Islamic Republic of Pakistan
Board of Investment (BOI)

THE PREPARATORY SURVEY ON JICA COOPERATION PROGRAM FOR INDUSTRY DEVELOPMENT (INVESTMENT CLIMATE IMPROVEMENT IN KARACHI)

FINAL REPORT

SEPTEMBER 2012

JAPAN INTERNATIONAL COOPERATION AGENCY

KRI INTERNATIONAL CORP.

Exchange Rate
PKR 1 = ¥ 0.840
USD 1 = ¥ 78.63
September 2012 (JICA designated rates)

Pictures of the Study

Karachi Export Processing Zone (KEPZ)

Bin Qasim Industrial Area

Rehabilitated Mehran Highway

Congested National Highway 05

Industrial Generators for Power Shortages

Industrial Gas Facilities for Gas Shortages

Sindh Police Car

Patrolling Sindh Police Officers

Supermarket in Karachi

Opening Remarks by Chairman, BOI
Seminar on Study Results (August 6, 2012)

Daruma Eye Opening with Hope for
Investment Climate Improvement in Karachi
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Preparatory Survey on JICA Cooperation Program for Industry Development
(Investment Climate Improvement in Karachi)

Final Report

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List of Abbreviations

ADB	Asian Development Bank
AIDP	Auto Industry Development Program
APTTA	Afghan-Pak Transit Trade Agreement
ATI	Association of Trade and Industry
AT&TC	Automotive Testing and Training Centre
BOI	Board of Investment
CMI	Census of Manufacturing Industries
CBU	Complete Built Up
CKD	Complete Knocked Down
CNC	Computerized Numerical Control
CPS	Country Partnership Strategy
CRC	Cold Rolled Coils
ECC	Economic Coordination Committee
EDB	Engineering Development Board
EPZ	Export Processing Zone
FBR	Federal Board of Revenue
FDI	Foreign Direct Investment
FTA	Free Trade Agreement
GDP	Gross Domestic Product
GNI	Gross National Income
GNP	Gross National Product
GOS	Government of Sindh
ICT	Information and Communications Technology
IFC	International Financial Corporation
IMF	International Monetary Fund
IPP	Independent Power Producer
IPR	Intellectual Property Rights
JACI	Japanese Association of Commerce and Industry
JBIC	Japan Bank for International Cooperation
JETRO	Japan External Trade Organization
JICA	Japan International Cooperation Agency
JPBCC	Japan-Pakistan Business Co-operation Committee
KCCI	Karachi Chamber of Commerce and Industry
KEPZA	Karachi Export Processing Zone Authority
KESC	Karachi Electric Supply Corporation
KMC	Karachi Metropolitan Corporation
KTDMC	Karachi Tools Dies and Moldes Centre
MFN	Most Favored Nation
MIGA	Multilateral Investment Guarantee Agency
MNC	Multinational Company
MOC	Ministry of Communication
MOCOM	Ministry of Commerce
MOE	Ministry of Environment
MOI	Ministry of Industry
NEC	National Economic Council
ODA	Official Development Assistance
OECD	Organization for Economic Cooperation and Development

OEM	Original Equipment Manufacturer
OICCI	Overseas Investors Chamber of Commerce and Industry
PAAPAM	Pakistan Association of Automotive Parts Accessories Manufacturers
PAKEPA	Pakistan Environmental Protection Agency
PAMA	Pakistan Automotive Manufacturers Association
PC	Planning Commission
PJBF	Pakistan-Japan Business Forum
PQA	Port Qasim Authority
PSM	Pakistan Steel Mills
PSMA	Pakistan Steel Melters Association
PSQCA	Pakistan Standard and Quality Control Authority
PTA	Provincial Transport Authority
SBOI	Sindh Board of Investment
SDMI	Sindh Development and Maintenance of Infrastructure
SECP	Securities and Exchange Commission
SEZ	Special Economic Zone
SITE	Sindh Industrial and Trading Estate
SMEDA	Small and Medium Enterprise Development Agency
SP	Sindh Police
WTO	World Trade Organization

Chapter 1 Study Outline and Summary

1.1 Study Outline

1.1.1 Background

In response to the request of the Government of Pakistan, the Japan International Cooperation Agency (JICA) decided to dispatch an Investment Climate Advisor (hereinafter referred to as the Advisor) to the Board of Investment (BOI). The Advisor started his work in May 2009.

Under the initiative of the Advisor, "Problem-Analysis and Solution-Action" was submitted to the BOI by the Japan Association for Commerce and Industries (JACI) and the Japan External Trade Organization (JETRO). A number of suggestions from the Japanese private sector were given to improve the business climate in Karachi and these were included in the "Problem-Analysis and Solution-Action". It is strongly recommended for the Government of Pakistan to steadily implement these suggestions to meet the demand of foreign investors and attract future foreign direct investment (FDI).

BOI, JICA, and the Advisor shared the opinion that, in order to put the suggestions into concrete actions, there is a necessity to conduct detailed studies by different specialists from different areas. For the purpose of making a quick response to these requests from the private sector, BOI, JICA, and the Advisor agreed to conduct the "Basic Study on Program for Investment Climate in Karachi" (hereinafter referred to as the Study). Accordingly, JICA decided to undertake the Study in close cooperation with the BOI. The scope of work between BOI and JICA was concluded on October 14, 2011.

1.1.2 Objectives of the Study

The objectives of the Study are: 1) To identify the problems and bottlenecks in the area of a) administrative regulation, permissions, and authorizations on corporate activities and b) security, commutation and living environment for foreign employees to attract investment to the study area in Karachi and 2) To suggest action plans to solve and remove them, and 3) To make a "Policy Matrix for Investment Climate Improvement" in the formulation of future program/projects under the Japanese official development assistance (ODA).

1.1.3 Study Area

The Study targets 1) Karachi Export Processing Zone and 2) Bin Qasim Industrial Area.

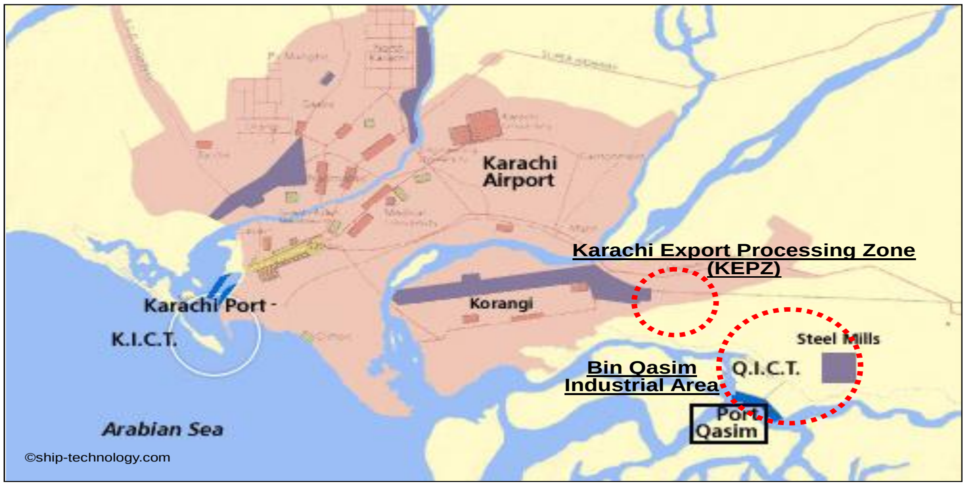


Figure 1.1.1: Map of the Study Area

1.2 Study Methods

1.2.1 Schedule of the Study

The Study was implemented from April to September 2012 in accordance with the following chart. The Inception Report, Interim Report, and Draft Final Report were discussed and agreed with the Pakistani counterpart, BOI. Study results, including priority issues and a policy matrix, were presented and discussed with authorities concerned and private companies at the BOI-JICA Joint Seminar on Investor Friendly Climate Improvement in Karachi on August 6, 2012. This report was prepared in light of opinions given at the seminar.

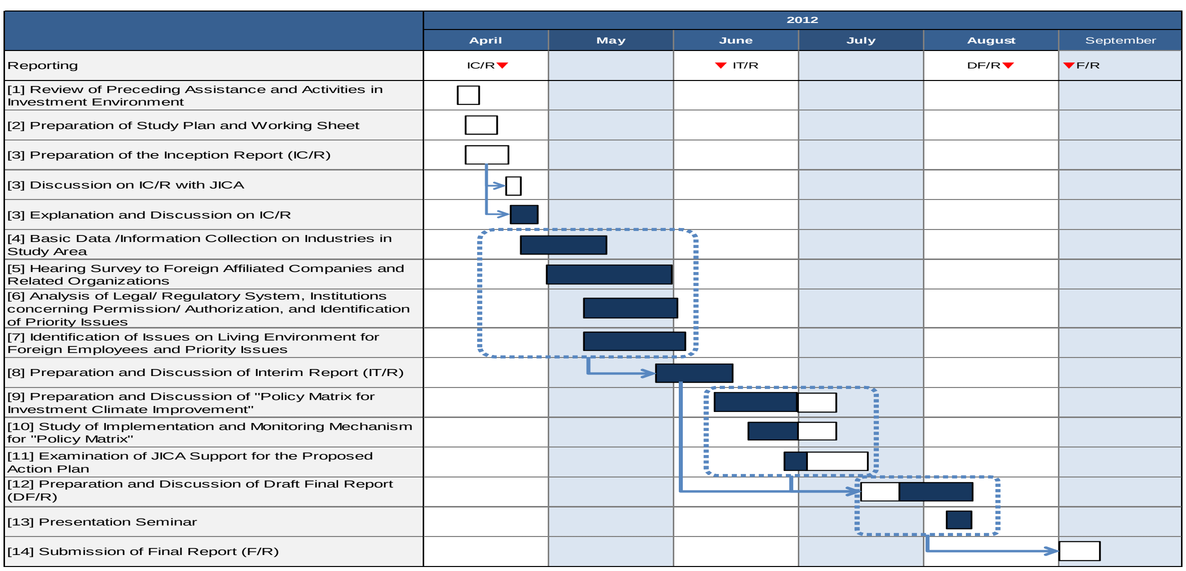


Figure 1.2.1: Study Schedule

1.2.2 Study Methodology

The Study was conducted through (1) literature reviews; (2) interviews with government bodies and industry groups; and (3) interviews with and questionnaire surveys to foreign companies in Karachi

(1) Literature Reviews

Literature reviews are shown in Chapters 2 and 3. Analyzed were reports by Pakistani government bodies like the Planning Commission (PC), international organizations such as the International Monetary Fund (IMF), World Bank, Asian Development Bank (ADB) , and JICA including the then Japan Bank for International Cooperation (JBIC), and requests and suggestions to the government from industry groups.

(2) Interviews with Government Bodies and Industrial Groups

- Government bodies: BOI Karachi Office, Karachi Export Processing Zone Authority (KEZA), Port Qasim Authority (PQA), Sindh Board of Invesment (SBOI), Karachi Metropolitan Corporation (KMC), JETRO, Pakistan Standard and Quality Control Authority (PSQCA), etc.
- Industry groups: Pakistan –Japan Business Forum (PJBF), Karachi Chamber of Commerce and Industry (KCCI), Overseas Investors Chamber of Commerce and Industry (OICCI), Pakistan Automotive Manufacturers Association (PAMA), Pakistan Association of Automotive Parts Accessories Manufacturers (PAAPAM), etc.

(3) Interviews with and Questionnaire Survey to Foreign Companies in Karachi

- Foreign companies (interviews on business activities only): Japanese trade companies (6), Japanese bank (1)
- Foreign companies (questionnaire survey on business activities): Japanese companies (5), other foreign companies (20)
- Foreign managers (questionnaire survey on the living environment): 13
- Local employees (questionnaire survey on the living environment): 24

1.3 Summary

The following numbers of chapters, sections, figures, and tables correspond to those in Chapters 2 to 5.

Chapter 2 Needs of Economic Development and Karachi Development Potential

2.1 Introduction

2.2 Economic Growth of Pakistan

Since its independence in 1947, the Pakistani economy has grown with fluctuations. In the last sixty years, Pakistan has maintained an average growth rate of more than 5% per annum. This growth rate has been attributed to a conscious effort of the government and policy makers on industrial and commercial sector development. However, despite being an agrarian economy, agricultural output growth has been around 3.7% per annum, on the average.

The agriculture sector was the main productive sector, contributing 37% of the gross domestic product (GDP) in 1970. However, with the passage of time, non-agricultural sectors have grown more than the agriculture sector, as shown in Table 2.2.2. This resulted in the reduction of agriculture sector's share in GDP to 21% in 2011. The manufacturing sector has increased its share from about 16% in 1970 to more than 18% in 2011. Given the economic transition away from the agriculture sector to the manufacturing and services sectors, the manufacturing sector needs to grow to absorb redundant labor force. However, the manufacturing sector has remained stagnant while other sectors have increased their share in the gross domestic output. There has been an overall increase in the share of services sectors including retail trade in GDP.

Table 2.2.2: Sectorial Share in GDP (%)

SECTOR	1970	1980	1990	2000	2011
Aggregate	100.0	100.0	100.0	100.0	100.0
Agriculture	36.83	29.60	26.00	26.17	21.20
Mining and Quarrying	0.53	1.06	0.71	1.37	2.40
Manufacturing	16.10	15.84	17.41	14.81	18.70
Utilities	1.52	2.28	2.83	3.96	2.30
Construction	4.20	5.66	4.22	2.50	2.10
Retail Trade	14.94	16.01	17.00	17.62	17.10
Transport	6.80	7.36	8.00	11.36	9.90
Finance	5.50	5.94	7.31	6.90	7.40
Services	13.62	16.27	16.58	15.35	19.00

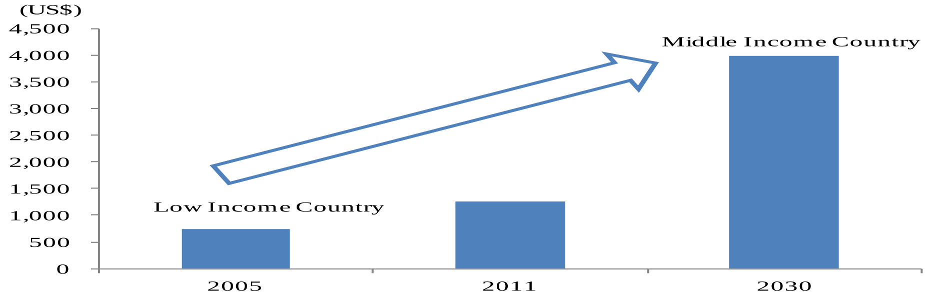
Source: JICA Study Team' calculation based on Government of Pakistan, "Economic Survey" various issues

Although there are wide fluctuations in sectorial and aggregate real GDP growth rates in different time periods, the overall performance of the economy in terms of growth has been fairly well.

2.3 Need for Sustainable Economic Development

The vision statement projects that a 7-8% growth rate per annum will contribute to an increase in the per-capita GDP of Pakistan from US$742 in 2005 to US$4000 in 2030 (Figure 2.3.1). Should this projection materialize, Pakistan will ascend from its position as a low-income country and join the ranks of the middle-income countries.

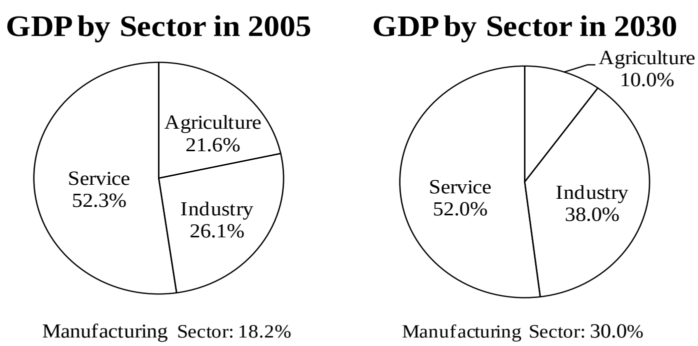
The annual GDP growth rate of the country was 5.5% on average for five decades from 1961 to 2010. In order to achieve these quantitative targets, the annual growth rate needs to be increased further by more than 1.5-2.5% from this long-term trend of GDP growth. Considering the wide swings in GDP growth rates during the period, the target growth rate seems considerably challenging for the administration.



Source: Vision 2030

Figure 2.3.1: Development Target of GDP per Capita in 2030

In order to embark on a long-term sustainable growth path, Pakistan's economy will have to go through significant structural changes. In terms of GDP share by sector, the value added goods generated by the agricultural, industrial (manufacturing), and service sectors, currently stand at 21.6%, 26.1% (18.2% for manufacturing), and 52.3%, respectively. If Pakistan is to achieve its "Vision 2030" targets, then over time these shares will have to change to10%, 38% (30% for manufacturing), and 52%, respectively, in fiscal year 2030.

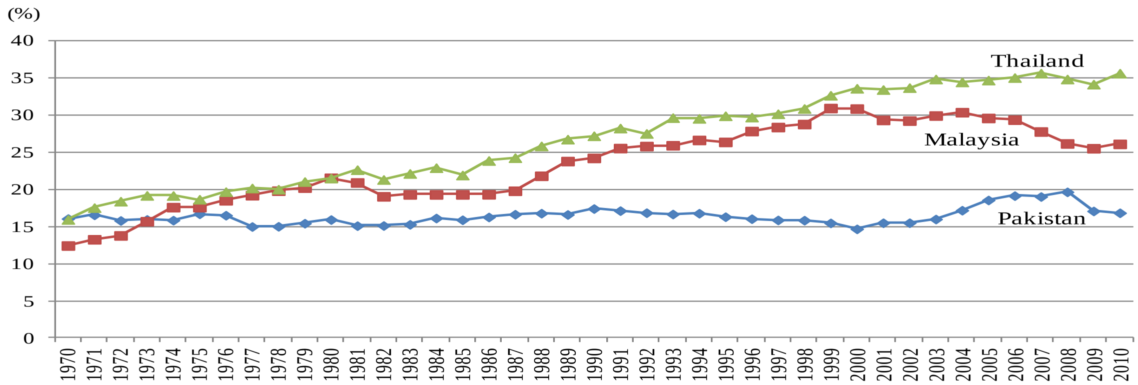


Source: Planning Commission, "Vision 2030"

Figure 2.3.2: Development Targets by Sector in 2030

2.4 Need for Industrial Sector Development

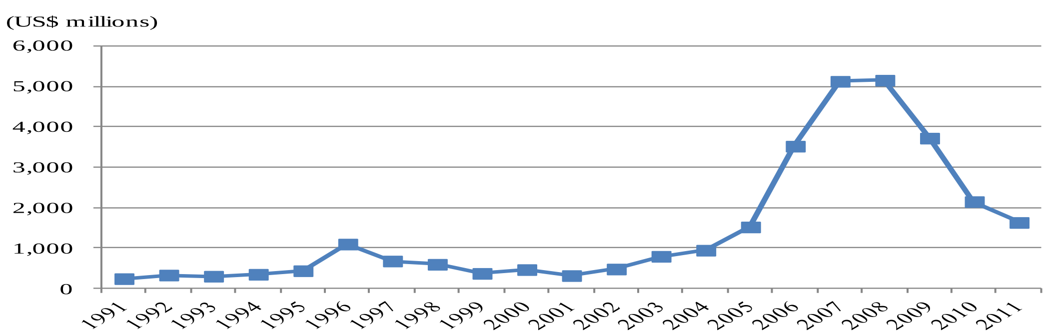
Figure 2.4.3 exhibits the trends of manufacturing shares in GDP of Pakistan, Malaysia, and Thailand. The share of manufacturing in Pakistani GDP reveals a meager improvement during the period from 1970 to 2010 with wide fluctuations. The share of GDP in 1970 was stood at around 16.1% in 1970 and increased to over 19% in 2006. However, it reverted back to 16.8% in 2010. Meanwhile, the manufacturing value added to GDP in Malaysia increased from 12.4 % in 1970 to almost 30 % in 2006, and stood at 26.1% in 2010. In the case of Thailand, the manufacturing value added to GDP increased from about 16% to 35.6% from 1970 to 2010.



Source: World Bank, World Development Indicators

Figure 2.4.3: Shares of Manufacturing in GDP in Pakistan, Malaysia, and Thailand

Since 2007/08, the direct investment in the country continues to decline. Many reasons seem to attribute to the decrease after 2008: one of the major reasons is the global economic and financial recession after 2008. Other reasons were: the tainted credibility and inconsistent policies of the administration; the deteriorated law and order conditions in the country; the delayed and still unresolved energy crisis; and enterprises could not regain confidence with frequently alternated administration and absences of long-term investment plans under current law and order conditions.



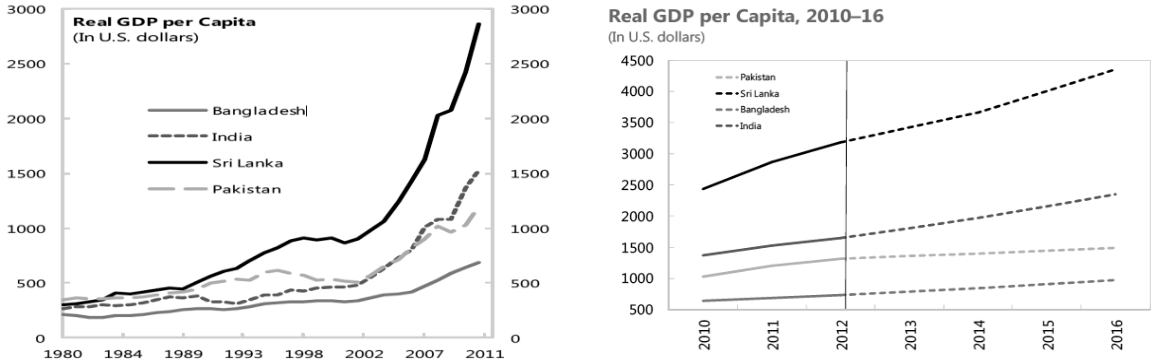
Source: Economic Survey of Pakistan 2010/11

Figure 2.4.5: FDI Trends in Pakistan

2.5 Partnership Strategies and Reforms Scenarios

2.5.1 Reforms Support from the International Monitory Fund (IMF)

Pakistan's per capita real income has risen by 0.7% in 2010/11 as opposed to 2.9% in 2009/10. This reflects the impact at a slower economic growth. The per capita income rose from US$1073 in 2009 to US$1254 in 2010/11, thereby showing a tremendous increase of 16.9%. This is mainly because of the stable exchange rate as well as the higher growth in nominal gross national product (GNP).It is estimated that if this trend continues then per capita income will rise to US$1500 in 2016.[1]



Source: IMF Country Report No. 12/35, February 2012

Figure 2.6.1: GDP per Capita Trend of Pakistan and South Asian Countries and GDP per Capita Estimation in 2016 by IMF Staff

2.5.2 Partnership with the World Bank

The four strategic pillars of the Country Partnership Strategy (CPS) are described below:

- Improving economic governance;
- Improving human development and social protection;
- Improving infrastructure to support growth; and
- Improving security and reducing the risk of conflict.

2.5.3 Partnership with ADB

The main areas of current ADB operations in Pakistan reflected in the CPS 2009-2013 are stated below:

- Energy;
- Infrastructure investments in transport, logistics, and irrigation;
- Reforms in key sectors including energy, finance, agriculture, and industry; and
- Urban services, including water, waste management, and transport.

2.6 Karachi Development Potentials

2.6.1 Population

Karachi has increased its share to the total Pakistan, from 4.96% in 1971 and 3.52% in 1981 to 4.05% in 2010. With rapid expansion and growth, the current population share in the country's total population was estimated at over 10% in 2010.

[1] International Monitory Fund, "Pakistan 2011 Article IV Consultation and Proposal for Post-Program Monitoring, 2012" http://www.imf.org/external/pubs/ft/scr/2012/cr1235.pdf

Table 2.6.1: Population Trend and Projections of Karachi

Year	1931	1941	1947	1951	1961	1971	1981	1998	2005	2010	2020	2030
Population (million)	0.26	0.38	0.40	1.07	1.91	3.51	6.44	9.86	15.12	18.9	27.6	31.6
Area (persons/sq km)	-	-	233	-	-	-	1994	3527	3566	-	-	-
Growth Rate (%)	3.7	11.6	-	6.05	5.0	4.96	3.52	3.02	4.16	4.05	3.50	3.50

Source: JICA Study Team's calculation based on various sources.

2.6.2 Karachi Mega-city

One of the competitive advantages of the city is its geo-strategic location as major seaports and networks which provide a potential gateway to investors for access to Central Asian Corridors. Along with extensive industrial infrastructure, the city is also the nucleus headquarters of major banks, financial institutions, and business houses.

Karachi is the financial and commercial capital of Pakistan. The city accounts for a lion's share of Pakistan's revenue generation. It generates approximately 53.38% of the total collections of the Federal Board of Revenue, of which 53.33% are customs duty and sales tax on imports[2]. Karachi produces about 30% of the value-added in large scale manufacturing[3] and 20%[4] of the GDP of Pakistan.

2.6.3 Karachi Vitalization Scenario

JICA (the then JBIC) report on "Karachi Vitalization Scenario, 2004" concluded that Karachi is also the center of Pakistan's manufacturing industry and serves as a key hub for transport and distribution operations due to its close proximity to shipping lanes through two major seaports. As such, it serves as a hub not only for Pakistan's domestic distribution network but also for the flow of goods to neighboring countries like Afghanistan and points across Central Asia. On the other hand, the report pointed out that infrastructure deficiencies are bottlenecks in the development of Karachi. Therefore, necessary measures are required to improve the investment climate.

Karachi vitalization requires full collaboration between the public and private sector.

2.7 Current Conditions of Manufacturing Sector in Karachi

2.7.1 Position of Manufacturing Sector in Karachi

Census of Manufacturing Industries (CMI) 2005/06 showed the value of production at Rs2929

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[2] Federal Board of Revenue. "Year Book" (2006-2007) http://www.cbr.gov.pk/YearBook/20062007/FBRyearbook2006-2007.pdf.
[3] Pakistan and Gulf Economist. "Karachi: Step-motherly treatment". http://www.pakistaneconomist.com/database2/cover/c99-15.asp.
[4] ADB. "Karachi Mega-Cities Preparation Project".http://www.adb.org/Documents/Produced-Under-TA/38405/38405-PAK-DPTA.pdf.

billion depicting an increase of 165% over Rs1104 billion in 2000/01. The values of production in Sindh Province is ranked as second and accounted for almost 40% of the country.

Table 2.7.2: Value of Production at Producers' Prices in Latest CMIs (Rs million)

Region	**1990-91**	**1995-96**	**2000-01**	**2005-06**
Pakistan	369,664	678,196	1,104,185	2,929,320
Punjab	162,052	321,623	497,708	1,405,699
Sindh	179,736	280,662	522,617	1,200,402
KP	14,993	60,689	46,439	164,313
Balochistan	9,822	8,843	23,828	136,582
Islamabad	3,061	6,379	13,593	22,324

Source: CMI 2005-06

2.7.2 Current Manufacturing Conditions in Karachi

According to the "Directory of Industrial Establishments in Sindh 2010", there were 1218 units (Manufacturers in Karachi) in 45 sectors. The garments industry had the largest share of the manufacturing sector with 128 units and accounted for about 10.5% of the whole. It is followed by the dyeing and printing and engineering and miscellaneous industries which had 97 and 90 units and accounted for 8.0% and 7.4%, respectively.

2.7.3 Current Conditions of the Automobile Industry Representing Karachi

The automobile industry in Pakistan is a medium-sized but fast growing industry.[5] It is one of the important industries to be promoted on account of its broad expansion of supporting industries and big employment effects. The total manufacturing employees are 192,000, and 1,392,000 if including the indirect sectors of 12,500 car dealers.

2.7.4 Current Conditions of the Steel Industry Representing Karachi

The iron and steel industry is one of core industries in Pakistan such as petrochemicals, cement, electricity/gas, refinery, automobile industries.

The total availability of mild steel re-rolled products was estimated at about 4.7million tons, out of which about 2.8 million tons (about 60%) was supplied through domestic production including production of Pakistan Steel Mills (PSM) and 1.8 million tons (about 40%) through imports of various types of finished products. Imports have consistently increased year by year. Foreign steel makers such as Japanese and Korean companies have invested in substantial quantities of construction and building materials and high quality steel for the automobile industry to meet domestic demand which reflects insufficient local production capacity

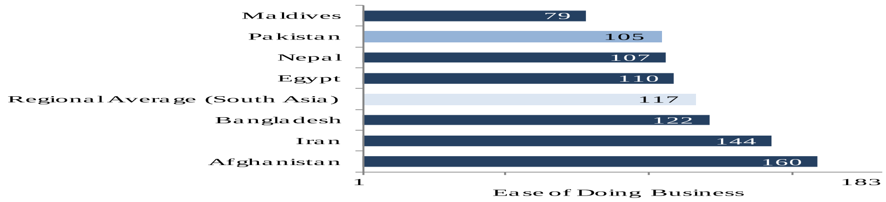
[5] UNICO International Corporation/ JICA. 2011. "Final Report: Project for Automobile Industry Development Policy in the Islamic Republic of Pakisnta".

Chapter 3 Issues of Investment Climate Proposed by International Organizations and Industrial Associations

3.1 The Business Environment – Doing Business 2012

3.1.1 International Comparisons

In the World Bank "Doing Business Report 2012", Pakistan ranked 105th out of 183 countries.



Source: World Bank, "Doing Business Report 2012"

Figure 3.1.1: Pakistan and Competitive Economy's Ranking on the Ease of Doing Business

3.1.3 Domestic Comparisons

A new report ranked Faisalabad as the most business-friendly city in Pakistan, followed by Multan (2nd) and Lahore (3rd). Pakistan's largest commercial metropolis Karachi, came out at 9th place in the list of 13 cities in Pakistan.

3.2 Business Environment and Investment Survey

3.2.1 World Bank Enterprise Survey

The country profile for Pakistan is based on the data from the Enterprise Surveys conducted by the World Bank. Business owners and top managers in 935 firms were interviewed from September 2006 through June 2007. The benchmarks included the averages for the group of countries in South Asia and Pakistan's income group.

More than 65% of the respondents considered electricity as the biggest obstacle in their businesses, followed by corruption and others.

When responses were compared with regional averages of the South Asian region, Pakistan has better position in most cases except for electricity and corruption. The World Bank`s Enterprise Survey has been further explained in Appendix C.

3.2.2 Perception and Investment Survey 2011 by the Overseas Investors Chamber of Commerce and Industry (OICCI)

The Perception and Investment Survey 2011 was conducted with responses received from 105 members of the OICCI, representing 13 industrial sectors.

If OICCI takes only the worse rating, Pakistan fares relatively poor compared to the eight other economies. Most importantly, 45% of the respondents preferred that India is better for ease of doing business than in Pakistan. While 17% of the respondents felt that there is more ease of doing business in Pakistan than in India while 19% perceived that conditions to be the same.

In the context of the overall present environment in Pakistan, the mixed responses can be termed marginally satisfactory.

3.3.2 Additional Information Relating to Industrial Activity

The following new information was obtained through this study.

Electricity outage in Karachi is better than Islamabad and Lahore.

(i) Hundred percent of firms in Islamabad experienced power outages in 2010 compared to 66% in 2007. Firms in the Karachi region, however, are evenly split on their perception on the improvement of electricity supply which was an obstacle to their business from 2007 to 2010.
(ii) The Karachi region saw the smallest increase (from 33 outages per month in 2007 to 80 in 2010), while firms in Islamabad and Lahore both saw much higher increases in the number of power outages (averaging about 150 outages a month in 2010).
(iii) Corruption appears relatively less problematic.
(iv) From 2007 to 2010, the percentage of firms that considered corruption to be a severe obstacle decreased from 27% to 14%, and the percentage perceiving it to be a major obstacle decreased from 38% to 15%.
(v) Financial flow problem.

Since the global financial and economic crisis started in 2008, bank exposure to public sectors has been rising. This is on account of the increase in government reliance in the banking sector to fund its deficits and is manifested in both advances and investment portfolios. With 87% of the budget deficit of Rs1.1 trillion for FY 2013 projected to be financed through domestic sources, exposure of the banking sector to public sectors is expected to increase further.

3.3 Proposal Proposed by Japan-Pakistan Business Co-operation Committee (JPBCC) and Pakistan-Japan Business Forum (PJBF)

During the field survey, both suggestions and requests from the Japanese side in 2009 had been confirmed through the interview survey. However, almost all issues are pointed out by key informants of the foreign affiliated companies. This means that investment climate improvement has almost no progress from 2009 to date

3.4 Problem–Solution Analysis

Problem-Analysis and Solution-Action was formulated and submitted by the Japanese side in February 2011.

The progress of the implementation of such action plans and measures are identified below, through interviews with the BOI, JACI, and the JICA Investment Climate Advisor to BOI. As to the results of the progress, roughly, i) half of the requests were already solved, ii) one-fourth of the requests were almost solved but not yet completed, iii) another one-fourth of the requests were not yet solved and are still under negotiation with related organizations in Pakistan.

Table 3.4.1: Requests for Improvement from Japanese Companies in Karachi (April 2011)

Sector	Requests
KEPZ	1) Improvement of security; 2) Improvement of access to road, power, and water; 3)Improvement of safety preventive system (fire hydrant, guard man); and 4)Improvement of taxation, operational/ administrative producers.
Banking Operation	1) Relaxation of banking regulations.
Automobile Industry	1)Improvement of security; 2) Introduction of stable policy preferable to local mobile manufactures; 3) Improvement of power and water supply; 4) Improvement of taxation; 5) Road expansion; 6) Development of access road to Qasim Port; and 7)Establishment of export repayment system.
Steel Industry	1)Improvement of security; 2) Road expansion; 3)Improvement of import duties; and 4)Establishment of subsidy and relief scheme.

Source: “Problem -Analysis and Solution-Action"

Chapter 4 Issues Identified from Interview Survey

4.1 Introduction

The Study is focused on the industrial activity in Karachi. In this regard, the JICA Study Team carried out a survey to collect information on companies in respect of their characteristics, business activities, security of business operation, legal/regulatory environment, access to and processing of information, status of infrastructure and its improvement, administrative procedure/facilitation for FDI and management issues of companies. Furthermore, the survey also covered the living environment issues of foreign and local employees.

The survey was carried out in May 2012. The sample size of the survey consisted to 25 multinational and joint-venture companies. These companies represented highly diversified nationalities of the world. They included: Japan, the United States of America, United Kingdom, France, Germany, the Netherlands, Switzerland, Hong Kong, Taiwan, Malaysia, South Korea, United Arab Emirates, etc. From the companies surveyed, 20% of the sample comprised of Japanese firms only.

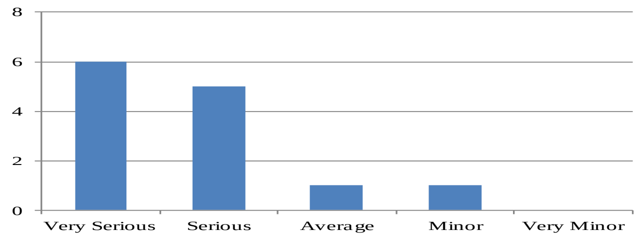
These companies operated in various locations of Karachi. However, 68% of the companies in the survey were located in industrial zones under the operation of KEPZA and PQA. The majority of the companies in the sample were old establishments. More than 40% were established during 1970s and 1980s. While another 33% started their operation in the1990s. Most of the firms, around 63% in the sample, were private listed companies, while public listed companies comprised 21% in the sample.

The production operation of the companies in the sample survey was quite widely diversified. Their products include apparel, pharmaceutical, chemicals, engineering and electronic items, metal and plastic products, etc. However, majority of firms, about 20% in the sample, were producing textile products. It was found out in the survey that the availability of raw materials and the firm's products in the domestic market were the main reasons that these companies made their investment in Karachi. In this connection, more than 83% of companies in the sample mentioned that they were successful according to their investment plans.

It was found out that companies in the sample have arranged various security measures such as installation of closed-circuit television cameras (CCTV), security guards, security escorts, etc. In this regard, they were also concerned with the law and order situation. However, majority of the companies, about 90% in the sample, did not find themselves under terrorist threat. On the other hand, foreign employees working in companies in the sample felt relatively less secured in their capacity as compared to the organizations in which they are working. These observations demonstrated the existence of security and law and order situation in the city, which is seriously needed.

Although companies were relatively satisfied with the facilities and services offered by KEPZA and PQA, in general, they showed large discontentment with the role of government institutions and other regulatory bodies. This is true especially when firms were confronted with different problems and issues such as poor infrastructure, provision of utilities, access of information, administrative procedures for FDI approval, management issues, etc. The sample data of companies regarding satisfaction in the investment which they made in their business operation, their dissatisfaction with the law and order situation, discontentment with the role of the government and other regulatory bodies in attracting investors and the operation of companies need to be taken on a serious note in order to improve the investment climate in Karachi and in other parts of the country. It requires a more efficient role of government institutions in delivering their tasks, good governance, and consistent policies in order to create an enabling environment for more FDIs and better business opportunities in the country.

The questionnaire used also addressed various issues about the living environment for foreign and local nationals working in the sample companies. These included: security, housing, commuting, food, healthcare, education, entertainment, etc. The data in the sample reflected that foreign nationals took all these issues seriously, therefore, it cannot be ignored and need to be addressed. As a whole, Karachi is not a pleasant environment for foreign people to live in. As shown in the figure below, as many as 11 out of 13 respondents rated the overall living environment as a very serious or serious concern.



Source: JICA Study Team

Figure 4.3.9: Foreign Employees' Views on Severity of Overall Living Environment

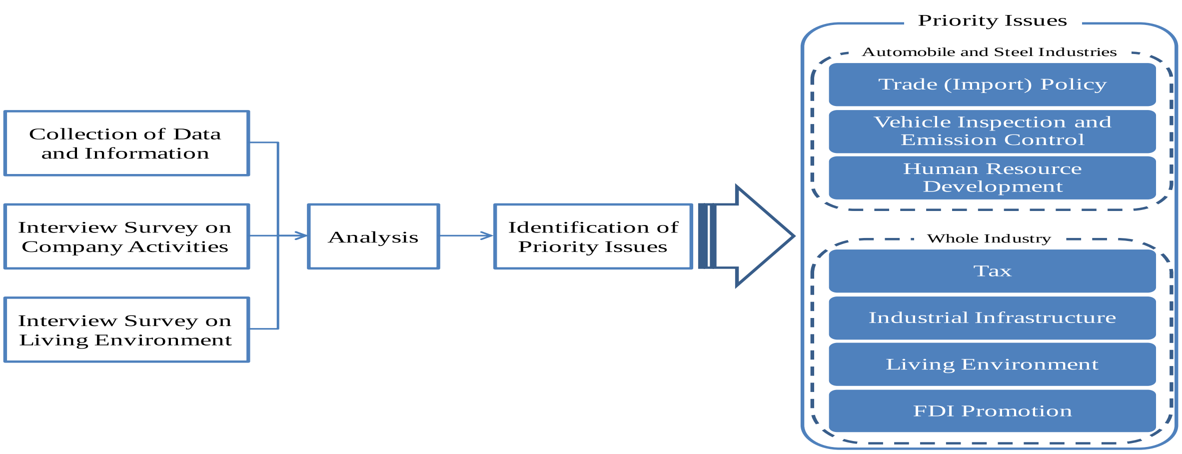
Chapter 5 Identification of Priority Issues and Policy Matrix for Investment Climate Improvement in Karachi

5.1 Priority Issues

5.1.1 Process to Identify Priority Issues

To identify priority issues, the JICA Study Team interviewed foreign companies in Karachi about their business activities and living environment and analyzed issues of the investment climate in light of the following preceding studies: BOI "Problem-Analysis and Solution-Action", World Bank "Doing Business" and "Enterprise Survey" and suggestions from JPBCC, PJBF, and OICCI.

Consequently, priority issues identified are seven: Trade (import) policy; vehicle inspection and emission control; human resource development; tax; industrial infrastructure; living environment; and FDI promotion and approval and trade procedures. They are categorized into two groups, namely 1) issues with big impacts on the development of and the promotion of FDI in the automobile and steel industries and 2) issues with impacts on the promotion of FDI in the whole industry, as shown in Figure 5.1.1.



Source: JICA Study Team

Figure 5.1.1: Process to Identify Priority Issues and their Categories

5.1.2 Rationales for the Identification of Priority Issues with Big Impacts on the Automobile and Steel Industries

(1) Trade (Import) Policy

The issue of import policy was raised in "Problem-Analysis and Solution-Action" and also in the interview survey during this study.

(2) Vehicle Inspection and Emission Control

The development of vehicle inspection and emission control was suggested in the JICA Project for the Automobile Industry Development Policy in 2011. Moreover, the development of the automobile industry is national policy.

(3) Human Resource Development

Human resource development for the automobile industry was suggested in the JICA's Project for the Automobile Industry Development Policy and was also requested in the interview survey. Moreover, the automobile industry has a broad base of supporting industries and can create employment opportunities.

5.1.3 Rationales for the Identification of Priority Issues with Impacts on the Whole Industry

(1) Tax

The issue of taxes was raised in "Problem-Analysis and Solution-Action", "Doing Business", the OICCI's report and also in the interview survey.

(2) Industrial Infrastructure

The issue of industrial infrastructure was raised in "Problem-Analysis and Solution-Action", "Doing Business", the OICCI's report and also in the interview survey.

(3) Living Environment

The issue of the living environment was raised in "Problem-Analysis and Solution-Action" and also in the interview survey.

(4) FDI Promotion

Strengthening BOI functions and powers and the minimum investment size in SEZ were identified as issues in consultation with the Investment Climate Advisor. Improvement in EPZA services was suggested in "Problem-Analysis and Solution-Action" and was identified as an issue in consultation with the Advisor.

5.2 Issues with Big Impacts on the Automobile and Steel Industries

5.3 Issues with Impacts on the Whole Industry

The current situation and implications of each issue were made by the JICA Study Team as shown in the following sheets.

(i) Import Policy (refer to Table 5.2.1 in the following sheet)
(ii) Vehicle Inspection and Emission Control (refer to Table 5.2.2)
(iii) Human Resource Development (refer to Table 5.2.3)
(iv) Tax (refer to Table 5.3.1)
(v) Industrial Infrastructure (refer to Table 5.3.2)
(vi) Living Environment (refer to Table 5.3.3)
(vii)FDI Promotion (refer to Table 5.3.4)

5.4 Policy Matrix for Investment Climate Improvement in Karachi

Among the seven priority issues, tax and industrial infrastructure are not included in policy matrix because they are in the hands of the Investment Climate Advisor and another study team. Below are the five pillars of policy matrix formulated to solve the priority issues to be taken by the Pakistani side based on outcomes and outcome indicators.

PILLAR-1: Formulation of Import Policy (refer to Table 5.4.1 in the following sheet)
PILLAR-2: Consolidation of Environment Friendly and Safe Transport System (refer to Table 5.4.2)
PILLAR-3: Human Resource Development in Automotive Industry (refer to Table 5.4.3)
PILLAR-4: Establishing Safe Commuting (refer to Table 5.4.4)
PILLAR-5: Capacity Development of One-Stop Services for FDI Promotion (refer to Table 5.4.5)

Pillars 1 to 3 will have effects on the development of and FDI promotion in the automobile and steel industries and provide solutions issues faced mainly by Japanese companies in Karachi. Meanwhile, Pillars 4 and 5 will have effects on the whole industry and promote FDI in the whole industry.

As the issues are wide-ranging, overall outcome goals and indicators are based on "Vision 2030," IMF reform scenario, and Auto Industry Development Program (AIDP).

5.6 Projects to be Implemented for FDI Promotion

Some of the projects in the above policy matrix may be difficult for the Pakistani side to implement alone and may need technical and financial support from bilateral and/or multilateral donors. Figure 5.6.1 shows the projects that will require support from the donors.

Category	Project Name	Scheme	Implementation Schedule					Project Budget	Financial Support	Executing Agency
			2013	2014	2015	2016	2017			
Capacidy Development for FDI Promotion	Dispatching an investment policy expert to BOI	TC							No	BOI
Human Resource Development in Automobile Industry	Dispatching an industrial policy expert to BOI	TC							No	EDB
	Dispatching technical experts for high-technology guidance to the automobile industry in Karachi	TC							No	SMEDA
	Provision of high-technology equipment for a technical training center	Grant						US$2 million	Required	EDB, KTDMC
	Provision of testing equipment and tools for emission control (Euro-2)	Grant						US$1 million	Required	PSQCA
Reinforcement of Security during Commuting	Capacity development of the Sindh Police for tighter security	TC						US$145,000	Required	SP

Source: JICA Study Team
Note: Preparation stage, Execution

Figure 5.6.1: Projects to Acquire Technical and Financial Support

Priority Issues

1. Automobile and Steel Industries

Table 5.2.1: Import Policy

Category	Current Situation	Implications
Import duty	● Tariff rates on complete built up (CBU) motor vehicles units were reduced from the 75-150% range to the 50-75% range in 2005/06 and a further proposed reduction in slabs to 40-75% in 2012/13. ● A maximum tax of 35% is imposed on imported parts that have been already manufactured domestically, but it is to be reduced to 30% in 2012/13. ● In the case of greenfield investment, even parts can be imported at the complete knock down (CKD) tax rate for three years as a special case of CKD, probably for the promotion of FDI. The special period is to be extended from three to four years or more. ● In the steel industry, an import tax on competing products, namely cold rolled steel sheets, was lowered from 10% to 5% in 2011.	The development of the local parts manufacturing industry is important in view of employment and ripple effects on linked industries. Reductions in import duties force local parts manufacturers to lower their product prices down to those of import products and therefore cannot secure profits as planned with subsequent negative impacts on their management. Frequent changes in duty rates disturb long-term business planning, sound corporate management, and investment expansion from a long-term standpoint. Import duties are imposed on CKD parts, but the rate is lower than that on CBU units. The small difference between the two rates discourages the localization of CKD parts. Local parts manufacturers consist of many local companies and contribute to employment creation. Tariff cuts will harm the competitiveness of locally manufactured products against competitive than import parts and make it difficult to develop the local parts manufacturing industry, thereby influencing employment and technical transfer adversely.
Import of Used Vehicles	● The age limit of imported used cars was relaxed from three years to five years in 2011. ● Despite the age limit, cars worn out in the rest of Asia are imported and modified for local use. Especially many decrepit trucks are imported illegally by abusing the category of "Special Purpose Vehicle". ● Chinese companies under-invoice many imported used cars and motorcycle parts.	Pakistan's domestic market is huge, considering the population size. Under the influence of the import of used cars and the global financial crisis in 2008, the volume of car production is much less than estimated in the target of the Auto Industry Development Program (AIDP). The annual demand of automobiles is 220,000, of which 4,000 were imported used automobiles. Due to uncertainty about the future market size, investors are unable to decide new investment. Under-invoicing of imported used cars impedes fair competition in the domestic market and harms the local automobile industry. There is a concern that the import of decrepit used vehicles will also have negative effects on the environment, and traffic safety.

Source: JICA Study Team

Table 5.2.2: Vehicle Inspection and Emission Control

Category	Current Situation	Implications
Safe transport and environmental protection.	● Vehicle inspection is not required for motorcycles and passenger cars while semi-annual inspection on commercial vehicles (buses, trucks, taxis, and rickshaws) is compulsory. ● Exhaust emissions have been regulated since 2007.	Only 30% of vehicle owners receive semi-annual compulsory inspection according to inspectors. Specifications for inspection items are not clearly defined. Inspection is carried out visually and no equipment is used. Some examiners are said to check documents only and do not inspect vehicles. Such lax enforcement of vehicle inspection is a problem, in addition to lack of equipment for vehicle inspection and designated inspection stations. Euro-2 emission standards were introduced, yet with lack of testing facilities, Pakistan Standard and Quality Control Authority (PSQCA) and the Provincial Transport Authority (PTA) have difficulty in implementing emission tests and controlling emission thoroughly. The incomplete implementation of vehicle inspection and emission control is likely to facilitate the import of old used cars, thereby harming the local automobile industry as mentioned above. There is concern that decrepit cars such as scrapped cars may cause safety and environmental problems.

Source: JICA Study Team

Table 5.2.3: Human Resource Development

Category	Current Situation	Implications
Technology and quality upgrading in the automobile parts industry	● The automobile industry is faced with shortage of skilled workers. Human resources are developed through in-house training such as on–the-job training of automakers with human resources that can give technical guidance. ● There is shortage of skilled human resources in repair. ● The automobile industry is concerned that local parts manufacturers will fail due to lack of international competitiveness if Pakistan normalizes trade relations with India and automobile parts are imported from India.	The rapid growth in the automotive sector in Pakistan is difficult to sustain without efficient human resources. Presently, the industry is faced with severe shortage of trained engineers, supervisors and workers in the assembly operation and parts manufacturing. The deficiency of skilled personnel, which is a serious handicap, is more on account of rapid growth of the automotive sector and also due to lack of any institution for providing the high quality training required by the automotive industry. Also, the management of local parts manufacturing lacks skills and knowledge about business management. As a result, product failure rates are high and delivery deadlines are not strictly observed. This hinders the expansion of their business with automakers.

Source: JICA Study Team

2. Whole Industry

Table 5.3.1: Tax

Category	Current Situation	Implications
Turnover tax	● A turnover tax is imposed on the sales of corporations. Pakistani taxation is incoherent. The turnover tax was 0.5% in 2009 but was changed to 1.0% in 2010. In 2012/13, however, the minimum turnover tax is to be reduced back to 0.5%.	The current tax on sales leaves some companies in the red after tax and causes a loss to them. Frequently changed taxation is not attractive to foreign investors and does not promote FDI.
Infrastructure cess	● Although companies in export processing zones (EPZs) are exempted from many taxes, an infrastructure cess of 0.5% on imported materials is still levied in KEPZ.	According to the EPZ Act, Import Policy Order applicable to ordinary import is not applied to import to EPZs. The infrastructure cess is applied only by the Government of Sindh among provincial governments. Its application to companies in KEPZ is contradictory to the Export Processing Zone (EPZ) Act and unreasonable.

Source: JICA Study Team

Table 5.3.2: Industrial Infrastructure

Category	Current Situation	Implications
Access roads	● Industrial transportation, such as the import of materials, the export of product, and employees' commuting, depends on road transport because of its inefficient railway transport system. ● Despite the importance road transport, recently general crimes, such as robbery at gunpoint, have been happening frequently in traffic jams during commuting hours.	Traffic conditions are poor not only for commuting but also for economic activities, such as transportation of materials and products. Poor traffic conditions contribute to traffic jams, which are a big cause of crime on the road, such as robbery at gunpoint.
Electricity	● In Karachi, power supply is unstable and load shedding happen frequently. ● In a company whose business is power generation, if sales proceeds do not come in, fuel cannot be procured. This is one of the reasons why local electricity production is running at only 50 60% of the actual capacity. This low operating rate is attributable to the circular debt, which amounts to Rs400 billion.	Unstable power supply disrupts normal production. Stable electricity supply is required for stable production. Some companies utilize in-house power generating facilities for stable production, but their costs are higher than those of electricity from Karachi Export Processing Corporation (KESC), leading to increases in operation costs and reductions in profitability.
Gas	● The problem of gas depletion has not affected Sindh as badly as the other parts. ● Sindh produces 70% of the total gas production in the country. The Constitution of Pakistan secures the first right on gas of the Province of Sindh, stipulating that the province has "precedence over the other parts of Pakistan in meeting its requirements" from its own well heads.	Although gas depletion has not affected Sindh as badly as the other parts, it became a problem around 2005 and is becoming more serious over time in Sindh. There is concern that a shortage of gas supply disrupts normal production and leads to increases in costs and reductions in profitability.
Water	● Inadequate water supply is not such a serious problem, compared with electricity outages. In time of occasional water shortages, some companies purchase water from water tankers to maintain production.	Unstable water supply disrupts normal production. Stable water supply is required for production activity. Inadequate water supply leads to increases in costs and reductions in profits.

Source: JICA Study Team

Table 5.3.3: Living Environment

Category	Current Situation	Implications
Security	● Security is poor in Karachi. Recently general crimes, such as robbery at gunpoint, have been a more serious concern than terrorist threats. Crimes in Karachi have increased six times since 2005.	Security is one of the greatest hindrances to investment as pointed out in "Doing Business 2012" by the World Bank and also in the interview survey. The high incidence of crime is a major threat to both foreign and local employees. Interview respondents indicated that although they wanted to invite their business partners to Pakistan, some of them refused to come due to security grounds. Similarly, respondents ordered their employees to come to Karachi, but they refused due to security reasons. Some respondents hold meetings abroad for security purposes. Thus, the deterioration of law and order disturbs business activities. Improvement in security requires the Sindh Police to take the initiative in enhancing security measures. However, interviews revealed that many respondents had little or no confidence in the police due to not only the bribes demanded by them but also their tedious procedures and unproductive actions. It was reported by some respondents that even though the police witnessed crimes, they took no action. Another challenge faced by the police is political pressure. Respondents pointed out that the police did not take action against crimes involving political parties. One reason behind this is that some police officers were employed and connected with political parties. Rigorous enforcement of law and strict action against crime are urgently needed. However, the police are under budget constraints. A respondent provided an example: The police could not afford patrol vehicles and motorcycles and fuel, even if culprits were arrested. Police officers escorted culprits to the police station by motorcycle but paid for the fuel themselves. Some officers are not active in arresting culprits since they have to cover costs at their own expense. Thus, the Sind Police lack appropriate security measures despite the serious security problem in Karachi.
Commuting	● Various attempts to improve traffic conditions are being made, such as the Mehran Highway, Malir Expressway, and Karachi Circular Railway. ● Although road rehabilitation improved	Poor road conditions are a cause of traffic jams and muggings at gunpoint occur mostly during these jams. The incidence of highway robberies in Karachi, including the National Highway 05, one of the main commuting routes to KEPZ and the Bin Qasim Industrial Area, more than quadrupled over the last decade.

	traffic conditions, congestion especially during commuter rush hours remained a problem. There is still a need to further improve road conditions. ● Modes of commuting are a problem especially for local employees due to poor public transport. Some companies provide transport for their employees. The employees of other companies have no choice but to depend on private vehicles and public transport.	This rising street crime plays a part in worsening security mentioned above. Apart from poor road conditions, poor public transportation is one of the reasons for the frequent use of private vehicles and heavy traffic, contributing to crimes in jams. Improvement in traffic conditions requires the Sindh Police to take strict action against street crimes, rallies and protests on the road, and traffic offences, but appropriate action is not being taken due to lack of police officers' motivation caused by political pressure and discouragingly low pay.

Source: JICA Study Team

Table 5.3.4: FDI Promotion

Category	Current Situation	Implications
BOI functions	● In order to confirm the actual FDI activity in Karachi, the JICA Study Team visited several regulatory organizations. However, none of these organizations was able to provide useful data on FDI activity such as the number of firms, types of industries, manufactured items, and the number of employees.	If the Government of Pakistan wishes to invite foreign companies into Pakistan, basic data regarding FDI and the domestic industry are essential for them. Foreign investors usually consider the existing FDI activity before making an actual investment themselves, but relevant data are unavailable in Karachi. FDI promotion requires strong cooperation among the BOI Karachi Office, SBOI, and KEPZA, but it is weak. For example, SBOI finds projects to promote investment in Sindh, but their information is not shared with BOI and BOI cannot provide information about promising projects in Karachi for interested foreign companies. This causes losses of business opportunities and has negative effects on not only the Sindh government but also the Pakistani government. Apart from this, the BOI faces the problem of the insufficient number of qualified officials in its Karachi Office who can have dialogues with the private sector.
EPZA services	● EPZA is attempting to attract foreign companies with one-stop services. However, services provided for investors by the EPZA are insufficient. Companies in EPZA are having clearance problems.	Companies have to go through procedures for the export and import of raw materials and processed products. Each time companies make arrangements for tax exemption at customs offices. EPZA services are insufficient, compared with cases in other countries, and need to be improved.
Minimum size of investment in SEZ	● The SEZ Act was approved by the parliament in July 2012. Investors are not allowed to select a development site of less than 50 acres in the SEZ.	The SEZ Act does not benefit investment other than big investment of over 50 acres and does not give incentives to small investment of below 50 acres

Source: JICA Study Team

Policy Matrix for Investment Climate Improvement

Overall Outcome Goals:	Overall Outcome Indicators and Targets:
1. Personal income will be increased (GDP per capita: US$4000 in 2030). 2. Employment ratio will be increased. 3. A safer means of transportation for the Pakistani people will be developed. 4. A safe living environment will be created.	1. GDP growth rate will increase from 2.4% in 2010/11 to 5.5% in 2016 2. Unemployment ratio will be reduced by less than 10% from 13.1% in 2016 3. Adequate pollution control and traffic safety will be achieved. 4. Crimes will be reduced.

Table 5.4.1: PILLAR-1: Formulation of Import Policy

Outcome Goal	Outcome Indicator and Target
1. Long term industrial development policy will be formulated and issued by the government.	1. The production of new cars will be increased from 134,000 in 2011 to 350,000 in 2016.

Issue	Action (Input)			By Whom
	Short Term (2012/13-2013/14)	Mid-term (2014/15-2015/16)	Long Term (2016/17)	
1. Import duty on steel products was reduced from 10% to 5 %. 2. Import duty (max. 35%) on automotive parts is to be changed. 3. Under-invoicing of imported used cars and motorcycle parts is allowed 4. The import of used cars for commercial purposes is allowed.	➢ A Task Force for import policy will be formulated by MOI and MOCOM. ➢ Import of used cars will be studied through discussion between the public and private sectors. ➢ AIDP-2 will be drafted through discussion with the automobile industry. ➢ New import duty and regulations (non-tariff barriers) on the import of used cars will be submitted to ECC for approval.	➢ Import duty on automotive parts based on AIDP-2 will be implemented. ➢ New regulations (non-tariff barriers) on under-invoicing of imported used cars will be implemented. ➢ At the first stage of phased improvement in regulations on the import of used cars, the age of imported cars will be reduced to less than 3 years old.	➢ At the second stage, legislation will be enacted to prohibit the import of used cars for commercial purpose ➢ The implementation of AIDP-2 will be reviewed and revised, if necessary.	MOI (*) MOCOM EDB

Source: JICA Study Team

Note: MOI: Ministry of Industry, (*): Responsible organization, MOCOM: Ministry of Commerce, EDB: Engineering Development Board, ECC: Economic Coordination Committee.

Table 5.4.2: PILLAR-2: Consolidation of Environment Friendly and Safe Transport System

Outcome Goal	Outcome Indicator and Target
1. The vehicle inspection system will be improved. 2. Emission control will be enforced.	1. Vehicle inspection facilities and emission control testing equipment will be installed in Karachi.

Issue	Action (Input)			By Whom
	Short Term (2012/13-2013/14)	Mid-term (2014/15-2015/16)	Long Term (2016/17)	
1. The existing law (Motor Vehicle Rules 1969) is not complied with. 2. There is no emission control testing equipment for Euro-2. 3. The vehicle fitness system is not functioning.	➢ A legal system relating to vehicle fitness certification will be developed to apply inspection to passenger cars. ➢ Safety standards enforced through inspection with testing equipment instead of visual inspection will be established. ➢ Guidance sessions for safe transportation will be conducted for GOS. ➢ Overseas training for concerned officials will be conducted to introduce safe transportation and measures for Euro-2.	➢ Road traffic laws and ordinances will be partially enforced by GOS. ➢ Guidance sessions for safe transportation will be conducted by GOS. ➢ Pilot emission control facilities complying with Euro-2 environmental standards will be developed, ➢ Overseas training for concerned officials will be conducted to introduce safe transportation and measures for Euro-2.	➢ Road traffic administration system by local government will be improved, ➢ Emission control testing equipment for Euro-2 will be installed at PSQCA, PTA, etc. ➢ Pilot vehicle inspection facilities with testing equipment will be established in Karachi. ➢ Awareness campaigns about the necessity of vehicle inspections and emission control will be carried out for drivers and vehicle owners.	MOC (*) MOE (*) PTA PAKEPA GOS SP PSQCA

Source: JICA Study Team

Note: MOC: Ministry of Communication, (*) Responsible Organization, MOE: Ministry of Environment, PTA: Provincial Transport Authority, PAKEPA: Pakistan Environmental Protection Agency, GOS: Government of Sindh, SP: Sindh Police, PSQCA: Pakistan Standard & Quality Control Authority.

Table 5.4.3: PILLAR-3: Human Resource Development in the Automotive Industry

<table>
<tr><th colspan="3">Outcome Goal</th><th colspan="3">Outcome Indicator and Target</th></tr>
<tr><td colspan="3">1. The automotive parts procurement ratio will be increased by OEMs (assemblers).</td><td colspan="3">1. Domestic parts procurement ratio will increase from 50% in 2011/12 to 70% in 2016/17.</td></tr>
<tr><th rowspan="2">Issue</th><th colspan="4">Action (Input)</th><th rowspan="2">By Whom</th></tr>
<tr><th>Short Term (2012/13-2013/14)</th><th colspan="2">Mid-term (2014/15-2015/16)</th><th>Long Term (2016/17)</th></tr>
<tr><td>1. Local manufacturers are unable to supply the qualified parts by designated deadlines.
2. Car production costs increase due to procurement of automotive parts from overseas.
3. Local automotive parts manufacturers cannot survive due to lack of international competitiveness.</td><td>➢ Obstacles to AIDP-I implementation will be discussed and overcome by EDB, PAMA, and PAAPAM for the certain implementation of AIDP-II.
➢ Periodical technical guidance will be given the local automotive industry by SMEDA experts.
➢ Local trainers will be upgraded under the guidance of SMEDA experts at technical training centers.
➢ Overseas technical guidance will be promoted to acquire new technology (dies and molds).</td><td colspan="2">➢ Periodical technical guidance will be given to the local automotive industry by SMEDA experts.
➢ Local trainers will be upgraded under the guidance of SMEDA experts at technical training centers.
➢ Overseas technical guidance will be promoted to acquire new technology
➢ High-technology equipment will be installed at automotive technical centers.</td><td>➢ Staff training for the automotive industry will be conducted by local trainers of SMEDA.
➢ The implementation of AIDP-II will be reviewed and a new program will be drafted.</td><td>MOI (*)
EDB
SMEDA
KTDMC
AT&TC
PSQCA</td></tr>
</table>

Source: JICA Study Team

Note: MOI: Ministry of Industry, (*): Responsible Organization, EDB: Engineering Development Board, SMEDA: Small and Medium Enterprise Development Agency, KTDMC: Karachi Tools Dies & Molds Centre, AT&TC: Automotive Testing & Training Center, PSQCA: Pakistan Standard & Quality Control Authority.

Table 5.4.4: PILLAR-4: Establishing Safe Commuting

Outcome Goal	Outcome Indicators and Target
1. Safe commuting between residences and workplaces will be enabled.	1. Crimes in Karachi will be eradicated.

Issue	Action (Input)			By Whom
	Short term (2012/13-2013/14)	Mid-term (2014/15-2015/16)	Long Term (2016/17)	
1. Congestion and crime at gunpoint during traffic jams are common. 2. There is lack of a security system and strict action.	➢ An outline of a security system (CCTV camera monitoring and check posts) will be drafted by SP. ➢ Contractors and suppliers will be selected by tender. ➢ A detailed security inspection plan after the introduction of the securing system will be drafted by SP.	➢ A CCTV camera monitoring system and check posts will be established along main commuting routes such as N-5. ➢ Additional police motorcycles for security control of main commuting routes such as N-5 will be introduced. ➢ Overseas training of 10-20 police officers will be conducted. ➢ Public announcements of an increase in police patrols will be made as psychological operations to reduce crime.	➢ Check posts along main commuting routes such as N-5 will be established. ➢ The patrolling system will be reviewed and reinforced by SP. ➢ Overseas training of 10-20 police officers will be conducted. ➢ Public announcements of an increase in police patrols will be made as psychological operations to reduce crime.	GOS (*) KMC SP

Source: JICA Study Team
Note: GOS: Government of Sindh, (*): Responsible Organization, KMC: Karachi Metropolitan Corporation, SP: Sindh Police.

Table 5.4.5: PILLAR-5: Capacity Development of One-Stop Services for FDI Promotion

Outcome Goal	Outcome Indicator and Target
1. FDI will increase on an annual basis.	1. FDI will increase from US$1.7 billion in 2010/11 to more than US$6 billion in 2016/17.

Issue	Action (Input)			By Whom
	Short Term (2012/13-2013/14)	Mid-term (2014/15-2015/16)	Long Term (2016/17)	
1. The facilitation functions of BOI among related organizations mandated by the government are inadequate. 2. The number of qualified officials in the BOI Karachi Office is inadequate. 3. The one-stop service functions of EPZA need to be strengthened. 4. The investor side is not able to select less than 50 acres in the development site of the SEZ.	➢ A Task Force will be created and be comprised of representatives from related organizations (BOI, FBR, MOCOM, MOI, EDB, EPZA, and SBOI) to strengthen FDI promotion. ➢ The reinforcement of one-stop service functions will be studied by the Task Force and submitted to the related organizations for approval. ➢ Five new appropriately qualified officials will be allocated to the BOI Karachi Office. ➢ The SEZ Act will be revised so that a system to give special approval to land of even below 50 acres with a certain amount of investment as SEZ with ECC's approval can be developed.	➢ Task Force meetings will be held quarterly for improvement in FDI promotion functions. ➢ BOI's service function to assist foreign companies in permitting processes such as corporate registration will be strengthened. ➢ An amendment to regulations to reinforce EPZA's one-stop service function will be submitted to ECC for approval.	➢ Task Force meetings will be held quarterly for improvement in FDI promotion functions. ➢ BOI's service function to support companies will be reviewed by the Task Force in consultation with industrial associations. ➢ One-stop service functions will be reviewed by the Task Force and reported to the related organizations.	BOI (*) FBR MOCOM MOI EDB EPZA SBOI

Source: JICA Study Team

Note: BOI: Board of Investment, (*): Responsible Organization, MOCOM: Ministry of Commerce, MOI: Ministry of Industry, EDB: Engineering Development Board, EPZA: Export Processing Zone, SBOI: Sindh Board of Investment, SEZ: Special Economic Zone, ECC Economic Coordination Committee.

Chapter 2 Needs of Economic Development and Karachi Development Potentials

2.1 Introduction

The objective of the discussion in this chapter is to situate the past with present and connect the present strategies to a foreseeable and better outcome in the future. In this regard, the first part of the chapter focuses on economic growth, structural transformation, development in trade, and technological capability of the manufacturing sector in Pakistan.

The second part of the chapter takes a briefing on various concept papers that outlines the future long-term strategy of economic development and growth in Pakistan, which include Vision-2030, Pakistan's New Growth Strategy, and Karachi Vitalization Scenario, etc. The focuses of the first two documents are economic growth and development, and industrial development in Pakistan; while the third one is specific to Karachi. The latter section also provides a brief background on the importance of the city of Karachi being one of the most important cities in the world in terms of its population, economic potential and geo-strategic location, contributing significantly to the growth engine of the national economy.

2.2 Economic Growth of Pakistan

2.2.1 Economic Structural Transformation

Since its independence in 1947, the Pakistani economy has grown with fluctuations. Table 2.2.1 gives the average real growth rates of output at aggregate and sectorial level in the period of 1951-2011. In the last sixty years, Pakistan has maintained an average growth rate of more than 5% per annum. This growth rate has been attributed to a conscious effort of the government and policy makers on industrial and commercial sector development. However, despite being an agrarian economy, agriculture output growth has been around 3.7% per annum, on the average.

Table 2.2.1: Real Growth Rates of Sectorial Output in Pakistan

(%, Annual average)

SECTOR	1971-80	1981-90	1991-00	2001-11
Aggregate	4.58	5.90	6.22	4.45
Agriculture	3.01	4.00	6.20	2.80
Mining & Quarrying	9.86	3.58	17.85	4.51
Manufacturing	4.56	6.72	4.51	6.61
Utilities	8.57	8.10	9.50	-1.38
Construction	7.46	3.05	0.80	2.46
Retail Trade	4.25	7.52	6.50	4.83
Transport	5.10	7.00	9.70	5.43
Finance	5.66	7.78	5.40	3.81
Services	6.18	6.26	5.36	5.10

Source: JICA Study Team' calculation based on Government of Pakistan, "Economic Survey" various issues

Table 2.2.2 highlights a decade-wise analysis of the structural transformation by sector. Apart from aggregate and sectorial growth rate, there has been a structural shift from traditional to modern sector. The agriculture sector was the main productive sector, contributing 37% of the gross domestic product (GDP) in 1970. However, with the passage of time, non-agricultural sectors have grown more than the agriculture sector, as shown in Table 2.2.2. This resulted in the reduction of agriculture sector's share in GDP to 21% in 2011. The manufacturing sector has increased its share from about 16% in 1970 to more than 18% in 2011. Given the economic transition away from the agriculture sector to the manufacturing and services sectors, the manufacturing sector needs to grow to absorb redundant labor force. However, the manufacturing sector has remained stagnant while other sectors have increased their share in the gross domestic output. There has been an overall increase in the share of services sectors including retail trade in GDP.

Table 2.2.2: Sectorial Share in GDP (%)

SECTOR	1970	1980	1990	2000	2011
Aggregate	100.00	100.00	100.00	100.00	100.00
Agriculture	36.83	29.60	26.00	26.17	21.20
Mining & Quarrying	0.53	1.06	0.71	1.37	2.40
Manufacturing	16.10	15.84	17.41	14.81	18.70
Utilities	1.52	2.28	2.83	3.96	2.30
Construction	4.20	5.66	4.22	2.50	2.10
Retail Trade	14.94	16.01	17.00	17.62	17.10
Transport	6.80	7.36	8.00	11.36	9.90
Finance	5.50	5.94	7.31	6.90	7.40
Services	13.62	16.27	16.58	15.35	19.00

Source: JICA Study Team' calculation based on Government of Pakistan, "Economic Survey" various issues

2.3 Need for Sustainable Economic Development

2.3.1 Pakistan in the 21st Century: Vision 2030

In order to overcome the deficiencies confronted in the five year plan, in 2007, the National Economic Council (NEC) approved a document entitled "Vision 2030". The document was formulated by PC based on an approach paper entitled "Strategic Directions to Achieve Vision 2030". This document was prepared by the PC and approved by the NEC in February 2006. The document is relatively long-term, and would take a span of 25 years to design and implement the strategy for economic growth and development of Pakistan.

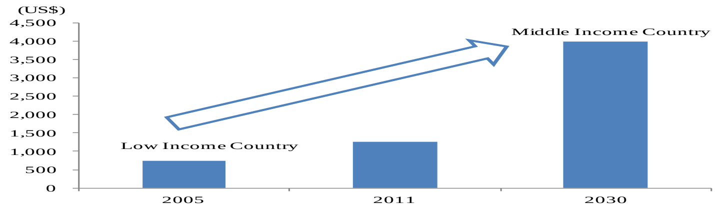
The Vision 2030 envisaged "a developed, industrialized, just, and prosperous Pakistan, through rapid and sustainable development in a resource constrained economy by deploying knowledge inputs".

The presentation of such vision statement is not limited to Pakistan as the long-term development scenario of the country. Malaysia, for instance, also has Vision 2020, which was presented by the former Prime Minister.

2.3.2 Quantitative Targets

The vision statement projected that a 7-8% growth rate per annum will contribute to an increase in the per-capita GDP of Pakistan from US$742 in 2005 to US$4000 in 2030 (refer to Figure 2.3.1). Should this projection materialize, Pakistan will ascend from its position as a low-income country and join the ranks of the middle-income countries.

The annual GDP growth rate of the country was 5.5% on average for five decades from 1961 to 2010. In order to achieve these quantitative targets, the annual growth rate needs to be increased further by more than 1.5-2.5% from this long-term trend of GDP growth. Considering the wide swings in the GDP growth rates during the period, the target growth rate seems considerably challenging for the administrations.



Source: JICA Study Team based on Planning Commission, "Vision 2030"

Figure 2.3.1: Development Target of GDP per Capita in 2030

The document comprises an introductory chapter and ten substantive chapters which, are listed below:

- Global Imperatives: Challenges and Opportunities
- The Basic Goal: A Just and Sustainable Society
- The Institutions of State and Government
- Realizing Vision 2030: The Macroeconomic Framework
- Agriculture Growth: Food, Water, and Land
- Manufacturing and Industry
- Building the Innovative Society: Knowledge, Technology, and Competition
- Energy for Growth
- Rural and Urban Development
- The State and Security

The President of Pakistan at that time, described Vision 2030 as "an important milestone" and commended it for presenting "a clear picture of emerging and expected challenges" pertaining to water, energy, infrastructure, climate change, and world trade and markets. As noted by the Prime Minister at that time, Vision 2030 was aimed at sustaining GDP growth at "around 7-8% per annum, which will enable Pakistan to join the ranks of middle-income countries in 2030, with a per capita income of around US$4000 at 2007 prices".

In sectorial terms, agriculture will be an efficient provider of food and nutrition. The economy is expected to be dominated by high-end manufacturing and services, with an increasing base of knowledge, technology, and skills serving as the tool for achieving the change and target.

Emphasis is also placed on manufacturing and industry to play its role. Vision 2030 envisages the share of the manufacturing sector to change the current 18.3% of GDP to nearly 30% (or US$300 billion in current terms) by the end of the vision period. In order to attain this target, the manufacturing sector will need to grow at a sustained average growth of around 10%. The manufacturing industry needs to grow by 10% every year from 2006 to 2030 in order to reach the target of 30% share in GDP. Considering the fact that the average annual growth rate of manufacturing industry from 1961 to 2000 was 7.1%, the target of 10% growth rate seems very ambitious and challenging.

Table 2.3.1: Growth Rates of GDP and Sectorial GDP in Pakistan

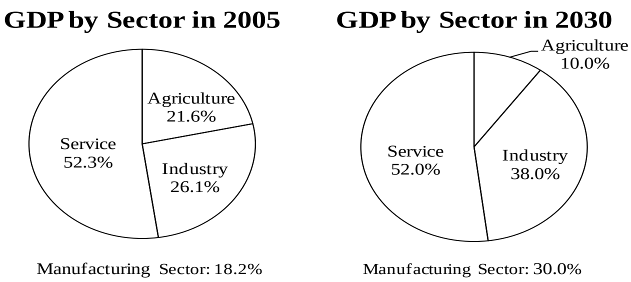
Period	GDP (%)	Agriculture (%)	Manufacturing (%)	Service (%)
1961-2000	5.7	4.3	7.1	6.1
2000-2010	4.8	3.2	7.0	5.3

Source: Economic Survey of Pakistan, Statistical Supplement 2010/11

However, to meet this ambitious target, Pakistan has to take serious efforts in terms of necessary human, technical, legal, and physical infrastructure to put them in place. These are the instruments needed for matching trans-national skills so that investments and possible relocation of manufacturing and design from developed economies can be facilitated accordingly. While excellence of public institutions and stability of macroeconomic policies are basic requirements, the driving force will remain flexible, skilled, and innovative technical personnel with fast and efficient physical and electronic connectivity. Pakistan has to make important strategic choices to ensure sustainable growth in the manufacturing sector in a rapidly changing and international competitive environment.

The country has never been able to achieve an average of 6% GDP growth rate for a sustained period, nor its manufacturing sector has ever averaged a growth approaching to 7% with some exceptions. When the present recession is over, if Pakistan is to achieve this target, Pakistan will have to maintain a real GDP growth of 8% and population growth of around 1.4%, on an average annual basis.

In order to embark on a long-term sustainable growth path, Pakistan's economy will have to go through significant structural changes. In terms of GDP share by sector, the value added goods generated by the agricultural, industrial (manufacturing), and service sectors, currently stand at 21.6%, 26.1% (18.2% for manufacturing), and 52.3%, respectively. If Pakistan is to achieve its "Vision 2030" targets, then over time these shares will have to change to 10%, 38% (30% for manufacturing), and 52%, respectively, in fiscal year 2030. This will mean that there will be pronounced growth in the industrial sector, and especially in manufacturing, which, along with the service sector, will contribute substantially to GDP growth as shown in Figure 2.3.2. Concurrently, the share of agriculture in GDP will decline. To achieve these projections, Pakistan's manufacturing sector must register an annual average growth close to 10% in the value added goods it produces.



Source: Planning Commission, "Vision 2030"

Figure 2.3.2: Development Target by Sector in 2030

Table B1 in Appendix B provides projected estimates of real GDP along with output of agriculture, services, industry and manufacturing sector, for the period 2006-2030. These estimates are based on the Vision 2030 targeted estimates of 8% per annum real GDP growth rate, while agriculture, services, industry and manufacturing sector's growth rates are 4.5%, 8%, 9.7%, and 10%, respectively. It is estimated that if economic policies are continued according to Vision 2030 strategy, then in 2030, agriculture sector's share will be reduced to 10% of GDP, while manufacturing sector's share will be increased to 30% of GDP. The services sector's share will remain stagnant, at 52% of GDP.

Furthermore, the Vision 2030 advocates for diversification of industries, encouragement and development of small- and medium-enterprises, acquisition of technological capability and productivity increase are contributory factors for high economic growth. In addition to this, the development of human resources and creation of knowledge based society through high standard of education and training which will enable an environment of information and communication technology infrastructure are expected to yield sustained economic development.

The Vision 2030 agenda’s targets also require massive structural changes rather than marginal change, a shift in the production paradigm to technology and knowledge based industrialization with focus on the quantitative and qualitative growth of an integrated and competitive industry in the private sector. The inefficiencies of import substitution will be reduced through tariff rationalization and export led strategy. The lack of diversification in Pakistan’s manufacturing sector has been due to heavy protection granted to resource based industries, high rates of import duties on raw materials used in the machinery, equipment, and chemical industries, and zero or low rates of import duties on finished and semi-finished goods relating to these sectors. This is further compounded by widespread smuggling of all consumer durables. Many of these issues have been resolved to some extent through tariff rationalization in the last few years, but further fine tuning is needed to encourage investments in manufacturing.

The vision for manufacturing aims to strengthen present industrial activity and enhance its output and productivity, so that it can become competitive, flexible, and agile. While investment flows to increase capacity and technology at the original equipment manufacturer (OEM) level are being encouraged, local design capability is also being enhanced through new clusters for training, design, and testing, which will drive medium technology activities such as automobiles petrochemicals, as well as high technology sectors in electronics and pharmaceuticals. The construction industry is also enjoying robust growth with major demand for cement and steel. There has been a doubling of demand and capacity for cement in the last five years, fertilizers composition has changed but fertilizer production has not changed much over the last few years.

As a result of incentives and policies, the range of manufacturing activities is expanding with new activities (pioneering industries which would include new products, processes or technologies) in electronics, software, petrochemicals, fertilizers, chemicals, steel, and shipbuilding, among others. Secondly, the human and technical infrastructure for exploitation of natural products, and biotechnology design tools are being established. These building blocks are essential to meet the targets of Vision 2030.[6]

Recognizing the rural and urban dimensions, the role of cities as engine of growth, the Vision 2030 envisages that better human lives, workplaces, education, skills, trade, and competition would result into demographic dividends, in turn, transforming urban areas into knowledge society. While rural areas will have an increase in productivity through efficient, competitive, and sustainable agriculture.

[6] Planning Commission of Pakistan, “Vision 2030”, (August 2007)

Significantly from the angle of sustainability, the energy has its role in the development process. The efficient use of energy along with a mix of variety of sources of energy, including clean sources such as hydropower with a view to limiting the increase in the country's greenhouse gas emissions, will need to be expedited in order to have cost efficient production activity and better livelihood.

The Vision 2030 will be implemented through a five-year development framework. The Vision document was stated to be reviewed in 2015.

2.3.3 Pakistan's Framework for Economic Growth

In continuation to high growth and development objectives, the National Economic Council on May 28, 2011 approved a document titled "Framework for Economic Growth (FEG)", prepared by the Planning Commission (PC) with the help of a team of Pakistani officials and experts led by the Deputy Chairman of the PC. The document was approved on the basis of extensive consultations with external experts, Pakistani academia, civil society organizations, development partners, including the United Nations (UN) agencies, funds and programs, provincial governments, and parliamentarians.

The document is the most recent policy guideline, meant to guide the federal and provincial governments in elaborating their development plans. Based on the slogan of "Reform is a continuing process and it needs to be institutionalized", the approach paper pointed out the result based management for effective and efficient implementation of Pakistan's new growth strategy by taking stakeholders on board from public and private sectors. Unlike in the past, the emphasis is to link clearly the achievement of long-term goals and targets.

The Government of Pakistan recognizes that the economy has performed well below its potential and requires an annual average growth rate of 7% to absorb the youth labor growth. It has therefore formulated FEG. The FEG advocates for sustained growth by addressing the two main constraints of growth:

(i) Inadequate market development, caused by lack of competition, policy distortions, entry barriers, and poor regulation.
(ii) Inefficient public sector management, especially in the provision of core public goods such as security of life, property, transactions, and contracts, and in the accumulation of human and physical capital.

The FEG encourages a joint government and private sector effort to increase productivity by tackling noncompetitive markets, poor governance, limited urban development, inadequate education, low openness, and limited innovation due to limited research. It also acknowledges the role that provincial governments will play following the 18th amendment of the Constitution.

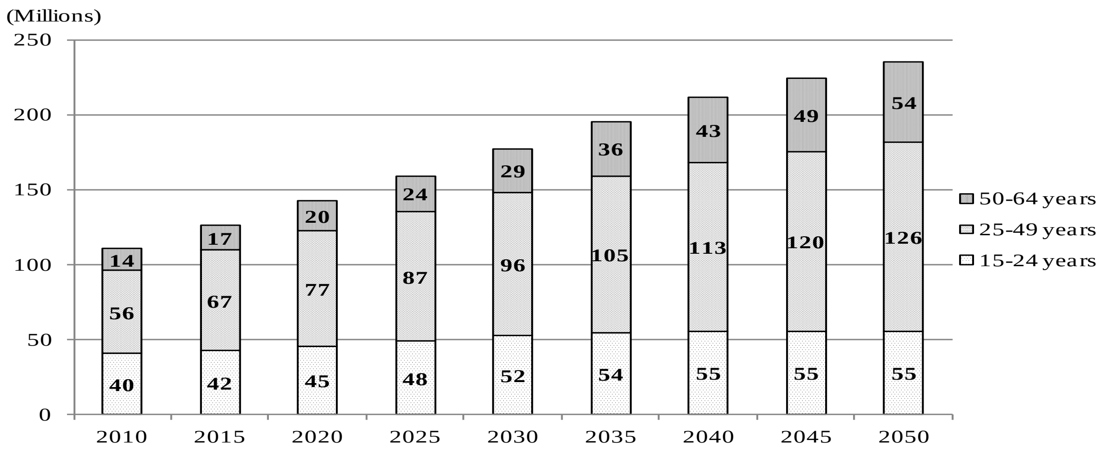
An approach paper pointed out the backdrop of the formidable challenges faced since its independence. Pakistan has made a remarkable transition from being a producer of agricultural raw materials to semi-industrialized economy. Per capita income has gone up more than tenfolds and the living standards of the majority of its burgeoning population compared favorably with other South Asian and Third World countries.[7]

One of the key socio-economic areas highlighted in the document is the unemployment rate in

[7]UNCSD, Stocktaking Report on Sustainable Development in Pakistan, (June 2012)

Pakistan while the others are education and health standards. Pakistan occupied the 143rd position out of 200 countries and has the third highest employment rate in South Asia (after Nepal and Maldives).[8] This is specifically applicable in the case of women who constituted 48% of the population but only occupied 22% of the jobs. The report highlighted the demographic challenges by a five and a half fold increase in population since its independence. According to the document, nearly 50% of the population is below 20 years of age and over 60% below 30 years. In the backdrop of current growing unemployment, there are likely chances of disconnection between the youth and economy. Thus, youths of Pakistan are vulnerable to the blandishments of extremists.

The population of Pakistan is projected to reach over 350 million in 2050.[9] More than the size of the population, the major concern is the age structure, as the number of working age group and elderly will continue to increase significantly after 2035. According to the growth paper, more than 236 million people will be in the working age group by year 2050, reflecting proportion of 67.5% of the total population. While on the other hand the dependency ratio (younger dependency ration) will be lower. Figure 2.3.3 below, shows the trends of dominating the population by youth in the country will continue for the next 30-35 years. This entails the need of economic development for sustainable GDP growth to avoid any anarchy.



Source: Planning Commission - Framework for Economic Growth – Pakistan 2011

Figure 2.3.3: Projected Labor Force Size and its Composition

The approach paper also discussed the social life of common man, lack of security of life and assets, and disruption of normal life in the wake of the deteriorated law and order situation. The sustainable development in the country is also linked to the proper and appropriate implementation of rule of law throughout the country.

The Ministry of Industries and Production estimated excess capacity in the manufacturing sector in 2009-10 at 51%. It attributes the under-utilization of capacity to constrained energy sector, the high cost of production and depressed external demand. The problems with the energy sector are particularly significant and are taking a toll on manufacturing sector productivity. The total manufacturing sector losses because of the energy shortfall are estimated at 2.5% of GDP.

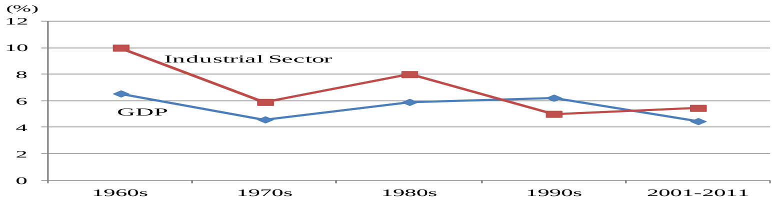
[8]Ibid
[9]Planning Commission, Framework for Economic Growth– Pakistan,(2011)

It must be argued here that Pakistan's industrial sector is still far from open. The liberalization of trade and investment regimes allow for new ideas and creative opportunities besides ensuring a substantial consumer surplus across the board. There is an urgent need to revisit the role of entities responsible for reducing tariff and nontariff barriers.

2.4 Need for Industrial Sector Development

2.4.1 Trend of Industrial Sectors Growth

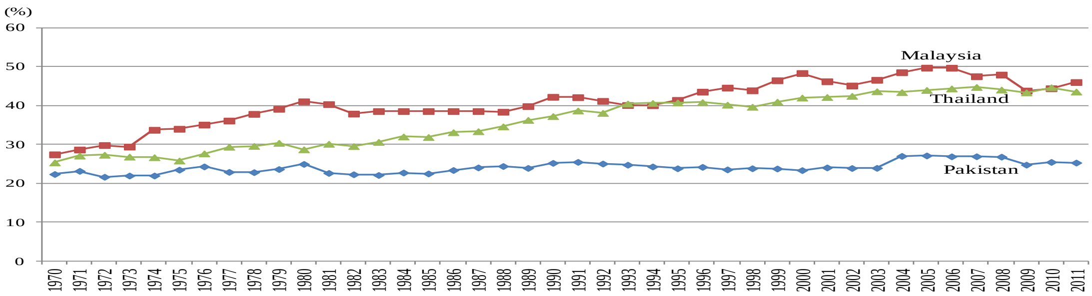
Figure 2.4.1 shows the growth rates of Pakistani industrial sectors since 1960. The growth rate reflects considerable fluctuations year after year. In the period of 1960 and 1980, the country achieved high growth rates, however, the rate dropped in 1970 and 2001. The fluctuation hampered the sustainable growth of the country. Up to the 1990s, the growth rate of GDP showed a similar trend as that of industrial sector. The growth rate of the industrial sector showed high trend after 2000.



Source: Government of Pakistan, Economic Survey 2011/12

Figure 2.4.1: Average Growth Rates of Pakistan's GDP and Industrial Sector

Comparing with other countries in the region, it is also difficult to say that Pakistan's industrial sector have achieved sustainable growth as observed with other Asian countries such as Malaysia and Thailand. Figure 2.4.2 compares the Pakistan's rate of industrial value added to GDP with those of Malaysia and Thailand, Asian countries successful in industrial development. In the beginning of the 1970s, the rates of all the three countries were in the range of 20% to 30%. However, Malaysia increased the rate from 27.4% to almost 50% from 1970 to 2006, and 25.3% to 44.3% in the case of Thailand. On the other hand, Pakistan increased the rate slightly from 22.3% to 26.9 % in the same period. This means that the Pakistan economy could not achieve sustainable growth during the period.

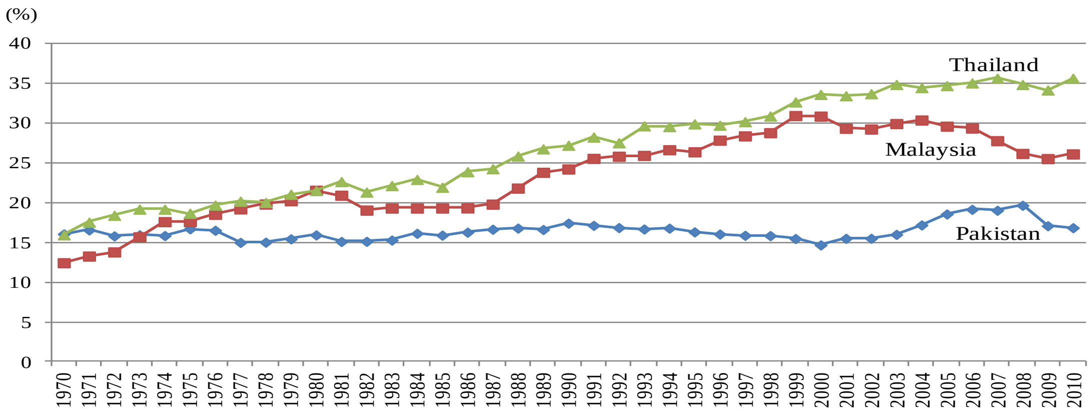


Source: World Bank, World Development Indicators

Figure 2.4.2: Shares of Industry in GDP in Pakistan, Malaysia, and Thailand

2.4.2 Important Role of Manufacturing Sector for Economic Development

Same with the industrial sector, similar trends were observed for the manufacturing value added to GDP while comparing with other Asian countries. Figure 2.4.3, exhibits the trends of manufacturing value added to GDP of Pakistan, Malaysia, and Thailand. The share of manufacturing in Pakistan's GDP revealed a meager improvement during the period from 1970 to 2010 with wide fluctuation. The share of GDP in 1970 was at around 16.1% in 1970 and increased to over 19% in 2006, however went back to 16.8% in 2010. Whereas, the manufacturing value added to GDP in Malaysia increased from 12.4% in 1970 to almost 30% in 2006, and stood at 26.1% in 2010. In the case of Thailand, the manufacturing value added to GDP increased from about 16% to 35.6% from 1970 to 2010.



Source: World Bank, World Development Indicators

Figure 2.4.3: Shares of Manufacturing in GDP in Pakistan, Malaysia, and Thailand

Currently, Pakistan's manufacturing industry is internationally competitive in low-tech products which are in general, low value added agricultural based products such as textile and food. This is clearly reflected from the composition of exports, where low-tech products accounted for over 70% of the country's export. Thus, a whole share of Pakistan's export remains stagnant with a meager increase during the last three decades. This is mainly due to the increasing share of medium to high-tech exports in the world market over the last years. The important thing that needs to be noticed is that the share of industrial sector has remained the same in the past several decades.

Table 2.4.1 shows that traditional products such as food and textile still dominate the industrial sector in Pakistan. Food and fiber system that consists of food including tobacco and textile is the main industry and its share did not change so much from 53.5% to 50.8% in the past two decades from 1981/82 to 1999/2000. The share is still dominant in the whole industrial sector. However, there is a little increase in the share of machinery and transport equipment and chemicals, which are rather relatively high value-added products as compared to food, beverages, and tobacco, and textile and clothing. While comparing with other Asian countries such as Malaysia and Thailand, there is a considerable shift from low-tech to high-tech products. This shift is more prominent in Malaysia. Its industrial structure shifted from food, beverages, and tobacco in 1981/82 to machinery and transport equipment in 1999/2000.

Table 2.4.1: Composition of Manufacturing Sectors (% of Value Added)

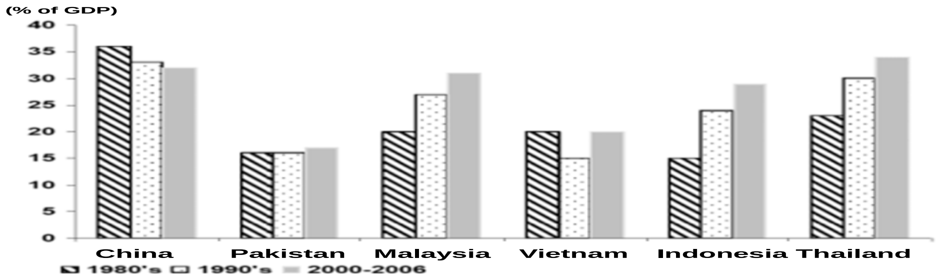
Sectors	Pakistan		Malaysia		Thailand	
	1981/82	1999/2000*	1981/82	1999/2000	1981/82	1999/2000
Food, Beverages and Tobacco	34.0	22.9	23.1	8.0	55.4	25.5
Textile and Clothing	19.5	27.9	5.9	4.1	7.7	17.0
Machinery and Transport Equipment	7.2	8.5	22.7	41.5	9.2	9.8
Chemicals	12.0	15.5	5.6	7.9	6.8	9.8
Other Manufacturing	27.3	25.2	42.8	38.6	21.0	40.1
Total	**100**	**100**	**100**	**100**	**100**	**100**

* Average of 90s
Source: JICA Study Team's calculations based on data from World Development Indicators.

It may be noted that group of industry, which procures the majority of raw materials from the domestic market, accounted for more than half of the total industrial value-added. However, the share has decreased year after year. On the other hand, the share of the chemical industry increased from 12% in 1981/82 to over 15% in 1999/2000. The chemical industry which includes pharmaceutical products would be new rival against the food and fiber system.

Figure 2.4.4 provide manufacturing output share in GDP of selected countries during the 1980s, 1990s, and from 2000 to 2008. Pakistan's manufacturing sector's share in GDP has remained stagnant as well as least among all selected countries in last three decades.

Unlike other countries, particularly in East Asia, Pakistan's manufacturing is still dominated by products at the lower end of the technology spectrum, and the share of high-tech products was low at about 5%. This implied that Pakistan's manufacturing sector is significantly smaller than that of the successful Southeast Asian countries, and that it needs substantial product upgrading.



Source: World Bank, World Development Indicators, April 2008

Figure 2.4.4: Manufacturing Output Share

2.4.3 External Trade Performance

(1) Trade Transformation from Primary to Value Addition

Table 2.4.2 presents a decomposed classification of imports and exports. Figures are shares of standard classified aggregates in total value. Numbers in the table provided some insight in the transformation process of the country. During the early periods of independence, the economic structure of Pakistan was heavily dependent on foreign trade. A large part of imports consisted of consumer goods while more than 99% of the exports were primary commodities. This trend has changed in the last sixty years.

In the case of imports, capital goods and industrial raw materials for capital goods constituted about 61% in 1970, which has fallen to around 31% in total in 2011. There has been a sustained decline in the industrial raw material for capital goods from 11% in 1970 to 7% in 2011. On one hand, capital goods share a decline from 50% in 1970 to 24% in 2011. On the other hand, a share of raw materials for consumer goods and finished goods has increased. At the export front, there has been a switch over from primary and semi-manufactured goods exports to manufactured exports. There is a steep decline in the share of primary commodities, while for semi-manufactured goods have fluctuations over the period of time. However, the share of manufactured items has increased from 44% in 1970 to 69% in 2011.

Table 2.4.2: Economic Classification of Imports and Exports in Pakistan

Classification	Share in Total Trade (%)				
	1970	1980	1990	2000	2011
IMPORTS	100.0	100.0	100.0	100.0	100.0
Consumer Goods	10.0	16.0	19.0	14.0	16.0
Capital Goods	50.0	36.0	33.0	33.0	24.0
Industrial Raw Material for					
a. Capital Goods	11.0	6.0	7.0	7.0	7.0
b. Consumer Goods	29.0	42.0	41.0	54.0	53.0
EXPORTS	100.0	100.0	100.0	100.0	100.0
Primary Commodities	33.0	42.0	20.0	12.0	18.0
Semi-Manufactured	23.0	15.0	24.0	15.0	13.0
Manufactured	44.0	43.0	56.0	73.0	69.0

Source: Government of Pakistan, Economic Survey, 1997-98.

At the export front, Pakistan's export performance lags behind among neighboring as well as newly industrialized countries. Its exports per capita were very low at about US$110. The main reason for weak export performance was the narrow base of export which was largely cotton dependent. The question is whether countries like Pakistan can move up to the development ladder. Empirical evidence showed that countries must have mastered the production of a relatively wide and diversified range of other products to be able to manufacture advanced products. This learning process provides them with the necessary capabilities (e.g., production knowledge). Findings suggested that economic diversification should be at the center of their development strategy.

Pakistani manufacturing industry is internationally competitive in low-tech and generally low value added products such as textile and food as clearly shown in the composition of exports of the country. Whereas, the share of medium and high-tech products in world exports have been continuously increasing over the last decade. One of the key examples of such high-tech products is the automobile, which has large share in the world export today. The share of Pakistani export in the world export remained low at 0.2% and the expansion of the Pakistani share in the world export remained modest. Concerning the composition of exports, low-tech products such as textile consisted of over 50%[10] of the total Pakistani export. Pakistan's export sector performance has been relatively weak, especially recently. Its share of world export

[10] Author's Calculation, "Economic Survey of Pakistan" 2010-11

volume has been trending down since the mid-1980s, with a significant decline in 2007 amid the crisis. In nominal terms, Pakistan's share of world exports has been relatively stable since 2007, helped by the recovery in cotton prices.[11]

The speed at which countries can transform their productive structure and upgrade their exports depends on the path determined by their current production and export structures. For instance, Malaysia shifted its product structure from textiles in 1985 to electronics in 2000, and it started producing more sophisticated products. Pakistan's production structure on the other hand remained almost the same in 2000 as in 1985; it continued to concentrate on low productivity garments and textiles, and cereals. Although some industries like industrial chemicals, non-metallic products, electrical machinery have increased their share in total manufacturing output, other high value added and hi-tech industries remained stagnant. As a result, the country failed to add value to its industrial sector.

(2) Trade Policies of Pakistan 2000-11

Pakistan had a long history of inward-oriented import substitution policies, protecting domestic industry; however trends have been changed significantly with the liberalization of trade regimes by tariff cuts. Trade reforms in Pakistan started in late 1980s with the process of privatization, economic liberalization, and de-regulation in the country. These reforms were further intensified when World Trade Organization (WTO) came into existence and Pakistan being a WTO member was obliged to adopt and follow the rules and agreements. Furthermore, IMF programs in 2000-2004 geared the trade reform process. Trade reforms were deeply rooted and wide-ranging, having a significant bearing on the economy.

The Vision 2030 aims to turn Pakistan into a middle-income country in 2030 through rapid and sustainable development by, *inter alia*, deploying knowledge-intensive import items. Overall, trade policy has been focused on reducing protection, achieving a more outward-oriented trade regime, obtaining better market access for Pakistan's exports, and promoting greater integration into the global economy through increased economic efficiency, and thus international competitiveness, which would contribute to export-led growth.

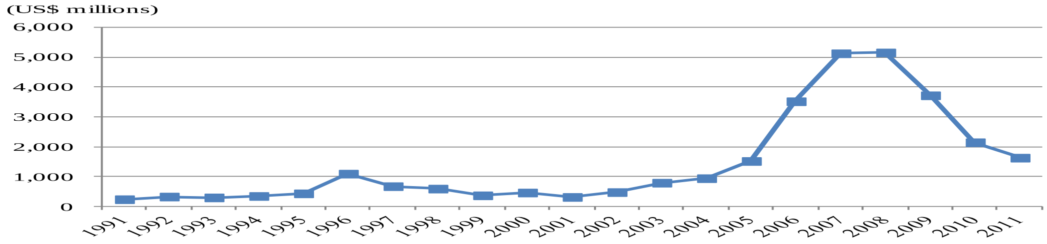
In addition to the Vision 2030, the Rapid Export Growth Strategy, which was introduced in 2005/06, adopted subsequently to increase export performance through indirect and qualitative measures.

As a result of these strategies, the exports have increased from US$16 billion in 2005/06 to US$25 billion in 2010/11, i.e., an increase by 56% in dollar terms.

2.4.4 Investment Scenario – FDI

During the period from 1991 to 2008, FDI reached the highest in the middle of the 1990s when privatization proceeds took place in the communication and energy sectors. During 1995 and 1996, FDI to GDP in country increased to 1.2% and1.5%, respectively. However, it decreased at the end of the 1990s and increased again after 2003/04. It then reached a historical peak in 2007/08, as shown in Figure 2.4.5. According to the World Development Indicator, the share of FDI to GDP was 0.7% in 2006, 2007 and 2008 were 3.35% and 3.32%, respectively.

[11] IMF, "Country Report No. 12/35", February 2012



Source: Economic Survey of Pakistan 2010/11

Figure 2.4.5: FDI Trends in Pakistan

Since 2007/08, the direct investment in the country continues to decline. Many reasons seem to attribute to the decrease after 2008: One of the major reasons is the global economic and financial recession after 2008. Other reasons are: the tainted credibility and inconsistent policies of the administration; the deteriorated law and order conditions in the country; the delayed and still unresolved energy crisis; and enterprises could not regain confidence with frequently changed administration which could not even formulate long-term investment plans under current law and order conditions.

However, increase in FDI in the country is largely attributed to the privatization process. Also, FDI trends in Pakistan revealed that the investments are dominated by those targeting at the domestic market having good potential based on its large population. However, it is true that economic conditions during the period of high FDI are far better than economic conditions in early 1990s. Nevertheless, the level of FDI in the country remains at infancy stage and there is still a long way to go. Stability and consistency to improve FDI in the country is very important particularly for the investment in manufacturing sector that often takes longer than a decade of continuous investment.

Table 2.4.3 shows the direction of FDI. While significant capital inflow are observed in mining, oil and gas explorations, transport, storage and telecommunication and financial business due to privatization, and investment in manufacturing sector still remains limited.

Table 2.4.3: Net Inflow of FDI (US$ Millions)

Sectors	1996/97	2006/07	2007/08	2011/12*
Power	244.8	204.6	68.9	-84.9
Chemicals, Pharmaceutical and Pesticides	51.7	90.9	152.8	114.6
Construction	14.5	157.1	89.0	71.7
Mining, Oil and Gas Explorations	37.7	568.8	677.3	620.0
Petroleum Refining	1.5	161.6	101.9	31.0
Food, Beverages and Tobacco	51.5	515.8	57.1	40.2
Textile	12.4	59.4	30.1	30.2
Transport, Storage and Telecommunication	6.4	1986.4	1814.4	-266.1
Trade	-	173.4	175.9	25.5
Electrical Machinery	4.1	3.4	18.3	8.3
Financial Business	106.5	930.1	1865.0	56.4
Tourism	7.4	30.2	6.6	17.3
Cement	49.4	33.7	102.5	-10.9

Source: State Bank of Pakistan
Note: Provisional data for 2011/2012.

Capital inflows in the country during the peak period of 2006/2008 were unfortunately drawn to stock markets and real estates, as inadequate investment opportunities existed in the domestic markets. In other words, it will be possible to invite capital inflows to industrial sectors if the sector can propose profitable investment opportunities.

2.5 Partnership Strategies and Reforms Scenarios

2.5.1 Reforms Support from IMF

(1) Economic Growth

The IMF has been actively engaged in Pakistan by providing support and technical assistance for reforms in the country. The stand-by agreement with IMF was supportedly considered to avoid the challenges of external and domestic economic shocks during the period of global economic and financial recession.

The authority issues frequent country reports stating the key issues and outlook of the economy. The report also includes the key policy recommendations to overcome the issues associated with the implementation of policies and hindrances in achieving targeted growth. Under the recent proposal for Post-Program Monitoring in Country Report No. 12/35 issued in February 2012, it is highlighted that there is a need to revisit the country policies. As highlighted by the new growth strategy paper in 2011, in the wake of current policies, it would be difficult to achieve the growth target. Also, it would not be easy to absorb the expected increase in labor force of the country. The report also highlighted some unresolved structural problems, specifically the energy crisis; the two major floods together with increasing fiscal deficit and increased inflation have left the economy highly vulnerable.

The approach paper significantly highlighted that the country is seriously confronted with challenges which include political uncertainty and law and order conditions. The report recommended the following policy actions:

(i) Strengthen public finances through revenue mobilization, cut in wasteful and low-priority expenditures and a strengthened fiscal decentralization framework;
(ii) Reform the energy sector to reduce power shortages and the large untargeted electricity subsidies, and more generally reduce the government’s footprint in the economy; and
(iii) Implement financial policies to reduce inflation, protect the external position, and safeguard the stability of the financial sector.

Table 2.5.1 provides estimates of basic macroeconomic indicators in baseline and reform scenarios for the period 2011/2012 and 2015/2016, respectively. The Reform Scenario estimates showed that a continued and sustained rise in GDP growth rate above the baseline scenario estimates which will have to trickle down positive effects on inflation, budget balance, current account balance, foreign exchange reserves, and unemployment rate. In 2015/2016, the economy of Pakistan will have a strong basics for higher growth strategy. Under the baseline scenario, real GDP was projected at 3.4% for 2011/12 and thereafter, a fixed growth of 3.5% was forecasted for the rest of period. While GDP growth was projected to increase from 4.5% to 5.5% during the period from 2012/13 to 2015/16 under reform scenario. Other economic indicators fiscal position, inflation, and unemployment were also projected to improve considerably from projections in baseline scenario.

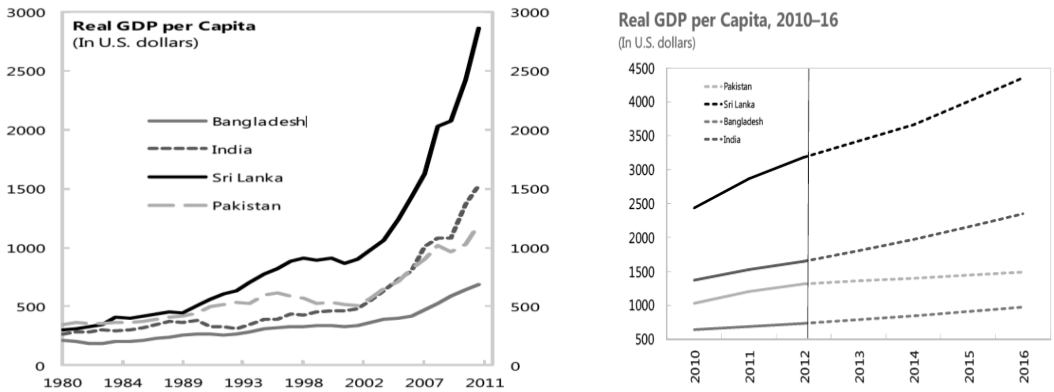
Table 2.5.1: Pakistan`s Baseline and Reforms Scenarios, 2010/11-2015/16

	Estimate	Projections				
	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16
Baseline Scenario						
Real GDP at Factor Cost (Percentage Change)	2.4	3.4	3.5	3.5	3.5	3.5
Consumer Prices (Period Average)	13.7	12.0	12.5	13.0	13.5	14.0
Budget Balance Excluding Grants (Percent of GDP)	-6.6	-6.9	-6.3	-6.1	-5.9	-5.8
Total Public Debt (Percent of GDP, Including All Obligations to the IMF)[1]	60.1	61.7	60.2	58.3	56.2	54.6
Current Account (Percent of GDP)	0.2	-2.0	-2.0	-3.0	-3.3	-3.7
Gross Reserves (Months of Next Year's Imports)	3.8	2.9	2.3	1.6	1.6	1.7
Unemployment (Percent)[2]	6.0	7.7	9.2	10.7	12.0	13.1
Reform Scenario						
Real GDP at Factor Cost (Percentage Change)	2.4	3.8	4.5	5.0	5.5	5.5
Consumer Prices (Period Average)	13.7	12.0	11.0	10.0	9.0	8.0
Budget Balance Excluding Grants (In Percent of GDP)	-6.6	-5.7	-4.4	-3.6	-3.3	-3.0
Total Public Debt (Percent of GDP, Including All Obligations to the IMF)[1]	60.1	60.0	56.6	52.8	49.1	46.2
Current Account (Percent of GDP)	0.2	-2.1	-1.7	-2.5	-2.6	-2.8
Gross Reserves (Months of Next Year's Imports)	3.8	3.0	3.0	3.0	3.0	3.0
Unemployment (Percent)[2]	6.0	7.5	8.6	9.3	9.8	10.1

Source: Pakistani authorities; and IMF staff estimates and projections.
Note 1: The debt figures in baseline scenario do not include future circular debt that may need to be taken over by the government.
Note 2: The employment elasticity of GDP growth estimate of 0.51 is assumed.

(2) GDP per Capita

Pakistan's per capita real income has risen by 0.7% in 2010/11 as against 2.9% in 2009/10. This reflects the impact of a slower economic growth. The per capita income rose from US$1073 in 2009 to US$1254 in 2010/11, thereby showing a tremendous increase of 16.9%. This is mainly because of a stable exchange rate as well as a higher growth in nominal gross national product (GNP). It is estimated that if this trend continues then per capita income will rise to US$1500 in 2016.[12]



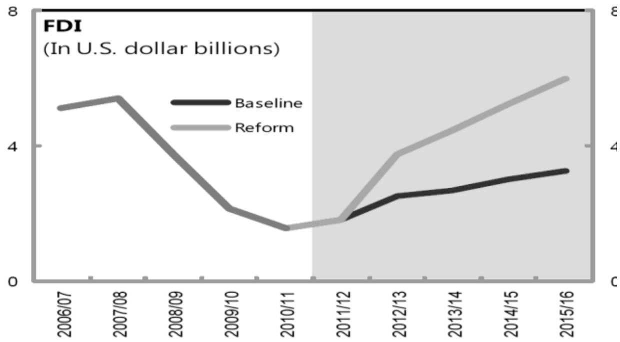
Source: IMF Country Report No. 12/35, February 2012

Figure 2.5.1: GDP per Capita Trend of Pakistan and South Asian Countries and GDP per Capita Estimation in 2016 by IMF Staff

[12]International Monitory Fund, "Pakistan 2011 Article IV Consultation and Proposal for Post-Program Monitoring, 2012"http://www.imf.org/external/pubs/ft/scr/2012/cr1235.pdf

(3) FDI Scenario

Portfolio investment provided a cushion against worsening of financial account and recorded an inflow of US$298 million as against the outflow of US$48million. FDI component registered much of the decline in non-debt creating inflows as FDI declined by 28.7% during July-April 2010/11 as a result of the fall inequity capital and reinvested earnings. The decline in FDI in Pakistan was mainly caused by domestic factors such as deteriorated law and order situation, energy crises, circular debt issues, and weak economic activity. Under the reform scenario, the investor's confidence is likely regain, and the FDI is projected to increase during the reform period.



Source: IMF

Figure 2.5.2: Decline in FDI and Forecast

2.5.2 Partnership with the World Bank

(1) Country Partnership Strategy

The Country Partnership Strategy (CPS) outlines the Bank's strategic approach in helping Pakistan to achieve its development goals over a four-year period. The World Bank's Board of Directors endorsed a Country Partnership Strategy for Pakistan on July 8, 2010, covering fiscal years 2010 through 2013. The goal of the strategy is to help steer Pakistan's economy back into a path of high economic growth by addressing key long-term constraints to growth, i.e., weak revenue mobilization, unreliable energy supply, and a fragile security situation.

A CPS Progress Report was presented to the World Bank's BOD on December 20, 2011. The progress report confirms that the overall strategic goal remains valid and consistent with the priorities of the Government of Pakistan as articulated in its New Framework for Growth Strategy.

The partnership remains centered on the existing strategic pillars of the CPS, i.e., economic governance; human development and social protection; infrastructure; and security and conflict risk reduction.

The four strategic pillars of the CPS are described below:

- Improving economic governance,
- Improving human development and social protection,
- Improving infrastructure to support growth, and
- Improving security and reducing the risk of conflict.

In November 2011, CPS was reviewed and adjusted on account of unprecedented floods in 2010 and 2011 together with devolution of responsibilities to provinces, unsettled security issues, and slow economic reforms. The strategic goal and pillars remain unchanged while emergency responses to the floods and a deepened engagement with the provinces were incorporated in the program. It was agreed with the government to extend the CPS period to include FY 2014 to deal with the adjustments.

(2) International Financial Corporation

The International Financial Corporation (IFC) is an integral part of the World Bank Group's program in Pakistan. The IFC strategy in Pakistan seeks to continue expanding investments in the sectors with the highest potential development impact and opportunities, including infrastructure (e.g., renewable energy, ports), financial markets (e.g., small medium enterprise support through access to finance, housing finance), and manufacturing and services (e.g., agribusiness, technical education). IFC is also focused on successful implementation of its advisory programs designed to improve the business enabling environment, strengthen financial markets, and support development of small businesses.

(3) Multilateral Investment Guarantee Agency

Pakistan is also a focus country for the Multilateral Investment Guarantee Agency (MIGA), where it has already provided guarantees in hydropower and microfinance. Moving forward, MIGA's strategy seeks to support investments into the International Distribution Alliance countries, south-south investments, complex infrastructure projects, and investments into conflict-affected areas.

2.5.3 Partnership with the Asian Development Bank

(1) The Country Partnership Strategy

The ADB Board of Directors endorsed the CPS covering the years 2009-2013 in January 2009. Consistent with the ADB's long-term strategic framework (Vision 2020), the CPS has the overarching objective of supporting sustainable and inclusive growth in Pakistan as a means of reducing the incidence of poverty and improving welfare.

The CPS outlines the ADB's strategic approach to assist Pakistan in achieving its development goals over the five-year period by facilitating structural change, investment and institutional effectiveness.

The main areas of current ADB operations in Pakistan reflected in the CPS 2009-2013 are as follows:

- Energy;
- Infrastructure investments in transport, logistics, and irrigation;
- Reforms in key sectors including energy, finance, agriculture and industry; and
- Urban services, including water, waste management, and transport.

(2) Policy Suggestions for Manufacturing Expansion and Export Promotion

CPS shows that in the medium- to long-term, macroeconomic stability is necessary but not sufficient condition for a country's development, which entails upgrading and diversification of the production and export structures. Empirical evidence from other countries that have achieved sustainable growth suggested that Pakistan needs to pass through different stages of growth, with a transfer of resources from the primary to secondary and tertiary sectors of the economy.

At some point, manufacturing (and industry in general) must take the lead in the growth process, as this sector is characterized by increasing returns to scale. Likewise, development is accompanied by technological and scale upgrading, especially in the manufacturing sector. The literature also showed that successful countries enter a phase of fast export growth during which they upgrade their export structures significantly.

(3) Export Performance and Sophistication

Empirical evidence showed that countries must have mastered the production of a relatively wide and diversified range of other products to be able to manufacture advanced products. This learning process provides them with the necessary capabilities (e.g., production knowledge). Findings suggested that economic diversification should be at the center of their development strategy.

The new dynamic theory of trade, which focuses on the elements of specialization patterns, argues that specializing in some products will bring faster growth than specializing in others; and that the current export composition of a country can determine subsequent growth of that country. Pakistan's major exports are heavily concentrated on low-end garments and textiles, indicating low sophistication of its exports basket compared to highly sophisticated machinery exports being produced and exported by developed countries.

The speed at which countries can transform their productive structure and upgrade their exports depends on the path determined by their current production and export structures. Taking the example of Malaysia, shifted from low-tech to medium and high-tech value products, and started producing more sophisticated products since 2000.

2.6 Karachi Development Potentials

Karachi, the cosmopolitan city is the largest city which houses the main seaport and economic and financial hub of Pakistan. It was also the capital of Pakistan and currently the capital of the province of Sindh. The city is located in the south of the country along the coastline meeting the Arabian Sea.

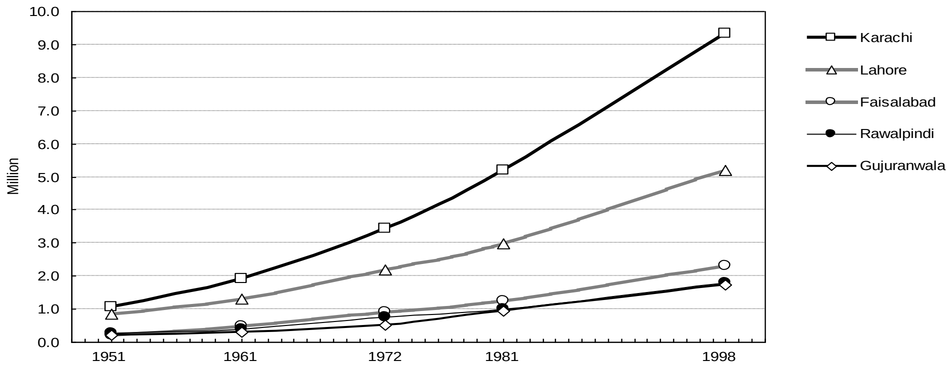
The city is the host of attractive business and investment opportunities. Karachi Port is an anchor of the city's commerce and trade sector. One of the competitive advantages of the city is the geo-strategic location as major seaports and network, provide potential gateway to investor's for better access to Central Asian Corridors. Along with extensive industrial infrastructure, the city is also the nucleus of headquarters of major banks, financial institutions, and business houses. The head offices of the main industries and offshore offices of the international companies are setup in Karachi and its stock exchange is one of the most important business centers of South Asia. Karachi Stock Exchange is the biggest and most liquid exchange in

Pakistan; about 639 companies were listed with a capital of Rs943.7 billion and an approximate market capitalization of Rs3,288.7 billion as of June 30, 2011.[13]

In line with its status as a major port and the largest metropolis, the city contributes a major share in the country's revenue collection. According to Sindh Board of Investment (SBOI), the city contributed about 60% in the total revenue collection of the country.

2.6.1 Population

Karachi is the most populous city which maintained high average annual growth rates in population among other cities like Lahore, Faisalabad, Rawalpindi, and Gujuranwala, both from 1972 to 1981 and 1981 to 1998; 4.8% and 3.5%, respectively (Refer to Figure 2.6.1). As the result, Karachi has increased the rate from 4.96% in 1971 and 3.52% in 1981 to 4.05% in 2010 (Refer to Table 2.6.1). With rapid expansion and growth, the current population share in the country's total population was estimated over 10% in 2010.



Source: Population Census 1998; The Study for Karachi Transportation Improvement Project – Interim Report 2011

Figure 2.6.1: Census Population Trends of Major Five Cities in Pakistan

Table 2.6.1: Population History and Projections of Karachi

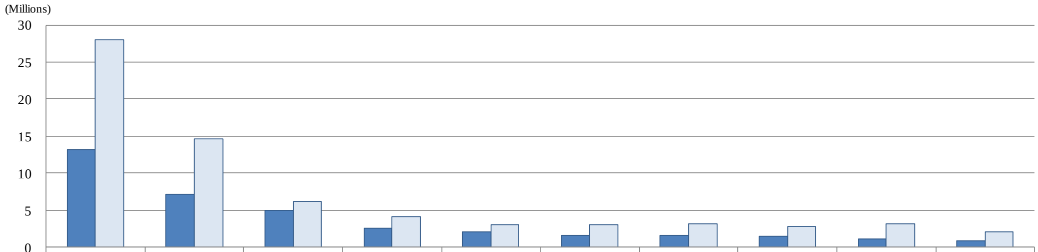
Year	1931	1941	1947	1951	1961	1971	1981	1998	2005	2010	2020	2030
Population (millions)	0.26	0.38	0.40	1.07	1.91	3.51	6.44	9.86	15.12	18.9	27.6	31.6
Area (persons/sq km)	-	-	233	-	-	-	1994	3527	3566	-	-	-
Growth Rate (%)	3.7	11.6	-	6.05	5.0	4.96	3.52	3.02	4.16	4.05	3.50	3.50

Source: JICA Study Team's calculation based on various sources

According to the last population census in 1998, the population of Karachi was 11.35 million, and the actual population reflected in the census was under-estimated by around 1.0 to 2.0 million to 9.96 million. This was mainly due to under-estimation on the number of people residing in the slum areas like Katchi Abdis and on the number of immigrants coming from

[13] www.jcrvis.com.pk

neighboring countries. To avoid the same misrepresentation, the Planning Commission of Pakistan has projected a population of almost 28 million in 2030. This figure is smaller than an estimate of 31.6 million in 2030 made in the Study for Karachi Transportation Improvement Project.



	Karachi	Lahore	Faisalabad	Rawalpindi	Multan	Hyderabad	Gujranwala	Peshawar	Islamabad	Quetta
Population (2010)	13,205,339	7,129,609	5,000,000	2,491,656	2,006,481	1,578,367	1,569,090	1,439,205	1,151,868	896,090
Population (2030)	27,993,000	14,626,000	6,192,000	4,149,000	3,025,000	3,005,000	3,143,000	2,778,000	3,175,000	2,038,000

Source: Vision 2030

Figure 2.6.2: Current and Estimated Population in Major Cities

The scale of this under-estimation is estimated to be 1.375 million and the 1998 Karachi population is accordingly modified to 11.35 million at an annual average growth rate of 4.68%. Based on the modified growth rate of 1998 census, the city's current population (2011) was estimated to be over 18.0 million and predicted to increase to 38.9 million in the year 2035. However, the natural increase in population growth is believed to be around 3.5% on account of refugees settlements in the city. Based on the natural growth rate, the discount applied on the year after 2020, the estimated population of the city is likely to be over 36.0 million in the year 2035.

2.6.2 Karachi Mega-City

Karachi is the financial and commercial capital of Pakistan; it accounts for a lion's share of Pakistan's revenue generation. It generated approximately 53.38% of the total collections of the Federal Board of Revenue, out of which 53.33% are customs duty and sales tax on imports[14]. Karachi produced about 30% of value added in large scale manufacturing[15] and 20%[16] of the GDP of Pakistan.

Although there are no official Pakistani statistics for the GDP by city, the UK Economic Outlook published by Price Water House Coopers in November 2009 estimated that the GDP of Karachi City in FY 2008/09 was US$8.9 billion. According to this outlook, the second and third largest cities in Pakistan in terms of the GDP are Lahore (US$4.0 billion) and Faisalabad (US$1.4 billion), illustrating Karachi City's by far dominant position.[17]

[14]"Federal Board of Revenue, "Year Book",(2006-2007) http://www.cbr.gov.pk/YearBook/20062007/FBRyearbook2006-2007.pdf.
[15]Pakistan and Gulf Economist. "Karachi: Step-motherly Treatment". http://www.pakistaneconomist.com/database2/cover/c99-15.asp.
[16] ADB. "Karachi Mega-Cities Preparation Project".http://www.adb.org/Documents/Produced-Under-TA/38405/38405-PAK-DPTA.pdf.
[17]The Study for Karachi Transportation Improvement Project – Interim Report 2011

According to economic trends gauged in the Karachi Strategic Development 2020 Study, Karachi is the largest city and considered as the trade and financial gateway to the outside world. The city's central role is gauged to 40% in country's financial activity, 20% of federal tax revenue and 40% of provincial revenues comes from the mega city. Based on 30% of manufacturing, 40% of large-scale manufacturing in the city, about 62% of income tax was also collected from the city. Based on port existence, 95% of foreign trade activities were generated in Karachi.

The economic hinterland extends to a much wider area. Its economic underpinnings include industries in seven major concentrations, namely, the Sindh, Korangi and Landhi Industrial Estates, Federal 'B' Area, North Karachi, the Export Processing Zone, and Port Qasim. It also has three satellite concentrations of manufacturing industry at Gharo in the South East, Nooriabad straddling the Karachi-Hyderabad Super Highway and the Hub Industrial Estate located in Baluchistan, The city is peppered with small concentrations of small-scale and household manufacturing industries, most of which house one specific category of manufacturing industry or specialized service.

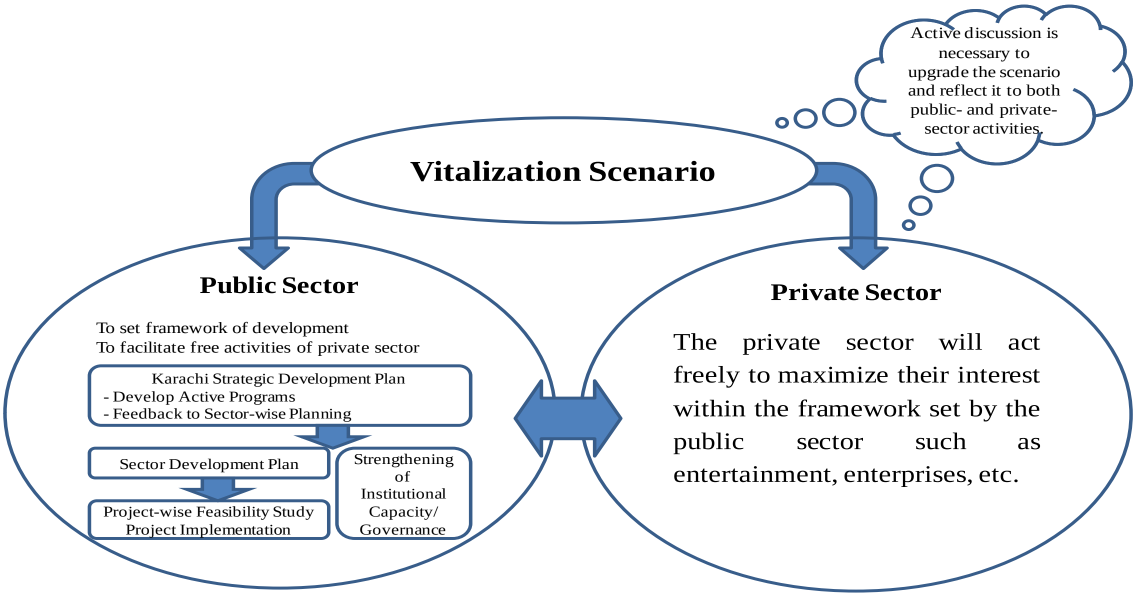
Based on extensive economic activities, the employment generation in the mega city is considerably high as compared to other cities. According to Household Survey in Karachi Transport Improvement Plan, there were about 5.6 million workers, 5.7 million household women (or men), and 4.1 million students. Jobless people accounted for only 5% of the total population, which is well below the unemployment rate in the country.

2.6.3 Karachi Vitalization Scenario

JICA (the then JBIC) in its report on "Karachi Vitalization Scenario, 2004", concluded that Karachi is the center of Pakistan's manufacturing industry and serves as a key hub for transport and distribution operations due to its close proximity to shipping lanes through two major seaports. As such, it serves as a hub not only for Pakistan's domestic distribution network but also for the flow of goods to neighboring countries like Afghanistan and points across Central Asia. On the other hand, the report pointed out that infrastructure deficiencies are bottlenecks in the development of Karachi, and suggested necessary measures to improve the investment climate.

Karachi is the heart of Pakistan's economy. Economic development in Pakistan as a whole cannot proceed in the absence of the economic advancement of Karachi. Pakistan needs to push ahead boldly with large-scale infrastructure projects in Karachi, the largest urban business center. To this end, it is essential that Japan provide public and private development assistance driven by the provision of private-sector technologies and experience, and the utilization of public-sector human resources training programs and ODA loans.

Karachi vitalization requires full collaboration between public sector and private sector, where each sector has its own roles. It is important for both sectors to play their own roles so that mutual and effective reinforcement of economic activities can give optimal targeted outcome. Figure 2.6.3 exhibits interactive mechanism between public and private sector.



Source: "Karachi Vitalization Scenario, 2004"

Figure 2.6.3: Karachi Vitalization Scenario

The insufficient infrastructure development has been a major inhibiting factor from the viewpoint of improving the investment climate. According to the Study on Strengthening of Industry for Private Sector Activation in Pakistan (November 2006), a market oriented economy should be developed by strengthening industry through pro-active incentives and policies for the private sector. This study report not only raised issues such as cluster formation and development of promising industries through the analysis of manufacturing actual condition of Pakistan, but also analyzed the impact of industrial development strategies for the economy as a whole. In order to achieve the target of "Vision 2030", it is concluded that upgrading of higher technical level is essential for high growth industry as well as high value-added industry, in particular.

Regarding Japan's ODA support, improving the investment climate is important in raising competitiveness and diversifying manufacturing sector (automotive industry in particular), and developing small and medium-sized industry. This study is closely linked with these support policy.

2.7 Current Conditions of Manufacturing Sector in Karachi

2.7.1 Position of Manufacturing Sector in Karachi

Manufacturing is a key part of the economy. In fiscal year 2005/06, it contributed about 19% of the GDP of Pakistan. It is traditionally divided into large-scale manufacturing and small-scale manufacturing industries. The CMI focuses on the production and investment behavior of large scale manufacturing industries covering establishments employing ten or more employees. Results for small-scale manufacturing industries would be provided by the Survey of Small and Household Manufacturing Industries presently being conducted by the Federal Bureau of Statistics.

A large number of multinational companies (MNCs) and local companies are present in almost every sector of the Pakistan's economy, especially in the consumer durable market and oil and gas sector. Currently, there are 600 operational companies in Pakistan, out of which, 170 are from MNC. Sindh, in this regard, is composed of almost all operational companies in Pakistan. With Karachi Stock Exchange in Sindh, one of the best exchange markets in the world, businesses seek to start their roots from Karachi. Some of the major companies operating from Karachi includes: Standard Chartered Bank (Pakistan) Limited, Siemens Pak Limited, Shell Pakistan Limited, ICI Pakistan, Unilever, Lotte Pakistan PTA Limited, ENGRO Corporation Pakistan, National Foods Limited, Lucky Cement Pakistan, Toyota-Indus Motors, Habib-Metro Cash and Carry, GSK Limited, Pfizer Pakistan, Novartis, Getz Pharma, etc.[18]

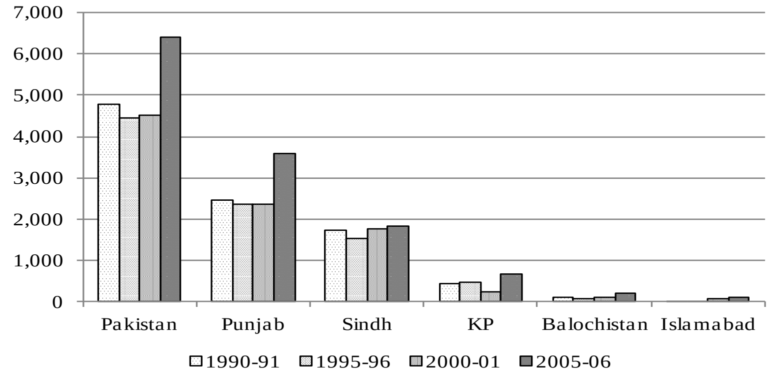
(1) Coverage

The Census of Large Scale Manufacturing Industries is conducted every five years using data from the provincial labor departments. CMI 2005-06 data was enhanced using industrial directories provided by Provincial Directorates of Industries as well as results of the Economic Census 2001 conducted by the Federal Bureau of Statistics. Intensified efforts were made to improve coverage. The information was collected through mailed questionnaires followed by field visits by Provincial Directorates of Industries. Annual reports of the establishments listed with stock exchanges were also used to augment the coverage. As a result, the number of establishments covered in CMI 2005-06 were 41.7% higher than CMI 2000-01, as shown in Table 2.7.1 and Figure 2.7.2.

Table 2.7.1: Number of Manufacturing Establishments Covered in Latest CMI

Region	1990-91	1995-96	2000-01	2005-06
Pakistan	4,792	4,474	4,528	6,417
Punjab	2,452	2,364	2,357	3,590
Sindh	1,751	1,528	1,768	1,825
KP	425	468	236	673
Balochistan	110	69	93	212
Islamabad	54	45	74	117

Source: CMI 2005-06



Source: CMI 2005-06

Figure 2.7.1: CMI Comparison by Years

[18]Sindh Board of Investment, http://www.sbi.gos.pk/success-stories.php (accessed July 29, 2012)

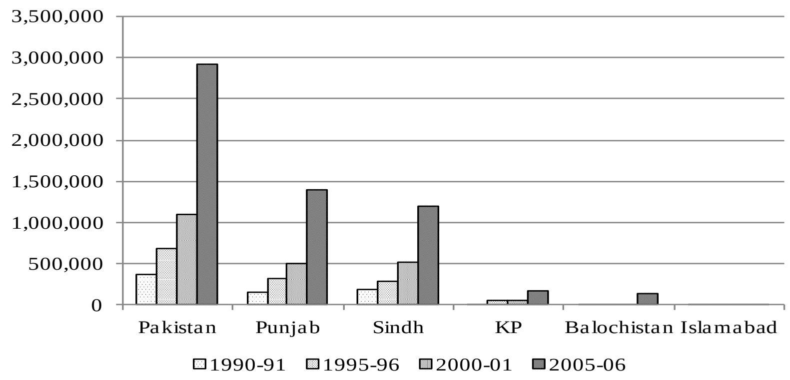
(2) Production Value

CMI 2005/06 showed the value of production at Rs2,929 billion depicting an increase of 165% over Rs1,104 billion in the CMI 2000/01. The values of production at producer prices recorded at the national and provincial levels in the last four CMIs are given in Table 2.7.2. and Figure 2.7.3. It may be noted that these values include all indirect taxes (net of subsidies) except general sales tax.

Table 2.7.2: Value of Production at Producer's Prices in the Latest CMI (Rs million)

Region	1990-91	1995-96	2000-01	2005-06
Pakistan	369,664	678,196	1,104,185	2,929,320
Punjab	162,052	321,623	497,708	1,405,699
Sindh	179,736	280,662	522,617	1,200,402
KP	14,993	60,689	46,439	164,313
Balochistan	9,822	8,843	23,828	136,582
Islamabad	3,061	6,379	13,593	22,324

Source: CMI 2005-06



Source: CMI 2005-06

Figure 2.7.2: Trends in the Production Value by Provinces

2.7.2 Current Manufacturing Conditions in Karachi

(1) Number of Business Units

According to the Securities and Exchange Commission (SECP) of Pakistan, the number of registered companies is 19,820 including non-manufacturing businesses. This number however, also includes companies that are no longer operational.

As per the Karachi Chamber of Commerce and Industry (KCCI), the total number of their registered members changes each year, due to the fact that some companies do not renew their memberships. The latest information of 2011 recorded around 10,716 as registered members. This list too, consists of manufacturing as well as non-manufacturing businesses.

As per the Overseas Investors Chamber of Commerce and Industry (OICCI), the number of member companies is 187. Again, this list includes manufacturing as well as non-manufacturing companies.

Table 2.7.3: Number of Business Units in Karachi

Registering Body	Number of Industrial Units
SECP	19,820
KCCI	10,716
OICCI	187

Source: SECP, KCCI, and OICCI

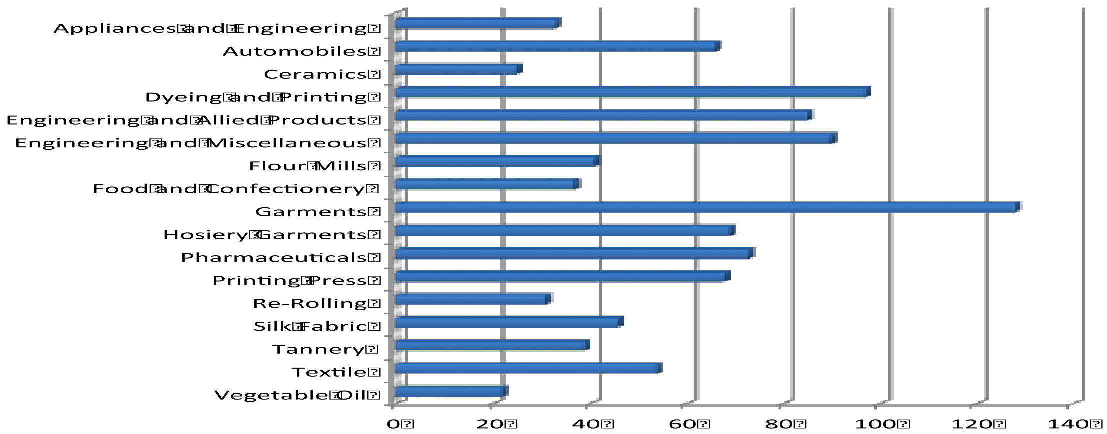
(2) Manufacturing Structure in Karachi

According to the Directory of Industrial Establishments in Sindh 2010, there were 1218 units (number of manufacturers in Karachi) in 45 sectors, as shown in Table 2.7.4 and Figure 2.7.3. The garments industry has the largest share in the manufacturing sector with 128 units and accounted for about 10.5% of the whole. It is followed by the dyeing and printing and engineering and miscellaneous industries which have 97 and 90 units, accounted for 8.0% and 7.4%, respectively.

Table 2.7.4: Number of Manufacturing Companies in Karachi by Sector

No.	Industries	No. of Companies	No.	Industries	No. of Companies
1	Appliances and Engineering	33	24	Match	1
2	Automobiles	66	25	Paints	6
3	Beverages and Soft Drinks	5	26	Paper Board	4
4	Canvas and Tarpaulin Threads	11	27	Pharmaceuticals	73
5	Carpets	9	28	Polish	3
6	Ceramics	25	29	Poultry Feeds	7
7	Chemical	9	30	Printing Press	68
8	Cosmetics	13	31	Re-rolling	31
9	Dairy Products	5	32	Refinery and Lubricants	15
10	Dyeing and Printing	97	33	Rubber	10
11	Engineering and Allied Products	85	34	Rubber and Tyres	3
12	Engineering and Miscellaneous	90	35	Salt	2
13	Fisheries	11	36	Silk Fabric	46
14	Flour Mills	41	37	Soap	17
15	Food and Confectionery	37	38	Tannery	39
16	Footwear	6	39	Tea	4
17	Garments	128	40	Textile	54
18	Herbal Laboratories	6	41	Thread	17
19	Hosiery Garments	69	42	Tobacco	1
20	Ink	1	43	Vegetable Oil	22
21	Insecticides and Pest Control	10	44	Woolen	5
22	Jute	1	45	Woolen/ Plywood	17
23	Lace and Hosiery	15		**Total**	**1,218**

Source: Directory of Industrial Establishments in Sindh 2010,

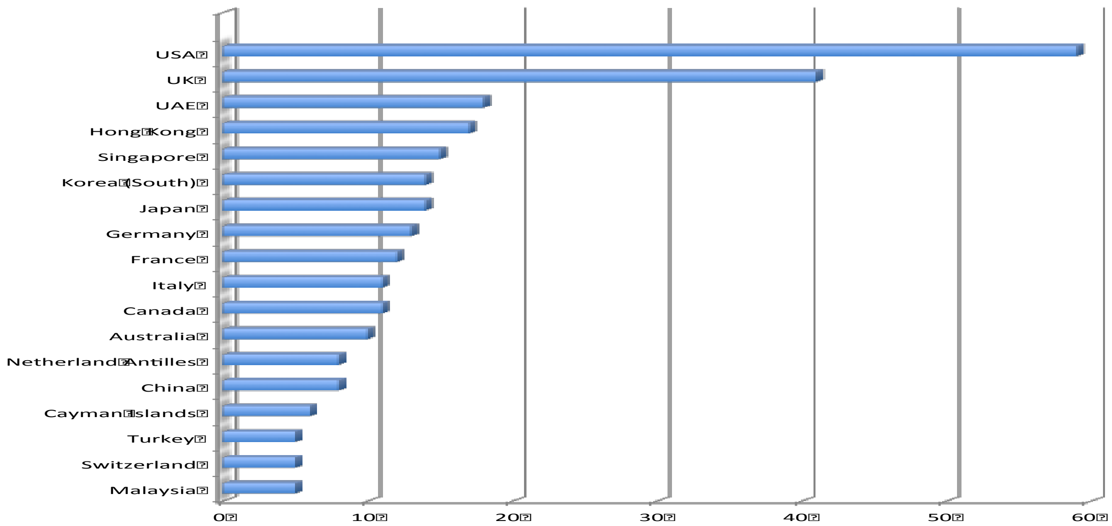


Source: Directory of Industrial Establishments in Sindh 2010

Figure 2.7.3: Number of Major Manufacturing Companies in Karachi by Sector

(3) Foreign Companies by Nationality

As per the list obtained by the SECP, there are around 346 foreign companies in Karachi. These companies belong to both manufacturing as well as non-manufacturing sectors. The top five countries with offices in Karachi are the USA, United Kingdom, United Arab Emirates, Hong Kong, and Singapore with 59, 41, 18, 17, and 15 companies, respectively. This can be seen in Figure 2.7.4 below:



Source: SECP

Figure 2.7.4: Foreign Companies in Karachi

(4) Industrial Estates in Karachi

Industrial activities in Karachi are spread over different areas. Specifically, there are nine industrial zones/areas where industrial establishments are concentrated. Each industrial zone/area is represented by an association, named after the area which it represents. The purpose of each association is to facilitate its members in operating their businesses efficiently and without hindrances. For this purpose, they are responsible directly or indirectly, to liaise with all the managing departments, infrastructure, utilities, security and permits/licenses, amongst others.

The following are the various associations present in the industrial areas of Karachi:

(i) **Karachi Export Processing Zone Authority (KEPZA)**: KEPZA is an industrial area in Karachi working, under the umbrella of the Ministry of Industries and as part of a group of export processing zones located in various cities throughout Pakistan. It is a fully independent department, having the authority to authorize, register, facilitate, and provide land and services to investors, without the intervention of any other government departments. KEPZ - ideally is located in close proximity to the Gulf, the Middle East and African markets, with good prospects for the markets of the European Economic Community (EEC) and the USA.

(ii) **Port Qasim Authority (PQA)**: Port Qasim is one of the two ports in Karachi, with a contained area, housing several companies both local and foreign. Though it is independent and very similar in its operations to KEPZA, companies considering putting up their factories in the area, must coordinate with separate government departments to begin their operation. PQA was established in 1973 following the site selection of Pakistan Steel in 1972, and its development is still ongoing. Even after 40 years, the function of Port Qasim Industrial Area is far from completion. PQA itself, is responsible for developing and maintaining the infrastructure within the contained area. PQIA - is unique in character having 12,200 acres of land above high water mark for the development of industries/commercial complexes.

(iii) **Bin Qasim Association of Trade and Industry**: Bin Qasim Association of Trade and Industry (ATI) is the association that manages all the companies in the Bin Qasim area including those within the PQA. The purpose of the association is to facilitate companies in their day-to-day problems, by connecting them to various government or non-government departments responsible for solving those problems. The association is under the Ministry of Commerce.

(iv) **Korangi Association of Trade and Industry**: Korangi ATI is the association managing the Korangi Industrial Area. The purpose of the association is to facilitate companies in their day-to-day problems by connecting them to various government or non-government departmentsresponsible for solving those problems. It works with a company, Korangi Industrial Territory Estate–Development and Management Company, which is responsible for developing and maintaining the infrastructure of the area. This company works under the Ministry of Industries, Sindh through the Sindh Infrastructure Board.

(v) **Landhi Association of Trade and Industry**: Landhi ATI is the association managing the Landhi Industrial Area. The purpose of the association is to facilitate companies in their day-to-day problems by connecting them to the various government or non-government departments responsible for solving those problems. It works with a company, Landhi Industrial Trading Estate (LITE), which is responsible for developing and maintaining the infrastructure of the area. This company works under the Ministry of Industries, Sindh through the Sindh Infrastructure Board.

(vi) **SITE Association of Trade and Industry**: SITE ATI is the association managing the SITE Industrial Area. The purpose of the association is to facilitate companies in their day-to-day problems by connecting them to the various government or non-government departments responsible for solving those problems. It works with a company, SITE Limited, which is responsible for developing and maintaining the infrastructure of the area. This company works under the Ministry of Industries, Sindh through the Sindh Infrastructure Board.

(vii) **Federal 'B' Area Association of Trade and Industry**: Federal 'B" Area ATI is the association managing the Federal 'B' Industrial Area. The purpose of the association is to facilitate companies in their day-to-day problems by connecting them to the various government or non-government departments responsible for solving those problems. It works with a company, Development and Management Company, which is responsible for developing and maintaining the infrastructure of the area. This company works under the Ministry of Industries, Sindh through the Sindh Infrastructure Board.

(viii) **North Karachi Association of Trade and Industry**: North Karachi ATI is the association managing the North Karachi Industrial Area. The purpose of the association is to facilitate companies in their day-to-day problems by connecting them to the various government or non-government departments responsible for solving those problems. It works with a company, North Karachi Industrial Development and Management Company, which is responsible for developing and maintaining the infrastructure of the area. This company works under the Ministry of Industries, Sindh through the Sindh Infrastructure Board.

(ix) **SITE Superhighway Association of Industry**: SITE Superhighway AI, is the association managing the industrial area located on the left hand side of the Super Highway, while traveling in the direction of Hyderabad. The purpose of the association is to facilitate companies in their day-to-day problems by connecting them to the various government or non-government departments responsible for solving those problems. It works with the same company, as SITE ATI i.e. SITE Limited, which is responsible for developing and maintaining the infrastructure of the area. This company works under the Ministry of Industries, Sindh through the Sindh Infrastructure Board.

Table 2.7.5: Number of Companies by Industrial Estate in Karachi

No.	Industrial Zone	No. of Company		Registered Members in Associations	No. of FDI/JV
		Unit	%	Unit [2]	
1	Korangi Association of Trade & Industry	4,500	26%	487	*
2	Landhi Association of Trade & Industry	1,080	6%	105	*
3	SITE Association of Trade & Industry	3,001	18%	*	21/*
4	Federal 'B' Area Association of Trade & Industry	2,000	12%	*	*
5	North Karachi Association of Trade & Industry	2,500	15%	400	*
6	SITE Association of Trade & Industry – Super Highway	130	1%	*	*
7	Bin Qasim Association of Trade & Industry	180	1%	*	15/8
8	Others	3,700	22%	*	*
9	Karachi Export Processing Zone Authority	*	*	114	40/23
	Total	17,091[1]	100%	1106[3]	

Source: JICA Study Team
Notes: * Sufficient data are not available.
1) Data given by KCCI includes manufacturing and non-manufacturing companies.
2) Only manufacturing companies registered with the industrial associations.
3) This figure does not include companies from the associations with a * in the registered members column.

2.7.3 Current Conditions of the Automobile Industry Representing Karachi

The automobile industry in Pakistan is a medium-sized but fast growing industry.[19] It is one of the important industries to be promoted on account of its broad expansion of supporting industries and big employment effects. Therefore, this section gives an overview of the industry.

(1) Production Trends

The Auto Industry Development Program (AIDP) sets target unit production for four wheeled vehicles, i.e., 380,000 units in 2009/10 and 560,000 units in 2011/12. When AIDP's target and actual production are compared, an annual target for 2006/07 of 200,000 units was mostly achieved with actual production of 178,000 units. However, in the subsequent years, the gap between the target and actual production widens gradually. In 2010/11, actual production remained at 134,000 units in comparison to the target of 440,000 units.[20] The actual production rate was limited to approximately 30% of the target units for 2010/11.

(2) Car Ownership

As of 2007, there were approximately 1.85 million cars in Pakistan. Also in 2007, the country's ownership rate[21] of four-wheeled cars was eight per 1000 persons and 22 per 1000 persons for two-wheeled vehicles. The four-wheeler ownership rate of only eight units per 1000 persons was much higher than three in 1991 but far below the world average (122) and lower than those in India (12) and China (10). Major reasons for the slow pace of ownership growth are because of the developing state of the national economy; a large disparity in wealth; and a rapid rise in car prices.

(3) Large Market Share of Japanese Companies

According to AIDP, assemblers are comprised of 82 companies: six for cars and LCV; five for buses and trucks; two for tractors; nine for motorcycles all of which are members of the Pakistan Automotive Manufacturers Association (PAMA); while the remaining 60 companies are outside PAMA.

In the Pakistani automobile market, Japanese manufacturers hold a dominant share in both four- and two-wheeled vehicles. They account for a combined total of 99.5% of the passenger car market, 94% of the truck market, and 73% of the bus market. In the two wheeler market, Japanese manufacturers hold a 45% share.

The total manufacturing employees are 192,000, and 1,392,000 if including the indirect sectors of 12,500 car dealers.

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[19] UNICO International Corporation/ JICA. 2011. "Final Report: Project for Automobile Industry Development Policy in the Islamic Republic of Pakisnta".
[20] Ibid.
[21] The car ownership rate is calculated as the number of cars per population.

(4) Automotive Parts Industry

Automotive parts suppliers operating in Pakistan are estimated at around 1600-1700 companies. The majority of them are engaged in the production of repair parts and 200-240 companies supply parts for OEM production.

For the Pakistani automobile industry facing various issues and challenges, increasing production of assembled cars is critical to the industry's sustainable growth. At present, automakers operate production systems where manual work still plays an important role, including the remaking of parts with low levels of accuracy. If the quality of supplied parts is improved to be on par with the international level, automakers will be able to boost their outputs by installing an advanced production line, including industrial robots that are widely seen in countries having world class automobile industry.

The domestic automobile industry requires automakers to achieve local content of over 70%. As a result, the parts industry has grown steadily in terms of production volume, while it has still to obtain international competitiveness in terms of quality and other factors.

The rapid growth in the automotive sector in Pakistan is difficult to sustain without efficient human resources. Presently, the industry is faced with severe shortage of trained engineers, supervisors and workers in the assembly operation and parts manufacturing. The deficiency of skilled personnel, which is a serious handicap, is more on account of rapid growth of the automotive sector and also due to lack of any institution for providing the high quality training required by the automotive industry.

2.7.4 Current Conditions of the Steel Industry Representing Karachi

The iron and steel industry is one of core industries in Pakistan such as petrochemicals, cement, electricity/gas, refinery, automobile industries.

(1) Domestic Production Capacity

The production capacity in Pakistan is estimated at about 3.7 million to 3.9 million tons as shown in Table 2.7.6. The Pakistan Steel Mills (PSM) is the country's only integrated steel mill which produces steel from iron ore and coking coal through the blast finance and converter technology. The annual capacity of PSM is 1.0 million to 1.2 million tons, which accounts for about 30% of the market. The production capacity of steel melters/furnaces and ship breakers in the country are 2.4 million and 200,000-300,000 tons per annum respectively.

In the 19080s and 1990s, Pakistan was rated as the foremost ship breaking country in the world, with its facilities and operations based at Gadani Beach, some 50 km from Karachi City. Currently ship breakers face difficulty in managing their business due to competition with neighboring countries.

Table 2.7.6: Steel and Iron Production Capacity (2004/05)

Source of Supply	Quantity (Thousand Tons)
PSM	1,080-1,230
Melters	2,400
Ship Breaking	200-300
Total Production Capacity	3,680-3,930

Source: Planning Commission, 2006, "Pre-Feasibility Study for Steel and Related Products"

In addition to integrated steel complex of PSM, there were 450 foundries, 334 re-rolling mills, and etc. in the country in 2004/05 as indicate Table 2.7.7.

In January 1971, the Governments of Pakistan and the then Union of Soviet Socialist Republics signed an agreement where the latter undertook to provide technological and financial assistance for the construction of PSM as a coastal based integrated steel complex. The construction work on the main plant was started in 1976. Among the main complexes and units of the project, the first coke oven battery was commissioned in 1981, the first blast furnace in 1981,the billet mill in 1982, and the two converters, one bloom caster and two slab casters of the steelmaking plant between 1982 and 1983. The hot strip mill was commissioned in 1983, the second blast furnace in 1984, the cold rolling mill in 1984, the second coke oven battery in 1985 and the expansion project billet caster in 1989.

PSM is located some 40 kilometers to the east of Karachi. PSM and its related facilities are spread over an area of 18,600 acres, or about 29 square miles.

PSM's production capacity of billet ranges from 400,000 tons to 450,000 tons per annum. The annual output of hot rolled sheets is in a range from 350,000 tons to 450,000 tons, cold rolled sheets of 100,000 tons, galvanized sheets of 80,000 tons, and formed sections of 150,000 tons.

Table 2.7.7: Profile of Iron and Steel Industry in Pakistan (2004/05）

Type	No. of Units
Integrated Steel Mills	1
Special Steel Mill	1
Foundries	450
Scrap Melters	82
Re-rolling Mills	334
Steel Pipe Mills	Over 60

Source: Planning Commission, 2006, "Pre-Feasibility Study for Steel and Related Products"

Companies registered in Pakistan Steel Melters Association (PSMA) are 173 in 2012. Seventy companies (about 40%) are located in Lahore. Only six companies are located in Karachi, although the largest steel mill, PSM, is in Karachi.

Table 2.7.8: Number of Companies Registered in PSMA by Region

Region	No of Companies
Lahore	70
Gujranwala	54
Islamabad	27
Peshawar/Gadoon/Hattar	11
Quetta/Azad Kashimir/Faisalbad	5
Karachi/Hyderabad	6
Total	173

Source: PSMA, "All Members List of All Regions" http://www.steelmelters.com/members.htm#All Members

(2) Supply and Demand for Iron and Steel Products

The total availability of mild steel re-rolled products was estimated at about 4.7million tons, out of which about 2.8 million tons (about 60%) was supplied through domestic production including production of PSM and 1.8 million tons (about 40%) through imports of various types of finished products.

Table 2.7.9: Availability of Iron and Steel Products (2004/05)

Source of Supply	Quantity (Tons)	Share (%)
PSM	675,000	14.5
Melters	2,100,000	45.1
Imports	1,834,000	39.4
Ship Breaking	44,000	0.9
Total	4,653,000	100.0

Source: Planning Commission, 2006, "Pre-Feasibility Study for Steel and Related Products"

(3) Import of Iron and Steel Finished Products

Pakistan imports iron and steel billets and finished products of about 1.8 million tons in 2004/05, which is about Rs50 billion. Imports have consistently increased year by year. Foreign steel makers such as Japanese and Korean companies have invested in substantial quantities of construction and building materials and high quality steel for the automobile industry to meet domestic demand which reflects insufficient local production capacity

Table 2.7.10: Import of Iron and Steel Finished Products

	2002/03	2003/04	2004/05
Quantity (Thousand Tons)	1,099	1,264	1,834
Total Value (Rs Millions)	23,513	29,485	50,079

Source: Planning Commission, 2006, "Pre-Feasibility Study for Steel and Related Products"

Chapter 3 Issues on Investment Climate Proposed by the International Organizations and Industrial Associations

3.1 The Business Environment–Doing Business 2012

This chapter provides an overview of various international studies which are carried out from time to time. These studies collect comparable data sets that are related with business and investment environment in various countries around the world.

3.1.1 International Comparisons

The keys to Pakistan's external competitiveness are improved security conditions, reliable energy supply, and efficient business environment and governance. Out of 142 countries included in the World Economic Forum's Global Competitiveness Report 2011/12, Pakistan ranked at 118th. Some of the country's weaknesses were identified which include issues in:

- Macroeconomic environment;
- Labor market efficiency;
- Higher education and training; and
- Infrastructure.

According to the World Bank Doing Business Report 2011, in which Pakistan ranked 83rd out of 183 countries, indicated that the cost of doing business in Pakistan could be reduced in the following areas:

- Enforcing contracts;
- Paying taxes; and
- Registering property.

Based on the latest Country Policy and Institutional Assessment (CPIA) of the World Bank, Pakistan ranked 57th out of 77 low-income countries with the following areas of improvement:

- Macroeconomic management;
- Fiscal policy; and
- Transparency, accountability, and corruption in the public sector.

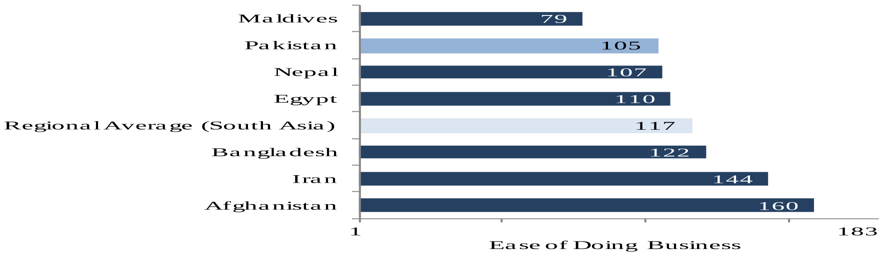
The following Table 3.1.1 lists the overall "Ease of Doing Business" rank (out of 183 economies) and the rankings by each topic. The rest of the table summarize the key indicators for each topic and benchmark against regional and high-income economy of the Organization for Economic Cooperation and Development (OECD) averages.

Table 3.1.1: Comparison of Ease of Doing Business in Pakistan

DOING BUSINESS 2012 RANK	DOING BUSINESS 2011 RANK		CHANGE IN RANK
Overall Ranking	105	96	↓-9
Topic Rankings	**2012 Rank**	**2011 Rank**	**Change in Rank**
Starting a Business	90	86	↓-4
Dealing with Construction Permits	104	100	↓-4
Getting Electricity	166	170	↑4
Registering Property	125	125	No change
Getting Credit	67	64	↓-3
Protecting Investors	29	28	↓-1
Paying Taxes	158	116	↓-42
Trading Across Borders	75	75	No change
Enforcing Contracts	154	155	↑1
Resolving Insolvency	74	71	↓-3

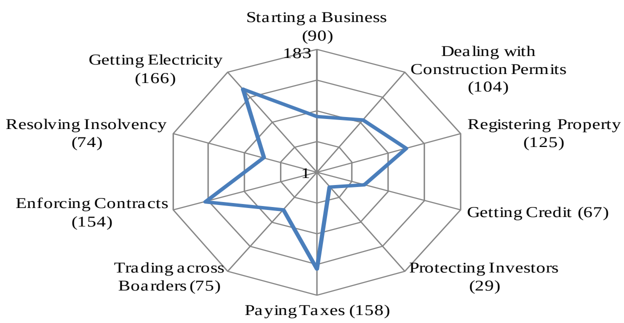
Source: World Bank, "Doing Business Report 2012"

For policy makers, knowing where the economy stands in the aggregate ranking on the Ease of Doing Business Index is useful. It is also useful to know how the economy ranks compared with other economies and with the regional average (Figure 3.1.1). The economy's rankings on the topics included in the Ease of Doing Business Index provide another perspective (Figure 3.1.2).



Source: World Bank, "Doing Business Report 2012"

Figure 3.1.1: Pakistan and Competitive Economy's Ranks on the Ease of Doing Business



Source: World Bank, "Doing Business Report 2012".
Note: Figures in parentheses show rankings.

Figure 3.1.2: How Pakistan Ranks on the Doing Business Topics

For policy makers trying to improve the economy's regulatory environment for business, a good place to start is to find out how it compares with the regulatory environment of other economies. *Doing Business* provides an aggregate ranking on the ease of doing business based on indicator sets that measure and benchmark regulations applying to domestic small to medium-size businesses through their life cycle. Economies are ranked from 1 to 183 on the Ease of Doing Business Index. For each economy the index is calculated as a simple average of its percentile rankings on each of the ten topics included in the index in *Doing Business 2012*:

(i) Starting a business
(ii) Dealing with construction permits
(iii) Getting electricity
(iv) Registering property
(v) Getting credit
(vi) Protecting investors
(vii) Paying taxes
(viii) Trading across borders
(ix) Enforcing contracts
(x) Resolving insolvency

The aggregate ranking on the ease of doing business, benchmarks each economy's performance on the indicators against all other economies in the *Doing Business* sample (Figure 3.1.2). While this ranking tells much about the business environment in an economy, it does not tell the whole story. The ranking on the ease of doing business, and the underlying indicators, do not measure all aspects of the business environment that matters most to the firms and investors or that affect the competitiveness of the economy. Still, a high ranking does mean the government has created a regulatory environment conducive to operate a business.

3.1.2 Domestic Comparisons

A new report ranked Faisalabad as the most business-friendly city in Pakistan, followed by Multan (2nd) and Lahore (3rd). Pakistan's largest commercial metropolis, Karachi, came out as 9th place in the list of 13 cities in Pakistan. The full ranking is enumerated below:

1st: Faisalabad
2nd: Multan
3rd: Lahore
4th: Islamabad
5th: Sheikhupura
6th: Gujranwala
7th: Sukkur
8th: Peshawar
9th: Karachi
10th: Rawalpindi
11th: Sialkot
12th: Quetta
13th: Hyderabad

In the first ranking conducted in 2007, Karachi was declared the top city in Pakistan in terms of business-friendliness. However, the comparison over time may not be entirely accurate since the

2007 ranking had included only six cities, as opposed to 13 in the 2010 rankings; and the methodology has also improved over the past two reports.

Doing Business in Pakistan 2010, reported on the research conducted collaboratively by the World Bank and the International Finance Corporation (IFC) and compared the regulatory environment for business in 13 Pakistani cities. It measured the performance across the following six stages of “the life of a small- to mid-sized domestic enterprise”:

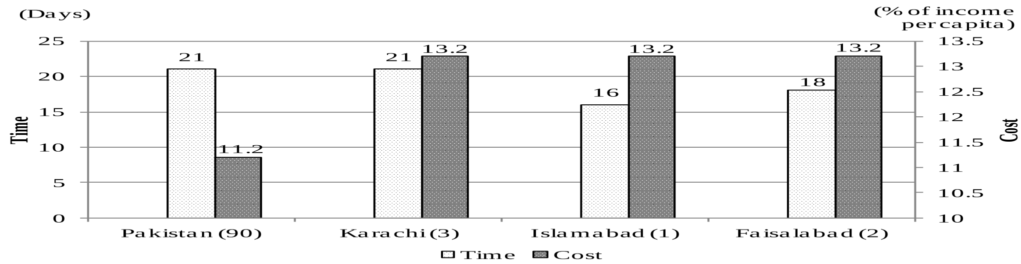
(i) Starting a business
(ii) Dealing with construction permits
(iii) Registering property
(iv) Paying taxes
(v) Enforcing contracts
(vi) Trading across borders

According to the study, Pakistan as a whole ranked 85th out of 183 economies in terms of ease of doing business, but if the best practices that are already practiced in different cities in Pakistan will be adopted in all cities. Pakistan’s ranking will improve to its previous condition and may be able to get to 69th place.[22]

(1) Starting a Business

The first indicator of doing business is the challenges associated with the launching of a new business which include the number of procedures to comply with, from basic permission to proper launching and commencement of business. It examines the procedure, time, and cost involved in launching commercial or industrial firm with up to 50 employees and startup capital of ten times the economy’s per capita gross national income (GNI). The average time required to complete such procedures and the cost associated with the same as a percentage of GNI per capita. The value of indicator of minimum capital requirements in Pakistan is null as there is no such minimum capital requirement imposed by regulatory authorities in the entire country.

Also there are about ten number of total procedures required for starting a new business and these are same across the country. Figure 3.1.3 exhibits the ranking of the country on international scale for ease in starting a business along with the domestic rankings of top three cities compared with Karachi on selected indicators.



Source: World Bank and IFC, “Doing Business Report in Pakistan 2010”.
Note: Figures in parentheses show rankings.

Figure 3.1.3: Starting a Business

[22]The World Bank, ‘Doing Business in a more Transparent World’ 2012, http://www.doingbusiness.org/~/media/fpdkm/doing%20business/documents/profiles/country/PAK.pdf

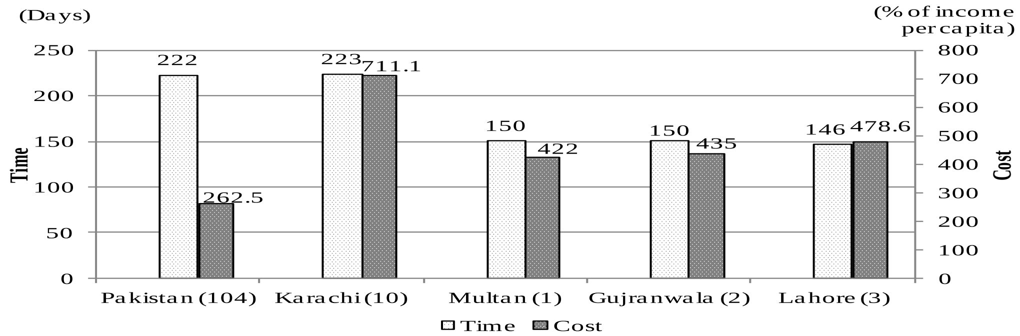
As exhibited in the graph above, ranking of Pakistan stood at 90. To register a firm in Pakistan, the investor has to fulfill about ten number of registering procedures which is considered higher as compared to South Asia (seven procedures) and OECD (five procedures). However, in terms of time and cost (% income per capita), Pakistan is better than other countries in South Asia. Time required for the said purpose in Pakistan is 21 days as against 23 days in South Asia. Whereas cost is also lower at 11.2% of per capita income in Pakistan as against 21.6% in South Asia.

While the average time required to register a firm in Islamabad stood far below the average across the country, Islamabad ranked first, domestically. This followed by Faisalabad City, which stood at second position with an average time (in days) of 18 days, required to register a firm in the city. Compared to previous doing business rankings, Faisalabad and Lahore have both maintained their ranking by introducing reforms in more than one area measured in this report. Both cities are now using e-Services for business start-up. Karachi stood at third position, sharing the position with Lahore and Peshawar, where average time to register a firm requires 21 days.

(2) Dealing with Construction Permits

Dealing with construction permits tracks the procedures, time, and costs to build a ware house – including obtaining necessary licenses and permits, completing required notifications and inspections, and obtaining utility connections.

Pakistan ranks at 104th for dealing with construction permits due to high cost per capita and days required in some major cities like Karachi and Islamabad. Average number of days required for such permission is about 222 days, while cost is about 262% of per capita income in the country. Whereas in South Asian and OECD countries, average of days required are 222 days and 152 days, respectively, and about 980% and 45.7% of the per capita income, respectively, is the cost to obtain such construction permits. Figure 3.1.4 exhibits the domestic comparison and rankings on selected indicators.



Source: World Bank and IFC, "Doing Business Report in Pakistan 2010"
Note: Figures in parentheses show rankings.

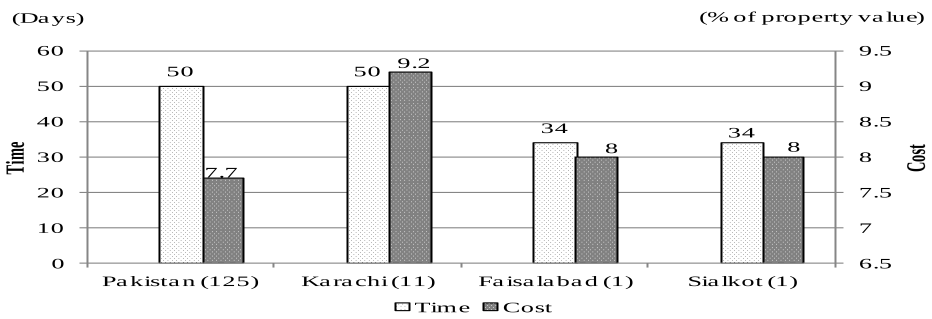
Figure 3.1.4: Dealing with Construction Permits

Multan ranked first amongst other major cities mainly on account of lower cost, i.e., 422.0% of income per capita which is lowest amongst the selected 13 cities. However, there are other cities which have considerably lower cost than Multan as revealed from the average cost of 262.5% of income per capita in Pakistan. Karachi which is the major financial, economic, and industrial hub, ranked much lower at 10th position, both on account of higher time in days about 223 days and the second highest cost at 711.1% of income per capita in the country after Islamabad (797.9% of income per capita).

(3) Registering Property

With an assumption as standardized case of entrepreneur who wants to purchase land and a building that is already registered and free of title dispute, registering property indicator examines the steps, time, and cost involved in registering property.

In 2011, Pakistan made registering property more expensive by doubling the capital value tax to 4%. Despite this, there is no change in the ranking of Pakistan and stood at 125th position (2011: 125th Position) in "Doing Business 2012". The average number of days required is 50 days, while cost of registering is about 7.7% of property value. Whereas, in South Asia and OECD, the average number of days required to register a property stood at 105 days and 31 days, respectively. This reflects a better position for Pakistan as against South Asian countries in terms of number of days.



Source: World Bank and IFC, "Doing Business Report in Pakistan 2010".
Note: Figures in parentheses show rankings.

Figure 3.1.5: Registering Property

Domestically, Faisalabad and Sialkot share the top position largely due to fewer numbers of days required to register a property, i.e., 34 days. Karachi ranked at 11th position both on account relatively higher number of days (50 days) and high cost of 9.2% of property value. This cost is only an official cost required by law, adding the corruption and bribery, the cost of registering property in the mega city is much higher. Despite some reforms in 2006, the stamp duty decreased from 3% to 2% of property value. However, the positive impact of the reform was overcome by the reinstatement of the Capital Value Tax of 2% at the national level by the Finance Act 2006, causing a net increase of 1% in the total cost to transfer property. Second as compared to other mega cities, the property values in Karachi have increased significantly during the past decade.

(4) Paying Taxes

The mandatory contributions required by law that a medium-size company must pay or withhold in a given year. The indicator also measures administrative burden in paying taxes. According to Doing Business 2012, Pakistan increases the profit tax rate for small firms.

There is a considerable deterioration of Pakistan's ranking, as it is lowered considerably from 116th position in 2011 to 158th position in 2012. This is mainly because of the increase in the total tax rate as percentage of profit from 31.6% in 2011 to 35.3% in 2012. The number of payments in a year is also higher at 47, as compared to 28 and 13 in South Asia and OECD countries, respectively. The time required to prepare, file, and pay (or withhold) the corporate income tax, value added tax, and social security contributions also stood higher at 560 hours (per year). Whereas in South Asia and OECD countries, this stood at 281 hours and 186 hours, respectively per year.

Table 3.1.2: Tax Rates

Country/City	Ranking	Selected Indicators					
		Payments (number per year)	Time (hours per year)	Profit Tax (%)	Labor Tax & Contributions (%)	Other Taxes (%)	Total Tax Rate (% Profit)
Pakistan	**158**	**47**	**560**	**-**	**-**	**-**	**-**
Islamabad	1	35	559	15.6	5.5	4.9	26.0
Quetta	2	47	560	14.4	12.2	4.5	31.2
Lahore	3	47	560	14.3	12.2	5.1	31.6
Karachi	**11**	**47**	**560**	**14.3**	**12.2**	**5.1**	**31.6**

Source: World Bank and IFC, "Doing Business Report in Pakistan 2010".

Amongst the 13 cities of Pakistan, Islamabad ranked 1st, wholly on account of lower tax rate as percentage of profit, followed by Quetta. Karachi ranked at 11th position, on account of relatively higher tax rates as compared to other cities.

(5) Trading Across Borders

The position of Pakistan is relatively better amongst 183 countries in trading across border, and also amongst other indicators. Pakistan ranked at 75th position on international scale. Since 2011, Pakistan reduced the time to export by improving electronic communication between the Karachi Port authorities and the private terminals. This improved the time to export and import which stood currently at 21 and 18 days, respectively, better than when compared to 32 and 33 days, respectively in South Asian countries.

Cost to export and import in Pakistan is significantly lower at US$660 and US$705 per container, respectively as compared to South Asia and OECD. This is mainly due to the large industrial activities being done in the port city of Karachi. Cost of export and import in South Asia is US$1590 and 1768, respectively, whereas in OECD, export and import costs around US$1032 and US$ 1085 per container, respectively.

Table 3.1.3: Trading

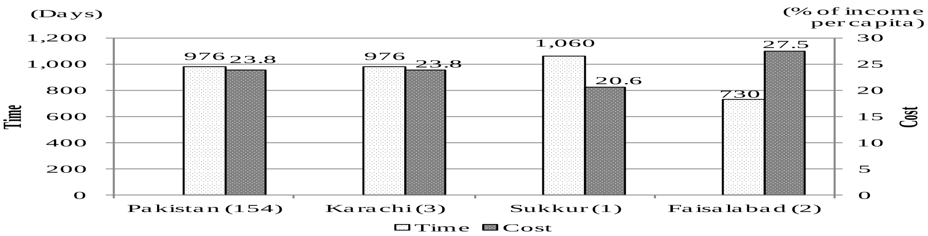
Country/City	Ranking	Selected Indicators					
		Documents to Export (number)	Time to Export (days)	Cost to Export (US$ per Container)	Documents to Import (number)	Time to Import (days)	Cost to Import (US$ per container)
Pakistan	**75**	**7**	**21**	**660**	**8**	**18**	**705**
Karachi	**1**	**9**	**22**	**611**	**8**	**18**	**680**
Hyderabad	2	9	20	616	8	20	708
Sukkur	3	9	21	639	8	18	784
Faisalabad	4	9	22	639	8	20	739
Multan	5	9	22	624	8	20	936
Sialkot	5	9	22	639	8	20	860
Sheikhupura	7	9	21	639	8	20	1,088
Peshawar	8	9	22	715	8	20	784
Quetta	9	9	23	619	8	21	693
Gujranwala	10	9	23	677	8	20	936
Islamabad	11	9	22	670	8	21	936
Rawalpindi	12	9	23	685	8	20	1,012
Lahore	13	9	23	791	8	20	1,088

Source: World Bank and IFC, "Doing Business Report in Pakistan 2010".

Being the country's only major port city, the cost of container export and import is considerably lower when compared with other cities; the city is also the major industrial hub of the country, contributing largely in GDP. About US$611 and US$680 are required on average to export and import a container, respectively. Cost is considered as a major indicator of ease in trading across borders and the cities are largely ranked according to this indicator. Therefore, the cost of other cities increases as distance increases from the major port city of the country. As revealed in the table, the distance of Lahore, Rawalpindi, and Islamabad is relatively more, therefore the cost per container to export and import in these cities are considerably higher. Hence, Hyderabad being the closest city (also considered as twin city) to Karachi positioned and ranked as 2nd.

(6) Enforcing Contracts

Enforcing contract is measured by following the evolution of a sale of good dispute and tracking the time, cost and number of procedures involved from the moment of filling the lawsuit until actual payment. Pakistan's position has improved slightly. However, the position of 154 (2011: 155) reveals poor performance of the country. This is largely on the account of poor performance of the justice system with common problems on the delays in justice, mismanagement, lack of transparency, and other procedural complexities. At the same time, there is also dearth of resources and physical infrastructure in Pakistan. Despite these problems, Pakistan is at a better position in the South Asian region.



Source: World Bank and IFC, "Doing Business Report in Pakistan 2010".
Note: Figures in parentheses show rankings.

Figure 3.1.6: Enforcing Contracts

Karachi ranked 3rd amongst the 13 cities, led by Sukkur and Faisalabad at 1st and 2nd. Cost and time are the key indicators, and are largely associated with the size of population. With the increased population, the number of filed cases has also gone up but there has not been a corresponding increase in the number of courts and staff. As revealed from the doing business data, the cities which have large population or where the infrastructure is relatively poor, the cost and time to deal with enforcing contracts are also higher. Multan, Peshawar, and Quetta Multan, with low infrastructure and relatively large population ranked at 4th, 8th, and 13th,respectively. Meanwhile, Lahore ranked 8th and Islamabad at 10th. This is largely on account of high number of cases filed in Lahore and Islamabad courts as former being the capital city of the province and latter being the capital city of Pakistan. Karachi also being the populous city, however having relatively good infrastructure, the city is in much better position in terms of time and cost associated with enforcing contracts.

Key Findings and Remarks

The report on doing business highlighted three key findings (quoted directly from the report):

First: Consistent reformers outperform others. Since the publication of Doing Business in South Asia 2007, Faisalabad and Lahore have both maintained their high ranking by introducing reforms in more than one area measured in this report. Both cities are now using e-Services for business start-up and have adopted new uniform building and zoning regulations for construction permits. Other cities like Karachi or Sialkot dropped, relative to their peers. Some of these changes can be attributed to the addition of seven new cities, with some of them, like Multan, having competitive regulatory frameworks.

Second: No single city does well on all indicators. For example, Islamabad ranks well on the ease of starting a business and ease of paying taxes, but lags behind on enforcing contracts and trading across borders. Karachi, while efficient in trading across borders and contract enforcement, lags behind other cities on the ease of obtaining a construction permit, transferring a property title, and paying taxes. These results can guide policy makers regarding areas where improvements are possible. Cities can learn from each other and adopt the good practices that already existed elsewhere in Pakistan. For example, Sukkur can look to Faisalabad for ways to improve starting a business and registering property.

Third: Size does not determine ranking. Cities can compare themselves both with their peers and their larger and smaller neighbors. Both smaller cities, such as Multan and Sheikhupura, and larger cities, like Faisalabad and Lahore, are ranked in the upper half. Smaller cities may be more competitive by promoting the use of technology, while maintaining low costs.

Government offices in large business centers deal with a high volume of operations, which can lead to bottlenecks and higher costs for professional services. On the other hand, these cities benefit from economies of scale and may have more resources at their disposal to invest in administrative modernization than their smaller neighbors.

Apart from the above findings, it can be noted that Karachi lags behind other cities on dealing with construction permits and registering property firstly because their costs are high and secondly because the time required in Karachi is longer than in other cities. Karachi also ranks low on paying taxes, yet tax rates are almost the same as other cities with the exception of Islamabad. Therefore, it is considered that Karachi ranks low on paying taxes although there is no big difference from other cities.

3.2 Business Environment and Investment Survey

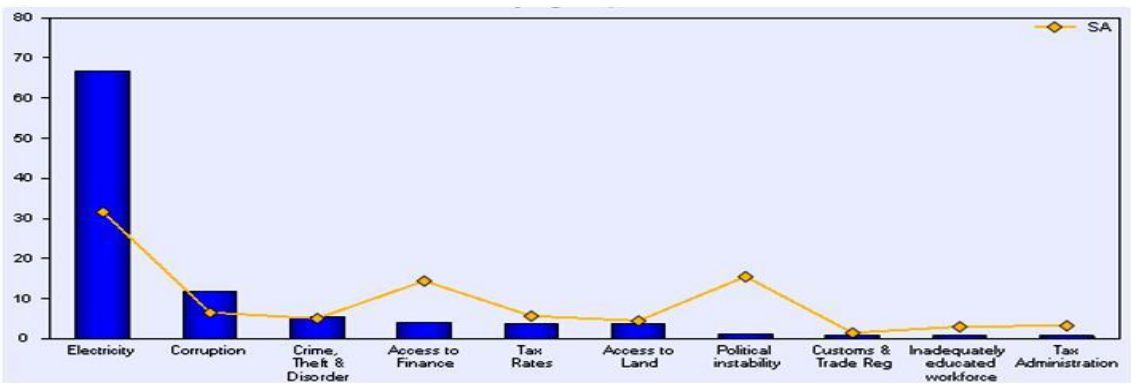
The World Bank and Overseas Investors Chamber of Commerce and Industry (OCCI) conducted surveys to study the obstacles in the business environment as well as the perception of the business environment in Pakistan in 2007 and 2010, respectively.

3.2.1 World Bank Enterprise Survey

The World Bank Enterprise Surveys in Pakistan was carried out in the period of September 2006 through June 2007. It interviewed 935 business firm’s owners and top managers to create the data set and country profile for Pakistan. For comparative analysis, the benchmarks of the averages for the group of countries in South Asia and the Pakistan income group were taken.

(1) Biggest Obstacles in Business Environment

Figure 3.2.1 provides a snapshot of the biggest business environment obstacles as perceived by firms and presents the top ten constraints as identified by firms in Pakistan, benchmarked against the regional averages. These obstacles are electricity, corruption, crime, theft & disorder, access to finance, tax rates, access to land, political instability, customs & trade regulations, inadequately educated workforce, and tax administration.



Source: World Bank, “Enterprise Surveys in Pakistan 2007”

Figure 3.2.1: Biggest Obstacles in Business Environment

More than 65% of the respondents considered electricity as the biggest obstacle in their businesses, followed by corruption and others. It may be noted apart from electricity, about 5% or fewer respondents considered crime, theft and disorder, access to finance, tax rates, access to land, political instability, customs and trade regulations, inadequately educated workforce, and tax administration as obstacles. When responses were compared with regional averages of South Asian region, Pakistan has better position in most cases except for electricity and corruption. The World Bank`s Enterprise Survey has been further explained in Appendix C.

3.2.2 Perception and Investment Survey 2011 by OICCI

The OICCI, Overseas Investors Chamber of Commerce & Industry, conducts the Perception and Investment Survey every year for the information of its members and stakeholders. The following are extracts from 2011 survey:

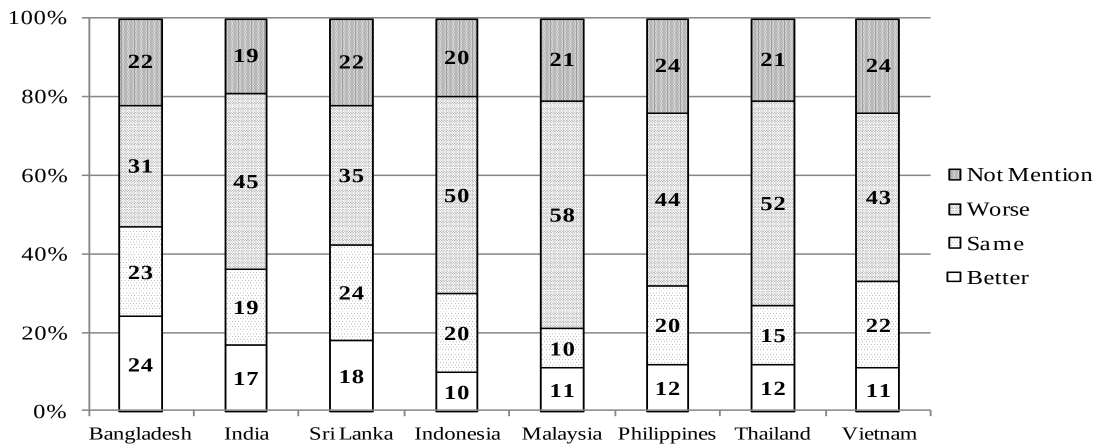
(1) Ease of Doing Business

The survey not only covered various aspects of doing business but also compared Pakistan with eight other countries which are considered competitors for foreign investment in Pakistan.

While it may be true that the countries mentioned in the survey have more conducive business climate than Pakistan due to better macro-economic indicators and stable political environment, in most cases there is still a healthy proportion of respondents who feel that ease of doing business in Pakistan is the same or better as compared to other economies.

If only the "worse" rating is considered, Pakistan fares relatively poor compared to the eight other economies. Most importantly, 45% of the respondents feel India is better for ease of doing business than Pakistan. While 17% of the respondents felt that there is more ease of doing business in Pakistan than in India while 19% perceived conditions to be the same.

The overall present environment in Pakistan received mixed responses but a relatively higher percentage of “worse” than the eight countries.



Source: OICCI Investment Survey Report 2011

Figure 3.2.2: Ease of Doing Business

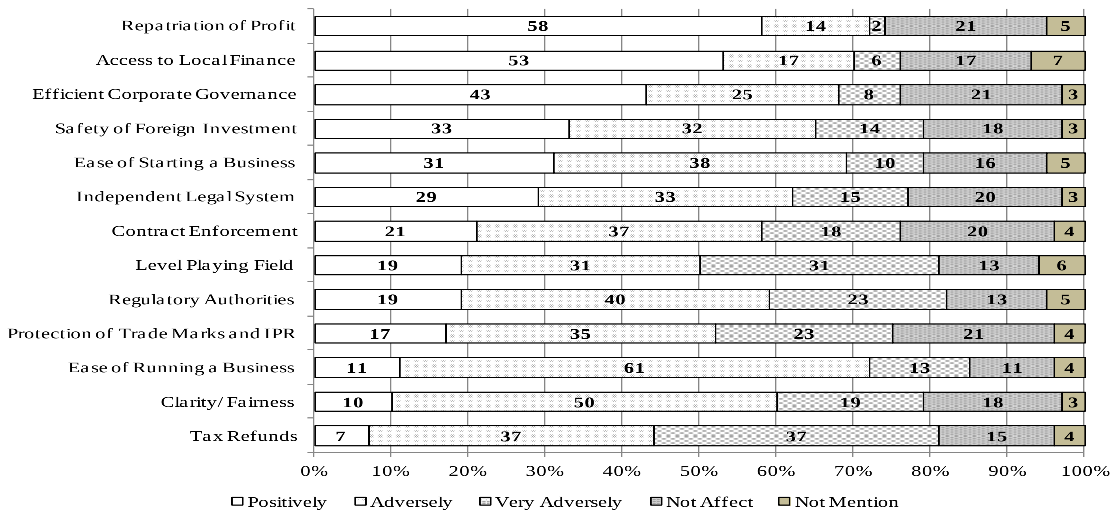
(2) Aspects of Doing Business

The Survey revealed that Pakistan ranks favorably for aspects of doing business like the 'repatriation of profits', 'access to local finance', and 'corporate governance'. Fifty eight percent of respondents felt that repatriation of profits is smooth and facilitates doing business, reflecting the liberal and investor-friendly policies in place which are appreciated by foreign investors.

On the flipside, tax refunds, or the delay in settling refunds, unfair regulations, difficulties in running day to day operations, lack of protection of Intellectual Property Rights (IPRs), and contract enforcement remain serious challenges to business operations.

Delayed tax refunds continue to agitate the business community. Some companies are still waiting on refunds due for a long time. Apart from these, a significantly high proportion of respondents consider 'fairness of laws and regulations' to be a problem in conducting business activities.

The pharmaceutical sector is highly concerned with non-level playing field and threats to protection of trademarks and IPRs. Sixty seven percent of IT sector respondents also identified these issues as reasons behind limited new investment in their sector.



Source: OICCI Investment Survey Report 2011

Figure 3.2.3: Aspects of Doing Business

OICCI`s Investment Survey Report 2011 has been further explained in Appendix C.

3.2.3 Additional Information Relating to Industrial Activity

The following information are useful for potential investors:

(i) Electricity outage in Karachi is better than Islamabad and Lahore,
(ii) Corruption appears relatively less problematic, and
(iii) Financial flow problem.

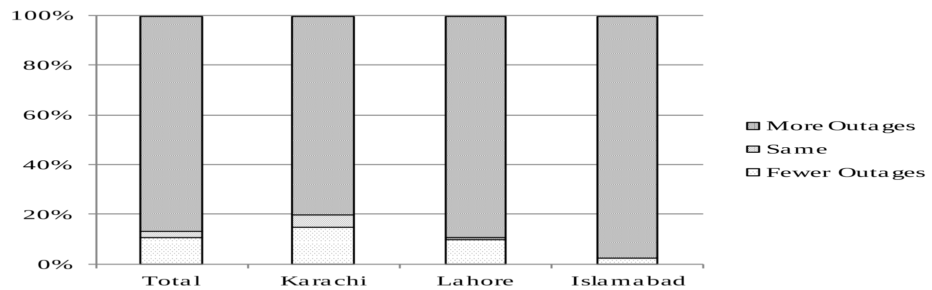
(1) Electricity outage in Karachi is better than Islamabad and Lahore

According to "The World Bank's Enterprise Analysis Unit surveyed the same group of 319 Afghani firms in 2008 and 2010, as well as a group of 385 Pakistani firms in 2007 and 2010", 100% of firms in Islamabad experienced power outages in 2010 compared to 66% in 2007. Firms in the Karachi region, however, are evenly split on their opinion between how they perceive electricity to have changed as an obstacle from 2007 to 2010.

Small firms are more likely to view electricity as a major constraint to daily operations. In 2010, small and micro-sized firms reported electricity to be a major constraint at a significantly higher rate than medium or large firms (90% of small, 78% of medium, and 74% of large).

The deterioration of electricity is evident from objective reporting on outages. Although the average duration of power outages decreased in Pakistan from 3 to 1.5 hours, the number of power outages per month increased substantially. Electricity supply is intermittent and inconsistent and almost all firms in Pakistan report more power outages per month in 2010 than in 2007—from 30 in 2007 to over 120 in 2010, or an average of once a day to four times a day (Figure 3.3.1).

The Karachi region saw the smallest increase (from 33 outages per month in 2007 to 80 in 2010), while firms in Islamabad and Lahore both saw much higher increases in the number of power outages (averaging about 150 outages a month in 2010). While these numbers appeared incredibly large, the demand for power in Pakistan vastly exceeds the supply and the shortage of electric power in Pakistan is a real and an urgent problem.



Source: Yang, Judy S. 2011. "Business Environment Perceptions in Afghanistan and Pakistan"

Figure 3.3.1: Change in Power Outages

(2) Perceptions on corruption are improving

From 2007 to 2010, the percentage of firms that consider corruption to be a severe obstacle decreased from 27% to 14%, and the percent perceiving it to be a major obstacle decreased from 38% to 15%. Among objective measures, Pakistani firms spend more time dealing with regulations, face fewer visits from tax officials, and are less likely to be expected to give gifts in meetings with tax inspectors.

Across regions, firms in Islamabad report the fewest visits by tax officials (one visit) and managers spend the least amount of time dealing with tax officials (6%). In all regions of Pakistan, at least 75% of firms ranked corruption less severely as an obstacle to daily operations in 2010 than in 2007. The Lahore region showed the greatest decline in the percent of firms reporting that they were expected to give gifts, 35% in 2010 compared to 54% in 2007.

In 2010, senior management from large firms spent about 15% of their time dealing with regulations, had about 6 six visits a year from tax officials, and 66% of large firms were expected to give gifts in these meetings. Compared to Afghanistan, large Pakistani firms have more visits and are more likely to be asked to give gifts. Although objective measures appear more negative in Pakistan than in Afghanistan, the improvements in subjective perceptions on corruption may be due to the fact that other elements such as electricity and political instability are much more severe in comparison. In other words, tolerance for corruption may have changed in light of the emergence of more urgent issues, and corruption appears relatively less problematic.[23]

(3) Financial flow problem

Since the global financial and economic crisis started in 2008, banks' exposure to public sector has been on a rise. This is on account of increase in government's reliance on banking sector to fund its deficits and is manifested in both advances and investment portfolios. The bank's investment in government bonds has increased by almost 34% to Rs2.8 trillion (June 2011: Rs2.1 trillion; June 2010: Rs1.4 trillion), over the last year. Apart from this, credit to government sector amounted to Rs479 billion (June-2011: Rs409 billion) at the end of June 2012. This was much lower at Rs133 billion at the end of June 2008. With 87% of the budget deficit of Rs1.1 trillion for FY2013 projected to be financed through domestic sources, exposure of the banking sector to public sector is expected to increase further.

While demand for public sector credit has remained strong in the backdrop of circular debt crisis and commodity financing needs, demand for private sector credit remained weak. The latter has remained stagnant at Rs2.92 trillion (June 2011: Rs2.92 trillion; June 2010: Rs2.75 trillion) at the end of June 2012. The slow growth in advances is reflective of slowdown in private sector credit demand, as well as a cautious stance taken by the banking sector, faced with rising non-performance.

From a commercial bank's perspective, exposure to government bond represents the best credit available in a domestic context (Government can always print money and repay them). Besides risk-free investments, these help generate healthy spreads given the ability of commercial banks to mobilize low cost deposits as enabled by increasing remittances and inherent money velocity. While this contributes to the phenomenon of crowding out of the private sector, the bank earns healthy spreads without having a concern of growth in non-performing loan and provisioning. Moreover, the banks also enjoy an advantage for capital adequacy ratio where government bonds have a zero risk weight as opposed to over 100% for certain loans. However, the ability of public sector to timely service its obligations other than treasury securities, as evident from repayment of independent power producers (IPPs), is dependent on future budgetary resources.

3.3 Requests Proposed by JPBCC and PJBF

In order to help achieve the targets of Vision 2030, the Japan-Pakistan Business Co-operation Committee (JPBCC) and Pakistan-Japan Business Forum (PJBF) submitted the "Joint Study Report for Vision 2030 of Pakistan" in May 2009.

[23]World Bank Group, "Business Environment Perceptions in Afghanistan and Pakistan, Enterprise Note No. 2 7", 2011

During the field survey, both suggestions and requests from Japanese side in 2009 had been confirmed through the interview survey. However, almost all issues were pointed out by key informants of foreign affiliated companies. This means that investment climate improvement has been almost no progress since 2009 to date.

Table 3.3.1: Issues and Requests for Achievement of Vision 2030

Sector	Current Issues	Requests Proposed by the Japanese Side
Manufacturing Sector	Manufacturing sector will have to grow faster than other sectors and increase its share in GDP. This section discusses two industries in particular - one that is resource intensive and the other is technology-intensive. The former is the textile sector, while the latter is the automobile sector.	JPBCC specially focuses on the automobile sector, as a main vehicle for moving manufacturing sector on a large scale with higher value-addition. Pakistan's manufacturing sector must register annual average growth of close to 10% in the value-addition.
Automobile/ Motorcycle Sector	For a country of 170 million people, the car ownership rate in Pakistan is far below than that of China, Thailand, and other middle countries. As Pakistan approaches to a middle-income country, its own demands for automotive products will continue to grow. So far, Japanese companies suffer a serious blow because of under-invoicing particularly from China. Japanese side requests to establish tactics to resolve this unfair trade due to the imposition of federal excise duty (5%) and withholding tax at the time of car registration, consumer's demand for automobile is decreasing. Also, the appreciation in Japanese yen value and the depreciation of Pakistan rupee has increased the cost of production for the automobiles and therefore, the selling price. Additionally, the current high interest rate of borrowing has discouraged car loan facility, negatively affecting the overall market demand. One of the reasons for the slump in car sales in Pakistan is that the registration fee for new cars is expensive; for the 800 cc car, Rs7500 of registration fee and for the 2000 cc, Rs 50,000. Presently, less than three years old cars are allowed for import, but there are frequent revisions in the price setting (e.g., depreciation rate) and tax. Other countries have solid policies for the protection of domestic manufacturers (e.g., used car import is prohibited). Presently, no environment protection regulation is being applied. In order to save the environment, auto safety inspection and emission control regulations are necessary.	This demonstrates that the potential for growth of the automobile and its ancillary industry in Pakistan is significant. Because of the large size of the market, Pakistan also has the potential to acquire economies of scale in the industry that can lead to reducing its cost of production, and also export products from this industry and earn increasing foreign exchange for the country. Action to improve such unfair trade of motorcycles is being requested to the government. Japanese automobile and motorcycle companies requested for a revision in the taxation system on the auto industry. Also, withholding tax should be removed immediately. Japanese auto and motorcycle companies requested to introduce policy that gives preference and benefit to the domestic manufacturers. If these environment protection regulations are not introduced, there will be no replacement for over-age and old cars and will result in an issue of safety and environmental pollution. Therefore, consistent policy for environment safety needs to be introduced at the earliest.

Sector	Current Issues	Requests Proposed by the Japanese Side
Textile Sector	Pakistan is the fourth largest producer of cotton in the world. This resource base provides a comparative advantage to the local textile industry. Accordingly, textile is the backbone industry of Pakistan, contributing approximately 70% of national exports, 14% of GDP, and 50% of industrial employment. Strong initiative of government is required to promote higher value added products in textile industries, which further contributes to export, and to improve the quality of labor (inferior to Vietnam).	Pakistan needs to consider how to activate and expand its textile industry, which is one of the most important export drivers. For comparison, in Bangladesh for example, some apparel manufactures from Japan, USA, and EU have set up their offices with considerable numbers of buyers from each market. Pakistan is behind in this respect. Pakistan needs to formulate the national plan to develop textile industry, considering fundamental factors such as comparative advantages/ disadvantages. Further improvement of infrastructure would attract more foreign investment and buyers in textile industry.
External Factors (FDI/FTA)	The stock of FDI in Pakistan is roughly half of the world's average. This is caused by the (1) lack of judicial transparency, which brings social insecurity and (2) bureaucratic hurdles, namely red-taping and corruption. Concerning incentives, the government can lower the corporate income tax rate to 12.5%, as practiced in Ireland.	Expansion of trading opportunities and strengthening of investment will be accompanied by technical assistance and sharing of development experiences. Possibilities of signing free trade agreements (FTAs) with countries should be explored. The Vision 2030 is targeting to integrate the economy of Pakistan regionally and globally. The Vision 2030 will only be achieved by addressing the challenges of (1) education, (2) land reforms, (3) simplification of administrative procedures including one window operation, (4) normalization in law and order situation (including Pakistan image building), and (5) judicial efficiency and transparency.
Infrastructure	Infrastructure development is vital for effective business operation. A country lacking adequate infrastructure cannot attract significant amounts of FDIs in its manufacturing sector.	Infrastructure development has significant influenced on FDI and an important determinant that guide foreign companies in their choice of investment target. It would be suggested that the recognition on infrastructure conditions of the current industrial park, and the improvement of those as promised at the time of inviting new investment are essential prior to discussing the new special economic zone for Japan.
Power	Most serious and immediate bottlenecks to growth and investment come in the way of electrical energy shortages. Shortage in generation capacity is estimated at roughly 3500 MW. At times, operational capacity increases to more than 5000 MW when water levels are low. Energy is available at an increasing cost, especially for the industrial sector. The underlying reason for the present energy shortage in the country can be fairly attributed to the lack of planning over the last decade.	The issue can be addressed by considering two alternatives. Firstly, the more indigenous coal must be used to generate power. Currently, coal contributes 0.1% to the power generation of Pakistan. This should be increased up to 50% till the year 2030, which can possibly reduce the cost of power generation by 30-35%. Secondly, the hydro-power must be generated by the construction of dams. However, land registration issues hamper the development, thereby causing delays in the establishment of such projects. The government must address the issue of land registration.

Sector	Current Issues	Requests Proposed by the Japanese Side
Human Resources	The government may impose a special contribution specifically to human resources development (HRD) for industries. HRD is a key issue to be addressed on an immediate basis. For example, the lack of establishment of a Petrochemical industry in Pakistan has been a result of the shortage of trained and skilled manpower.	Pakistan's automotive industry needs a transition into a more high-tech based industry, and it faces serious challenges in terms of securing qualified human resources. The government should maintain certain budget allocation for education and vocation training, an example would be 7-8% in 2015 should be maintained.
Governance	A number of political analysts in and outside of Pakistan have argued that poor governance lies at the basis of a number of ills that affect Pakistan. There are essentially two elements, within which issues of governance can be addressed. One is the transparency of government decision-making. The other is appropriate and legitimate system of accountability for those who are engaged in unethical and corrupt practices.	In order to attain the targets of Vision 2030, Pakistan has to improve its governance. The government is expected to take serious action against corruption, which can be a barrier to fair competition of the business sector.

Source: "Vision 2030 of Pakistan, Joint Study Report"

Table 3.3.2: Questionnaire Survey Results in "JPBCC-PJBF" Joint Study

Categories	Results of Responses to the Survey
Reasons for investments in Pakistan	Six companies (38%) answered "as sales and service basis"
	Six (38%) responded with "as production basis"
	Five answered "other" (as representative office, investment company, agent, distribution basis, etc.)
Future business plans in Pakistan	Eight companies (50%) answered that their plans entailed "expansion, reinforcement, and development"
	As advantage, more than 80% noted Pakistan's "large population" and "big market scale"
	Following the above answers, respondents noted the factors of "geographic location" and "low competition"
Risks in establishing operations	Almost all respondents noted "political and social instability" and "security"
	Over half addressed "poor legal system", "poor infrastructure", and "poor supporting industry" with the majority of noting in multiple
	Two-thirds considered power supply to be "very important" and that power shortage and frequent supply failure result in significant problems to business operation
Labor market	Low-level workers can be secured (for construction) There are many who leave Pakistan in search for temporary jobs to the Middle East, and difficult to secure sufficient workers (for construction) Engineers tend to go to higher-wage countries such as America (for IT) There is a tendency for high-level engineers, executives, and senior managers to flow to European and American companies in Pakistan or in the Gulf countries
Promising industries	Many mentioned agriculture, food processing, textile, IT, infrastructure (power, water, and transportation), and automobile parts Because the skill levels of doctors and middle-range managers are relatively high, Pakistan should develop its pharmaceutical industry and increase exports to Central Asia and Africa
Expectation from Japanese Government	69% of respondents considered "customs duty reduction such as abolition of non-tariff barriers, etc.," as "important" It would be necessary also for Japan to make efforts. Expected efforts included "customs duty reduction", "acceptance of workers", and "expansion of ODA" and "HRD" were highly ranked as expectation

Source: Prepared by JICA Study Team based on "JPBCCA-PJBF Joint Study"

3.4 Problem–Solution Analysis

"Problem-Analysis & Solution-Action" was formulated and submitted by the Japanese side in collaboration with JACI, JETRO Karachi Office, and the JICA Investment Climate Advisor to BOI in February 2011. The proposal has been made to:

(i) Appoint a person responsible for the action plan as well as,
(ii) Promptly begin the coordination between the relevant ministries and agencies (see the table below).

The progress of the implementation of such action plans and measures are identified below, through interviews with the BOI, JACI, and the Advisor.

Table 3.4.2 and Table 3.4.5 are prepared by BOI and progress of issues is explained by these tables for the related stakeholders (In tables, ○ means "almost solved or completed", △ means "partially solved but not yet completed", and × means "not yet progress") .

Table 3.4.1: Requests for Improvement from Japanese Companies in Karachi (April 2011)

Sector	Requests
KEPZ	1) Improvement of security 2) Improvement of access to road, power, and water 3)Improvement of safety preventive system (fire hydrant and guard man) 4)Improvement of taxation and operational/administrative producers
Banking	1)Establishment of ODA special loan accounts in Japanese banks 2) Relaxation of banking regulations
Automobile industry	1)Improvement of security 2) Introduction of stable policy preferable to local mobile manufactures 3) Improvement of power/water supply 4) Improvement of taxation 5) Road expansion 6) Development of access road to Qasim Port 7)Establishment of export repayment system
Steel mill	1)Improvement of security 2) Road expansion 3)Improvement of import duties 4)Establishment of subsidy and relief scheme

Source: "Problem -Analysis & Solution-Action"

3.4.1 KEPZ (Karachi Export Processing Zone)

Table 3.4.2: Karachi Export Processing Zone

S/NO:1 SECTOR: KEPZ (=KARACHI EXPORT PROCESSING ZONE)					
NO	**REQUEST/DESCRIPTION**	**LATEST SITUATION**	**IMPACT**		**REMAINING ACTION**
1	RECOVERY OF SECURITY ① BULLET CASE-3 IN FACTORY ② GUNPOINT CASE ON COMMUTING ROAD	1-1 SECURITY POST W/GUARD MAN INSTALLED IN KEPZ **1-2 POLICE CHECK POST/OPENED IN H.CHOWKI (21/9/11)** **1-3 POLICE OFFICER (18)+PATROL CAR (1) ALLOCATED** **1-4 SECURITY CONTROL TIGHTENED THRU RANGER OPERATION FOR KARACHI IND. ZONE**	**1-1 KEPZ INSIDE SECURITY IMPROVED** 1-2 SECURITY OUTSIDE KEPZ/ NOW BETTER COMPARATIVELY 1-3 INSECURITY THREAT STILL UNAVOIDABLE	O	**1-1 GOS CONTINUE HIGH SECURITY OPERATION**
2	IMPROVE: ① ROAD ② INFRASTRUCTURE • ELECTRICITY • WATER	2-1 ACCESS ROAD FOR KEPZ (3.2KM) /INNOVATED & COMPLETED UNDER GOS FUND (20/3/11)	**2-1 IMPROVED:** **① TRAFFIC ACCIDENT/REDUCED** **② TRUCK OPERATION** **③ SECURITY LEVEL**	O	**2-1 INAUGURATION CEREMONY (13/4/'12)** 2-2 GOS/KMC/CONTINUE CORRECT ROAD MAINTENANCE
		2-2 CONNECTING ROAD (KEPZ-PQA) -PAK/STL 7.1KM)/SUPPORTED BY CVF(EOJ)/JICA 2-3 ABOVE CONNECTING ROAD/TO BE COMPLETED (APR'13)	2-2 EXPECTED: ① TTL ROAD CONNECTION COMPLETED ② GOOD FOR ALL INVESTORS IN IND. ZONE **→INV. FRIENDLY CLIMATE**	Δ	2-3 FOLLOW-UP PROCEDURE: ① PC-I ② APPROVAL ③ CONSTRUCTION ④ COMPLETION
		2-4 ELECTRICITY ① REPEATED NEGO. WITH KESC FOR PRIORITIZED ELEC. SUPPLY FOR MFG SECTOR ② L/SHEDDING SITUATION IMPROVED ③ 3-4HRS/D('11)→1HR/D('12) MIDNIGHT ONLY	**2-4 L/SHEDDING/DECREASED** **2-5 PROD. STABILITY MAINTAINED**	O	**2-4 GOS/CONTINUE FULL SUPPORT TO MFG SCETOR**
3	IMPROVE: ① SAFETY PREVENTIVE SYSTEM (PS) • FIRE HYDRANT • GUARDMAN	3-1 FIRE HYDRANT/INSTALLED 3-2 GUARD MAN/ALLOCATED 24HRS BASIS	**3-1 SAFETY PS/ESTABLISHED**	O	**3-1 GOS/CONTINUE FULL SUPPORT TO MFG SECTOR**
4	SOLVE: ① OPERATIONAL/PROCEDURE PROBLEM • DUTY FREE IMPORT • CUSTOMS RULES (C/CLEARANCE AFTER 3PM ONLY)	4-1 DUTY FREE IMPORT FOR OFC CAR NOW ALLOWED 4-2 CUSTOMS OFFICER/STATIONED IN KEPZ→NON STOP OPERATION	4-1 TOYOTA CAMRY 1 U/T IMPORTED FOR OFC 4-2 C/CLEARANCE NOW SMOOTHENED	O	**4-1 EPZ/CONTINUE FULL SUPPORT TO MFG SECTOR**
		4-3 M/C IMPORT FOR EPZA SHALL BE DUTY EXEMPTED BUT IS STILL LEVIED (OVER RS2M)→INFRA/CESS = 0.5% I/VALUE **4-4 YKK KEPT APPEALING TO AUTHORITY OVER 5 YEARS** **4-5 THIS CASE/NOW UNDER GOS/C.MIN FOR FINAL DECISION.**	**4-3 GOS FINAL APPROVAL ANXIOUSLY AWAITED** **4-4 IF SO ,EXPECTED:** **① KEPZ=TRUE DUTY FREE ZONE** **② KEPZ=TRULY ATTRACTED FOR ANY NEW INVESTOR**	X	**4-3 GOS/TO EXPEDITE FINAL DECISION BY E/MAR'12**

Source: BOI

(1) Recovery of Security

a) Problems/Requests to the Government

- Aerial firing in the neighborhood creates security concern in the area and factory. Three empty bullet shells were found inside the premises, one of which had pierced through the roof of the factory.
- Y-Company desired to have security check post near there factory;
- Most of the check posts inside KEPZ were without guard men, so proper security monitoring was not possible.
- Employee of Y-Company was robbed at gunpoint while coming to work in the morning on the public bus outside KEPZ. His cash money and cellphone were stolen during the incident.
- Investors pointed out security concern on the daily commuting route from home to office. They specifically pointed out trouble spots where they feel most insecure. Some of the trouble spots are Manzil Pump, Malir 15, Quaidabad, Dawood Chowrangi, and Bhains Colony.

b) Latest Situation/Impact

- Overall security inside KEPZ has improved substantially.
- Security outside KEPZ is comparatively better than last year.
- Even though the insecurity threat on the daily commuting route of investors and employees from Downtown Karachi to Port Qasim and nearby industrial zones is still high, the increase in patrolling of police and rangers at the trouble spots has improved the security.

c) Remaining Issues

- Regular coordination with KEPZ and Sindh police is needed to improve security and continue full support to the investors.
- Properly equipped policemen to conduct any rescue operation is lacking at the Sindh Police Force, mainly due to lack of resources and willingness.
- Sindh Government should continue security operation in Karachi.

(2) Improvement of Infrastrucure

a) Problems/Requests to the Government

- The road patch outside Y-Company factory was damaged and needed repair works and attention by KEPZA.
- The road outside KEPZ was designed to be two by two (2x2), that is, two lanes on each side, but only one side was operational (one lane for each way if traffic).
- Regular electric supply should be provided to factories inside KEPZ by the KEPZA with the help of Karachi Electric Supply Company (KESC).
- KEPZA should confirm efficient water storage and supply system for the factories inside KEPZ.
- Fire hydrant should be installed near Y-Company factory for any emergency operation.

b) Latest Situation/Impact

- Sindh Government approved funding for the rehabilitation and renovation of Mehran Highway (3.2 km) which is located near the access road to KEPZ. The Mehran Highway rehabilitation was completed and inaugurated on April 20, 2012 by the Chief Minister and Governor of Sindh.
- KESC has minimized load shedding during production hours. Load shedding situation has improved when comparing the situation in 2011 (three to four hours) to the current year 2012 (one to two hours) only at night time.
- Fire hydrant has been installed near Y-Company factory for any emergency operation.
- Proper road is now available for Y-Company factory management and employees inside KEPZ.
- Fully operational Mehran Highway has greatly reduced traffic congestion and accidents. At the same time security has been improved due to the proper road construction.
- The extension of the Mehran Highway (8 km) which will be funded by the Embassy of Japan will provide a short and quick access to Port Qasim for traffic from KEPZ and nearby industrial areas. At the same time, the new highway will provide an alternative route to the National Highway (N5), which was the only way to access Port Qasim.
- Productivity loss is minimized due to regular supply of electricity to the factories inside

KEPZ.

- Safety preventive system for better and secure environment is established inside KEPZ.

c) Remaining Issues

- Karachi Metropolitan Corporation (KMC) and KEPZA should maintain and continue timely maintenance of roads outside and inside KEPZ respectively.
- Load shedding normally decreases in winter times but during summer the duration of load shedding normally increases. Close coordination will be required between factories management and KEPZA for minimizing the load shedding during production hours in summer.
- Close coordination is a must between BOI and Sindh Government for the completion of proposed extension of the Mehran Highway and for future development projects.

(3) Operational/Procedural Problems

a) Problems/Requests to the Government

- According to the laws of KEPZ, foreign investor/company is entitled to import one car for the use of company top executive. Y-Company applied for import of duty free car, but due to long government procedures, the issue was pending with the KEPZA.
- Customs clearance office inside the KEPZ used to open after 3:00 pm, making it inconvenient for factories inside KEPZ for quick clearance of their goods. The deliveries to the customers were delayed due to this problem.
- Government of Sindh levied infrastructure cess (duty) equivalent to 0.5% on the import of machinery by the factories inside KEPZ. According to KEPZ rules and laws, the factories inside KEPZ are exempted from any duties and cess.

b) Latest Situation/Impact

- Y-Company successfully imported a Toyota Camry for their office use.
- 24 hours Customs Clearance Office is now operational inside KEPZ.
- Government of Sindh final approval on exemption of infrastructure cess on import of machineries inside KEPZ, is anxiously awaited by the investors.

c) Remaining Issues

- BOI is appealing to all concerned government executives to immediately resolve infrastructure cess levied on KEPZ by the Sindh Government.
- Close/repeated/continuous coordination with KEPZA is recommended on long-term basis.

3.4.2 Banking

Table 3.4.3: Banking

S/NO: 2 SECTOR: BANKING SECTOR					
NO	REQUEST/DESCRIPTION	LATEST SITUATION	IMPACT		REMAING ACTION
1	1 RELAX/DEREGULATE BANKING CONTROL:				
	① FOREIGN BANK/DISALLOWED TO USE PAID - IN CAPITAL FUND FOR LENDINGS	① STILL UNREALISED	1.BIZ CLIMATE/IMPROVED & NOW REINFORCED, IF REALIZED.	X	GOP/TO EXPEDITE FINAL SOLUTION
	② FOREIGN BANK/OBLIGED TO DEPOSIT INTEREST FREE A/C AT NBP OR PROVIDE GOP WITH BOND AS COLLATERAL	② STILL UNREALISED		X	
	③ FORWARD BOOKING FOR ALL IMPORTS FORZEN	③ FORWARD BOOKING SYSTEM/ RECOVERED (22/3/11)			
	→ LARGE SCALLED MFG. COS I.E. AUTO MAKERS ARE ALWAYS HAVING DIFFICULTIES FIXING MFG. COST THRU MATERIAL IMPORT			O	

Source: BOI

a) Problems/Requests to the Government

- Foreign banks are not allowed to use paid-in capital lending's by the bank to companies or customers inside Pakistan.
- Foreign banks have to open interest free account at the National Bank of Pakistan (Government Bank) or provide the Government of Pakistan security bond as a collateral for protective measure in response to any emergency situation (bank failure) with the foreign bank.
- Forward bookings to all imports were frozen by the Government of Pakistan. Therefore, large scale manufacturing companies had difficulties in fixing the cost for their imports through the bank.

b) Latest Situation/Impact

- Forward bookings to all imports is now opened by the Government of Pakistan.
- Manufacturing sector is able to fix the costs of imports. Now, the sector is able to take long-term financial decisions which can be beneficial to the companies.

c) Remaining Issues

- No progress has been observed on the issue of lendings by foreign bank through paid-in capital and on interest free account in the National Bank.

3.4.3 Automobile Industry

Table 3.4.4: Automobile Industry

S/NO:3 (1/2) SECTOR: AUTOMOBILE INDUSTRY

NO.	REQUEST/DESCRIPTION	LATEST SITUATION: SUZUKI/KHI	TOYOTA/KHI	HONDA/LHR	IMPACT		REMAINING ACTION
1	RECOVERY OF SECURITY: →SERIOUS FREQ. THREAT FOR: ①GUNPOINT ②RIOT ③TRAFFIC ACCIDENT ④PROTEST	ROBBERY CASE (2) AUG'11-(1) DEC'11-(1) STILL SERIOUS THREAT	STILL SERIOUS THREAT	1.BOMBING CASE/REDUCED ('10→'12) 2.FEW GUNPOINT CASE ONLY REMARKABLY IMPROVED	1.INSECURITY IS STILL NEGATIVE IMPACT FOR ON-GOING/ANY NEW INVESTOR 2.SECURITY LEVEL SEEMS COMPARATIVELY IMPRO-VED, BUT SHOULD BE FUR-THER IMPROVED.	X	1.GOP/TO FURTHER IMPROVE SECURITY SITUATION
2	ESTABLISH POLICY: → ①STABLE (CONSISTENT) ②STRATEGIC ③LONGER TERM ④LOCAL CAR DEVELOP-MENT ORIENTED	EXPECTATION TO GOP/BOI→CONVEYED TO EDB: 1. <u>ENCOURAGE DOMESTIC MARKET GROWTH</u> USED CAR IMPORT IS BOTTLENECK OF THE MARKET GROWTH ↓ AUTO POLICY FOR MARKET EXPANSION IS EXPECTED 2. <u>CONSISTENT AUTO POLICY</u> ① AIDP BY JUL'12:FLEXIBLE IMPLEMENTATION TO BE EXPECTED ② FAVOURABLE DUTY FOR NEW-ENTRIES: → FAIR TREATMENT TO BE NEEDED ③ BAN ON CNG KIT IMPORT OEM (PC): →IMPLEMENTATION TIMING TO BE REVIEWED			1.HEALTHY AUTO INDUSTRY /EXPANDED, IF REALIZED 2.PAK INDUSTRIAL FUNDA-MENTALS/GENERATED & REINFORCED, IF REALIZED	X	1.GOP/TO EXPEDITE SOLUTION
3	SOLVE INFRASTRUCTURE: → ①ELECTRICITY ②WATER ③GAS	PROGRESS:			1. IMPROVED FOR IND. ZONE	O	1.GOP/TO CONTINUE FULL ELE. SUPPLY
					1.BENEFIT FOR MFG. COS.	O	1.GOP/TO CONTINUE FULL SUPPORT
					1.GOOD FOR MFG. COS.	O	1.GOP/TO CONTINUE FULL SUPPORT

		SUZUKI/KHI			TOYOTA/KHI		HONDA/LHR	
ELE		'10	'11	'12(1-3)	'10	'12	'10	'12
	L/SHEDDING (HR)	2844	13478	O	4H/D	2H/D	10H/D→6H/D	
	PROD. DOWN RATIO (%)	2	7	O	N/A	N/A	N/A	
	UNPRODUCED UNITS	1400	6900	O	472	19 (?)	N/A	
	SO FAR IMPROVED/SUMMER MAY WORSE=Δ						IMPROVED=O	
WATER	FULL SUPPLY SINCE '92 FROM PAK STEEL				OK		BIT CONTAMINATED	
GAS	1.USE/DISALLOWED FOR 0700/SU-0700/MO (SSG) 2.C/M: MON/OPE 0725→0825				OK		OK	

S/NO:3 (2/2) SECTOR: AUTOMOBILE INDUSTRY

NO	REQUEST/DISCRIPTION	LATEST SITUATION	IMPACT		REMAINING ACTION
4	SOLVED TAXATION PROBLEM: → ① TURN OVER TAX (0.5% JUN'10)→(1.0% JUL'10) ② ADVANCE INCOME TAX (3% OF CKD VALUE) ↓ SERIOUS/NEGATEIVE IMPACT FOR CASH M'GMNT	1- THIS ISSUE HAS BEEN SENT FROM PAMA +PAARAM TO EDB 2- EDB IS NOW SCREENING/SOLVING THIS ISSUE TOGETHER WITH FBR 3- THIS ISSUE IS EXPECTED TO BE SOLVE PRIOR TO NEW BUDGET 2012 START → <u>BY E/APR'12</u>	1- BIZ. FRIENDLY TAX CLIMATE REALIZED, IF SOLVED 2- ENCOURAGE COS. TO SECURE STRATEGIC BIZ. PLAN, IF SOLVED	X	GOP/ TO EXPEDITE FINAL SOLUTION
5	SOLVE ROAD PROBLEM: → ① LANE 2 X 2→3 X 3 ② CONGESTION ↓ NAT. H/WAY (N5)=QAIDABAD - P/QASIM 12 KM	1- JICA TIED UP WITH BOI FOR F/S SURVEY →IND. ZONE CLIMATE IMPROVEMENT PAKISTAN 2- JICA EXPERT TEAM (JAPAN): →<u>APR'12</u>	1- LOG. & TRUCK OPERATION/ SMOOTHEND IF SOLVED 2- IND. ZONE CLMATE/ IMPROVED, IF SOLVED 3- SECURITY LEVEL/ IMPROVED, IF SOLVED	X	JICA/TO EXPEDITE F/S SURVEY
6	SET UP NEW ROAD: → RES. AREA (DHA) - PORT QASIM	1- JICA EXPERT TEAM (JAPAN) →<u>APR'12</u> 2- BEST SCHEME / TO BE ANALYZE/ FIXED B JICA EXPERT TEAM	1- TOTAL IND. ZONE CLIMATE/ IMPROVED IF REALIZED 2- IND. ZONE/BECOME ATTRACTIVE FOR ANY NEW INVESTOR	X	JICA/TO EXPEDITE F/S SURVEY
7	SET UP EXPORT BACK UP SYSTEM	1- PAMA/PAARAM REQUEST (EXPORT <u>USANCE 90 DAYS→180DAYS)→EDB</u> 2- EDB NEGOTIATION WITH FBR	1- EXPORT/ACCELERATED, IF REALIZED 2- FOREIGN CURRENCY/OBTAINABLE, IF REALIZED 3- INTERNATIOANL COMPETITIVENESS GENERATED, IF REALIZED	Δ	GOP/ TO EXPEDITE FINAL SOLUTION

Source: BOI

(1) Recovery of Security

a) Problems/Requests to the Government

- Investors pointed out security concern on the daily commuting route from home to office in Karachi. They specifically pointed out, trouble spots where they feel most insecure.
- Due to high congestion when the car stops at these trouble spots in Karachi, armed gunmen mostly on motor bikes approaches the car with pistols and demand for cash and

cellular phones. They also take all the handy/carry able items such as laptops with them.

- During any protest or riot, the National Highway (N5) in Karachi, which is the frequent commuting road of investors and employees going to work usually is closed to traffic.
- In case of emergency, there is almost no counter measure. Police is very slow to mobilize and the worst congestion in Karachi makes their job even harder.

b) Latest Situation/Impact

- Increase of patrolling by police and rangers at the trouble spots identified by the investors especially during morning and evening rush hours has improved the security situation on the commuting way from downtown Karachi to Port Qasim.
- Even though the insecurity threat on the daily commuting route of investors and employees from downtown Karachi to Port Qasim and nearby industrial zones is still high, the increase in patrolling by police and rangers at the trouble spots has some what improved the security situation.

c) Remaining Issues

- Regular coordination with Sindh Government Police is needed to continue full support to the investors.
- Properly equipped policemen to conduct any rescue operation is lacking at the Sindh Police Force, mainly due to lack of resources and willingness.
- The Sindh Government should continue security operation in Karachi with full dedication.

(2) Establishment of Policies

a) Problems/Requests to the Government

- Long-term, consistent, and investor's friendly policies are missing from the Government of Pakistan.
- Government failed to implement their policies.
- Local automobile industry oriented policies are missing from the government sector. Used car imports are damaging to the local auto industry.
- Favorable duties for new entrant/investor are missing for auto sector.

b) Latest Situation/Impact

- Ten years corporate tax holiday for new investors will help the government in attracting new investors to Pakistan.
- Government new auto policy will be announced in the coming months. Favorable duties for auto sector will help the investors in making future investment decisions.

c) Remaining Issues

- Government has banned used car imports for commercial purposes, but used cars are imported for personal use. The local industry is suffering from influx of used cars imports. At the same time, government is losing revenue from allowing the used car imports.

(3) Betterment of Infrastructure

a) Problems/Requests to the Government

- The expansion of the National Highway (N5) from two by two to three by three lanes (2x2→3x3) is immediately required due to increasing congestion.
- Over head bridges are required on certain points of the National Highway (N5) in order to avoid congestion areas.
- New highway is required for investors and commuters heading to work from the residence in DHA-7 to Port Qasim.
- Although the power shortfall is a national issue and crisis. Government should provide maximum electric supply to manufacturing industries, especially in the production hours. Load shedding schedule should be fixed with consultation with the manufacturers and unscheduled load shedding should be avoided.
- Government should take immediate and true steps in resolving electricity crisis.
- Gas load shedding is another crisis faced by the government, it is also negatively effecting the production and cash flows of the manufacturing companies.
- Stable and clean water supply is needed for the manufacturing companies.
- Improvement of access road is needed from Lahore downtown to B-Company factory.
- B-Company has applied for gas connection for their factory but no progress.

b) Latest Situation/Impact

- Production has increased and maintenance cost has decreased due to improve electric supply in Karachi.
- New flyover will improve traffic conditions on the National Highway (N5) in Karachi.
- Newly renovated road to B-Company factory has improved logistic operation.

c) Remaining Issues

- Government has told that they have insufficient funds for the improvement of the National Highway (N5) expansion and renovation from Quaidabad to Pak Steel Cross-section.
- Government has told that they have insufficient funds to build the flyover on the National Highway.
- Government should seriously consider resolving the electricity and gas crisis.
- Gas connection to B-Company factory in Lahore is still pending with Punjab Government.

(4) Solve Taxation Problems

a) Problems/Requests to the Government

- Government increased turnover tax from 0.5% to 1.0% from July 2010. The turnover tax is paid on total sales of the company, even if the company has negative profitability. The manufacturing sector demands abolishment of turnover tax on stock exchange listed companies. The government has failed to timely refund the excess tax collected by the auto companies on turn over tax payments.
- Automobile sector request the government to abolish the advance tax (3%) on imports of complete knock down (CKD) auto components from different countries.

b) Latest Situation/Impact

- Although BOI requested the government to abolish turnover tax, but the reduction from 1.0% to 0.5% will help auto sector in moving towards stable financial operations.

c) Remaining Issues

- Government has not taken any action on BOI appeal for abolishment of advance tax. BOI is consistently appealing the government to resolve this issue on urgent basis.

3.4.5 Steel Mill

Table 3.4.5: Steel Mill

S/NO:4 SECTOR: STEEL MILL					
NO	**REQUEST/DISCRIPTION**	**LATEST SITUATION**	**IMPACT**		**REMAINING ACTION**
1	RECOVERY OF SECURITY →SERIOUS FREQUENT THREAT FOR: ①GUNPOINT ②RIOT ③TRAFFIC ACCIDENT ④PROTEST	1.SECURITY INSIDE IND. ZONE/OKAYED 2.DAILY COMMUTING: ①NO SERIOUS THREAT SO FAR ② UNDER JEEP W/GUARD MAN **GUNPOINT/ROBBERY CASE WITH NAT. STAFF=1 (9/3/'12)**	**1.SECURITY/MAINTAINED** **2. INSECURITY THREAT /STILL UNAVOIDABLE**	O	**1.GOP & GOS/CONTINUE TO IMPROVE SECURITY SITUATION**
2	SOLVE ROAD PROBLEM: → ①LANE 2X2→3X3 ②CONGESTION	1.NAT H/WAY (N5) PJ: ④JICA TEAM FOR FS SURVEY (APR'12) **SERIOUS NEED FOR DOUBLE DECKED HIGHWAY**	1.F/S SURVEY/DELAYED **2.F/S SURVEY EXPECTED TO SPEED UP**	Δ	**1.JICA TEAM DISPATCH** **2.FIX MOST APPROAPRIATE H/WAY PLAN, & REALIZE**
3	SOLVE I/DUTY PROBLEM: → ①10%→5% (JUL'11) ②NEGATIVE IMPACT ③LOCAL INVESTOR NOT PROTECTED	1.BOI'S REPEATED NEGOTIATION WITH FBR, EDB & M/PROD (JUL'11-FEB'12) 2.EDB ACCEPTED FINAL JUSTIFICATION SUMMARY, & WILL NEGOTIATE WITH FBR **3.GOP FINAL DECISION IS EXPECTED E/APR'12**	**1.HEALTHY INVESTORS GROWTH/SECURED, IF REALIZED** **2.STEADY CONTRIBUTION TO PAK ECONOMY/ REALIZED,IF REALIZED**	X	**1.GOP/FINAL DECISION**
4	SET UP SUBSIDY/RELIEF SCHEME → ①RS DEVALUATION-30% (UP) ②COST UP/EXTRA CASH FLOW REQUIRED ③PROJECT DELAYED OVER 1 YEAR ↓ **①NO TIMELY RELIEF BY GOP** **②DISCOURAGE INVESTOR**	1.NO SUBSIDY/RELIEF SCHEME FOR ELIGIBLE INVESTOR	1.SAME AS ABOVE	X	**1.GOP/GENERATE BEST RELIEF SCHEME.**

Source: BOI

(1) Recovery of Security

a) Problems/Requests to the Government

Same as mentioned in the automobile sector.

b) Latest Situation/Impact

Same as mentioned in the automobile sector.

c) Remaining Issues

Same as mentioned in the automobile sector.

(2) Betterment of Infrastructure

a) Problems/Requests to the Government:

Same as mentioned in the automobile sector.

b) Impact

Same as mentioned in the automobile sector.

c) Remaining Issues

Same as mentioned in the automobile sector.

(3) Solve Import Duty Problems

a) Problems/Requests to the Government

- Due to lack of domestic production of cold rolled coils (CRC) and increasing demand, the government had reduced duty on import of cold roll coil from 10% to 5% in July 2011. The step was justified, as the government intended to protect the public from paying higher prices for cold roll coil.
- Now C-Company has started producing quality cold roll coil with the enough capacity to fulfill domestic demand. Therefore, the government should increase import duty on cold roll coil, so that the local industry could be protected from cheaper and low quality imports.

b) Latest Situation/Impact

- The issue is still pending, although the Engineering Development Board (EDB) might send a proposal to the Federal Board of Revenue (FBR) for increment of the import duty from 5% to 10% on CRC coils.

c) Remaining Issues

- True protection and encouragement of local industry will be realized, if the government increases the import duty.

(4) Setup Subsidy/Relief Scheme

a) Problems/Requests to the Government

- During the last few years the Pakistani currency has substantially devaluated against foreign currency. Therefore, the cost of investment has increased fourfolds, which makes it harder for investors to arrange additional finances for the completion of the factory. C-Company project was delayed for over one year due to devaluation and inflation in Pakistan.
- C-Company requested the government for subsidy or relief scheme which can help the suffering investors in time of financial crisis.

b) Latest Situation/Impact

- Government has no enough funds or willingness to implement such relief scheme for investors.

c) Remaining Issues

- BOI will repeatedly negotiate with the government for long-term investor friendly strategy and ideas

Chapter 4 Issues Identified from the Interview Survey

4.1 Introduction

The Study is focused on the industrial activity in Karachi. In this regard, the JICA Study Team carried out a survey to collect information on companies with respect to their characteristics, business activities, security of business operation, legal and regulatory environment, access to and processing of information, status of infrastructure and its improvement, administrative procedure and facilitation for FDI and management issues of companies. Furthermore, the survey also covered the living environment issues of foreign and local employees.

The survey was carried out in May 2012. The sample consisted of 25 multinational and joint-venture companies. These companies represented highly diversified nationalities of the world. About 80% of the sample included companies from the USA, Europe, South East Asia, and Middle East Asia, while 20% of the sample comprised of Japanese firms only.

These companies operated in various locations of Karachi. However, 68% of the companies sampled in the survey were located within industrial zones under the operation of KEPZA and PQA. The majority of the companies in the sample were old establishments. More than 40% were established during the 1970s and 1980s, while 33% started their operation in the 1990s. Around 63% in the sample were privately-owned companies, while 21% were publicly-listed companies.

The production operation of the companies in the sample survey was widely diversified. Their products included apparel, pharmaceutical, chemicals, engineering and electronic items, metal and plastic products. However, about 20% in the sample were textile producing companies. It is found in the survey that the availability of raw materials and domestic market were the main reasons, among others, that made companies invest in Karachi. In this connection, more than 83% in the sample mentioned that they had been successful according to their investment plans.

It was found that the companies in the sample have arranged various security measures such as installation of closed-circuit television (CCTV) cameras, security guards and escorts. In this regard, they were also concerned with the law and order situation. However, about 90% in the sample did not find themselves under threat. On the other hand, foreign employees working in companies in the sample felt relatively less secured in their capacity as compared to local organizations. These observations demonstrated the existence of security and law and order in the city, which is highly important.

Although companies were relatively satisfied with the facilities and services offered by KEPZA and PQA, in general, they showed large discontent towards the role of government institutions and other regulatory bodies. This is true when firms were confronted with different problems and issues, such as poor infrastructure, provision of utilities, access of information, administrative procedures for FDI approval, and other management issues. The satisfaction in the investment, dissatisfaction with the law and order situation, and discontent with the role of the government and other regulatory bodies in the attraction of investment and operation of companies need to be taken as a serious note in order to improve the investment climate in Karachi and other parts of the country as well. It requires more efficient government institutions in delivering their tasks, good governance and consistent policies in order to create an enabling environment for more FDI and better business opportunities in the country.

The questionnaire used also addressed various issues about the living environment for foreigners and locals working in the sampled companies. These included security, housing, commuting, food, healthcare, education, leisure and entertainment. The data in the sample demonstrated that foreigners take all these issues seriously, therefore, it cannot be ignored and must be addressed.

4.2 Issues of Investment Climate Identified in the Interview Survey

The purpose of this chapter is to identify the various issues faced by the foreign companies operating in Karachi and suggests the most efficient and practical solutions. For this, however, it was not considered necessary to conduct a study from the ground up as this had already been conducted in the past, i.e., the problem-analysis and solution-action, which served the same purpose. Therefore, the discussion on the information collected from the survey was a confirmation of that study and should be construed accordingly.

4.2.1 Outline of the Company`s Activities in the Proposed Site (Section A)

The proposed site is situated in the vicinity of Port Qasim and KEPZ. PQA was established through an act of parliament on June 29, 1973. The port was established following the site selection of Pakistan Steel Mills in 1972. The site development is still under progress, and even after four decades since its establishment, the functional performance remains inefficient. The port is under the administrative control of the Ministry of Ports and Shipping, Government of Pakistan. The chairman serves as the chief executive of the port. All policy decisions are vested in the PQA board comprising seven members headed by the Chairman of PQA. The board is composed of individuals from the public and private sectors. PQA is primarily a service-oriented organization. The port provides shore-based facilities and services to international shipping lines and to other concerned agencies. These services are in the form of adequate water depth in the channel, berths, terminals, cargo handling equipment, storage areas and other facilities for safe day and night transit of vessels. [24]The condition of the industrial site is not very good particularly due to infrastructure issues like water supply. It is highly needed to improve the road network in the industrial area, and to stabilize industrial power and water supply. Furthermore, the industrial area is far from the residential areas of Karachi City. However, the industrial site has been recognized to be promising based on the cluster of steel and automobile sector. Despite this, the inefficient performance of the Pakistan Steel Mill, the automobile industries located in the cluster imports raw material like steel rolls and pressed parts.

The KEPZ, which is situated in the same industrial area, was established in 1980. The Export Processing Zones Authority is a Pakistan government venture conceived and designed to increase and improve the exports of the country. Its main objectives are to accelerate the pace of industrialization in the country and enhance the volume of exports. These objectives will promote an environment for investors to initiate export-oriented projects in the Zones which would, as a corollary, create job opportunities, bring in new technology and attract foreign investments. It is one of the fast-growing projects undertaken by the Pakistan government and is appealing for both local and overseas investors.[25]

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[24] Port Qasim Authority, http://www.portqasim.org.pk
[25] Export Processing Zone Authority, http://www.epza.gov.pk

Out of the 25 companies selected for the interview survey, nine were located in KEPZA; eight were located in PQA; two were located in Landhi Industrial Area; two in Bin Qasim Industrial Area; while the remaining three were in Sindh Industrial Trading Estate (SITE), West Wharf, and along M.T. Khan Road, respectively. Both KEPZA and PQA are industrial hubs in Karachi followed by Landhi, SITE, and West Wharf. M.T. Khan Road is not an industrial area but is home to the head offices of several companies. Table 4.2.1 shows the distribution of the companies where the sample survey was carried out.

Table 4.2.1: Location of the Surveyed Companies

Location	**KEPZA**	**PQA**	**Bin Qasim**	**Landhi**	**West Wharf**	**SITE**	**M. T. Khan Road**	**Total**
Number	9 (36%)	8 (32%)	2 (8%)	2 (8%)	2 (8%)	1 (4%)	1 (4%)	**25 (100%)**

Source: JICA Study Team
Note: Figures in parentheses are percentage of the total sample.

The companies were randomly selected from the lists provided by KEPZA and PQA. Initially, only the companies in KEPZA and PQA were to be interviewed, but due to the lack of foreign companies in these locations, companies outside these areas were chosen. Majority of the samples were in KEPZ and PQA because the proposed site will be situated in the same vicinity. Therefore, more accurate and realistic information about business environment can be gathered from the firms operating in the same area.

The primary criterion, for the selection of the companies surveyed, was their origin or affiliation, i.e., they were either FDI or joint ventures. The secondary criterion was the type of industry, i.e., they should belong to the manufacturing sector. Though the primary criterion was met in all cases, the secondary criterion was not possible in every case, due to either the reluctance of companies to invite the JICA Study Team or the unavailability of relevant personnel.

The companies belonged to or had joint ventures with the following countries are listed in Table 4.2.2.

Table 4.2.2: Nationalities of the Surveyed Companies

Country	**Number of Companies**	**Country**	**Number of Companies**
Japan	5 (20%)	Malaysia	1 (4%)
Hong Kong	2 (8%)	South Korea	1 (4%)
Taiwan	2 (8%)	Switzerland	1 (4%)
The Netherlands	2 (8%)	UK	1 (4%)
UAE	2 (8%)	USA	1 (4%)
France	1 (4%)	Others	5 (20%)
Germany	1 (4%)	**Total**	**25 (100%)**

Source: JICA Study Team
Note: Figures in parentheses are percentage of the total sample.

As exhibited in Table 4.2.2, companies originating from Japan accounts for 20% of the total sample, followed by Hong Kong, Taiwan, the Netherlands, and UAE occupying 8% each. While the remaining 4% were composed of one of each from France, Germany, Malaysia, South Korea, and Switzerland, United Kingdom, and USA.

The sample size and type of industries included companies from different sectors as shown in Table 4.2.3. Textile and apparel accounts for 20%; followed by chemicals and chemical products, and automobile at 12% each. Due to the limited sample size, there were companies from other sectors having only a single representation in the sample size. Other companies included were light engineering works, Guar Gum (a thickening powder used in the textile industry for printing purposes) manufacturing, edible oils, terminal services, and marble products.

Table 4.2.3: Types of Industry of the Surveyed Companies

Type of Industry	No.
Apparel	5
Coke and Refined Petroleum Products	1
Chemicals and Chemical Products	3
Basic Pharmaceutical Products and Pharmaceutical Preparations	2
Rubber and Plastic Products	1
Basic Metals	1
Fabricated Metal Products, except Machinery and Equipment	1
Computer, Electronics, and Optical Products	1
Electrical Equipment	1
Automobile (Motor Vehicles, Trailers, and Semi-trailers)	3
Edible Oils	1
Guar Gum	1
Light Engineering Works	1
Marble Products	1
Other Manufacturing	2
Total	**25**

Source: JICA Study Team

Some of these companies have been doing business since the independence of Pakistan and, over the period, have become very well established in the country. Those who started as small businesses became large companies and those who started off as small manufacturing units became large manufacturers. The pharmaceutical industry in Karachi is the best example of this. They started small and gradually expanded their businesses to cater to not only the domestic but also the international markets. Table 4.2.4 distributes the number of companies in the sample according to the year of establishment

Table 4.2.4: Year of Establishment of the Surveyed Companies

< 1979	1980s	1990s	2000s	**Total**
7 (28%)	3 (13%)	8 (33%)	6 (25%)	**24** **(100%)**

Source: JICA Study Team
Note: Only 24 out of 25 responded, figures in parentheses are percentage of total.

Around 75% of the companies in the sample started their operation before the year 2000.. It was found in the survey that those who invested in the early 90s were the most successful.

The ownership pattern of the companies selected in the sample survey varies. Around 63% of the companies in the sample were privately-owned while another 21% were publicly-listed. As for the remaining companies, three were under sole proprietorship while one was under a partnership, as shown in Table 4.2.5.The distribution of ownership have similar patterns that have been found in the enterprise surveys, which was carried out by the World Bank. The high number of privately owned companies is due to the freedom in fast decision making, especially in the areas where there is uncertainty in terms of security and government policies. They are not supposed to take any approval or permission for their business, as public-listed companies do from their shareholders. Large corporations may have a large board of directors, with a number of officers and shareholders. Therefore, large corporations have to undergo votes by all shareholders to decide on corporate initiatives.

Table 4.2.5: Registration Status

Publicly-listed	**Privately-owned**	**Sole Proprietorship**	**Partnership**	**Total**
5 (21%)	15 (63%)	3 (13%)	1 (4%)	**24 (100%)**

Source: JICA Study Team
Note: Only 24 out of 25 responded, figures in parentheses are percentage of total.

In response to the question about the investment reasons in Karachi, 25% of the companies stated that the investment in Karachi is lucrative and the domestic market size is large. That is why the 40% of the surveyed firms were wholly domestic-oriented, while 20% were both domestic- and foreign-oriented. The rest sees the foreign market as their main destination. Since Karachi is a natural seaport, importing raw material is much cheaper than any other part of Pakistan which was the reason why five companies invested in this city. Three companies said they invested because of cheap labor, made possible because of the city’s enormous population; while ten said it was because of the possibilities of expansion, duty free imports in certain areas, availability of land at low costs, and close proximity to the port. The reasons stated in the investment decision highlights the potential of the city of Karachi, which is considered as the regional hub and potential gateway to Central Asian countries, and also provides strong and long-standing links between the Middle East and South Asia. Second, the reasons corroborate the importance of the city population, which not only potentially offers large market but also a source of huge working force. One of the key examples is foreign investment in the automobile sector currently targeting almost wholly the domestic sector. Table 4.2.6 lists the reasons for investing in Karachi.

Table 4.2.6: Reasons for Investment in Karachi

Availability of Raw Material	Domestic Market	Export to Neighboring Countries	Export to Home Country	Cheap Labor Cost	Other	**Total**
5 (21%)	6 (25%)	0 (0%)	0 (0%)	3 (13%)	10 (42%)	**24 (100%)**

Source: JICA Study Team
Note: 24 out of 25 responded, figures in parentheses are percentage of total.

Despite the current law and order situation of the city, out of 24 companies, 20 are operating their businesses successfully as per their initial plans, while four have not been as successful. Some companies in Karachi have shown excellence in adapting with their contingency plans, which ensure their survival. On the other hand, there were a few who were ready to wind up. This entails that majority of the respondents were optimistic about their businesses as well as outlook of country’s economy.

The results were very encouraging and in accordance with the OICCI, where more than 70% of the respondents were willing to invest further in the next few years. According to such optimistic view, a significant contribution is expected in GDP growth, which will stimulate employment opportunities. Table 4.2.7 describes the success of business as per investment plans.

Table 4.2.7: Success of Business as per Investment Plans

Yes	No	**Total**
20 (83%)	4 (17%)	**24 (100%)**

Source: JICA Study Team
Note: Figures in parentheses are percentage of total. Only 24 out of 25 responded.

4.2.2 Security (Section B)

Out of 24 companies, 22 companies were not victims of any acts of terrorism or other crimes during the past one year. However, the incidents of mugging and snatching of valuables at gunpoint were very high. Such incidents have become so common in Karachi that people residing there do not seem to be alarmed, as they now seem to consider this to be part of Karachi's way of life.

This fact conforms to the findings of the Enterprise Survey result, where 5% or fewer respondents consider crime, theft, and disorder a major business environment obstacle. Furthermore, crimes like theft, robberies, vandalism, and arson in Pakistan costs less than 0.5% of their sales as compared to 1.3% in low income countries.[26] Also, people usually do not even report such incidents to the local police, due to their inefficient way of working and bad behavior. Table 4.2.8 counts the victims of crimes and terrorism in Karachi.

Table 4.2.8: Victims of Acts of Terrorism or other Crimes

Yes	No	**Total**
2 (8%)	22 (92%)	**24 (100%)**

Source: JICA Study Team
Note: Figures in parentheses are percentage of total. Only 24 out of 25 responded.

In contrast to this, among the challenges to business identified in the survey results of the OICCI, law and order is considered as the biggest challenge. Nonetheless, this confirms the current study as different countermeasures have been taken to ensure the safety of employees within the office premises, the most common being the hiring of private security guards. Majority of the surveyed companies, or 12 out of 23, have taken this measure while five considered security precautions to be a wasted effort, based on the frequency of crimes in Karachi. There was, however, no or very little security provided for employees outside the work area. Only the most senior executives were provided with security escorts who ensure the safe travel to and from work every day.

Table 4.2.9 shows the type of security measures adopted by the surveyed companies.

[26] World Bank, "Enterprise Survey",2011

Table 4.2.9: Protection Available for Staff

Security Guards	Security Escorts	CCTV	Insurance	Zone Protection*	No Protection	**Total**
12 (52%)	2 (9%)	3 (13%)	0 (0%)	1 (4%)	5 (22%)	**23 (100%)**

Source: JICA Study Team
Notes: Figures in parentheses are percentage of total. Only 23 out of 25 surveyed companies responded.
* protection provided by the industrial zone.

Out of all the industrial areas, only KEPZA and PQA provide appropriate security measures to the companies within their premises. However, this security is only limited within their boundaries. Beyond the areas, company personnel must take their own precautions. For this service, KEPZA charges the occupants for export processing zone, a rate of 0.5% service charges on freight on board (FOB).

Half of the companies surveyed stated that the cost of security is high, while the other half stated it to be low. Regarding protection against natural disasters, several companies have their own disaster management and rescue teams. The companies routinely carry out drills to deal with unforeseen events such as earthquakes, fires, and floods.

One of the respondents at the PQA indicated their plan to designate pickup points in the city for employees, from where onwards security guards would escort them to the company and back.

A number of foreign workers proposed the establishment of an enclave for foreigners only where can live with their families, work and have recreational facilities so that they do not need to travel far within the city.

4.2.3 Legal/Regulatory Operations (Section C)

The study revealed various problems faced by various companies. Among the companies surveyed, 13 indicated that the current deteriorating law and order situation as the main issue that requires governmental support; whereas seven companies requested an improvement in the time duration for which policies are implemented. Four of the companies suggested that the environment of business activities must be made positive by improving the company-government relationship through various departments. These departments include the customs, Karachi Metropolitan Corporation, or the department of the government responsible for the development and maintenance of Karachi’s infrastructure. The residential areas where foreign employees live should likewise be improved. The complete list of requests is provided in Table 4.2.10.

Table 4.2.10: Support Needed from the Government

Support/ Improvement Requested from the Government	No. of Requests
Adequate Security Measures	1
Better Supply of Utilities (Electricity, Water, and Gas)	2
Branding of Pakistani Products to Promote Recognition	1
Consistent Policies for Longer Periods	7
Cooperation from FBR	1
Elimination of Corruption	1
Fulfillment of Contractual Obligations	1
Improvement of Law and Order Conditions	13
Lift Ban on the Import of CNG* Kits	1
Limit the Import of Used Vehicles	1
Lower Cost of Doing Business	1
Ministry of Health Should be Revived	1
Open Trade with India	1
Positive Environment for Business Activities	4
Reduced Import Duties	1
Strengthening of the Police	1
Tax-Free Incentives for All Industrial Areas	1
Training of Workers	1
No Support Required	2
Total	**42**

*Compressed natural gas
Source: JICA Study Team

Over 50% of the respondents in the study confirmed the deteriorating law and order condition as the biggest challenge. Similar results can be seen in the Perception and Investment Survey 2011 by OICCI, where 80% of the respondents were concerned with the law and order conditions.

About 60% of the companies surveyed denied receipt of any substantial support from the government. They complained that available basic facilities are not adequate. Over 50% of the responses reveal dissatisfaction with the services provided to them by government and government industrial authorities. Two companies, however, stated the basic facilities they get, such as the security provided by KEPZA and PQA, are excellent (please refer to Table 4.2.11). It was observed that the companies located in KEPZA and PQA get better facilities than the companies in other industrial areas. Three of these companies were quite satisfied with the managements of their areas, which entails relatively poor services as only 12.5% of respondents commented positively on the competency of management at KEPZA and PQA. Two companies indicated the duty-free import policies of KEPZA to be highly favorable in promoting investment climate. However, this benefit is limited to KEPZA only, whereas companies in the other industrial areas also indicated their wish to have such policies. In terms of support provided to industrial sectors, absence of industrial support programs like seminars and events felt as only one respondent commented on it.

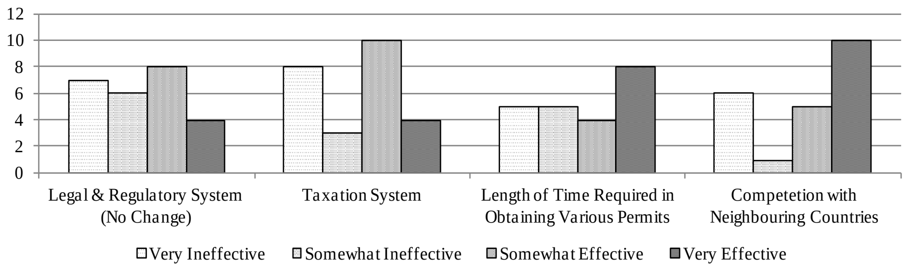
These results corroborate with the survey results of the OICCI, where about 53% of respondents think that the government and government authorities are incapable of resolving issues faced by investors.

Table 4.2.11: Support Provided by the Government

Support Provided by the Government	No. of Responses
Competent Managements at KEPZA and PQA	3
Consistent Supply of Industrial Gas	1
Duty-Free import and Export in KEPZA	2
Higher Duties to Import CBU	1
Inappropriate Support	13
Industrial Support Programs (Seminars, Events etc.)	1
Security by KEPZA and PQA	2
Tax Exemption	1
Total	**24**

Source: JICA Study Team
Note: Figures in parentheses are percentage of total

The respondents were asked which factors may affect their business; the factors listed in Figure 4.2.1 are divided into four categories. Almost 50% of the respondents who responded to this question considered legal and regulatory system important and affective for their businesses. Effectiveness of the taxation system to business has relatively moderate implications, as about 32% considers it ineffective, while 40% considers somewhat effective. Over 50% of the respondents revealed that obtaining permits for business is efficient and effective, while only 23% stated this mechanism very ineffective and inefficient. Competition with neighboring countries considered very effective by about 46% of the respondent, while 22% considered it as somewhat effective to their business.



Source: JICA Study Team

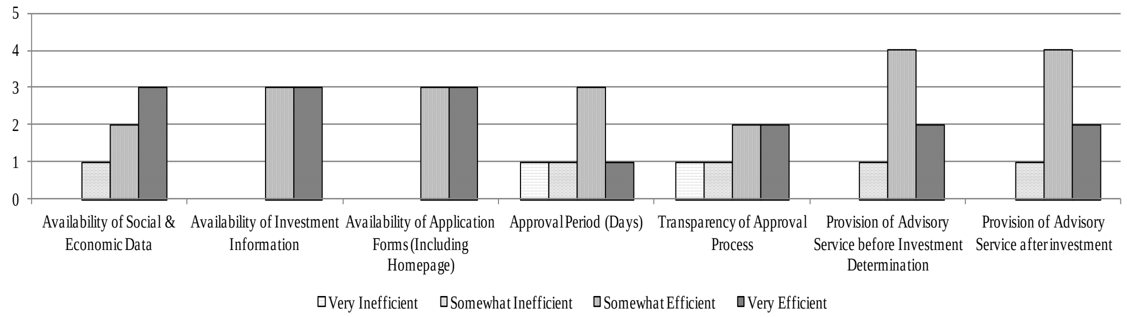
Figure 4.2.1: Factors Affecting Business

4.2.4 Access to Information on Investment Climate and Market (Section D)

The prime responsibility of the BOI is to promote domestic and foreign investment, enhance Pakistan's international competitiveness and contribute to its economic and social development. However, the prevailing perception about the BOI is that they only assist in processing the visas of foreign employees. Due to this incorrect perception, most of the companies surveyed had never even considered approaching them for assistance.

The respondents stated that the BOI must change their attitude and the way they are perceived by foreign and local businessmen. They need to promote their existence along with the services they offer. For this, suggestions were made for them to devise and implement better marketing strategies. As per the suggestions from interviewed respondents, this could require BOI to publish small brochures, leaflets, etc. in Urdu and English as well as other languages, the speakers of which were deemed to be potential investment partners.

Figure 4.2.2 shows the efficiency of the BOI when contacted regarding specific queries by the companies surveyed. In most cases, companies received efficient response for their queries. However, response rate to their opinion on efficiency of the BOI were considerably lower, as only 24% of the surveyed companies responded to the question. An important thing to note here is that only about 17% of the respondents rated the approval process, i.e., approval period and transparency of approval process, as "very inefficient". On the other hand, about 50% of the respondents positively admitted the availability and accessibility to information was very efficient. This category includes availability of social and economic data, investment information and application forms.



Source: JICA Study Team

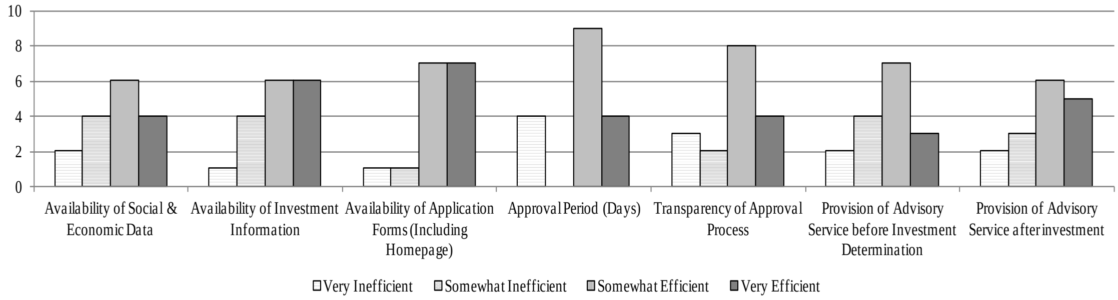
Figure 4.2.2: Efficiency of BOI when Contacted

Regarding the role and response of business associations in their respective industrial zones, most of the companies stated their interaction with the association of their industrial zones was usually positive. Companies in KEPZA and PQA appear to be more satisfied than the other areas, due to their proactive way of working. Companies in the other areas, where the survey was conducted, were also contented with the efficiency of their areas' associations, but not at par with their expectations.

About 64% of the respondents answered the question on the efficiency of industrial services by respective industries zones, i.e., KEPZA and PQA. On an average, only 12% of the total respondents, showed dissatisfaction and rated the services as "very inefficient", while over 30% of respondents rated the services of the respective industrial organizations as very efficient. The latter was also supported strongly as about 44% respondents considered the services as somewhat efficient, together with this the satisfaction level considered as efficient accounted by 75% of the respondents. On the financing services, only 28% of the respondents considered it as very important.

These can be easily linked to the findings of World Bank's Enterprise Survey where only 10% to 15% of the firms use external financial services. Also, it was found that, on the average, about 85% of the working capital requirement is financed through internal sources of firms in Pakistan. As stated in the explanation, most of the firms use banks for checking and business transaction purposes. While the less number of firms take loans or have line of credit from banks.

Figure 4.2.3 shows the efficiency of the various industrial area associations, when contacted regarding specific queries, by the companies surveyed.

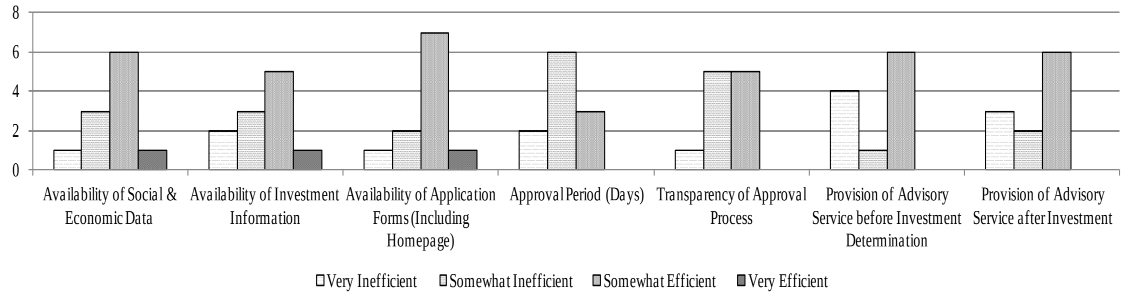


Source: JICA Study Team

Figure 4.2.3: Efficiency of the Industrial Zones when Contacted

The majority of the companies surveyed indicated that the attitude of the government, when contacted for support is somewhat efficient; and this category accounts for about 54% of the total responses. Details of the queries and the number of responses in their favor can be seen in Figure 4.2.4. The figure reveals that the response of the government offices when contacted for various issues is satisfactory and efficient.

Results are also in line with the indicators of ease of doing business in Karachi by IMF and World Bank, where Karachi City ranked third amongst the 13 cities of Pakistan. Despite the fact that about 10 procedures are required to start a new business in Karachi, as compared to the seven procedures in South Asia, the average number of days per procedure comes out at 4.5, which is considerably better than other South Asian Countries. Also, in the World Bank Enterprise Survey, on inquiries about delays in days when businesses require licenses and permits for their establishments, it is found that Pakistan is in better position in terms of delays in obtaining import license and operation license in South Asian regional and low income countries. While construction related permits have considerable less number of delays in terms of days in Pakistan as compared to other selected group of countries.



Source: JICA Study Team

Figure 4.2.4: Efficiency of the Government Departments when Contacted

4.2.5 Countermeasures on Poor Infrastructure (Section E)

Basic infrastructure is one of the most important prerequisites for a company, to operate successfully. This includes the availability of good roads and an ample supply of water, gas, and electricity. Unfortunately, due to several reasons, this basic infrastructure is limitedly available or at some places not available to the industries in Pakistan, due to which they are suffering tremendously.

For this reason, companies have attempted to become adaptable accordingly. For example, for the shortage of electricity, companies have purchased their own power generators. For the shortage of water, they have had their own wells dug. And where there is limited gas, they have started using liquefied petroleum gas (LPG). These measures, though effective in maintaining steady production lines, also result in high production costs, making it difficult for them to compete in the local as well as international markets.

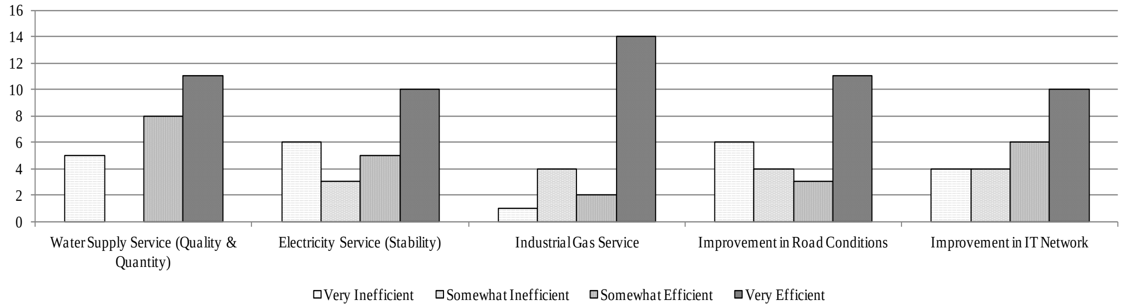
According to some respondents, due to these costs, several companies have moved their production facilities to Sri Lanka and Bangladesh. It is because of the reason that Bangladesh has been given tax-free access to 37 countries including the European Union, Canada and Australia. This is one of the key reasons why a large number of Pakistani textile units have relocated in recent times to this one of the largest deltas of the world with a population of over 142.32 million. In this regard, the Textile Minister Makhdoom Shahabuddin also believes that the main reason behind the shifting of textile industry to Bangladesh were not because of electricity, gas outages, and power tariffs in Pakistan, but due to the preferential treatment of Dhaka for the European Union and the United States. [27]

Based on the study conducted, the only area in Karachi where companies were not dissatisfied by the lack of infrastructure is KEPZA. KEPZA provides a consistent supply of electricity, water, and gas to all the industries located within its premises and maintains good road conditions. Furthermore, there has been an agreement between KESC and KEPZA of no load shedding. The grid station of KEPZA was donated to KESC. PQA, on the other hand, is unable to provide electricity to all of its occupants due to the limitations imposed by KESC on power loads. Water, gas, and road maintenance, on the other hand, are taken care of by PQA, in a more efficient manner.

As per the survey, the condition in other industrial areas is not so good. Electricity outages and gas load shedding are frequent, while the supply of water is limited. The relevant associations, not being government authorities like KEPZA and PQA, are therefore unable to influence the responsible authorities to maintain the steady supply of the required utilities.

About 45.8% of the respondents rated the water supply services in their respective industrial areas as very efficient; while only 21% said their respective areas are very inefficient. Almost similar results were attributed with variations of ±5%, respectively for electricity services by the respondents. For water supply, there were only three out of the total 21 respondents who have taken some countermeasures to avoid any inefficiency of water supply by the authorities. This supports their high satisfaction for the said services. On the other hand, the moderate satisfaction level, or about 68% of the respondents has alternate and standby arrangement for failure of electricity services. The major source for this is in terms of power generators. For industrial gas services, there were no such countermeasures observed as almost 67% stated that the services of their respective industrial estates to be very efficient. Only 5% of the respondents reported their respective estates to highly inefficient in terms of supplying industrial gas. For the improvement of road services within the industrial estates, about 25% of the respondents showed dissatisfaction and rated the service as very inefficient. The efficiency of the utilities and infrastructure, as per the respondents, can be seen in Figure 4.2.5.

[27] Mir Shakil-ur- Rahman, The News, 30th, May 12



Source: JICA Study Team

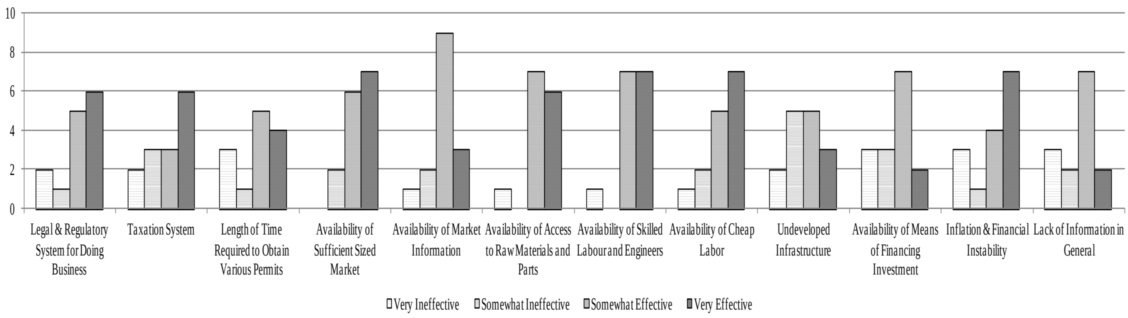
Figure 4.2.5: Efficiency of Utilities and Infrastructure

4.2.6 Administrative Procedures for FDI Approvals (Section F)

As mentioned earlier, BOI is responsible for assisting companies in obtaining visas only. Based on the views of several respondents, there is a dire need to correct and clarify this, and build positive image. Various means of promotion must be undertaken, which could include brochures, leaflets, and newsletters. Also, maintaining an up-to-date website and participating in the national as well as international trade fairs will help promote BOI.

The administrative procedures for FDIs, as per most of the respondents, in response to most of the queries in the survey, were either very efficient or somewhat efficient. However, a very few respondents felt that these procedures were very or somewhat inefficient.

On an average, on survey queries of factors which may affect the business of respondents, only 56% of the respondents answered. Of this, about 36% stated these factors or supports as very efficient; while about only 15% stated the services on these factors by BOI / government as very inefficient. Details of all the queries posed, the type, and the number of responses can be seen in Figure 4.2.6.



Source: JICA Study Team

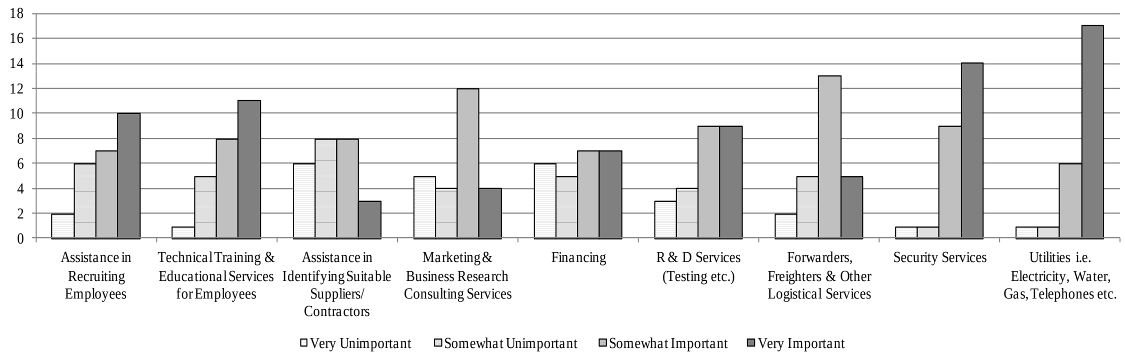
Figure 4.2.6: Factors that Affect Business Activities

4.2.7 Management Issues (Section G)

Besides all the government and legislation related matters, a very important aspect of operating company is the management related issue, which cover recruitment, training, identification of suppliers, marketing, finance, research and development (R&D), logistics, security, and utilities. When asked about these matters, most of the respondents stated that the services related to them were either very, or somewhat important. The highest number of respondents indicated that the utilities were the most important while the second majority prioritized security. Almost all respondents have responded to the queries in this section.

In the OICCI survey, there was an almost unanimous response that electricity, information technology, and telecommunications are critical to doing business. There is an urgent need to solve and manage the ongoing power crisis which has become a threat to business operations and the economy as a whole. The OICCI survey also explains about three biggest challenges, i.e., law and order, energy supply, government, and political instability.

On a similar pattern, responses in the investment climate survey reveals that the most important concern of the responding companies were the utilities, followed by security and training of human resources. The most important category in which respondents need improvement for their businesses was the utility services, which cover 68% of the total sample. About 56% of the respondents marked security services as highly important, entailing the lack of implementation of law in the city. The details of the responses to all the queries can be seen in Figure 4.2.7.



Source: JICA Study Team

Figure 4.2.7: Importance of Improvement in the Services Received from the Government

4.3 Issues of Living Environment Identified from the Interview Survey

4.3.1 Living Environment of Foreign Employees

The living environment of foreign employees is an important consideration of foreign-affiliated companies that are operating or will operate in Karachi. Therefore, the following items regarding the living environment of foreign employees were studied:

- Security;
- Commuting;
- Housing;
- Food;
- Health care;
- Education for children;
- Relationships with neighbors;
- Convenience of life; and
- Overall living environment

(1) Respondents on the Living Environment

As shown in Table 4.3.1, a total of 13 foreign-affiliated organizations, mainly companies in the KEPZ and PQA, were surveyed through personal interviews with a questionnaire. The respondents were members of the management. Out of the 13 respondents, 11 were Japanese since many of the interviewed foreign-affiliated companies did not have foreign employees, primarily for security reasons.

Table 4.3.1: Number of Respondents on the Living Environment of Foreign Employees by Area

	KEPZ	Bin Qasim	Others	Total
Number of Respondents	2 (15%)	4 (31%)	7 (54%)	13 (100%)

Source: JICA Study Team
Note: Figures in parentheses are percentage of total.

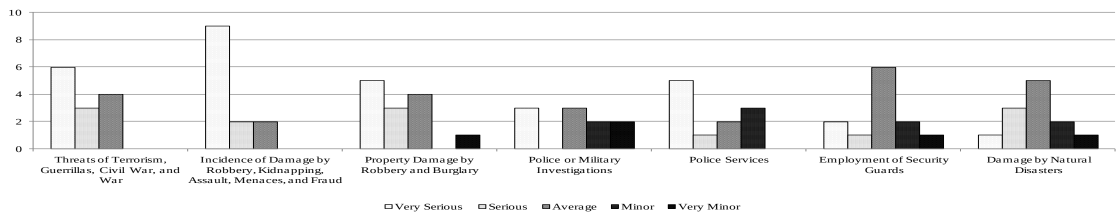
(2) Foreign Employees' Views on Security

The lack of security in Karachi poses a serious threat to foreign employees. As shown in Figure 4.3.1, six out of the 13 respondents viewed threats of terrorism, guerrilla activities, civil war, and war as very serious concerns. Terrorism is a grave threat, but crimes faced in daily life are a more acute problem as nine of the 13 respondents cited losses from robbery, kidnapping, assault, menaces, and fraud. During interviews, many respondents pointed out about the growing incidence of crimes, especially robbery at gunpoint. To prevent such crimes, some foreigners use four-wheel drive vehicles with window tints escorted by an armed guard. Property damages by burglary and robbery was also perceived as serious. Five and three of the 13 respondents regarded the issue on security as very serious and serious, respectively. A few of them showed that they carried an extra mobile phone and purse, and an inexpensive watch so that they could be easily given in case of robbery at gunpoint to alleviate higher property loss.

Police and military investigations were perceived as a very serious concern by three out of the 10 respondents; while four regarded it as minor and very minor. Five of the 11 respondents answered that problems related to police services were very serious. Respondents indicated that the police were unreliable, taking longer time, and unnecessary money to work on cases.

It seems usual for foreign employees to hire security guards, but their employment is not a very serious problem. Six out of 12 respondents considered it as an average issue.

Natural disasters such as floods and droughts occasionally affect Karachi. Five of 12 respondents rated their damages as average.



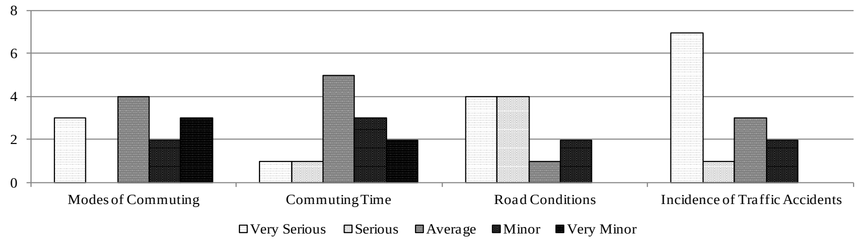
Source: JICA Study Team
Note: Multiple answers to one question were considered invalid.

Figure 4.3.1: Foreign Employees' Views on the Severity of Security Problems

(3) Foreign Employees' Views on Commuting

Figure 4.3.2 shows the severity of problems concerning commuting. The modes of commuting are not a grave problem for many respondents as four out of 12 respondents regarding average; two as minor; and three as very minor. The modes of commuting were a minor problem largely because foreigners travel by private car. Similarly, commuting time was rated as average by five out of 12 respondents.

In contrast to commuting modes and time, road condition was a serious concern. Four respondents perceived road conditions as very serious, while another four regarded it as serious. The construction of flyovers and toll roads, extension of the Mehran Highway to Bin Qasim, and increase in the number of lanes from two to three lanes were suggested for improvement. The incidents of traffic accidents were also a considerable concern, considered very serious by seven out of the 13 respondents.



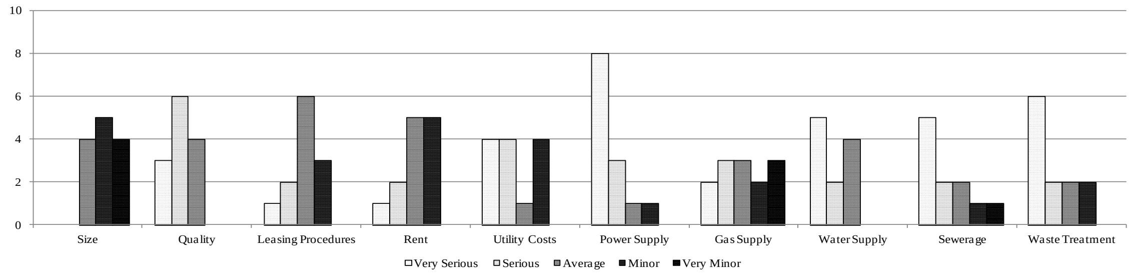
Source: JICA Study Team
Note: Multiple answers to one question were considered invalid.

Figure 4.3.2: Foreign Employees' Views on the Severity of Commuting Problems

(4) Foreign Employees' Views on Housing

As shown in Figure 4.3.3, all the 13 respondents saw the size of their residences as an average or minor problem. By contrast, the quality of house is a severe problem since three and six out of 13 respondents regarded it as very serious and serious, respectively. Leasing procedures and rents pose less serious problems. Six out of 12 respondents rated the severity of problems about leasing procedures as average. Meanwhile, five respondents regarded rents as an average problem while another five perceived it is a minor problem.

Amongst housing problems, problems concerning public utilities are the worst. A total of eight of the 13 respondents said that utility charges were a serious problem while four perceived it as minor. The high utility cost is attributable to expensive electricity. Electricity also causes a very acute problem of supply, which was perceived by very severe and severe by 11 of the 13 respondents. There are frequent power cuts and it is usual to have generators at home. Gas supply is not as serious as electricity supply largely because Sindh has gas fields and prioritizes gas distribution. On the other hand, water supply gives a very serious problem to five respondents and a serious problem to two. The examples of problems about water supply include no water supply, purchase of water from tankers, and poor water quality. Likewise, sewage and waste treatment were rated as very serious by five of 11 respondents and six of 12 respectively.

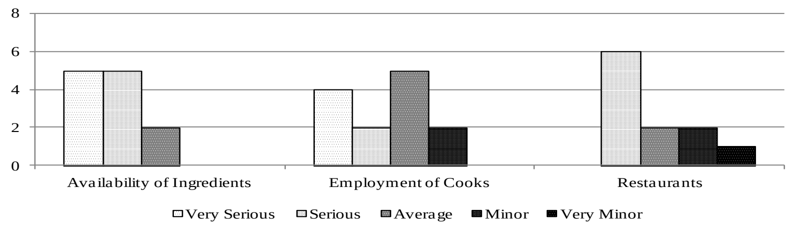


Source: JICA Study Team
Note: Multiple answers to one question were considered invalid.

Figure 4.3.3: Foreign Employees' Views on the Severity of Housing Problems

(5)Foreign Employees' Views on Food

As shown in Figure 4.3.4, five out of 12 respondents have serious concern about the availability of ingredients. Problems lie in the limited availability of seasoning and the poor quality of raw food such as vegetables and meat. The employment of cooks was a relatively serious problem. Five out of the respondents regarded the issue as average whereas four viewed it as very serious. Restaurants were a very serious problem to six out of 11 respondents. Limited good restaurants and poor hygiene were given as examples of problems.



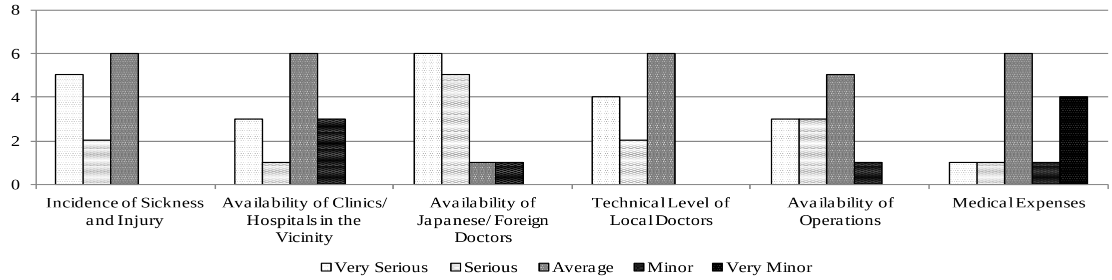
Source: JICA Study Team
Note: Multiple answers to one question were considered invalid.

Figure 4.3.4: Foreign Employees' Views on the Severity of Food Problems

(6)Foreign Employees' Views on Health Care

As shown in Figure 4.3.5, six out of 13 respondents rated the incidence of sickness and injury as an average issue; while five regarded it as very serious. Six out of the 13 respondents responded that problems regarding the availability of clinics and hospitals in the vicinity were average. Meanwhile, the availability of foreign doctors was a very serious issue. Six and five of the 13 respondents perceived this problem as very serious" and serious, respectively. In absence of foreign doctors, there is no choice but to see a local doctor. Six out of 12 respondents expressed that the technical level of local doctors was of average concern. In case of serious sickness and injuries, operations may be needed. Six of 12 respondents expressed very serious or serious concern over the availability of operation, while five rated it as average. Respondents expressed that they did not want to have operations in Pakistan.

Medical expenses are somewhat a minor problem. Six out of the 13 respondents rated the cost as average while four perceived it as very minor. Interviews revealed that medical expenses in Karachi were not high.

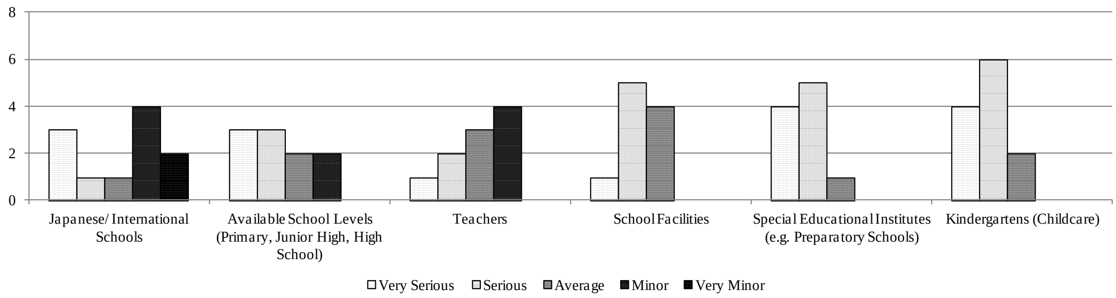


Source: Study Team
Note: Multiple answers to one question were considered invalid.

Figure 4.3.5: Foreign Employees' Views on the Severity of Health Care Problems

(7) Foreign Employees' Views on Education for Children

Figure 4.3.6 below shows that four out of 11 respondents rated problems about international schools as minor whereas three regarded the issue as very serious. Three respondents opined that the availability of school levels was a very serious problem, while another three regarded it as a serious problem, respectively. Teachers were viewed as a minor problem by four of 10 respondents while school facilities as a serious problem by five of 10 respondents. The critical problems about education are special educational institutes, such as preparatory schools and kindergartens. Nine of 10 respondents rated the former as very serious or serious, whereas the figure for the latter stands at 10 out of 12 respondents.

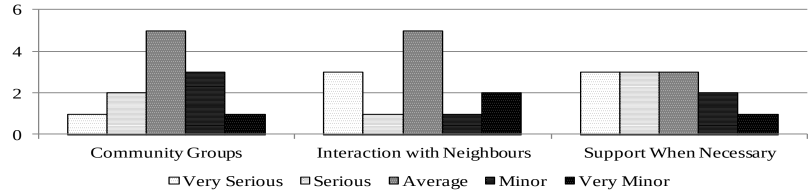


Source: JICA Study Team
Note: Multiple answers to one question were considered invalid.

Figure 4.3.6: Foreign Employees' Views on the Severity of Problems of Education for Children

(8)Foreign Employees' Views on Relationships with Neighbors

Figure 4.3.7 shows that problems with regard to community groups were not of major concern, which was viewed as average by five out of 12 respondents. Similarly, five out of 12 respondents stated that the severity of problems about interaction with neighbors was average. Support from neighbors when necessary was of deeper concern. Out of 12 respondents, three perceived it as very severe, while another three said it was severe.

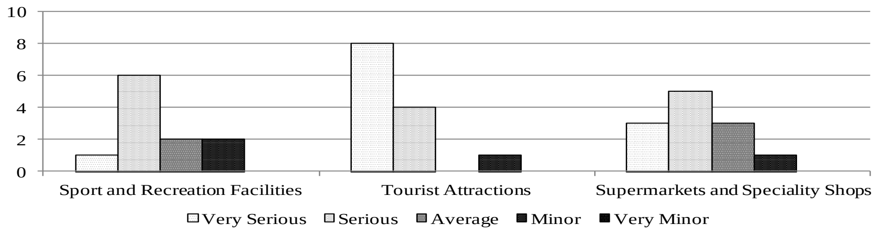


Source: JICA Study Team
Note: Multiple answers to one question were considered invalid.

Figure 4.3.7: Foreign Employees' Views on the Severity of Problems of Relationships with Neighbors

(9) Foreign Employees' Views on the Convenience of Life

As shown in Figure 4.3.8, six of 11 respondents opined that sports and recreational facilities were a serious problem. There are limited facilities such as golf courses and gyms at hotels. Tourist attractions were more of serious concern. Out of the 13 respondents, eight and four perceived their problems as very serious and serious, respectively. The availability of super markets and specialty shops were also of serious concern. Out of 12 respondents, five and three perceived their problems as very serious and serious, respectively. Furthermore, shopping malls and specialty shops do not have fine and wide selection of goods.

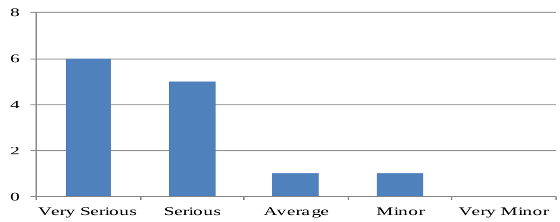


Source: JICA Study Team
Note: Multiple answers to one question were considered invalid.

Figure 4.3.8: Foreign Employees' Views on Recreational Facilities and Convenience of Life

(10) Foreign Employees' Views on the Overall Living Environment

As a whole, Karachi is not a pleasant environment for foreign people to live in. As shown in the figure below, as many as 11 out of 13 respondents rated the overall living environment as very serious or serious.



Source: JICA Study Team

Figure 4.3.9: Foreign Employees' Views on the Severity of Overall Living Environment

4.3.2 Living Environment of Local Employees

Security and commuting of local or Pakistani employees were direct concerns since their problems can negatively affect the business of companies. Therefore, security and commuting of local employees were studied.

(1) Respondent on the Living Environment of Local Employees

As shown in Table 4.3.2, a total of 24 foreign-affiliated companies, mainly those in the KEPZ and Bin Qasim, were surveyed through personal interviews with a questionnaire. The respondents were Pakistani management familiar with the living environment of local employees.

Table 4.3.2: Number of Respondents on the Living Environment of Local Employees by Area

	KEPZ	Bin Qasim	Others	Total
Number of Respondents	8 (33%)	5 (21%)	11 (46%)	24 (100%)

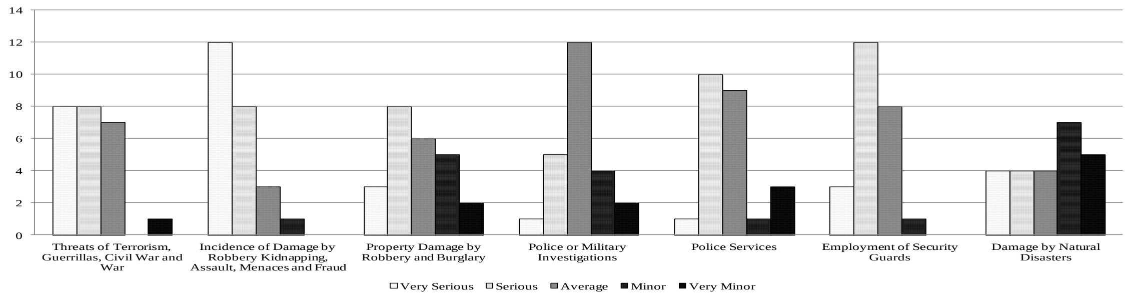
Source: JICA Study Team
Note: Figures in parentheses are percentage of total.

(2) Local Employees' Views on Security

As is the case with foreign employees, respondents expressed great concern over the security situation in Karachi. Figure 4.3.10 shows that eight respondents rated threats of terrorism, guerrilla activities, civil war, and war as very serious, while another eight regarded them as serious. The incidence of damage by robbery, kidnapping, assault, menaces, and fraud was a more severe issue. Out of the 24 respondents, 12 perceived it as a very serious problem. Respondents indicated that the incidents of mugging were increasing within the city. Employees were at high risk while commuting, especially when robbery at gunpoint happen in long traffic jams. Property damage due to robbery and burglary was a serious problem for eight out of 24 respondents.

Police and military investigations were viewed as average by 12 respondents. The perception on the problems on police services was rated as serious by ten out of the 24 respondents, whereas nine rated it as average. Most of respondents stated that they were reluctant to interact with the police due to lengthy procedures with no outcome. It was also pointed out that despite the daily occurrences of snatching and robberies, the police do not take appropriate action. Therefore, they are expected to take action against crimes efficiently and effectively.

Damage by natural disasters was considered minor and very minor by seven and five respondents, respectively, out of the 24 respondents.



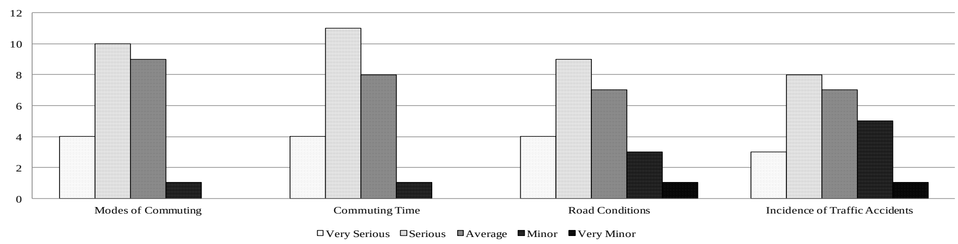
Source: JICA Study Team

Figure 4.3.10: Local Employees' Views on the Severity of Security Problems

(3) Local employees' views on commuting

Figure 4.3.11 shows that 10 out of the 24 respondents regarded the modes of commuting as a serious problem. Some respondents provided transport for their employees. The employees of other respondents depended on private vehicles and public transport. Some respondents indicated that public transport is of poor quality and should be upgraded. Commuting time was also a serious problem, which was rated as serious by 11 out of the 24 respondents. It was pointed out that despite the fact that flyovers were recently constructed in Shahra-e-Faisal, the average commuting time remained the same as it was before.

Road conditions are very bad. Nine out of the 24 respondents perceived this issue as serious. Respondents were of the opinion that roads were improved but needed further improvement. The poor maintenance and repair of roads created avoidable traffic jams. Therefore, the appropriate maintenance and repair of roads as well as the strict enforcement of traffic rules were suggested for improvement. Traffic accidents are also a serious issue, viewed as serious by eight out of the 24 respondents.



Source: JICA Study Team

Figure 4.3.11: Local Employees' Views on the Severity of Commuting Problems

Chapter 5 Identification of Priority Issues and Policy Matrix for Investment Climate Improvement in Karachi

5.1 Priority Issues

Pakistan urgently needs to find out ways and means to promote the expansion of its dynamic market-based economy. This study is an attempt to identify issues and suggest measures to promote industries by means of improving industrial infrastructure and the living and working environment. Industrialization could be achieved through the simultaneous acceleration of the social sector, particularly the strengthening of the middle class. The latter would provide equal opportunities in society and would result in improved law and order conditions. This would also lead to the development of a sustainable society.

No policy is meaningful or goal-oriented unless it is effectively implemented. Industrial promotion is profoundly related to other policy issues and its success hinges on certain policies. These include trade policy, human resource development policy, environment policy, and urban development policy along with the most needed infrastructure policy. Pakistan lacks a strong policy-making body that integrates such a variety of policies.

This chapter is based on the analysis of Chapters 2 to 4. It recollects all the problems and issues identified by various international studies and the JICA Study Team's own interview surveys at KEPZ and PQA in Karachi. It identifies priority issues to be solved and suggest a policy matrix as solutions to the priority issues.

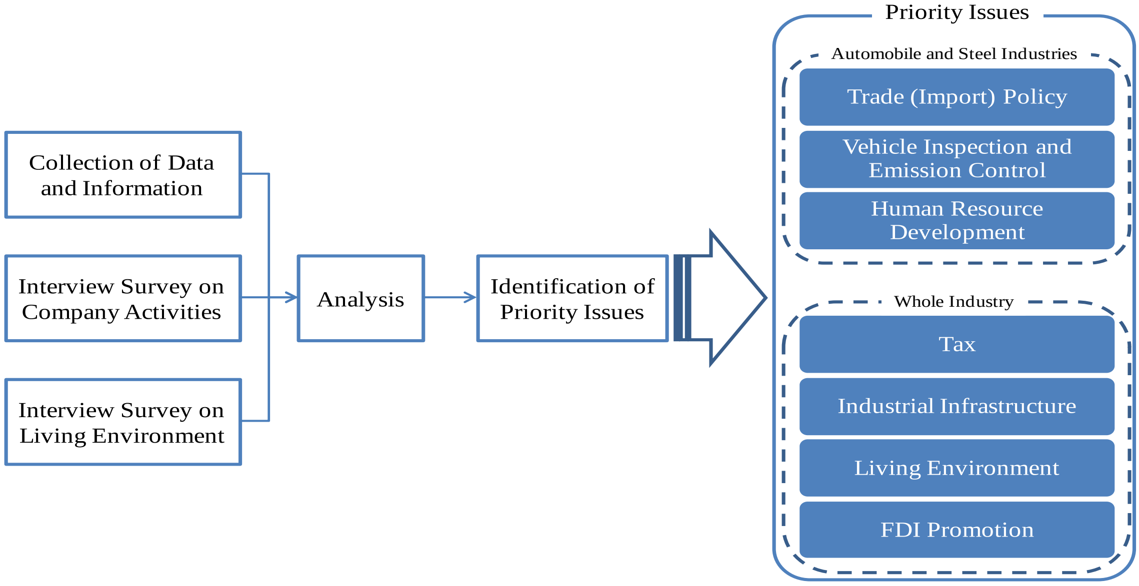
5.1.1 Process to Identify Priority Issues

To identify priority issues, the JICA Study Team interviewed foreign companies in Karachi about their business activities and living environment and analyzed issues of the investment climate in light of the following preceding studies:

Since May 2010, JICA has dispatched an Investment Climate Advisor to BOI to analyze issues of the investment climate in Pakistan and suggest and implement concrete solutions for improvement in investment policy and institutions. Under the initiative of the Advisor, "Problem-Analysis and Solution-Action" was submitted to BOI, which included issues concerning the investment climate and suggestions to solve them.

Priority issues were identified in view of suggestions for improvement in the investment climate in Pakistan by the World Bank in their "Doing Business" and "Enterprise Survey" and industrial associations such as JPBCC, PJBF, and OICCI.

Consequently, priority issues identified are seven: Trade (import) policy; vehicle inspection and emission control; human resource development; tax; industrial infrastructure; living environment; and FDI promotion and approval and trade procedures. They are categorized into two groups, namely 1) issues with big impacts on the development of and the promotion of FDI in the automobile and steel industries and 2) issues with impacts on the promotion of FDI in the whole industry, as shown in Figure 5.1.1.



Source: JICA Study Team

Figure 5.1.1: Process to Identify Priority Issues and their Categories

5.1.2 Rationales for the Identification of Priority Issues with Big Impacts on the Automobile and Steel Industries

Priority issues of the automobile and steel industries are 1) trade (import) policy; 2) vehicle inspection and emission control; and 3) human resource development. Below are the rationales for the identification.

(1) Trade (Import) Policy

The issue of import policy was raised in "Problem-Analysis and Solution-Action" and also in the interview survey during this study.

(2) Vehicle Inspection and Emission Control

The development of vehicle inspection and emission control was suggested in the JICA Project for the Automobile Industry Development Policy in 2011. Moreover, the development of the automobile industry is national policy.

(3) Human Resource Development

Human resource development for the automobile industry was suggested in the JICA's Project for the Automobile Industry Development Policy and was also requested in the interview survey. Moreover, the automobile industry has a broad base of supporting industries and can create employment opportunities.

5.1.3 Rationales for the Identification of Priority Issues with Impacts on the Whole Industry

Priority issues of the whole industries are 1) tax; 2) industrial infrastructure; 3) living environment; and 4) FDI promotion. Below are the rationales for their identification.

(1) Tax

The issue of taxes was raised in "Problem-Analysis and Solution-Action", "Doing Business", the OICCI's report and also in the interview survey.

(2) Industrial Infrastructure

The issue of industrial infrastructure was raised in "Problem-Analysis and Solution-Action", "Doing Business", the OICCI's report and also in the interview survey.

(3) Living Environment

The issue of the living environment was raised in "Problem-Analysis and Solution-Action" and also in the interview survey.

(4) FDI Promotion

Strengthening BOI functions and powers and the minimum investment size in special economic zones (SEZs) were identified as issues in consultation with the Investment Climate Advisor. Improvement in EPZA services was suggested in "Problem-Analysis and Solution-Action" and was identified as an issue in consultation with the Advisor.

5.2 Issues with Big Impacts on the Automobile and Steel Industries

5.2.1 Trade (Import) Policy

(1) Import Duty

(1) Current Situation

Pakistan has a long history of inward-oriented import substitution policies, which protect the domestic industry. However, trends have been changed significantly with the liberalization of trade regimes by tariff cuts. The general maximum rate of custom duties which was higher at 65% in 1996/97 was significantly reduced to 25% in 2002/03[28]. However, the figure rose again to a maximum of 35% in 2008. In 2012/13, the general maximum rate of custom duties was again reduced to 30%. Accordingly, tariff rates on complete built up (CBU) motor vehicles units were reduced from the 75-150% range to the 50-75% range in 2005/06 and a further proposed

[28] World Bank. 2006. "Pakistan: Growth and Export Competitiveness." (http://siteresources.worldbank.org/INTRANETTRADE/Resources/Pakistan_DTIS_Apr06.pdf).

reduction in slabs to 40-75% in 2012/13. A maximum tax of 35% is imposed on imported parts that have been already manufactured domestically, but it is to be reduced to 30% in 2012/13. In the case of greenfield investment, even parts can be imported at the CKD tax rate for three years as a special case of CKD, probably for the promotion of FDI. The special period is to be extended from three to four years or more.

In the steel industry, an import tax on competing products, namely cold rolled steel sheets, was lowered from 10% to 5% in 2011.

(2) Implications

The development of the local parts manufacturing industry is important in view of employment and ripple effects on linked industries. Reductions in import duties force local parts manufacturers to lower their product prices down to those of import products and therefore cannot secure profits as planned with subsequent negative impacts on their management. Frequent changes in duty rates disturb long-term business planning, sound corporate management, and investment expansion from a long-term standpoint.

Import duties are imposed on CKD parts, but the rate is lower than that on CBU units. The small difference between the two rates discourages the localization of CKD parts. Local parts manufacturers consist of many local companies and contribute to employment creation. Tariff cuts will harm the competitiveness of locally manufactured products against competitive than import parts and make it difficult to develop the local parts manufacturing industry, thereby influencing employment and technical transfer adversely.

(3) Suggestions for Improvement

Import policy, including import duty rates, should not be changed frequently so that investors can draw up long-term business plans, maintain sound management, and make investment from a long-term viewpoint.

An increase in the local content rate is part of industrial policy. If the local content rate is lowered by reductions in import tariffs, the development of the local parts industry will be negatively affected. Therefore, tariff cuts on parts should be carefully examined.

The hindrance to the development of the local parts industry will have negative impacts on employment and technical transfer. Conversely, reductions in import through the development of local parts manufacturers will save foreign currencies and improve the national economy. Therefore, import policy that can promote the local parts industry is recommended.

Likewise, the expansion of the special period of the favorable treatment for new investment is likely to impede the development of the local industry. The current period of three years should remain unchanged for the development of the parts industry by the automobile manufacturers.

(2) Import of Used Vehicles

(a) Current Situation

Due to inconsistencies in governmental policies, the age limit of imported used cars was relaxed from three years to five years in 2011. Despite the age limit, cars worn out in the rest of Asia are imported and modified for local use. Especially many decrepit trucks are imported illegally by abusing the category of "Special Purpose Vehicle". Also, Chinese companies under-invoice many imported used cars and motorcycle parts.

(b) Implications

Pakistan's domestic market is huge, considering the population size. Under the influence of the import of used cars and the global financial crisis in 2008, the volume of car production is much less than estimated in the target of AIDP. The annual demand of automobiles is 220,000, of which 4,000 were imported used automobiles. Due to uncertainty about the future market size, investors are unable to decide new investment.

Under-invoicing of imported used cars impedes fair competition in the domestic market and harms the local automobile industry. There is a concern that the import of decrepit used vehicles will also have negative effects on the environment, and traffic safety.

(C) Suggestions for Improvement

The development of manufacturing represented by the automobile industry is essential because Pakistan aims to be a middle-income country in 2030 and needs to secure employment. The automobile industry has huge supporting industries and related companies absorb enormous workers. Since policy that can develop the local automobile industry and expand employment should be actively supported, the illegal import of used cars should be regulated. Also, employment should be expanded through the promotion of policy for automobile industry development because a loss in employment opportunities is one factor in increasing crimes.

As countermeasures against illegal import, OICCI recommends the following non-tariff barriers adopted in India and Thailand to support the local industry. The government should examine them toward their realization.

- Registration of vehicles in the importers' names for one year;
- Right-hand drive vehicles with a speedometer in km/hour;
- Importers' submission of pre-shipment certificates for conformance from the Ministry of Commerce (MOCOM);
- Confirmation of original homologation certificates issued at registration; and
- Approval to importers from PSQCA.

5.2.2 Vehicle Inspection and Emission Control

(a) Current Situation

In Pakistan, vehicle inspection is not required for motorcycles and passenger cars while semi-annual inspection on commercial vehicles (buses, trucks, taxis, and rickshaws) is compulsory. Since 2007, exhaust emissions have been regulated. On May 16, 2009, the Ministry of Environment revised the Annex III on the National Environmental Quality Standards for Motor Vehicle, Exhaust and Noise to the Pakistan Environmental Protection Act of 1997 (XXXIV of 1997). It was then published in the official gazette dated August 18, 2009, as summarized as follows:

Euro-2 emission standards for new gasoline cars were introduced on July 1, 2009, and those for diesel-powered cars are slated for implementation on July l, 2012. Maximum noise is set at 85 db at a 7.5 m distance.

Exhaust, nitrogen dioxide, and noise standards (maximum permissible limits) are set at 40%, 60%, and 85 db, respectively, while current ways for measurement methods and adaptation were inherited without revision until June 30, 2012.

(b) Implications

Only 30% of vehicle owners receive semi-annual compulsory inspection according to inspectors. Specifications for inspection items are not clearly defined. Inspection is carried out visually and no equipment is used. Some examiners are said to check documents only and do not inspect vehicles. Such lax enforcement of vehicle inspection is a problem, in addition to lack of equipment for vehicle inspection and designated inspection stations.

Euro-2 emission standards were introduced, yet with lack of testing facilities, PSQCA and the Provincial Transport Authority (PTA) have difficulty in implementing emission tests and controlling emission thoroughly.

The incomplete implementation of vehicle inspection and emission control is likely to facilitate the import of old used cars, thereby harming the local automobile industry as mentioned above. There is concern that decrepit cars such as scrapped cars may cause safety and environmental problems.

(c) Suggestions for Improvement

Safety standards should be set so that inspection can be conducted at inspection bodies with standard facilities instead of current visual inspection. While voices are raised to demand the expansion of the vehicle examination system to passenger cars, it is recommended to launch drastic reforms on the present system.

PSQCA and PTA lack both expertise and facilities required for inspection on automobile parts. To enable quality control up to international standards, it is necessary to introduce testing facilities while reinforcing PSQCA's inspection capability. The following concrete actions are required:

- Regular inspection on commercial vehicles is compulsory, but the legal system to apply inspection to passenger cars should be developed. Meanwhile, specifications for inspection items should be established because they are not clearly defined.
- Qualifications for PTA's fitness examiners should be clearly defined. Also, PTA should be allowed to authorize repairing houses under certain conditions to enhance the fitness center system.
- The Motor Vehicle Rule of 1965 and the legal system related to vehicle fitness certification should be improved. The fitness system should be developed through the introduction of vehicle examination facilities.
- Vehicle owners should be informed through public relations activities that they are responsible for maintenance.

- The road traffic law needs to be administered more properly because the road traffic administration system is not fully managed by the local government and also because safe transport is indispensable.

5.2.3 Human Resource Development

(a) Current Situation

The automobile industry is faced with shortage of skilled workers. Human resources are developed through in-house training such as on–the-job training of automakers with human resources that can give technical guidance. Automobile repair services are provided at official dealers' repair shops and independent workshops. There is shortage of skilled human resources in repair. The automobile industry is concerned that local parts manufacturers will fail due to lack of international competitiveness if Pakistan normalizes trade relations with India and automobile parts are imported from India.

(b) Implications

The rapid growth in the automotive sector in Pakistan is difficult to sustain without efficient human resources. Presently, the industry is faced with severe shortage of trained engineers, supervisors and workers in the assembly operation and parts manufacturing. The deficiency of skilled personnel, which is a serious handicap, is more on account of rapid growth of the automotive sector and also due to lack of any institution for providing the high quality training required by the automotive industry. Also, the management of local parts manufacturing lacks skills and knowledge about business management. As a result, product failure rates are high and delivery deadlines are not strictly observed. This hinders the expansion of their business with automakers.

(c) Suggestions for Improvement

Pakistani technology does not comply with international standards. Training facilities are not equipped with upgraded equipment required for training for upgraded technology (dies and molds). Such equipment should be installed. The Pakistani automobile industry should improve their technology levels (quality, cost, and delivery) to compete with imported parts in the domestic market, initiated by the government.

Human resource development can be promoted with the use of existing centers in Karachi, namely the Karachi Tools Dies & Molds Centre (KTDMC) and Automotive Testing & Training Center (AT&TC) under the Ministry of Industry (MOI). However, Pakistan lacks die and mold technology. It is necessary to develop technical training centers where dies and molds coupled with automobile production and repair technologies and skills can be studied. Such technologies and skills include computerized numerical control (CNC) machining, metrology, welding (gas, arc, etc.), painting and surface treatment, automotive diagnostics, maintenance and service, and business studies (to enable students to run their own businesses),

5.3 Issues with Impacts on the Whole Industry

5.3.1 Tax

Since the issue of taxation is handled by the Investment Climate Advisor, this section presents a brief overview.

(1) Turnover Tax

(a) Current Situation

At present, a turnover tax is imposed on the sales of corporations. Pakistani taxation is incoherent. The turnover tax was 0.5% in 2009 but was changed to 1.0% in 2010. In 2012/13, however, the minimum turnover tax is to be reduced back to 0.5%.

(b) Implications

The current tax on sales leaves some companies in the red after tax and causes a loss to them. Frequently changed taxation is not attractive to foreign investors and does not promote FDI.

(c) Suggestions for Improvement

Appropriate taxation is needed to expand job opportunities as well as to promote FDI and technical transfer and. The method of tax calculation should be changed from the current turnover tax which can cause a loss after tax to the corporate tax on pre-tax profits that is international customary. The Pakistani government is concerned that it is difficult to know profits. However, the government should differentiate between listed companies that disclose their financial statements and unlisted companies and apply the corporate tax on profits at least to listed companies that disclose their financial statements audited properly.

(2) Infrastructure Cess

(a) Current Situation

Although companies in export processing zones (EPZs) are exempted from many taxes, an infrastructure cess of 0.5% on imported materials is still levied in KEPZ.

(b) Implications

According to the EPZ Act, Import Policy Order applicable to ordinary import is not applied to import to EPZs. The infrastructure cess is applied only by the Government of Sindh among provincial governments. Its application to companies in KEPZ is contradictory to the EPZ Act and unreasonable.

(c) Suggestions for Improvement

Companies in KEPZ already paid the infrastructure tax. It should be refunded, which is under discussion with the authorities concerned, such as KEPZA.

It would be beneficial to the Pakistani economy to prioritize the EPZ Act and promote the attraction of FDI because unreasonable taxes give a negative impression to foreign companies regardless of their amounts.

5.3.2 Industrial Infrastructure

Since a survey on infrastructure in the study area is being conducted by another JICA study team, this section presents a brief overview.

(1) Access Roads

(a) Current Situation

Pakistani transportation system heavily depends on the road transport system because of its inefficient railway transport system. The exports of the country are delivered to Karachi Port from the other parts of the country through roads. Thus, industrial transportation, such as the import of materials, the export of product, and employees’ commuting, also depends on road transport. Despite the importance road transport, recently general crimes, such as robbery at gunpoint, have been happening frequently in traffic jams during commuting hours.

(b) Implications

Traffic conditions are poor not only for commuting but also for economic activities, such as transportation of materials and products. Poor traffic conditions contribute to traffic jams, which are a big cause of crime on the road, such as robbery at gunpoint.

(c) Suggestions for Improvement

Road improvement will not only increase economic and production activity but also relieve congestion and crime during traffic jams. An access road to KEPZ, the Mehran Highway, was rehabilitated by KMC in 2012, but its extension to Port Qasim is required.

(2) Electricity

(a) Current Situation

In Karachi, power supply is unstable and load shedding happen frequently. In a company whose business is power generation, if sales proceeds do not come in, fuel cannot be procured. This is one of the reasons why local electricity production is running at only 50-60% of the actual capacity. This low operating rate is attributable to the circular debt, which amounts to Rs400 billion.

(b) Implications

Unstable power supply disrupts normal production. Stable electricity supply is required for stable production. Some companies utilize in-house power generating facilities for stable production, but their costs are higher than those of electricity from KESC, leading to increases in operation costs and reductions in profitability.

(c) Suggestions for Improvement

The biggest debtor of the circular debt is the government. They justify this unsettled debt by claiming that they give subsidies to the power industry. It will take time to clear the circular debt. The problem will not be solved unless the unit cost of power generation is lowered by using coal or hydropower.

(3) Gas

(a) Current Situation

Although the problem of gas depletion prevails throughout most of Pakistan, it has not affected Sindh as badly as the other parts. Sindh produces 70% of the total gas production in the country.[29] The Constitution of Pakistan secures the first right on gas of the Province of Sindh, stipulating that the province has "precedence over the other parts of Pakistan in meeting its requirements" from its own well heads.

(b) Implications

Although gas depletion has not affected Sindh as badly as the other parts, it became a problem around 2005 and is becoming more serious over time in Sindh. There is concern that a shortage of gas supply disrupts normal production and leads to increases in costs and reductions in profitability.

(c) Suggestions for Improvement

The Iran-Pakistan pipeline project is expected to be accomplished. Moreover, it is necessary to devise and implement fundamental solutions to secure long-term stable gas supply.

[29] Ministry of Petroleum and Natural Resources, Hydrocarbon Development Institute of Pakistan. 2010. "Pakistan Energy Yearbook 2010." (http://www.scribd.com/doc/53512742/Pakistan-Energy-Yearbook-2010)

(4) Water

(a) Current Situation

Inadequate water supply is not such a serious problem, compared with electricity outages. In time of occasional water shortages, some companies purchase water from water tankers to maintain production.

(b) Implications

Unstable water supply disrupts normal production. Stable water supply is required for production activity. Inadequate water supply leads to increases in costs and reductions in profits.

(c) Suggestions for Improvement

Water supply facilities should be developed to enable stable water supply, including water quality.

5.3.3 Living Environment

(1) Security

(a) Current Situation

Security is poor in Karachi. Interviews revealed that recently general crimes, such as robbery at gunpoint, have been a more serious concern than terrorist threats. Crimes in Karachi have been on the rise since 2005 that recorded 24,661 and hit a record high of 58,689 in 2010.[30] The number declined to 42,467 in 2011 but has increased six times over the past six years.

(b) Implications

Security is one of the greatest hindrances to investment as pointed out in “Doing Business 2012” by the World Bank and also in the interview survey. The high incidence of crime is a major threat to both foreign and local employees. Interview respondents indicated that although they wanted to invite their business partners to Pakistan, some of them refused to come due to security grounds. Similarly, respondents ordered their employees to come to Karachi, but they refused due to security reasons. Some respondents hold meetings abroad for security purposes. Thus, the deterioration of law and order disturbs business activities.

Improvement in security requires the Sindh Police to take the initiative in enhancing security measures. However, interviews revealed that many respondents had little or no confidence in the police due to not only the bribes demanded by them but also their tedious procedures and unproductive actions. It was reported by some respondents that even though the police witnessed crimes, they took no action. Another challenge faced by the police is political pressure. Respondents pointed out that the police did not take action against crimes involving political parties. One reason behind this is that some police officers were employed and connected with political parties.

[30] Citizens-Police Liaison Committee, “Crime Statistics”.

Rigorous enforcement of law and strict action against crime are urgently needed. However, the police are under budget constraints. A respondent provided an example: The police could not afford patrol vehicles and motorcycles and fuel, even if culprits were arrested. Police officers escorted culprits to the police station by motorcycle but paid for the fuel themselves. Some officers are not active in arresting culprits since they have to cover costs at their own expense. Thus, the Sind Police lack appropriate security measures despite the serious security problem in Karachi.

(c) Suggestions for Improvement

Security should be considered a top priority to promote FDI. Rigorous enforcement of law and strict action against crime are badly needed. The police stated that they were willing to adopt countermeasures against crime but had very limited budget. It is therefore recommended that necessary equipment such as police cars and motorcycles and CCTV cameras be provided to assist the police in tightening security. The overseas training of police officers will also be helpful in raising their awareness on security measures and improving their expertise.

(2) Commuting

(a) Current Situation

Various attempts to improve traffic conditions are being made, such as the Mehran Highway, Malir Expressway, and Karachi Circular Railway. Respondents showed that although road rehabilitation improved traffic conditions, congestion especially during commuter rush hours remained a problem and that there was still a need to further improve road conditions.

Modes of commuting are a problem especially for local employees due to poor public transport. Some companies provide transport for their employees. The employees of other companies have no choice but to depend on private vehicles and public transport.

(b) Implications

Poor road conditions are a cause of traffic jams and muggings at gunpoint occur mostly during these jams. The incidence of highway robberies in Karachi, including the National Highway 05, one of the main commuting routes to KEPZ and the Bin Qasim Industrial Area, was the highest at 10 cases in 2004 during a period from 1997 to 2006 but increased from 19 in 2007 to 42 in 2011.[31] This rising street crime plays a part in worsening security mentioned above.

Apart from poor road conditions, poor public transportation is one of the reasons for the frequent use of private vehicles and heavy traffic, contributing to crimes in jams.

Improvement in traffic conditions requires the Sindh Police to take strict action against street crimes, rallies and protests on the road, and traffic offences, but appropriate action is not being taken due to lack of police officers' motivation caused by political pressure and discouragingly low pay.

[31] Citizens-Police Liaison Committee, "Crime Statistics".

(c) Suggestions for Improvement

To ease congestion and reduce the crime rate, the construction of flyovers and toll roads and road expansion from two- to three-lanes, together with their repair and maintenance are suggested.

In addition, the development of public transport is required. Upgrading public transportation can greatly contribute to reducing dependency on private vehicles and alleviating traffic jams, thereby reducing road related crimes.

Security systems, such as CCTV surveillance and check posts, will be effective in reducing crimes on the road. As stated above, however, assistance such as equipment provision would be necessary, given the budget constraints on the Sindh Police.

5.3.4 FDI Promotion

(1) BOI Functions

(a) Current Situation

In order to confirm the actual FDI activity in Karachi, the JICA Study Team visited several regulatory organizations. However, none of these organizations was able to provide useful data on FDI activity such as the number of firms, types of industries, manufactured items, and the number of employees.

The BOI Karachi Office is expected to play a pivotal role in FDI promotion, but little is known about BOI activities by businessmen. The recognition of BOI is low because they serves as a window for work permits but has no authority for approval.

(b) Implications

If the Government of Pakistan wishes to invite foreign companies into Pakistan, basic data regarding FDI and the domestic industry are essential for them. Foreign investors usually consider the existing FDI activity before making an actual investment themselves, but relevant data are unavailable in Karachi.

FDI promotion requires strong cooperation among the BOI Karachi Office, SBOI, and KEPZA, but it is weak. For example, SBOI finds projects to promote investment in Sindh, but their information is not shared with BOI and BOI cannot provide information about promising projects in Karachi for interested foreign companies. This causes losses of business opportunities and has negative effects on not only the Sindh government but also the Pakistani government. Apart from this, the BOI faces the problem of the insufficient number of qualified officials in its Karachi Office who can have dialogues with the private sector.

(c) Suggestions for Improvement

Related organizations, such as BOI and SBOI, should collect and store basic data on FDI and the domestic industry. In order to promote FDI, it is important to give a good impression to foreign companies by means of providing data for those interested. BOI is expected to collect and organize basic data on foreign companies by sector and nationality. For BOI or SBOI, this dissemination of information to related organizations or companies can be very useful, as their activities will be recognized and their status will be elevated in Pakistan.

FDI promotion requires stronger links among BOI, SBOI, and KEPZA. BOI should assume leadership in coordination. Since foreign companies have to submit documents for registration to secure land for production sites, BOI should provide guidance and advice on how to prepare the documents to support them.

These solutions are difficult to implement by current BOI Karachi officers. Qualified officials who can have dialogues with the private sector and comply with its requirements are required to be reinforced in BOI Karachi Office.

(2) EPZA Services

(a) Current Situation

EPZA is attempting to attract foreign companies with one-stop services. However, services provided for investors by the EPZA are insufficient. Companies in EPZA are having clearance problems.

(b) Implications

Companies have to go through procedures for the export and import of raw materials and processed products. Each time companies make arrangements for tax exemption at customs offices. EPZA services are insufficient, compared with cases in other countries, and need to be improved.

(c) Suggestions for Improvement

It is advisable to establish a branch office of FBR in EPZA where procedures for tax exemption required for export and import can be taken or to simplify the procedures by giving EPZA the authority to give approval and licenses related to export and import.

(3) Minimum Size of Investment in SEZ

(a) Current Situation

The SEZ Act was approved by the parliament in July 2012. Investors are not allowed to select a development site of less than 50 acres in the SEZ.

(b) Implications

The SEZ Act does not benefit investment other than big investment of over 50 acres and does not give incentives to small investment of below 50 acres.

(c) Suggestions for Improvement

The SEZ Act should adequately reflect the preference of investors as to site selection for FDI promotion. It is preferable to reduce the development site scale to less than 50 acres, which is too big for some investors. Apart from site selection, infrastructure is a primary requirement for investors. Infrastructure in the SEZ should be developed by the Pakistani side to promote FDI.

5.4 Policy Matrix for Investment Climate Improvement in Karachi

Among the seven issues, tax and industrial infrastructure are removed from policy matrix because they are in the hands of the Investment Climate Advisor and another study team. Below are the five pillars of policy matrix formulated to solve the priority issues to be taken by the Pakistani side based on outcomes and outcome indicators.

PILLAR-1: Formulation of Import Policy
PILLAR-2: Consolidation of Environment Friendly and Safe Transport System
PILLAR-3: Human Resource Development in Automotive Industry
PILLAR-4: Establishing Safe Commuting
PILLAR-5: Capacity Development of One-Stop Services for FDI Promotion

Pillars 1 to 3 will have effects on the development of and FDI promotion in the automobile and steel industries and provide solutions issues faced mainly by Japanese companies in Karachi. Meanwhile, Pillars 4 and 5 will have effects on the whole industry and promote FDI in the whole industry.

As the issues are wide-ranging, overall outcome goals and indicators are based on "Vision 2030," IMF reform scenario, and AIDP.

Overall Outcome Goals:	Overall Outcome Indicators and Targets:
1. Personal income will be increased (GDP per capita: US$4000 in 2030). 2. Employment ratio will be increased. 3. A safer means of transportation for the Pakistani people will be developed. 4. A safe living environment will be created.	1. GDP growth rate will increase from 2.4% in 2010/11 to 5.5% in 2016 2. Unemployment ratio will be reduced by less than 10% from 13.1% in 2016 3. Adequate pollution control and traffic safety will be achieved. 4. Crimes will be reduced.

PILLAR-1: Formulation of Import Policy

Outcome Goal	Outcome Indicator and Target
1. Long term industrial development policy will be formulated and issued by the government.	1. The production of new cars will be increased from 134,000 in 2011 to 350,000 in 2016.

Issue	Action (Input)			By Whom
	Short Term (2012/13-2013/14)	Mid-term (2014/15-2015/16)	Long Term (2016/17)	
1. Import duty on steel products was reduced from 10% to 5 %. 2. Import duty (max. 35%) on automotive parts is to be changed. 3. Under-invoicing of imported used cars and motorcycle parts is allowed 4. The import of used cars for commercial purposes is allowed.	➢ A Task Force for import policy will be formulated by MOI and MOCOM. ➢ Import of used cars will be studied through discussion between the public and private sectors. ➢ AIDP-2 will be drafted through discussion with the automobile industry. ➢ New import duty and regulations (non-tariff barriers) on the import of used cars will be submitted to ECC for approval.	➢ Import duty on automotive parts based on AIDP-2 will be implemented. ➢ New regulations (non-tariff barriers) on under-invoicing of imported used cars will be implemented. ➢ At the first stage of phased improvement in regulations on the import of used cars, the age of imported cars will be reduced to less than 3 years old.	➢ At the second stage, legislation will be enacted to prohibit the import of used cars for commercial purpose ➢ The implementation of AIDP-2 will be reviewed and revised, if necessary.	MOI (*) MOCOM EDB

Source: JICA Study Team

Note: MOI: Ministry of Industry, (*): Responsible organization, MOCOM: Ministry of Commerce, EDB: Engineering Development Board, ECC: Economic Coordination Committee.

PILLAR-2: Consolidation of Environment Friendly and Safe Transport System

Outcome Goal	Outcome Indicator and Target
1. The vehicle inspection system will be improved. 2. Emission control will be enforced.	1. Vehicle inspection facilities and emission control testing equipment will be installed in Karachi.

Issue	Action (Input)			By Whom
	Short Term (2012/13-2013/14)	Mid-term (2014/15-2015/16)	Long Term (2016/17)	
1. The existing law (Motor Vehicle Rules 1969) is not complied with. 2. There is no emission control testing equipment for Euro-2. 3. The vehicle fitness system is not functioning.	➢ A legal system relating to vehicle fitness certification will be developed to apply inspection to passenger cars. ➢ Safety standards enforced through inspection with testing equipment instead of visual inspection will be established. ➢ Guidance sessions for safe transportation will be conducted for GOS. ➢ Overseas training for concerned officials will be conducted to introduce safe transportation and measures for Euro-2.	➢ Road traffic laws and ordinances will be partially enforced by GOS. ➢ Guidance sessions for safe transportation will be conducted by GOS. ➢ Pilot emission control facilities complying with Euro-2 environmental standards will be developed, ➢ Overseas training for concerned officials will be conducted to introduce safe transportation and measures for Euro-2.	➢ Road traffic administration system by local government will be improved, ➢ Emission control testing equipment for Euro-2 will be installed at PSQCA, PTA, etc. ➢ Pilot vehicle inspection facilities with testing equipment will be established in Karachi. ➢ Awareness campaigns about the necessity of vehicle inspections and emission control will be carried out for drivers and vehicle owners.	MOC (*) MOE (*) PTA PAKEPA GOS SP PSQCA

Source: JICA Study Team

Note: MOC: Ministry of Communication, (*) Responsible Organization, MOE: Ministry of Environment, PTA: Provincial Transport Authority, PAKEPA: Pakistan Environmental Protection Agency, GOS: Government of Sindh, SP: Sindh Police, PSQCA: Pakistan Standard & Quality Control Authority.

PILLAR-3: Human Resource Development in the Automotive Industry

Outcome Goal	Outcome Indicator and Target
1. The automotive parts procurement ratio will be increased by OEMs (assemblers).	1. Domestic parts procurement ratio will increase from 50% in 2011/12 to 70% in 2016/17.

<table>
<tr><th rowspan="2">Issue</th><th colspan="3">Action (Input)</th><th rowspan="2">By Whom</th></tr>
<tr><th>Short Term (2012/13-2013/14)</th><th>Mid-term (2014/15-2015/16)</th><th>Long Term (2016/17)</th></tr>
<tr>
<td>1. Local manufacturers are unable to supply the qualified parts by designated deadlines.
2. Car production costs increase due to procurement of automotive parts from overseas.
3. Local automotive parts manufacturers cannot survive due to lack of international competitiveness.</td>
<td>➢ Obstacles to AIDP-1 implementation will be discussed and overcome by EDB, PAMA, and PAAPAM for the certain implementation of AIDP-2.
➢ Periodical technical guidance will be given the local automotive industry by SMEDA experts.
➢ Local trainers will be upgraded under the guidance of SMEDA experts at technical training centers.
➢ Overseas technical guidance will be promoted to acquire new technology (dies and molds).</td>
<td>➢ Periodical technical guidance will be given to the local automotive industry by SMEDA experts.
➢ Local trainers will be upgraded under the guidance of SMEDA experts at technical training centers.
➢ Overseas technical guidance will be promoted to acquire new technology
➢ High-technology equipment will be installed at automotive technical centers.</td>
<td>➢ Staff training for the automotive industry will be conducted by local trainers of SMEDA.
➢ The implementation of AIDP-2 will be reviewed and a new program will be drafted.</td>
<td>MOI (*)
EDB
SMEDA
KTDMC
AT&TC
PSQCA</td>
</tr>
</table>

Source: JICA Study Team

Note: MOI: Ministry of Industry, (*): Responsible Organization, EDB: Engineering Development Board, SMEDA: Small and Medium Enterprise Development Agency, KTDMC: Karachi Tools Dies & Molds Centre, AT&TC: Automotive Testing & Training Center, PSQCA: Pakistan Standard & Quality Control Authority.

PILLAR-4: Establishing Safe Commuting

Outcome Goal	Outcome Indicators and Target
1. Safe commuting between residences and workplaces will be enabled.	1. Crimes in Karachi will be eradicated.

Issue	Action (Input)			By Whom
	Short term (2012/13-2013/14)	Mid-term (2014/15-2015/16)	Long Term (2016/17)	
1. Congestion and crime at gunpoint during traffic jams are common. 2. There is lack of a security system and strict action.	➢ An outline of a security system (CCTV camera monitoring and check posts) will be drafted by SP. ➢ Contractors and suppliers will be selected by tender. ➢ A detailed security inspection plan after the introduction of the securing system will be drafted by SP.	➢ A CCTV camera monitoring system and check posts will be established along main commuting routes such as N-5. ➢ Additional police motorcycles for security control of main commuting routes such as N-5 will be introduced. ➢ Overseas training of 10-20 police officers will be conducted. ➢ Public announcements of an increase in police patrols will be made as psychological operations to reduce crime.	➢ Check posts along main commuting routes such as N-5 will be established. ➢ The patrolling system will be reviewed and reinforced by SP. ➢ Overseas training of 10-20 police officers will be conducted. ➢ Public announcements of an increase in police patrols will be made as psychological operations to reduce crime.	GOS (*) KMC SP

Source: JICA Study Team
Note: GOS: Government of Sindh, (*): Responsible Organization, KMC: Karachi Metropolitan Corporation, SP: Sindh Police.

PILLAR-5: Capacity Development of One-Stop Services for FDI Promotion

Outcome Goal	Outcome Indicator and Target
1. FDI will increase on an annual basis.	1. FDI will increase from US$1.7 billion in 2010/11 to more than US$6 billion in 2016/17.

Issue	Action (Input)			By Whom
	Short Term (2012/13-2013/14)	Mid-term (2014/15-2015/16)	Long Term (2016/17)	
1. The facilitation functions of BOI among related organizations mandated by the government are inadequate. 2. The number of qualified officials in the BOI Karachi Office is inadequate. 3. The one-stop service functions of EPZA need to be strengthened. 4. The investor side is not able to select less than 50 acres in the development site of the SEZ.	➢ A Task Force will be created and be comprised of representatives from related organizations (BOI, FBR, MOCOM, MOI, EDB, EPZA, and SBOI) to strengthen FDI promotion. ➢ The reinforcement of one-stop service functions will be studied by the Task Force and submitted to the related organizations for approval. ➢ Five new appropriately qualified officials will be allocated to the BOI Karachi Office. ➢ The SEZ Act will be revised so that a system to give special approval to land of even below 50 acres with a certain amount of investment as SEZ with ECC's approval can be developed.	➢ Task Force meetings will be held quarterly for improvement in FDI promotion functions. ➢ BOI's service function to assist foreign companies in permitting processes such as corporate registration will be strengthened. ➢ An amendment to regulations to reinforce EPZA's one-stop service function will be submitted to ECC for approval.	➢ Task Force meetings will be held quarterly for improvement in FDI promotion functions. ➢ BOI's service function to support companies will be reviewed by the Task Force in consultation with industrial associations. ➢ One-stop service functions will be reviewed by the Task Force and reported to the related organizations.	BOI (*) FBR MOCOM MOI EDB EPZA SBOI

Source: JICA Study Team

Note: BOI: Board of Investment, (*): Responsible Organization, MOCOM: Ministry of Commerce, MOI: Ministry of Industry, EDB: Engineering Development Board, EPZA: Export Processing Zone, SBOI: Sindh Board of Investment, SEZ: Special Economic Zone, ECC Economic Coordination Committee.

5.5 Establishment of the Monitoring System for Policy Matrix

It is necessary to establish a system to monitor the progress in the policy matrix. Since BOI is not only monitoring but also coordinating relevant organizations, it is recommendable to implement the monitoring of progress in the policy matrix by BOI. Subsequently, results should be disclosed to the related organizations on a quarterly basis.

5.6 Projects to be Implemented for FDI Promotion

The above policy matrix was shared and agreed by Pakistani authorities concerned at the seminar on survey results on August 6, 2012. However, some of the projects in the policy matrix will be difficult to implement by the Pakistani government alone. To expedite the implementation, the Pakistani side should request Japan's assistance, such as dispatching policy experts, technical guidance for the automobile industry, equipment provision, and overseas training. The combined implementation of these schemes is considered effective and will need to be examined.

1. Capacity Development for FDI Promotion

Project name: Dispatching an investment policy expert to BOI
Activity: One foreign expert is to be dispatched to BOI for the coordination and facilitation of a Task Force to be formulated by related organizations such as KEPZA and SBOI to strengthen one-stop services for FDI promotion in Karachi.
Scheme: Technical Cooperation (TC)
Implementation Schedule: 2014-2015 for two years
Project Budget: -
Financial Support: No
Executing Agency: BOI

2. Human Resources Development in the Automobile Industry

(1) Project name: Dispatching an industrial policy expert to EDB
Activity: One foreign expert is to be dispatched to EDB for the coordination and facilitation of a Task Force to be formulated by related organizations such as Ministry of Communication (MOC) and FBR for improvement in import policy and the proposal of measures to facilitate progress in AIDP.
Scheme: TC
Implementation Schedule: 2013-2014 for two years
Project Budget: -
Financial Support: No
Executing Agency: EDB

(2) Project name: Dispatching technical experts for high-technology guidance to the automobile industry in Karachi
Activity: Foreign technical experts of different specialization are to be dispatched to the automotive parts industry through SMEDA to upgrade the production technology and quality to reinforce international competitiveness.

Scheme: TC
Implementation Schedule: 2013-2015 for three years
Project Budget: -
Financial Support: No
Executing Agency: SMEDA

(3) Project name: Provision of high-technology equipment for a technical training center
Activity: High-technology equipment and tools will be provided for the technical training center proposed in Karachi. The types of equipment required to acquire new technology (dies and molds) will be studied in the project preparation stage.
Scheme: Grant
Implementation Schedule: 2014-2016 for three years including the project preparation stage for one year
Project Budget: US$2 million (1 lot)
Financial Support: Required
Executing Agency: EDB and Karachi Tools Dies and Molds Centre (KTDMC)

(4) Project name: Provision of testing equipment and tools for emission control of Euro-2
Activity: Testing equipment and tools for emission control of Euro-2 in Karachi will be provided as a pilot project to demonstrate significant effects. The types of equipment and tools required for emission control of Euro-2 will be studied in the project preparation stage.
Scheme: Grant
Implementation Schedule: 2014-2016 for three years including the project preparation stage for 1 year
Project Budget: US$1 million (1 lot)
Financial Support: Required
Executing Agency: PSQCA

3. Reinforcement of Security during Commuting

Project name: Capacity Development of the Sindh Police for Tighter Security
Activity 1: A CCTV monitoring system will be provided and installed along main commuting routes such as N-5 to reinforce security. The detailed specifications of the monitoring system and the quantity of equipment will be drafted in the project preparation stage, based on geographical conditions.
Activity 2: Check posts will be constructed along main commuting routes such as N-5 to reinforce security. The detailed specifications of check posts and construction sites will be drafted in the project preparation stage, based on geographical conditions.
Scheme: Grant
Activity 3: Additional police motorcycles will be introduced for main commuting routes such as N-5 to reinforce patrolling system. The required number and specifications of the motorcycles will be drafted in the project preparation stage based on geographical conditions.
Activity 4: Overseas training of 10-20 police officers will be conducted to strengthen their motivation in reinforcing security and protection against crimes during commuting.
Scheme: TC
Implementation Schedule: 2013-2017 for five years including the project preparation stage for one year

Project Budget: US$145,000

- Activity 1: US$50,000 (1 lot, 20 km),
- Activity 2: US$20,000 (US$2,000/unit x 10 units),
- Activity 3: US$75,000 (US$1,500/unit x 50 units)

Financial Support: Required
Executing Agency: SP

The details of the above projects are listed in Figure 5.6.1.

Category	Project Name	Scheme	Implementation Schedule					Project Budget	Financial Support	Executing Agency
			2013	2014	2015	2016	2017			
Capacidy Development for FDI Promotion	Dispatching an investment policy expert to BOI	TC		■	■				No	BOI
Human Resource Development in Automobile Industry	Dispatching an industrial policy expert to BOI	TC	■	■					No	EDB
	Dispatching technical experts for high-technology guidance to the automobile industry in Karachi	TC	■	■	■				No	SMEDA
	Provision of high-technology equipment for a technical training center	Grant		□	■	■		US$2 million	Required	EDB, KTDMC
	Provision of testing equipment and tools for emission control (Euro-2)	Grant		□	■	■		US$1 million	Required	PSQCA
Reinforcement of Security during Commuting	Capacity development of the Sindh Police for tighter security	TC	□	■	■	■	■	US$145,000	Required	SP

Source: JICA Study Team
Note: □ Preparation stage, ■ Execution

Figure 5.6.1: Projects to Acquire Technical and Financial Support

Appendix A

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Appendix B

Change in Sectorial Share in GDP

Table:B1 Projected Change in Sectorial Share in GDP –Vision 2030

Fiscal Year	GDP (at factor Cost)	Agriculture Sector	Service Sector	Industrial Sector	Manufacturing Sector
	Rs. Billion	% Share in GDP			
2006	7,713.00	21.60%	52.30%	26.10%	18.20%
2007	8,330.68	20.92%	52.29%	26.51%	18.58%
2008	8,997.83	20.26%	52.27%	26.93%	18.97%
2009	9,718.40	19.62%	52.26%	27.36%	19.37%
2010	10,496.68	19.00%	52.25%	27.79%	19.78%
2011	11,337.29	18.40%	52.24%	28.23%	20.20%
2012	12,245.22	17.82%	52.22%	28.67%	20.62%
2013	13,225.85	17.25%	52.21%	29.12%	21.06%
2014	14,285.02	16.71%	52.20%	29.58%	21.50%
2015	15,429.01	16.18%	52.19%	30.05%	21.95%
2016	16,664.62	15.67%	52.17%	30.52%	22.41%
2017	17,999.17	15.18%	52.16%	31.01%	22.89%
2018	19,440.60	14.70%	52.15%	31.49%	23.37%
2019	20,997.47	14.23%	52.14%	31.99%	23.86%
2020	22,679.01	13.78%	52.12%	32.50%	24.36%
2021	24,495.22	13.35%	52.11%	33.01%	24.88%
2022	26,456.87	12.93%	52.10%	33.53%	25.40%
2023	28,575.62	12.52%	52.09%	34.06%	25.93%
2024	30,864.05	12.12%	52.07%	34.60%	26.48%
2025	33,335.74	11.74%	52.06%	35.14%	27.04%
2026	36,005.37	11.37%	52.05%	35.70%	27.61%
2027	38,888.79	11.01%	52.04%	36.26%	28.19%
2028	42,003.13	10.66%	52.02%	36.83%	28.78%
2029	45,366.87	10.33%	52.01%	37.41%	29.39%
2030	49,000.00	10.00%	52.00%	38.00%	30.00%

Appendix C

Surveys by the World Bank and OICCI

C-1: The World Bank Enterprise Surveys in Pakistan

a) Introduction

This section of the appendix provides a broad scenario of the overall business and investment environment in Pakistan. In this context, two different international survey-based data sets were analyzed to supplement the purpose of the present study. These data sets are: World Bank's *Enterprise Survey* and the Overseas Investors Chamber of Commerce and Industry's *Perception and Investment Survey*. These surveys were carried out during 2006, 2007 and 2011, respectively. The two survey-based data sets can be compared with the current report to evaluate whether there have been positive changes in the business and investment environment or if it has deteriorated over time.

The data sets in these surveys cover a larger sample size spread at the national level and focus on much broader issues and problems confronted by the businesses and investments in Pakistan. Karachi, being the largest business city in Pakistan, is part of the sample in these studies. Therefore, a comparable data set helps investigate and find inter-country as well as intra-country variations in better ways.

The World Bank Enterprise Surveys in Pakistan were carried out in the period from September 2006 to June 2007. In the survey, 935 business firm owners and top managers were interviewed to create the data set and country profile for Pakistan. For comparative analysis, the benchmarks of the averages for the group of countries in South Asia and the Pakistan income group have been taken.

b) Infrastructure

Infrastructures are the key ingredient for business and investment activities. On the one hand, it facilitates the businesses; while on the other hand, it shows the extent of government support in direct and indirect ways to businesses and industries. A strong infrastructure enhances the competitiveness of an economy and generates a business environment conducive to firm growth and development. Quality standard and good infrastructure increases a firm’s efficiency in carrying out the business with their customers and suppliers, and enables them the use of modern production technologies.

Conversely, deficiencies in infrastructure create barriers for productive opportunities and increase the cost for the firms, which vary from micro enterprises to large multinational corporations. Specifically, large multinationals are more sensitive to infrastructure as they have to keep/follow certain international standards for doing their businesses and investments. In this context, utilities/resource and institutional infrastructures to facilitate and address the issues/problems related with businesses and investments are important.

The World Bank Enterprise Surveys make note of the dual challenge of providing a strong infrastructure for electricity, water supply, telephone connections, etc., and the development of institutions that effectively provide and maintain public services.

The first set of indicators shows the extent to which firms face failures due to the shortage of electricity and the effect of these failures on sales. Inadequate electricity supply increases costs, disrupts production, and reduces profitability. Figure C1 shows that Pakistan has relatively better position in the South Asian region in terms of power outages and loss in business due to the power outages. This position becomes reversed when compared with averages of low income countries. Since 2000, the power demand of Pakistan is growing rapidly. On the other hand, the generating capacity is not growing at the same pace. This causes increasing gap between the power demand and supply. The increase in demand is largely on the back of domestic demand, while the industrial demand has been mostly stable over the last few years. Out of the total energy consumption, shares of electricity consumption are less and only about 16.2% of energy in terms of electricity is consumed. Of this, 27.5% (about 4.5% of the total energy consumption) is consumed by the industrial sector in Pakistan during 2010-11.[1]

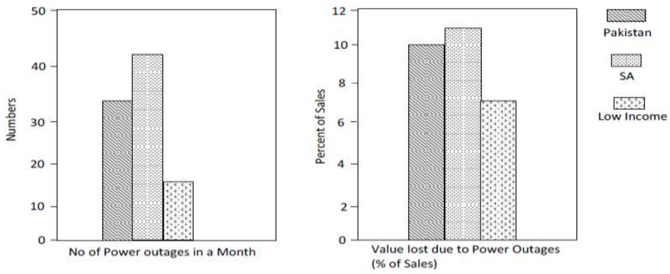

Figure C1: Infrastructure - Electricity

The second set of indicators measures the access to water supply and the shortage for the manufacturing sector. Many manufacturing sectors depend on efficient sources of water for their operations. Figure C2 portrays that Pakistan is a water-deficient country when compared to regional and low-income countries' averages.

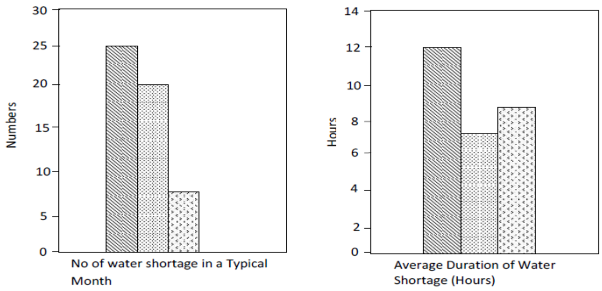

Figure C2 : Infrastructure - Water

The third set of indicators evaluates the access to infrastructure services, by quantifying the delays in obtaining electricity, water, and telephone connections. Service delays impose additional costs on firms and may act as barriers to entry and investment.

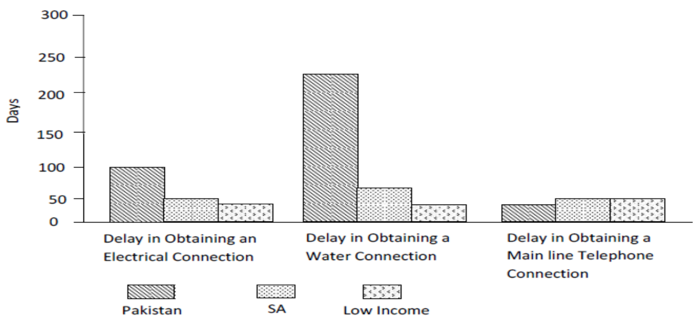

Figure C3: Infrastructure – Service Delays

[1] Economic Survey of Pakistan 2011-12

Figure C3 shows that water and electricity connections are highly time-consuming. On the average, it takes more than 3 and 8 months to obtain electricity and water connections, respectively. There appears to be a high correlation between the delay in connection and the outages of electricity and shortages of water (as demonstrated in Figures C1, C2 and C3). Obtaining telephone connections are much faster in Pakistan than in other South Asian regions and low-income countries. This may be attributed to the liberalization policy in telecommunication and development of information technology sector in Pakistan, where competition in the private sector has increased the access of fixed as well as cellular phone connections tremendously.

d) Trade

Trade has an important role in the economic development of any nation. It does not only fetch foreign exchange from exports and create competitive environment, it is also a channel of technological development where the process of imitation to innovation in domestic firms evolves in order to raise the products standard, and in turn, market expansion. Therefore, trade contributes to firms' businesses as well as nations. On one hand, open markets allow firms to expand, raise standards for efficiency in exports, and enable firms to import supplies at low cost. On the other hand, trading firms are also confronted with various customs services and trade regulations, acquisition of export and import licenses, compliance of banking regulations for foreign exchange earnings and payments, and in some cases, also face additional costs due to losses during transportation. The Enterprise Surveys collected information on the operational constraints faced by exporters and importers and also quantifies their trade activities. A number of indicators are used to investigate trade-related issues, as will be discussed in the following paragraphs.

The first set of indicators provides a measure of the intensity of foreign trade in the private sector. The first panel in Figure C4 shows the percentage of firms who export their products directly or indirectly. The second panel on the other hand shows the percentage of manufacturing firms who use inputs or supplies of foreign origin.

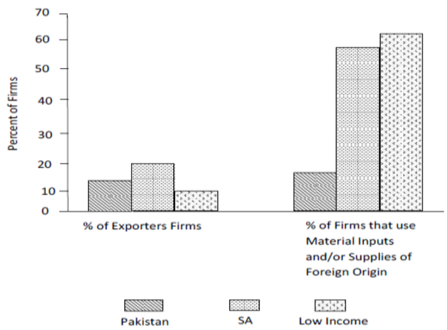

Figure C4: Trade –Exports and Imports

There are fewer firms in Pakistan who export their products as compared to the regional average. However, among low-income countries, Pakistani firms are more export-oriented. In Figure C4, around 15% of Pakistani firms in the sample are exporters, while in low income countries, there are only 10% firms in the sample who export their products. As far as the use of material inputs and/or supplies from foreign origin by firms is concerned, there is a wide-gap between Pakistani firms and those from the South Asian region and low income countries. More Pakistani firms use local inputs (about 82% in the sample) as compared to South Asian (48%) and low income (39%) countries, on average.

The second set of indicators measures the average number of days it takes the imports and exports to clear customs. A delay in customs clearing may create additional costs for the firm like insurance coverage, addition of demurrage, interruption and/or delay in production, which in turn affects the sales, resulting into damaged supplies or merchandise. Figure C5 demonstrates that Pakistan is relatively better in terms of customs clearance for exports and imports than in other South Asian region as well as in low income countries.

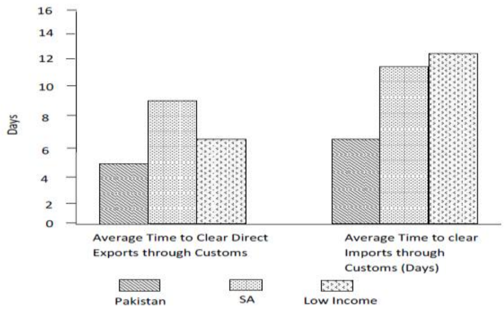

Figure C5: Trade – Customs Efficiency

The third set of indicators shows the percentage value of exports lost during transportation, due to merchandise theft, breakage or spoilage. This would reflect on the transportation risks that firms face during the export process. The sample data corresponding to Pakistani firms reveal that there are insignificant losses of about less than 0.5% of sales that firms suffer due to theft and breakage or spoilage in their exports. The same losses in exports are much higher in the South Asian region and low income countries, on the averages, as shown in Figure C6.

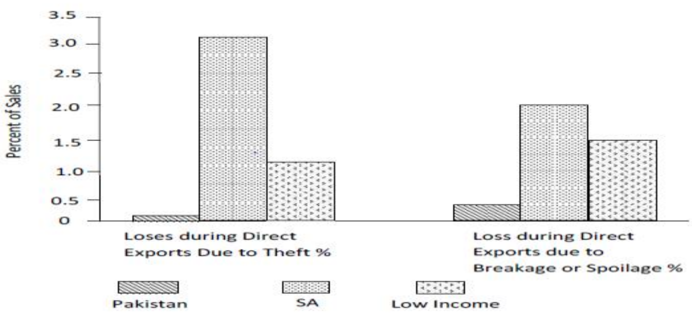

Figure C6: Trade – Losses during Direct Export

e) Regulations, Taxes, and Business Licensing

Good governance in areas such as taxation, regulations, and business licensing is a fundamental pillar for the creation of a favorable business environment. Effective regulations reconcile private and public interests, and also address market failures that inhibit productive investment.

The number of permits and approvals that businesses need to obtain are essential part of the firms' operations. It involves time as well as cost. It also depends on the existing legislation of the country and business culture. It determines the type of legal forms which private firms opt/want to carry out on their business operation. It also determines the level of protection which is given for investors as an incentive to invest. The Enterprise Surveys provide qualitative and quantitative measures of taxation, regulations, and business licensing.

The first set of indicators focuses on the efficiency of government offices in granting business licensing and permits services.

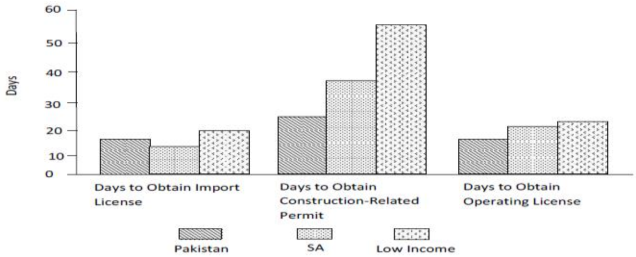

Figure C7: Regulations, Taxes and Business Licensing – Delays

In the last decade, the Government of Pakistan has substantially simplified the regulatory environment for the setting up of business operations in the country. This also includes the establishment of a Business Support Centre to provide assistance in starting a business in Pakistan to potential local and foreign investors. In enquiries about the delays in days when businesses require licenses and permits for their establishments, it was found that Pakistan is in a much better position in terms of delays in the number of days for obtaining import and operation licenses in the South Asian region and in low income countries. While construction-related permits have considerably less number of delays in terms of days in Pakistan as compared to other selected group of countries.

The second set of indicators first approximates the “time tax” imposed by regulations: it measures the time spent by senior management in meetings with public officials. Second, it measures the average number of tax inspections or meetings with tax inspectors in a given year. Given these two approximate measures of "time tax", data reveals better situation in Pakistan. Figure C8 shows that senior management of Pakistani firms spent less than one-third of the time in dealing with the requirements of government regulation than what is observed in other South Asian regions and low income countries. Furthermore, Pakistani firms have less number of visits and meetings with tax officials.

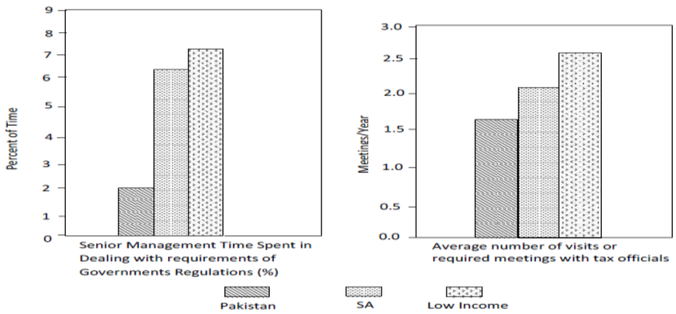

Figure C8: Regulations, Taxes and Business Licensing – Time Tax

The third indicator shows the relative use of the different legal forms of business establishments under which private sector firms operate. Most legal forms around the world can be classified into shareholding companies with shares traded privately or not traded at all (closed), shareholding companies publicly traded (open), sole proprietorships, partnerships, and limited partnerships. A residual category is included to capture legal forms not easily classified into other categories.

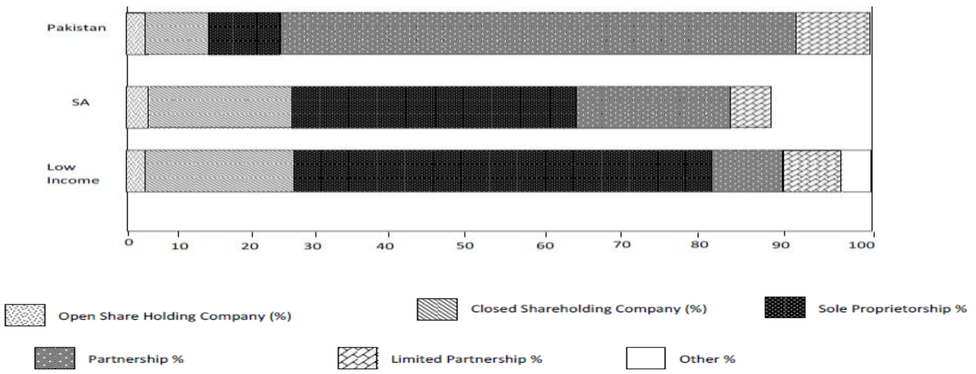

Figure C9: Regulations, Taxes and Business Licensing – Legal Forms of Firms

Figure C9 shows that there are no clear trends of business establishments. In South Asian regions and low income countries, sole proprietorship appears to be more common. In Pakistan, majority of firms are partnership establishments. This may be due to the reason that these firms belong to family businesses where family members/relatives are board of directors' members. Also, there are no such regulatory requirements to comply within partnership models as compared to limited partnership or shareholding models. Some reasons behind opting for the partnership model in Pakistan are:

1. Partnership models are registered by provincial authorities and is a provincial subject;
2. There is no such requirement for obtaining certificate of commencement of business and the firm can commence business just after its incorporation;
3. There is no such requirement of minimum capital;
4. Minimum tax rate on income applied is 25% as compared to 35% on limited partnership or shareholding;
5. Filing of accounts is not required by partnership firms, thus, no such account audit and allowing tax evasion activities by these firms;

f) Corruption

Corruption by public officials may present a major administrative and financial burden on firms. Corruption creates an unfavorable business environment by undermining the operational efficiency of firms and raising the costs and risks associated with doing business.

Inefficient regulations constrain firm efficiency. As firms provide opportunities for soliciting bribes, they are required to make unofficial payments to public officials to get things done. In many countries, bribes are common and are quite high. They add to the bureaucratic costs in obtaining required permits and licenses. Bribing can be a serious impediment for the growth and development of firms.

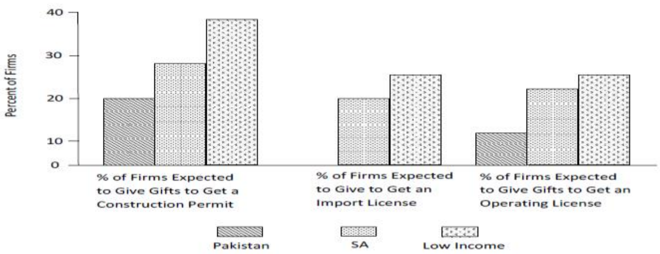

Figure C10: Corruption – Bribes for Licenses and Permits

The first set of indicators measures a composite index of corruption. The Graft Index reflects the proportion of times a firm was asked or was expected to pay a bribe when soliciting six different public services, permits or licenses. The summary of data in Figure C10 portrays that relatively less number of firms in Pakistan has to give gifts/bribes to obtain license and permits for their businesses.

The second set of indicators identifies the extent to which specific regulatory and administrative officials require bribe payments during meetings with tax inspectors or in order to secure a government contract.

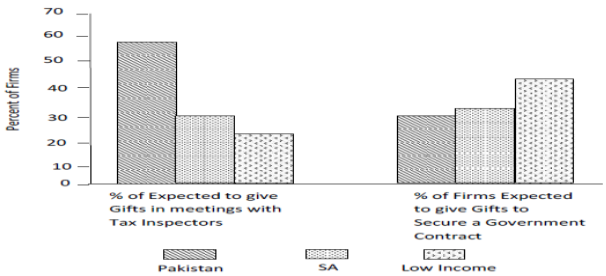

Figure C11: Corruption – Bribes during Meetings

A large number of firms (around 60%) in Pakistan mentioned that they are supposed to give gifts when meeting with tax officials, while less than one-third of the sampled firms face similar situations in order to secure government contracts. Figure C11 provides a comparative summary of corruption in Pakistan, South Asia and low income countries.

The third set of indicators focuses on bribes to obtain specific licenses or permits. Indicators show the share of firms that are expected to make informal payments when securing import and operating licenses and obtaining construction permits.

When the summary of facts in Figures C7, C8 and C10 are combined together; it shows that there is a built-in system of corruption in Pakistan where firms have minimum interaction with tax and government officials.

g) Crime and Informality

Crime imposes costs to firms when they are forced to divert resources from productive uses to cover security costs. Both foreign and domestic investors perceive crime as an indication of social instability, as crime drives up the cost of doing business. Also, commercial disputes between firms and their clients occur regularly in the course of doing business. Resolving these disputes can be challenging when legal institutions are weak or non-existent.

Similarly, a large informal sector has serious consequences for formal private sectors. The informal sector may pose unfair competition for formal firms. According to the Economic Survey of Pakistan 2011-2012, about 73.8% of the total country's labor force is employed by the informal sector. In developing countries, a large part of the economy constitutes the informal sector. In Pakistan, more than half of the economy is unregistered and therefore, pay no taxes. The firms operating in the informal sector evade taxes to save cost of doing business, which in turn creates a tough business environment to formally registered firms.

The Enterprise Surveys capture key dimensions of the effect of crime on the sales of firms, the extent to which entrepreneurs identify courts as fair, and the degree of informality in an economy.

The first indicator shows the share of firms that recognize the functioning of the courts as being fair, impartial, and uncorrupted. The summary indicator in Figure C12 shows that more than 80% of firms in Pakistan suspects that court functions are not fair, partial and uncorrupted. While in other selected regions and groups, around 60% of firms in the data have similar impressions.

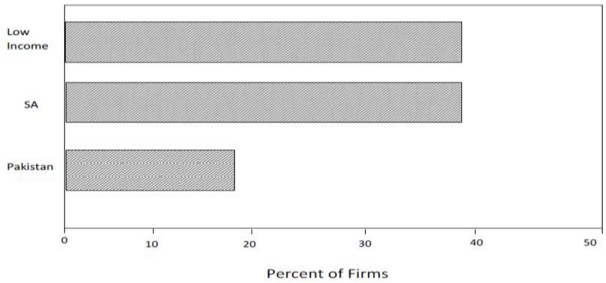

Figure C12: Crime and Informality – Perception About the Courts

The second set of indicators measures the direct cost of security incurred by firms as well as their direct losses due to crime. These resources represent an opportunity cost since they could have been invested in productive activities. Figure C13 demonstrates that firms in Pakistan pay relatively less cost for security purposes in carrying out their business as compared to low income countries. Furthermore, crimes like theft, robberies, vandalism and arson attacks against firms in Pakistan cost less than 0.5% of their sales as compared to 1.3% in low income countries.

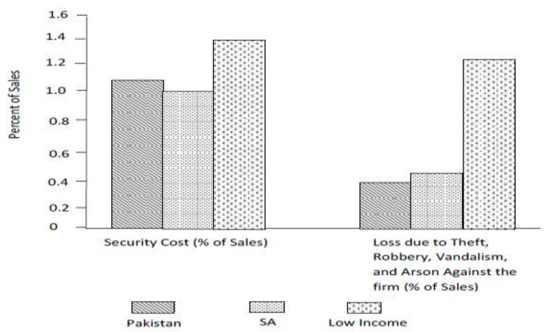

Figure C13: Crime and Informality – Cost of Crime

The third set of indicators shows the percentage of firms that started operations without being formally registered. It is an approximation of the prevalence of informality in the private economy. Figure C14 provides no information regarding formal registration of firms at the time of start-up operation in Pakistan. While around 90% of the firms in the South Asian region and low income countries get formally registered when they start their business operations. Data variation in the formal registration of firms in Pakistan and other selected region and countries is because of the difference in business culture. Historically, most of the firms in Pakistan start their business as trade and/or small-medium scale manufacturing set-ups where no formal registrations are required. These are self-financed businesses without any external financing. During the early stage, they also avoid tax payments. Once the firms' businesses have grown and are set in, formal registrations are then carried out to secure loans and open trade accounts, tax registration, accounts audit, etc.

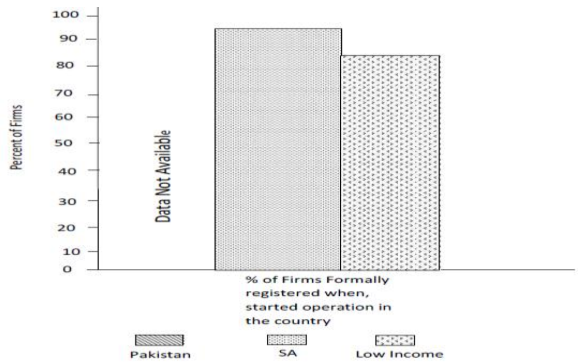

Figure C14: Crime and Informality – Informal Business Startups

h) Finance

Developed financial markets provide payment services, mobilize deposits, and ease investment financing. Efficient financial markets reduce the reliance on internal funds or money from informal sources such as family and friends by connecting firms to a broad range of lenders and investors. In this connection, the Enterprise Surveys provide indicators of how firms finance their operations and the characteristics of their financial transactions.

The first set of indicators compares the relative use of various sources to finance investment. Excessive reliance on internal funds is a sign of a potentially inefficient financial intermediation. Figure C15 shows that most of the firms rely on internal finance for investment in Pakistan, South Asia regions as well as in low income countries. These facts are further validated when it is combined with the establishment forms of different firms (as portrayed in Figure C9), where the majority of firms operate under closed shareholding, sole proprietorship or partnership.

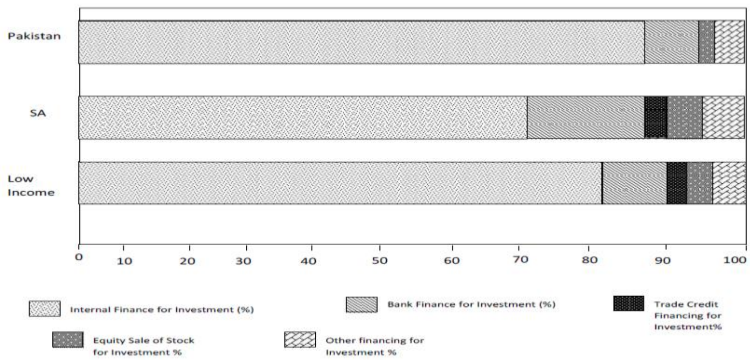

Figure C15: Finance – Use of Sources of Investment

The second set of indicators measures the use of financial markets by individual firms. Each indicator is measured in terms of the percentage of working capital that is financed by external sources to the firm and the burden imposed by loan requirements based on collateral levels relative to the value of the loans. It is found that, on the average, about 85% of the working capital requirement is financed through internal sources of firms in Pakistan, while data of firms from other South Asian regions and low income countries relatively rely more on external finance. Furthermore, there is a wide difference in collateral requirement needed for bank loans in Pakistan and in other countries. In Pakistan, an average of 70% of the loan amount is needed as collateral; while in other countries, it is more than one and a half times of the loan required, as shown in Figure C16. This indicates that access to finance in Pakistan is relatively easier as compared to countries in South Asia and other low income countries.

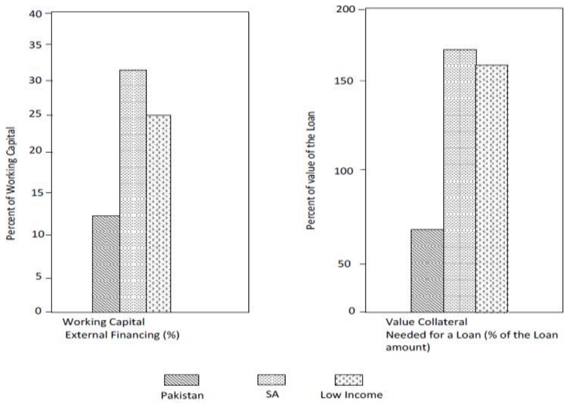

Figure C16: Finance – Financing Through External Sources

The third set of indicators focuses on the use of financial services by private firms, both on the credit side, by measuring the percentage of firms with bank loans or lines of credit, and on the deposit mobilization side, by measuring the percentage of firms with checking or savings accounts. Figure C17 provides a comparison between the countries. The pattern appears to be similar, i.e. most of the firms use banking services for checking and business transaction purposes, while less number of firms take loans or have line of credit from banks.

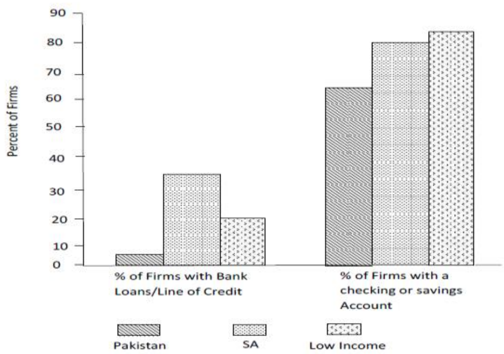

Figure C17: Finance – Use of Banking Financial Services by Firms

i) Innovation and Workforce

The Enterprise Surveys provide indicators that describe several dimensions of technology use and innovation. Information on the characteristics of the workforce employed in the non-agricultural private economy is also collected.

The first set of indicators measures the extent to which firms invest in obtaining recognized certificates of production and accounting practices. Obtaining international quality certifications can open doors to technology and innovation, and also provide a sign of high quality that may open market opportunities. About 10% of the firms in Pakistan as well as in selected regions and countries go for international certification. This may be due to the reason that most of the firms have local markets for their products. This fact is further justified with the graph of Figure C4 which shows the percentage of firms who export their products. Figure C18 also provides information about external audit of firms. Around 20% of the firms in

Pakistan carry out external audits of their accounts. It may be because business ownerships are largely based and rely on self-finance that large numbers of firms do not carry out external audit of their accounts.

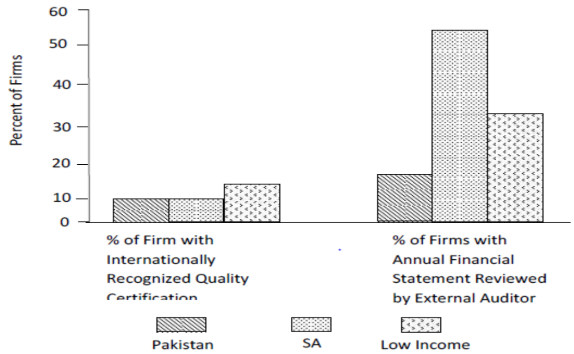

Figure C18: Innovation and Workforce - Certificates

The second set of indicators demonstrates the use of information and communication technologies (ICT) in business transactions. ICT, such as the Internet are important tools for all firms because they provide even the smallest of enterprises with the ability to reach national and international markets at a low cost. In this connection, Figure C19 shows that more than 90% of Pakistani firms use their own websites to reach national and international clients/ customers to market their products, while less number of firms in South Asian regions and low income countries have their own websites and in turn, rely only on emails or communication channels.

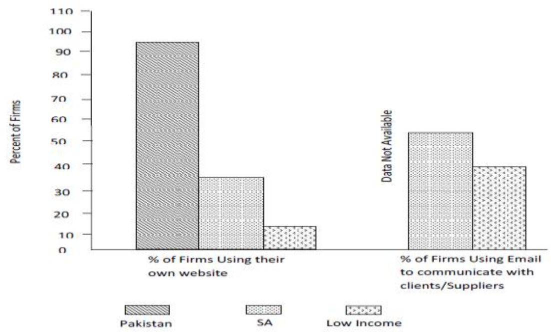

Figure C19: Innovation and Workforce – Use of Internet

The third set of indicators presents the composition of the firm's workforce by the type of contract and gender. Labor regulations have a direct effect on the type of employment favored by firms and may have a different impact on employment by gender. The first two indicators present the composition of the workforce classified into temporary and permanent workers. The average numbers shown in Figure C21 indicates that most of the surveyed firms in the sample are small- and medium-sized firms. Largely, firms have full-time workers. However, they do not employ permanent workers. This may be because firms want to avoid additional financial burden which they have to pay in terms of pension, gratuity, insurance and other benefits after retirement to permanent workers.

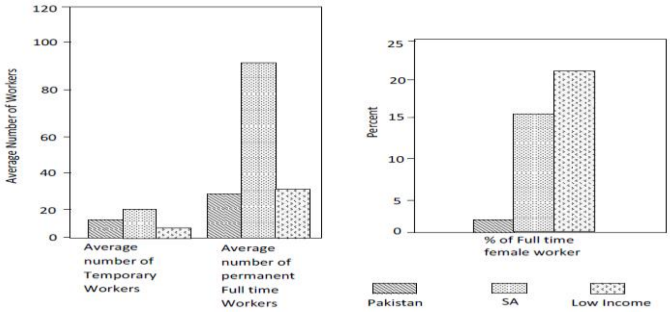

Figure C20: Innovation and Workforce – Employment by Contract and Gender

The last indicator in Figure C20 reflects the participation of women in regular full-time employment which gives a contrast picture. In Pakistan, firms have less than 2% full-time female workers, while in other countries, female participation rises to more than 16%. The small proportion of full-time female workers in Pakistan conforms to the social and cultural norms that prevail in the society.

C-2: Perception and Investment Survey 2011 by OICCI

The Overseas Investors Chamber of Commerce and Industry (OICCI) conducts yearly, perception and investment surveys for the information of its members and stakeholders. The following are extracts from the 2011 survey:

a) Business Risk in Pakistan

About half of respondents perceive that Pakistan is a 'High Risk' venue for investment, as was the case in the 2009 survey as well.

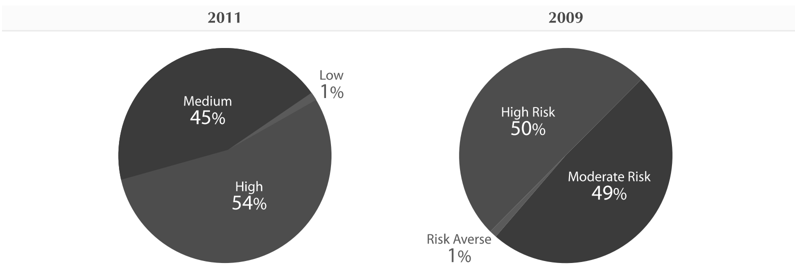

Figure C21: Business Risk in Pakistan

b) Criticality of Utilities

Almost all of the members perceived electricity-power and I.T. and telecommunications to be indispensable for smooth functioning. Other utilities, although equally important, vary in significance according to the needs of the members.

It is clear from the almost unanimous response that electricity-power and I.T. and telecommunications are critical and necessary in doing business. There is an urgent need to solve and manage the ongoing power crisis which has become a threat to business operations and the economy as a whole. Moreover, I.T. and telecommunications cannot function without electricity-power. Although the government has taken several steps to improve the power situation, there is an urgent need to comprehensively resolve energy supply issues.

Further analysis of the sector-wise data reveals variation in the importance of different utilities for different companies: electricity, and I.T. and telecommunications are important for all businesses; petroleum products are more important to oil, gas and energy companies than to financial services companies. Similarly, natural gas is critical for chemical and fertilizer companies but not for shipping, printing and security companies.

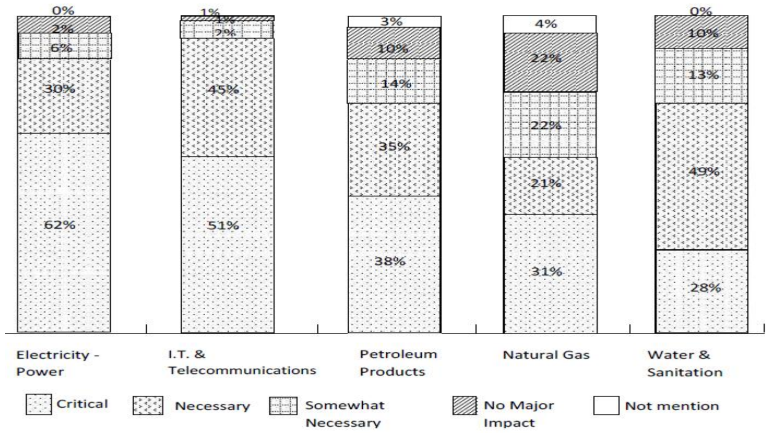

Figure C22: Criticality of Utilities

c) Challenges to Business

Participants were asked to rank the major challenges faced in doing business on a scale of one to ten, with one being the highest and ten the lowest. The ranking indicates the importance of each challenge to the different sectors.

As in 2009, the three biggest challenges continue to be law and order, energy supply and government/political instability, closely followed by price inflation, which has been in double digits for over four years (in 2009 the fourth biggest challenge was infrastructure). The fifth biggest challenge in the current survey is perceived as policy implementation, whereas it was cost of operations in 2009. Respondents were asked for their top challenges over the next 2-3 years and the next 4-5 years, responses for these periods were more or less the same.

More than 80% of respondents ranked law and order at either number one or number two position. The issue of circular debt which impacts electricity and gas supply as well as cost, has led participants to rank energy supply as their second biggest challenge.

Inflation is fuelled by a combination of high international oil prices, unbridled government spending especially on security and by inefficiencies in large state-controlled enterprises. Related to inflation is the cost of doing business, which is a matter of great concern for the business community as it raises the possibility of inability to compete with cheaper imports of products from other countries.

Another matter of serious concern to investors is the issue of policy implementation.

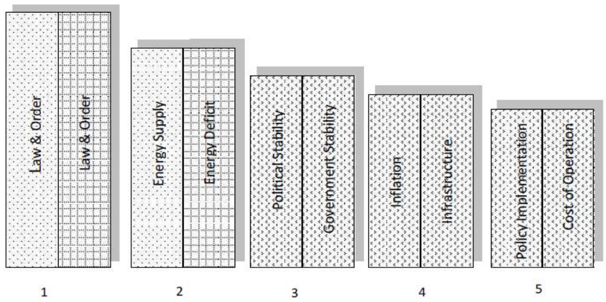

Figure C23: Top Challenges to Businesses

d) Perception of the Government of Pakistan

An overwhelming majority of foreign investors (82%) believe that the Pakistani government is aware of the problems being faced by the business community, but lacks the political will or 'seriousness' required to tackle these issues. The government does not seem to have gained full investor confidence, as respondents are divided in terms of their opinions regarding the government's ability to resolve investor issues. Among sectors that questioned the government's ability include the food and consumer products sector.

Figure C24: Perception of the Government of Pakistan

e) Obstacles to Businesses: Policy Formulation vs. Implementation

Foreign investors believe that the government has framed excellent policies as only 20% of the survey respondents regarded certain policy formulations as obstacles to improve the business environment. However, an overwhelming majority (79%) of respondents stated that policy implementation is a major concern and obstacle.

Although policy implementation continues to be a major issue, the good news for the government and its regulatory bodies is that foreign investors believe implementation has improved as borne out by the negative perception decreasing from 86% in 2009 to 79% in 2011.

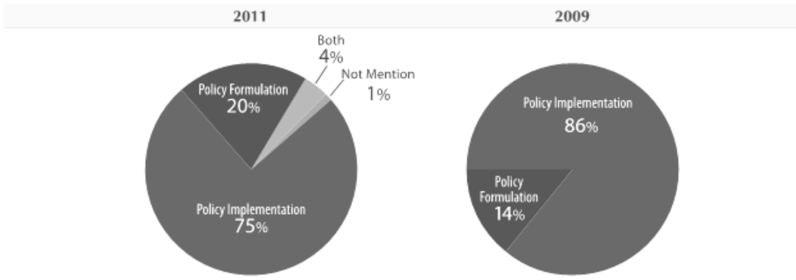

Figure C25: Obstacles to Business: Policy Formulation Vs. Implementation

f) Impact of Trade and Fiscal Policies

<u>Trade Policies</u>

Trade with India: The minority negative responses are because the cost of doing business in India is relatively lower in many business sectors than in Pakistan where costs have gone up significantly in the recent past. Some companies feel that removal of barriers for entry of Indian goods to Pakistan will render local businesses uncompetitive, leading to eventual business closure.

On the other hand, OICCI members believe that MFN status should be granted to India and that the government should look into protecting some selected segments of the economy.

Revised APTTA: 39% positive responses may be due to measures adopted by the government under the new APTTA to curb unauthorized trade. These include installing tracking devices on all transport units, ensuring custom-to-custom information sharing and providing financial guarantees to be deposited by authorized brokers/clearing agents that will be released after goods exit the country.

<u>Fiscal Policies</u>

18th Amendment: Although various matters have been devolved to different provinces under the 18th amendment, half of the respondents perceive this to have no significant impact on their business. The pharmaceutical sector stands alone in seeing this to have an adverse impact as the infrastructure for health affairs within the provinces is not yet fully set up.

Taxes and Levies: Another area of uncertainty is the Sindh Sales Tax Act on Services 2011 which has been enacted whilst the corresponding FBR provision was still intact at the time this survey was done. Fifty-three percent of respondents have strongly criticized this tax. Furthermore, the Sind Development and Maintenance of Infrastructure (SDMI) cess continues to be an issue for businesses based in Sindh, contributing to increased costs of doing business. It may be noted that a similar tax does not exist in other provinces. Also, with comparative analysis of taxability, there are many services which are considered taxable in Sindh under the Sindh Sales Tax Services Act 2011 but such services are not taxable in other provinces of Pakistan. There are also conflicts between the federal and province regarding the collection of taxes on services despite the fact that under the 18^{th} amendment, sales tax on services has been removed from the domain of the federation. This also creates the issue of the double taxation.

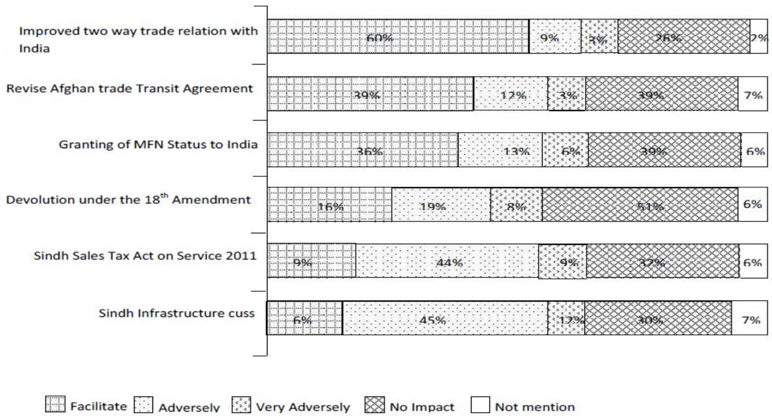

Figure C26: Impact of Trade and Fiscal Policies

g) Plans for Operations in the Next Few Years

Foreign direct investment in Pakistan, as per reported official figures, is declining. OICCI members however, have indicated a bullish outlook as far as their own operations in Pakistan are concerned.

Foreign investors continue to exhibit their confidence in the country and value its potential despite the current macro-economic and socio-political climate. The government should take this positive response and match it with concrete policy steps to improve the business environment through effective and regular public-private interaction. Improved perceptions, as compared to 2009 when 10% of the respondents answered "Yes" when asked whether they plan to curtail operations in Pakistan, is due to the fact that foreign investors have done very well in terms of their bottom lines, as per companies' published reports.

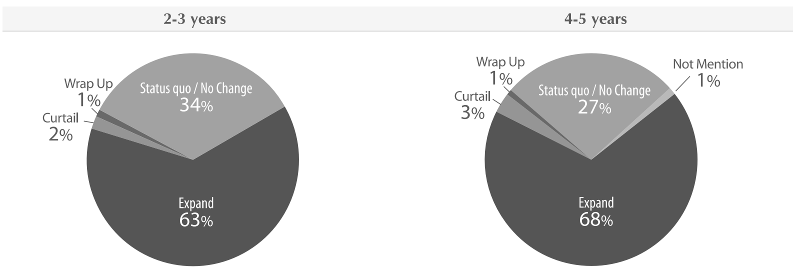

Figure C27: Plans for Operations in Next Few Years

h) Planned Investment

While investment plans are encouraging the amount of investment per company, investments are still lower than what is needed to stimulate economic growth. Less than 10%, or 11 member companies, foresee investing in excess of US$50 million over the next five years. However, the collective total investment by the respondents is approximately US$3 billion in the next 2-5 years. If this materializes, it is likely to contribute somewhat to the forecasted GDP growth of 3.5% and to stimulate employment opportunities over the same time period.

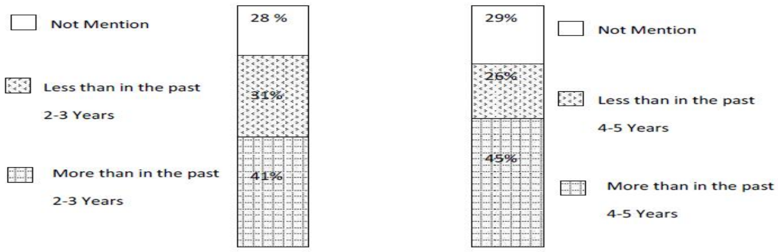

Figure C28: Planned Investment

i) Growth in Next 2-3 years

Food and consumer goods and trading sectors are expected to be the major prospective investors. The growing population and increasing middle-income group in Pakistan have encouraged existing players to plan on expanding. International supermarket chains have also entered the market to tap this growth. Some sectors like engineering, industrial goods and chemicals and fertilizers have indicated a lower appetite for expansion and/or investment.

Revenue and Profitability are important aspects to business continuity as they can significantly impact the size and structure of an industry. In view of this significance, expectations of revenue and profitability in the coming years formed part of the survey. The obtained results are consistent with the expansion plans detailed earlier.

There were however, some concerns expressed by 6% of respondents who expect reduced revenues while 18% perceive lower profits.

Amongst 85% of respondents who have a positive outlook for revenues, 46 members indicated a growth rate averaging 21.5%. Similarly, of the respondents who are optimistic about their profits, 34 members (66%) have indicated a growth rate averaging 19%.

A high proportion of respondents from all sectors expect their revenues to increase in the next 2-3 years. Similarly, the majority of respondents from all sectors except pharmaceuticals are very optimistic about their profitability. The concern of pharmaceutical companies is understandable as prices in Pakistan are controlled and no price increase have been granted since December 2001, with the exception of only a few products which have been granted hardship price increases since 2008. The positive perception of increased revenue and profits is expected to lead to expanded business activity and enhanced level of employment.

Sector-wise, eight out of ten food/consumer goods companies are likely to increase headcounts, as does the trading sector. Only a few members have indicated reducing employment.

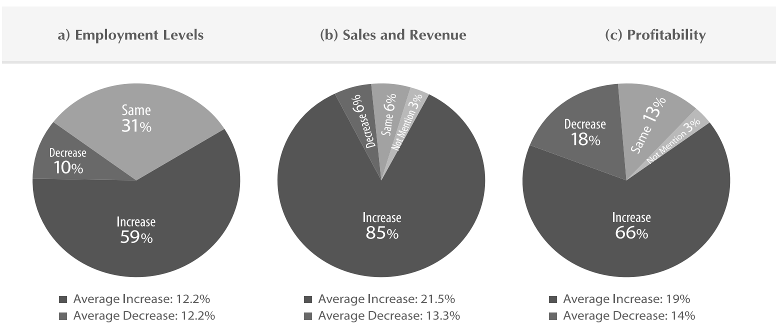

Figure C29: Growth in the Next 2-3 Years

Appendix D

Interview Questionnaires

QUESTIONNAIRE
FOR
INVESTMENT CLIMATE IMPROVEMENT IN KARACHI

INTERVIEW SURVEY

To be filled by the Interviewer

Ref. No.: ___________________________ Date of Interview: ______ - ______ - 2012
dd mm

Interviewer: ____

Interviewee: ____________________________________ Title: __________________________________

Section A – Outline of the Company's activities

1- Name of Company A1a): Karachi ____

A1b): Home Country ____________________________________

2- Address of Headquarters A2a): Karachi ____

____

A2b): Home Country ____________________________________

____

3- Telephone Nos. A3): Karachi ____

4- Fax No. A4): Karachi ____

5- Email Address A5a): Karachi ____

A5b) Home Country ____________________________________

6- Type of Industry A6a): Karachi

i) food products		ii) beverages		iii) tobacco products	
iv) textiles		v) apparel		vi) leather & related products	
vii) wood & wood products, cork		viii) paper & paper products		ix) printing & reproduction of recorded media	
x) coke & refined petroleum products		xi) chemicals & chemical products		xii) basic pharmaceutical products & pharmaceutical preparations	
xiii) rubber & plastic products		xiv) other non-metallic mineral products		xv) basic metals	
xvi) fabricated metal products, except machinery & equipment		xvii) computer, electronics & optical products		xviii) electrical equipment	
xix) machinery & equipment n.e.c.		xx) motor vehicles, trailers & semi-trailers		xxi) other transport equipment	
xxii) furniture		xxiii) other manufacturing		xxiv) repair & installation of machinery & equipment	

A6b) Home Country

i) food products		ii) beverages		iii) tobacco products	
iv) textiles		v) apparel		vi) leather & related products	
vii) wood & wood products, cork		viii) paper & paper products		ix) printing & reproduction of recorded media	

x) coke & refined petroleum products		xi) chemicals & chemical products		xii) basic pharmaceutical products & pharmaceutical preparations	
xiii) rubber & plastic products		xiv) other non-metallic mineral products		xv) basic metals	
xvi) fabricated metal products, except machinery & equipment		xvii) computer, electronics & optical products		xviii) electrical equipment	
xix) machinery & equipment n.e.c.		xx) motor vehicles, trailers & semi-trailers		xxi) other transport equipment	
xxii) furniture		xxiii) other manufacturing		xxiv) repair & installation of machinery & equipment	

7- Name of Executive Officer A7): Karachi ____

8- Year of Establishment A8) Karachi: ____

9- Registration Status of Business A9) Karachi

i) Public listed company		ii) Private held limited company		iii) Sole proprietorship	
iv) Partnership		v) Family business		vi) Other, please specify below	

10- Total number of staff? A10a) Karachi: ____

A10ai) Karachi – Management ____________________________

A10aii) Karachi – Administration ___________________________

11- List of branch offices & factories A11) Pakistan ____

____

12- Main Markets A12a) Domestic: ____

A12b) Foreign Country: __________________________________

13- Future Markets A13a) Domestic: ____

A13b) Foreign Country: __________________________________

14- Total Annual Revenue of the Fiscal Year 2011 (if possible): A14a) Karachi: ____

A14b) National: ____

15- Reasons of Investment in Karachi A15) Karachi

i) Availability of raw material		ii) Domestic market		iii) Export to neighboring countries. Name countries below	
iv) Export to home country		v) Cheap labor cost		vi) Other, please specify below	

16- Do you think your business is successful as per the initial investment plan or not?

Yes		No. Please indicate the reasons below	

Section B – Security

1- Has your company been the victim of any terrorist or guerilla crimes during the past 1 year?

No		Yes. Please indicate the circumstances below	

2- Have your foreign staff been victims of crimes during the past 1 year?

No		Yes. Please indicate the circumstances below	

3- If your response to question 2 is Yes, then, did you report the incident/s to the local police?

Yes. Please indicate their response and attitude below		No	

4- If your response to question 3 is No, please explain why ______________________________

____

5- What kind of protection is usually made available for staff? ______________________________

____

6- Do you think security cost is expensive for the company? Yes ________________ No ________________

7- What kind of natural disasters are possible in this area? ______________________________

8- Does your company prepare & protect itself from such disasters? Yes ________________ No ________________

Section C – Legal/ Regulatory Operation

1- What kind of support or improvement do you need from the Pakistani government?

2- What kind of support do you get from the Pakistani government?

3- Please indicate which of the following factors may affect your business:

	Very Inefficient	Somewhat Inefficient	Somewhat Efficient	Very Efficient
Legal & regulatory system (no change)				
Taxation system				
Length of time required to obtain various permits e.g. export permit etc. Please specify best time and worst time, below:				
Competition with neighboring countries				
Other, please specify below				

Section D – Access to Information on Investment Climate & Market

1- Efficiency of BOI service or support when contacted. *Please evaluate level/ grade of services received from BOI (please select from the following, based on your experiences):*

	Very Inefficient	Somewhat Inefficient	Somewhat Efficient	Very Efficient
Availability of social & economic data				
Availability of investment information				
Availability of application forms (including homepage)				
Approval period (days) by the government				
Transparency of approval process				
Provision of advisory service before investment determination				
Provision of advisory service after investment				
Other, please specify below				

2- Efficiency of service or support from the industrial zone when contacted. *Please evaluate level/ grade of services received from KEPZA/ PQA (please select from the following, based on your experiences):*

	Very Inefficient	Somewhat Inefficient	Somewhat Efficient	Very Efficient
Availability of social & economic data				
Availability of investment information				
Availability of application forms (including homepage)				
Approval period (days) by the government				
Transparency of approval process				
Provision of advisory service before investment determination				
Provision of advisory service after investment				
Other, please specify below				

3- Efficiency of service or support from the government when contacted. *Please evaluate level/ grade of services received from Sindh's government (please select from the following, based on your experiences):*

	Very Inefficient	Somewhat Inefficient	Somewhat Efficient	Very Efficient
Availability of social & economic data				
Availability of investment information				
Availability of application forms (including homepage)				
Approval period (days) by the government				
Transparency of approval process				
Provision of advisory service before investment determination				
Provision of advisory service after investment				
Other, please specify below				

Section E – Countermeasures on poor Infrastructure

1- Please indicate the extent of which of the following countermeasures you have taken:

	Very Inefficient	Somewhat Inefficient	Somewhat Efficient	Very Efficient
Water supply service (quality & quantity) *Own Well* Yes: _____ No: _____ Other Source: ___________				
Electricity service (stable) Own Generator Yes: _____ No: _____ Other Source: ___________				
Industrial gas service Any countermeasures? ____				
Improvement of road conditions in 3 years. Please specify what actions were taken, below:				
Improvement of IT network				
Other, please specify below				

Section F – Administrative Procedures for FDI Approval

1- What kind of support or improvement do you need from the government/ BOI?

____

____

____

____

2- Please indicate the extent of which of the following factors may affect your business:

	Very Inefficient	Somewhat Inefficient	Somewhat Efficient	Very Efficient
Legal and regulatory system for doing business				
Taxation system				
Length of time required to obtain various permits				
Availability of a sufficient sized market				
Availability of market information				
Availability of access to raw materials and parts				
Availability of skilled labor or engineers				
Availability of cheap labor				
Undeveloped infrastructure				
Availability of means of financing investment				
Inflation & financial instability				
Lack of information in general				
Other, please specify below				

Section G – Management Issues

1- To what extent do you consider the improvement of the following services important?

	Very Unimportant	Somewhat Unimportant	Somewhat Important	Very Important
Assistance in recruiting employees				
Technical training & educational services for employees				
Assistance in identifying suitable suppliers/ contractors				
Marketing & business research consulting services				
Financing				
R & D services (testing etc.)				
Forwarders, freighters & other logistical services				
Security services				
Utilities i.e. electricity, water, gas, telephones etc. Please specify the top three ones, below:				
Other, please specify below				

THANK YOU FOR YOUR COOPERATION

Preparatory Study on JICA Cooperation Program for Industry Development (Investment Climate Improvement in Karachi)

Questionnaire on the Living Environment of Foreign (non-Pakistani) Employees

Notes

- The study aims to identify issues about 1) the legal system and administrative organs for approval and licensing and 2) the living environment of company employees, suggest action plans to resolve the issues, and develop a policy matrix for improvement in the investment climate with the formulation of Japanese ODA program and projects in mind. Your response will be used exclusively for the purpose of the study. Your response will be used in such a manner that the respondent cannot be identified.
- Please **tick the option that best describes your view** in Parts II to X.
- If you have any questions, please feel free to contact Izumi Ogawa, JICA Study Team:
  Address: Board of Investment Karachi Office, Syedna Taher Saifuddin Memorial Foundation, 3rd Floor, Plot No. CD-10/20/2, Beaumont Road, Civil Lines, Karachi
  Mobile: +92 336 5147270 E-mail: ogawa-iz@n-koei.jp

I. Respondent Information

Company name:

Address:

Phone: Fax:

Respondent's name:

Respondent's designation:

E-mail:

II. Security

How serious are the following problems?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
1	Threats of Terrorism, Guerrillas, Civil War, and War					
2	Incidence of Damage by Robbery, Kidnapping, Assault, Menaces, and Fraud					
3	Property Damage by Robbery and Burglary					
4	Police or Military Investigations					
5	Police Services					
6	Employment of Security Guards					
7	Damage by Natural Disasters					

III. Commuting

How serious are the following problems?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
1	Modes of Commuting					
2	Commuting Time					
3	Road Conditions					
4	Incidence of Traffic Accidents					

IV. Housing

How serious are the following problems?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
1	Size					
2	Quality					
3	Leasing Procedures					
4	Rent					
5	Utility Costs					
6	Power Supply					
7	Gas Supply					
8	Water Supply					
9	Sewerage					
10	Waste Treatment					

V. Food

How serious are the following problems?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
1	Availability of Ingredients					
2	Employment of Cooks					
3	Restaurants					

VI. Healthcare

How serious are the following problems?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
1	Incidence of Sickness and Injury					
2	Availability of Clinics/ Hospitals in the Vicinity					
3	Availability of Japanese/ Foreign Doctors					
4	Technical Level of Local Doctors					
5	Availability of Operations					
6	Medical Expenses					

VII. Education for Children

How serious are the following problems?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
1	Japanese/ International Schools					
2	Available School Levels (Primary, Junior High, High School)					
3	Teachers					
4	School Facilities					
5	Special Educational Institutes (e.g. Preparatory Schools)					
6	Kindergartens (Childcare)					

VIII. Relationships with Neighbours

How serious are the following problems?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
1	Community Groups					
2	Interaction with Neighbours					
3	Support When Necessary					

IX. Convenience of Life

How serious are the following problems?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
1	Sport and Recreation Facilities					
2	Tourist Attractions					
3	Supermarkets and Speciality Shops					

X. Overall Living Environment

How serious is the following problem?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
1	Overall Living Environment					

Thank you for your cooperation.

Preparatory Study on JICA Cooperation Program for Industry Development (Investment Climate Improvement in Karachi)

Questionnaire about the Living Environment of <u>Local Employees</u>

Notes

- The study aims to identify issues about 1) the legal system and administrative organs for approval and licensing and 2) the living environment of company employees, suggest action plans to resolve the issues, and develop a policy matrix for improvement in the investment climate with the formulation of Japanese ODA program and projects in mind. Your response will be used exclusively for the purpose of the study. Your response will be used in such a manner that the respondent cannot be identified.
- Please **<u>tick the option that best describes your view</u>** in Parts II to III.
- If you have any questions, please feel free to contact Izumi Ogawa, JICA Study Team:
  Address: Board of Investment Karachi Office, Syedna Taher Saifuddin Memorial Foundation, 3rd Floor, Plot No. CD-10/20/2, Beaumont Road, Civil Lines, Karachi
  Mobile: +92 336 5147270 E-mail: ogawa-iz@n-koei.jp

I. Respondent Information

Company name:

Address:

Phone: Fax:

Respondent's name:

Respondent's designation:

E-mail:

II. Security

How serious are the following problems?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
8	Threats of Terrorism, Guerrillas, Civil War, and War					
9	Incidence of Damage by Robbery, Kidnapping, Assault, Menaces, and Fraud					
10	Property Damage by Robbery and Burglary					
11	Police or Military Investigations					
12	Police Services					
13	Employment of Security Guards					
14	Damage by Natural Disasters					

III. Commuting

How serious are the following problems?

S/N	Item	Seriousness of the Problem				
		Very Serious	Serious	Average	Minor	Very Minor
5	Modes of Commuting					
6	Commuting Time					
7	Road Conditions					
8	Incidence of Traffic Accidents					

Thank you for your cooperation.