for private companies.

Secondly, China makes policies to guide FDI in Pakistan. In 2004, the Ministry of Commerce and the Ministry of Foreign Affairs jointly issued the *Guiding Directory in Country and Industry for China's FDI*, guiding Chinese investors to select countries and industries to invest. As a good friend of China, Pakistan is a key destination of Chinese FDI. As for industries, it is strongly recommended to invest in Pakistani industries such as machinery manufacturing, electronic communication equipment manufacturing, textiles and garments, construction, power generation and supply. Since 2009, Chinese Academy of International Trade and Economic Cooperation (CAITEC), Investment Promotion Agency of the Ministry of Commerce and overseas economic and commercial organizations began to jointly issue the annual report of *Regional Guidance for China's FDI (Pakistan)*, which explains the policy environment, featured industries and potential risks to the Chinese investors, and provides macro guidance and services for them to invest in Pakistan. The policy guidance helps Chinese investors choose optimal industries to invest and prevents them from blind investment, it helps them to get to know more about Pakistan, and reduces risks by making rational choices. In Table 4.2, industries like

<sup>28</sup>The joint-stock enterprises converted from state-owned enterprises often retain some links with the government and enjoy more government support than other joint-stock enterprises, so they are more active in responding to national policies and strategies.



commercial service,<sup>29</sup> manufacturing, power, construction and mining rank in the top<sup>30</sup> among 153 records, just as recommended mostly by the Chinese government.

Thirdly, China ensures financial supports and insurance services for state-owned banks and financial institutions investing in Pakistan. China Development Bank established an Energy Project Leadership Group for CEPC, providing favorable policies and green channels for CPEC. By the end of March 2015, China Development Bank has financed ten projects in Pakistan, with a reviewed investment of US\$1.3 billion and a cumulative payment of US\$950 million. Besides, Industrial and Commercial Bank of China also entered agreements with a total amount of US\$4.3 billion for projects including Suki Kinari Hydroelectric Project, Dawood Wind Power Project, Sahiwal Coal-fired Power Project and Thar Block-I Project.<sup>31</sup> The involvement of Chinese state-owned banks effectively reduced the serious financial constraints faced by Chinese investors to invest in Pakistan. At the same time, as one of the major countermeasures taken by the Chinese government to spur FDI in Pakistan, Chinese insurance companies are also mitigating investment risks. For example, China Export & Credit Insurance Corporation (SINOSURE), a policy insurer, provided overseas insurance service to compensate investors for economic losses caused by foreign exchange restrictions, expropriation, war, political riots, and default risks in the host country. SINOSURE's underwrote approximately US\$95.8 billion for export, investment and contract projects along the Belt and Road in 2014.<sup>32</sup> In April 2015, SINOSURE signed a framework agreement with Pakistan's hydropower department to provide political and commercial insurance services for Chinese hydropower

<sup>29</sup> According to the industry of the parent company and the investment scope disclosed in the data, this paper roughly classifies the industries of China's FDI in Pakistan. Among them, the representative offices set up in Pakistan with the aim of getting familiar with the market, promoting enterprises and providing after-sales service are classified into the category of business service industry.

<sup>30</sup> In Table 4.2, the ranking of investment industries is made based on the number of investments. If the amount of fund invested in each industry can be obtained, the ranking order may change accordingly, which may be especially true for the communications industry.

<sup>31</sup> Du, J., and Yang, Y., "Chinese Financial Institutions Actively Participate in the Construction of China-Pakistan Economic Corridor," *Financial News* (April 2015), [http://www.financialnews.com.cn/yw/jryw/201504/t20150422\\_74961.html](http://www.financialnews.com.cn/yw/jryw/201504/t20150422_74961.html).

<sup>32</sup> SINOSURE's Export Credit Insurance Coverage Continued to Expand in the First Quarter, [www.ce.cn](http://www.ce.cn), <http://district.ce.cn/zg/201505/25/t201505255456463.shtml>, May 25, 2015.

and energy companies investing in Pakistan. The above-mentioned measures of the Chinese government not only stimulated the enthusiasm of Chinese investors to invest in Pakistan, but also strengthened their tolerance to terrorism and other institutional risks in Pakistan to a certain extent.

2. The host country (Pakistan): to make efforts in fighting terrorism, providing multiple protections and rapid emergency supports.

As the host country for Chinese investors, Pakistan is making political and military efforts in anti-terrorism war across the country. It protects Chinese FDI by various means, such as improving emergency support capacity to lower the probability and destructiveness of related risks.

Firstly, the Pakistani government and the military are fighting terrorism together. After the Sharif government failed to make any achievements by negotiating with Pakistan Taliban, the Pakistani military launched the Prophet's Sword, a large-scale armed operation, to suppress the illegal force of Pakistan Taliban in North Waziristan in June 2014. Pakistan Taliban attacked back for revenge at the Peshawar Military School in December 2014, making the Pakistani government and the military more determined to give terrorists heavier punishments such as death sentence.<sup>33</sup> In addition, Pakistan and Afghanistan are fighting those terrorists who constantly make troubles along the border, forming a strong deterrent to terrorists within and beyond Pakistan. By June 2016, the Pakistani military had cleared illegal militants, 992 fortified points, 253 tons of explosives and a number of rockets in over 3600 km<sup>2</sup> of the North Waziristan region in the Prophet's Sword operation, and closed 7500 bomb production sites in the Shawal Valley.<sup>34</sup> As a result, domestic terrorist attacks were reduced significantly, effectively protecting all the FDI in Pakistan.

Secondly, Pakistan strengthens the protection of security of Chinese FDI and its personnel in Pakistan. According to the National Counter Terrorism Authority (NACTA), by September 2014, there were 8956 Chinese citizens working in Pakistan, receiving protection by 12,596

<sup>33</sup> Li, W., "Pakistan to Step up Counter-terrorism Efforts," *World Affairs* 1 (2015): 30–31.

<sup>34</sup> Pakistan Waves Sword against Terrorism, [www.xinhuanet.com](http://www.xinhuanet.com), [http://news.xinhuanet.com/mil/2016-06/16/c\\_129068622.htm](http://news.xinhuanet.com/mil/2016-06/16/c_129068622.htm), June 16, 2016.

Pakistani security personnel.<sup>35</sup> For some projects, Pakistan even dispatched special forces to protect the security of Chinese FDI and personnel. Taking Dongfang Electric Corporation (DEC)'s Nandipur Power Plant as an example. The project was carried out in a densely populated area in Punjab where the potential security risks were relatively high. In order to protect Chinese engineers and other staff, Pakistani security department collected and investigated background information of 5000 households living nearby, to prevent possible terrorist attacks. Besides, a large number of police forces and senior officers were deployed around the power plant to patrol and guarantee the smooth implementation of the project.<sup>36</sup> On May 31st, 2014, the first unit of Nandipur Power Plant was connected to the grid for power generation, and all units were completed by the end of 2014, bringing about a win-win result. The success of the project instantly set a good example to attract more FDI in Pakistan by other Chinese investors. DEC officially established an office in Pakistan in September 2014 to make marketing and FDI in Pakistan and surrounding countries; in 2015, DEC Steam turbine Co., Ltd, Dongfang Electric Machinery Co., Ltd. and Shandong Electric Power Construction Corporation (SEPCO) together signed the equipment contract for 2 × 660MW emergency coal-fired power stations at Qasim Port in Pakistan. It was the first CPEC project that had been officially launched.<sup>37</sup>

Thirdly, the Pakistani government also protects Chinese FDI by its rapid emergency response and continuous efforts to minimize the losses. In October 2004, two Chinese engineers from Sinohydro No 13 Bureau, which built Pakistan's Gomal Zam Dam project, were kidnapped on their way to the construction site. Pakistan's then President Musharraf and Foreign Minister Kasuri expressed their concern at once. The Interior Minister Sherpao was in charge of the rescue and negotiation with the kidnappers. Pakistan gathered hundreds of local tribal elders there to urge the kidnappers to release the engineers as soon as possible. When the

<sup>35</sup> Chinese Nationals: Senate Body Seeks Briefing over Security, September 26, 2014, Tribune, <http://tribune.com.pk/story/767415/chinese-nationals-senate-body-seeks-briefing-over-security/>.

<sup>36</sup> Security of Chinese Engineers: Information about Nandipur Dwellers Being Gathered. August 5, 2014, <http://www.dawn.com/news/1123417>.

<sup>37</sup> Dongfang Electric Corporation and Shangdong No. 3 Power Construction Co., Ltd. Signed 2×660MW Coal-fired Power Plant Projects at Qasim Port, Pakistan, Dongfang Electric Corporation, <http://www.dongfang.com/data/v/201505/4623.html>, May 22, 2015.

kidnappers rejected all the peaceful solutions, Pakistan was forced to rescue the hostages by military actions. Although the result was not that satisfying, but all the rescue efforts, aftermath measures and desire of Pakistan to improve security protection were unprecedented in comparison with all the consular rescue cases that ever happened.<sup>38</sup> After this event, Pakistan further strengthened protection for Chinese FDI and personnel, and greatly reduced the loss of Chinese investors.<sup>39</sup>

### 3. Cooperation between local governments: to deepen friendship and increase mutual understanding

The local governments in both countries cooperate with each other more closely, making local people better understand Chinese FDI in Pakistan and to promote sustainable development of multi-level cooperations. Since the local governments in Pakistan enjoy greater authority to make decisions on internal affairs, supports from local governments are required to implement projects. Strengthening cooperation between local governments is as important as reducing risks of FDI in Pakistan. So far, cooperations between local governments are mainly carried out in terms of mutual visits and friendship cities or provinces. As of April 2016, three provinces and eight cities in China had been paired with friendship counterparts in Pakistan.<sup>40</sup> After CPEC and BRI were proposed, another three pairs of friendship cities emerged in both countries.<sup>41</sup> More and more communication channels for economic and cultural exchanges were established, enhancing the friendship, mutual trust and understanding between the local governments and people. Besides, it is also conducive to the promotion of economic cooperation, images and influences for both sides. For example, after Zhuhai City and Gwadar City paired as friendship

<sup>38</sup> Fan, C., "On the Security and Protection of Chinese Citizens in Pakistan," Master's thesis, China Foreign Affairs University, 2008.

<sup>39</sup> A Chinese engineer was murdered in 2004, and similar incidents didn't happen again thereafter. In August 2008, two engineers of the Chinese ZET Corporation got kidnapped in Pakistan. It took nearly half a year for the two engineers (one managed to escape successfully) to be brought back to safety thanks to the rescue efforts of the Pakistani government and the military.

<sup>40</sup> *Data source:* China International Friendship Cities Association, <http://www.cifca.org.cn/Web/SearchByZhou.aspx?guojia=%b0%cd%bb%f9%cb%b9%cc%b9>, login time: June 25, 2016.

<sup>41</sup> The three new pairs of China-Pakistan friendship cities are Chengdu and Lahore, Karamay and Gwadar, Zhuhai and Gwadar.

cities, Zhuhai Port and Gwadar Port also became friendship ports with the priority to cooperate with each other. On October 28, 2015, Zhuhai Port and China Overseas Port Holdings Co., Ltd. signed a strategic agreement worth of ¥6.5 billion to jointly develop Gwadar Port, laying a foundation for subsequent large-scale FDI. As shown in Table 4.2, among 153 FDI projects in Pakistan from January 1, 2004 to June 15, 2015, Chinese parent companies thereof are mainly concentrated in Zhejiang province, Shandong province, Beijing, Shanghai, Guangdong province and Sichuan province. Five provinces out of the top ten have been paired with friendship provinces (or cities) in Pakistan. To a certain extent, this indicates that friendly political relations of local cities are equally important for enhancing development potentials and stability of Chinese FDI in Pakistan.

Therefore, it can be concluded that China's choices to directly invest in Pakistan despite of the high institutional is greatly influenced by friendly political relations. The long-term friendship and mutual trust are reflected in policy adjustment based on mutual interests, and in cooperation and exchanges between central and local governments, mitigating risks for Chinese FDI and ensuring a greater prospect in Pakistan. Chinese FDI in Pakistan has grown rapidly since 2003. The number of Chinese-invested projects in Pakistan increased from only one in 2004 to ten in 2007, then to nineteen in 2013 and forty-three in 2014 (see Table 4.2). In 2014, Chinese FDI in Pakistan surpassed developed countries including the United States, Britain, Switzerland and Japan, and became the largest FDI source country. It proves that friendly political relations have mitigated investment risks effectively to a certain extent. It also indicates that good political relations are much more valuable when a host country has high institutional risks, because while foreign investors are discouraged to invest in there, those from a country that has good political relations with the host country may gain even bigger development opportunities there.

#### 4.5 MAIN CHALLENGES AND DEVELOPMENT PROSPECTS

From the perspective of bilateral political relations, Pakistan's institutional risks in terms of terrorism are generally high, but friendly political relations between China and Pakistan can, to a certain extent, play a role in mitigating practical risks by various means, and as an important factor, encourage Chinese FDI in Pakistan. It should be noted that the risk-mitigating function of friendly relations are not sufficient to prevent all kinds of risks, therefore, Chinese FDI in Pakistan still faces lots of challenges.



#### 4.5.1 *Challenges Faced by Chinese FDI in Pakistan*

First of all, the institutional risks of Pakistan should not be underestimated. Pakistan's political situation still remains complicated due to intertwined terrorism, nationalism, religious conflicts and political and social problems, and is easily affected by external factors such as Afghanistan and India. None of these issues can be resolved in the short term. Although terrorist forces are currently under control in Pakistan, they will still exist in the long run. Moreover, partisan struggles are fierce in Pakistan. While implementing CPEC, differences of opinion of the opposition parties and the ruling party have slowed down the process dramatically, because no agreement can be reached on which provinces the corridor is going to pass through. Besides, the competition between the government and the military over the leadership of the security forces for CPEC has halted some of the CPEC projects. These risks are not likely to be resolved in the short term by traditional means of political negotiation, so their threats to Chinese FDI should not be underestimated.

Secondly, attacks on Chinese FDI and personnel tend to increase. The all-weather strategic partnership provides conveniences for Chinese FDI in Pakistan, especially for the implementation of CPEC, but it also becomes the reason for terrorist organizations and separatist forces to attack Chinese FDI and personnel on purpose. As the the Pakistani government and the military are making more efforts in fighting terrorism, in order to draw attention and gain bargaining chips for political negotiation with the government, some armed forces start to attack Chinese FDI and personnel for revenge, hoping to harm the friendship between China and Pakistan and impede CPEC as well. The number of this kind of attacks increases sharply as Chinese FDI grow larger and larger in Pakistan.

Thirdly, there are still gaps in understanding of CPEC among all circles in Pakistan. As the flagship project of BRI, CPEC is also seen as a fate changer in Pakistan. The economic and strategic significance thereof is highly recognized by both countries. However, ordinary Pakistani people and mainstream media are still having doubts about CPEC. Instigated by the opposition parties and ethnic minorities, some ordinary people tend to believe that CPEC might leave Pakistan heavily indebted, domestic enterprises might be hit hard, and even the political intentions of Pakistan might be controlled by China, so they've organized several small-scale parades to protest against it.<sup>42</sup> The gaps in understanding of CPEC by the

<sup>42</sup>Why do some Pakistanis oppose CPEC, [Sohu.com](http://mt.sohu.com/20160510/n448621277.shtml), <http://mt.sohu.com/20160510/n448621277.shtml> (May 2016).

Pakistani society are likely to evolve into more anti-China movements in the future. And this is also the major challenge that Chinese FDI in Pakistan might encounter in the future.

#### 4.5.2 *Policies and Prospects*

In the face of these serious challenges, the protection of security and interests of China's FDI has become increasingly vital. In order to provide policies to protect and support CPEC and Chinese FDI along the Belt and Road, especially in countries with high institutional risks, the current risk-mitigating mechanism should be further strengthened and multi-level communication and exchange channels should be established on the basis of strengthening bilateral policy communication and intergovernmental cooperation.

First, China and Pakistan should strengthen anti-terrorism cooperation. From both geopolitical and geo-economic reasons, the bilateral friendship and cooperation should be further deepened in areas of anti-terrorism, information sharing, joint counter-strike military exercises and other non-traditional spheres between China and Pakistan. The stability of political environment in Pakistan and the security of Chinese FDI and personnel should be well protected to brace for negative impacts of the high institutional risks of Pakistan.

Second, more risk-mitigating methods should be developed by multiple diplomatic means. As the main bodies and carriers of Chinese FDI in Pakistan are diversified and the sources of institutional risks are complicated, China could hardly deal with the high institutional risks faced by FDI if it continued to depend on the single means of government diplomacy. This requires more political cooperation channels. China should exert its advantage in governmental diplomacy in terms of conference diplomacy, party diplomacy (especially with the opposition parties), public diplomacy and non-governmental diplomacy, according to the political characteristics of Pakistan, developing a multiple diplomatic risk-mitigating mechanism.

Third, the risk-mitigating mechanism with multiple parties involved should be improved. With the increase of Chinese FDI in Pakistan, exchanges of enterprises, organizations, media and ordinary workers between the two countries also tend to be more frequent. Under this background, the overseas interests should not only be protected by the Chinese government, but also actively and voluntarily protected by

non-governmental forces, for instance, Chinese multinational companies, organizations, social media and overseas citizens in Pakistan. China should encourage Chinese enterprises and individuals to assimilate into the local society. While implementing infrastructure construction, they should also invest in local people's livelihood and education so as to bring more benefits to them. Meanwhile, China should publicize through media, non-profit organizations and other agencies to dispel misgivings and misunderstandings about Chinese FDI by the ordinary Pakistani people, thus enhancing the mutual understanding and trust between both countries.

This study bears particular significance for Chinese FDI in countries with high institutional risks along the Belt and Road. First, China should strengthen bilateral communications on policies and intergovernmental cooperation, and promote political mutual trust by building multi-level bilateral communication channels before making large-scale FDI; second, multi-dimensional friendship should not only be developed between China and the ruling party of the host country, but also through bilateral cooperation with its major governmental organizations and widely-recognized non-government organizations in political, economic, diplomatic and anti-terrorism spheres to protect Chinese FDI; third, Chinese enterprises to make FDI should not only make good use of bilateral political relations, but also be aware of security matters and behavior norms, enhance risk control capacities and improve the tolerance for institutional risks of the host country, thus continuously promoting the healthy and sustainable development of Chinese FDI in host countries with high institutional risks.



# Fiscal System and the Development of Baloch Nationalist Movement: On the Influence of China-Pakistan Economic Corridor

*Yuhang Xie*

## 5.1 GWADAR PORT AND BALOCHISTAN SEPARATISM

CPEC is the flagship project of China's Belt and Road Initiative (BRI), with its southern end at the Gwadar Port in Balochistan province. As the key junction to the Indian Ocean, it bears unique strategic and economic significance to both China and Pakistan.

For Pakistan, Gwadar Port is the third largest deep-water port, after Karachi and Qassim Ports. Compared to the latter two, Gwadar Port is far

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away from India, providing reliable guarantee for the national security of Pakistan. What's equally important is the construction of industrial zones, free trade zones and special economic zones around Gwadar, making it an important growth pole for Pakistan by creating more employment opportunities and promoting local economic development.

For China, Gwadar Port plays an important role in ensuring China's energy security, boosting economic growth in the western region, and strengthening China's overseas influence.<sup>1</sup> So far, more than 50 percent of China's crude oil consumption is dependent on imports, 75 percent of which needs to be transported back to China via the Strait of Malacca.<sup>2</sup> Once the Gwadar Port and the on-land energy channel which connects Gwadar Port and China's Xinjiang province are completed, it will not only lessen the transportation time and costs greatly, but also solve the Malacca dilemma, and guarantee China's energy security. Besides, because of Gwadar Port and CPEC projects, Xinjiang will become a transit hub which connects the Indian Ocean and China's mainland. This is conducive to stimulating investment and trade in the western region, and turning the region into an inland center of open economy. This will contribute to the economic rise of the western region. Finally, China's actual operation of Gwadar Port will increase China's influence in the Indian Ocean region and bring more benefits for China's future development.

However, Gwadar Ports is located in Balochistan where nationalist movement is thriving. Local separatists have taken various actions to fight for their independence, posing a major threat to CPEC. In order to achieve their independent political goals, they used bomb blasts and launched armed attacks<sup>3</sup> to various energy infrastructures and non-Baloch

<sup>1</sup> Liu Xinhua, "Field of Force, Gwadar Port and China's Interests in the West Indian Ocean," *Forum of World Economics & Politics*, No. 5 (2013): 1-18.

<sup>2</sup> "China's Oil Supply Fortress: The Malacca Dilemma," <http://www.wusuobuneng.cn/archives/20284>.

<sup>3</sup> It should be noted that not all the armed attacks in Balochistan are organized by the local separatist groups. According to researches by Pipes, Islamist terrorist organizations such as Taliban and Al Qaeda are also organizing terrorist attacks within the region. Inter-tribal conflicts are another reason for local armed attacks. These three kinds of attacks have different aims and targets. The Baloch separatists' targets are energy facilities, transportation facilities, large-scale projects, security forces, etc.; Taliban and other terrorist organizations' targets are religious institutions and girls' schools which are often attacked by suicide bombs; and tribal conflicts are internal killings within tribes. See Pipes, "The Baloch-Islamabad Tensions: Problems of National Integration," *DTIC Document* (2010).

people in Balochistan, which made the local security situation very critical. What's worth mentioning is that the local separatist groups are also hostile to CPEC. According to a report published in February 2016 by the *International Business Times* (IB Times) entitled "Balochistan separatists urge China and Pakistan to scrap CPEC deal," the Baloch Republican Party opposed CPEC because they believed the purpose of China and Pakistan was to deprive them of the local natural resources by means of CPEC, and claimed to accelerate more kidnaps and murders.<sup>4</sup>

Although the Federal Government has already sent an armed force to protect the security of Chinese personnel and projects (Pakistan plans to station an army brigade in the Gwadar Port area to control the port area and make it a large physically isolated zone to provide a secure environment for the development of the port area).<sup>5</sup> However, the economic and social costs of such isolation measure are extremely high. Moreover, this might also intensify the hostility of Baloch people towards the personnel and projects related to CPEC.

So why does the nationalist movement in Balochistan arise? Has the federal government taken measures to control the separatism in the nationalist movement? What measures should be taken to help CPEC projects avoid such risks?

In this paper, Part II reviews two opinions on the origin of the nationalist movement in Balochistan, and makes it clear that the domestic political situation in Pakistan will definitely get worse, no matter the government decides to weaken the political power of the Punjab people according to the theory of political federalism, or to solve the Baloch nationalism by abolishing the Sardar system according to the theory of tribal structure. Part III puts forward the framework of studying the Baloch nationalist movement from the perspective of the fiscal system. It believes that the unfair fiscal system is an important reason for the rise of the movement, and a reform of the fiscal system is also a relatively more acceptable plan for all parties. Part IV systematically analyzes the overall structure of the Pakistani government's fiscal system from 1974 to 2009, indicating that the unfair fiscal arrangement was the reason for the rise of separatism in

<sup>4</sup>Iaccino, L. "Balochistan Separatists Urge China and Pakistan to Scrap CPEC Deal Over 'Human-Rights Abuses'". <http://www.ibtimes.co.uk/balochistan-separatists-urge-china-pakistan-scrap-cpec-deal-over-human-rights-abuses-1542193>.

<sup>5</sup>"Four factors affecting the development of Gwadar Port (District)," [http://blog.sina.com.cn/s/blog\\_52f526870102vqzm.html](http://blog.sina.com.cn/s/blog_52f526870102vqzm.html).

the movement. Part V analyzes the main content of Pakistan's fiscal system reform in 2010, and its effect on suppressing the movement. Part VI points out that the fiscal reform in 2010 is still not enough, and continuing to deepen the reform of Pakistan's fiscal system is an important measure to alleviate the Balochistan separatist movement.

## 5.2 THE ORIGIN OF BALOCH NATIONALISM AND SEPARATISM: THE FAILURE OF POLITICAL FEDERALISM OR THE TRIBAL LOYALTY THAT WEAKENS THE SENSE OF IDENTITY AS PAKISTANIS?

There are two typical opinions in current studies on the origin of the Baloch nationalism and separatism.<sup>6</sup>

The first one is the failure of political federalism. Khan<sup>7</sup> points out that although Pakistan is a federal state according to the Constitution, neither the military autocratic government nor the elected government truly follows the federal principles, such as mutual negotiation, decentralization, provincial autonomy, and valid political access of all ethnic groups in the federal government and the army. For a province like Balochistan, which is vast and rich in resources but has a very low population share in the country, these principles are particularly important. The failure to follow these federal principles leads to so strong a sense of marginalization among the Baloch ethnic groups that they can only resort to nationalist movement or even separatist movement to seek for more autonomy.

<sup>6</sup>According to the definition of the British scholar Ernest Gellner, nationalism is first of all a political principle, politics and nationalism should be measured by the same dimension. Nationalism, as an emotion or a movement, can be most appropriately defined by this principle. Nationalist sentiment refers to the anger that arises when this principle is violated, or the satisfaction that comes from the realization of this principle. The nationalist movement is a movement promoted by this sentiment. See Ernest Gellner, "Nation and Nationalism," translated by Han Hong, Central Compilation & Translation Press, 2002. This paper follows this interpretation of the nationalist movement. The rise of Baloch nationalist movement was also because of the violation of this principle. The aim of the movement is not for unification. Some of them are demanding independence. Therefore, in this paper, they are called separatist forces or nationalist and separatist forces. Most Baloch people hope to satisfy their demands through reforms of the current federal system, and are not asking for independence or separation. They are called moderate nationalists or federalist nationalists.

<sup>7</sup>Khan, G., *Politics of Nationalism, Federalism, and Separatism: The Case of Balochistan in Pakistan*, University of Westminster, 2014.

Therefore, Khan<sup>8</sup> believes that revising Pakistan's federalism and protecting the political power of Balochistan are effective measures to resolve the separatist problem there. He also proposes to give more autonomy to Balochistan to control provincial resources and taxation; give the Senate and the National Assembly the same powers, so as to solve the problem of insufficient seats in the National Assembly; and split Punjab into smaller provinces to solve the problem of absolute dominance of Punjab in the federal government once and for all.

Indeed, the theory of political federalism fundamentally explains why the Baloch people are always marginalized in Pakistan and not fully represented in the central government. It is necessary to take three reforms: splitting the majority group, strengthening the power of the Senate and improving the provincial autonomy, so as to truly ensure the relative power balance of various ethnic groups and interest groups, and realize "unity in diversity" in Pakistan. However, the amendment of the above-mentioned federal principles will damage the interests of the Punjabi greatly. Under the current federal structure with Punjabi's domination in politics, these reform plans simply can never be passed by the National Assembly. Therefore, if Pakistan chooses to protect the interests of the Baloch people and alleviate their nationalist sentiments by weakening the political power of the Punjabis from a political federalism perspective, it is very likely to trigger further conflicts and confrontations between the federal government and Balochistan.

According to the second view, the weak sense of identity as Pakistanis among the Baloch people can be attributed to their tribal structure. Hasnat<sup>9</sup> has argued that under the sardari system and tribal structure, tribal members are loyal to tribal leaders and lack a sense of belonging towards Pakistan. This makes the ordinary Baloch people susceptible to incitement by the sardars to defy the federal government. However, the federal government is in fact largely responsible for the powerful grip the sardari system continues to have on the region. By neglecting its socio-economic development for too long, the federal government has contributed to the widespread poverty and the low levels of political literacy and educational attainment in the province, which constitute the objective social and economic underpinning for the population's susceptibility to

<sup>8</sup>Khan, G., *Politics of Nationalism, Federalism, and Separatism: The Case of Balochistan in Pakistan*, University of Westminster, 2014.

<sup>9</sup>Hasnat S.F., "Pakistan," ABC-CLIO (2011).



incitement. These unfavorable local conditions mean that not only would any attempt by the federal government to abolish the sardari system by force be largely ineffective, even worse, it might lead to the escalation of armed insurgency by Baloch nationalists, as did Ali Bhutto government's attempt to do so in the 1970s.

### 5.3 FISCAL SYSTEM AND NATIONAL UNITY

Taken together, both theories do offer different perspectives on the origin of the Baloch nationalist movement in Pakistan. However, when you apply the causal logic to find a solution to manage nationalism, both imply that there will be drastic changes in domestic political and social structure, and it is difficult to predict where the reform will end.

In comparison, fiscal reform is a relatively mild and more acceptable plan for all parties. Moreover, Pakistan's federal government has already taken some reform measures to ease the conflict, but more efforts are still needed and related researches should also be further deepened.

In fact, the intergovernmental fiscal system is used as a mechanism to determine the distribution of benefits and responsibilities between the federal and local governments, and between local governments at the same level as well. It is an important factor affecting the attitudes of the local people toward the federal government and other provinces. What's more, the high visibility of Pakistan's transfer payment system (which means the rules and distributions of transfer payments are simple and clear for the ordinary people to understand) further strengthens this connection. Therefore, the Baloch nationalist movement is worth analyzing from the perspective of the intergovernmental fiscal system. It is not only an important reason for the rise of the movement, but also a powerful tool for coping with the local nationalism.

To begin with, the fiscal system helps to compensate the disutility due to the loss of political autonomy of the local people. By using the analytical framework of the new political economy, Bolton & Roland<sup>10</sup> analyze the utility function of median voters in a region, and conclude that there are three major factors for determining whether the votes in a region are split or unified. The first one is the political effect. Different regions may have different preferences for fiscal policies. If two regions are two

<sup>10</sup> Bolton P. and Roland G., "The Breakup of Nations: A Political Economy Analysis," *The Quarterly Journal of Economics* (1997): 1057–1090.

independent countries, the local median voters have the right to vote for their own. However, in a unified country, national policies chosen by the national median voters may not conform to interests of local regions. When local residents have to abide by the policies chosen by the national median voters, they have to bear the disutility of the loss of political autonomy. The second one is the effect of economies of scale. A unified country can obtain efficiency gains from the economies of scale in the joint supply of public goods.<sup>11</sup> Therefore, the separation will always increase the cost of independent regions. The third one is the tax base effect. Since the per capita incomes of different regions are different, when the two regions are combined together, the one with lower per capita income can always benefit from it, while the one with higher per capita income will suffer from the declined tax base. The total utility of regional voters is the sum of the above three factors, if it is positive, then the region will vote for unity, otherwise, it will vote for independence. Since the latter two factors are given in this framework, in order to maintain the unity of the country, the federal government is likely to make fiscal policies to compensate the disutility of local voters due to the loss of political autonomy.

Motohiro Sato<sup>12</sup> believes that fiscal transfer payments are an important tool for maintaining national unity. He points out that intergovernmental subsidies can be used as a means for political vote transaction to maintain the unity of the country. As a result, the unity will be maintained by ensuring economic prosperity of a certain region.

Finally, fiscal equalization policy is conducive to strengthening national identity and winning support for the federalist political parties. Béland and Lecours<sup>13</sup> who have studied the role of fiscal equalization by transfer payments in the political reconciliation in multi-ethnic country such as Canada, and they point out that equalization can not only help unify the federal state by “buying” votes from the poorer regions, but also help strengthen their sense of identity as one nation, generating unity and cohesion across the country. For example, Quebec has continuously obtained the largest federal equalized transfer payment in absolute terms

<sup>11</sup> Persson T., and Tabellini G., “Political Economics: Explaining Economic Policy,” trans. Fang Min, China Renmin University Press (2007).

<sup>12</sup> Sato M., “The Political Economy of Interregional Grants,” in *Intergovernmental Fiscal Transfers: Principles and Practice*, World Bank Washington, DC, 2007: 173–197.

<sup>13</sup> Béland D., Lecours A., “Accommodation and the Politics of Fiscal Equalization in Multinational States: The Case of Canada,” *Nations and Nationalism* 20, no. 2 (2014): 337–354.

in regional fiscal redistribution since Canada established the fiscal equalization project in 1957, which is of great value for Quebec's federalist political parties to keep defending Quebec's existence as a province of Canada.

#### 5.4 UNFAIR TRANSFER PAYMENTS AND THE RISING TENDENCY OF BALOCH SEPARATISM FROM 1974 TO 2010

Pakistan became independent in 1947, and its inter-governmental fiscal arrangement officially started in 1951. However, Balochistan was only granted the status of a federal province in 1970.<sup>14</sup> In addition, It was disintegrated into East Pakistan (present-day Bangladesh) and West Pakistan (present-day Pakistan) in 1971. Since the fiscal system between the federal and provincial governments had undergone major changes, the study thereof only began with the first fiscal arrangement implemented in 1974 after the disintegration. The period from 1974 to 2010 was the first stage of Pakistan's fiscal system arrangement, characterized by high concentration of the federal government's fiscal power and the high degree of unfairness in the transfer payment arrangements for Balochistan. The nationalist sentiment of the Baloch people accumulated during this period, which ended in a large-scale armed rebellion. With the increasingly radicalized nationalist movement, the separatist forces demanding independence are showing a clear upward trend.

##### 5.4.1 1974–2010: *Highly Centralized Fiscal Power and Unfair Transfer Distribution Mechanism*

###### 1. Highly centralized fiscal arrangements

Pakistan's 1973 Constitution stipulates the overall framework of the fiscal structure between the federal government and provincial governments, including the division of taxes, duties and responsibilities, etc.<sup>15</sup> The National Finance Commission (NFC) is organized every 5 years under the guidance of the 1973 Constitution, to divide income between the federal government and provincial governments in each period. Since

<sup>14</sup>Hasnat S.F., "Pakistan," ABC-CLIO (2011).

<sup>15</sup>The Constitution of the Islamic Republic of Pakistan 1973, Article 160 (National Finance Commission). <http://www.pakistani.org/pakistan/constitution/>.

the establishment of the first National Finance Committee in 1974, Pakistan has altogether established 7 NFC, but only 4 of them have reached a consensus,<sup>16</sup> respectively in 1974, 1991, 1997 and 2010. Although Pakistan is a federal country, from 1974 to 2010, the fiscal spending power, financial resources and duties and responsibilities were highly concentrated in the federal government, showing a strong characteristics of centralization.

On the one hand, tax categories assigned to the federal government are all with broad tax bases, buoyant sources of revenue. For instance, the direct taxes such as personal income tax and corporate profit tax, and indirect taxes such as duties and sales taxes. On the contrary, although more tax categories are assigned to provincial governments, most of them are based on small-scale incomes, for instance, property tax, property transfer tax, land income tax, agricultural income tax, capital gains tax, stamp duty, automobile tax and entertainment tax, etc. The federal government's tax revenues account for more than 90 percent of the national tax revenue. The 1973 Constitution has divided the responsibilities of the federal government and the concurrent responsibilities of both federal government and provincial governments: 67 subjects are enshrined in the federal legislative list, on which the legislative powers are solely possessed by the federal government; 47 subjects are enshrined in the concurrent legislative list,<sup>17</sup> on which the legislative powers are possessed by both federal government and provincial governments. Other subjects not stipulated in the Constitution are assigned to provincial governments according to subsidiarity principle. At the same time, Article 143 of the Constitution stipulates that when there is a conflict between the federal government and the provincial government in terms of concurrent responsibilities, the federal law shall prevail. This gives the federal government larger discretion, while the autonomy of provincial governments is considerably restricted.<sup>18</sup>

<sup>16</sup>According to the Constitution, the distribution arrangement proposed by NFC can come into effect only under the consensus by all the four provinces (Punjab, Sindh, Khyber Pashtu and Balochistan). So when the 2nd and 3rd NFC failed to reach a consensus, the fiscal arrangement of 1974 had to be followed continuously. See Bahl R, Wallace S and Cyan M., "Pakistan: Provincial Government Taxation. International Center for Public Policy," *Andrew Young School of Policy Studies*, Georgia State University (2008): 24.

<sup>17</sup>The Constitution of the Islamic Republic of Pakistan 1973, Fourth Schedule [Article 70 (4)].

<sup>18</sup>Khan G., "Politics of Nationalism, Federalism, and Separatism: The Case of Balochistan in Pakistan," in University of Westminster (2014).

Under such a highly centralized fiscal system, provincial governments have very limited autonomy in terms of fiscal revenue and expenditure. This can easily cause the following problems: firstly, where a province suffers from poor economic growth, inaccessible public service and low living standard, the provincial government is easily to claim that the federal government should be responsible because of insufficient fiscal resources; secondly, the vertical fiscal imbalance existing under the centralized system will make provincial governments highly dependent on the transfer payment funds of the federal government. Therefore, if transfer payments are unfairly distributed among provinces, it will lead to conflicts and dissatisfaction between different provinces and between the federal government and provincial governments as well; thirdly, when intervening too much in the affairs that are supposed to be dealt with by provincial governments, the federal government seldom considers the needs and preferences of the local people, while provincial and local governments cannot participate in decision-making of local affairs of vital interests. The local people will feel themselves being marginalized totally, thus distrusting the federal government thereafter. These problems are more prominent in places, where the inter-provincial border is divided by ethnicity.

2. Transfer payments based on divisible pool of taxes: population is the only criterion for transfer payment distribution

Over 90 percent of the country's tax revenue goes to the federal government, but the federal government is only responsible for about 70 percent of the fiscal expenditure.<sup>19</sup> In order to adjust the vertical fiscal imbalance between the federal and provincial governments, previous NFCs have proposed corresponding transfer payment plans, which mainly include divisible pool of taxes,<sup>20</sup> straight transfers, development grants and non-development grants.

Among them, divisible pool of taxes accounts is the dominant method (over 60 percent) in the total transfer payment of the federal government to provincial governments. Therefore, it is decisive to the fiscal capacity of

<sup>19</sup>Wasti S., "Intergovernmental Fiscal Relations: A Case Study of Pakistan," in University of Portsmouth (2013).

<sup>20</sup>Since the establishment of the first NFC in 1974, the federal taxes that make up the divisible pool of taxes had changed from time to time. For instance, in 1974, it only included income tax, sales tax and export duties on cotton. In 2010, all federal taxes were included according the 7th NFC plan.

provincial governments and the inter-provincial fiscal equalization. Straight transfers refer to the fiscal revenue first collected by the federal government from the natural resources of provinces (oil royalty, natural gas development surcharge, royalty and sales tax, and hydropower profit) and then transferred to provincial governments. Development grants are conditional grants and are special funds provided by the federal government for annual development projects of provincial governments. Before 1991, non-development grants were mainly for revenue deficits of provincial governments. After the ban on funds for income deficits in 1991, it is now special backwardness grant for Khyber Pakhtunkhwa and Balochistan. Among these four transfer payments, the former two are the main reasons for Balochistan's complaint, because it has been treated unfairly in the distribution of these two incomes.

The 1974 NFC plan was the first federal-provincial government fiscal distribution plan announced by Pakistan after Bangladesh became independent in 1971. The NFC took the population of each province as the only criterion for distributing transfer payments from the federal government's divisible pool of taxes. This criterion has been used for nearly 30 years, until a new distribution plan was proposed by the 7th NFC in 2010.<sup>21</sup> This plan was very favorable to Punjab, because it can obtain the same per capita transfer payments as other provinces. Punjab boasts high population density, low poverty rate and relatively more developed economy and infrastructure. Therefore, the per capita supply cost of basic public services in Punjab is lower than that in other provinces. To the contrary, Balochistan has a very low population density (18.9 people per square kilometer).<sup>22</sup> It suffers from poor urbanization level and economic growth, the roads and infrastructures are in bad condition. Therefore, to have the same per capita supply of basic public services as that of Punjab, the cost will be very high. At the same time, Balochistan's fiscal revenue also lags far behind due to economic backwardness. So this kind of fiscal transfer payment distribution plan based only on population lacks horizontal fairness, because it neglects the actual fiscal expenditure needs and fiscal revenue capacity of provinces. And this is one of the important reasons for Balochistan's dissatisfaction with the federal government.

<sup>21</sup> Ahmad I., Mustafa U., and Khalid M., "National Finance Commission Awards in Pakistan: A Historical Perspective," in University Library of Munich, Germany (February 2007).

<sup>22</sup> The average population density of Pakistan is 831.56 persons per km<sup>2</sup>.

### 3. Straight transfers: unfair profit distribution of natural resources

Pakistan began mass production of natural gas in 1952. The biggest Sui gas field was discovered in DeraBugti in Balochistan at that time, and exploitation and drilling began within two or three years. In 1955, the natural gas pipeline project connecting Sui and Karachi was completed, and natural gas was supplied to Karachi, which was then the capital of Pakistan. More gas fields in Balochistan were developed including Uch in 1955, Pirkoh in 1975, Loti in 1985 and Zarghun in 2002. Balochistan had been Pakistan's most important energy production base for nearly half a century until the 1990s. Its natural gas production accounted for more than half of Pakistan's total natural gas production. In 1994–1995, the natural gas production of Balochistan accounted for nearly 56 percent of the country's total output. However, due to the increasingly severe security situation, the exploration and development of new natural gas fields in Balochistan was much less. Therefore, although its natural gas production kept increasing, its proportion in Pakistan's total output was declining. By 2004–2005, its total output accounted for only 25 percent of the national output.<sup>23</sup>

Balochistan's revenue from natural gas development consists of three parts: natural gas royalty, Gas Development Surcharge (GDS) and excise duty. These fees are collected by the federal government and then returned to provincial governments in the form of straight transfer after deducting 2 percent of the levy.<sup>24</sup> According to Article 161, paragraph 1, of Pakistan's 1973 Constitution, "the net income of the federal natural gas excise tax levied by the federal government at wellheads, and the royalties levied by the federal government, should not be included in the unified federal fund, but be paid to the provincial government where the natural gas wellheads are located."<sup>25</sup> Among these three natural gas-related incomes, the excise tax is levied at a fixed tax rate of 5.4 rupees per MMBtu. The 7th NFC's plan has increased the tax rate to 10 rupees. All provinces are agreeing with the collection and distribution of the excise tax, and Balochistan is strongly dissatisfied with the calculation method of royalties and GDS.

<sup>23</sup> World Bank, "Pakistan-Balochistan Economic Report: From Periphery to Core," *World Bank Other Operational Studies*, World Bank (2008): 52.

<sup>24</sup> G. Anderson, *Oil and Gas in Federal Systems*, Oxford University Press, 2012.

<sup>25</sup> The Constitution of the Islamic Republic of Pakistan 1973, Article 161 (1). <http://www.pakistani.org/pakistan/constitution/>.

Since the calculation of royalties and GDS is closely related to several domestic natural gas prices set by the federal government, we must, first of all, understand Pakistan's domestic natural gas pricing policy. There are three main types of participants in Pakistan's natural gas industry, which are exploration and production companies (E&P company), natural gas transmission and sales companies (namely the two major state-owned companies, Sui Southern Gas Company and Sui North Natural Gas Company) and natural gas consumers, according to the upstream and downstream relationship of the production process. There are three prices related to these three kinds of participants: the first is the wellhead price (the producer price is obtained after deducting the royalty by 12.5 percent) at which an E&P company sells natural gas to the two transmission and sales companies; the second is the governmental price set by the government after considering the operating costs of transmission and sales companies; the third is the notified consumer price determined by the federal government, the final consumer price of natural gas will be the notified price plus the general sales tax (See Table 5.1).

First, the natural gas royalty. In Pakistan, the natural gas royalty is paid by E&P company to the government by 12.5 percent of the wellhead price. The wellhead price is set by the Oil and Gas Administration (OGRA) of the federal government, and published on its official website on a

**Table 5.1** The composition of gas consumer prices in Pakistan (2012)

<i>Composition of prices</i>	<i>USD/MMBTU</i>
Producer price	3.76
+royalty (12.5%)	0.54
= Wellhead price	4.30
+ consumption tax (10 rupees per MMBtu)	0.09
+operating and maintenance cost	0.37
+RoA	0.23
+other	-0.18
=Prescribed price	4.80
+GDS	0.05
=Notified consumer price	4.85
+general sales tax	0.78
=Final consumer price	5.63

*Source:* Gomes I. Natural Gas in Pakistan and Bangladesh: current issues and trends, Oxford Institute for Energy Studies, 2013

*Note:* The Pakistani government published wellhead price and notified consumer price on OGRA official website, producer price = wellhead price - royalty



**Table 5.2** The wellhead prices of natural gas published by OGRA on July 1st, 2014

<i>Natural gas field</i>	<i>Province</i>	<i>USD/MMbtu</i>	<i>Natural gas field</i>	<i>Province</i>	<i>USD/MMbtu</i>
Bhit	Sindh	4.7652	Zamzama	Sindh	4.3464
Kandkot	Sindh	(2.2671)	Dhodak	Punjab	(2.9477)
Kadanwari	Sindh	8.5004	Nandpur, Panjpir	Punjab	(3.7337)
QadirPur	Sindh	3.0177	Loti	Balochistan	(1.3862)
Sawan	Sindh	4.4366	Pirkoh	Balochistan	(1.3862)
Latif Field	Sindh	6.1186	Sui	Balochistan	(2.1657)
Miano	Sindh	4.4366	UCH	Balochistan	3.9223

*Source:* OGRA: Field-wise Well Head Gas Prices, <http://www.org.pk/images/data/downloads/1429698862.pdf>

*Note:* Since the prices published by Pakistan's OGRA are in rupee, the dollar price in parenthesis is calculated by the author based on the exchange rate of rupee to the dollar at that time. On July 1, 2014, the exchange rate of the Pakistani Rupee to the U.S. dollar was 1PKR = 0.010142USD

regular basis. According to the 2001 pricing system, the wellhead price at which natural gas is sold to the two transmission and sales companies began to be linked to international crude oil prices, and was adjusted twice a year according to the announcement of OGRA. Among all the natural gas fields developed in Balochistan, only Zarghun, a natural gas field developed in 2002 and accounting for merely 1 percent of Balochistan's remaining natural gas reserves, is fully applicable to the 2001 pricing system. For projects such as Sui, Uch, Pirkoh and Loti which were developed before 2002, the gas prices are still set according to the natural gas pricing policy when the development concession was approved.<sup>26</sup> They all adopt the cost plus pricing, and their prices are much lower than the natural gas price set by the 2001 pricing system. Although the federal government did systematically adjust the wellhead prices of these earlier developed natural gas fields in 2001, it can be seen from Table 5.2 that as of July 1, 2014, the wellhead prices of these natural gas fields in Balochistan were still significantly lower than those in other provinces. Therefore, the relatively lower natural gas wellhead prices in Balochistan have led to low royalty incomes compared to other provinces for a long time, especially Sindh.<sup>27</sup>

<sup>26</sup>For instance, the wellhead price of Sui natural gas field was set according to the Gas Pricing Agreement signed by the Pakistani government and Pakistan Petroleum Limited and promulgated by the federal government.

<sup>27</sup>Since the mid-1990s, the development of natural gas fields in Sindh has continued to increase, and has gradually become Pakistan's largest natural gas producing province, so it has benefited the most from the new pricing mechanism.

Second, the Gas Development Surcharge (GDS). GDS is levied under the Natural Gas (Development Surcharge) Ordinance of 1967, the revenue belongs to the federal government. Its purpose is to finance for the construction of Pakistan's natural gas pipelines, to ensure the equilibrium of oil and gas prices. According to the provisions of the 1967 Ordinance, the gap between the notified consumer price set by the federal government and the prescribed price for natural gas transmission and sales companies (Prescribed price for Gas Companies)<sup>28</sup> is defined as a GDS.

From 1967 to 1990, most natural gas pipelines had been constructed and a surplus of GDS began to appear. Therefore, in 1990, NFC transferred GDS as a direct transfer payment from the federal government to provincial governments. Article 6 of the 1990 NFC plan issued in the form of Presidential Decree No. 1 of 1991 stipulates that "The proportion of GDS collected by each province in each fiscal year in the total GDS equals the percentage of this province's natural gas production at well-heads to the total natural gas production of the same year." This means that the annual revenue of GDS will be distributed among provinces according to their respective natural gas production. Due to the above pricing policy, the weighted average natural gas wellhead price in Balochistan was the lowest among the four provinces, but its consumer price of natural gas was the same with that produced by Sindh and other provinces. Therefore, Balochistan had made the biggest contribution to GDS revenue, but according to the 1991 distribution policy, the transfer payment for Balochistan was less than any other province, far below its reasonable share.

Balochistan's industrial development is lagging behind. However, the natural resources such as natural gas are abundant in the province. The straight transfer payment from natural gas is the second largest source of revenue for Balochistan, hence, the unfair inter-provincial distribution of straight transfer is more likely to arouse complaint of the Baloch people against the federal government.

<sup>28</sup> For example, the prescribed prices of Sui North Gas Company (SNGPL) and Sui South Gas Company (SSGCL) are determined based on the following factors: wellhead price of gas, wellhead excise tax, operation and maintenance costs, depreciation, RoA of natural gas companies (17.5 percent for SNGPL and 17 percent for SSGCL). There is a negative correlation between GDS and royalty. For example, the higher the wellhead price is, the higher the royalty and the lower the GDS will be, and vice versa.

#### 5.4.2 *The Increasing Radicalization and Separatist Tendency of the Baloch Nationalist Movement*

The above-mentioned fiscal arrangements have lasted for nearly 30 years. The Baloch people, who have been unfairly treated by the federal government for a long time, have to fight for their rights through various nationalist movements. From the perspective of the development process of nationalist movements, the political demands and corresponding actions of the nationalists can be divided into two categories: one is to demand greater autonomy in Balochistan under the federal framework. This kind of nationalists wants to participate in provincial and national elections by establishing nationalist parties, hoping to solve problems of unfair treatment through peaceful dialogue and political negotiation. The other is to demand independence from Pakistan and to found an independent country for the Baloch people to defend their own interests. This kind of nationalists wants to fight the government forces by organizing various armed organizations and terrorist attacks, and fight against the central government to express their desire for independence by attacking enterprises and personnel from other provinces or foreign countries. The typical representatives of nationalist and separatist groups include Balochistan Liberation Army, Baloch Republican Army, Baloch Nationalist Front, etc. (See Table 5.3)

In the 1980s and 1990s, mainstream public opinion was represented by federalist parties among Baloch nationalists, whose political demands were mainly to amend the constitution and obtain greater provincial autonomy. According to the research by Grare,<sup>29</sup> nationalist parties during this period were very active, and they had also received widespread support from the Baloch people. In provincial elections, the combined votes for nationalist parties reached 47.8 percent in 1988 and 51.74 percent in 1990. And the nationalist parties won the election again and formed a government in 1997. Later, the separatist forces in the Baloch nationalist movement began to rise, and gradually evolved into military operations against the federal government. Their political demands changed from amending the Constitution to creating a new country for the Baloch people, especially during the reign of Musharraf. With the rise of nationalist movement, various nationalist and separatist groups launched many armed attacks in Balochistan and other regions. Musharraf took large-scale cleanup

<sup>29</sup> Grare F., "Balochistan: The State Versus the Nation," 2013.

**Table 5.3** Balochistan nationalist groups and political demands thereof

<i>Name</i>	<i>Political demand</i>
Balochistan Liberation Army	An armed separatist group demanding the independence of Greater Balochistan of the Baloch people from Pakistan, Iran, and Afghanistan
Baloch Republican Party	A nationalist political party supporting the independence of Greater Balochistan and opposing any form of political dialogue
Baloch Republican Army	Armed forces of the Baloch Republican Party
The National Party	A moderate, center-left Balochistan nationalist party that claims to represent the middle class and usually participates in elections
Balochistan National Party	A moderate nationalist party demanding an increase in Balochistan's revenue share from provincial resources and greater provincial autonomy
Baloch National Front	A nationalist party refusing to participate in the political process and calling for the independence of Greater Balochistan
Baloch Student Organization (BSO-Azad)	Supporters of the Balochistan's Liberation Army, demanding the independence of Balochistan

*Source:* Grare F. Balochistan: The State Versus the Nation, Carnegie Endowment for International Peace, Washington DC, 2013

operations but still failed to eliminate the separatist forces in Balochistan. Besides, the moderate nationalist parties were also strongly dissatisfied with the federal government and refused to participate in the general election in 2008.

The political demands of the Baloch nationalists became more and more radicalized. With the emerging nationalist groups and parties demanding independence, the political factor can be an explanation, for example, the Baloch people did not have enough seats and power in the federal government and military. What's more important was that the long-term unfair fiscal system had already caused considerable consequences for Balochistan's social and economic growth and the relationship between the local people and the federal government as well.

First of all, under such fiscal system, Balochistan has been distributed with insufficient fiscal revenue and profit from natural resources for a long time. The public expenditures were too low to promote social and economic development. As shown in Table 5.4, Balochistan was lagging far behind other provinces in aspects of employment rate, health condition of

**Table 5.4** Major social and economic indicators of Balochistan in 2010–2011

<i>Indicators</i>	<i>Pakistan</i>	<i>Punjab</i>	<i>Sindh</i>	<i>Khyber-Pakhtunkhwa</i>	<i>Balochistan</i>
Employment rate (%)	30.9	33.1	31.0	24.3	24.5
Proportion of children under 5 years of age who are underweight (%)	31.5	29.8	40.5	24.1	39.6
Consumption-based Gini index	0.2752	0.2832	0.2825	0.2379	0.1899
Net enrollment rate of primary schools (%)	56	61	53	51	47
Completion rate of grade 1 to grade 5 (%)	49	52	52	41	32
Literacy rate (%)	58	60	59	50	41
Gender equality index in primary schools	0.88	0.95	0.84	0.79	0.63
Gender equality index in middle schools	0.85	0.97	0.79	0.60	0.41
Gender equality index of youth literacy rate	0.79	0.87	0.78	0.57	0.39
Proportion of children fully immunized within 12–23 months (%)	81	86	75	77	56
Proportion of children fully immunized against measles under one year old (%)	82	86	77	78	58
Proportion of population with access to improved water (%)	87	93	89	70	47
Proportion of population using health facilities (%)	66	72	62	62	31
Human Development Index (2005)	0.6196	0.6699	0.6282	0.6065	0.5557

*Source:* (1) Pakistan Millennium Development Goals Report 2013; (2) Haroon Jamal & Amir Jahan Khan, Trends in Regional Human Development Indices, Research Report No. 73, 2007

*Note:* The gender equality index refers to the enrollment rate of girls relative to boys, that is, the number of girls per boy. The closer the value is to 1, the more equal it will be

children, net enrollment rate of primary schools, adult literacy rate, proportion of people with access to clean water and medical and health service, etc., remaining the worst among the four provinces. In regard to the comprehensive indicator of Human Development Index (HDI), Balochistan scored 0.5557 in 2005, well below the average level of 0.6196 of Pakistan and that of other provinces. The standing backwardness and

poverty were the fundamental reasons for the dominance of separatist forces in Balochistan during this period.

Second, the highly centralized fiscal power not only caused distrust of the Balochistan government against the federal government led by the Punjab people, but also a weakening sense of identity as Pakistanis. Balochistan had been ceaselessly demanding an abolition of the concurrent list and a higher provincial autonomy since the 1973 Constitution stipulated the concurrent legislative list and the 1974 NFC determined the distribution plan of transfer payments among the federal and provincial governments. Balochistan proposed to take the indicators such as the level of regional economic development into consideration for distribution planning, and asked for reasonable share of revenue from natural gas resources. However, for more than 30 years, none of these requirements have been met. Khan pointed out, "The main demands of Baluchistan nationalists have always been provincial autonomy and local control of their resources, but these demands have been repeatedly rejected since the founding of Pakistan."<sup>30</sup>

As a result, the dissatisfaction of Baloch nationalists kept accumulating for long, leading to strong feelings of being marginalized and deprived and complete distrust in the federal government led by the Punjab people. After Musharraf won the election, he launched many large-scale development projects in Balochistan with no negotiation with the provincial government at all, such as the Gwadar deep-water port<sup>31</sup> and mining projects of mineral resources, which further irritated the nationalists. They did not trust the federal government, believing that these projects could be colonial plans against the Baloch people if the provincial government was not allowed to get involved.<sup>32</sup> In addition, Musharraf used to suppress the

<sup>30</sup>Khan A., "Renewed Ethnonationalist Insurgency in Balochistan, Pakistan: The Militarized State and Continuing Economic Deprivation," *Asian Survey* 49, no. 6 (2009): 1071–1091.

<sup>31</sup>Khan (2009) points out when President Musharraf and Chinese Vice Premier Wu Bangguo signed the Gwadar Port project agreement on March 24, 2002, no representatives of the Balochistan were present. Moreover, Musharraf also took advantage of the federal government's highly centralized power (for example, the Constitution stipulates that it shall be the duty and responsibility of the federal government to carry out port development projects and determine the scope and organizational structure of port authorities) to assign eleven representatives to the Board of Gwadar Port Authority, with only from Balochistan.

<sup>32</sup>Khan A., "Renewed Ethnonationalist Insurgency in Balochistan, Pakistan: The Militarized State and Continuing Economic Deprivation," *Asian Survey* 49, no. 6 (2009): 1071–1091.

Baloch nationalist movement by military means, further stimulating the spread of the movement.

Therefore, the conflict between the Baloch nationalists and the federal government had already intensified by the end of Musharraf's rule. Not only did the Baloch separatists intensify their armed attacks due to their rising strength, even the moderate nationalist parties were also strongly dissatisfied with the federal government, which was very likely to push them to join the separatist groups.

## 5.5 THE 2010 FISCAL REFORM AND CHANGES OF POLITICAL DEMANDS OF THE BALOCH NATIONALISTS

From 2010 till now, the fiscal system of Pakistan has entered the second stage. The fiscal reform was implemented during this period, and larger autonomy was granted to Balochistan. The share of revenue of Balochistan in transfer payments has been increased, and the profit distribution of natural resources has also reflected the principle of fairness. These measures are conducive to further conciliating the Baloch nationalist movement, and the separatist tendency has been mitigated by consolidating nationalists who support the federal government.

### *5.5.1 The Fairness of Fiscal System has been Enhanced after the Diversified Distribution Criteria Were Adopted in 2010*

Zardari of the Pakistan People's Party was elected president in 2008, he has been committed to promoting reconciliation among ethnic groups in Pakistan,<sup>33</sup> and has implemented "two milestone reforms that changed the characteristics of Pakistan".<sup>34</sup> The first reform was the amendment to the Constitution, which granted larger amount of political autonomy to provincial governments, making Pakistan a truly federal state; the other was the 7th NFC plan which gave larger fiscal power to provincial governments.

<sup>33</sup>The measures include pardoning and encouraging Baloch radical nationalists in exile to return to their homeland, and releasing Baloch nationalist activists in custody, etc. See Wenhua Xiang, "Evaluation of the Ruling Practice of Pakistan People's Party in Zardari's Reign," *Issues of Contemporary World Socialism*, no. 3 (2014): 68–82.

<sup>34</sup>"Opinion: A Step Towards Fiscal Autonomy." [http://www.pk.undorg/content/pakistan/en/home/library/hiv\\_aids/development-advocate-pakistan-volume-2-issue-1/opinion-a-step-towards-fiscal-autonomy.html](http://www.pk.undorg/content/pakistan/en/home/library/hiv_aids/development-advocate-pakistan-volume-2-issue-1/opinion-a-step-towards-fiscal-autonomy.html).

1. The federal government decentralize larger expenditure autonomy to provincial governments

On April 8, 2010, the 18th Amendment to the Constitution passed by the National Assembly abolished the concurrent legislative list as prescribed by the 1973 Constitution. Of the 47 subjects listed in the concurrent list, 44 were decentralized to provincial governments, including marriage, labor, education and environmental protection, etc. These matters are now fully under the legislative authority of provincial governments. For the Baloch people, provincial government can make better policies to meet the needs and preferences of the local people in spheres closely related to their lives. Therefore, their accusations against the federal government will be reduced to a certain extent.

2. Transfer payments based on divisible pool of taxes: diversified distribution criteria

The 7th NFC plan, coming into effect on July 1, 2010, increased the vertical shares for provinces in the divisible pool of taxes from 46 percent to 57.5 percent,<sup>35</sup> improving the fiscal strengths of provincial governments greatly. Moreover, diversified distribution criteria have been adopted to distribute revenues of the divisible pool of taxes. New factors including population proportion, level of poverty or backwardness income collection or income generation, and population density into the horizontal distribution criteria for each province. The weights of these four factors are 82 percent, 10.3 percent, 5 percent and 2.7 percent respectively (see Table 5.5). Under this new distribution plan, Balochistan's share of the transfer payment in the federal government's divisible pool of taxes increased to 9.09 percent. This distribution plan has increased the overall share of the other three provinces except Punjab. However, due to the substantial increase in the vertical share for provinces, all provinces including Punjab have received more transfer payments than before. And that is also an important reason why the current NFC distribution plan can be unanimously agreed by all provinces.

Although some scholars have pointed out that due to the low management ability of the Balochistan government, the policy intentions of the

<sup>35</sup> Pakistan National Finance Commission Secretariat, *Report of the NFC 2009*. [http://www.finance.gov.pk/nfc/reportofthenfc\\_2009.pdf](http://www.finance.gov.pk/nfc/reportofthenfc_2009.pdf).



**Table 5.5** NFC Award 2010 Transfer payments based on divisible pool of taxes (%)

<i>Indicators</i>	<i>Pakistan</i>	<i>Punjab</i>	<i>Sindh</i>	<i>Khyber- Pakhtunkhwa</i>	<i>Balochistan</i>
Proportion of Population (1998 Census)	82.0	57.36	23.71	13.82	5.11
Poverty/backwardness	10.3	23.16	23.41	27.82	25.61
Income generation/income collection	5.0	44.0	50.0	5.0	1.0
Inverse population density index	2.7	4.34	7.21	6.54	81.92
Total share	100	51.74	24.55	14.62	9.09

*Note:* Inverse population density index = 1/population density of a province

central government cannot be realized by locally, so the decentralization and increase of funds may lead to an increase in violent conflicts.<sup>36</sup> But the author believes that the next step should be the governance structure reform of Balochistan government rather than centralizing the power again.

### 3. Straight transfer: fair distribution plan.

In the 7th NFC plan, a new allocation plan for GDS was adopted to ensure fairness. The plan adds up the national natural gas royalty and GDS together to calculate the price per MMBtu. After that, the royalty will still be distributed in the original way, but the distribution of GDS will be adjusted according to the average price.

The formula is as follows:

$$\text{GDS of all provinces} = \left[ \frac{(\text{national natural gas GDS} + \text{national natural gas royalty})}{\text{national natural gas production}} \right] \times \text{natural gas production of provinces} - \text{GDS revenue of provinces}$$

Under the new distribution plan, the same GDS and royalty per MMBtu will be distributed to each province (see Table 5.6), regardless of the level

<sup>36</sup>Brown M., Dawaod M., ArashIranlatab, and Naqi M., Balochistan Case Study, INAF 5493-S: Ethnic Conflict: Causes, Consequences and Management, June 21, 2012, [www4.carleton.ca/cifp/app/serve.php/1398.pdf](http://www4.carleton.ca/cifp/app/serve.php/1398.pdf).

**Table 5.6** Comparison of provincial revenues of GDS and royalty under the new and old mechanisms

	Production			Old mechanism			New mechanism			Rupee/ MMBtu
	BBTU	GDS (1 million rupees)	Royalty (1 million rupees)	Total (1 million rupees)	Rupee/ MMBtu	GDS (1 million rupees)	Royalty (1 million rupees)	Total (1 million rupees)		
Balochistan	233,179	4282	4716	8998	38.59	6099	4716	10,815	46.38	
Northwest frontier province	32,533	469	876	1345	41.34	633	876	1509	46.38	
Punjab	61,939	1121	1207	2328	37.59	1666	1207	2873	46.38	
Sindh	873,840	15,361	27,696	43,057	49.27	12,835	27,696	40,531	46.38	
Pakistan	1,201,490	21,233	34,495	55,728	46.38	21,233	34,495	55,728	46.38	

Source: Report of the NFC 2009, [http://www.finance.gov.pk/nfc/reportofthefnc\\_2009.pdf](http://www.finance.gov.pk/nfc/reportofthefnc_2009.pdf)

of wellhead prices. Provinces with lower royalties will receive higher revenue of GDS, and provinces with higher royalties will receive lower revenue of GDS. Taking the data of 2009–2010 fiscal year as an example, Balochistan received a revenue of 10.815 billion rupees under the new mechanism, 1.817 billion rupees more than the under the old mechanism, while the revenue received by Sindh decreased by 2.526 billion rupees. The conflict between the provinces on the revenue distribution of natural gas resources has been resolved accordingly. At the same time, the federal government also promised to compensate Balochistan for the lessened revenue of GDS from July 1, 2002 to June 30, 2009, according to the new mechanism. However, the lessened revenue of royalties caused by the lower wellhead prices in Balochistan has not yet been compensated by the federal government.

### 5.5.2 *The Separatist Tendency of the Baloch Nationalists has been Suppressed to a Certain Extent*

Although the effect of the above-mentioned reform of inter-provincial fiscal arrangements is somewhat limited, this reform still reflects the good faith of the federal government for political dialogue and national reconciliation, given the fact that from 1974 to 2010, Balochistan's call for fiscal reform was continuously neglected. Some observers spoke highly of the new NFC plan, and regarded it as "a great achievement in achieving inter-provincial harmony" and a "graduation ceremony for Pakistan's democracy".<sup>37</sup> The plan has satisfied some of the core demands of the ordinary people and nationalists in Balochistan, including the political procedure of democratic consultation, decentralization of power and fair share of transfer payments. It is conducive to controlling the separatist tendency of the Baloch nationalists in the following aspects:

1. According to a Gallup poll, most Baloch people prefer to stay within the federal framework.

A Gallup survey, commissioned by the Department for International Development (DFID) of the British government on July 20, 2012, shows that most Baloch people oppose the independence of Balochistan,<sup>38</sup>

<sup>37</sup> Hasnat S.F., "Pakistan," *ABC-CLIO* (2011).

<sup>38</sup> "37Pc Baloch Favour Independence: UK Survey". <http://www.thenews.com.pk/Todays-News-13-16755-37pc-Baloch-favour-independence-UK-survey>.

because 67 percent of the local people, including both Baloch and Pashtun, are supporting larger provincial autonomy rather than separating Balochistan from Pakistan. It makes it clear that a unified Pakistani Federation still has a greater public opinion foundation in Balochistan, which also provides the foundation for solving the nationalist problem there in the future.

2. Nationalist parties of Balochistan participated in the provincial election again to seek for larger provincial autonomy and fiscal resources, rather than resorting to local independence or violent activities.

The participation of Baloch nationalist parties in provincial election is obviously important. The legitimacy of the provincial government is fully valid only when they are participating in administrative affairs of Balochistan. A legal and credible Balochistan government can help rebuild the self-control of Balochistan, thereby reducing violence and seeking for the benefits of Balochistan at the federal level.

The 2010 fiscal reform has largely ignited the confidence of Baloch federalist parties in the federal government and parliamentary politics, for they believe they can seek for larger provincial autonomy and control over their own mineral and geological resources under the federal structure, and thus better protecting the interests of the Baloch people. Therefore, the National Party and Baloch National Party who refused to participate in the general election in 2008, both participated in the election in May, 2013.<sup>39</sup> In the end, the National Party won ten seats out of the total sixty-four seats of the provincial assembly, raking 3rd behind Pakistan Muslim League Nawaz (PML-N) with twenty-two seats and Pakhtunkhwa Milli Awami Party (PkMAP) with fourteen seats. These three parties formed the governing coalition of Balochistan, and the chairman of the National Party Abdul Malik Baloch was appointed as the chief minister of Balochistan.

It can be seen that the 2010 fiscal reform has, indeed, played a positive role in rallying the Baloch people, for it has provided positive incentives for the Baloch nationalist parties that support federalism to participate in political mediation and seek for interests of Balochistan through peaceful means, and thus accelerating the internal division of the nationalist

<sup>39</sup> Khan G., "Politics of Nationalism, Federalism, and Separatism: The Case of Balochistan in Pakistan," University of Westminster (2014).

movement and strengthening the cohesive force of the federal government. Pipes' research shows that any (political, economic and military) conciliatory action of the federal government will decrease the number of attacks in Balochistan, even those launched by separatist forces.<sup>40</sup>

## 5.6 COUNTERMEASURES AGAINST BALOCH SEPARATISM UNDER THE BACKGROUND OF CPEC

The 2010 fiscal reform is the first significant step to reverse the unfair inter-provincial distribution of fiscal resources. It also helps control the separatist tendency of the Baloch nationalists. However, its effect in redistributing resources among provinces is not big enough to narrow the gap of social and economic conditions between Balochistan and eastern provinces. Obviously, the demands of Baloch nationalists for fiscal reform will not stop from there.

Therefore, the federal government should seize the opportunity to introduce further fiscal measures, so as to ease the relationship between the federal government and the Baloch people, and minimize the security risks of armed attacks by the local separatist groups and the political risks of their demand for independence.

1. The federal government should not only equalize transfer payments of the divisible pool of taxes, but also the fiscal revenue capacities and public service costs of provincial governments.<sup>41</sup> Diversified distribution criteria have been adopted to distribute revenues of the divisible pool of taxes after the 2010 fiscal reform, but it is still not highly equalized. The indicator of population is referenced in the old way, the indicator of income generation/income collection is more favorable for Sindh and Punjab with more developed economy and stronger fiscal capacities; only the indicators of poverty/backwardness and inverse population density index take into account the poor socio-economic conditions and the low revenue and high expenditure caused by low population density of Balochistan to some extent, but these two indicators only weigh as low as

<sup>40</sup>Pipes G.D., "The Baloch-Islamabad Tensions: Problems of National Integration DTIC Document" (2010).

<sup>41</sup>Full fiscal equalization requires comprehensive consideration of the fiscal revenue capacity of local governments and the supply costs of providing public services similar to those in other regions. See Xie Yuhang and Chen Yongzheng, "The Impact of Transfer Payment Systems in Developed Countries on Local Finance and Public Services," *Finance and Economics*, no. 9 (2016): 64–76.

13 percent. The federal government should take the practices of fiscal equalization in developed countries as reference, introduce more indicators such as the revenue capacities and public service costs (e.g. transportation, health care and education) of provincial governments by calculating related tax bases and costs, to compensate for Balochistan's high expenditure costs (e.g. the transportation and communication costs caused by the scattered population, and the problem in public administration due to the lack of scale economy, etc.), given its socio-economic and geographical characteristics, and let it have a chance, at least in the aspect of fiscal resources, to provide the similar public services as other provinces do.

2. The federal government should decentralize taxation power in order to establish a new fiscal governance structure in which provincial governments are accountable to the local people. Earlier analysis has shown that, while the 2010 reform plan did call for devolving some of the fiscal spending power (fiscal duties and responsibilities) to provincial governments, it left the federal government's taxation power essentially unchanged. Although it led to greater provincial autonomy in fiscal spending, it also increased provincial deficit and made provincial governments more dependent on transfer payment from the federal government. According to studies on fiscal federalism, high dependence on transfer payment often leads to a lower degree of accountability of provincial governments to the local people, and is likely to give rise to soft budget constraints and excessive expansion of the size of government. In other words, provincial governments may exhibit fiscal irresponsibility and fail to translate spending into high-quality public services. Therefore, carefully calibrated decentralization of taxation power should go hand-in-hand with that of fiscal spending power. The high economic and political costs of tax collection would give, all provincial governments, including the government of Balochistan, an incentive to improve their performance and their relationship with both the local population and the federal government.

In addition, the Chinese government and enterprises as stakeholders can also support the socio-economic development of Balochistan.

1. Besides the US\$46 billion investment plan, the Chinese government can set up special funds for backward provinces along CPEC such as Balochistan, to help improve local conditions. The special fund is appropriated with specific usage, which can be determined by the Chinese government, the federal government and the provincial government together, for example, to be used for badly needed basic public services (employment training, etc).

2. Chinese companies are encouraged to invest more in Balochistan to improve the local social and economic conditions. Chinese companies should invest in the basic public service projects, such as education, clean water projects, and basic medical and health services. These investments can make up for the insufficient governmental effort and improve the living standards in Balochistan.

Just like the reform in 2010, these measures will increase the cost of splitting for the Baloch separatists, and make more ordinary people willing to stay within the federal framework, thus supporting the moderate nationalist parties. This will gradually reduce the space for the activities of nationalist and separatist forces, and bring peace and stability to Balochistan ultimately.



# Implications of Pakistani Dynastic Politics for the Construction of China-Pakistan Economic Corridor: Potential Risks and Policy Responses

*Ruoshui Jiao*

## 6.1 INTRODUCTION

As the flagship project of China's Belt and Road Initiative (BRI), the China-Pakistan Economic Corridor (CPEC) is given multiple expectations at the strategic level: the pioneering work of BRI, China's efforts to reshape Pakistan's national image, China's efforts to crack the Malacca dilemma and cope with the pressure of the West Pacific, and the outline of

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China's land power strategy.<sup>1</sup> Indeed, with a super-scale investment of US\$46 billion, CPEC is absolutely a milestone for both China and Pakistan. Pakistan is often likely to describe its friendship with China as "higher than the mountains and deeper than the sea". This fate-changing project is supposed to be a complete success in Pakistan. However, the reality is that the details of the CPEC, even the overall framework of CPEC have been the most hotly contested issues among Pakistan's political parties from the very beginning. The more exaggerated evolution is that except for the starting point at Khunjerab Pass and the finishing point at Gwadar Port, almost all the political parties had fabricated a different interpretation of CPEC each. Among which, the most typical and long-lasting dispute was over the western route or the eastern route. The local forces in Pakistan had made completely opposite plans for routes and details, some provinces even announced they would never let a single CPEC project launch in their provinces.<sup>2</sup> Obviously, CPEC is still facing a lot of structural risks. For instance, the Qassim coal-fired power plant, an energy flagship project of CPEC, has already started for more than one year, but the land use right is still not decided so far.<sup>3</sup> Not only that, even if the project is successfully completed and delivered, the import of coal, operation management, connection to the grid and other issues. There seem to be endless problems and challenges. It is worth noting that domestic dynastic politics and local political forces in Pakistan seem to have unimaginable problem-making capacities. If China fails to predict the potential risks well, the dispute over Qassim will neither be the first nor the last.

With the advancement of CPEC, similar problems continue to emerge in various forms, arousing extensive attention in the academic circle.<sup>4</sup> The Chinese domestic scholars, especially sociologists, have proposed many

<sup>1</sup>Gao Bai, "China-Pakistan Railway is the Key to China's Land Power Strategy," [www.guancha.cn](http://www.guancha.cn), (April 2015), [http://www.cbrc.com//www.guancha.cn/gaobai/2015\\_04\\_21\\_316648.shtml](http://www.cbrc.com//www.guancha.cn/gaobai/2015_04_21_316648.shtml).

<sup>2</sup>Liang Tong, "China-Pakistan Economic Corridor, When Will the Pilot Project of the Belt and Road Initiative be Really Launched," [www.guancha.cn](http://www.guancha.cn), (June 2015), [http://www.guancha.cn/liangtong/2015\\_06\\_03\\_321901\\_2.shtml](http://www.guancha.cn/liangtong/2015_06_03_321901_2.shtml).

<sup>3</sup>Hao Zhou, "Problem of Port Qassim of China-Pakistan Economic Corridor," *Caijing Magazine* (April 2017).

<sup>4</sup>Shi Guoqing, "Belt and Road Initiative: New Development Space for Sociology in China," Seminar on "Social Governance and Community Development" of Tsinghua University, December 31, 2016, <http://www.webaobo.com/index.php?m=article&f=view&cid=2284>.

countermeasures such as establishing a social risk assessment system, or enhancing the participation and sense of gain for countries and regions along the corridor, etc. It has important reference value in micro-details, but they still cannot solve the structural challenges faced by CPEC, because they have failed to consider the local political environment or the social structure encumbered by dynastic politics. However, the countermeasures and suggestions put forward from the international political level are faced with the trap of interfering in other countries internal affairs, and are infeasible to be carried out and are not feasible in practical operation.

Only by scientifically studying and judging the risk issues facing the construction of the CPEC, and identifying the key independent variables that affect it, can we be more comprehensive understand the causal mechanism of various problems in the CPEC, and put forward practical policy recommendations to minimize risks faced by CPEC construction and maximize the benefits of corridor construction. What, indeed, are the structural factors that affect CPEC? Taking the biggest dispute over the “West Line-East Line” as an example, the reasons given by all sides are varied, and behind them are manipulation and hype by western countries and India. Because of Pakistan’s national conditions and history, but in the final analysis, it’s all expression of local interests entrapped by dynastic politics. Due to Pakistan’s special national conditions and the influence of its founding history, Pakistan’s domestic Politics has followed the “local family political manipulation—democratic elections to power—the division and return of family political interests—the cycle of “re-consolidation of family political power”, this will become very clear when Pakistani politicians attack each other. The biggest opposition provinces such as Balochistan and Khyber-Pakhtunkhwa may put it in a mild way that what they really oppose is not CPEC, but turning CPEC into the local interests of Punjab, the home base of Prime Minister Sharif. That’s why they always criticize the dynastic politics of the three family members including Sharif, his brother Shahbaz Sharif who is the Chief Minister of Punjab, and his son Hamza Shahbaz, for they are seeking benefits from CPEC for their own zones of influence. And fierce the rhetoric is because Balochistan and Khyber Pakhtunkhwa are a minority in the central government, and it is difficult to influence the central government’s decision. The only way they can fight for their own interests is to put pressure on the Chinese side. In a word, all the social, environmental, legal, and religious issues are apparently tools of dynastic politics. If the countermeasures are taken only

towards these issues on the surface, the effect will be transient for sure. And it will be impossible to change the deep-rooted social and political structure in Pakistan. In other words, Pakistan's overall political and social ecology dynastic politics is the internal cause and the key independent variable, the others are just external causes and intermediate variables.

The only way to design policies with an overarching vision that can meet the challenges posed by dynastic politics in Pakistan is to have a good grasp of the basic mode of this kind of politics in Pakistan, and understand what its impact might be on CPEC and China's interests. At the same time, the political transformation of many countries along the "Belt and Road is" have the challenge of lagging political transformation, Pakistan is not an exception to dynastic politics. If CPEC as the pilot project failed to find an effective method to cope with it, there would certainly be more potential challenges and problems for BRI in the future.

## 6.2 DYNASTIC POLITICS AND PAKISTAN'S POLITICAL ECOLOGY

### 6.2.1 *The Formation and Operation Logic of Pakistani Dynastic Politics*

Pakistan was birthed directly by the ending of British colonization of the South Asian subcontinent, a process that was not marked by either political struggle or revolution. Since the country's founding, state apparatus has been in the control of politically seasoned families. Add to that interference from political forces in different countries at that time, Pakistan's dynastic politics were deliberately fomented and encouraged to grow. First, this is a legacy of the British colonial strategy to divide and rule. The British modus operandi was "rule the Punjabis, intimidate the Sindhis, gang up the Pushtun, and honor the Baloch". During Pakistan's fight for independence, the British created and nurtured separatist forces both inside and outside Pakistan to protect its vested interests. Secondly, under the continuing influence of long-standing local powers, religious sects and other factors, nationalist sympathizers and local ruling parties play an important role in Pakistan's political ecology. Pakistan has a population of about 200 million. There are a lot of political parties, but ordinary people are hardly participating in democratic politics. Actually, dynastic politics is controlling the social and economic development of the country entirely.

Those parties which have won in the election and become the ruling parties are in fact manipulated by dynastic politics, too. Without the support of dynastic politics, the political interests of the ruling parties will surely be damaged. And this makes dynastic politics a norm in Pakistan's political environment.

On the surface, Pakistan, where more than 95 percent of its residents believe in Islam, is an Islamic country. Religious identity could have been one of the foundations for the construction of national identity. But because of geographical, historical and cultural constraints, Pakistan is actually a multi-ethnic country made up of the Punjabi people, Sindhi people, Pathan (Pashtun) people and Baloch people. In Pakistan, people are more accustomed to referring to the people in the four provinces as Punjabi, Sindh, Bataan (Pashtun) and Luzhi according to the concept of region. Moreover, there are a number of minorities in Pakistan, too. For instance, the Kashmiri, Brahuis, Chitral and Gujarati, etc. Therefore, Pakistan has not established a unified sense of national identity and national belonging for a long time. The fragile balance between dynastic politics and local politics maintains the state governance structure for a long time and threatens the stability of state power and economic and social development from the perspective of the whole country, political families are fighting for both state power and relevant departments and exerting every effort to convert national interests into local interests. At the local level, it is embodied by several big families occupying and consolidating their spheres of influence who have formed their own vote warehouses, and continue to strengthen the influence of dynastic politics through benefit transmission and vote control. Besides, the traditional Sardar tribes still exist in Balochistan, making it an extra-legal place beyond the reach of the central government. While implementing CPEC, the Chinese and Pakistani central governments are carrying out cooperation at the state level. Since the Pakistani central government lacks credibility and coordination capacities, the national interests of Pakistan may be encumbered and utilized by local political groups, and the national interests of China may also be damaged after the shift of political power. Moreover, in Pakistan, the dispute over the unevenly distributed interests between the oppositions' dynastic politics and the local interest groups may cause huge risks for CPEC. Generally speaking, major political families that have national influence in Pakistan include the Punjab-based Nawaz Sharif family, the Sindh-based Bhutto Zardari family, the Brahmandagh Bugti family who leads the Baloch separatist forces and the Imran Khan family whose

Pakistan Tehrik-e-Insaf (PTI, Pakistan Movement for Justice) is also emerging in recent years. These political families are competing for political resources under the disguise of the democratic system. For example, Pakistan Muslim League Nawaz (PML-N) led by Sharif and Pakistan People's Party (PPP) led by Bhutto are the two biggest political parties with the longest history and strongest strength in Pakistan. In order to secure their votes, they scramble for national resources into their own zones of influence. Power struggles among them are fierce, and controlling state power is their common way to seek greater local interests. Once they are elected, they will greatly expand their sphere of influence and control the situation based on the local people's sentiment to protect their own interests, and strengthen their political and economic privileges with "big industrial aristocracy plus feudal landlord".

After years of power shifts and social disturbances, the Pakistani people are already aware of what these political families have done, but to protect themselves, they still have to support these local giants for ethnic, religious, and caste reasons. These political giants are controlling Pakistan's political and economic systems for their own families and interests. Even the national interests have never been the priority of Pakistan's politics, let alone the interests of CPEC for China and Pakistan or the provision of regional public security. Pakistan's complicated political environment has not been fundamentally changed even today. To some extent, stimulated by the huge interests behind the economic corridor, the fragile balance of the original family political group ecosystem will be broken, and the game between various forces around the China-Pakistan economic corridor will be more intense.

### *6.2.2 Prominent Challenges of Dynastic Politics to CPEC*

The widely recognized biggest risk for CPEC comes from the province of Balochistan, where the Sardari system and tribe structure has been preserved till today. It is the most typical form of traditional dynastic politics in modern Pakistan. Balochistan separatism has been conflicting since the founding of Pakistan and has been entangled for more than half a century. It is now the most serious political issue in Pakistan and the most prominent challenge for CPEC, too. The game between the political forces of Balochistan and the central government in the past four decades has vividly demonstrated the operational logic of the local dynastic politics, which helps us to grasp the possible risks of dynastic politics in the construction

of the Pakistan Economic Corridor. Ever since the age of Ali Bhutto (1971–1977) started, the central government has taken multiple measures to promote the development of Balochistan. Although Bhutto’s policy has been the positive evaluation of “Promote Balochistan’s socio-economic literature development on an unprecedented scale,<sup>5</sup> still caught in the trap of conspiracy theories. The central government’s plan to build roads and other infrastructures are interpreted as “to provide more conveniences for the military to control Balochistan and for the Punjabi people to plunder the Baloch people, and development is just an excuse for the central government to exploit Balochistan.”<sup>6</sup> During Zia Haque’s administration (1977–1988), its development policy tries to escape the insufficiency of the Bhutto policy, but it still cannot prevent the development project from becoming a “hypocritical essay”, the real beneficial one was the officials and developers in Punjab, but not the Baloch people. The local political forces asserted that the central government had implemented internal colonialism by political means, the Baloch people’s could not effectively participate in the decision-making of their province, for their opinions were not even asked; the exploitation of the central government was the true reason for Balochistan’s backwardness.<sup>7</sup> During Musharraf’s era (1999–2008), the development policy was called “settlement of the Punjabi people in Balochistan in the name of large-scale construction project”.<sup>8</sup> Some blamed that the development project didn’t provide any job or training opportunities for the locals. The developers from Punjab and Sindh who had made a fortune from trading land in Balochistan did not build schools and other social infrastructures as they had agreed. The government did not fulfill its promise to promote the economic and social development of Balochistan, and the rural areas of Balochistan were getting even poorer.<sup>9</sup>

<sup>5</sup> Rajsherr Jetly, “Baluch Ethnicity and Nationalism (1971–1981): An Assessment,” *Asian Ethnicity* 5, no. 1 (2004): 7–26.

<sup>6</sup> Urmila Phadnis, “Ethnicity and Nation-building in South Asia,” *New Delhi: Sage Publications*, 187, 177.

<sup>7</sup> Urmila Phadnis, “Ethnicity and Nation-building in SouthAsia,” *New Delhi: Sage Publications*, 180.

<sup>8</sup> Muhammad Ijaz Laifand Muhammad Amir Hamza, “Ethnic Nationalism in Pakistan: A Case Study of Baloch Nationalism during Musharraf Regime,” *Pakistan Vision* 10, no. 1: 49–81.

<sup>9</sup> Quratulain Siddiqui, “Understanding Balochistan,” <http://news.dawn.com/wps/wcm/connect/dawn-content-library/dawn/news/pakistan/balochistan/Understanding-Balochistan-qs>.

It can be seen that in regard to the intervention of external development resources and forces, the province of Balochistan had already formed a set of widely spread rhetoric. In this discourse system, the Baluchistan nationalists a priori judge the various government policies as violations and control are reported to be prevented, faulty, resisted and resisted.<sup>10</sup> The government would face an accusation of internal oppression and inequality if it did not develop the province and would be interpreted as conspiracy and internal colonialism if it did develop the province. These two seemingly contradictory discourse systems are in Balochistan form a parallel logic that continued to replicate and expand its influence and became a very representative ideological system of intensified family political struggle in Pakistan. We have every reason to believe that tribal leaders and local political tycoons will fully copy this kind of criticizing rhetoric. Their criticizing and questioning about CPEC can already be seen in local media reports. It is even true that the more effectively CPEC is advancing, the more afraid of their vested interests being affected the local political families will be, and the stronger their opposition will be. In this case, China could be the direct target of attacks by local political families in Balochistan.

### 6.2.3 *Instabilities of CPEC Cooperation Caused by Dynastic Politics*

So far, to implement CPEC under such a political environment, China can only cooperate with the ruling party's government of Pakistan. However, the ruling party's government which is every so often the central government is also encumbered by local dynastic politics. It faces fundamental conflicts and challenges in balancing its own interests and the overall strategic arrangement. Local political groups had already had critical disputes and conflicts over CPEC even before its construction was started. The core issue was how to distribute the practical fruit of CPEC among different local political groups. The ruling party of Prime Minister Sharif insisted on the leverage role of CPEC across the country which was supposed to take the relatively developed eastern region as a fulcrum to leverage more rapid development nationwide. Other local forces believe that Sharif's policy will turn the China-Pakistan Corridor into a China-Punjab Corridor,

<sup>10</sup>Qian Xuemei, "An Analysis of Baluchistan Nationalism in Pakistan," *Journal of World Peoples Studies*, no. 3 (2013).

so it is strong. Require inter-provincial “balance role” and propose that “corrective care” should be given to the development of backward areas in the layout of economic projects to avoid the construction of the Pakistan Economic Corridor has further exacerbated the already prominent gap between the rich and the poor in Pakistan. The opinions of both sides were reasonable. If the central government were very good at balancing different regions, the dispute would turn into a problem of whether to allow some people to get rich first or allow all the people to get rich together and what the focus of each phase would be. But under a political environment characterized by the fierce game of dynastic politics, any choice would be judged as a conspiracy or decision based on self-interest. In order to prove to the public that the Sharif family had already controlled CPEC and even operated the project by private means, the opposition parties would not waste any chance to fight for their own interests and retaliate against the Sharif family. In response, the Sharif family also vigorously suppressed the opposition parties so as to consolidate its once-in-a-lifetime ruling position. During a parade protesting against the priority of the eastern route in planning and construction of CPEC in front of the Pakistani Parliament Building on May 12, 2016, the protesters even shouted out “We want China-Pakistan friendship, but not China-Punjab friendship”. Sharif intended to make Punjab province the privileged and biggest beneficiary of CPEC, which was firmly opposed by Balochistan and Khyber-Pakhtunkhwa provinces. Balochistan even claimed that it would burn the oil and gas within its provincial territory for nothing rather than let it flow into Punjab to boost the economic growth there. It would not allow its gap of development compared with Punjab to grow larger, hence staying totally opposed to the construction of CPEC. Brahamdagh Bugti, the leader of the Baloch separatist forces, also said directly that the rulers of Punjab could do whatever they wanted, but Balochistan would never allow China and Punjab to take advantage of Balochistan or its land and resources for their own benefits. Khyber-Pakhtunkhwa also put pressure on CPEC by bargaining in the name of fighting terrorism.

The China-Pakistan Economic Corridor, which began construction during the dispute, has made many major adjustments in design, but it is still difficult to pacify Pakistan. Scholars specializing in Pakistan’s politics reminded that the protest against CPEC by domestic opposition parties might reach its peak before the 2017 election. Therefore, it was necessary to get ready for monitoring public opinions as well as emergency response. The opposition parties well understood that CPEC was a historical



opportunity to change Pakistan's fate, and the chance of the political game would only exist when the achievements had not yet been made; once the Sharif government successfully implemented CPEC and got re-elected as prime minister in 2018, his ruling position would be further consolidated and there would be hardly any chance left for the opposition parties to win again. A source specifically mentioned that Punjab was the home base for the Sharif family, Sharif had promised to complete the tap water project for local households by 2017 in order to secure his votes there. This project would solve the problem of water safety which had obsessed the local residents for a long time, and help lock nearly 90 million votes in Sharif's hands. But when the author interviewed young students from Punjab several times, they all said they'd never heard of the tap water project, this was totally fake news of the media controlled by Sharif. Pakistan's economic growth and infrastructure construction hardly got any progress during Sharif's administration, they unanimously stated that they would vote for Imran Khan in the 2018 general election because he was not only a popular sports star in the Cricket Hall of Fame, but also an innocent resume as the opposition party member. Besides, he was also good at using the widespread dissatisfaction due to the high unemployment rate of young people. What had happened in the US elections was very like to repeat in the 2018 election of Pakistan. Obama was elected with the support of the young people, and Trump who had no political experience was elected to the White House by American voters in 2016. This instability in the election judges, reflects the intricacies of Pakistan's Mixed family political ecology, also an indirect embodiment of the game between conservative and youth-dominated new forces in Pakistan.

Another important source for predicting public opinions lies in studies on social sciences. During the author's visit to 6 universities in Islamabad and Punjab, almost all of the scholars of social sciences I met there believed there were no risks with CPEC. In English slang: TOO GOOD TO BE TRUE. Even if they say there's a risk, they would attribute the reason to external factors, especially foreign relations with India and the US. Overall, in order to seek greater benefits in the construction of the China-Pakistan Economic Corridor, the Pakistani academic circle and the government are highly consistent, and it may deliberately avoid potential risk factors and adopt the attitude of getting the project first, intentionally amplify positive factors, so that the medium and long-term risks of the construction of the CPEC are greatly underestimated and the potential risks are virtually ignored and disregard.

### 6.3 RISKS AND CHALLENGES OF DYNASTIC POLITICS TO THE CONSTRUCTION OF CPEC

Dynastic politics in Pakistan often used democracy as a tool to attract more votes. The reason for Sharif to exaggerate the benefits of CPEC was to overstate his political contribution, which had been frequently reported by the media controlled by his family. During my visit there, some Pakistani scholars even said “with such rapid economic growth, China will soon become the largest economy in the world, and it will be fine for Pakistan to be the second-largest economy then.” And for many projects that China participates in, under the guidance of dynastic politics Interest localization, Pakistan’s specific partners have a certain mentality of dependence or even hold-up. For instance, some Pakistani colleges were very interested in cooperating with Chinese colleges; however, they asked the Chinese side to bear the expenses in full even when organizing international academic conferences together. Their reason sounded more ridiculous: “as CPEC is to be built by China, the expenses for organizing all the related conferences should be on the Chinese side, too.” Actually, the Pakistani side was extremely shrewd to grasp the vital part of Chinese overseas projects. Taking advantage of the determination of the Chinese government to build CPEC, some Pakistani cooperation partners tried to gain more supports from China by formalist means, which led to a distortion of information for decision-making. A more serious problem was that some projects even turned out to be tools for Pakistani powerful families to seek private interests as driven by dynastic politics. This would not only deviate from the original intention of China to propose CPEC, but also create enormous hidden hazards for China’s FDI in Pakistan after regular shifts of administrations in the future.<sup>11</sup>

First of all, the high-level route leads to the lack of local participation and uneven benefit sharing in project construction CPEC was planned by the central governments of both countries. However, the intricate political forces in Pakistan, especially the crucial strategic provinces—The separatist forces in Balochistan have become one of the most severe challenges to the implementation of this strategy. In comparison with mature and stable exchanges between the central governments of both countries, the negotiation and coordination mechanism between Chinese government and

<sup>11</sup>Ye Hailin, “Minefields of Pakistan’s Top Politics,” *The Paper* (March 2015), [http://www.thepaper.cn/newsDetail\\_forward\\_1311745](http://www.thepaper.cn/newsDetail_forward_1311745).

Pakistani local political forces should be improved immediately. Accounting for a large proportion of the central government and military departments in Pakistan, the Punjabi people are the largest ethnic group in Pakistan (approximately 63 percent of the total population), and also the people who benefit the most from various policies. On the contrary, for Balochistan, the poorest and backward province, the local people are dissatisfied with the excessive power of the central government and believe that the rights and interests of the province are not respected and protected, feeling strongly of being deprived. For example, most of the gains from developing local natural resources had gone to the central government and Punjab province with greater political influence. In addition, many large-scale CPEC projects were fully controlled by the federal government, this leads to the lack of decision-making power and discourse power of local governments. As the domestic political structure was difficult to change, local forces would create various excuses to protest against CPEC. The goal of most local people in the Balochistan province was to fight for greater autonomy right. However, some separatist organizations took the chance to advocate for separatism, and some even organized terrorist attacks on foreign workers of aided construction projects within the province. A Balochistan scholar directly pointed out that CPEC would make Sharif a competent dictator, and Punjab would become the largest internal colonialist force in Pakistan by absorbing national resources through CPEC. Around Karachi, the capital of Sindh Province, it was also common to see that local land was mostly occupied by non-Sindh people. In early May 2016, news appeared in Chinese online media, reporting that some people in Pakistan have protested against the China-Pakistan economy Corridor parade. The organizer of the march was the Jeay Sindh MuttahidaMahaz. Similarly, another attack against Chinese people in Karachi was reported at the end of May, and the attacker was the “Sindhudesh Revolutionary Party”.<sup>12</sup> Local organizations including Jeay Sindh MuttahidaMahaz, Sindhudesh Revolutionary Party and Baloch Republican Party had organized endless small-scale anti-China protests. There were enormous potential risks for CPEC behind the seemingly subtle change in the attitude of the local political forces. If these risks were not managed or controlled in time and in a proper way, coupled with the impetus of complicated nationalist sentiments of the local people, all the

<sup>12</sup>Lu Yang, “Fierce Struggle Behind the China-Pakistan Economic Corridor,” [hexun.com](http://opinion.hexun.com/2016-06-28/184621281.html) (June 2016), <http://opinion.hexun.com/2016-06-28/184621281.html>.

objective conflicts and problems would get escalated at specific time points and might become a catalyst to ignite a large-scale anti-CPEC movement.

The dilemma is that opponents of the construction of the China-Pakistan Economic Corridor will compete in various ways take the investment projects and preferential measures from China, but the method of operation is still consistent to safeguard dynastic politics and local interests mainly, at the same time creating all kinds of troubles for the current Prime Minister Sharif, and doing everything possible to weaken the influence of the Sharif family. There would be potential risks for China's interests in smoothly implementing CPEC no matter which trend prevailed. However, risks could not frighten China, either. CPEC is the first stop for BRI to go abroad, and Pakistan is also a precious all-weather strategic partner of China. Risks and challenges might be on the road, but there will still be chances for mediation and rehabilitation. At the moment, China should figure out how to seize this valuable opportunity and make all-around research and assessment of risks by social and academic experts, so as to get prepared for implementing other Chinese projects in other foreign countries in the next stage.

Secondly, the path dependence of dynastic politics leads to the lack of communication mechanisms between China and the opposition. China-Pakistan Economic Corridor is under construction the single-line connection between the two governments' high-level governments, leading to the control of many projects by the central government, was which gave the opposition parties an excuse to attack and weaken the ruling force, and even to protest CPEC in the first place. In early October 2016, the Chinese Ambassador to Pakistan Sun Weidong met with Pakistani opposition leader and Pakistan Tehrik-e-Insaf (PTI) Chairman Imran Khan, hoping the latter to ensure that its protest parade against the government to be launched on November 2nd would not affect its support for CPEC. The media described this meeting as rare, indicating that China was too dependent on government diplomacy in the past, especially at the central government level. Now, it was crucial to build up negotiation channels with the local family political forces and the opposition parties immediately. This also reflected, to a certain extent, the urgency of building negotiation channels between the two peoples during the implementation of BRI, as demanded by President Xi Jinping.

Thirdly, the high-level negotiation also caused the risk for an organized and morbid situation of bureaucracy in which everyone was accountable but everyone was irresponsible in the short term, as well as huge potential

risks for developing CPEC in the long term. According to a source who had participated in the front-line work of CPEC for a long time, some CPEC projects were actually contracted. When large-scale enterprises won the projects, they would divide them into smaller companies through contracts. The completion of projects was delayed correspondingly, and risks were increased, too. It is more noted that many companies are the first to undertake overseas construction projects, there is no long-term planning for the future overseas projects, even holding “fire a shot and then change a place” and “if something goes wrong, the country will solve it.” Some of the Chinese enterprises were regarded as scam companies by the local people because of their way and default on wage payments as well as excessive working hours, seriously damaging the images of Chinese enterprises and CPEC. Enterprises were the main actor of the market, and projects were of certain construction cycles. The nature of the business operation was to do everything possible to efficiently complete projects and make profits, so it was understandable for them to run business by high-level negotiations. Besides, since Chinese enterprises were not familiar with the complicated political environment, they still followed the unspoken rules of domestic projects in China, and even sought to promote the projects by high-level negotiations so as to realize short-term interests of their own. They purposely neglected the national interests only to avoid extra costs and risks with the aim of achieving self-interests maximum during the construction period of CPEC. Meanwhile, in order to accelerate the strategic dividends of CPEC and consolidate its ruling position, the Sharif government attempted to boost CPEC by various means including taking shortcuts, arousing criticisms by the opposition parties and leaving potential risks and challenges for the operation of CPEC in the future. For the Gwadar Port project in Balochistan, technical jobs were occupied mostly by the Punjabi people or other ethnic groups, and hardly by the Baluchis people. The Chinese enterprises and the Pakistani central government had reached a consensus on the one hand, but driven by local interests and political competitions, the opposition parties were looking for loopholes and problems in aspects of laws, policies, environmental protection and employment of CPEC on the other hand.

In addition, the high-level route leads to the lack of systematic and comprehensive research and evaluation. The insufficient coordination mechanism would influence the effects of CPEC at present and in the future. CPEC is an FDI project with a relatively long construction period. About 40,000 Chinese personnel are participating in implementing CPEC

in an environment full of policy, legal and cultural challenges. The Chinese enterprises participating in CPEC are large-scale state-owned enterprises and some private enterprises. While operating abroad, they should not only be regulated by domestic administrations, but also negotiate and coordinate with the Pakistani side. As a result, the lack of transition and coordination are both exist at the same time. The Chinese enterprises are familiar with the operating mode which is from top to bottom, but are not familiar with Pakistan's multiple operating modes, especially the mode which is from the bottom top.

Overseas-aided construction projects carried out by Europe, the United States and Japan have already formed a set of effective social evaluation systems and methods. However, due to the differences in ideology and human rights awareness, China could not directly use its assessment methods. In order to ensure the safety of CPEC, it is necessary to develop a set of governance systems of China's own by referencing western overall ideas as well as details. In the past, Chinese foreign aided construction projects were generally small-scale and uncomplicated. Currently, Chinese coordinating systems for overseas activities are still forming. Therefore, the problem of fragmented governance that each entity only cares about its own business is prominent. In order to avoid risks, the relevant departments and enterprises have a strong motive to seek favorable Pakistani partners through high-level negotiations. Therefore, they get easily involved in the complicated political disputes in Pakistan, which also brings potential risks for the overall interests and strategy of China. So it is urgent to establish a multi-dimensional dialogue and coordination system, especially negotiation channels with the opposition parties, by more flexible means of social organizations, non-governmental exchanges and thinks tanks.

#### 6.4 RECOMMENDED POLICIES

Frankly speaking, Chinese academic studies on underdeveloped countries has not been deep enough for a long time, and cannot meet the needs of developing BRI. Although there are plenty of studies on CPEC, the production of effective knowledge still remains insufficient. Except for the completed projects of CPEC, the biggest achievement of this long-term cooperation with our all-weather partner should be the full assessment of actual and potential risks of overseas projects, rich practical experiences for the BRI projects to be implemented in other countries in the future, and formation of supporting policy and assessment system. It is no

exaggeration to say that if China can develop a set of relatively complete governance systems for overseas activities in Pakistan, its value for China under the context of globalization will be much higher than the current US\$40 billion.

#### *6.4.1 Establish a Complete Social Risk Assessment System for CPEC*

First, Establishing a coordinated mechanism for social science research in the China-Pakistan Economic Corridor. The existing research on the construction of the CPEC is carried out in disciplines, fields, and projects, but lacks top-level design and overall design to solve the problem of fragmented governance, we should vigorously promote in-depth cooperation between college think-tanks of both countries, and overcome the constraint of the so-called “diplomacy is no small matter” and the fragmented management by different departments. Avoiding sensitive issues and risks is no different than taking the ostrich policy which is similar to the Emperor’s New Suit. We should conduct studies on sensitive issues of CPEC skillfully, collect information from various channels, and provide feasible and useful results for the decision-making of the government. For major and urgent issues, we should provide related warnings as early as possible. Secondly, to establish a sound research evaluation system, to change the current situation that there are a lot of research results but little is useful. Besides the feasibility assessment and social stability and risk assessment, we should also establish a whole-process tracing assessment system for large-scale projects to collect legal, cultural, religious, social, economic, environmental, safety, and health information of projects in an all-around way. For important projects, long-term tracing research and assessment systems should be developed to provide effective support for future decision-making and management.

#### *6.4.2 Establish an Inter-provincial Exchange Platform for CPEC to Hedge the Negative Impact of Dynastic Politics*

Although the dynastic politics in Pakistan is rather complicated, for CPEC, the most crucial places are Balochistan and Khyber-Pakhtunkhwa provinces. At present, relevant Chinese provinces should first establish an inter-provincial exchange platform with these two Pakistani provinces, setting

up a good model, and gradually hedging the negative impact of dynastic politics on CPEC. Besides, we should establish and improve a negotiation platform with local political forces in Pakistan, especially the stakeholders with whom the central government is inconvenient to directly negotiate, to make up for the insufficient coordination in implementing CEPC. This platform can be first built among provinces, and then expand to other spheres including colleges, think tanks, social organizations, and chambers of commerce, forming a multi-level social exchange system supplementary to both central governments. China should actively communicate with the local political forces and grassroots people in Pakistan to effectively respond to the potential risks caused by the instability of Pakistan's politics, making full use of a multi-channel platform of closer people-to-people ties and policy coordination, to gain social supports for road connectivity, unimpeded trade, and currency convertibility.

Khyber-Pakhtunkhwa province and China's Xinjiang Uyghur Autonomous Region established a relationship of friendly provinces in 2009. However, at that time, exchanges at the provincial level were enough neither to meet the needs of BRI, nor to make up for the insufficiency of exchanges at the central government level. In regard to key issues, exchanges at the provincial level failed to form supplementary strategies for the central governments, and could not reduce risks and maximize the benefits of cooperation through CPEC. Therefore, a new partnership should be designed on this basis. The cooperation between Xinjiang and Khyber-Pakhtunkhwa can be considered as a start point for jointly developing the border zone. Strategic benefits should be given to the source area of CPEC through preferential policies. This will reduce local terrorist activities significantly in the short run, fighting terrorism radically. At the same time, multi-level exchanges with local political forces in Khyber-Pakhtunkhwa should also be established so as to grasp the initiative of cooperation in our hands.

The key problem in Balochistan is the lack of professional and technical staff, leading to insufficient benefits for local people from the industrial development driven by Gwadar Port. It is suggested that China's Gansu province establish an inter-provincial friendship with Balochistan. On the one hand, there are a lot of Muslims living in Gansu, and the management of religious issues is mature there, providing feasibility of developing inter-provincial religious and cultural exchanges. The developing mode of Muslim secular society is a positive reference for solving problems of tribal



society of Balochistan, because of the same religious origin. On the other hand, Gansu has strong industrial enterprises specialized in construction, roads and bridges, and colleges including Lanzhou University which has long-term exchanges and rich experiences in education for international students and vocational skills training with universities in Central Asia and South Asia. Such exchanges can provide all-around training and technical cooperation of professional skills, commerce, and logistics, internet, halal industry, etc, for the middle class in Balochistan. Without affecting the local tribe's power in the case of interest, starting from multiple levels of religion, culture, technology, and economy, to consolidate the construction of local people in the CPEC the sense of gain, to create a safe and effective social public opinion foundation.

#### *6.4.3 To Cultivate a Reliable, Useful, Trusted Overseas Activity Talent Team*

China has carried out a scheme of 10,000 overseas students for BRI, which not only greatly expands the positive influence among the young people in countries along the Belt and Road, but also becomes medium and long term resource and support for closer people-to-people ties. Going out is equally important as bringing in. Some relevant departments prefer to not deal with sensitive issues and neglect the crucial role of Muslim students in BRI, and the overall national interests are affected accordingly by these departments for their interests. So far, in Pakistan, there are nearly 1000 overseas Chinese students, most of them are coming from Gansu, Ningxia, Qinghai, Yunan and Henan provinces. Currently, about 700 students are studying at International Islamic University, Islamabad, and more than 200 are studying at the National University of Modern Languages. Most of these international students are proficient in English, Urdu, Arabic Rabo language and majors are widely distributed, which allows this large-scale group to have sufficient opportunities to contact all parties in Pakistan. During the construction of CPEC, the international students participated deeply through translation, project management, and technical coordination. Accumulated a lot of practical work experience in project construction and operation, experience among our partners of BRI, the number of Islamic countries is more than 30, with about 22 countries speaking Arabic. Besides, Urdu is also the main language that covers the Indian subcontinent. So as to superior human resources, these students

can play a critical role in implementing CEPC. If we can guide them with patriotism and exert their talents, the Chinese students studying in Pakistan will grow into reliable, competent, and trustworthy talents for overseas activities. They will definitely make their contributions to CPEC and bilateral cultural exchanges and mutual trust as well.

#### *6.4.4 Build a Carrier and Platform for People-to-People Connectivity*

A multi-level and multi-dimensional system of closer people-to-people ties is the most effective way to hedge the risks of high-level negotiation, and also a weakness of the current implementation of CPEC. Shortly, we need to innovate in the following aspects:

First, social organizations should play an active role in fulfilling the strategy of closer people-to-people ties. China has launched the cultural going-out strategy by means of establishing Confucius Institutes in foreign countries, etc. However, it still cannot meet the huge needs of CPEC. Meanwhile, going out also requires close and multi-level cooperation among the government, the market, and the entire society. Chinese students in Pakistan based on the “China-Pakistan Education Social organization carriers such as “Cultural Center” provide Chinese language education and skills training for Pakistani companies and people, and provide Chinese companies with Provide Urdu language learning, policy and legal consultation, understanding of local folk culture and other aspects, with greater flexibility. As a useful supplement to the official cultural exchange channels, this kind of non-government exchange meets the social needs more precisely during the implementation of CPEC. By referencing the mature experiences in supporting social organizations in western countries, we can develop a number of overseas social and cultural organizations as platforms with our own domestic social governance and innovation experiences, to guide social forces to participate in fulfilling the hedging strategy in Pakistan together with western social organizations. This can not only actively promote closer people-to-people ties between China and Pakistan through non-government exchanges, but also reduce or even eliminate the risks for CPEC in multiple ways. Secondly, enterprises should play an active role in fulfilling the strategy of closer people-to-people ties. A large number of construction projects in the CPEC should establish cooperative relations with local private enterprises, by providing a large

number of jobs enhance the sense of participation and profit of the local people, and plans to implement employment skills upgrading programs for the workforce, sense laying a firm human resource foundation for the Chinese enterprises to go out and organize overseas activities and a stable economic foundation for social exchanges as well.

All in all, the challenges and risks facing the CPEC in the near term need to be studied scientifically and carefully. The rich experience of the CPEC should inform the construction of a scientific and sound overseas governance policy system for China's "going global" initiative. It will offer lessons beneficial to the smooth implementation of the "Belt and Road" initiative, facilitate the modernization of the national governance system and strengthen our governance capacity, and boost China's standing in global political and economic governance.



# Research on the Industry Spatial Layout of China-Pakistan Economic Corridor

*Qingyuan Tang*

## 7.1 TOPICS IN THIS CHAPTER

The essence of CPEC is the reorganization and redistribution of Pakistan's domestic production factors, which is a kind of restructuring of the country's existing industry spatial layout. Such large-scale adjustment and refactoring of production factors are of great significance on Pakistan's industry spatial layout, hence the interests of all concerned parties must be taken into account. Meanwhile, the impact of terrorism cannot be ignored since Pakistan is at the periphery of the hotbed of international terrorism, the occasional terrorist attacks have become the primary threat to the country's attraction of foreign investment. The western provinces of Balochistan and Khyber-Pakhtunkhwa, in particular, are the epicenter of

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terrorism in Pakistan. Statistics show that 73 percent of the country's terrorist attacks in 2015 took place in these two provinces. Terrorism has made the restructuring of Pakistan's industry spatial layout more complicated. Given this, whether China and Pakistan can achieve their own strategic goals through the construction of CPEC is decided by the outcome of combating terrorism.

In this chapter, the author interprets CPEC from the perspective of Pakistan's industry spatial layout and offers suggestions for competent authorities, attempting to help CPEC projects maximize their return on investment (ROI).

## 7.2 CONTRADICTIONS WITH TRADITIONAL LOCATION THEORY

As the theoretical basis for the current research on optimization of industry layout, location theory studies the spatial selection of human activities and the organization of human activities in that space. To put it simply, it is a kind of optimality theory on the spatial selection of human activities.<sup>1</sup> In a given area, the allocation of production factors must be optimized allocation of resources based on location theory, with cost factor, market factor and behavior factor etc, all playing an important role in affecting industry layout. The industry spatial layout of CPEC is no exception from the point of view of maximizing economic benefits, but it has particularity relatively to each school of traditional location theory (i.e., cost school, market school, and behavior school).

### 7.2.1 *Cost School*

As the trailblazer of location theory, the cost school holds that the spatial layout of any economic activity must be able to minimize costs, which is the basis for determining the location of businesses. The cost school, with the core idea of minimizing transportation cost, is represented by Weber's theory of the location of industries. According to Weber, the process of industrial production is mainly divided into three key links, namely production, circulation and consumption. By introducing the concept of location, he explains the reasons for the large-scale agglomeration of

<sup>1</sup>Qian Wei, "Analysis and Evaluation of the Three University Schools of Location Theory", *Science and Technology Entrepreneurship Monthly*, no. 2 (2006): 179-180.

industries and population during the period of industrial upswing, arguing that the theory of the location of industries only needs to measure three impact factors, namely transportation cost, labor cost and agglomeration benefit. When choosing the best location of industries, the relationship among the three impact factors must be balanced. In other words, the best location of industries is the one with minimum costs and maximum benefits.

According to the way of thinking of the cost school, when China and Pakistan are looking for CPEC's industry spatial layout with the minimum costs, the two provinces of Punjab and Sindh in eastern Pakistan are undoubtedly the best choices. With superior natural conditions, a large population, convenient transportation, and all sorts of supporting enterprises, these two provinces are ideal locations of industries with the lowest costs as endorsed by Weber. However, the reality in Pakistan, namely the unbalanced regional economic development, must also be taken into account when choosing locations for CPEC projects. If the backward and isolate western provinces continue to be ignored, the economic gap between east and west Pakistan will further widen. As a unified country made up of four major provinces resided by four large ethnic groups, Pakistan has all along been plagued by acute contradictions among ethnic groups; therefore, the industry spatial layout simply based on Weber's theory may eventually lead to domestic unrest and even national secession.

### 7.2.2 *Market School*

After Weber's theory was proposed, major industrial countries started the trend of urbanization, giving rise to a hierarchy between cities which have gradually occupied an important position in the entire socio-economy. Cities, especially large-sized ones, are absolutely at the center of the hierarchy and also developed into the hubs of industries, commerce, services and transportation. Christaller's central place theory emerged against this background. According to him, under the central place system dictated by marketing principle, transportation principle and administrative principle, the central place network, which possesses diverse market structures, is arranged strictly in the hierarchical order of central places and market areas. In order to maximize their economic benefits, producers always try to get access to the largest market area and keep away from other producers, while consumers like to go shopping or get services in the nearest central place to save travel expenses.

According to the above viewpoint, the best location for CPEC's industry spatial layout is cities, especially large-sized ones. A city is a place where all kinds of industries are highly concentrated, and industry clusters are favorable conditions for increasing returns to industry scale and for gathering of population and resources, thereby raising the use efficiency of labor, capital and other factors and quickening their flow among enterprises, as well as promoting the expansion and development of industries. Considering this, the large cities in eastern Pakistan, such as Karachi and Lahore, are ideal sites for CPEC projects. The two cities, each with a population of more than ten million, have developed into a city cluster in the eastern region. In contrast, western Pakistan has no central cities, let alone city clusters. Even Peshawar—the largest western city with a population accounting for a quarter of western Pakistan's total population—cannot be counted as a central city. Moreover, due to a low urbanization rate, western Pakistan is mainly made up of impoverished rural areas. If things go on like this, the economic gap between eastern and western regions will further widen, and such gap between urban and rural areas may enlarge dramatically. What's worse, the vast rural areas in the west are habitats of tribal groups. The chronic economic backwardness has made tribal people easily deluded by extreme religionism, laying hidden dangers for the spread of terrorism, which may eventually undermine the construction of CPEC.

### 7.2.3 *Behavior School*

The cost and market schools of location theory regard the subjects of location layout as brokers who are eager to maximize profits or minimize costs through location layout. To this end, economic actors must have complete control of all sorts of information about the surrounding environment, but in reality, it is impossible for people to obtain such information fully and completely, hence their location selection is usually a subjective judgment made on the basis of available but incomplete information. Therefore, human subjective factors began to draw more and more attention and give rise to the behavior school of location theory. The American scholar Praed, a representative figure of the behavior school, holds that location selection is decided by economic actors on the basis of available information. Whether their decisions are reasonable or not mainly depends on the amount of available information or on their abilities to use such information.

Supposing that the layout of CPEC projects was to be carried out according to the amount of information owned by decision makers and their abilities to use that information, then eastern Pakistan would be a candidate much more qualified than its western counterpart. Those with power in Pakistan usually come from certain powerful families in the two eastern provinces, no wonder both the Sharif administration and the Bhutto administration defend the interests of the east robustly, making the western provinces lack of discourse power at the central decision-making level increasingly marginalized. Even more worry are the entrenched separatist forces in the west, they have been holding grudge against the federal government for unfair resource allocation policies. Pakistan cannot let the current situation go on like this, because Gwadar Port, which is located in the western Baluchistan Province, is of vital importance for promoting the construction of CPEC—a critical link in the realization of Pakistan and China’s national strategies.

#### 7.2.4 *Comments on Traditional Location Theory*

By analyzing the thoughts of various schools of location theory, it can be seen that industry spatial layout is a key issue concerning the stable and sustainable development of regional economy, politics, and society. But the traditional location theory only values the industry layout, which is conducive to economic benefits, insisting that economic benefits should be the evaluation criterion of optimal industry spatial layout, and optimal industry spatial layout must be able to maximize economic benefits. In fact, it is a one-sided understanding of industry spatial layout and a narrow-minded evaluation criterion.

Poverty breeds terrorism, particularly in countries like Pakistan where there are complex contradictions between ethnic groups, fierce factional struggles, a large economic gap between eastern and western regions and between urban and rural areas, and serious separatist tendencies. So, it is far from enough to determine industry spatial layout of CPEC only from economic consideration. The overall national strategy should always precede over the economic factors, which is the prerequisite for CPEC to help realize China and Pakistan’s national strategies. Otherwise, Pakistan can only see exacerbated regional economic imbalance, political turbulence and more rampant terrorism, which will eventually threaten the construction of CPEC and the realization of the two countries’ strategic goals. In short, regarding the industry spatial layout of CPEC, more



consideration should be given to the national strategies of China and Pakistan, which is the only way that promotes the construction and sustainable development of CPEC, even though it deviates from the traditional location theory.

### 7.3 CHARACTERISTICS OF PAKISTAN'S EXISTING INDUSTRY SPATIAL LAYOUT

The existing industry spatial layout of Pakistan is mainly economic oriented, which caters to the requirements of the traditional location theory. On the whole, the industries in Pakistan are more in the east but less in the west, strong in the south but weak in the north, hence enlarging the economic development gap between regions. Eastern Pakistan, covering only a quarter of the country's total land area, accommodates a variety of industries with GDP accounting for about 80 percent of the country's total. But in the western region there is scarce distribution of industries and a small proportion of GDP in the country's total (less than 20 percent), regardless of a vast territory occupying three quarters of Pakistan's land.

Although Pakistan is the twenty-fifth largest economy in the world, its industry foundation remains fragile, its industry category is not yet complete, and its industries and enterprises are mostly small-scale. The economy of Pakistan is dominated by agriculture and service industry, with the former accounting for about 24 percent of the country's GDP and the latter accounting for 53 percent. In addition, Pakistan's service industry is characterized by low-end wholesale and retail, and industrial sector contributes only about 20 percent of the country's GDP.

In terms of industrial output value, Punjab ranks first in Pakistan, accounting for 48 percent of the country's gross industrial output value, followed by Sindh with a share of 41 percent, so the two provinces represent a combined share of nearly 90 percent. By contrast, the provinces of Khyber-Pakhtunkhwa and Baluchistan, both in western Pakistan, altogether occupy a tiny share of 10 percent. Regarding the industrial output value of cities, Karachi in Sindh is far ahead of other cities with a share of 26 percent of Pakistan's gross industrial output value, followed by Lahore in Punjab, accounting for 7.4 percent; and Faisalabad, a textile city in Punjab, comes next with a share of 6.6 percent. These three cities, with a combined share of about 40 percent of Pakistan's gross industrial output value, all belong to the eastern developed provinces.

In terms of major industries in Pakistan, most of the textile, leather, iron and steel industries are distributed in the industrial parks of varying sizes. Pakistan now has seventy-four major industrial parks which are situated in Sindh (twenty-eight), Punjab (twenty-seven), Khyber-Pakhtunkhwa (twelve) and Balochistan (seven), namely 74 percent of the country's industrial parks are concentrated in eastern provinces. As for the time when these industrial parks were built, those in the east are generally fore-runners, with the first batch being built as early as the 1950s. And the eastern industrial parks are much larger than their western counterparts. A typical example is the Karachi Industrial Park, covering an area of 4,460 acres, is the largest one in Sindh. In western Pakistan, the average area of industrial parks are no more than one hundred acres. In spite of this, the industrial parks in both eastern and western provinces have a common feature, namely all of them are close to surrounding large cities.

### *7.3.1 Textile Industry: Concentrated in Certain Eastern Textile Cities, and Scattered in a Handful of Western Central Cities*

Pakistan is the fifth largest cotton producer in the world. Textile industry is the pillar of Pakistan's national economy, and also the fifth largest cotton producer in the world. As the largest industrial sector in Pakistan, textile industry plays a pivotal role in the country's socio-economy, contributing 8.5 percent of its GDP and providing about 34 percent of its employment opportunities. Pakistan's textile industry is engaged in production of cotton, cotton yarn, cotton fabrics, towels and garments, and in dyeing of gray fabrics. In 2014, the country produced 2.41 million tons of cotton (accounting for 9 percent of the world's total output), 3.066 million tons of cotton yarn, and 103.6 billion square meters of cotton cloth. In the same year, Pakistan saw the value of imports and exports of textiles reach US\$31.582 billion, accounting for 45 percent of its total value of imports and exports in foreign trade. In Pakistan there are about thirty thousand various types of textile companies which are engaged in ginning, spinning, weaving, processing and post-processing, but most of them are small-sized businesses or even workshops. With backward technologies, these companies mainly produce low value-added products; for example, more than 70 percent of them produce roving fabric and medium-count yarn. Among Pakistan's total textile companies, only about 456 are large-sized and highly industrialized, merely accounting for about 10 percent, including

the leading companies such as Crescent Textile Mills and Ibrahim Fibers. Additionally, more than 60 percent of Pakistan's textile companies are distributed in Punjab—a major cotton-producing province, 30 percent in Sindh, and less than 10 percent in the vast western region. Karachi in Sindh, Lahore and Faisalabad in Punjab have dedicated textile industrial zones, and Faisalabad is even known as textile center. Among the fifty-five industrial parks in the eastern provinces of Punjab and Sindh, twenty-five of them are bases of textile companies, but in the west, it is the two industrial parks in Khyber-Pakhtunkhwa that are involved in textile companies.

### *7.3.2 Leather Industry: Densely Concentrated in Major Eastern Cities*

In Pakistan, leather is the second largest export industry after textiles. Thanks to developed animal husbandry and a large number of livestock raised per capita, Pakistan has abundant raw materials for the development of leather industry. According to the results of the 2006 animal husbandry census, one-fifth of Pakistan's population, namely about thirty-five million Pakistanis, work in animal husbandry, and income from animal husbandry accounts for as much as 20 percent of household income. In 2014, the output value of Pakistan's leather industry reached US\$2.3 billion, accounting for about 1 percent of its GDP, and this industry has created jobs for about one million Pakistanis. Also, leather products are one of the important foreign trade goods in Pakistan, and their output ranked the forefront of the world in 2014: leather gloves ranked second, leather clothing ranked fourth, leatherware ranked fifteenth, and leather shoes ranked thirty-sixth. In the same year, the value of imports and exports of leather industry reached US\$1.041 billion, accounting for 4 percent of Pakistan's total value of imports and exports in foreign trade. The eastern provinces of Punjab and Sindh, where the excellent forage grass and superior irrigation conditions are fairly suitable for raising livestock, are known for high output of good-quality raw hide, hence becoming sources of raw hide and sites of leather processing companies. According to the 2007 statistics, in Pakistan there were a total of more than 720 leather processing companies, most of which were distributed in the eastern cities of Kasur (180-plus), Karachi (170-plus), and Sialkot (130-plus). The leather products produced in the Karachi Export Processing Zone are directly sold to the European and American markets. About 500,000 Pakistanis were employees in leather industry.

### *7.3.3 Large-scale Manufacturing Industry: Mainly Located in Eastern Central Cities, and Rarely Seen in Western Provinces*

Large-scale manufacturing industry is of vital importance for Pakistan's national economy. In 2012, Pakistan altogether had 12,808 manufacturing companies, of which 8,239 were situated in Punjab, accounting for 69 percent of the total; but in Balochistan there were only 309 manufacturing companies. On top of that, the country's large-scale manufacturing industry is also concentrated in the eastern region. In 2005, more than 90 percent of the 2,000-plus large-sized manufacturing companies were distributed in eastern provinces, mainly making the machinery equipment catering to the need of domestic economy, such as building materials machinery, textiles machinery, sugar-making machinery and industrial boilers, as well as some small household appliances and certain auto parts ordered by foreign automobile plants. These companies are either large-sized state-owned enterprises, such as Heavy Industries Taxila, Karachi Shipyard and Pakistan Machine Tool Factory, or small and medium-sized private plants. The province of Punjab, in particular, has the most industrial parks dedicated to large-scale manufacturing, and its capital city Lahore is Pakistan's key manufacturing base. For example, the Lahore Industrial Zone (Block 1) and the Lahore-Kot Lakhpat Industrial Zone are typical electrical manufacturing bases. Besides, the Karachi Export Processing Zone and the Suku Industrial Zone, both in eastern Pakistan's Sindh Province, are auto parts production bases. In contrast, the Khatar Industrial Zone in Khyber-Pakhtunkhwa is only manufacturer of chemical and electromechanical equipment in western Pakistan, and Balochistan does have any industrial parks dedicated to large-scale manufacturing.

### *7.3.4 Steel Industry: Widespread in Major Eastern Cities, But Rarely Seen in Western Provinces*

With a relatively intact upstream and downstream steel industry chain, Pakistan is capable of making pig iron, steel ingot, pipe, coil, and wire. However, the existing steel-smelting mills are generally small-sized, either lack of advanced technologies or complete product categories. Among the 138 steel-smelting mills in Pakistan, with combined annual production capacity of three million tons of crude steel, more than 85 percent of them are concentrated in Lahore and Gujrawala in Punjab, and the Lahore Industrial Zone (Block 1) is Pakistan's top industrial zone dedicated to steel-making. Except the state-owned and large-sized Pakistan Steel Mills,

which possesses advanced technologies, ability to use iron ore for smelting, and annual production capacity of over 500,000 tons, all the other steel-smelting mills are small-sized private businesses which use steel scraps as raw materials and only produce about 100,000 tons of crude steel every year. Pakistan also has 276 steel-rolling mills, of which more than 90 percent, with combined annual production capacity of four million tons, are distributed in Lahore and Karachi; however, only six of them have annual production capacity of above 50,000 tons, and the remaining majority is small and medium-sized.

*7.3.5 Service Industry: Widely Distributed Nationwide,  
with High-end Services Mainly Available in Certain Eastern  
Large Cities*

Although service industry is the main driving force for Pakistan's economic development, it is still dominated by low-end wholesale and retail trade, with high-end services such as finance and insurance accounting for 5 percent of the country's GDP and only available in certain large cities such as Karachi and Lahore, while small and medium-sized retail businesses contribute about 19 percent of GDP. Statistics show that the total revenue of Pakistan's retail trade in 2014 reached US\$48,0994.5 billion, registering an annual growth rate of 10 percent. Currently, there are about 4.43 million Pakistanis working in retail trade, accounting for 11 percent of the country's total employees. Pakistan's retail trade, which mainly relies on household management and family-run operation, is made up of general merchandise market and specialty stores that sell basic living articles.

**7.4 CHARACTERISTICS OF CHINA-FUNDED CPEC'S  
INDUSTRY SPATIAL LAYOUT**

The industry spatial layout of China-funded CPEC is also characterized by a distribution pattern of more in the east and less in the west. In 2015, China and Pakistan signed fifty-one memorandums of understanding (MOUs) on cooperation, worth US\$46 billion and involving multiple fields such as transportation infrastructure, energy and finance, and commenced the construction of eight collaborative projects and five power stations. To be specific, the two countries determined the "1 PLUS\_SPI 4" layout of cooperation focusing on CPEC construction and supported by Gwadar Port, energy, transportation infrastructure and industrial cooperation. Since the location selection of the fifty-one CPEC projects is only

based on economic considerations, that is, under the guidance of the traditional location theory, most of these projects are to be situated in developed eastern Pakistan, except the construction of Gwadar Port in the western province of Baluchistan.

#### *7.4.1 Most Energy Projects Are Built in the Eastern Provinces*

The spatial layout of CPEC energy projects shows great imbalance since most of them are concentrated in eastern Pakistan. China and Pakistan signed agreements on a total of eighteen energy projects, accounting for one third of all CPEC projects. They are mainly funded and constructed by Chinese major state-owned enterprises (SOEs). Among all CPEC projects, energy projects have the largest number, the highest investment, and the most intensive work-in-progress construction, and they involve extensive fields such as hydropower, nuclear power, coal power, and new energy (wind power and solar power). But the spatial layout of the eighteen projects is greatly imbalanced, that is, sixteen projects are to be built in the eastern Sindh and Punjab provinces, and in particular, they are concentrated in the vicinity of large cities such as Karachi and Lahore. Sindh Province alone is to have eleven projects, more than half of the total of eighteen, hence becoming the primary beneficiary of CPEC energy projects. By contrast, western Pakistan only has two projects, and both of them are situated in Balochistan, with Khyber-Pakhtunkhwa looking like an outsider.

#### *7.4.2 Transportation Projects Focus on the Developed Eastern Region*

CPEC transportation projects are about to connect major cities in eastern Pakistan. Although there are not many transportation projects under CPEC framework, their vital role cannot be ignored. One of the arteries is from Kashgar in Xinjiang, China to Gwadar Port in Balochistan, Pakistan. Although the feasibility study on the Eastern Route and Western Route is not yet finished, it seems that the Eastern Route is more likely to prevail, that is, the railway starting from Kashgar firstly runs through eastern Pakistan, while bypassing the vast western region, then connects Karachi—the largest city in Pakistan, and finally ends at Gwadar Port. If so, western Pakistan will be deprived of the economic benefits from CPEC transportation projects. Besides, most of the finalized transportation projects are north-south directional, except for the railway connecting northern Pakistan to Xinjiang's Kashgar. A few east-west transportation projects are

merely implemented to renovate and upgrade the existing railways or highways. It can be seen that CPEC transportation projects focus on the developed parts of Pakistan, especially the major cities of Karachi and Lahore. For example, the Lahore Orange Line Metro, which is built in Lahore—the second largest city in Pakistan, is the only urban mass transit project under CPEC framework.

### 7.4.3 *Gwadar Port: The Only Key Construction Site in Western Pakistan*

Gwadar Port boasts an important geostrategic location as it lies in the southwestern part of Balochistan, just more than 400 kilometers away from the Persian Gulf—a vital international energy channel. That's why Gwadar Port is chosen as a key CPEC project in western Pakistan, and associated with the realization of the national strategies of China and Pakistan. In November 2015, the operation of Gwadar Port was transferred to China Overseas Holdings Limited with a lease term of forty-three years for building it into Pakistan's first special economic zone. But Gwadar Port is currently isolated for lack of connections with the vast hinterland, hence making it hard to play a proper role as the destination of the China-Pakistan Railway in the future. Therefore, China has started offering new capital injections into the infrastructure construction of Gwadar Port. Table 7.1 lists out a total of four infrastructure projects (hospital, expressway, international airport, and public welfare facility) in the port area with a planned investment of US\$750 million, of which the construction of the expressway and the international airport was already approved.

**Table 7.1** Investments of CPEC Gwadar Projects

<i>Project</i>	<i>Investment (million USD)</i>	<i>Partner</i>	<i>Status</i>
Exchange of documents for the feasibility study of the hospital	Unknown	Unknown	Unknown
Eastbay expressway	140	CCCC*	Approved
International airport	180	CCCC	Approved
Public welfare facility	Unknown	Unknown	Unknown

Note: "CCCC" is short for China Communications Construction Company Limited

Source: CPEC leads the development of the Belt and Road Initiative, concept stock takes off soon, Securities Times, <http://www.stcn.com/>, April 6, 2015.

## 7.5 RELATIONSHIP BETWEEN CPEC'S INDUSTRY SPATIAL LAYOUT AND NATIONAL STRATEGIES OF CHINA AND PAKISTAN

The industry spatial layout of CPEC concerns the realization of the national strategies of China and Pakistan. For the part of China, CPEC is of great strategic significance since it is a vital part of the Silk Road Economic Belt and the 21st Century Maritime Silk Road (hereinafter referred to as the Belt and Road), and also a major component of the China-Pakistan Community of Shared Destiny in the new era. For the part of Pakistan, it takes CPEC as an unprecedented development opportunity to fulfill its dream of becoming the Asian Tiger, just like Pakistani Prime Minister Sharif once commented that CPEC was sure to change the destiny of Pakistan. Therefore, when planning for the industry spatial layout of CPEC, the two countries cannot simply focus on short-term economic benefits, but think about how to realize their national strategies from a geostrategic perspective. In short, CPEC should be a two-way integration of China's "opening up to the west" intention and Pakistan's Asian Tiger dream, and a sign of the high-degree compatibility between their national strategies.<sup>2</sup>

### 7.5.1 *Relationship Between CPEC's Industry Spatial Layout and China's National Strategy*

As an influential power that is rising peacefully, China has been promoting the implementation of the Belt and Road Initiative (BRI) in an all-round manner despite of the containment of the United States, Japan and other countries in the Southeast Asian region. China has no serious territorial dispute with neighboring countries, except for India that lies in the south-west, and it even befriends Pakistan as its only all-weather strategic partner. Based on a high level of mutual trust, the two countries have maintained extensive and in-depth cooperation and exchanges in politics, economy, culture, and military. Therefore, the construction of CPEC, which is an important part of China's westward development plan, has become an inevitable choice for China to realize its national strategy. And reasonable industry spatial layout of CPEC is the prerequisite to achieve this purpose.

<sup>2</sup>Deng Zhimei, "Promoting the Implementation of the China-Pakistan Economic Corridor", *China Social Science News*, August 14, 2015.



## 1) Play the role of inspiration, leadership, and demonstration

CPEC is a flagship project among the six major economic corridors planned to be constructed under the framework of BRI. China intends to give play to Pakistan's radiating, leading and exemplary role for other countries along the Belt and Road. As China's external development strategy, BRI involves three continents as Asia, Europe and Africa, and spans seventy-seven countries and regions, accounting for one third of the world's total. Among the countries along the Belt and Road, Pakistan is the most credible political partner of China. Based on their traditional friendship, the two countries have all along maintained close cooperation in various fields. Moreover, Pakistan has a special geographical location with its eastern and northeastern parts adjoining the major powers as India and China, the southern part reaching the Indian Ocean, the western part bordering on the Islamic states as Afghanistan and Iran, and the northern part adjacent to central Asia—the heartland of Eurasia mentioned by the geopolitical scientist Mackinder. Besides, the vast western region of Pakistan is in a state of poverty and backwardness, and some areas remain under tribal rule. If CPEC is a standard template experimenting China's philosophy of eradicating terrorism through economic development, then western Pakistan is no doubt an ideal test ground since it decides the result of Pakistan's combat against terrorism.<sup>3</sup> For this reason, CPEC's industry spatial layout should be appropriately tilted to western Pakistan to enable all provinces of the country to benefit from CPEC's investment of US\$46 billion, thereby relieving the western region from poverty.<sup>4</sup> If it works, western Pakistan will become a role model more convincing than its eastern counterpart, proving to the underdeveloped countries along the Belt and Road that China is doing good to their well-being, rather than practicing the so-called neo-colonialism stigmatized by the Western media. Meanwhile, the success of western Pakistan will accelerate the process of regional economic integration, help China further expand its regional influence, and accumulate experiences for the overall advancement of BRI.

## 2) Create a foundation for the long-term stability of the border area

<sup>3</sup> Chongyang Institute of Finance, Renmin University of China, Finance Magazine, *China-Pakistan Economic Corridor Field Research Report*, December 2016.

<sup>4</sup> Li Xiguang, Sun Lizhou, "The Strategic Value and Security Situation of the China-Pakistan Economic Corridor", *People's Forum·Academic Frontiers*, no. 12 (2015): 32-50.

To fulfill its national strategy, China must maintain the lasting stability of its border areas. After the construction of CPEC was announced, a large amount of funds has been injected into China's western borderland, coupled with the Kashgar-Gwadar Railway Project, hence bringing a golden development opportunity for these border areas. To be specific, CPEC will provide China's border areas with the nearest outlet to the ocean, cultivating these areas to be a new development frontier and a new economic, traffic and cultural hub in the western borderland with Kashgar of Xinjiang as the center. However, the years' economic stagnation in the borderland between China and Pakistan, which is attributed to its proximity to the center of world terrorism and its internal complicated situation, has bred the three forces of terrorism, separatism and extremism inside and outside China, while the western part of Pakistan happens to be the base camp of the three forces. Therefore, the long-term stability of China's western borderland, to a large extent, depends on whether Pakistan can uproot the three forces from its western region. Now that the existence of the three forces is mainly caused by poverty, if western Pakistan was to be left impoverished, the regional economic gap would further widen, terrorism was bound to become more rampant, and in the end Pakistan's turbulence would undermine the stability of China's borderland. On account of this, the industry spatial layout of CPEC should be appropriately tilted to western Pakistan, so as to prevent foreign forces from manipulating domestic ethnic conflicts, eliminate all kinds of insecurity factors that induce instability in China's border areas, create a solid economic foundation for combating the three forces, and safeguard the security of China's western borderland.<sup>5</sup>

### 3) Ease the strategic pressure from the containment of the United States, Japan and other countries in Southeast Asia

For the sake of its national strategy, China also needs to ease the strategic pressure on the west coast of the Pacific caused by countries such as the United States and Japan. Because of the US "Pivot to Asia" strategy and deployment of a THAAD battery to South Korea, coupled with Japan and other countries' provocation of territorial disputes around the South

<sup>5</sup>Yuan Jianmin, "The Strategic Significance and Countermeasures of the China-Pakistan Economic Corridor: Taking Xinjiang's Strategic Position and Role in the "Silk Road Economic Belt" as an Example", *Xinjiang Social Science Forum*, no. 1 (2015): 25-36.

China Sea, their intent to contain China is as clear as daylight, not only threatening the national defense of China's southeast coastal region, but also squeezing its strategic depth. But the development of Gwadar Port will create a new outlet to the Indian Ocean for China, forcing relevant countries to re-examine their strategies and shift attention to the Indian Ocean region. Since Gwadar Port is within easy reach of the Persian Gulf—the world's top energy channel, these countries have to be scrupulous about their strategic suppression off the southeast coast of China, hence alleviating the pressure on China. And beyond that, Gwadar Port—China's new outlet to the sea and currently under its operation—lies in poverty-stricken western Pakistan, China must ensure the safety of this port by narrowing the economic gap between the eastern and western parts of Pakistan, which requires the industry spatial layout of CPEC to be tilted towards western Pakistan to invigorate the local economy, thereby eradicating the breeding ground for terrorism, allowing China to concentrate on pushing into the wider Western and Central Asia and counter the strategic pressure of the United States, Japan and other countries off its southeast coast. It can be said that CPEC, to a certain extent, is an opportunity for China to shift from passive acceptance to active response.<sup>6</sup>

#### 4) Solving the Malacca Dilemma

The development of Gwadar Port provides an opportunity for China to break through the Malacca Dilemma. With rapid economic development, China has a large demand for energy imports such as oil, with foreign-trade dependence as high as 60 percent and more than 80 percent of the oil are imported from the Middle East and Africa passing through the Strait of Malacca. However, it is the United States, which has long regarded China as a potential adversary, that has actual control of this strait. The over-reliance on the Strait of Malacca therefore becomes a potential threat to China's energy security, hence forming the so-called Malacca Dilemma. But Gwadar Port, situated in western Pakistan and just 400 kilometers away from the Persian Gulf—the artery for global oil supply, will provide China with a new strategic energy channel. Once the construction of the Kashgar-Gwadar Port Railway is completed, China will see its oil imports transited from Gwadar Port to Xinjiang by land, crossing over a distance

<sup>6</sup>Gao Fei, "China's "Westward Advance" Strategy and Sino-US Russia-Central Asia Rivalry", *Journal of China Foreign Affairs University*, no. 5 (2013): 39-50.

of 2,400 kilometers, much shorter than the traditional route of more than 12,000 kilometers through the Strait of Malacca. With lower freight charge and less time spent on long-distance transport, China is likely to break through the Malacca Dilemma in the future. For this reason, China must guarantee the safety of Gwadar Port—the nearest oil transmission channel connecting Xinjiang. To this end, more CPEC project investments should be diverted to western Pakistan. Only in this way can the Pakistanis from western provinces have more job opportunities, which will maintain the stability of the western region and help China strengthen its energy security. Besides, the operation of Gwadar Port will change the existing regional development pattern, not only lifting western Pakistan from poverty and backwardness, but also offering the nearest outlet to the sea and a maritime transit station to neighboring countries, and further expanding China's influence in this region.

### 7.5.2 *Relationship Between CPEC's Industry Spatial Layout and Pakistan's National Strategy*

Owing to its long-standing economic stagnation, frequent terrorist attacks, a treacherous geopolitical environment, an impoverished and war-torn neighbor (Afghanistan) in the west, and an aggressive old enemy (India) in the southeast, Pakistan takes the cooperation with China as its only strategic choice. In this context, the reasonable industry spatial layout of CPEC is closely related to Pakistan's future development, and able to help the country fulfill the dream to be the Asian Tiger at an early date.<sup>7</sup>

#### 1) Promote the common development of eastern and western regions

To realize its national strategy, Pakistan must promote common development of eastern and western regions. In July 2015, to respond to the strong appeal of western provinces, Pakistan's Prime Minister Sharif announced that twenty-nine industrial parks and twenty-one resource development zones under CPEC framework were to be built in four provinces: the western provinces of Balochistan and Khyber-Pakhtunkhwa would have sixteen industrial parks (55 percent of the total), and seventeen resource development zones (72 percent of the total) would also be located

<sup>7</sup> Gao Bai, "China-Pakistan Railway: The Outline of China's Land Power Strategy", April 21, 2015, [https://www.guancha.cn/gaobai/2015\\_04\\_21\\_316648\\_s.shtml](https://www.guancha.cn/gaobai/2015_04_21_316648_s.shtml).

in the west, hence giving hope to the vast western region with a weak industrial foundation. Being aware of the importance of the industry spatial layout in its western part, Pakistan must pay great attention to the development of western provinces to realize its national strategy and all-round development. Once the construction of CPEC is fully rolled out, western provinces will have a large number of social infrastructure projects, infrastructure facilities and factories, which will provide numerous jobs to local young and middle-aged laborers, inject new vitality into the local economic development, enable local people to lead a peaceful and prosperous life, and in the end benefit the common development of Pakistan.

## 2) Strengthen control over the areas with separatist tendency

The national strategy also requires Pakistan to strengthen its control over the areas with separatist tendency. The four provinces are inhabited by different ethnic groups, instead of being dominated by a main ethnic group. Such a national structure goes against the formation of a sense of national identity. What's worse, the economic development of western provinces lags far behind their eastern counterparts. The most prosperous Punjab Province contributes more than 60 percent to Pakistan's GDP, Sindh Province is at the intermediate level, while Balochistan and Khyber-Pakhtunkhwa provinces are underdeveloped. The existing industry spatial layout of CPEC, which is concentrated in eastern Pakistan, has created an undesirable cycle of the strong becomes stronger and the weak weaker. The western region has been plagued by serious nationalist sentiments, separatist tendencies, and discontent with the current fiscal, tax and distribution policies. If this situation continues, the investment dividends of CPEC cannot benefit all provinces of Pakistan, but eventually aggravate the contradiction between the eastern and western regions, and make the tendencies of nationalism and separatism more serious. Therefore, the industry spatial layout of CPEC should be tilted to the western provinces of Pakistan, and their interests must be taken into account. The construction of CPEC projects, among which the Gwadar Port project is the top priority, will stimulate the socio-economic development of western Pakistan, realize interest-bundling, weaken and isolate local separatist forces, and strengthen the federal government's control over the areas with separatist tendency.<sup>8</sup>

<sup>8</sup>Gao Huiping, "Pakistan Risk Analysis in the Construction of the China-Pakistan Economic Corridor", *Southeast Asia and South Asia Studies*, no. 1 (2014): 64-68.

### 3) Ease the strategic pressure brought by India

As a part of its national strategy, Pakistan needs to build a strategic rear area to relieve the strategic pressure from India—its long-standing enemy and also a neighbor sharing a 2,900-km-long borderline. Since their partition in 1947, India and Pakistan had gone to three wars to fight for the sovereignty of Kashmir. In the Second Indo-Pak War, the Indian army approached Lahore, Pakistan's second largest city. In the third Indo-Pak War, India occupied 2,600 square kilometers of land in Sindh Province. Since India has an absolute advantage in politics, economy, population and military strength, Pakistan is not yet able to settle the Kashmir dispute between India. Therefore, if the industry spatial layout of CPEC is concentrated in eastern Pakistan which is adjacent to India (Pakistan's largest city Karachi and second largest city Lahore are no more than 500 kilometers away from the Indian border), once another Indo-Pak War breaks out, Pakistan may sink into the abyss for lack of a strategic rear area. Unlike the eastern provinces which are mainly plain areas, the vast western region has numerous mountains and valleys, which means that Pakistan should have certain industries located in the west, in an aim at consolidate its strategic rear area and ease the strategic pressure from India.

## 7.6 COUNTERMEASURES AND SUGGESTIONS FOR CPEC'S INDUSTRY SPATIAL LAYOUT IN THE FUTURE

In Pakistan, the location of China-funded projects highly overlaps with the country's existing industry spatial layout, namely they are concentrated in the eastern provinces, but scattered in the vast western region. In order to realize their national strategies, the two countries shall have CPEC's industry spatial layout appropriately tilt to western Pakistan, so as to reverse the situation where CPEC's existing industry spatial layout goes against its sustainable development, prevent the aggravation of the Matthew Effect as the strong becomes stronger and the weak weaker, and narrow the economic gap between the prosperous eastern region and the impoverished western region. If such gap keeps widening in the future, terrorist attacks will further spread and become increasingly rampant, which will eventually undermine the entire CPEC construction.

In his speech to the Pakistani Parliament in 2015, Chinese President Xi Jinping pointed out that the planning and layout of CPEC projects should take into account all parts of Pakistan, so that the development of the corridor can benefit the entire population; however, the current CPEC investments are mainly aimed at economic returns, which do not go far enough toward achieving the grand strategic goals of China and Pakistan. So, the two countries must determine the industry spatial layout of CPEC as a matter of strategic importance. Now that the traditional location theory is not suitable for the Site selection for CPEC projects, this paper hereby proposes the following countermeasures and suggestions:

### *7.6.1 Provide Incentives to the Projects Built in Western Pakistan*

The industry spatial layout of CPEC should be appropriately tilted to western Pakistan. Both Chinese and Pakistani governments should introduce some incentive policies, rewarding or giving preferential treatment to the major CPEC projects to be built in western Pakistan. And the projects, which can be either built in eastern or western provinces, are encouraged to be located in the west. The construction of major CPEC projects will promote the exploitation of advantageous resources in western Pakistan, and accelerate the pre-construction work of some key projects and high-quality reserve projects. By making full use of this rare opportunity, both countries shall make reasonable layout of resource-intensive and labor-intensive industries in western Pakistan, and form a more scientific investment pattern. Resource development projects are encouraged to be located in the western part of Pakistan, and the east-based projects in need of long-distance transport of resources from the west for deep processing will not be approved under normal circumstances, hence forcing project owners to process resources within or near the western provinces, which will help narrow the economic and social development gap between the eastern and western regions.

### *7.6.2 Vigorously Cultivate Competitive Signature Industry Clusters in Western Pakistan*

The development of local signature industry clusters is the most direct and effective means to revitalize the economy of western Pakistan. Therefore, the country must try to, based on the existing signature industries in

western provinces, promote transition of resource industries and cultivate the signature industry clusters with competitive edge. Western Pakistan has abundant mineral resources, especially considerable reserves of oil, natural gas, and precious stone. However, an extensive and export-oriented development pattern in the past decades has failed to transform local resource endowment into economic superiority. In the future, the western provinces should make full use of capital, technologies and talents to promote intensive resource extraction, extend the resource extraction cycle, reduce resource waste, and avoid degrading the ecological environment. In order to meet market demand and enhance economic competitiveness, Pakistan should vigorously cultivate signature industries that have a broad market prospect and can drive the overall economic development, integrate all production factors and give full play to their role, give priority to the development of competitive signature industries in the western region, such as petrochemistry, steel, building materials and gem processing, extend the industry chain, optimize the industry system, and form signature industry clusters.

### *7.6.3 Seek Common Development Through East-west Collaboration*

The construction of CPEC should create a situation where there are east-west cooperation, paired assistance, and common development. Eastern and western provinces of Pakistan are encouraged to carry out all-round cooperation that caters to market demand, centers on economic efficiency, pursues mutual benefit, and allows enterprises to serve as the main body, in an aim at establish a new mechanism for them to advance side by side. On the one hand, Pakistan will see surplus funds and technologies continuously flow from the east to the west to help the latter develop its competitive industries. On the other hand, eastern provinces will have a broad market and vast resources through the industrial linkage with western provinces, so that the separate advantages of all provinces can be combined to cultivate industry clusters with integration advantage and brand advantage. The key is to extensively develop associated industries, extend the industry chain of energy and raw materials, and create a win-win situation. At the same time, developed eastern provinces can help impoverished western provinces through a paired assistance mechanism, so there may be the pair of Punjab and Balochistan and the pair of Sindh and



Khyber-Pakhtunkhwa; and eastern cities can establish sister-city relations with their western counterparts, hence sequentially forming an all-around assistance mechanism which involves intergovernmental aid, support from all types of market entities, and participation of all sectors of society, including social groups, non-governmental organizations, and good-hearted people.



# Changes on CPEC's Logistics Channel: Case Study on the Site selection for Kashgar-Gwadar Railway

*Fang Zhao*

The construction of China-Pakistan Economic Corridor (CPEC) requires improvement of the land access from Kashgar in Xinjiang, China to Gwadar Port in western Pakistan. This logistics channel is of vital importance to CPEC, but its site selection has undergone twists and turns with the initial Eastern Route Plan finally replaced by the Western Route Plan. Why does the western Pakistan, which is economically backward and has poor investment prospects, become the priority area for the passage construction? Can the Western Route Plan benefit the socio-economic development of China and Pakistan? These are main topics of this chapter.

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## 8.1 FROM EAST TO WEST: CHANGES ON THE SITE SELECTION FOR CPEC'S LOGISTICS CHANNEL

Demands for logistics services are essentially derivative<sup>1</sup> of the demand for the movements of products from real economic activities such as production and consumption. Logistics channels form the physical infrastructure for the supply of logistics services, with their trade flow and direction subject to the impact of real economy. Therefore, the location of logistics channels closely relates to the location of real economy and changes accordingly.

As a crucial part of CPEC, which was officially launched in 2013, China and Pakistan planned to build a logistics channel (including roads, railways, and oil pipelines) for transporting imported and exported energy and other products between the two countries. However, the siting of this logistics channel soon aroused heated discussion within Pakistan. Any place that this logistics channel passes through can benefit from CPEC, hence no local government yielded an inch. The western provinces, in particular, tried with all their might to put pressure on the federal government since they hated for being deprived opportunities for economic development and inadequate political rights. While claiming that CPEC would come to nothing if bypassing the west,<sup>2</sup> governments of western provinces even resorted to non-constructive expressions such as reproaching in the parliament, organizing political campaigns on the streets, and threatening to thwart the construction of CPEC. As a result, the initial Eastern Route Plan was finally replaced by a Multi-route Plan with western Pakistan taking top priority, thereby giving birth to the Kashgar-Gwadar logistics channel.<sup>3</sup>

<sup>1</sup> Derivativeness (Derivativeness) demand, that is, the demand for a certain kind of goods or services is determined by the supply or consumption of another or several kinds of goods or services. The goods and services that trigger this derivative demand have their origins, such as manufacturing products and entertainment services.

<sup>2</sup> Yao Yuanmei, "The hidden worries of the China-Pakistan Economic Corridor: How to avoid falling into that "black hole"?" *The Paper*, [http://www.thepaper.cn/newsDetail\\_forward\\_1405420](http://www.thepaper.cn/newsDetail_forward_1405420), Dec 6, 2015.

<sup>3</sup> The Eastern Route Plan: Starts from Mansehra (exit on the Karakoram Highway), enters Punjab via Islamabad, passes Lahore to Multan, then follows Multan-Hyderabad and Hyderabad-Karachi M-9 highway, and finally runs along the Karachi-Gwadar coastal highway N-10 to Gwadar Port. The "Western Route" plan: Starts from Kashgar in the north, crosses the Mount Hongqlap into Pakistan, follows the Karakoram Highway into Gilgit-Baltistan (in Pak-controlled Kashmir), passes through Abbotabad, enters Khyber-Pakhtunkhwa, via Mianwali and Bannu to reach Dera Ismail Khan, leaves from Dera Ismail Khan for Balochistan, via Zhob, Quetta, Khuzdar and Panjgur, and finally arrives at Gwadar Port.

From the perspective of investment, the Eastern Route holds greater appeal. The eastern provinces of Punjab and Sindh, where the logistics channel will pass through, are affluent regions with relatively dense populations (consumption activities) and industries (production activities), conforming to the general law that logistics planning caters to the development of the real economy. In contrast, the Gilgit-Baltistan area in Pakistan-occupied Kashmir and the provinces of Khyber-Pakhtunkhwa and Balochistan, which the Western Route would pass through the Western Route, are economically backward. What's worse, separatist forces often launch terrorist attacks in the areas near the Western Route, while the Pakistani government is incapable of wiping them out for the moment. From the evaluation of investment income and safety, the Western Route is highly risky. For this reason, there are voices within China opposed to such a huge investment of tens of billions of dollars in a route passing through disputed areas.<sup>4</sup> Although the Western Route may be an alternative foreign trade (including energy imports) channel of China, it is not an ideal option due to its huge consumption of human, physical and financial resources, slow cost recovery and risk of loss. Aslo, it is not as convenient and economical as the upgrading of the existing Eastern Route.<sup>5</sup>

This article holds that the Site selection for any cross-border logistics channel should be a holistic decision based on long-term and systemic considerations to balance the development of regions, host countries and even participating countries, instead of simply pursuing short-term benefits. The selection of either Eastern or Western Route is in essence a contest between two theoretical perspectives or concepts: The Eastern Route conveys a project operation concept, requiring an early evaluation of the economic level and ROI of the destination for investment. Although the short-term benefits of the Eastern Route are obvious, traffic lines in the eastern region are quite dense, which means that increasing transportation investment will be together with a decreasing marginal income. Meanwhile, negative consequences such as traffic congestion and environmental pollution will occur. The Western Route reflects a regional development concept, attempting to bring long-term development opportunities to western

<sup>4</sup> "Indian media: China-Pakistan Economic Corridor may be blocked", <http://www.cankaoxiaoxi.com/finance/20160113/1051426.shtml>, January 13, 2016.

<sup>5</sup> "The first railway line of the China-Pakistan Economic Corridor is exposed", <http://www.cankaoxiaoxi.com/finance/20150424/755241.shtml>, Apr 24, 2015.

Pakistan and narrow the economic gap between the eastern and western regions.

In recent years, Pakistan has already made attempts to boost the construction of logistics infrastructure in the western provinces in order to narrow the regional development gap, but neither economic nor social development indicators are significantly improved. This article holds that this is not blamed on the failure of the regional development concept, but attributed to the overlook of the important supporting factor—the logistics infrastructure network. The reasonable Site selection for CPEC logistics channel is to create a new resultful “network”, instead of optimizing the existing one. The valuable point of this article is to, based on the regional development concept and in combination of the actual situation in Pakistan, propose “a network development concept” suitable for late-developing countries. According to the network development concept, CPEC logistics channel should be preferentially located in western Pakistan, and more efforts should be made to build the local infrastructure network, since a perfect economic “structure” provides a valid path for increasing the economic volume.

The following sections firstly review the existing concept on the Site selection for CPEC and point out its shortcomings, then introduce the more suitable network development concept, and finally put forward pertinent suggestions for the development of CPEC.

## 8.2 FROM “OPERATION” TO “DEVELOPMENT”: CHANGES IN SITE SELECTION CRITERIA FOR CPEC’S LOGISTICS INFRASTRUCTURE

Location selection of logistics infrastructure, which plays an important role in determining the investment for logistics infrastructure, is decided on the basis of the benefits and costs of the project. Generally, different concepts for project evaluation—the project operation concept and the regional development concept—can derive from different understandings of benefits and costs. The project operation concept stresses the direct economic returns and costs of the project, while the regional development concept also takes the social and economic benefits and costs indirectly induced by the project into account. In Pakistan, the application of the two concepts has brought different results of site selection.

### 8.2.1 *Site Selection for Logistics Infrastructure and Spatial Concentration of Pakistan's Economy According to the Project Operation Concept*

Logistics infrastructure,<sup>6</sup> while usually a kind of public good provided by the government, is a physical capital that needs project investment; and its large investment scale forces investors to carefully evaluate the benefits and costs of the project. Part of Pakistan's logistics infrastructure was built by the British East India Company (BEIC) in colonial times, and the other part was constructed with foreign aid after the country gained its independence. Considering the colonial development and the country's solvency of debt, Pakistan had all along taking minimum costs and maximum benefits as the precondition for funding the construction of logistics infrastructure.

According to the principle of minimizing investment cost, a reasonable logistics route should be, on the basis of natural conditions and technical strength, the shortest path between two traffic nodes.<sup>7</sup> Generally speaking, the logistics construction cost in flat areas is lower than that in mountainous areas and other areas with harsh conditions, and road construction is less costly than railway construction in the same period.

During the British India period (1858–1947), most of Pakistan's logistics infrastructure was located in the eastern plains and irrigated areas. In 1865, by building a railway from Karachi to Kotri (both in Sindh Province), Pakistan was incorporated into the pan-Indian rail network and since then Pakistan embarked on the construction of its modern transportation system.<sup>8</sup> The Karachi-Kotri Railway, which was later connected with the railway from Islamabad to southern Pakistan and passed through the eastern

<sup>6</sup>This paper focuses on the discussion of logistics “infrastructure” facilities, that is, in each basic link of logistics (transportation, storage, loading and unloading, handling, packaging, circulation processing, distribution, and information processing) with a single function of the place or tangible capital. Some studies also include logistics parks, logistics centers, or distribution centers into the scope of logistics infrastructure. These facilities are the product of the development of modern logistics in recent years. They often integrate a variety of basic functions except transportation. They are a specialized “comprehensive” facility that does not belong to the category of “infrastructure” which is mainly studied in this paper.

<sup>7</sup>Bodrigue Jean-Paul et al., “Geography of Transportation”, translated by Wang Jianwei and Fu Xin, People's Communications Publishing House, 2014.

<sup>8</sup>Vakil C., “Railways and roads in India”, *Annals of the American Academy of Political and Social Science*, vol.233 (1944): 187–192.

plains, has become the country's trunk railway.<sup>9</sup> These kinds of railways, with ports and inland political and economic centers as nodes and connecting areas with sound traffic conditions along the way, are commonplace in most colonial and semi-colonial states. The suzerain states had been exploiting the resources of their colonies with the minimum investment, which according with their strategic goal.<sup>10</sup> By relying on the local traffic routes, they had been developing the modern economic structure and economic location of their colonies from scratch, thereby forming an export-oriented economy in favor of their own interest. Even to this day, the production of Pakistan's main tradable products, such as textiles and clothing, remains concentrated in the eastern part.

After independence, Pakistan's infrastructure construction was highly dependent on foreign aid, and the focus of construction soon shifted from railways to highways. Like most developing countries, Pakistan also has weak infrastructure, and the financial fund mobilized by the government is far from enough to support the country's infrastructure construction.<sup>11</sup> From the 1960s to the 1970s, Pakistan became the largest recipient of aid in Asia. But the foreign funds were mainly used in the fields to benefit the political and commercial interests of the capital export countries.<sup>12</sup> It was during this period that Pakistan's transportation investment, which had until then heavily favored railroad construction, began to tilt more towards highway construction.<sup>13</sup> According to research, this change was not only due to domestic demand, but also due to the advice of foreign consulting agencies, such as the Harvard Advisory Group. An important piece of advice is that the construction of highways is less costly and quicker to get

<sup>9</sup> Donaldson D., Hornbeck R., "Railroads and American Economic Growth: a 'Market Access' Approach", *NBER Working*, 2013, paper No.19213.

<sup>10</sup> Debie J., "From Colonization to National Territories in Continental West Africa: The Historical Geography of a Transport Infrastructure Network", *Journal of Transport Geography*, vol.18 (2010): 292–300.

<sup>11</sup> Looney R.E., Winterford D., "Infrastructure and Regional Development in Pakistan", *Review of Urban and Regional Development Studies*, vol.5 (1993): 95–114.

<sup>12</sup> Mustafa S., "Pakistan: Development of Underdevelopment", *Pakistan Horizon*, Vol.28, No.2 (1975): 48–58.

<sup>13</sup> According to the "Pakistan Economic Survey 2009–2010" published by the Ministry of Finance of Pakistan, since the 1970s, the proportion of railway passenger transportation in Pakistan has dropped from 41 percent to 10 percent, and the proportion of cargo transportation has dropped from 73 percent to 4 percent.

payback.<sup>14</sup> Since the 1990s, the foreign aid flowing to Pakistan is mainly in the form of loans charging commercial interest rates, hence aggravating the country's burden of debt.<sup>15</sup>

Under the pressure of debt repayment, the location of Pakistan's logistics infrastructure projects during this period is selected not only for minimizing the cost of investment, but also for maximizing ROI. As far as the project itself is concerned, the direct benefits of a logistics infrastructure project mainly come from the toll and service charges generated by cargo and passenger flow, as well as the local tax revenue along the way. Such project in the areas with larger flow of cargo and passengers can earn higher income. Recently, in review of the loan application for the highway construction in Sindh, the Asian Development Bank (ADB) calculated the ROI of several highways proposed by the local government on the basis of their traffic flow, then ranked them according to their net present value, and finally approved the loan for the most promising highways.<sup>16</sup> The formation and size of cargo flow depend on the development level of local industries and the demand for trade. Therefore, the eastern part of Pakistan, with a sound modern industrial base dated back to the colonial period, remains the preferred location for the logistics infrastructure projects, and its status has been further consolidated due to cumulative causation.

According to the project operation concept, the location of logistics infrastructure in the eastern region has made both Pakistan's industry gathering and economic development concentrate in the east later on, forming a wide economic gap between eastern and western provinces. If this concept is applied to the Site selection for CPEC projects, the western provinces will be discontented with their eastern counterparts and the federal government for depriving western provinces' development opportunities again, What is more, they may obstruct the construction of CPEC.

<sup>14</sup> Irfan M., *Institutional Barriers to Sustainable Urban Transport in Pakistan*, Oxford University Press, 2010.

<sup>15</sup> Khan M.A., Ahmed A., "Foreign Aid—Blessing or Curse: Evidence from Pakistan", *The Pakistan Development Review*, vol.46 (2007): 215–240.

<sup>16</sup> PPTA, "Islamic republics of Pakistan: Provincial Road Improvement Project", *ADB Technical Assistance Consultant's Report*, 2015, Project Number: 46377-001/TA 8406-PAK.



### 8.2.2 *Site Selection for Logistics Infrastructure and Pakistan's Imbalanced Regional Development According to the Regional Development Concept*

As a kind of public good, the ultimate goal of infrastructure is to improve the social and economic conditions of a region. The project site selection based on the regional development concept, which measures the social and economic costs and benefits of the project, tends to give priority to underdeveloped areas. In order to stimulate the economic development in impoverished provinces, the Pakistani government has already made attempt to build logistics infrastructure in the west, but not yet achieved any satisfactory result.

In terms of a logistics infrastructure project, its social and economic benefits mainly include the economic growth effect and the resource redistribution effect of the area where it is located and so on,<sup>17</sup> while its costs are made up of local land premiums, traffic congestion and environmental pollution and so on.<sup>18</sup> Most countries take the site selection for logistics infrastructure projects as an important mean to promoting the development of backward areas and regional economic integration. This is based on economists' theoretical analysis and long-term observation of the relationship between investment in transportation infrastructure<sup>19</sup> and economic growth. In most cases, through construction of logistics infrastructure projects, an area can increase its gross output, income level and productivity,<sup>20</sup> and such effect is more prominent in underdeveloped or

<sup>17</sup>Banister D., Berchman J., *Transport Investment and Economic Development*, University College London Press, 2000.

<sup>18</sup>Redding S.J., Turner M.A., "Transportation Costs and the Spatial Organization of Economic Activity", in Gilles Duranton, J.Vernon Henderson, William C. Strange ed., *Handbook of Regional and Urban Economics Volume 5 B*, North-Holland, 2015.

<sup>19</sup>The function of transportation infrastructure is to realize the spatial displacement of "goods" and "people". In addition to production activities, the displacement of "people" also includes a large number of life-oriented trips (such as travel, visiting relatives and friends); the latter is not a substantial factor in promoting regional economic development, especially economic growth. There have been a lot of studies on the relationship between transportation infrastructure investment and economic development. This paper mainly analyzes the relationship between logistics infrastructure investment and economic development.

<sup>20</sup>From a theoretical point of view, transportation infrastructure investment can form the capital stock of a region on the one hand, and on the other hand help reduce the transportation cost of the manufacturing industry and improve its production efficiency; they affect the capital variable and total factor productivity in the production function respectively and become the source of economic growth.

non-urban areas.<sup>21</sup> However, more logistics infrastructure projects also mean that the area has to pay higher social and economic costs.

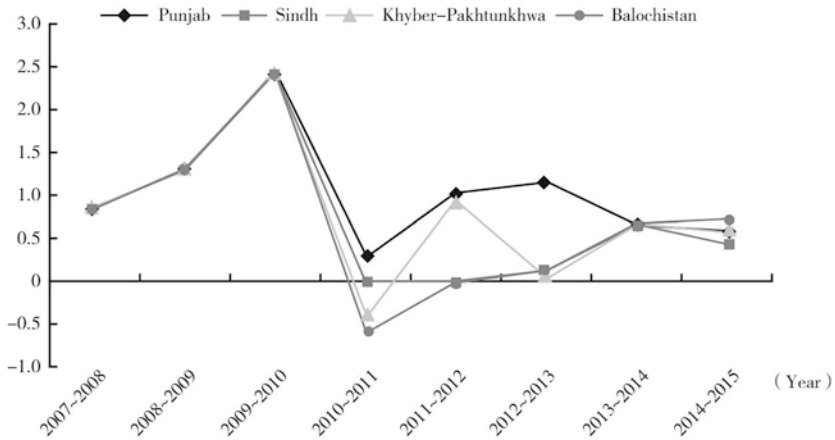
In order to narrow the regional development gap, the Pakistani government has started paying attention to the layout of logistics infrastructure in the underdeveloped western region. In the Seventh Five-Year Plan (1988–1993), the government admitted that Pakistan's regional inequality is attributed to political, economic and social factors, and proposed an ambitious program to reduce regional disparities, including equal distribution of basic demand and supply... boosting the economy of backward areas in a comprehensive way through construction of more and better infrastructure...<sup>22</sup> It is believed that the endowment of logistics infrastructure is an accurate reflection of the development level of all parts of Pakistan.<sup>23</sup> In 2005, the Pakistani government launched the National Trade Corridor Improvement Program (NTCIP), trying to upgrade the existing North-South Corridor (Peshawar-Lahore-Karachi) by improving the trade and logistics chains. The NTCIP was also designed to strengthen the east-west connection and the connection with neighboring countries such as Iran, Afghanistan and India. In 2007, the NTCIP was included into the Pakistan Vision 2025 and expected to become a bond between remote areas and urban centers, an integrated network between economic centers, and a high-capacity corridor connecting major regional trading partners.<sup>24</sup> Correspondingly, the growth rate of highway length in the western provinces (Balochistan and Khyber Pakhtunkhwa) during the fiscal years 2007–2008 and 2009–2010 remained the same as that in the eastern provinces (Punjab and Sindh). During the fiscal year 2010–2011, all provincial highways were destroyed more or less by the widespread floods. After two years' reconstruction, the growth rate of highway length in the

<sup>21</sup>Hirschman A.: *The Strategy of Economic Development*, Yale University Press, 1958; Hansen N.M., "Unbalanced Growth and Regional Development", *Western Economic Journal*, (1965) 4 (1): 3–14; Michael G., "The Effect of Trade on the Demand for Skill-Evidence from the Interstate Highway System", *Rev.Econ.*, no.7 (2008): 247–264; Donaldson, D., "Railroad of the Raj: Estimating the impact of transportation infrastructure", *NBER working paper*, No.16487, 2010.

<sup>22</sup>Planning Commission: "Seventh Five Year Plan 1988–93 & Perspective Plan 1988–2003", Government of Pakistan.1988.

<sup>23</sup>Looney R.E., Winterford D., "Infrastructure and Regional Development in Pakistan", *Review of Urban and Regional Development Studies*, vol.5 (1993): 95–114.

<sup>24</sup>Ministry of Finance, "Pakistan Economic Survey 2014–15", Government of Pakistan, [http://fi-nance.gov.pk/survey\\_1415.html](http://fi-nance.gov.pk/survey_1415.html).



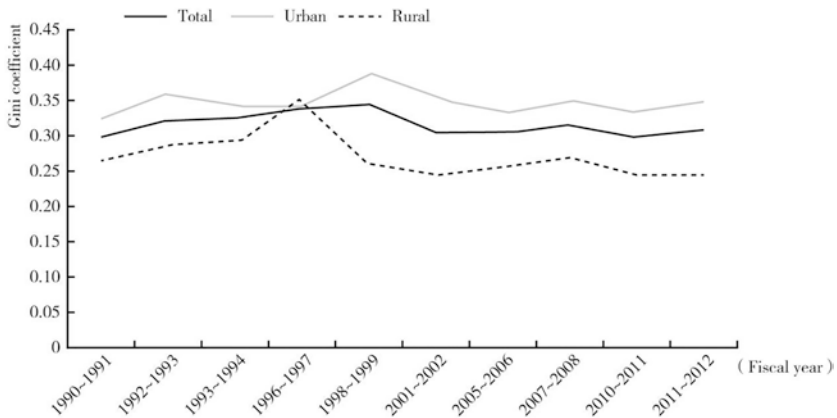
**Fig. 8.1** Growth rate of highway length in Pakistan's four provinces from 2007 to 2015

western provinces surpassed that in the eastern provinces during the fiscal year 2012–2013, as shown in Fig. 8.1.

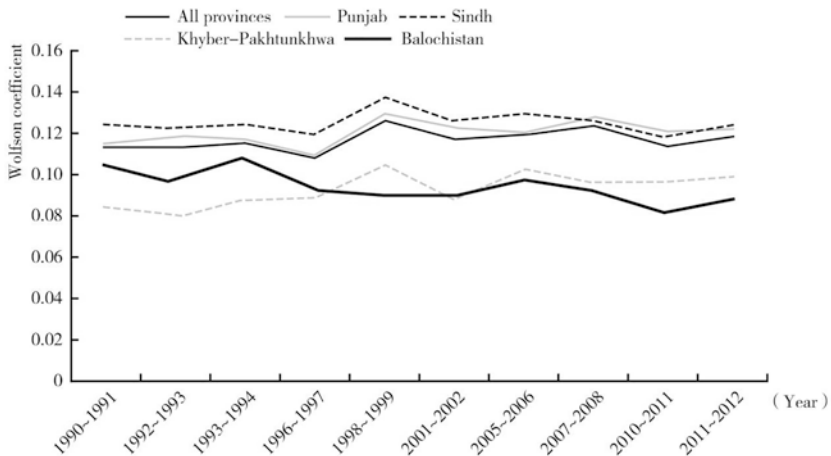
However, despite an increase in logistics infrastructure construction in Pakistan's western provinces, unbalanced regional development has seen little improvement. Research shows that since the 1990s the degree of inequality among Pakistan's provinces has been fluctuating within a limited range, and the inequality is greater in urban areas than in rural areas, as shown in Fig. 8.2. The income gap between the rich and the poor in the east is much wider than that in the west. Balochistan is the only province that sees income polarization easing slightly, as shown in Fig. 8.3. Through empirical research, Pakistani scholars have found that, from the fiscal year 1975–1976 to the fiscal year 2010–2011, the impact of Pakistan's highway construction on its per capita GDP growth was not as significant as expected, and the spending on the extension and upgrading of the highway network (especially expressways) had failed to translate into tangible benefits.<sup>25</sup>

There are several explanations for the failure of the regional development concept. One is that Pakistan may have invested too much in

<sup>25</sup> Imran M., Niazi J., "Infrastructure and Growth", *The Pakistan Development Review*, vol.50 (4) (2011): 355–364.



**Fig. 8.2** Changes in the Gini coefficient of Palestinians' income from 1990 to 2012: urban vs. rural



**Fig. 8.3** Changes in the Wolfson coefficient of Pakistan's provincial income from 1990 to 2012

highways, especially in highway infrastructure,<sup>26</sup> even though its density of highways is higher than that of neighboring Iran and Bangladesh. But this explanation is too data-intuitive and lack of a convincing logical basis. From a global perspective, authoritative bodies such as the World Bank and the ADB comment that Pakistan—a low- and middle-income country—is desperately lack of capital investment, with its highway density of 0.33 km/km<sup>2</sup> higher than that of some neighboring countries with lower income, but much lower than India's 1 km/km<sup>2</sup>.<sup>27</sup> The other explanation is that the Pakistani governments at all levels have corrupt practices in mobilizing the funds for logistics infrastructure.<sup>28</sup> In most developing countries with immature institutions, including China and India, corruption exists to varying degrees in the stage of rapid economic development. Corruption, which is a kind of social cost, has uncertain impact on the economic growth of developing countries. Some studies show that in countries or regions with low institutional efficiency, moderate corruption may be beneficial to economic growth.<sup>29</sup> Therefore, corruption is not the root cause of the failure of regional development concept.

In fact, the reason why the regional development concept has yielded little effect in Pakistan is mainly because the executive agencies don't have thorough understanding of its applicability. First of all, they are unaware that infrastructure investment is only a necessary condition for regional development, instead of a sufficient condition. Second, they have forgotten that the implementation of this necessary condition in developing countries requires the collaboration of other relative factors.

The previous experiences show that the logistics infrastructure built in western Pakistan is not as beneficial as those logistics infrastructures located in the eastern provinces. However, the eastern region has been

<sup>26</sup> Imran M., Niazi J., "Infrastructure and Growth", *The Pakistan Development Review*, vol.50 (4), (2011): 355–364.

<sup>27</sup> Source: Ministry of Finance, "Pakistan Economic Survey 2009–10", Government of Pakistan, [http://finance.gov.pk/survey\\_0910.html](http://finance.gov.pk/survey_0910.html).

<sup>28</sup> Khan M.A., Ahmed A., "Foreign Aid—Blessing or Curse: Evidence from Pakistan", *The Pakistan Development Review*, vol.46 (2007): 215–240.

<sup>29</sup> Bardhan P., "Corruption and Development: A Review of Issues", *Journal of Economic Literature*, vol.35 (3), (1997): 1320–1346; Acemoglu D., Thierry V., "Property Rights, Corruption and the Allocation of Talent: A General Equilibrium Approach", *Economic Journal*, vol.108 (1998): 1381–1403; Adit T., "Corruption, Institutions and Economic Development", *Oxford Review of Economic Policy*, vol.25 (2009): 271–291; "Regional Corruption and Marketization in China's Economic Growth", *Journal of Management World*, vol. 11 (2011): 10–17, 27.

troubled by the outstanding problems such as environmental pollution, traffic congestion and accidents in recent years.<sup>30</sup> If CPEC's logistics channel is to be located in eastern Pakistan, it will face increasing social costs and decreasing social benefits. Therefore, the Site selection for CPEC's logistics channel must be based on the current situation of Pakistan. Besides, efforts must be made to identify the fundamental factors that enable logistics infrastructure to promote the economic development of underdeveloped areas, so as to provide new theories and perspectives for the Site selection for CPEC's logistics channel.

### 8.3 FROM “STRUCTURE” TO “VOLUME”: THE NETWORK DEVELOPMENT CONCEPT FOR CPEC'S LOGISTICS CHANNEL

In addition to increasing the logistics infrastructure stock in Pakistan, the construction of CPEC's logistics channel also changes the structure of Pakistan's entire infrastructure network. For developing countries, the key to activating production factors and boosting economic development lies in the changes in their logistics infrastructure network. The idea of increasing the regional economic volume by improving the structure of the logistics infrastructure network is known as “the network development concept”.

#### 8.3.1 *Logistics Infrastructure Is a Necessary Condition for Promoting Regional Development*

The investment in logistics infrastructure has long been regarded by policy makers as a prerequisite for economic development. As the Chinese saying goes, “if you want to get rich, build roads first”. But the analysis of successful cases has revealed that the investment in logistics infrastructure usually takes place after economic take-off, not before that. For example, the British railway system was built in 1852, but the British Industrial Revolution began as early as around 1760,<sup>31</sup> showing that railways are part of the industrial revolution, not a prerequisite. This rule is also seen in

<sup>30</sup> Measood M.T., “Transportation Problems in Developing Countries Pakistan: A Case-in-Point”, *International Journal of Business and Management*, vol.6, no.11 (2011): 256–266; Sánchez-Triana E., Afzal J., Biller D., Malik S., “Greening Growth in Pakistan through Transport Sector Reforms: A Strategic Environmental, Poverty, and Social Assessment”, World Bank, 2013.

<sup>31</sup> Mitchell B.R., “The Coming of the Railway and UK Economic Growth”, *Journal of Economic History*, vol.24 (3) (1964): 315–316.

some representative studies on the positive correlation between logistics infrastructure and economic development in the United States from 1850 to 1860 and from 1870 to 1890 after the American Industrial Revolution.<sup>32</sup>

This means that only when certain indicators or underlying momentum already exist, investment in transportation or logistics infrastructure can make economic growth more productive. And these indicators or underlying momentum are necessary conditions for logistics infrastructure to promote regional development. According to existing research, these necessary conditions mainly fall into three categories: First, investment factors, including investment scale, location, and type. Second, political factors, such as supportive organizations, policies and institutions, and procedures. Third, positive externalities of local economy, such as agglomeration economy and scale economy.<sup>33</sup>

In the past, the location of logistics infrastructure in western Pakistan basically satisfied the combination of two necessary conditions—investment factors and political factors. Although these two factors need to be improved, what western Pakistan needs more of is positive economic externalities, which is the main reason for the limited impact of logistics infrastructure investment on economic development.

The significance of positive economic externalities for logistics infrastructure lies in the functioning of local logistics market. Logistics industry is an industry separating from the procurement and distribution links due to the specialized development of manufacturing industry. The demand scale and service level of logistics depend on the scale and level of specialization of local manufacturing industry, while the development of manufacturing industry is driven by decreasing costs and increasing efficiency brought about by logistics service. In short, logistics and manufacturing industries support each other and develop in a coordinated way, hence eventually forming positive economic externalities of local economy.

Spatial agglomeration is an important manifestation of the scale and specialized development of manufacturing industry. After all these years, the manufacturing industry in western Pakistan has failed to gain any sound

<sup>32</sup>Haines M.R., Margo R.A., “Railroads and local economic development: the United States in the 1850s”, in Rosenbloom J.L., ed., *Quantitative Economic History: The Good of Counting*. Routledge, 2008; Donaldson, D., Hornbeck, R., “Railroads and American economic growth: a ‘market access’ Approach”, *NBER Working*, 2013, paper No.19213; Academics generally agree that the industrial revolution in the United States began around 1820.

<sup>33</sup>Banister D., Berchman J., *Transport Investment and Economic Development*, University College London Press, 2000.

momentum of agglomeration development. In this country, the production activities are highly concentrated in the eastern major cities of Lahore and Karachi,<sup>34</sup> and the areas with medium industrial agglomeration are close to these cities, making them have access to professional labor force, advanced knowledge, intermediate goods and product markets of the two cities, and benefit from the large market size. By contrast, in the vast western part, Swat is the only area with medium industrial agglomeration. And the types of agglomerated industries are rather simplified, being mostly resource-intensive industries dealing with marbles, minerals, pharmaceuticals, and plastics. Both Karak and Kalat have medium-to-low agglomeration of manufacturing industry.<sup>35</sup> The spatial layout of manufacturing industry in Swat, Karak and Kalat is independent of each other, hence unable to drive the development of manufacturing industry in neighboring areas.

In western Pakistan where the manufacturing industry is of small scale on the whole and the demand for logistics service remains low, local logistics infrastructure is unable to perform its basic functions fully and effectively. Straightly speaking, although the Pakistani government has increased investment in the construction of logistics infrastructure in the west, it forgets to vigorously cultivate and develop the local logistics market. Because of this, Pakistan can hardly achieve the goal of promoting the economic development of the western region through investment in logistics infrastructure.

### 8.3.2 *The Neglected “Structure”: “Lines” vs. “Network”*

When putting forward the proposition that “investment in logistics infrastructure” promotes “Pakistan’s regional economic development”, researchers usually simplify logistics infrastructure as an investment factor and ignore its function of stimulating local economic externalities. The key to stimulating this function is the “structure” of logistics infrastructure, that is, the “network” form of logistics facilities in a country or region. The network can connect more regions and markets, forming the manifestation of economies of scale—the network economy effect, and

<sup>34</sup> Sánchez-Triana E., Afzal J., Biller D., Malik S., “Greening Growth in Pakistan through Transport Sector Reforms: A Strategic Environmental, Poverty, and Social Assessment”, World Bank, 2013.

<sup>35</sup> Burki A.A., Khan M., A., “Spatial Inequity and Geographic Concentration of Manufacturing Industries in Pakistan”, Conference Paper, 2010, <https://www.researchgate.net/publication/257356238>.



economies of scale are the basis for the formation of a positive externality economy. Therefore, the less profitable logistics infrastructure in western Pakistan is also blamed on the neglect of its “structure”.

In fact, there exists a long reaction chain between “investment in logistics infrastructure” and promotion of “regional economic development”. The most direct and controllable impact of logistics infrastructure investment is the accessibility of travelers,<sup>36</sup> which is the first level of the impact. The accessibility is closely related to the connectivity, density and structure of the logistics network. The improvement of accessibility can help reduce logistics costs and raise logistics efficiency, thereby promoting the increase of productivity and the changes of production location and spatial agglomeration, which is the second level of the impact. Changes in productivity and production location in turn affect economic growth and balanced development, which is the third level of the impact.

The second level of the impact is a critical path for the effects of logistics infrastructure to shift from micro-level to meso-level. Generally, a single logistics route or node only connect a limited number of areas and markets. But in a logistics network, a newly-built route, when coupled with the existing ones, can increase the accessible paths in a geometric progression. Then these paths will connect more areas and markets to form a scale economy based on logistics activities. Therefore, network is an important structure of logistics infrastructure, and also a mainstay for generating a scale economy with positive externalities.

Most related studies, especially those of developed countries or regions, presume that the network of logistics infrastructure is already in place and the network effect has already materialized. The analysis of the relationship between “site selection for logistics infrastructure investment” and “economic development” is to verify the improvement of network effect by building new routes in underdeveloped or rural areas based on the existing logistics network. Generally, the extension of highway or railway network can accelerate the agglomeration of businesses and production factors to the areas along the way, and then help increase enterprise productivity and local income.<sup>37</sup>

<sup>36</sup> Accessibility essentially refers to how easy it is to get from one place to another.

<sup>37</sup> Chandra A., Thompson E., “Does public infrastructure affect economic activity? Evidence from the rural interstate highway system”, *Reg.Sci.Urban Econ*, vol.30 (2000): 457–490; Michael G., “The Effect of Trade on the Demand for Skill-Evidence from the Interstate Highway System”, *Rev.Econ*, vol.71 (2008): 247–264; Donaldson D., “Railroad of the Raj: Estimating the impact of transportation infrastructure”, *NBER working paper*, No.16487, 2010.

However, western Pakistan had not formed an effective logistics infrastructure network before CPEC was launched.<sup>38</sup> More than 90 percent of Pakistan's logistics activities are borne by highways, of which national highways undertake about 80 percent of the country's commercial transportation.<sup>39</sup> The network of national highways in west Pakistan has two characteristics: First, it is in a fanlike structure with Quetta and Peshawar (capitals of Balochistan and Khyber-Pakhtunkhwa respectively) as the center. Second, the two capital cities connect the cities and areas along the way through an arterial highway, but there are hardly any feeder roads in the cities and areas along the way. The highways in such structure seems like dedicated transport lines, while an interconnected logistics network has not formed yet. The crisscross structure of highways in eastern Pakistan is more prominent, so there are more hub or nodal cities. In terms of railways, the endowment of railways is a sign that distinguishes between developed and underdeveloped areas in Pakistan.<sup>40</sup> Quetta and Peshawar, although they are connected by railways with the eastern developed cities such as Islamabad and Karachi, do not have any railways linking the two or between them and Gwadar Port. In other words, the north-south railways in western Pakistan remain unavailable, and the railways in this region are in an isolated local network with Quetta and Peshawar as the center.

Because of its inadequate network structure, the network effects of the logistics infrastructure in western Pakistan have yet to materialize. According to the integral network theory, the accessibility and effect of network from small to large are ranked as follows: two closed local networks, a hub-and-spoke network formed by connecting the main nodes in two closed networks, and a multiple closed network formed by connecting all nodes.<sup>41</sup> The railway and highway networks in western Pakistan belong to the former two networks respectively. Such networks

<sup>38</sup>The transportation network between regions or cities pays more attention to the network structure of criss-cross and interconnection.

<sup>39</sup>The National Highway network is mainly managed by the National Highway Authority (NHA) of Pakistan, including national highways, expressways and strategic roads. *Source*: Ministry of Finance. "Pakistan Economic Survey 2009–10", Government of Pakistan, [http://finance.gov.pk/survey\\_1415.html](http://finance.gov.pk/survey_1415.html).

<sup>40</sup>Looney R.E., Winterford D., "Infrastructure and Regional Development in Pakistan", *Review of Urban and Regional Development Studies*, vol.5 (1993): 95–114.

<sup>41</sup>Liu Jun, *Analysis of the Whole Network*, Gezhi Publishing House, Shanghai People's Publishing House, 2014.

neither make full and effective use of existing nodes nor tap their economic potential, hence weighing on the economic growth of the region and the country at large.

In a nutshell, the development concept for the Site selection for Pakistan's logistics infrastructure is to build an effective network through reasonable site selection, instead of optimizing site selection based on an effective network. According to the network theory, the Site selection for Pakistan's logistics infrastructure should firstly give priority to the construction and improvement of the logistics infrastructure network, and on this basis form the necessary conditions for promoting economic development.

### 8.3.3 *Site Selection for the Kashgar-Gwadar Railway: Let "Structure" Drive Growth of "Volume"*

Different from the traditional regional development concept that highlights investment in "volume", the network development concept gives priority to improving the "structure" of the logistics infrastructure network, since an improved "structure" is the prerequisite and guarantee for giving play to the network effect, scale effect and positive economic externalities, and for increasing economic "volume".

The Kashgar-Gwadar Railway, which is to be built in Khyber-Pakhtunkhwa and Balochistan provinces where the density of highways and railways remains low, is sure to solidify and extend the existing logistics infrastructure network in west Pakistan, as shown in Fig. 8.1. This logistics channel connecting the western major cities of Quetta and Peshawar and the port city of Gwadar will greatly shorten the sailing distance from China, Afghanistan and the inland countries of Central Asia to the Indian Ocean, and gradually change the economic geographic structure of Pakistan and its neighboring countries. Take the developing countries surrounding Pakistan as an example, India started carrying out a large-scale highway network construction plan, namely the Golden Quadrilateral (GQ), since 2001. Compared with the previously built east-west and north-south corridors, the GQ plan has increased the enterprise entry rate and productivity of non-nodal cities along the way.<sup>42</sup> Similarly, the successful development of China's city

<sup>42</sup> Ghani E., Goswami, A.G., Kerr, W.R., "Highway to Success: The Impact of the Golden Quadrilateral Project for the Location and Performance of Indian Manufacturing", *The Economic Journal*, vol.126, Issue 591 (2015): 317-357.

clusters shows that the “networking” of traffic lines can drive the common economic growth of the cities within the network and bridge their development gap.<sup>43</sup>

The location of CPEC's logistics channel in western Pakistan, in addition to improving the whole country's logistics network, creates positive externalities of local economy. On the one hand, the Sino-Pakistan trade potential can guarantee stable source of goods for CPEC and help cultivate the local logistics market of western Pakistan. In 2015, the total value of China's imports from and exports to Pakistan reached 117.589 billion yuan, of which only 1.966-billion-yuan worth of goods flew through the ports in Xinjiang,<sup>44</sup> showing that there is room for further tapping the China-Pakistan trade potential.<sup>45</sup>

After the construction of CPEC is completed, the distance between China and the Indian Ocean can be shortened by up to 85 percent, which will greatly motivate China's central and western provinces to trade with the countries in South Asia (especially Pakistan), Europe and Africa through this corridor, thereby driving the development of the local logistics market along the way. In fact, since the launch of CPEC in 2013, Pakistan has witnessed an upward trend in software indicators such as the Logistics Performance Index (LPI) and services, although the ranking of hardware indicators has not changed or even declined slightly. This shows that the local logistics market has been activated and started to develop, as shown in Table 8.1. By the end of June 2016, Gwadar Port in western Pakistan had acquired basic operational capability. On November 12, 2016, CPEC Joint Trade Convoy, which was composed of more than sixty trucks, reached western Pakistan by passing through the overland logistics channel connecting Kashgar, Xinjiang and Gwadar Port for the first time. After shipment at Gwadar Port, this batch of goods was transited to the

<sup>43</sup> Li Yuwei, Ni Pengfei, “Externalities, Transportation Networks and Economic Growth of Urban Agglomerations”, *Chinese Social Sciences*, no.3 (2013): 22–42.

<sup>44</sup> “Table of Total Value of Import and Export Commodities by Country (Region) in December 2015”, General Administration of Customs of China, <http://www.customs.gov.cn/publish/portal0/tab49667/info785132.htm>, January 21, 2016.

<sup>45</sup> Gao Zhigang, Zhang Yan, “Study on the Potential and Efficiency of Bilateral Trade in the Construction of the China-Pakistan Economic Corridor: Based on the Analysis of Stochastic Frontier Gravity Model”, *Science of Finance and Economics*, no. 11 (2015): 101–109.

**Table 8.1** Ranking of Pakistan's LPI in the world

Year	LPI	Hardware index			Software index		
		Customs	Infrastruc ture	International freight	Logistics quality & competitiveness	Tracking & tracing	Timeliness
2012	71	46	71	68	72	90	83
2014	72	58	69	56	75	86	123
2016	69	71	69	66	68	67	58

Note: The "year" in the table is the year of assessment which is based on the situation and data of the previous year

Source: Arvis, Jean-François et. al, "Connecting to Compete 2016: Trade Logistics in the Global Economy", World Bank Report, <http://lpi.worldbank.org>, 2016

overseas markets including the Middle East and Africa,<sup>46</sup> heralding an era where the logistics market in western Pakistan will be activated and begin to develop rapidly.

Besides, if the strategic goals of CPEC were achieved, the manufacturing industry along the corridor would have greater development opportunities, thereby forming the primary traffic demand for the local logistics market. The construction of CPEC has never been narrowly defined as a logistics corridor, because it is designed to open a new page for the comprehensive cooperation between China and Pakistan in all fields (not limited to energy) with infrastructure as the starting point. At present, Chinese companies have found huge room for cooperation with Pakistan in multiple fields such as electrical appliance manufacturing, agriculture, and textile. In 2015, at the meeting of the Working Group of CPEC Joint Cooperation Committee chaired by Ahsan Iqbal, Pakistan's Minister of Planning and Development, the representatives from Punjab, Sindh and Khyber-Pakhtunkhwa submitted their site selection plans for the economic and industrial parks along the corridor, and introduced the road connectivity and logistics infrastructure construction for the industrial parks.<sup>47</sup> At the beginning of 2016, the Government of Khyber-Pakhtunkhwa issued

<sup>46</sup> Chongyang Institute of Finance, Renmin University of China, Finance Magazine: "China-Pakistan Economic Corridor Field Research Report", <http://www.rdcy.org/displaynews.php?id=28599>, December 20, 2016.

<sup>47</sup> "Determination of Intention for Site selection for China-Pakistan Economic Corridor Economic Industrial Park", Ministry of Commerce website, <http://www.mofcom.gov.cn/article/i/jyj/j/201510/20151001134202.shtml>, October 25, 2015.

the provincial industrialization policy for the first time, trying to create an attractive environment for industrial investment through tax reduction and exemption, process simplification, and improvement of supporting services.<sup>48</sup> Western Pakistan is rich in mineral resources. Take the mining of copper and gold in China as an example, the cost of obtaining the mining right for one million tons of copper or gold is more than one billion yuan, but such cost in Pakistan is as low as about 100 million yuan. To date, the Sino-Pak joint venture Kodali Mining Co., Ltd. has, from the mining departments under the Federal Government of Pakistan and the Provincial Government of Balochistan, obtained the mineral exploration and development rights covering an area of 1200 km<sup>2</sup>.<sup>49</sup> It shows that while the construction of logistics infrastructure is underway, the development of other industries has been put on the right track, injecting new vitality into the economic development of the western Pakistan and the country at large.

In short, from the perspective of network development and in the context of CPEC's construction, the site location of logistics infrastructure in western Pakistan will help to make up for the shortcomings of the traditional development concept in terms of necessary conditions and logistics network construction, and balance the development of regional economy.

#### 8.4 FROM "ROUTE" TO "NETWORK": SUGGESTIONS

CPEC is a long-term strategy, a flagship project and a demonstration project of BRI. In order to achieve the established goals of CPEC, China should think about how to improve Pakistan's logistics infrastructure network through the construction of both logistics channels and supporting facilities, so as to promote the network-based development of Pakistan's logistics industry, and form an economic network that coordinates the development of logistics and manufacturing industries.

<sup>48</sup> "Pakistan's Cape Province's first industrialization policy attracts attention", Economic Daily website, [http://paper.ce.cn/jjrb/html/2016-02/26/content\\_294014.htm](http://paper.ce.cn/jjrb/html/2016-02/26/content_294014.htm), February 26, 2016.

<sup>49</sup> "China National Assets Industry Park "First Hand" China-Pakistan Economic Corridor", China Enterprise News website, [http://epaper.zqcn.com.cn/content/2015-04/28/content\\_8129.htm](http://epaper.zqcn.com.cn/content/2015-04/28/content_8129.htm), April 28, 2015.

#### 8.4.1 *Improve Investment and Political Factors, and Promote the Construction of Logistics Infrastructure*

Among the necessary conditions for logistics infrastructure to promote regional development, in addition to positive economic externalities, Pakistan's investment and political conditions also need to be further improved. However, it is hard to do so because of the country's complex ethnic and political contradictions.

In terms of investment, part of Pakistan's funds for logistics infrastructure construction and operation come from foreign aid and private capital, and most of these funds are hardly stable or sustainable due to certain restraints or the geopolitical and strategic interests of donor countries. The other part comes from the Public Sector Development Program (PSDP) of the Pakistani government. Since the PSDP funds are allocated on a departmental basis rather than on a provincial basis, the political favoritism of competent authorities has resulted in large regional differences in fund allocation. Even if there may be fund allocation by province, it is just a drop in the ocean.

In terms of politics, because of long-standing ethnic and religious conflicts, political rivalry in Pakistan often impedes economic affairs, causing low efficiency in economic planning and decision-making. What's worse, the lack of an independent national-level transportation department has caused inefficient implementation of plans and decisions. Amid the dispute over the location of CPEC's logistics channel in Pakistan, the nationalist forces and local ruling parties first wrangled over the necessity of this channel and then fought to be the preferred site of this channel. No party was willing to yield an inch, hence making the planning and implementation of this logistics channel an outstanding issue.<sup>50</sup> Besides, inefficient implementation of existing plans and projects is another chronic disease in Pakistan.<sup>51</sup> The country has a separate Ministry of Railways, but the National Highway Authority (NHA) and port authorities are subordinate

<sup>50</sup>Liang Tong, "When Will CPEC and Belt and Road Really Make Their Presence Felt", *Observer.com*, [http://www.guancha.cn/liangtong/2015\\_06\\_03\\_321901\\_s.shtml](http://www.guancha.cn/liangtong/2015_06_03_321901_s.shtml), June 3, 2015.

<sup>51</sup>Measood M.T., "Transportation Problems in Developing Countries Pakistan: A Case-in-Point", *International Journal of Business and Management*, 2011, vol.6, No.11, 256–266; Stough R.R., "A National Transport Policy: the Case of Pakistan", in Stimson R., Haynes K.S., ed., "Studies in Applied Geography and Spatial Analysis: Addressing Real World Issues", Edward Elgar Publishing, 2012.

to the Ministry of Communications (MOC). The planning for transportation and logistics requires the participation of highway, railway and port authorities, but lack of coordination often goes against the work in need of multi-departmental participation.

This shows that investment factors and political factors in Pakistan are closely interrelated. In order to implement the planned CPEC projects as soon as possible, China and Pakistan should firstly try a variety of financing options, such as absorption of private capital, so as to provide stable funds for CPEC projects. The construction of CPEC is so costly that it is unrealistic for China itself to provide concessional loans. Appropriate policies should be introduced to support Chinese and Pakistani banks to work together as partners, and motivate private capital to invest in CPEC's supporting projects. Joint participation and shared interests between all parties are better ways to maintain stable investment in the long run. Secondly, the Federal Government of Pakistan should do a good job in transferring payment in the secondary fund allocation, and try to allocate resources on the basis of regional and project priorities, so as to guarantee a fair and equitable result of allocation. Finally, in order to implement CPEC projects, the two countries have developed the Long-term Plan (2017–2030), established the Joint Cooperation Committee, and held meetings in a regular manner, but they still need to make more efforts to vigorously promote the project construction. Pakistan may think about establishing a unified transportation department that coordinates diverse modes of transportation, which will benefit the construction of logistics infrastructure and its subsequent operation and management.

#### *8.4.2 Build a Western Logistics Channel Covering Multiple Modes of Transportation and Improve the Network Structure of Logistics Infrastructure*

At present, most of the logistics infrastructure projects under CPEC are highway projects that are to be built in western Pakistan. However, CPEC is a typical mini landbridge from the perspective of transportation geography,<sup>52</sup> implying that a single mode of transportation cannot fully perform the function of a “land bridge”, “corridor” or “passage”. Therefore, if the Western Route Plan is preferred, we suggest that railways

<sup>52</sup>The mini land bridge refers to the use of land connections in the transportation chain, and includes an exotic starting point and a continental end terminal.



projects in western Pakistan should be started as soon as possible, in an aim to build a land passage made up of both highways and railways and improve the country's overall logistics infrastructure network.

From a technical and economic point of view, Pakistan's economic development requires the support of railway transportation. First of all, compared with highways that are suitable for short-distance transport, railways are preferred for medium or long-distance and mass transportation and more conducive to the cargo with low value-to-weight ratio.<sup>53</sup> Textile, energy and mining are mainstay industries in Pakistan, while the reserves of natural gas, coal, ferrochrome, copper, sulfur and marble in western province of Balochistan account for 50 percent of the country's total mineral resources.<sup>54</sup> Since these materials are large in size and weight, their long-distance transportation by railway is more economical. Secondly, it is not true that Pakistan's railway transportation has neither development potential nor value. For a long time, railway transportation has been downplayed by all sectors of Pakistani society, and mainly used for passenger traffic, even though freight revenue is much larger than passenger revenue. The reason why Pakistan's railway operations survive to date despite of long-term losses owes to the subsidy from freight revenue.<sup>55</sup> After the launch of a large number of highway projects under CPEC, the World Bank lowered the evaluation of Pakistan's highway quality, but raised the evaluation of its railway quality, as shown in Table 8.2. Correspondingly, in 2013, Pakistan's railway freight turnover increased significantly from the previous 401.9 million ton-kilometers to 109 million ton-kilometers, and further rose to 330 million ton-kilometers and 350 million ton-kilometers in 2014 and 2015.<sup>56</sup> This shows that

<sup>53</sup> Redding S., J., Turner, M., A., "Transportation Costs and the Spatial Organization of Economic Activity", in Gilles Duranton, J.Vernon Henderson, William C. Strange ed., "Handbook of Regional and Urban Economics Volume 5 B", North-Holland, 2015.

<sup>54</sup> Liu Weiguo, "Survey Report on the Economic Status of Pakistan's Balochistan Province", website of the Economic and Commercial Office of the Consulate General of the PRC in Karachi, <http://www.mofcom.gov.cn/aarticle/i/dxfw/cj/200710/20071005160574.html>, Oct 5, 2007.

<sup>55</sup> Sánchez-Triana E., Afzal J., Biller D., Malik S.", Greening Growth in Pakistan through Transport Sector Reforms: A Strategic Environmental, Poverty, and Social Assessment", World Bank, 2013.

<sup>56</sup> Ministry of Finance, "Pakistan Economic Survey 2015–16", Government of Pakistan, [http://finance.gov.pk/survey/chapters\\_16/13\\_Transport.pdf](http://finance.gov.pk/survey/chapters_16/13_Transport.pdf).

**Table 8.2** Pakistan's infrastructure quality in the world ranking

<i>Year</i>	<i>Overall quality of infrastructure</i>	<i>Highway</i>	<i>Railway</i>	<i>Port</i>	<i>Aviation</i>
2013–2014	119	72	75	55	88
2014–2015	113	75	72	59	92
2015–2016	98	77	60	66	79

Note: The “year” in the table is the year of assessment which is based on the situation and data of the previous year

Source: Arvis, Jean-François et. al, “Connecting to Compete 2016: Trade Logistics in the Global Economy”, World Bank Report, <http://lpi.worldbank.org>, 2016

highways, after they are greatly improved, may share the railway passenger traffic and then give play to the potential of railways in freight transportation. Finally, western Pakistan doesn't have any north-south railway at present; therefore, if the two local logistics networks centered on Quetta and Peshawar could be connected by a railway, it would have a greater network effect on the west and the whole country.

The construction of a railway linking China and western Pakistan, which is both China's initial plan and Pakistan's social appeal, can help improve Pakistan's entire logistics network structure. At first, China planned to build two strategic railways in Pakistan through bilateral cooperation: the Kashgar-Peshawar-Quetta Railway and the Quetta-Gwadar Railway.<sup>57</sup> But the implementation of this plan has been progressing slowly for all kinds of reasons, and not included in the Early Harvest Program (EHP). Recently, the Committee on Underdeveloped Areas in Pakistan began to ask the Federal Government to upgrade the railways (namely the Kandahar-Chaman-Bostan-Zhob-DI Khan Railway and the Bisma-Quetta-Malakand-Dargi Railway) as soon as possible under the framework of CPEC's Western Route Plan.<sup>58</sup> Given this, with the deepening of the construction of CPEC, the China-Western Pakistan Railway Project should be started as soon as possible.

<sup>57</sup> “China Research on China-Pakistan Railway Project”, Strategic Network, [http://mil.chinaiiss.com/html/20146/30/a6d099\\_3.html](http://mil.chinaiiss.com/html/20146/30/a6d099_3.html), June 30, 2014.

<sup>58</sup> “Relevant Departments of Pakistan Call for Railway Upgrade and Transformation on the West Line of the China-Pakistan Economic Corridor”, Ministry of Commerce website, <http://www.mofcom.gov.cn/article/i/jyj/j/201604/20160401296045.shtml>, April 14, 2016.

#### *8.4.3 Cultivate the Industry Network Corresponding to the Logistics Network, and Coordinate the Development of Manufacturing and Logistics Industries*

Lack of infrastructure is a problem that needs to be solved urgently in Pakistan. However, we should realize that logistics infrastructure is only the hardware part of a logistics channel. In order to ensure smooth flow of goods, a logistics channel also needs the software support, that is, the agglomeration of logistics companies and the vigorous development of logistics market.

For a long time, all circles have attached great importance to the spatial changes of CPEC's logistics infrastructure network, but overlooked the changes in its logistics organization and operation network, that is, "highlighting carriers and downplaying subjects". At present, Pakistan's logistics organization is still difficult to make rapid adjustment to adapt to the spatial changes of infrastructure. In Pakistan, the logistics industry is dominated by small companies (most of which have less than fifteen employees) and mainly engage in freight forwarding.. Only 45 percent of logistics companies provide comprehensive third-party or fourth-party logistics services, but they occupy 83 percent of Pakistan's logistics market. Most of these companies are in fact local offices and representatives of large international companies, or agents of joint ventures with other countries.<sup>59</sup> The provision of comprehensive logistics services relies on networked operations, but most freight forwarders in Pakistan only operate one office responsible for local small-scope cargo canvassing,<sup>60</sup> and they are mainly distributed in the eastern provinces.

With the construction of CPEC's logistics channel, especially the implementation of the Western Route Plan, how to guide Pakistan's logistics companies to concentrate in the western region through incentives and preferential policies has become an issue worthy of discussion. In our opinion, the development of logistics industry is inseparable from its primary traffic demand from manufacturing industry. It means that the development of the logistics industry in western Pakistan should be combined with the layout of industrial parks along the way, so as to create a

<sup>59</sup>World Bank, "Transport Competitiveness in Pakistan: Analytical Underpinning for National Trade Corridor", Report No.36523-PK, 2006.

<sup>60</sup>Hine J.L., Chilver A.S., "Pakistan Road Freight Industry: An Overview", *Transport and Road Research Laboratory*, Research Report 314, 1991.

landscape where manufacturing and logistics industries promote each other and develop in a coordinated way. To this end, efforts must be made to firstly introduce certain land policies in favor of western Pakistan's logistics industry, and provide preferential treatment and a favorable operating environment for local logistics companies. Secondly, logistics companies are encouraged to take part in the production, procurement and distribution links of local manufacturing industry or cooperate with manufacturing companies' internal logistics departments, so as to seek a coordinated development model suitable for all industries. Thirdly, straighten out the government administration of freight transport and logistics companies. The Pakistani government has not realized that freight forwarding and logistics are counted as an industry until recent years. The lack of management and guidance on logistics market has resulted in fierce competition and made it difficult to cultivate large-sized and networked private companies in the domestic logistics country. Besides, Pakistan may think about allowing certain large-sized state-owned logistics companies, such as NLC, to join in market-oriented logistics business to enhance their corporate competitiveness. Finally, promote the application of modern logistics information technology and network technology, and help logistics companies realize networked and scale operation to provide better services.



# Terrorism→Poverty→Road Building: Risk Analysis of the Underlying Logic of the CPEC Infrastructure

*Cheng Zhongxing*

## 9.1 TOPICS IN THIS CHAPTER

“Terrorism→poverty→road building”, to a considerable extent, can be said to be the basic logic of the construction of CPEC—the flagship project of BRI.

On the one hand, terrorism is the biggest strategic risk that China faces in opening to the west. In the foreseeable future, no country along the Belt and Road is strategically capable of posing a lasting threat to China. At present, the only thing that China is worried about is the threat of terrorism that has a profound impact on the country’s long-term stability, especially the terrorist forces seeking “Xinjiang Independence”.

On the other hand, the technological route formed after the founding of the People’s Republic of China has accumulated unparalleled infrastructure capabilities in practice after the reform and opening up, especially the

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road building capacity represented by high-speed railway, which meets the greatest strategic needs of the countries along the Belt and Road. It is this capacity, combined with China's huge foreign exchange reserves, that gives the connectivity of BRI a realistic basis.

The question is, can the infrastructure capacity, which is represented by road building, eliminate the threat of terrorism faced by BRI? In this regard, the mainstream opinion leans heavily towards the affirmative. In this view, terrorism is rooted in poverty, while roads and other infrastructure are preconditions for eradicate poverty. Guided by the infrastructure logic of "terrorism→poverty→road building", most of the US\$46 billion projects involved in CPEC is invested in infrastructure (see Table 9.2).

However, is terrorism really rooted in poverty? After roads are built, would poverty be then eliminated? In fact, the logical chain of "terrorism→poverty→road building" contains great uncertainties, but the strategic risks it brings are also worrying. Details are given below.

## 9.2 DOES POVERTY LEAD TO TERRORISM?

The attribution of terrorism to poverty first comes from a spatial intuition. According to the cumulative spatial distribution map of terrorist attacks in forty-five years from 1970 to 2015, it is easy to see two important spatial characteristics of the distribution of terrorism: It is concentrated in impoverished areas where residents mostly believe in Islam.<sup>1</sup>

Perhaps based on this spatial intuition, former US President Barack Obama believes extreme poverty provides the ideal breeding ground for disease, terrorism and conflict. To solve the problem of terrorism, poor countries should be provided with more development assistance. However, can spatial intuition be further supported by science?

In this regard, based on the level of analysis units in social sciences, this paper will explore the causal mechanism between terrorism and poverty from three dimensions (individual dimension, organizational dimension, and national dimension).

First, at the individual level. As early as 1968, Becker put forward an explanatory framework for the economics of crime,<sup>2</sup> arguing that whether a person commits a crime is related to his assessment and choice of the

<sup>1</sup>The Global Terrorism Database (GTD), <https://www.start.umd.edu/gtd/>.

<sup>2</sup>Becker, Gary S.1968. "Crime and Punishment: An Economic Approach". *Journal of political economy*. March/April, 76: 2, pp. 160–217.

benefits and costs of crime. If the cost is too great, people will not commit a crime; but if the benefit exceeds the cost, they will commit a crime “rationally”. However, researchers have found that<sup>3</sup> although low-income people are more likely to commit “property crimes”, violent crime, however, rarely has anything to do with economic income.<sup>4</sup> By analogy, the link between terrorism and poverty is not compelling. Suicidal terrorist attacks, for example, are clearly not motivated by the pursuit of economic gains (the individual is dead and unable to enjoy it). Even if terrorist groups may promise to give pension to the dependents of those who will take their lives, the “middleman” who commits suicide (presumed by the model) could only dream in another world that this empty promise would be honored.

Landes,<sup>5</sup> Todd Sandler and others<sup>6</sup> have tested the above explanatory framework, and found that different terrorists have greatly different perceptions of the benefits and costs of terrorist acts, and that there is little direct correlation between poverty of individuals and their terrorist acts.

Since Becker’s explanatory framework at the individual level is not convincing, researchers put forward an explanatory framework based on economic sociology at the organizational level.<sup>7</sup> In 1999, Jefferson and others analyzed the characteristics of the “hate groups”. Using data on more than 300 so-called “hate groups” in 3100 counties across the United States, they analyzed in detail their relationship with unemployment rate, divorce rate and the difference in average personal income between blacks

<sup>3</sup> Isaac Ehrlich.1973. “Participation in Illegitimate Activities: A Theoretical and Empirical Investigation”. *Journal of Political Economy*. 81: 3, pp. 521–65. Richard B. Freeman. “Why Do So Many Young American Men Commit Crimes and What Might We Do About It?” *Journal of Economic Perspectives*. 10: 1, pp. 25–42.

<sup>4</sup> Piehl, Anne Morrison.1998. “Economic Conditions, Work, and Crime” in Michael Tonry, ed., *Handbook on Crime and Punishment*, edited by Michael Tonry, 302–319. New York: Oxford University Press. Christopher J. Ruhm. 2000. “Are Recessions Good for Your Health?” *The Quarterly Journal of Economics* 115: 2, pp. 617–650.

<sup>5</sup> Landes, William.1978. “An Economic Study of U.S. Aircraft Hijackings, 1961–1976”. *Journal of Law and Economics*. 21: 1, pp. 1–31.

<sup>6</sup> Todd Sandler, John T. Tschirhart and Jon Cauley. 1983. “A Theoretical Analysis of Transnational Terrorism”. *American Political Science Review*. 77: 1, pp. 36–54.

<sup>7</sup> Kressel, Neil J. 1996. *Mass Hate: The Global Rise of Genocide and Terror*. New York: Plenum Press. Mark S. Hamm, 1998. “Terrorism, Hate Crime, and Antigovernment Violence: A Review of the Research”. In: *The Future of Terrorism: Violence in the New Millennium*. Harvey W. Kushner, ed. London: SAGE, pp. 59–96.

and whites in these counties. It turns out that the economic and social explanations for “hate groups” are far less important than other external environmental factors.<sup>8</sup> Coincidentally, Krueger and others analyzed ethnic violence incidents in 543 counties in Germany in the early 1990s, and found that there was no significant correlation between violence incidents and people’s income.<sup>9</sup> In addition, according to the survey data of the Palestinian Center for Policy and Survey Research (PCPSR),<sup>10</sup> it was found that in the years before the “9.11 Event”, that is, from 1998 to 2000, the economic situation of Palestinians living in the West Bank and Gaza Strip showed a trend of improvement rather than deterioration (Table 9.1). It can be seen that there is no direct connection between local terrorist activities and poor economic condition.

In conclusion, there is no direct causal relationship between poverty and terrorism at either the individual level or the organizational level. Is there a causal link between poverty and terrorism at the national level? In other words, do poor countries export more terrorists than rich ones? Krueger, a well-known American terrorism researcher, analyzed 956 terrorist cases from 1997 to 2003 and found that the countries with the poorest economy and the lowest literacy rate did not export more terrorists. And the statistical tests even found a negative correlation in suicide attacks. In other words, the poorest countries are the least likely to be the hotbed of suicide attacks.<sup>11</sup>

Even so, people still believe that poverty is an important cause of terrorism. For example, it is easy to find that economic depression is a catalyst for political and social conflicts in a country.<sup>12</sup> This paper holds that although poverty is not a statistically significant cause of terrorism, it can partially explain (as an independent variable) some actual cases of terrorism, because what statistical significance tests always tell us is probabilistic causation.

<sup>8</sup> Philip N. Jefferson and Frederic L. Pryor. 1999. “On the Geography of Hate”. *Economics Letters*. 65: 3, pp. 389–395.

<sup>9</sup> Alan B. Krueger, Jorn-Steffen Pischke. 1997. “A Statistical Analysis of Crime Against Foreigners in Unified Germany”. *Journal of Human Resources*. 32: 1, pp. 182–209.

<sup>10</sup> <http://www.pcpsr.org>.

<sup>11</sup> Alan B. Krueger. *What Makes a Terrorist: Economics and the Roots of Terrorism*. Princeton University Press, 2008.

<sup>12</sup> Paul Collier & Anke Hoeffler, 2004. “Greed and grievance in civil war”. *Oxford Economic Papers* 56 (2004), pp. 563–595.



**Table 9.1** PCPSR survey on the economic status of residents over 18 years old in the West Bank and Gaza Strip<sup>a</sup>

<i>Date</i>	<i>Unemployment rate</i>	<i>Financial condition improved in the past three years</i>	<i>Financial condition deteriorated in the past three years</i>	<i>Optimistic about their financial condition over the next three years</i>	<i>Pessimistic about their financial condition over the next three years</i>
Mar 1995	38	37.5	31.2	50.8	29.2
Mar 1996	49				
Nov 1997	27				
Jul ~ Aug 1998	26				
Oct 1998	29				
Nov 1998	24				
Jan 1999	25				
Apr 1999	20	39.2	27.6	50.4	27.5
Jun 1999	20				
Jul 1999	18				
Sep 1999	23				
Oct 1999	17				
Dec 1999	19				
Jan 2000	23				
Feb 2000	19	43.3	24.6	55.8	27.2
Mar ~ Apr 2000	17				
Dec 2001	21				

Unit: %

Source: PCPSR polls conducted at various times, <http://www.pcpsr.org/en/search/node/files>

<sup>a</sup>Alan B. Krueger; Jitka Maleková. "Education, Poverty and Terrorism: Is There a Causal Connection?" *The Journal of Economic Perspectives*, Vol. 17, No. 4. (Autumn, 2003), pp. 119–144

So far, we have found that the spatial intuition of poverty and terrorism is far from certain. The same is true if we apply spatial intuition to the implement of CPEC.<sup>13</sup>

The most severe terrorist attacks were concentrated in the Federally Administered Tribal Areas (FATA) in northwestern Pakistan and Sindh Province in the southeast. The Pakistan's economic data reflect a

<sup>13</sup>South Asia Terrorism Portal. [http://www.satp.org/satporgtp/southasia/images/Conflict\\_Map.html](http://www.satp.org/satporgtp/southasia/images/Conflict_Map.html).

paradoxical phenomenon: The two most terrorist-prone areas in Pakistan are at two extremes economically: One is the poorest (FATA) and the other is the richest (Sindh). In the FATA, animal husbandry and opium cultivation are the main sources of income, and the per capita GDP is only US\$663. By contrast, Sindh is the industrial and financial center of Pakistan, with a per capita GDP of US\$1500.<sup>14</sup> Evidently, from a spatial perspective, we may draw a conclusion that poverty and terrorism have a direct causal connection with the FATA as an example, or we may come to the conclusion that terrorism and poverty are not directly causally related if we take Sindh as an example. Then which one is correct?

In the spring of 2009, Graeme Blair and other researchers surveyed 6000 people in four provinces of Pakistan: Punjab, Sindh, Baluchistan and Khyber-Pakhtunkhwa.<sup>15</sup> The scale of this survey was unprecedented, covering vast rural areas, and finally four conclusions were drawn:

1. The respondents generally have a negative attitude towards terrorist activities;
2. Those who live in areas with frequent terrorist activities, especially the residents of Khyber-Pakhtunkhwa, are more averse to terrorism;
3. Poor Pakistanis hate terrorism more than twice as much as middle class Pakistanis;
4. The urban poor are the group that hates terrorism the most among all residents.

At this point, we can basically conclude that the idea that poverty is the root cause of terrorism is questionable, and eliminating the risk of terrorism in CPEC by reducing poverty may not be the way to go. In 2009, the United States issued the Kerry-Lugar-Berman Act to provide Pakistan with US\$7.5 billion in aid to combat terrorism. However, little has been achieved after seven years have passed. In the process of CPEC construction, the first thing we need to overcome is dogmatism in the context of economic determinism, because this is the illusion that terrorism has challenged and will continue to challenge in the future.

<sup>14</sup> According to Pakistan's 2009 statistics, the country's GDP per capita at the provincial level is: Sindh (US\$1500), Punjab (US\$1200), Baluchistan (US\$757), FATA (US\$663), in descending order.

<sup>15</sup> Graeme Blair, C. Christine Fair, Neil Malhotra, Jacob N. Sha. *Pakistan's Middle Class Extremists: Why Development Aid Won't Solve Radicalism?* <https://www.foreignaffairs.com/articles/pakistan/2011-07-11/pakistans-middle-class-extremists>.

### 9.3 CAN ROAD BUILDING HELP TO ELIMINATE POVERTY?

“If you want to be rich, build roads first”. “A railway can bring along 500 kilograms of gold”. These Chinese proverbs perfectly explain the essence of economic development after the war. As the largest developing country in the world, China has not only held the two proverbs as a guideline, but also gradually formed an unparalleled infrastructure capacity in practice. In the Hollywood movie “2012”, the Noah’s Ark that finally saves human civilization is also made in China. Particularly worth mentioning is the high-speed railway, which is known as “the only strategic industry developed by China since the reform and opening up that can change the basic international and domestic political and economic pattern in the 21st century”,<sup>16</sup> which can be described as a representative of China’s powerful infrastructure capacity. It is not difficult to find that this capacity has been extended to the US\$45.04 billion CPEC projects (Table 9.2).

Table 9.2 shows us the logic of “poverty alleviation through transportation” in CPEC. Before we examine the implications of Table 9.2, we need to answer this question: Can we get rich once the road is built?

Mr. Fei Xiaotong, who had been “aspiring to enrich the people” all his life, also raised this question during his survey trip along the Beijing-Kowloon Railway in his later years. He took the Longhai Line (i.e., a railway connecting Lanzhou of Gansu with Lianyungang of Jiangsu) as an example. This line has been in operation for nearly a hundred years, but the cities along the line have not developed. The Beijing-Kowloon Railway has to avoid such embarrassing situation.<sup>17</sup>

In fact, in the field of development economics, both Rodan’s “Big Push” theory<sup>18</sup> and Rostovian’s “Take-off” model<sup>19</sup> regard transportation as the social overhead capital for economic growth. However, “transportation first” has not produced the expected effect in the practice of most developing countries. Zhang Xueliang, a Chinese scholar, by using China’s

<sup>16</sup>Gao Bai, *China’s High-Speed Rail and the 21st Century Grand Strategy*, Beijing: Social Sciences Academic Press (China), 2012.

<sup>17</sup>Fei Xiaotong, What Has Beijing-Kowloon Railway Bring About? In *Collected works of Fei Xiaotong*, Qunyan Publishing House, 1999.

<sup>18</sup>Paul Rosenstein-Rodan, “Problems of Industrialization of Eastern and South-Eastern Europe”, *The Economic Journal*, Vol. 53, nos.210/211, June-September 1943, pp. 202–211.

<sup>19</sup>W.W. Rostow, *The Stages of Economic Growth: A Non-Communist Manifesto*, Cambridge: Cambridge University Press, 1960.

**Table 9.2** List of CPEC projects

<i>No.</i>	<i>Energy priority projects</i>	<i>Estimated investment (US\$ million)</i>
1	Port Qasim Electric Company Coal Fired, 2*660, Sindh	1980
2	Sahiwal 2*660MW Coal Fired Power Plant, Punjab	1600
3	Engro Thar 4*330MW Coal Fired, Thar, Sindh	2000
	Surface mine in Block II of Thar Coal Fired, 6.5mtpa, Thar Sindh	1470
4	Gwadar Coal Power Project, Gwadar	360
5	HUBCO coal power plant 1*660MW, Hub Balochistan	970
6	Rahimyar Khan Coal Power Plant, Punjab	1600
7	SSRL Thar Coal Block I—6.5mtpa, Thar, Sindh	1300
	SSRL 2*660MW Mine Mouth Power Plant	2000
8	Quaid-e-Azam 1000MW Solar Park, Bahawalpur, Punjab	1350
9	Dawood 50MW Wind Farm, Bhambore, Sindh	125
10	UEP 100MW Wind Farm, Jhimpir, Sindh	250
11	Sachal 50MW Wind Farm, Jhimpir, Sindh	134
12	Sunnec 50MW Wind Farm, Jhimpir, Sindh	125
13	Suki Kinari Hydropower Station, KPK	1802
14	Karot Hydropower Station, AJK & Punjab	1420
15	Matiari to Lahore Transmission Line	1500
16	Matiari to Lahore Transmission Line	1500
17*	Gaddani Power Park Project	
	(i) 2*660MW	3960
	(ii) Jetty + Infrastructure	1200
18*	HUBCD coal power plant 1*660MW, Hub Balochistan	970
19*	Salt Range Mine Mouth Power Project including mining including mining, Punjab	800
20*	Kohala Hydrel Project, AJK	2397
21*	Pakistan Wind Farm II 2*50MW (Jhimpir, Thatta, Sindh)	150
22*	Thar Mine Mouth Oracle, Thar, Sindh	1300
23*	Muzaffargarh Coal Power Project, Punjab	1600
24*	Gas Power Plant 525MW	550
	Total	34413
<i>No.</i>	<i>Transportation infrastructure projects</i>	<i>Estimated investment (US\$ million)</i>
	Highway	
1	KKH Phase II (Raikot-Islambad Section)	3500
2	Peshawar-Karachi Motorway (Multan-Sukkur Section)	2600
	Railway	
1	Expansion and reconstruction of existing Line ML-1	3650
2	Havelian Dry Port (450M. Twenty-Foot Equivalent Units)	40
	Total	9790

*(continued)*

**Table 9.2** (continued)

<i>No.</i>	<i>Gwadar Port-related projects</i>	<i>Estimated investment (US\$ million)</i>
1	Eastbay Expressway	140.60
2	Gwadar International Airport	230.00
3	Construction of Breakwaters	123.00
4	Dredging of berthing areas & channels	27.00
5	Infrastructure for Free Zone & EPZ port related industries	32.00
6	Necessary Facilities of Fresh Water Treatment and Supply	130.00
7	Hospital at Gwadar	100.00
8	Technical and Vocational Institute at Gwadar	10.00
	Total	793.00
<i>No.</i>	<i>Other projects</i>	<i>Estimated investment (US\$ million)</i>
1	Cross Border Optical Fiber Cable	44
2	DTMB	
	Total	44
	CPEC total investment	45,040

Source: The data are sorted out according to the information and data made public on the website of Pakistan Board of Investment (BOI)

provincial panel data from 1993 to 2009 and the research method of spatial econometrics, calculated the output elasticity value of China's transportation infrastructure to regional economic growth as about 0.05–0.07,<sup>20</sup> which is far from the 0.39 obtained by Aschauer<sup>21</sup> by employing the neo-classical economic growth model. Besides, Zhang also found that the spatial spillover effect produced by China's infrastructure is evident. In other words, improved transportation may make it easier for production factors to flow to economically developed areas, thereby widening the regional gap. This is also corroborated by China's per capita GDP: In the ten years of the Western Development, the gap in per capita GDP between the east and the west has widened from 7000 yuan in 2000 to 21,000 yuan in 2010.

<sup>20</sup>Zhang Xueliang, "Has China's Transportation Infrastructure Promoted Regional Economic Growth—Also on the Spatial Spillover Effect of Transportation Infrastructure", *Social Sciences in China*, 2012, Issue 3, pp. 60–77.

<sup>21</sup>Aschauer D. A. (1989). "Is public expenditure productive?". *Journal of Monetary Economics*, 23 (2), pp. 177–200.

Not only that, different roads produce different results. Chinese scholar Zhang Guangnan and others used China's provincial panel data from 1989 to 2008 to explore the effect of "poverty alleviation through transportation". Their study found that the construction of railways and sub-standard highways in China's "poverty alleviation through transportation" project has promoted economic growth and increased the speed of regional economic convergence, thus achieving the goal of reducing regional economic disparity and poverty reduction; however, the economic losses caused by excessive investment in classified highways, such as diminishing marginal returns, crowding out effect and traffic corruption, have slowed down the convergence speed of regional economies.<sup>22</sup>

So far, we can preliminarily draw such a conclusion: Road construction is the overhead capital of poverty alleviation, and its effects can be large or small. There is no doubt about this. The problem lies in the spatial spill-over effect. Because of this effect, road construction sometimes fails to achieve the poverty alleviation effect, but may accelerate the outflow of resources within the region and widen the gap between the region and the outside.

Regarding CPEC, Table 9.2 at least shows the following facts: Pakistan, like China, is a country with an imbalance between the east and the west. However, the US\$45.04 billion investment in CPEC does not correct this imbalance, but accelerates it. Why is that?

On the one hand, Pakistan itself is a country with imbalanced layout of road network in eastern and western provinces. It is not difficult to find that Pakistan's highway density centers on Islamabad and Punjab, and spreads to the surrounding areas, while the railways center on Punjab and Sindh and spread to the surrounding areas. The density difference between the eastern and western road networks is obvious. Take the FATA as an example, the current road density is only 0.17 km/km<sup>2</sup>, which is much lower than the national average of 0.26 km/km<sup>2</sup>. Take Balochistan as another example, although Balochistan is rich in natural resources, the living standards of local people have remained low for years, and the rural poverty rate has even increased by 15 percent.<sup>23</sup> Therefore, the locals

<sup>22</sup> Zhang Guangnan, Zhang Haihui, Yang Quanfa, "Poverty Alleviation by Transport and Regional Economic Gap in China: A Study of Provincial Panel Data from 1989 to 2008", *Journal of Finance Research*, 2011, Issue 8, pp. 26–35.

<sup>23</sup> Qurat ul ain Siddiqui, Understanding Baluchistan, [http://news.dawn.com/wps/wcm/connect/dawn\\_content\\_library/dawn/news/pakistan/balochistan/Understanding\\_Balochistan\\_qs](http://news.dawn.com/wps/wcm/connect/dawn_content_library/dawn/news/pakistan/balochistan/Understanding_Balochistan_qs).

believe that the so-called development projects presided by successive federal governments are not in essence benefiting the locals, but plundering their resources. For example, a large number of road construction projects is “to help the military control us and help Punjabis plunder us... exploitation is being carried out in the name of development”.<sup>24</sup>

On the other hand, the construction of CPEC also has the problem of imbalance between the east and the west. In an article published on the website of Observer ([www.guancha.cn](http://www.guancha.cn)), it lamented that the construction of CPEC was delayed due to the dispute over the route selection and political infighting in Pakistan.<sup>25</sup> However, if the author could further analyze the distribution of CPEC projects, he would find that the route dispute is indeed a reflection of the imbalanced layout of CPEC projects.

First, in terms of the number of projects, of CPEC’s thirty-eight projects, nine are in Sindh, six are in Punjab, four are in Balochistan, and one is in Khyber-Pakhtunkhwa, namely, twenty in the east, fifteen in the west, and three in other regions. It can be seen that the construction of CPEC projects is tilted towards eastern Pakistan.

Second, in terms of project investment, the imbalance between the east and the west is even more obvious. The project investment in the east reaches US\$2.825 billion, while that in the west is only US\$1.03 billion. The former is nearly three times more than that of the latter.

Third, in terms of road construction projects alone, highway projects involving the northwest cost US\$2.6 billion, and railway projects involving the southeast cost US\$3.65 billion. The latter exceeds the former by US\$1 billion.

To sum up, the construction of CPEC may further widen the gap between the east and the west of Pakistan while promoting the economic growth of the country. The “relative deprivation” caused by such a gap is no doubt contrary to the original intention of CPEC, and may exacerbate ethnic disputes within the country. This is undoubtedly worse for Pakistan’s fragile ethnic relations.

<sup>24</sup>Urmila Phadnis, *Ethnicity and Nation-building in South Asia*, New Delhi: Sage Publications, p. 177.

<sup>25</sup>Liang Tong, “When Will CPEC and Belt and Road Really Make Their Presence Felt?” [http://www.guancha.cn/liangtong/2015\\_06\\_03\\_321901\\_s.shtml](http://www.guancha.cn/liangtong/2015_06_03_321901_s.shtml), June 3, 2015.

**Table 9.3** Statistics of terrorist attacks on railways in Pakistan (2000–2016)

<i>Year</i>	<i>Frequency</i>	<i>Death toll</i>	<i>Number of the injured</i>
2000	2	18	40+
2001	0	0	0
2002	0	0	0
2003	0	0	0
2004	2	0	6
2005	7	2	9
2006	0	0	0
2007	4	0	0
2008	0	0	0
2009	0	0	0
2010	11	3	3
2011	37	5	44
2012	30	12	89
2013	18	16	68
2014	8	29	157
2015	9	3	37
2016	6	8	23
Total	134	96	476+

#### 9.4 RISKS IN CPEC'S INFRASTRUCTURE CONSTRUCTION

At this point, we find that the infrastructure logic linking terrorism and road building through poverty is far from certain. The risk of terrorism to the Belt and Road, especially along the Silk Road Economic Belt, is more than China's vast infrastructure capacity can eliminate, and it may even be counterproductive.

First, the infrastructure of CPEC itself may become the target of terrorist attacks. Pakistan has set up a special force to protect the project, such deployment itself is indicative of this problem. In other words, road construction itself is the target of terrorist attacks in Pakistan. We can explain this by taking railways as an example (Table 9.3).

Table 9.3 shows that terrorist attacks on Pakistan's railways have been at a peak since 2010. The infrastructure construction of CPEC is forced to face terrorism directly. Not only that, people have reason to worry that due to the strengthening of China-Pakistan connectivity, it may further solidify the spatial correlation between the two countries on the issue of terrorism. By analyzing the global terrorism data from the University of



Maryland, we found that between the two neighboring countries as Afghanistan and Pakistan, it is the terrorist incidents in China and Pakistan have significant spatial correlation in time series.

Comparing Figs. 9.1 and 9.2, we find that although the number of terrorist attacks in China is far from that of Pakistan, the time series trends are very similar. Comparing with Fig. 9.3, it is not difficult to find that terrorist attacks in Afghanistan have been on the rise, while those in China

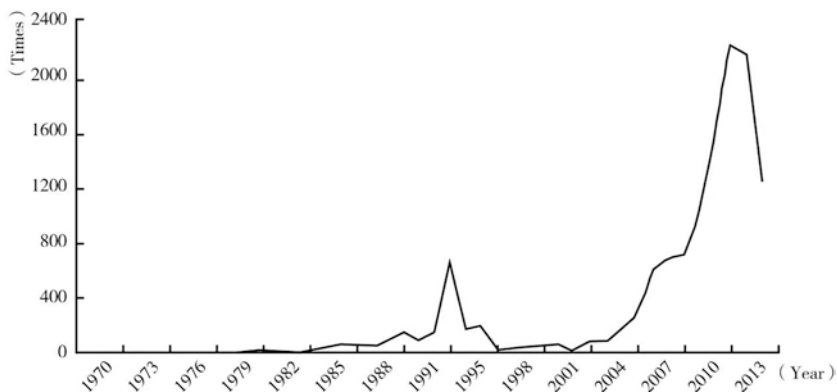


Fig. 9.1 Time chart of terrorist attacks in Pakistan

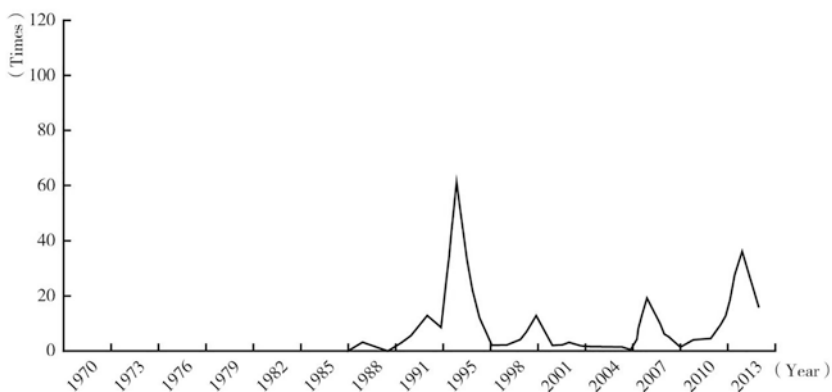


Fig. 9.2 Time chart of terrorism attacks in China

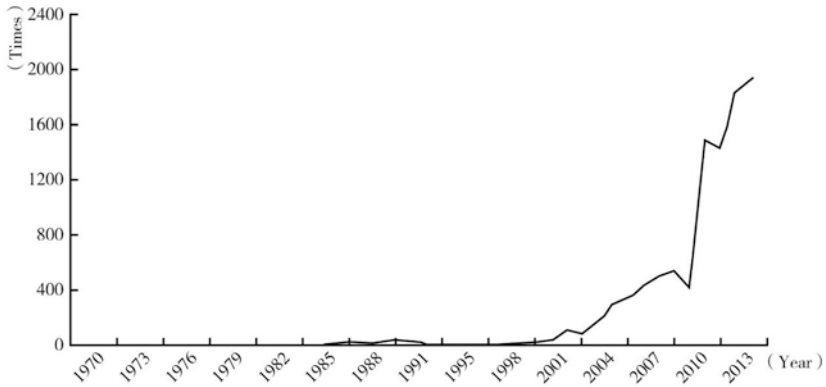


Fig. 9.3 Time chart of terrorist attacks in Afghanistan

and Pakistan show peaks and troughs. This kind of relevance in spatial reproduction may become increasingly prominent with the accelerated construction of CPEC, which is worthy of people’s worries.

## 9.5 CONCLUSION

The Belt and Road is essentially a kind of space production, in which infrastructure plays an important role, behind which is the logic chain of “terrorism→poverty→road building”. This logic is first and foremost reflected in the US\$45.04 billion infrastructure projects under CPEC—the flagship project of BRI. However, there is no direct causal link between terrorism and poverty. Building a road does not necessarily lead to wealth. Behind the infrastructure politics of CPEC lies, above all, a dogmatism based on economic determinism. In a sense, this dogmatism is the root of many problems in the process of implementing BRI. In this regard, the dialogue between Weber and Marx on the spiritual origin of capitalism is undoubtedly of great enlightenment significance.

More than that, this infrastructure logic also contains two major strategic risks: First of all, the security forces formed for CPEC shows that all related projects have become a target of terrorist threats. Secondly, the occurrence of terrorist incidents in China and Pakistan are similar in the trend of time series. This makes people worry that the strengthening of connectivity may also further solidify the spatial correlation of terrorism between China and Pakistan.



# Social Infrastructure Development Aid for Xinjiang and Lessons for CPEC: A Case Study of Shanghai-Kashgar Paired Assistance Program

*Bin Wang*

## 10.1 HOW CAN SOCIAL INFRASTRUCTURE DEVELOPMENT AID FOR XINJIANG GUIDE THE CONSTRUCTION OF CPEC?

China-Pakistan Economic Corridor (CPEC) is not only a pioneering project of the Belt and Road Initiative (BRI) but also window in Westward Opening of China in the New Period. At present, there are only a handful of studies on CPEC in the domestic academic community,<sup>1</sup> and most of

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<sup>1</sup>On July 12, 2016, the author searched academic papers under the title of “China-Pakistan Economic Corridor” in China Academic Journal Network Publishing Database, and found a total of 75 articles containing the search phrase, with the highest download rate of 858 times per article and the highest citation rate of 11 times per article.

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them focus on the macroscopic national strategic layout,<sup>2</sup> international trade,<sup>3</sup> and potential risks.<sup>4</sup> Although they can play a guiding role in CPEC's implementation, two prominent problems remain outstanding. On the one hand, most of the existing studies pay little attention to domestic reality and experiences. On the other hand, scholars seldom look at the future development and planning of CPEC from the dimension of social construction.

In fact, these two problems also explain the reason why China's foreign aid often gets into trouble. Being unaware of global social governance and failing to apply domestic poverty-relief experiences to foreign countries, the aid model that solely relies on infrastructure construction is often questioned by the people of recipient countries.<sup>5</sup> Likewise, CPEC is partly an overseas infrastructure project initiated by China. How can it avoid lessons from the past is a core clue of this paper. Given this, we must keep in mind that the smooth implementation of CPEC must be based on the combination of domestic experiences with social construction. To put it simply, we need to reorganize domestic experience from the dimension of social governance, refine our aid model and then apply it to BRI practices.

CPEC is a large-scale project involving both China and Pakistan. This bilaterality means we should not focus exclusively on Pakistan. Inadequate attention to and analysis of domestic construction experiences may lead to errors in our overseas strategies. In this sense, Kashgar of Xinjiang, as the starting point of CPEC in China, determines to a large extent the success of this cross-border corridor. Moreover, Kashgar is located at the center of southern Xinjiang which is even more underdeveloped than northern Xinjiang, so its development largely depends on support from other provinces and cities. Therefore, the analysis of the aid-to-Xinjiang (typically Kashgar) effect not only helps us learn about Kashgar's socio-economic situation but also enables us to apply relevant experiences to CPEC, thus

<sup>2</sup>Chen Jidong, Zhang Jianquan, "The Positioning of the China-Pakistan Economic Corridor in the Belt and Road Construction", *Journal of Xinjiang Normal University (Edition of Philosophy and Social Sciences)*, 2016, Issue 4.

<sup>3</sup>Cheng Yunjie, "Study on Deepening Trade in the Construction of the China-Pakistan Economic Corridor", *Research on Development*, 2015, Issue 4.

<sup>4</sup>Hu Jian, *Research on the "Belt and Road" Strategic Conception and Practice*, Beijing: Current Affairs Press, 2016, pp. 136–38.

<sup>5</sup>Kong Yongle, "The Righteousness and Benefits of China and the West in Aid to Africa", *Twenty-First Century*, February 2011.

helping the Chinese government, enterprises, and social organizations to go global more smoothly.

It is worth mentioning that the aid to Xinjiang is not only economic support, but also social infrastructure construction in the modern sense, which coincides with the purpose of BRI to strengthen people-to-people ties in the countries along the way. As far as CPEC is concerned, it was born for the exchange of economic factors, but along with the removal of institutional barriers, the exchanges in social fields such as environment, humanities, and non-traditional security will become increasingly important.<sup>6</sup>

General Secretary Xi Jinping pointed out the importance of social construction for BRI as early as 2014. In his view, when thinking about and planning for connectivity projects, we need to put people first, listen to the opinions of people at the grassroots level and increase their income, and intensify effort to solve social infrastructure issues such as electricity, drinking water, healthcare, schooling, employment, and Internet access. Gao Bai further enriched this point of view, stating that BRI, which is backed by high-speed rail, is not only about technology and politics, but also about systematic social engineering; we can never deny this point, or else China will suffer major setbacks in global competition, with its national interests seriously undermined.<sup>7</sup> Therefore, building CPEC from the perspectives of social undertakings and benefits, as well as people's lives, will ensure a more sustainable prospect for BRI.

In short, our discussion on CPEC should involve its economic and political gains, but more importantly, we also need to pay attention to the situation of Kashgar, especially the assistance to it offered by other provinces and cities, since the corridor is a crucial part of BRI. We must sum up the aid-to-Xinjiang experiences, especially those for improving people's lives, only on this basis can we promote people-to-people ties through social construction and achieve common modernization with countries along BRI. Based on this, the analysis in this paper is made up of four dimensions: (1) In the context of the implementation of BRI and CPEC, this paper outlines Kashgar's social and economic development during the Twelfth Five-Year-Plan period (2011–2015). (2) It briefly introduces the

<sup>6</sup> Lu Guangsheng, Deng Han, "Theoretical Source of CPEC and Its Enlightenment to the Construction of BCIM Economic Corridor", *South Asian Studies*, 2015, Issue 2.

<sup>7</sup> Gao Bai, "Why the collective innovation of China's high-speed rail can be successful", *Frontiers*, 2016, Issue 10.

current situation and risks of paired assistance for Kashgar from other provinces and cities. (3) It analyzes the content, characteristics, and effects of the social infrastructure development using the Shanghai-Xinjiang paired assistance program as an example. (4) It sums up the experiences in social infrastructure development aid to Xinjiang that may benefit CPEC.

## 10.2 SOCIAL AND ECONOMIC CONDITIONS IN KASHGAR

### 10.2.1 *Introduction to Kashgar*

Covering a total area of 162,000 square kilometers, Kashgar Prefecture is made up of one economic development zone (Kashgar EDZ), one county-level city (Kashgar), eleven counties (Shufu, Shule, Yingjisha, Yuepuhu, Jiashi, Shache, Zepu, Yecheng, Maigati, Bachu, and Tashkurgan Tajik). By the end of 2015, the total population of Kashgar has reached nearly 4.5 million. Kashgar boasts special resource advantages; it is China's top producer of high-quality cotton and a major supplier of dry and fresh fruit. It is also rich in oil, gas, and mineral resources which have great development potential. In 2010, the Opinions of the CPC Central Committee and the State Council on Promoting Xinjiang's Leapfrog Development and Long-term Governance and the Opinions of the State Council on Supporting the Construction of Kashgar and Horgos EDZs were released successively, marking that Kashgar would be ushered in a new era of development.

The geographical location of Kashgar is also of strategic importance. Kashgar borders or neighbors eight countries, including Kyrgyzstan, Tajikistan, Afghanistan, Pakistan, and India. With five ports leading to eight countries and a land route linking Europe and Asia, Kashgar boasts unique geographical advantages. It is the first stop of the Silk Road from Central Asia and South Asia to China, and the most convenient international passage from China to Central Asia, South Asia, West Asia, and Europe. Being connected to Pakistan by mountains and rivers, Kashgar is a natural gateway for Sino-Pak overland trade, enjoying the most favorable conditions and foundation for the development of trade and economic and technological cooperation. In the Vision and Actions on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road, Kashgar is listed as a node on the China-Central Asia-West Asia Economic Corridor, and Kashgar EDZ is identified as a major industrial park. With the advancement of BRI and CPEC, the advantages of Kashgar as a node

city and a strategic gallery bridge will become more and more prominent. According to China's strategic deployment, Kashgar should build itself into a joint point, growth pole, and a center on the Silk Road Economic Belt. The construction pattern of "one corridor, one artery traffic line, three bases, and five centers"<sup>8</sup> in Kashgar is taking shape at a fast pace.

### 10.2.2 *Social and Economic Situation in Kashgar*

During the Twelfth Five-Year-Plan period, the social economy of Kashgar has been rapidly improved, with local GDP growing by leaps and bounds, industrial structure optimized continuously, foreign trade developing steadily, and people's income increasing year by year.

- (1) GDP keeps growing and economic development remains on the fast track

Since entering the new century, the economy of Kashgar has achieved steady and rapid growth. In 2000, the GDP of Kashgar was only 7.4 billion yuan. After 2002, the GDP of Kashgar registered an average annual growth rate (AAGR) of over 12 percent. Even after the economic slowdown in most parts of China after 2010, Kashgar still maintained a double-digit AAGR and a good economic development momentum. In 2015, Kashgar achieved a GDP of 78 billion yuan, an increase of 108 percent from the 37.5 billion yuan in 2010. Generally speaking, the GDP of Kashgar at the end of the Twelfth Five-Year Plan period has doubled compared with the end of the Eleventh Five-Year-Plan period, achieving leap-frog growth of the local economy at a fast speed (Fig. 10.1).

- (2) Industrial structure is being optimized continuously with the embryonic form of a modern industry beginning to take shape

With the annual increase in GDP, the industrial structure of Kashgar has been optimized and upgraded. Since the Twelfth Five-Year Plan

<sup>8</sup>“One bridge” refers to the CPEC's covered bridge, “one line” refers to the “China-Central Asia-West Asia overland access to energy”, and “three bases” refer to the export product manufacturing and processing base, the imported energy resource reserve and processing base, and the commodity distribution trade base, and the “five centers” refer to the economic cooperation center, trade logistics center, financial center, cultural tourism center, and medical service center.

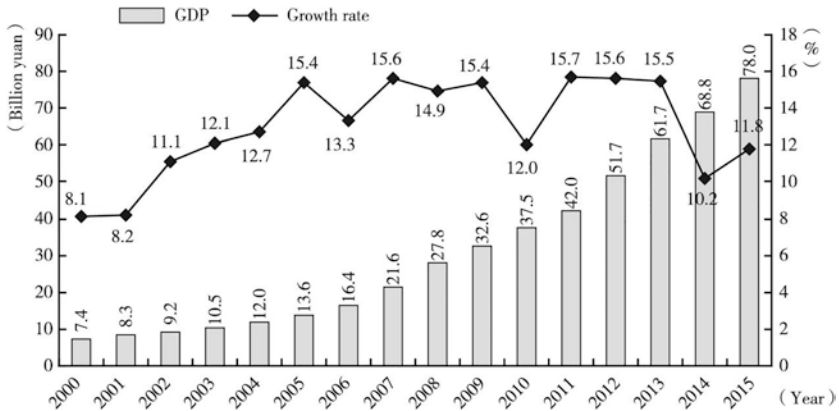


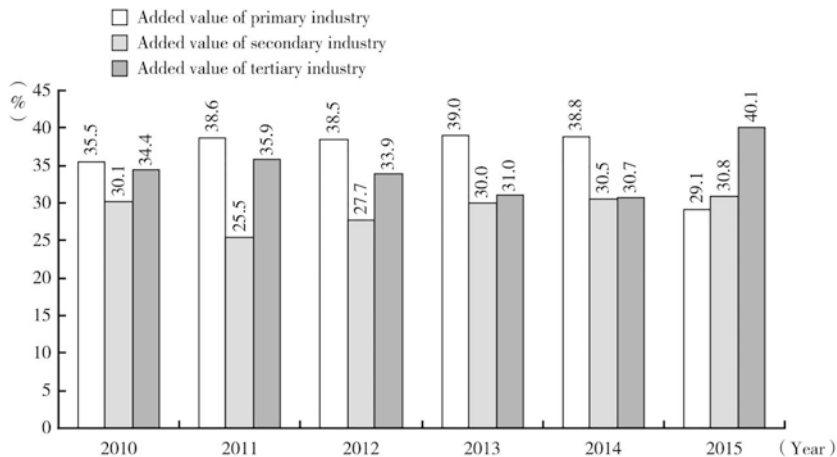
Fig. 10.1 GDP and growth rate of Kashgar from 2000 to 2015

period, the ratio of the three industries in Kashgar has been adjusted from 34.4 : 30.1 : 35.5 in 2010 to 29.1 : 30.8 : 40.1 in 2015, showing a shrinking share of the primary industry, little change in the share of the secondary industry, and an expanding tertiary industry. Although this industrial structure still has a certain gap from the eastern cities of China, it conforms to the law of modern industrial development (Fig. 10.2).

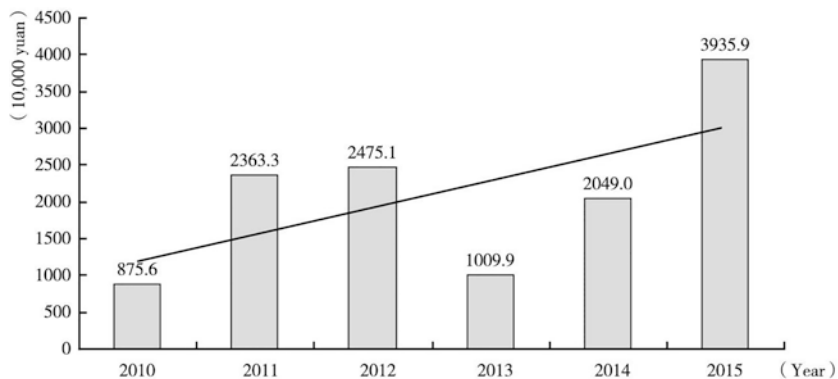
### (3) Foreign trade grows against the trend, and Sino-Pakistan economic and trade cooperation gets resumed and improved

In 2009, the international economic crisis caused Kashgar's border trade to decline, the total import and export trade of the whole year was US\$1.014 billion, down 39 percent from 2008. In 2010, due to the turmoil in Kyrgyzstan, the economic downturn in Tajikistan and the interruption of road traffic between China and Pakistan, the import and export of border trade in Kashgar continued to decline, receiving a total value of US\$915 million, down 9 percent compared with 2009. However, with the transfer of favorable domestic policies to Kashgar and the proposal of BRI, the total import and export trade of Kashgar began to pick up after 2011 and reached US\$1.154 billion in 2015. The trade between Kashgar and Pakistan also recovered quickly after a heavy hit in 2010, with trade volume between the two sides reaching US\$39.359 million in 2015, up





**Fig. 10.2** Changes the ratio of three industries in Kashgar from 2010 to 2015



**Fig. 10.3** Total trade volume between Kashgar and Pakistan from 2010 to 2015

92 percent from the previous year. The specific value of the total trade between Kashgar and Pakistan from 2010 to 2015 is shown in the Fig. 10.3 below.

- (4) The per capita disposable income of urban and rural residents increases year by year, and the people's living standards continues to improve

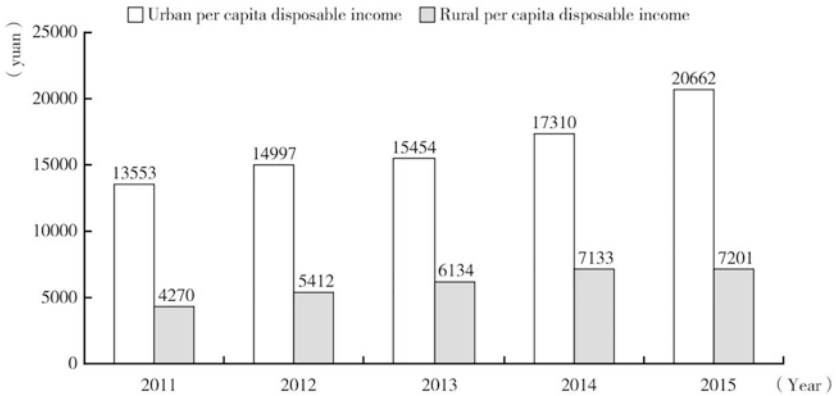


Fig. 10.4 Per capita disposable income in Kashgar from 2011 to 2015

During the Twelfth Five-Year-Plan period, the per capita disposable income of urban and rural residents in Kashgar has increased year by year. In 2011, the per capita disposable income of urban and rural residents were 13,553 yuan and 4270 yuan, and in 2015, these two figures rose to 20,662 yuan and 7201 yuan, respectively. The AAGR of per capita disposable income of urban residents was 10.4 percent, while that of per capita disposable income of rural residents was 13.7 percent (Fig. 10.4).

### 10.3 GENERAL SITUATION AND HIDDEN WORRIES OF PAIRED ASSISTANCE FOR KASHGAR FROM PROVINCES AND CITIES

Mr. Fei Xiaotong once pointed out that with the acceleration of industrialization in China, the proportion of agriculture in the national economy will be further reduced, and the development gap between border ethnic minority areas and the inland and coastal areas will continue to increase. To achieve prosperity and equality, all ethnic groups must rely on unity and mutual assistance between each other. Therefore, we must act in accordance with the principle of “let first comers help late comers”, that is, encourage the ethnic groups in developed regions to help their counterparts in underdeveloped regions in economy, culture, and other aspects. The state not only grants preferential policies to ethnic minority areas but

also provides them with practical help.<sup>9</sup> This argument of Mr. Fei provides a solid theoretical basis for China's policy of supporting border areas.

### 10.3.1 *Evolution of Aid-to-Xinjiang Policy Since the Founding of the People's Republic of China*

Supporting the development and construction of Xinjiang is undoubtedly an important part of China's support for border areas. It demonstrates the effectiveness and advantages of China's policy of unity and mutual assistance among ethnic groups. Historically, the thought of developing Xinjiang began in the middle of the Qing Dynasty and gradually took shape in the Republic of China.<sup>10</sup> After the founding of New China, the Central Government attached great importance to the work related to Xinjiang and put it in a special strategic position. In fact, the horizontal paired Xinjiang assistance program is more flexible and targeted than vertical transfers of state fiscal funds and policy support. Therefore, the policy of paired assistance for Xinjiang has become increasingly popular, and its formation is also a long-term dynamic process.

Some argue that paired assistance is a macro-control and regional mutual assistance model with Chinese characteristics. It started in the 1950s, was initially implemented in the 1960s, and finalized in 1979 by the CPC Central Committee Document No. 52 as a national policy.<sup>11</sup> Since the 1990s, to solve the problem of uneven regional economic development in China, all other provinces and cities started offering assistance to Xinjiang, which has become a supporting and regular policy for the development of the western region.

From the mid-1990s to the present, the focus of China's aid to Xinjiang has also undergone phased changes: The first stage is dominated by "cadres aid" and "intelligence aid". The second stage is characterized by "project aid" and "economic aid". In the third stage, a multi-level, wide-ranging, and all-round assistance model of "horizontal to the edge and vertical to the bottom" was initially formed, that is, economic, talents,

<sup>9</sup> Fei Xiaotong (ed.), *The Integrated Pattern of Pluralism of Chinese Nation*, Central University for Nationalities Press, 1999, pp. 34–35.

<sup>10</sup> Zhang Li, "Modern Chinese People's View of Development of Northwest", *Bulletin of the Institute of Modern History, Academia Sinica*, 1999, Issue 18.

<sup>11</sup> Li Na, "Survey on Current Situation of Paired Assistance for Kashgar and Research on Policy Measures", *Social Sciences in Xinjiang*, 2013, Issue 4.

science and technology, education, medical, and cultural assistance are paralleled, the paired assistance for Xinjiang is increasingly project-oriented and distinct.<sup>12</sup> In April 2005, the “Notice of the General Office of the CPC Central Committee and the General Office of the State Council on Establishing the Paired Assistance among Provinces, Municipalities, Enterprises, and Southern Xinjiang’s Four Prefectures and Three Divisions of Xinjiang Production and Construction Corps” was issued, marking other provinces and cities’ paired assistance for Xinjiang had taken shape. With the promulgation of the “Opinions on Further Promoting Xinjiang’ Personnel Work” and “Several Opinions of the State Council on Further Promoting Xinjiang’s Economic and Social Development”, the paired assistance work in Xinjiang has continued to deepen. At the end of March 2010, China’s first work conference on paired assistance for Xinjiang was held in Beijing. Since then, the pattern of paired assistance for Xinjiang in nineteen provinces and cities was fixed.<sup>13</sup>

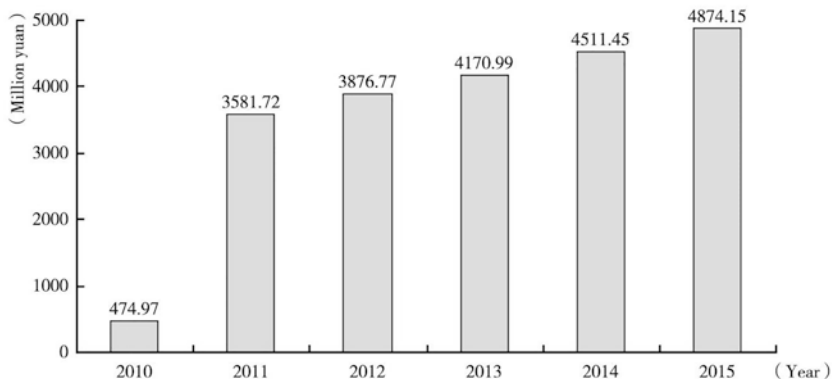
### 10.3.2 Paired Assistance for Kashgar During the Twelfth Five-year-Plan Period

The focus and difficult point of paired assistance for Xinjiang are in southern Xinjiang, while Kashgar, as the hinterland of southern Xinjiang, has always been the key to aid to Xinjiang. Since 1997, Shandong, Tianjin, and other provinces and cities have successively assisted Kashgar. In 2010, after some adjustment, Shanghai, Shenzhen, Guangdong, and Shandong were paired with Kashgar to assist. During the Twelfth Five-Year Plan period, the amount of money provided through paired assistance programs involving these four provinces and cities increased year by year (see Fig. 10.5). The paid-in funds in 2011 amounted to 3581.72 million yuan, and this figure rose to 4874.15 million yuan in 2015, an increase of 36 percent, and more than nine times the amount in 2010.

In the five years, the four provinces and cities planned to provide Kashgar with a total of 20.95 billion yuan in aid, and the amount already disbursed reached 22 billion yuan (including 540 million yuan for the

<sup>12</sup>Chen Hong, “On the Aid-to-Xinjiang Policy Since the Founding of New China”, *Journal of Xinjiang Normal University (Edition of Philosophy and Social Sciences)*, 2012, Issue 6.

<sup>13</sup>Yang Fuqiang, “Retrospect and Reflection on the Aid-to-Xinjiang Policy”, *Journal of Northwest Minzu University (Philosophy and Social Science)*, 2011, Issue 5.



**Fig. 10.5** Total paid-in funds for paired assistance for Xinjiang from four provinces and cities from 2010 to 2015

pilot year and 400 million yuan for the construction of Kashgar University sponsored by Shenzhen's government). A total of 1495 aid-to-Xinjiang projects have been implemented (Table 10.1).<sup>14</sup>

### 10.3.3 *Potential Problems and Manifestations*

In recent years, with the establishment of the Kashgar Special Economic Zone, a large amount of investment has begun to flow into Kashgar, making the economic and social development of this area greatly improved. Especially after BRI was put forward and CPEC projects were commenced, Kashgar has stepped onto the fast lane of development in the new era in terms of industrialization, urbanization, and informatization. However, due to the complex geographical, religious, and ethnic issues in Kashgar, the social changes triggered by rapid economic growth often contain strong social contradictions. Although the “paired assistance for Kashgar” of the four provinces and cities has resolved some local problems, it has also caused various social risks. For example, in recent years, other provinces and cities have increased their support to Kashgar to varying degrees, and the increasing aid funds in Kashgar have begun to

<sup>14</sup>Kashgar Development and Reform Commission, “Aid-to-Xinjiang Achievements in Kashgar during the Twelfth Five-Year-Plan Period, Portal of Kashgar Government”, <http://www.kashi.gov.cn/Item/31721.aspx>.

**Table 10.1** Paired assistance for Xinjiang involving four provinces (municipalities) from 2011 to 2015

<i>Donor provinces (municipalities)</i>	<i>Recipient area</i>	<i>Total amount of aid fund (billion yuan)</i>	<i>Total number of aid project</i>
Shanghai	Bachu, Shache, Zepu, Yecheng	9.234	65
Shenzhen	Kashgar downtown, Taxkorgan	3.85	12.6
Guangdong	Shufu, Jiashi, Xinjiang Production & Construction Corps Third Agricultural Division (Tumushuk)	6.327	12.5
Shandong	Shule, Yingshaji, Maigaiti, Yuepuhu	4.725	45.3

Source: Portal of Kashgar government (<http://www.kashi.gov.cn/>)

Note: As the statistics of the four provinces (municipalities) on relevant projects may be earlier than the statistics of the Kashgar Prefectural Party Committee, there is a certain discrepancy between the total amount of aid funds and projects in Kashgar and the provincial/municipal statistics. For specific data, please refer to the reports on the aid-to-Xinjiang work during the Twelfth Five-Year Plan published on the Kashgar government's official website

concentrate on urbanization-related fields. As a result, the speed and scale of Kashgar's new town construction have entered into an unprecedented period of growth. However, due to the weak industrial foundation and limited urban population of Kashgar, after the new town project is completed, it will often lead to two problems: One is the low-level repetition of industrial development; the other is a large number of high-rise buildings with a low occupancy rate.

On the one hand, since the new round of paired assistance for Xinjiang is in the form of "pairing", there is a lack of information exchange between donors, and sometimes they are competing against each other. Consequently, some major projects are more prone to repeated construction, and the crisis of industrial homogenization and falsely high GDP appears accordingly. This also causes the waste of resources, ecological damage, and unsustainable industrial foundation. As of 2013, Xinjiang had seen its cement production capacity reach 63 million tons and steel production capacity reach 24 million tons, far exceeding local market demand, hence the crisis of overcapacity gradually emerged. Moreover, steel, cement, and other similar projects themselves are energy-intensive and highly polluting industries, they are likely to increase the damage to the local ecological environment while overcapacity causes a waste of resources. In addition, China is in the "new normal" of the economy.

Industrial homogeneity and overcapacity means that industry will be quickly eliminated by the market. However, because of Kashgar's weak economic and industrial foundation, large-scale capacity cutting is bound to affect the employment and income of the local population. If it is not handled properly, it will directly threaten the social stability and long-term stability of the ethnic minority areas. Therefore, low-level industrial construction lacking social planning will inevitably reduce the positive pulling effect that paired assistance brings to Xinjiang.

On the other hand, aid to Kashgar began to flow into the real estate industry, showing that the phenomenon of passive urbanization was beginning to appear. During the Twelfth Five-Year-Plan period, Kashgar's economic development has been rapidly improved. At the end of 2015, Kashgar had a total population of 4,499,200, making it the most populous area in Xinjiang, accounting for 19 percent of Xinjiang's total population. However, Kashgar has a large area, a large proportion of agriculture, a scattered population, a small permanent population in the urban area, and a low level of urbanization. According to statistics, the urbanization rate of Kashgar's permanent population in 2011 was 22.3 percent, which was 21.2 percentage points lower than Xinjiang's average and 29 percentage points lower than the national level. In 2015, the urbanization rate of Kashgar's permanent population was only 24.23 percent, which was nearly 32 percentage points lower than the national level in the same period. From 2011 to 2015, the average annual growth rate of Kashgar's urbanization rate was only 0.6 percent, the urbanization rate grew slowly, and the urbanization rate even declined against the trend in some years (see Fig. 10.6).

It can be seen that the current situation of urbanization in Kashgar is as follows: limited urban population, low level of urbanization, and small scale of city construction. In order to improve the level of urbanization in Kashgar, aid funds began to flood into the city's infrastructure (especially real estate). A series of new downtown projects have started one after another, industrial parks, office buildings, commercial housing communities and other areas are being built intensively. Urban construction investment has been continuously strengthened, and the scale of Kashgar has continued to expand. Among them, commercial housing and affordable housing projects have the greatest impact on local residents. However, the supporting facilities of new buildings are poor, since water, electricity, gas, traffic networks, and educational facilities have not kept pace with the

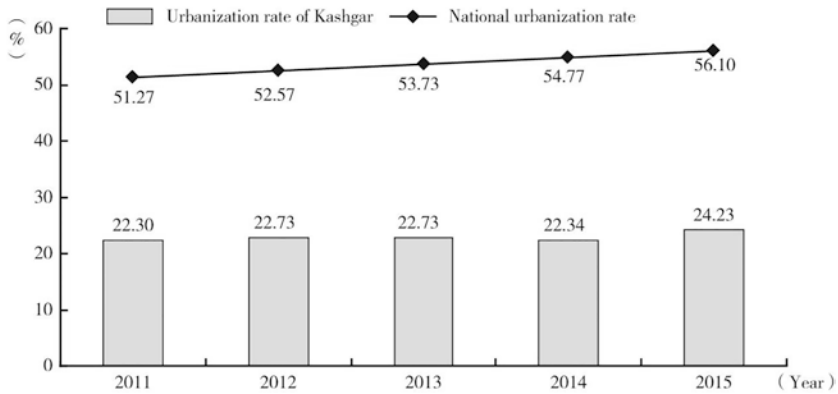


Fig. 10.6 Urbanization rates in Kashgar and in China from 2011 to 2015

construction of new houses. This has led to the reluctance of local people to move into new homes and a low occupancy rate of new communities. The grassroots society has also encountered an increasingly serious dilemma of “passive urbanization”.

During the investigation in Kashgar, the author interviewed some cadres of Han nationality. While affirming the achievements of Kashgar’s new town construction, they also expressed their views on the influx of “aid to Kashgar” projects into the real estate industry. Respondents generally believed that building new houses was originally an important measure to improve people’s lives, but some specific social and cultural factors must also be considered. The ethnic relations in Kashgar determine that it could not simply follow the old path of urbanization in inland cities of China. Guiding local people to move into new communities is a slow process requiring meticulous effort. Only by starting from other flexible aspects can we achieve the goal of optimizing the aid effect to Kashgar.

Therefore, to implement the spirit of the second Work Conference on Xinjiang, the aid to Kashgar must be carried out around the general goal of “social stability and long-term stability”, and the aid funds and projects in Kashgar should be further tilted to the grassroots, to the fields concerning people’s lives, to impoverished areas and people. The importance of social infrastructure development assistance for Xinjiang is thus highlighted.



## 10.4 CONTENT, CHARACTERISTICS, AND EFFECTIVENESS OF SOCIAL INFRASTRUCTURE DEVELOPMENT ASSISTANCE FOR XINJIANG: A CASE STUDY OF SHANGHAI-XINJIANG PAIRED ASSISTANCE PROGRAM

Paying attention to people's lives is an excellent legacy of China's traditional social thinking, and it is also an institutional feature of socialism with Chinese characteristics. Since the Sixteenth National Congress of the Communist Party of China in 2002, attaching importance to the development of social programs and improvement of people's wellbeing represents a major enhancement of the CPC's governance philosophy, which has changed the incoordination between economic growth and social development in China.<sup>15</sup> "People's lives and wellbeing" has begun to occupy an increasingly important position in the formulation of social policies in China. In terms of the aid-to-Xinjiang work, according to the deployment of the Central Government in 2010, the new round of assistance to Xinjiang will focus on safeguarding and improving people's lives, to help people of all ethnic groups solve basic everyday problems such as education, healthcare, employment, and housing, and promote the leap-frog development and long-term stability of Xinjiang through vigorous development of local advantageous industries. Since there are a variety of measures to support Kashgar through the development of social infrastructure in different regions, for the sake of explicit explanation and expression, this section will take Shanghai's paired assistance for Kashgar as an example to talk about the content, characteristics, and effectiveness of social infrastructure development assistance for Xinjiang.

### 10.4.1 *Main Content of Social Infrastructure Development Assistance for Xinjiang*

According to the instructions of the CPC Central Committee on the new round of assistance to Xinjiang, more than 70 percent of the aid funds to Xinjiang should be used for undertakings and projects that benefit people's livelihood. In this context, Shanghai comes up with its aid-to-Xinjiang program, that is, putting people's livelihood in the first place, and in the meantime doing a good job in industrial development, planning,

<sup>15</sup>Wen Jiabao, "Several Issues Regarding the Development of Social Undertakings and Improving People's Lives", *Seeking Truth*, 2010, Issue 7.

cultivation of talents, and supporting medical care and public health, affordable housing, and enriching-the-people projects, and infrastructure construction.

### 1. Increase education investment and improve education quality

For the economically underdeveloped ethnic minority concentrated area in the borderland, raising the average educational level of residents is the essence of strengthening national unity, and also a necessary condition for achieving leapfrog development and long-term social stability. Therefore, the first part of infrastructure assistance to Xinjiang is to strengthen education investment and improve education quality. During the Twelfth Five-Year-Plan period, Shanghai provided Kashgar with an education fund of 1249.10 million yuan and implemented eight-five education projects in Xinjiang. In 2014 alone, Shanghai's paired assistance for the four counties in Kashgar reached about 300 million yuan, and more than twenty teaching facilities and equipment projects were launched. The funds injected into these education projects are spent in the following areas: (1) The supporting facilities of educational infrastructure, which includes the construction or expansion of educational parks, the purchase of teaching equipment, and the construction of quality education bases. (2) The building of a teacher team. The Command Office of Shanghai's paired assistance for Xinjiang (hereinafter referred to as the Command Office) has increased the training of teachers for bilingual (Uyghur and Chinese) education.

From 2011 to 2015, more than 2000 teachers received intensive bilingual training and teaching practice valued at 11,500 yuan per person annually. (3) Targeted enrollment and training. More than ten high schools and more than twenty full-time four-year colleges and universities in Shanghai would enroll 2000 and 200 Kashgar students every year, respectively. In addition, the Command Office arranged for 1243 Xinjiang university students to participate in training for one and a half to two years in Shanghai. (4) To establish the Shanghai-Kashgar Vocational Education Alliance which will include more than seventy vocational colleges, enterprises, industry associations, and management departments in Shanghai and Xinjiang as member units, so as to open up channels for school-enterprise cooperation, talent interconnection, and resource sharing.

## 2. Develop medical services and improve people's health

Considering the suboptimal allocation of healthcare resources and slow development of public health in Kashgar, the improvement of the level of healthcare has become an important component of social infrastructure development aid to Xinjiang. From 2010 to 2014, nineteen provinces (municipalities) that were part of the paired Xinjiang assistance program executed 299 special healthcare assistance projects in Xinjiang, with actual expenditure of 3.5 billion yuan, to support Xinjiang's health and medical infrastructure construction, purchase of medical equipment, training of health and family planning personnel, and informatization of healthcare. During the Twelfth Five-Year Plan period, Shanghai arranged a total of 778.33 million yuan in health aid to Kashgar and implemented seventy-two health aid projects in Xinjiang, outperforming the assistance of other provinces and (municipalities) during the same period. Shanghai's health assistance to Xinjiang is mainly carried out from the following aspects: (1) Improve the infrastructure construction of healthcare institutions, and build the outpatient medical building of the Shache People's Hospital, the Yecheng County's Children's Center, and the Maternal and Child Health and Family Planning Center, the internal medicine building of the Zepu County People's Hospital, the inpatient building of the Bachu County People's Hospital, and the other key infrastructure projects. (2) Purchase medical equipment that is in short supply. Shanghai's Command Office completed the standardization of 1200 clinics, furnished township healthcare centers with basic diagnostic and treatment equipment, and allocated special funds for urgently needed equipment for achieving "three reductions and one increase" (reducing the incidence of infectious diseases, reducing maternal mortality rate, reduce infant and child mortality rate, and increasing life expectancy). (3) Build a health information platform to help the recipient areas to build an electronic health record and electronic medical record system for residents covering the whole territory, to realize the interconnection of residents' health management and medical information. (4) Create a medical technology exchange mechanism between Shanghai and Kashgar. Pudong, Minhang, Baoshan, and Jing'an districts in Shanghai will provide one-to-one technical assistance to Sheche, Zepu, Yecheng, and Bachu counties in Kashgar. On this basis, a new southern Xinjiang medical consortium is established, and remote consultation, two-way referral, personnel training, teaching cooperation, and other projects have been successfully carried out.

### 3. Improve supporting facilities and living conditions

During the Twelfth Five-Year Plan period, the four provinces (municipalities) that provide aid and assist to Kashgar have allocated a total of 4.56 billion yuan to Xinjiang, supporting the construction of 392,000 units of affordable housing, 6420 units of settled for grazing houses and supportive facilities. Shanghai's Infrastructure assistance Xinjiang also regards "settlement for enriching the people" and "settlement for developing animal husbandry" as the primary task of improving the living quality of Xinjiang people. Since 2010, Shanghai has invested a total of nearly two billion yuan into Xinjiang. By the end of 2015, 175,000 houses for "enriching the people" and for "developing animal husbandry" had been built, benefiting about 900,000 farmers and herdsmen. Shanghai's aid has benefited 40 percent of the twelve counties and cities in Kashgar, involving nearly sixty towns and more than 800 villages. It is worth mentioning that improving living conditions is not simply building houses and communities, but providing residents with sustainable livelihoods in an all-around way so that they can enjoy a better life.

On the one hand, Shanghai's Command Office has increased investment in infrastructure and improved housing construction. A single new house cannot truly benefit Kashgar residents, it is a complete set of supporting facilities that can make their lives more convenient. In 2014 alone, Shanghai's funding for infrastructure construction in the four counties reached 145.87 million yuan, accounting for 75.5 percent of similar funds in the region that year. Supporting funds are spent for solving the problems of water and electricity, roads, living, and entertainment facilities, so as to closely integrate the construction of new houses and the construction of communities. On the other hand, Shanghai's Command Office also merged "settling down" and "working in peace and contentment". Zepu and Yecheng counties have practiced the concept of combining the "enriching the people and settling down" concept with characteristic industries. Through the synchronous linkage of residential houses with Kashgar characteristics, courtyard economy, and tourism, the new houses and new businesses are complementary and mutually promoted

### 4. Establish an exchange mechanism to enrich cultural life

Historically, cultural exchange has been a key measure to promote ethnic integration and strengthen national identification. Vigorously

promoting the interaction between the Han culture and the Uyghur culture is also an inherent requirement for realizing ethnic relations that is characterized by “unity in diversity”. In terms of cultural life, the focus of social infrastructure development assistance for Xinjiang is to promote the integration of ethnic cultures. Under the guidance of modern culture, traditional culture and way of life are subconsciously sublated, so as to improve the local cultural soft power, preserve the intangible cultural resources, and reshape the regional image.

During the Twelfth Five-Year-Plan period, Shanghai had arranged a total of 50 million yuan to support cultural construction in Kashgar. In addition to the construction of key infrastructure projects such as the Bachu County Radio and Television Tower and Yecheng County Television Station Studios, a series of cultural products to promote Kashgar were also being developed and spread to the outside. Cultural products such as TV dramas, micro-documentaries, animation films, musicals, dramas, series of books, and atlases appeared one by one, which played a vital role in shaping Kashgar culture, demonstrating its customs, and promoting its tourism industry.

In addition, a normal mechanism for cultural exchanges and assistance between Shanghai and Kashgar has also been formed. Large-scale cultural exchange activities such as “Kashgar, a Good Place”, “Shanghai-Kashgar Culture Week”, and “Shanghai-Kashgar Kids Holding Hands” were launched one after another. Shanghai’s Command Office also subsidized the translation of a variety shows broadcast by Shanghai Satellite TV, and hired a team of experts to assist Kashgar TV Station in creating programs such as “Kashgar, You’re the Best”, to guide the cultural life of local residents positively. More importantly, through the development of cultural products, the improvement of cultural positions, and publicity and popularization into villages and households, modern culture can hedge against extreme religious ideas to a certain extent, and then play the role of “stabilizing Xinjiang” and “prospering Xinjiang”.

##### 5. Fine-tune industrial structure and improve employment

Employment is fundamental to people’s livelihood, and promoting employment is also a fundamental link in the improvement of people’s livelihood. Due to the relatively backward transportation and logistics infrastructure and industrial supporting facilities and infrastructure in Kashgar, and the relatively limited importance the ethnic minority

population has historically attached to regular and stable employment, both qualified workers and jobs are in short supply. The infrastructure assistance to Xinjiang is, to a large extent, to help the people in Xinjiang develop production and improve their employability so that they can create a happy life on their own and help realize the great rejuvenation of the Chinese nation.

During the Twelfth Five-Year-Plan period, Shanghai made great efforts in both “industry” and “employment” to support Xinjiang. A total of 2308.64 million yuan was allocated for the implementation of 208 industrial assistance projects in Xinjiang. The four counties receiving assistance have built industrial parks covering a total area of 44.2 square kilometers and employing more than 20,000 people.

Shanghai’s social infrastructure development assistance to Xinjiang has three main characteristics in terms of “promoting employment by industry”: (1) Combine the export-oriented business attraction and the domestically-oriented enterprise cultivation. To avoid the hollowing out of newly-built industrial parks, Shanghai’s Command Office stepped up its efforts to attract investment. On the one hand, promote Shanghai’s Zhangjiang, Jinshan, Xinzhuang, and Baoshan industrial parks or development zones to participate in the construction of the industrial parks in Kashgar’s four counties. On the other hand, vigorously promotes well-known enterprises in fields such as clothing, machinery assembly, forest and fruit processing, livestock and poultry breeding, and professional tooling to settle in Kashgar, so as to cultivate local tourism and characteristic forest and fruit industries with great development value, thereby enhancing the “hematopoietic” function of local industries and improving the quality of employment in a way that adapts to the skills of residents. (2) Combine concentrated employment with decentralized employment. The construction of industrial parks is an important way to realize concentrated employment, while the development of vegetable greenhouses, livestock and poultry bases, manual embroidery, and other industries can flexibly encourage local people to find jobs locally and nearby in a decentralized way, which is also in line with the actual situation and living habits of ethnic minority communities. (3) Combine mass entrepreneurship with independent employment. Build people’s livelihood entrepreneurship parks and enterprise incubation bases in the four counties, implement the Shanghai-Kashgar entrepreneurship assistance project, organize Shanghai-based innovation and entrepreneurship incubation platforms (such as

Mass Makerspaces Alliance), professional institutions, and volunteer expert groups to provide targeted guidance and consultation for enterprises to be incubated.

#### *10.4.2 Prominent Features of Social Infrastructure Development Assistance for Xinjiang*

The social infrastructure development aid to Xinjiang is a systematic project. It is by no means talking about people's livelihood as it stands but takes the construction of social undertakings as the main component of the assistance work to enable Xinjiang people to share the benefits of development and the dividends of reform. In essence, the social infrastructure development aid to Xinjiang is a pursuit, an idea, and even a governance approach. It requires us to optimize, integrate and organically match financial aid, industrial aid, technological aid, intellectual aid, grass-roots governance, and organizational construction, so as to consolidate the foundation of social and economic development in the recipient areas and improve the overall living standard and happiness of Xinjiang people through "a combination of boxing". As for Shanghai's social infrastructure development aid to Kashgar, it has the following four features:

1. Social infrastructure development aid to Xinjiang stresses the cultivation of endogenous power, aiming to enhance the sustainable development capacity of recipient areas

Sustainable development is a global consensus reached by all countries in the process of governance. The general goal of China's sustainable development strategy is to achieve the overall coordination of economic, social, cultural, political, and ecological construction. China's social and economic development is increasingly focusing on sustainability. The current "five development concepts" are not only an expression of Chinese discourse on sustainable development but also a further enrichment and deepening of sustainable development. In fact, in the process of paired assistance for Xinjiang, the relationship between "blood transfusion" (external aid) and "hematopoiesis" (endogenous power) has always been the top priority of the central government and the donor provinces (municipalities). Enhancing Xinjiang's "blood-making" ability and developing its endogenous advantages and sustainable capacity constitute the

fundamental task of aid to Xinjiang. However, Xinjiang's sustainable development is also facing extremely severe challenges, especially for Kashgar, which is located in southern Xinjiang, the limited natural environment, weak industrial foundation, poor entrepreneurial support system, and insufficient employment opportunities are all the key factors affecting its independent development ability. From this perspective, the primary characteristic of social infrastructure development assistance for Xinjiang is to break through the above development bottlenecks in a long-term way on the basis of respecting objective laws. It is worth noting that the cultivation of internal drive requires the replacement of improving hardware with the improvement of functions as the focus. By cementing the foundation, strengthening the grassroots structure, improving social infrastructure, and promoting stability, more work should be done to help Xinjiang increase employment opportunities, improve people's living standards and consolidate industries, and avoid the radicalized development model of "draining the pond to get all the fish". On the premise of ensuring the social stability and long-term peace of the recipient areas, a local development platform should be built to tap the local development potentials.

2. "Aiding Xinjiang", "stabilizing Xinjiang" and "rejuvenating Xinjiang" will be organically combined

After the Sixteenth National Congress of the Communist Party of China, "stabilizing and rejuvenating Xinjiang, enriching the people and consolidating borders" has become an important strategic guide for China's Xinjiang work in the new century. Therefore, the ultimate goal of paired assistance for Xinjiang is to promote long-term stability and prosperity in Xinjiang. "Aiding Xinjiang" is inseparable from "stabilizing Xinjiang" and "rejuvenating Xinjiang". In particular, social infrastructure development assistance for Xinjiang plays a strong role in promoting "stabilizing Xinjiang" and "rejuvenating Xinjiang". On the one hand, such assistance focuses on education, housing, medical care, and other substantial benefits for the people. This has played a key role in winning support from most ethnic minorities and in stabilizing the grassroots society. The second Work Conference on Xinjiang pointed out that social stability and long-term stability are the general goals for the region, as well as the focus of Xinjiang's construction; we must unwaveringly promote better and faster development of Xinjiang. At the same time, we need to put



development into practice to improve people's lives, benefit local communities and enhance unity, so that people of all ethnic groups can feel the care and warmth of the Party and the government. The importance of social infrastructure development aid for Xinjiang in "stabilizing Xinjiang" has been affirmed by the Party and the government, and its importance is becoming increasingly clear. On the other hand, social infrastructure development aid to Xinjiang also must include the establishment of a mechanism for guaranteeing people's wellbeing in the long term that can continue to make meaningful and perceptible differences in people's everyday lives. For example, through the establishment of a stable labor force training system, entrepreneurship park, bilingual teaching curriculum a new health service consortium and other initiatives aimed at capacity building for the local population, "rejuvenating Xinjiang" has been able to achieve greater and greater results.

In the long run, the realization of "stabilizing Xinjiang" and "rejuvenating Xinjiang" through social infrastructure development assistance can organically combine stability and development, making the assistance work in Xinjiang more targeted and more beneficial.

### 3. Social infrastructure development assistance for Xinjiang promotes two-way progress in economic growth and social development

Since the Sixteenth National Congress of the Communist Party of China, coordinated and balanced economic and social development has become the main theme. The problem of "one leg is long and one leg is short" in China's economic and social development has been continuously adjusted and resolved. To vigorously promote public services and improve people's wellbeing has become a practical step in social development and social governance. The essence of social infrastructure development assistance for Xinjiang is to achieve the organic unity of long-term stability and leapfrog development in Xinjiang through the assistance from other provinces (municipalities). In other words, the essence of social infrastructure development assistance for Xinjiang is to promote the two-way progress of social and economic development in Xinjiang. On the one hand, some industries aimed at increasing household income have been quickly established, and most of the labor force can earn stable income after receiving vocational training, which has a positive function of improving the benefits of ordinary people. On the other hand, social infrastructure development assistance for Xinjiang is not limited to economic construction, since

its effect on social construction is even greater. The social infrastructure development aid for Xinjiang focuses on the culture, education, health, public prosecution and justice, grassroots organizations, and public services that are directly related to the people, and strives to establish a social security and social service system with complete structure and covering all residents so that the sick can be treated, the elderly can be cared for and the students can be educated. Of course, the social development function of social infrastructure development aid for Xinjiang is not simply limited to public services, it can effectively stabilize the construction of grassroots organizations and grassroots positions. By setting up various service centers, training social workers, and supporting volunteers to visit villages, we can improve the ability of social governance to maintain stability and the organizational foundation for long-term peace and stability while improving people's lives.

4. Social infrastructure development assistance for Xinjiang has achieved the purpose of creating an identity-based development through integration

China is a multi-ethnic country, and the identification of various ethnic groups with the Chinese nation is particularly important. As for Xinjiang, especially in southern Xinjiang, social infrastructure development assistance for Xinjiang is, to a large extent, to realize the overall identification of the local population with the country, government, and the Chinese nation. Identification has two aspects: One is absolute identity, and the other is some special property that exists continuously.<sup>16</sup> Therefore, identification implies not only similarity but also difference. According to Fei Xiaotong, all fifty-six ethnic groups in China must allow for dual ethnic identification, that is, identification with their own ethnic group and with the Chinese nation at the same time; the identification with their own ethnic group is subordinate, while their identification with the Chinese nation is a subliminal form thereof. These two types of national identification can coexist and promote each other.<sup>17</sup>

<sup>16</sup>Xie Wenjing, "Virtual Space, Real Identity: Exploring Cultural Identity of Chinese Diaspora in Virtual Community". *Telematics and Informatics*, vol.22, iss.4, 2005, p. 396.

<sup>17</sup>Fei Xiaotong (ed.), *The Integrated Pattern of Pluralism of Chinese Nation*, Central University for Nationalities Press, 1999, pp. 34–35.

Based on this, we believe that identity-based development is a development model that puts people first, respects cultural differences, and aims to enhance national unity. It is bound to be inseparable from people's happiness perception, internal demands, and cultural background. Social infrastructure development assistance for Xinjiang focuses on the work methods of "strengthening the grassroots" and "benefiting people's lives". On the basis of fully respecting the wishes of ethnic compatriots, we should carry out highly specific and targeted assistance work in accordance with local conditions, so as to form a development model that integrates into local communities, benefits local people, and adapts to social conditions and public opinions. Of course, in addition to ensuring that people of all ethnic groups could share the fruits of economic and social progress, it is also important to give play the leading role of modern culture and modern way of life on the basis of mutual exchanges, so as to enhance the practical results of development and the common space for dialogue.

#### *10.4.3 Effectiveness of Social Infrastructure Development Assistance for Xinjiang*

During the Twelfth Five-Year Plan period, social infrastructure development assistance provided by Shanghai achieved great results in Xinjiang. The paired assistance for the four counties of Kashgar in social undertakings has achieved remarkable results, significantly improving people's living standards. The per capita net income of farmers in most of the aided areas more than doubled the level at the end of the Eleventh Five-Year Plan period. The infrastructure and service functions at the county, township, and village levels, such as culture, education, public health, public security, procuratorate, and public services, are basically complete. Issues related to the vital interests of people in education, medical care, employment, and culture are effectively resolved. At the same time, the implementation of the projects for urban and rural affordable housing, urban and rural water supply, urban and rural subsistence allowances, road network construction, and poverty grants have significantly improved the living environment of local people in the four aid counties (see Table 10.2).

The effectiveness of social infrastructure development assistance for Xinjiang is not only reflected in data and statistics, but also in the evaluation and perception of the local population. When visiting several entrepreneurial streets and factory clusters in Kashgar with a team led by Professor Zuo Xuejin of Shanghai Academy of Social Sciences, the author

**Table 10.2** Key indicators reflecting Shanghai's paired assistance for Kashgar's four counties

<i>Key indicators</i>	<i>Shache</i>	<i>Bachu</i>	<i>Yecheng</i>	<i>Zepu</i>
Net income of rural residents in 2015 (yuan)	6020	7463	8192	8845
Increase in the net income of rural residents from the end of the Eleventh Five-Year Plan period (yuan)	2395	3792	4587	5174
Net income of urban residents in 2015 (yuan)	17189	18250	16800	17784
Increase in the net income of urban residents from the end of the Eleventh Five-Year Plan period (yuan)	8010	5439	3989	5731
Houses built under the "enriching the people" program during the Twelfth Five-Year Plan period (100,000 households)	7.25	3.57	4.62	1.96

Source: Thirteenth Five-Year Plan (2016–2020) for Shanghai's paired assistance for Kashgar (Four Counties) in Xinjiang

interviewed some Uyghur people. A female worker at a garment factory told us that after she was placed in her current job immediately upon completing her vocational training, and the steady income helped her family tremendously; not only the improvement of employment but also the convenience of surrounding medical, education, and transportation conditions have greatly improved her living standards and happiness. It can be seen that the social infrastructure development assistance for Xinjiang can effectively improve the quality of the lives of the local population, while at the same time helping them build the capacity to pursue a better life. This provides a solid foundation for the prosperity and stability of Kashgar.

## 10.5 LESSONS FOR THE CONSTRUCTION OF CPEC

In fact, paired assistance for Xinjiang is closely related to the construction of the Belt and Road. From a certain level, to do a good job in aiding Xinjiang is to get ready for BRI. The author believes that paired assistance for Xinjiang and the implementation of BRI have the following three similarities: First, both of them have the nature of interconnectivity. BRI is, first of all, a national strategy aimed at improving the connectivity of various regions. At the international level, BRI is to achieve smooth economic and trade exchanges between China and the Eurasian continent. At the domestic level, it is to connect the east and west in terms of infrastructure and institutional mechanisms. From this perspective, paired assistance for Xinjiang is also to promote the effective connection between the western

frontier and the inland and to serve the development of BRI in the long run. Second, the content of promoting resource docking is interconnected. BRI includes promoting the free and orderly flow of economic factors, efficient allocation of resources and deep integration of markets, and jointly building a regional economic cooperation architecture that is open, inclusive, balanced, and beneficial to all through friendly cooperation with countries along the Belt and Road.<sup>18</sup> The content of paired assistance for Xinjiang is similar. It is also concerned with promoting the economic and social construction of Xinjiang in order to achieve an effective connection with the rest of the country in terms of capital flow, talent flow, information flow, and technology flow. Third, achieve the same purpose of “common modernization”. The ultimate goal of BRI is to maintain a global free trade system and an open world economic structure and establish a community of interests, a community of destiny, and a community of responsibilities through consultation, joint construction, and shared modernization. Correspondingly, paired assistance for Xinjiang is also aimed at driving the modernization of Xinjiang through the support and assistance of China’s eastern and central provinces (municipalities), and at implementing reform dividend sharing and regional coordinated development.

Of course, the author does not deny that there are many peculiarities between paired assistance for Xinjiang and BRI that deserve our careful comparison. However, for BRI to truly go global, it needs the support of relevant experience and knowledge accumulation in China. The interconnection between the two is , therefore necessary to reflect and summarize at this stage. In particular, as the construction of CPEC is put on the agenda, the distance between Pakistan and Kashgar, both are affected by Islamic civilization, will be further shortened. Deeply digging into the model and experience of “social infrastructure development assistance for Xinjiang (Kashgar)” will undoubtedly play a key role in informing the construction of CPEC—the pilot project of BRI. This can also effectively reduce the risk of project construction and achieve a smooth and precise strategic progress. In the following section, I will summarize the lessons that can be learned from these programs that might be applied to the construction of CPEC.

<sup>18</sup>Ke Yinbin, “The Essence of the ‘Belt and Road’ is Common Modernization”, in the *“Belt and Road” Annual Report: From Vision to Action* edited by Zhao Lei, Beijing: The Commercial Press, 2016, p. 62.

### *10.5.1 Put People First and Pursue Modernization That Is Based on Joint Contribution, Shared Benefits, Fairness, and Justice*

The Third Plenary Session of the Sixteenth CPC Central Committee put forward the scientific development concept as “we should put people first, foster a comprehensive, coordinated and sustainable outlook on development, and promote all-round economic, social and human development”. Since then, “putting people first” has become an important standard for China to formulate international and domestic policies. In October 2015, at the Asian Political Parties Conference on the Silk Road, Chinese President Xi Jinping pointed out that the Belt and Road construction pursues the purpose of putting people first and benefiting the people, it will bring tangible benefits to the people of the countries along the way. From this perspective, social infrastructure development assistance for Xinjiang not only enriches the meaning of “putting people first” in the Belt and Road development process but also provides specific work and construction guidelines for it.

“Putting people first” is not empty talk. Social infrastructure development assistance for Xinjiang has profoundly demonstrated the positive function of the idea of putting people first in regional modernization. Therefore, only when the people-centered approach is implemented in all stages of CPEC construction can this project be truly welcomed and supported by the people along the way, and can it become a symbolic bond for the sustainable friendship between Chinese and Pakistanis. Based on the experience of social infrastructure development assistance for Xinjiang, we believe that the people-oriented construction concept of CPEC should be reflected in the following two aspects. One is to follow the principle of co-construction and sharing. Although China and Pakistan are steadfast strategic cooperative partners, the two countries still have great differences in political systems and mainstream culture. “Putting people first” is to respect the religious beliefs and living habits of local people to the utmost extent, build a better life by seeking common ground while shelving differences, and call on the people along the corridor to participate in its construction. The other is to follow the principle of fairness and justice. CPEC is a common communication channel between China and Pakistan. Equity and justice are important factors for the sustained development of the corridor. But the “fairness and justice” we are talking about here is not

simply limited to the economic, trade, and political fields, but we hope to achieve social justice along the corridor through its construction. To this end, CPEC must transcend “economy” and start from social undertakings such as education, medical care, and culture that are closely linked to people’s lives. While activating the market, it also actively provides people with opportunities and rights for comprehensive development.

### *10.5.2 Meet the Needs of the People and Gain Support and Recognition Through the Development of Social Infrastructure and Undertakings*

Although we have repeatedly emphasized the important role of improving people’s lives in promoting social stability and safeguarding ethnic unity, we must point out that not all projects to improve people’s lives can be accepted by the people at the grassroots level. In other words, the livelihood of the people does not necessarily give birth to “people’s will”, and the “intermediate variable” connecting the two is the specific needs of the people in the specific cultural environment. Only on the basis of meeting the urgent needs of the people along the route in production and life at this stage, CPEC can fulfill its ambitious goal of building a community.

In fact, whether it is the construction of the Belt and Road or CPEC, clarifying the needs is the first step in our work. Without the analysis of people’s needs of the countries along the route, it will be difficult for the Belt and Road to go global. It is also worth noting that demand should not only be viewed from a national perspective, and should not be simply framed in terms of the exchange and mutual promotion of resources, energy, markets, and technologies between the two countries. Rather, it should be viewed from a “bottom-up” social perspective to meet the specific needs of the two peoples.

From the experience of social infrastructure development assistance for Xinjiang, we can see that by meeting the material and spiritual needs of the people, social stability and long-term stability can be achieved relatively smoothly. This also has an extremely important role in promoting the leapfrog development of the regional economy. Therefore, the construction of CPEC must pay attention to people’s lives and take meeting people’s basic needs and development demands as a measure of the progress of BRI. Relevant data show that the per capita GDP of Pakistan in 2012

and 2013 was US\$1266.4 and US\$1282, respectively,<sup>19</sup> while the per capita GDP of Kashgar in 2012 and 2013 were 12,500 yuan and 14,660 yuan, respectively. Compared with the current situation in Kashgar, Pakistan's social and economic development is more backward, and the needs of local people are more inclined to basic healthcare, employment, and education. Therefore, the relevant services and experience of "social infrastructure development aid for Xinjiang (Kashgar)" can be applied to the construction process of CPEC. At the same time, we also need to pay special attention to the dynamic changes in the needs of local populations to meet development needs in a more targeted and targeted way.

### ***10.5.3 Promote "resident-city interaction" and Strengthen the Coordination Between the Construction of New Downtown and Talent Cultivation***

The implementation of BRI will inevitably strengthen the transformation and upgrading of cities along the route, and promote the rapid development of their export-oriented and open economy. In terms of CPEC, its construction will release the huge potential of Pakistan's cities along the corridor. The City is a complex of current social and economic development. The resource aggregation of large cities can effectively integrate logistics, information flow, capital flow, and talent flow.

According to data from 2010 to 2013, Pakistan is in the middle of the initial stage of industrialization, with agriculture accounting for about 24 percent of its GDP. The country's current economic structure is transforming from agriculture-based to service-based,<sup>20</sup> and the urbanization rate remains low. The development of CPEC will surely bring new opportunities to cities along the corridor, and new downtown construction and old downtown renewal projects will also take place. However, according to our experience in the process of paired assistance for Xinjiang, when a large amount of capital flows into the urban construction in less developed areas, especially the real estate industry, the risk of repeated construction and industrial hollowing out becomes difficult to avoid.

<sup>19</sup> Huang Huiqun (ed.), *Report on the Process of Industrialization of Countries Along the Belt and Road*, Beijing: Social Sciences Academic Press (China), 2015, p. 97.

<sup>20</sup> Huang Huiqun (ed.), *Report on the Process of Industrialization of Countries Along the Belt and Road*, Beijing: Social Sciences Academic Press (China), 2015, p. 97.



Of course, we do not deny the great value of urban development to CPEC, but the experience of social infrastructure development assistance for Xinjiang reminds us that we should integrate the city with the people as the main body. That is to say, the construction of new downtown and the cultivation of new people should be synchronized. Only in this way can we truly realize the true meaning of modernization and the full liberation of human beings. Well, “new downtown” is easy to understand, so what is meant by “new people”? To some extent, the “new people” of our time are the new citizens, who have more marketable skills and a more open and tolerant mindset. Social infrastructure development assistance for Xinjiang has achieved certain results in cultivating new people, among which, the development of education, “industry-driven employment” and normal cultural exchanges have played a particularly important role. This experience can also be applied to the construction of CPEC. For example, while helping Pakistan to build infrastructure, China is upgrading the skills of Pakistani personnel through education and job training. At the same time, the two countries should establish a normal exchange mechanism for folk culture, give play to the functions of “enculturation” and “inclusion” in the culture, promote the harmonious interaction of Chinese and Pakistani cultures and enhance the cultural identity between each other. On the one hand, it can make up for the lack of economic and political exchanges. On the other hand, it can also reduce the social resistance in the construction of CPEC through the way of “enlightening people’s wisdom”, which is of great benefit to the development of the corridor.

#### *10.5.4 Form Synergy Between Social Resources and Increasing the Involvement of Social Organizations in China and Pakistan*

Social infrastructure development assistance for Xinjiang focuses on the “people”, here “people” refers to both the people and as the folk. Divorced from the people, there is no such thing as the lives of the people, and without the people, people’s lives cannot improve. From the experience of Shanghai’s social infrastructure development assistance for Xinjiang, Shanghai’s Command Office mainly encourages, guides, and supports local social work organizations to provide services in the communities and villages of the four counties in the form of government purchases of services, so as to form a multi-party interactive social synergy and not rely on the government to do it all. So it gives full play to the functions and

practical effects of social organizations in social governance and social construction and narrates the psychological distance between people of all ethnic groups. People-to-people connectivity is also one of the inherent goals of BRI, which is also the theme of CPEC. Therefore, it is obviously not enough to rely on the government to promote people-to-people connectivity. What is more serious is that this kind of one-dimensional government behavior sometimes even causes misunderstanding among the grassroots people.

Someone once argued that in construction process of CPEC, China can no longer build infrastructure and municipal projects alone, because these projects often fail to create direct and profound “Chinese goodwill” for local people. On the contrary, through the exchanges between the social organizations of the two countries, some flexible and comprehensive interactions can be effectively carried out, so as to bring the feeling of “needed” and “respected” to the people.<sup>21</sup> Currently, Pakistan is becoming a more mobile society. A large floating population and large-scale urbanization have led to new behavioral and thinking patterns. The Sunnis and other minorities in Pakistan have begun to examine their own religions. The previously isolated groups have gradually merged, and radical changes have taken place within Pakistani society.<sup>22</sup> The rapid social changes in Pakistan have created conditions for interaction, cooperation, and exchanges between social organizations in China and Pakistan. Judging from the current experience of social infrastructure development assistance for Xinjiang, social organizations in the two countries can start with volunteer activities, charity projects, and social work exchanges, and use service as a medium to shape a positive image of China, and then form a joint force of resources through social organizations to maximize understanding and support of the people.

## 10.6 CONCLUSION

For a long time, we have always believed that “when the Silk Road prospers, Kashgar prospers”. But as far as the current situation is concerned, this sentence is also true in reverse, because the advancement of BRI and

<sup>21</sup>Zhao Lei, *One Belt and One Road: China's Civilized Rise*, Beijing: CITIC Press Corporation, 2015, p. 183.

<sup>22</sup>Hastings Donnan, Pnina Werbner (eds.), *Economy and Culture in Pakistan: Migrants and Cities in a Muslim Society*. Palgrave Macmillan, 1991, p. 2.

the construction of CPEC have given Kashgar an increasingly important strategic position. “When Kashgar prospers, the Silk Road prospers” seems to be a better explanation of it as the key node of the current Belt and Road construction. Of course, the “prosperity” of Kashgar is not only the prosperity of the economy but also the overall development of the local economy and society. Therefore, maintaining social stability and long-term peace and stability in Xinjiang is not only the general principle of Xinjiang work in China but also the basic premise to ensure the smooth implementation of BRI. The donor provinces (municipalities) paired with Xinjiang, represented by Shanghai, have integrated the concept and practice of helping Xinjiang with people’s lives into their actual work, planning, and projects, thus creating a good atmosphere for social stability and economic development in Xinjiang. Furthermore, BRI is a new expression of Chinese discourse. It uses a series of words with Chinese characteristics, such as “belt”, “road”, “bridge” and “corridor”, to convey the “non-polarization” and “decentralization” concepts of equality, inclusiveness, and people-to-people connectivity. From this perspective, it requires us to stop simply misappropriating foreign theories or practices. The key step to boost the progress of CPEC is to correctly summarize and apply the experience of helping Xinjiang with people’s livelihood.

At the second Work Conference on Xinjiang, General Secretary Xi Jinping stressed that paired assistance for Xinjiang is a national strategy that must be adhered to for a long time, and we should make paired assistance for Xinjiang a project to strengthen ethnic unity. Correspondingly, the construction of CPEC is also part of BRI, and its ultimate goal is to achieve the common modernization of China and Pakistan. Therefore, drawing lessons from the experience of helping Xinjiang with people’s livelihood to promote the all-around development of Pakistan’s economy and society is the key to normalizing, tighten and deepening Sino-Pakistan economic and trade exchanges. In general, Belt and Road construction with CPEC as the flagship project is by no means a slogan, nor is it a “one-man show” performed by China on its own. In order to help BRI go global steadily, the academic community in China must pay close attention to the forward trend and conduct comprehensive empirical research on it, so as to provide powerful theoretical support and feasible policy suggestions for the better promotion of BRI.