FOREIGN INVESTMENT ENVIRONMENT IN PAKISTAN

Foreign Investment Advisory Service
a joint facility of
International Finance Corporation (IFC) and
Multilateral Investment Guarantee Agency (MIGA)

1818 H Street, N.W., Washington, D.C. 20433, U.S.A.

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A report by the
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EXECUTIVE SUMMARY

i. By wanting to attract foreign direct investment (FDI), Pakistan finds itself part of a regional and worldwide competition with countries aiming at inviting foreign investors to participate in their economic development. To succeed the Government of Pakistan needs to take the necessary policy, legal, administrative and institutional measures to improve the country's FDI climate. Based on a 1990 Time Magazine survey, Pakistan ranked lowest among 11 Asian countries in offering good trade opportunities, being open to change, and ease of doing business. The country ranked second from last for encouraging foreign investment.

ii. As part of its efforts to create a conducive investment climate, the Government invited the IFC/MIGA Foreign Investment Advisory Service (FIAS) to review its current achievement and to identify areas where additional improvements were required. Also, the Government and MIGA sponsored an investment promotion conference, held in November 1991.

iii. Although FDI flows into Pakistan seem to have more than doubled in the second half of 1980s, fresh inflows have been limited to US$30 million (see Table 1). FDI flows into Pakistan, expressed as totals or in relation to GDP, domestic investment or per capita, do not compare favorably with those of Indonesia, Malaysia, Thailand and Turkey, particularly in the last four years, since these countries adopted measures to enhance their FDI environment (see Figure 1). Pakistan compares even less favorably with these countries on a number of indexes of physical and human infrastructure, known to play a key role in attracting FDI (see Table 2-A & 2-B). The implication for budget expenditures is obvious if the Government intends to establish the foundation for a long and sustained industrialization and FDI inflows.

iv. The Government has recently taken a number of measures to liberalize the economy and encourage domestic and foreign investment. While these measures have instilled a certain degree of confidence in business circles, a number of impediments in the FDI environment remain in Pakistan. FIAS believes that Pakistan has the potential to attract higher volumes of FDI. To fulfil that potential and to ensure that FDI achieves an economic return to Pakistan, the present reform process needs to be continued and extended, and the impediments, be addressed.

v. FIAS has identified four critical elements in the reform process, each of which must proceed apace to help Pakistan achieve its FDI objectives. The first, is <u>political stability, law and order</u>. While this factor is beyond the competence of FIAS to evaluate, it is of paramount concern to the business community and a strong impediment to investment.

vi. The second, is <u>macroeconomic adjustment</u>. Pakistan needs to continue to address issues of economic policies, budgetary imbalances and privatization, all of which have an impact on FDI. For example, larger and more beneficial flows of FDI may be triggered by removing Pakistan's anti-export bias, which today discourages outward-looking investment flows, that have contributed to turning Thailand and Malaysia into exporters of sophisticated industrial goods.

vii. The third, is to further address specific issues related to investment policies and procedures, such as:

a) Due to short-term budgetary pressures, new taxes were imposed, which the business community considers *ad hoc* and counter to the industrialization drive;

b) Contradictory aspect of the investment policy, such as allowing 100 percent foreign equity ownership, yet requiring businesses over Rs100 million in equity to become public companies;

c) Overly generous investment incentives, that are likely to be ineffective and poor substitute for the development of infrastructure, as experiences in other countries have shown;

d) The complex, uncertain, at times weak and anachronistic regulatory framework needs a major overhaul. For example, it is not clear whether and when secular or Sharia laws apply; the extensive use of Special Regulatory Orders (SRO) to amend laws has at times created problems in interpreting these laws; laws passed to support the socialistic economic policy of the 1970s are still valid; and the protection offered to foreign investors under the Foreign Investment Act (1976) may have been inadvertently lost due to a technicality in the law; and

e) The establishment and operation of businesses are still mired in bureaucratic delays, and have essentially not changed beyond the removal of sanctioning. Combined with a weak infrastructure, the thicket of regulatory obstacles confronting potential investors accounts for the low implementation rate of approved projects, estimated by the World Bank to be as low as 14 percent.

viii. Finally, the fourth element of needed reform addresses the institutional framework for facilitating investments. Viewed against international experience, the present arrangements in Pakistan (mainly the Investment Promotion Bureau [IPB]) fall short of what is required to attract and implement FDI projects throughout the country:

a) IPB's weak legal basis - established by an administrative order, and lack of widespread recognition as the national investment promotion agency;

b) IPB's limited and unclear scope and functions, and poorly defined internal organizational structure;

c) the absence of a clear independence from the day-to-day activities and decision making of its parent ministry; and

d) serious weaknesses in human resources, able to undertake the specialized work of investment promotion.

ix. To support the top leadership's commitment to liberalize the economy and improve Pakistan's competitive position for FDI in the world, the Government needs to continue to improve trade and fiscal policies, and develop physical and human infrastructure. Also and more specifically, FIAS recommends that the Government undertakes the following:

a) In the short term, the legal bases for the recent policy changes ought to be strengthened and inconsistencies between policies and regulations, eliminated;

b) The administrative process for implementing investments needs to be simplified;

c) An independent, national investment promotion agency [IPB or a newly formed agency] should be established as a parastatal or state body, with a full range of investment promotion functions, a clear legal framework, a structure headed by a board of directors, strong private sector links and culture, appropriate staff and adequate resources. To improve the implementation rate of investment projects, enhance Pakistan's FDI climate and help investors realize their investment, the promotion agency should adopt as priority the development of investor services.

d) For the long term, the Government should streamline all laws and regulations relating to the business environment to remove inconsistencies and have them reflect the new economic climate.

e) Once the investment service function is established, the promotion agency should help develop and implement a long-term investment promotion strategy, including investment generation and image building. Presumably by that time most of the remaining problems in the investment environment will be solved, and Pakistan will have a good story to tell the investment community.

I. INTRODUCTION

1. The Government of Pakistan has expressed a strong interest in attracting foreign direct investment (FDI) and has initiated a number of important reforms to begin to achieve this objective. These efforts to attract investors place Pakistan amid a worldwide trend of, and in competition with, countries aiming at inviting foreign equity owners to participate in developing the domestic private sector. But to succeed the Government of Pakistan needs to take the necessary policy, legal, administrative and institutional measures to overcome the country's poor image among foreign investors. According to a Time Magazine survey conducted in 1990, Pakistan ranked lowest among eleven Asian countries for offering good trade opportunities, being open to change, and ease of doing business. The country ranked second from bottom for encouraging foreign investment.[1]

2. As part of its efforts to create a conducive investment environment, the Government of Pakistan invited the IFC/MIGA Foreign Investment Advisory Service (FIAS) to review its current achievement and to identify areas where additional improvements were required. To this end, FIAS fielded a diagnostic mission in July of 1991. The mission team visited Karachi, Lahore and Islamabad, and held meetings with domestic and foreign investors, financial institutions, chambers of commerce and government agencies. Concurrently, the Government of Pakistan and MIGA sponsored an investment promotion conference, attended by foreign and domestic investors to explore joint businesses in selected sectors.

3. Based on an analysis of these extensive discussions, and in light of worldwide experience, FIAS has concluded that Pakistan has the potential to attract higher volumes of foreign direct investment than it currently receives. The best approach for obtaining such higher volumes will be to continue the present reform process and to extend it to its fullest conclusion in an economy that is broadly open to both trade and investment flows. Indeed, carrying through the reform process not only should lead to larger flows of FDI, but also should ensure that such investment achieves an efficient, economic return for Pakistan.

4. FIAS has identified <u>four critical elements in the reform process</u>, each of which must proceed apace to bring Pakistan to its desired destination of receiving more foreign investment. The first of these is <u>political stability, law and order</u>. While this factor is beyond the competence of FIAS to evaluate objectively, so many investors raised this point with the mission team that it appears to be of paramount concern to the business community. Indeed, the importance of this factor is not unique to Pakistan. International research on the investment decisions of multinational firms shows that political stability, law and order are often ranked among the top factors influencing choice of investment location.

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[1] Reported in the <u>Dawn</u>-Economic and Business Review, Pakistan, February 2-8, 1991.

5. The second element of critical importance for attracting FDI is macroeconomic adjustment. Pakistan is already engaged in major efforts with the IMF and the World Bank to address its trade and budgetary imbalances. The success of these efforts is vital for creating an overall economic framework in which foreign investors can conduct business. Specifically, larger flows of FDI may be triggered by removing the major anti-export bias, which today discourages outward-looking investment. Indeed, having pursued a protectionist policy, Pakistan has denied itself access to a large pool of international investment. This pool has provided billions of dollars in recent years to transform countries such a Thailand and Malaysia into exporters of sophisticated industrial goods. Pakistan would find that by correcting its anti-export, protectionist bias it too could hope to achieve access to this pool of export-oriented investment.

6. The third element required in the reform process is to further liberalize specific investment-related policies and procedures. Pakistan has begun to take important strides in this direction, including limiting the approval process (sanctioning) to a short negative list of activities. Nonetheless, FIAS spoke with many investors who claimed that the process of establishing and operating businesses in Pakistan is still mired in bureaucratic delays. In fact, the thicket of regulatory obstacles confronting potential investors may help to account for the extremely low implementation rate of approved projects, which the World Bank has estimated to be only 14 percent.[2]

7. Finally, the fourth element of necessary reform addresses the institutional framework for facilitating investments. This organizational dimension is critical for encouraging a greater flow of new investment and providing assistance to foreign investors. Yet in Pakistan this element is lagging behind improvements in macroeconomic and investment policies. Efficiently functioning institutions are urgently needed to encourage more investment and to guide investors through a cumbersome set of laws and regulations. The concept of "service to investors" must become an organizational objective of public agencies in Pakistan. Institutional development should be spearheaded by a dynamic and well resourced investment promotion body, not only to encourage investors but also to ensure that the wider bureaucracy also facilitates private business. Such a body should help raise the implementation rate of new projects closer to the range of 60-80 percent found in countries that are successful in attracting FDI.

8. Progress among each of the four elements of the reform process - political stability, macroeconomic adjustment, investment policies/regulations and institutional structure - is equally important for attrac-

[2] "Pakistan - Towards a New Technology Policy - Sector Report (The World Bank, Washington, D.C., 1986). The implementation rate is based on data from before 1986. Because no significant changes occurred in the FDI environment in Pakistan for the rest of the 1980s, we have adopted the same rate for that period.

ting FDI to Pakistan and the authorities recognize and accept the need for additional measures and further reform. In evaluating what should be introduced in these areas this report firstly highlights some of the main problem areas and weaknesses which are seen to exist in present policies and institutions before going on to make recommendations for change. Some of the problems and weaknesses identified are unique to Pakistan, but many are common to other countries. To be successful in winning investment, particularly FDI, in the face of competition from other countries, the reforms required in Pakistan must match those being introduced elsewhere. The government, therefore, should continue with its reform and introduce further measures along the lines set out in this report.

9. The report focuses on investment policies/regulations and institutional structure, two of the four elements of the reform process noted above. Section III identifies problems with specific investment-related measures and offers potential solutions. Section IV diagnoses the present weakness of institutional structures and prescribes means to strengthen this element. As a forerunner to both these analytic sections, Section II describes the current situation in Pakistan by reviewing data on the existing flows of FDI, comparing Pakistan's business environment to that of selected countries and noting the progress-to-date on macroeconomic and investment-policy reforms.

II. THE PRESENT SITUATION AFFECTING THE INVESTMENT ENVIRONMENT

A. Flows of Foreign Direct Investment

10. On the surface, it appears that Pakistan has achieved a rapid increase in FDI inflows since 1986. Data reported by the IMF balance of payments statistics suggest that net FDI inflows to Pakistan have increased two-and-one-half times for the 1986-1990 period, from US$105.2 million to $249.1 million (see Table 1), for a high average annual growth rate of 24 percent. While this growth rate is over twice the growth rate achieved in the developing world for that period, the data overstate the amount of true FDI in Pakistan, since they include a number of elements, such as portfolio investments and other long-term and short-term capital flows that are not usually considered to be direct investment. To assess the amount of new FDI inflows, data from the Pakistan Economic Survey, published by the Ministry of Finance, show an annual average of only about US$30 million of fresh FDI inflows for 1987-89 (see Table 1). Also, according to the data published by the Investment Promotion Bureau (IPB), during the 1978-1988 period, 168 FDI projects totalling US$2,210 million were sanctioned, or US$201 million per year.[3] A World Bank study estimated the FDI realization rate to be 14 percent by value of approved investment for approximately that same period, or an average of US$28.14 million of new FDI per year.

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[3] Cited in Mahmood Iqbal, " Foreign Business Collaborations in Pakistan" (for full reference, see note in Table 1).

Table 1: NET FDI FLOWS TO PAKISTAN
(Current US$ Million)

Source of Data	1986	1987	1988	1989	1990
IMF BoP data	105.2	128.8	185.6	209.6	249.1
Pakistan economic survey /a	92.4	21.3	38.6	32.6/b	

/a Cited in Mahmood Iqbal, "Foreign Business Collaborations in Pakistan: The Experience of Canada, Japan, The United Kingdom and the United States," The Conference Board of Canada, March 1991.

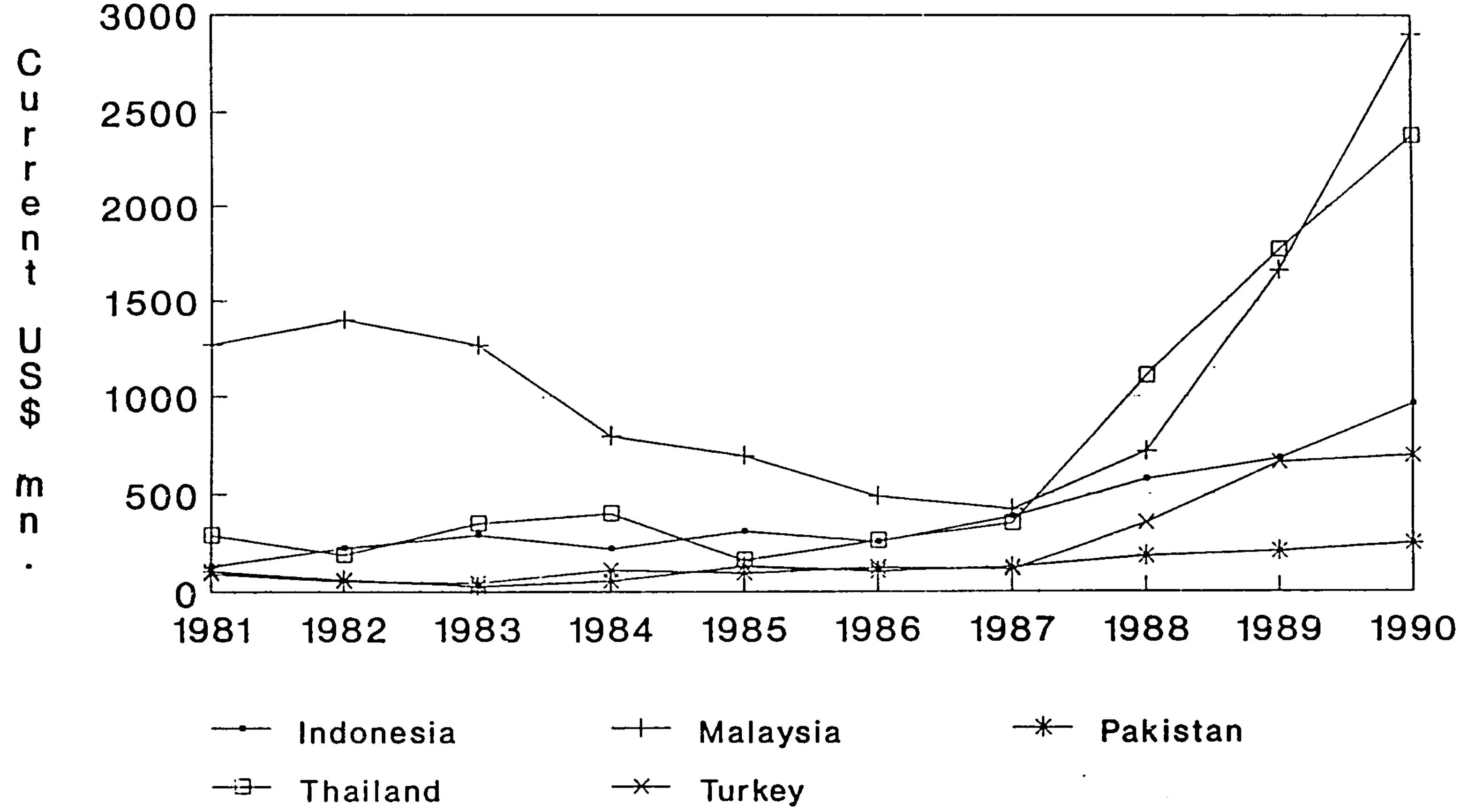
/b for 9 months only.

11. Even if the IMF balance of payment data provided an accurate picture of true FDI flows, Pakistan would be falling below its potential for attracting FDI. Other developing countries, with circumstances similar to those in Pakistan, have succeeded in receiving larger flows of investment. For example, for the 1988-1989 period, only 3 percent of domestic fixed investment was financed through FDI in Pakistan, as against 9 percent in Thailand and 13 percent in Malaysia. Net inflows of FDI stood at 0.5 percent of GPD in Pakistan, compared to 0.8 percent in Turkey, 2.2 percent in Thailand and 3.6 percent in Malaysia. Net FDI inflows per capita was US$1.8 in Pakistan, as against $3.6, $9, $25 and $75 in Indonesia, Turkey, Thailand and Malaysia respectively.[4]

12. Figure 1 shows the impact of two phenomena that have affected FDI flows into Malaysia, Indonesia, Thailand and Turkey in the second half of the 1980s. In the first half of the 1980s, as in Pakistan, FDI flows into Indonesia, Thailand and Turkey fluctuated but showed not much growth. But unlike in Pakistan, beginning in 1986 and surely 1987, FDI inflows grew very fast in all the four reference countries. This substantial growth in Malaysia, Indonesia and Thailand was the combined result of Japan seeking offshore sourcing following the rise of the yen and economic liberalization adopted in the host countries. Unlike its South-east Asian counterparts, Turkey experienced its FDI growth mainly as a result of its economic liberalization.

[4] Derived from data from the World Development Report 1990 and 1991, and Trends in Developing Economies, 1990, The World Bank.

Figure 1 - Foreign Direct Investment Inflows
Pakistan and Selected Countries



Source: IMF BOP Database, BESD.

13. Based on observations made by the FIAS mission, Pakistan seems to have an untapped potential for FDI in a number of sectors, including engineering, energy, transportation, telecommunications, durable consumer products, agri-business and leather products. Textile is one sector which Pakistan ought to develop into a highly integrated -- from cotton crops to garments -- and internationally competitive industry. Pakistan has yet to tap its great export market potential in higher added value textile products. To reach this potential, the country should profit from the technology, product design, marketing know-how, access to international markets and capital that FDI is in a position to offer.

14. Moreover, the attractiveness of Pakistan's untapped potential for foreign investment was clearly demonstrated by the large international participation in the recent Investment Promotion Conference held in Islamabad in November 1991, and co-sponsored by the Government of Pakistan and MIGA. For this conference, specific investment opportunities totalling over $1.5 billion were identified in engineering/electronics, agro-business, textiles, leather, energy, chemicals and fertilizers. The actual realization of these investments however, would significantly depend upon remedial changes in the investment climate as discussed below.

B. Pakistan's Operating Environment in a Comparative Context

15. It would be useful to compare Pakistan's business operations environment to those of Indonesia, Malaysia, Thailand and Turkey, these being countries Pakistan intends to compete with or emulate in terms of attracting FDI. The object of this comparison is not simply to contrast the level of economic development of Pakistan with that of these other four countries, but rather to highlight the important role physical infrastructure and human resources have played in attracting FDI to these countries and providing a conducing operating environment. A number of socio-economic and infrastructure indicators were selected for this comparison. (see Tables 2-A and 2-B). While no one indicator by itself is representative, taken as a whole they provide a realistic picture of a business environment.

16. Pakistan's level of industrialization, expressed as the share of industry in the gross domestic product and as the per capita energy consumption, is substantially lower than that of the four countries. Industry stands at 25 percent of Pakistan's GDP, and at 37 percent, 38 percent and 35 percent respectively of Indonesia's, Thailand's and Turkey's. Pakistan's per capita energy consumption is lower than any of the four countries and one fourth that of Malaysia and Turkey.

17. Pakistan is at an even worse disadvantage when it comes to social sectors, particularly education and health, two sectors key to economic development. Pakistan's adult illiteracy rate is a high 70 percent, while the next highest of the four countries is 27 percent for Malaysia. Only 40 percent of primary-school age children are enrolled in school (28 percent for female), and the lowest rate for the four

Table 2-A: ECONOMIC AND SOCIAL INDICATORS PAKISTAN AND SELECTED COUNTRIES

	GNP/Cap. (US$) 1989	Industry as a share of GDP (%) 1989	Energy Consumption per Capita (koe) a/ 1989	Central Government Share (%) of Expenditure			Percentage of enrollment in Primary School over primary-school age group 1988 b/	Adult Illiteracy (%) 1985	Infant Mortality Rate (per 1,000 live births) 1989
				Education 1988	Health 1988	Defense 1988			
Pakistan	370	24	213	2.6	0.9	29.5	40	70	106
Indonesia	500	37	263	10.0	1.8	8.3	119	26	64
Malaysia	2160	--	920	18.5 c/	6.8 d/	--	102	27	22
Thailand	1220	38	331	19.3	6.2	18.7	87	9	28
Turkey	1370	35	837	12.7	2.4	10.4	117	26	61

a/ koe: Kilogram of oil equivalent
b/ Some countries may exceed 100% because some pupils are younger or older than the country's standard primary school age.
c/ Public spending on education, 1987, in Jee-Peng Tan and Alain Mingat, "Educational Development in Asia," IDP-51, The World Bank, 1989.
d/ Charles C. Griffin, "Health Section Financing in Asia", IDP-68, The World Bank, 1990

Source: The World Bank, The World Development Report - 1990 and 1991.

Table 2-B: INFRASTRUCTURE INDICATORS PAKISTAN AND SELECTED COUNTRIES

	Road Network (mid-1980s)					Vehicles per '000 Population (1988)		Electricity produced per capita (Kwh) 1988	Population with acess to sanitation (Percent) 1988	Telephones per '000 population 1988
	Density in Km per		Percent Paved	Good to Fair condition (percent)						
	1,000 population	$1million of GNP		Paved	Unpaved	Cars	All Vehicles			
Pakistan	1.2	3.30	44	68	30	4.7	12.1	348	20	6.0
Indonesia	1.3	2.85	62	60	69	5.5	45.2	241	39	4.7
Malaysia	2.5	1.29	66	88	n.a.	78.9	246.6	1018	25	73.8
Thailand	3.1	3.07	21	80	75	15	91.6	685	78	18.5
Turkey	6.1	4.79	63	n.a.	n.a.	24.3	44.5	893	64 a/	91.5

a/ Access to safe water

Source: Asif Faiz, "Financing Infrastructure Development." Paper presented at the Conference on "Financing Pakistan's Development in the 1990s," Lahore, Pakistan, December 1991.

reference countries is 87 percent for Thailand. About 8 percent of total government spending[5] (including 2.6 percent from the central government) goes to education, the lowest of any of the four countries, and less than half of Malaysia's (18.5 percent) and Thailand (19.3 percent). Only 0.9 percent of the central government budget goes to health[6], half that of Indonesia and seven times less than Thailand's and Malaysia's. Pakistan's infant mortality rate is a high 106 per thousand, as against 64, 61, 28 and 22 respectively for Indonesia, Turkey, Thailand and Malaysia. On the other hand, Pakistan spends 29.5 percent of its budget on defence, against 8.3, 10.4 and 18.7 respectively for Indonesia, Turkey and Thailand.

18. The infrastructure of any of the four countries compared favorably with that of Pakistan. This fact puts Pakistan at a serious disadvantage for attracting FDI, because infrastructure constitutes an important factor in foreign investors' decision making process. Because of its low per capita GNP relative to the four countries, Pakistan compares well in terms of density of roads per dollar of GNP, but not in terms of density per population. After Thailand, Pakistan has the lowest percentage (44 percent) of paved road, and by far the lowest percentage (30 percent) of unpaved roads in good or fair condition (69 percent for Indonesia being the next lowest). The density of cars is comparable to Indonesia's, but three times less than Thailand's, five times less than Turkey's and 16 times less than Malaysia's. The density of all vehicles is even less favorable: about a quarter of Indonesia's and Turkey's, one eighth of Thailand's and 20 times less than Malaysia's.

19. Pakistan has six telephones per one thousand people, as against to 4.7, 18.5, 73.8 and 91.5 for Indonesia, Thailand, Malaysia and Turkey. Only 20 percent of its population have access to sanitation, as against to a range of 25 percent to 78 percent in the other four countries. Pakistan's amount of electricity produced per capita is higher than Indonesia's, but ranges from one third to one half of the other three countries.

20. The economic development successes of these four countries have resulted not only from the economic liberalization approaches they have adopted, but also from their deliberate and sustained investment in human resources and physical infrastructure. Such an investment is a key ingredient to long-term economic development. It is clear from this comparison that Pakistan falls short in these two sectors. If it truly wants to emulate or compete with these four countries, the Government needs to review its investment priorities accordingly.

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[5] World Bank estimate.

[6] Provincial government and private sector expenditures in the health sector in Pakistan are unavailable.

C. Macroeconomic Situation

21. Pakistan's poor performance to date in attracting FDI is indicative of deeper economic problems. In the late 1980s, Pakistan faced severe double deficits. The external current account deficit deteriorated in 1988 and 1989, due to, among other factors the decline of its terms of trade combined with stiffer international competition for its traditional exports, its heavier debt servicing burden, and lower remittances from workers abroad. At the same time the fiscal deficit went over 8 percent of GDP in FY87 and FY88[7], and public domestic debt to GNP increased substantially to 40 percent in 1988, double what it was in the early 1980s. Government revenues were constrained by a narrow tax base and inefficient tax administration. Inefficiencies of public enterprises remained a heavy financial burden, contributing to the decline of development expenditures and the neglect of infrastructure development. Both external and domestic deficit financing substantially increased debt servicing, limiting Pakistan's ability to tap the financial markets.

22. To address the worsening economic situation, in the mid-1980s the Government initiated a three-year macro-economic and structural adjustment program, supported by a fifteen-month stand-by arrangement of the IMF, a three-year structural adjustment facility arrangement of the IMF in consultation with the World Bank, and Bank adjustment lending in agriculture, energy and financial sectors. Another Bank adjustment loan in industry and trade is being considered at the present time.

23. The adjustment programs include structural fiscal reforms aimed at reducing inflation and the double deficits, and lessening anti-export biases. A foreign trade liberalization program is to gradually replace non-tariff barriers by tariffs, followed by a reduction of effective rate of protection of materials, intermediate goods and capital goods. To support the on-going import liberalization, and to promote exports, the Government began to manage the exchange rate more flexibly and to gradually loosen its foreign exchange control.

24. The Government has initiated measures to reduce its policy-imposed control or reduce impediments to the domestic mobilization of resources. These measures have included reforming the pricing system of publicly produced or administered goods and services, and restructuring public enterprises and prioritizing public investments. Also, private sector investments have been greatly encouraged in a variety of sectors, including infrastructure, while at the same time the Government has embarked on a privatization scheme for state-owned enterprises.

25. With these changes, the Government initiated the opening of the domestic economy. All the measures cited above are but the beginning of a difficult but necessary process of reform. The deepening and eventual success of the reforms will be vital for attracting foreign investors,

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[7] Pakistan fiscal year is from July 1st to June 30th.

particularly ones interested in export-oriented operations. In turn, new foreign investment will help to reinforce macroeconomic adjustment by creating employment, generating tax revenue and adding to foreign exchange reserves.

D. Investment - Related Policies and Regulations

26. Since late 1990, the Government in Pakistan has initiated a number of policy and regulatory measures to improve the business environment in general and attract FDI in particular. Based on our observations and notwithstanding some reservations on the part of business people, which are discussed later on in the report, domestic and foreign business circles have welcomed these measures, strongly support them and have found them to be credible. The following is a brief and partial presentation of these measures.

27. The requirement for government approval of foreign investment has been removed, with the exception of projects in industries included in the Specified List, which are: (a) arms and ammunition, (b) security printing, currency and mint, (c) high explosives, and (d) radioactive substances. In addition to the restrictions imposed by the Specified List, foreign investors are prohibited from investing in agricultural land, forestry, irrigation, real estate, radioactive minerals, insurance, and health and allied services. Investments in all other industries are open to domestic and foreign investors alike, and require no approval.

28. Prior to 1990, all FDI projects had to be approved. Later on, the regulations were modified to exempt FDI projects with equity under Rs.1 billion. At present, sanctioning is removed irrespective of the size of a project. The new policy of allowing 100 percent foreign equity ownership should reduce, if not remove, the pressure exerted by the authorities for foreign investors to take on domestic partners. Also, foreign firms are now permitted to engage in export trading activities.

29. The No Objection Certificate (NOC), issued from Provincial Governments to locate a project in their territory has been one of the bottlenecks in the approval process. Now, it appears that these Governments have declared so-called negative areas, where locating projects is not desirable and for which a NOC is still required. In principle, although not in practice as we shall note later, industrial projects can be set up outside the negative areas without a NOC.

30. One of the most important measures taken recently by the Government affecting FDI was the liberalization of the foreign exchange system. Residents and non-resident Pakistanis, and foreigners are now allowed to bring in, possess and take out foreign currency, and to open accounts and hold certificates in foreign currency. Foreign exchange accounts may now be operated from outside Pakistan. Unspent deposits in local currency, if originating in foreign exchange, may be converted back into the desired foreign currency and repatriated.

31. Foreigners using foreign exchange have now access to the capital market. For example, no permission is now required to issue shares of Pakistani companies to foreign investors or to transfer their shares between foreign investors, unless they belong to industries included in the Specified List. Companies have to go public when their paid-up capital is over Rs.100 million, instead of Rs.50 million (this requirement is in contradiction with the allowance for 100 percent foreign equity ownership, as discussed in para. 49). The prices of shares to be issued are now to be determined by the market and not according to specified government regulations, as they were previously.

32. Remittance of principal and dividends from FDI and from portfolio investment made by foreign and non-resident Pakistanis investors are allowed without prior permission or clearance from the State Bank of Pakistan (SBP). Only banks, insurance companies, foreign airlines and foreign shipping companies still require the SBP's permission for their remittances.

33. Managerial and technical personnel are not anymore required to obtain a work permit. Up to 50 percent of the monthly income of foreign nationals working in Pakistan may be remitted abroad. Upon the foreign nationals' return from Pakistan, they are allowed to repatriate all their savings.

34. Additional reform measures have been introduced to meet financial needs of foreign firms. Foreign-controlled firms may borrow rupees for their working capital from domestic financial institutions without permission from the SBP. These borrowings cannot exceed the equity of the foreign investor. Those that export a minimum of 50 percent of their production face no statutory limits on their domestic borrowing. Also, no permission is required for domestic loans used for fixed investment. Finally, the interest rate and repayment period for foreign loans need not now receive the approval of the SBP, if such loans are not guaranteed by the Government.

35. The elaborate controls that used to be imposed on the transfer of technology have been entirely removed. Technology buyers face no more ceilings over the amount of royalties and technical fees they are allowed to pay. Such amounts are now to be set by the market. Similarly, limits on advertising fees have been lifted.

36. To stimulate investment and export, the Government has adopted a set of fiscal and monetary incentives, some of which we believe are either unnecessary or counterproductive, as discussed later in the report. Industrial projects set up between December 1st 1990 and June 30th 1995 enjoy a three-year tax holiday, extended to five and eight years for projects in rural and underdeveloped areas, as specified. Imported machinery not manufactured locally is fully or partially exempted from import duties, depending on whether a project is located in a rural area, underdeveloped area, or industrial estates. In the latter two types of location, import surcharge and sales tax for such

machinery are also eliminated. Moreover, projects set up between July 1st 1991 and June 30th 1996 in the North West Frontier Province are exempted from sales tax on their output for a period of eight years.

37. A variety of other fiscal and monetary incentives are offered for projects in selected industries, the development of which is being encouraged in specific regions or across the country. These industries include electronics, tourism, pharmaceutical, dairy farming, mining, engineering, fertilizer and cement.

38. Export incentives have been introduced or enlarged. The 55 percent income tax rebate on export earnings was changed into a 75 percent rebate for export of high added value products, including engineering and electronics goods, and textile and leather garments, and a 50 percent rebate for all other products. The highly cumbersome duty-drawback system is being replaced with a scheme whereby 80 percent of the duty-drawback is paid automatically within three days to the firm, and the remaining 20 percent is paid within one week after inquiry. Finally, the import policy has been partially liberalized: the average import duty on raw materials was lowered, a number of quantitative restrictions and non-tariff barriers were removed, and the negative list of imports was reduced.

39. It is clear that these measures taken by the Government to improve Pakistan's investment policies and the FDI climate constitute a major step towards liberalizing the economy. These measures reflect the new economic development philosophy existing at the highest level of the Government, which ascribes a prominent role in economic development to the private sector and a diminishing one to the Government in the micro-management of the economy. It is this perceived new development philosophy and the corresponding measures taken up to now that have lent credibility within business circles to the Government's efforts at liberalizing the economy and enhancing the FDI environment.

III. POLICY AND REGULATORY IMPEDIMENTS TO FDI

40. Pakistan's FDI environment is in the early stages of a transition from a controlled system to a more liberal regime. Without diminishing the importance of the positive measures the Government has adopted, it is important to identify some of the remaining impediments so that the Government can take action to overcome them, maintain the liberalization momentum and position Pakistan as an attractive location for FDI. These impediments have been identified through discussions with representatives of the private sector in Pakistan and FIAS's analysis of the data collected on the business environment in Pakistan, bearing in mind the successful experiences of other countries. Six important ones are discussed in this section. They are:

a) Inconsistency between investment objectives and trade policies;

b) Inconsistency of stated policy objectives and actions;

c) Weak infrastructure;

d) Ineffective investment incentives;

e) Impediments in the regulatory framework; and

f) Complex and costly administrative procedures.

A. Inconsistency between Investment Objectives and Trade Policies

41. Despite the beginning of reform, Pakistan's trade regime remains protectionist and is still heavy with economic distortions. Maximum tariffs were recently lowered from 125 percent to 90 percent, and the coverage of non-tariff barriers has been declining in the last three years. However, the average tariff rate is still about 60 percent. In addition to customs duties, an import surcharge and iqra are levied on imports.

42. At the same time, there is a wide variation in effective protection due to inconsistencies in implementing trade policy. Tariffs, though high on average, are extremely dispersed and have a high incidence of exemptions. The Government tends to accommodate demands for protection, thus favoring a few activities, such as selected cotton manufactures and selected heavy industries, while providing very low (or negative) protection to others. Also, other policy objectives, e.g. regional development and export promotion, have tended to be met with extensive concessions on tariffs and other import taxes. The upshot is that actual tariff collection is only about one quarter of import value, well below the average statutory rates of about 60 percent. Also, the use of numerous exemptions has made the trade regime less simple and transparent, leading to anomalies in the structure of protection and opportunities for correction. The recent introduction of the investment incentive schemes mentioned earlier is bound to compound this problem, as discussed in Section D below.

43. Despite the exemptions, Pakistan relies heavily on trade taxes for revenue. Trade taxes (including tariffs, import surcharge, and the iqra) accounted for an annual average of 38 percent of budgetary revenues between 1984/85 and 1989/90. However, these revenues are generated using a very narrow import tax base. About 80 percent of tariff revenues are collected from 400 commodity categories (out of 5,360), and most of these items carry tariffs of 60 percent and higher. Often, tariffs are adjusted in response to revenue resources needed from year to year, especially on these 400 items. Government's reliance on trade taxes for fiscal revenues combined with very slow pace of resource mobilization from domestic taxes have been a major reason for the slow pace of tariff reforms.

44. Continuing protectionism has had two negative consequences on Pakistan's ability to attract and benefit from FDI. First, foreign investment which is enticed by the country's protected market has little

reason to strive for efficiency, meaning that Pakistan is liable to attract investments with dated technology and high cost production. Second, the most damaging consequence of protectionism has been to install an anti-export bias throughout the economy. Potential foreign investors for the most part do not look to Pakistan as a platform for labor-intensive production and export. At a time when wage pressure is forcing investors to leave Singapore, Malaysia and other traditional sites, they are looking to countries such as Sri Lanka and Indonesia, but not to Pakistan. By discouraging this type of investment through continuing protectionism, Pakistan is denying itself from realizing its own comparative advantage for attracting FDI.

45. Attracting foreign investment that can and will produce for world markets is one of the main objectives of the recent liberalization of investment policy. Because the effective demand of the domestic market is relatively small in most sectors, it is only investment oriented to world markets that could be available in sufficient quantities to make a difference in Pakistan's development. Yet continuation of policies with an anti-export bias virtually precludes attracting such investment in substantial quantities.

B. Inconsistency of Stated Policy Objectives and Actions

46. A number of inconsistencies exist between stated policies on the one hand, and the actions of the Government and relevant regulations on the other. These inconsistencies stem mostly from the complex incentive policy and system, the need to increase national revenues, and the magnitude and speed of policy changes which have created problems of coordination among government agencies and time lags in the regulatory framework. If not properly addressed, these inconsistencies will lower business confidence and government credibility.

47. The Government tends to accommodate demands for protection and meet other objectives (e.g. regional development) through the provision of extensive concessions on tariffs and other taxes. Moreover, incentive programs have tended to change rather frequently, and some were removed before their stated expiration period. The resulting complexity and lack of transparency of the trade and tax regimes have caused inconsistencies with stated policies and does not help raise business confidence.

48. The imperatives to increase national revenues seemed to have compelled the Government to adopt a set of measures that have been perceived as being contradictory to its most recent stated policy of industrialization, notwithstanding the generous tax holiday schemes extended to new industrial projects. In the 1991/92 budget, companies are required to pay a one time Corporate Assets Tax in 1992, based on the value of their assets. Similarly, a total of a 1/2 percent turnover tax was imposed on companies which have no taxable income (including those which qualify for a tax holiday), and on those whose total tax bill would amount to less than that 1/2 percent of turnover. Withdrawal of the tax credit and of the initial additional depreciation for invest-

ments made under the Balancing, Modernization and Replacement (BMR) scheme also appears to be contrary to the stated policies of encouraging investment, and negatively affects on-going business concerns, to which the newly introduced tax holiday schemes do not apply. Finally, non-income transfers from overseas to branches and offices of foreign trading companies to cover, for example, their operating expenses seem to be subject to income tax. This tax penalizes foreign companies wanting to establish business in Pakistan.

49. There are also inconsistencies between stated policy and effective regulations. For example, the Government has announced that 100 percent foreign equity ownership is allowed now. But enterprises with a paid-up capital investment of over Rs.100 million must convert themselves into public companies and offer 50 percent of their capital to the public in Pakistan. Therefore, a foreign firm, whose paid up capital exceeds Rs.100 million and whose preference is to remain 100 percent owned, would find itself facing contradictory policy measures. It is not clear whether this conflict in policies has resulted from the time lag that exists between policy pronouncements and modifying regulations accordingly, or that relevant regulations are not changed or passed to reflect the newly stated policies. In this particular case the Corporate Law Authority (CLA) has sought, on an ad hoc basis, to sanction 100 percent ownership even if the capital investment is over Rs.100 million.

C. Weak Infrastructure

50. The impediments to investment caused by the underdeveloped state of Pakistan's infrastructure were repeatedly mentioned by the business community. It is not necessary to dwell on the state of Pakistan's infrastructure, as its weakness was illustrated through its comparison with that of selected countries in Asia earlier in the report. But suffice to say that many investors have said that it has discouraged investment because of their inability to access or maintain reliable access to electricity, water, gas and production sites. Even some of the industrial estates developed by the Government do not offer infrastructure services adequate for manufacturing operations.

51. Investors face additional aggravation, delays and costs, when they try themselves to remedy the weaknesses of the infrastructure, e.g., by generating their own electricity or back up power, or building their own access road to the plant site. As a result, their domestic and international competitiveness is adversely affected. At a time when many countries are using their developed physical and service infrastructure to attract foreign investors, Pakistan finds itself at a disadvantage when competing for FDI with these countries.

52. The Government is trying to use fiscal incentives to compensate for inadequate infrastructure. However, in many locations in Pakistan, the cost of substituting private arrangements for public infrastructure is so prohibitive that investors are unwilling to invest even with seemingly generous incentives. It may be more advantageous to Pakistan

to lower or remove these fiscal incentives and use the resulting increased revenues toward building up the infrastructure. As the experience of those developing countries that have successfully attracted FDI has shown, "infrastructure incentives" are more powerful in the long term than temporary fiscal incentives.

D. <u>Ineffective Investment Incentives</u>

53. Views on the merits of special incentives to attract FDI are mixed, with a growing number of governments and international agencies recognizing their limited usefulness. Research shows that investors consider incentives to be of marginal significance in determining location of their investments around the world, with some impact on export-oriented projects. More important to them are such factors as political and economic stability, access to markets, skills and resources, the cost environment and the availability of necessary physical and software infrastructure.

54. What is also clear is that the provision of incentives will not make up for fundamental deficiencies in policies, in the availability of infrastructure, or in bureaucratic procedural systems. Providing incentives to investors where such fundamental problems exist has not overcome these problems.

55. As noted earlier, in Pakistan the investment incentives available include general, as well as area and industry specific incentives. The three year income tax holiday, allowed for all newly established industries throughout the country, can be extended to five or eight years in specified rural or development areas. In addition, a number of exemptions on income tax, sales tax and custom duties are available to projects located in specific areas or in specific industries.

56. These incentives have led, however, to concern on the part of many existing investors as to the distortions they have introduced in the investment environment, and to the fact that they discriminate against specific investors. For example, existing investors find it difficult to compete with new investors in the same sector, when the latter are exempted from the sales tax. The removal of the incentives related to BMR again penalizes existing investors in their efforts to update their technology and restructure their production operations, and in the aggregate favors new investments over expanding and raising the efficiency of existing investments. This is because only newly established companies, formed exclusively to take advantage of these incentives, may apply for the incentives. An existing company with a new project finds itself forced to establish a new company to comply with that regulation at additional financial and organizational costs. If the purpose of this requirement is to keep existing projects from trying to pass for new ones, surely there are other methods by which this objective can be accomplished.

57. At this point in time, it is difficult to assess the usefulness and effectiveness of these incentives, as they have been put in place only recently. Nevertheless, the merits of the three-year tax holiday are particularly difficult to identify. The fact that this incentive is available everywhere reduces the real attractions of regional specific incentives in nominated locations. Also questionable, is the broad scope of incentives provided for some industrial sectors, such as electronics, where it is difficult to understand why all elements of the particular sector merit special treatment rather than a targeted sub-sector, for which the country may have a potential comparative advantage. In fact, Pakistan seems to be going against the growing tendency of many countries to radically reform and in some cases to drop many of their special incentive programs. If the incentive package has been adopted to compensate serious deficiencies in the investment environment, then, based on experience in other countries, it is not likely to be successful.

58. Any review undertaken of the incentive package should determine its specific purpose, assess its effectiveness, evaluate alternative and less discriminatory ways of improving cost competitiveness, and establish the ground for removing some of the more serious anomalies in the existing incentive system. Indonesia's experience has shown that the dismantling of its incentive regime in the 1980's has had little negative impact on investment flows. In fact investment approvals there have increased over ten fold since the removal of incentives. These gains have been mainly due to a more liberal investment regime and improved macro economic and sector policies.

E. Impediments in the Regulatory Framework

59. To the extent possible, the Government of Pakistan has attempted to translate its desire at liberalizing the investment environment into implementing regulations. Yet, some fundamental issues need to be addressed by the Government in order to stabilize and strengthen the investment regulations and therefore the overall investment environment. As discussed earlier, inconsistencies and gaps still remain between policy pronouncements and regulations. Procedures for transforming policies into regulations often do not have a strong legal underpinning, thereby causing instability to creep into the regulations over time. Outdated and revised laws remain on the statute books and tend to interfere in the operations of enterprises. Finally, the extraordinary complexity and demands of the regulatory framework remain essentially intact. These factors cause problems for enterprises at the point of entry, upon start-up and during operations, and undermine the credibility of the "Open Door" policy in the eyes of foreign investors.

60. This section focuses on the complexity and stability of the regulatory framework governing investment. The complex and costly administrative process facing investors that has resulted from the regulatory framework is discussed in the next section.

1. Complex and Anachronistic Regulatory Framework.

61. Pakistan is characterized by a complex legal system. Because of its history, many types of governmental regimes can be identified in Pakistan: colonial rule, presidential rule, military government and marshal law, and parliamentary rule. Under each of these regime laws, regulations, ordinances, orders, circulars and administrative orders -- all having the force of law -- have been issued. They are often sustained over an unlimited period of time creating a large and complex network of laws and regulations that can be made applicable at any given time. To add to the complexity, the legal system in Pakistan operates at the federal and provincial levels, although where in conflict, federal laws have precedence over provincial laws.

62. The legal system in Pakistan can also be characterized as a juxtaposition of English and Islamic laws. The two legal systems are administered independently of each other and have their own judicial institutions to oversee the application of the laws (e.g., provisions of the Sharia Act of 1991). The presence of these two legal systems has been a source of great uncertainty, because foreign investors are not sure which of these two systems applies for their business operations.

63. The issuance of Special Regulatory Orders (SRO) is the primary vehicle by which the Government amends and changes laws to implement policies. Over time many SROs may have been issued under a particular law, having the effect of changing the scope and intent of the primary law. A number of cases of nested SROs - a SRO modifying a SRO, which itself may be modifying a prior SRO - have come to our attention. Over time SROs applicable to the same law have been shown to bring to the law incompatible interpretations. Clearly, this situation creates much confusion to the detriment of the business environment.

64. It is common that once a law is passed it remains on the books, even though it may have been rescinded or amended following major changes in policies. For example, orders passed during the socialist approach to economic development in Pakistan are still valid, even though the economic policy has shifted substantially. Cases in point are the Economic Reform Order of 1972 (President's Order No.1 of 1972) and the Industrial Sanctions and Licenses (Cancellation) Order of 1972. While these orders were not invoked against foreign investors at that time or subsequently, their statutory status in Pakistan today is unclear since it is not evident that they have been repealed or amended. If these orders are still valid, then a certain unnecessary degree of uncertainty in the business environment is introduced.

2. Weaknesses in the Regulations Governing Investment

65. The modalities of introducing changes into the regulatory environment have themselves created instances where the strength and the stability of that environment are put into question. In addition to using SROs, government agencies are empowered to introduce changes through administrative orders. For example, the removal of the invest-

ment approval requirement, or sanctioning, was executed by means of a circular issued by the authority of the Chief Research Offices of the Ministry of Industries (Circular No.6 (169/90 Policy), dated January 5, 1991). Also, the Capital Issues (Continuance and Control) Act of 1947, requires government sanctioning of project before the Corporate Law Authority (CLA) registers a company. The CLA passed a SRO to exempt companies from sanction in the form of an exception to a still valid clause for sanctioning in the Act, rather than removing that clause entirely. Neither the administrative circular nor the "exception" SRO legally lend the necessary strength or stability to the removal of the sanctioning requirement.

66. Uncertainty remains as to whether the requirement of a sanction still remains applicable for the establishment of certain foreign businesses. Prior to commencement of business and registration with the CLA, the CLA requires branch offices of foreign enterprises to register with, and obtain approval from, the Investment Promotion Bureau (IPB). Now that the sanction requirement has been essentially removed for foreign investors, it is not certain whether branch offices could be registered with the CLA without prior sanctions from the IPB.

67. Moreover, it appears that internationally recognized standards of protection extended to investors have been inadvertently lost in Pakistan due to a technicality in the law. The Foreign Investment (Promotion and Protection) Act of 1976 offers foreign investors with <u>approved</u> projects protection, such as foreign exchange repatriation facilities, and due process and adequate compensation against the acquisition by the Government of their capital and investment. The removal of the sanctioning requirement (except for the Specified List) has the implicit effect of technically rendering this Act ineffective, and thus removing the guarantees contained herein.

F. Complex and Costly Administrative Procedures

68. Business people are concerned that while project sanctioning has been removed, the process of investment realization remains cumbersome and bureaucratic, and constitutes a serious constraint on investment implementation. Forty to fifty permits and clearances from different government agencies at national, regional and local levels apply to investors. The actual number applicable for a project depends on the type of investment and its market focus with companies selling on the domestic market typically facing most difficulties.[8] Existing investors with considerable resources and experience estimate that this clearance and implementation process can take them up to two years. Such delays are far too long and would shatter the confidence of all but the most committed of investors.

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[8] See Zahid Zaheer & Associates, "Report on Bureaucratic Procedures for the World Bank," 1991.

69. Insufficient power, telecommunications, road access and other infrastructure services contribute to the complexity of the administrative process and to the difficulties in obtaining suitable investment sites. Despite the improvements introduced on paper in the new procedures for the provision of sites, the process still causes difficulties. Regional authorities apparently still demand "no objection" certificates even on sites selected outside the recently introduced restricted list system, partly on account of lack of infrastructure services.

70. Payment of taxes and contributions in Pakistan are complex and cumbersome. In addition to the corporate income taxes, a large number of indirect taxes are levied. Federal levies include import license fees, import and export registration fees, and sales taxes and surcharge on imports. At the provincial level there are stamp duties, professional taxes, boiler inspection fees, and weights and measures fees. In addition, local government taxes are levied, including a local metropolitan tax, the Octroi, trade license fees and export taxes. Both at the federal and provincial levels, labor taxes have to be paid separately in compliance with labor laws, such as the contributions to the Workers Welfare Fund, Employees Old Age Benefit Fund, Social Security, Worker's children's education cess, and Workers participation in profit and group insurance. Essentially, separate collection of taxes and contributions have forced enterprises to face unnecessary, cumbersome, and costly administrative procedures, and to deal with a large number of collecting agencies at all three levels of government.

71. Several existing firms report having to allocate a number of selected staff solely for the purpose of obtaining necessary clearances and of servicing the requirements of the bureaucracy. One senior executive, currently seeking to establish a large overseas project in the country says that the process has taken over two years to-date and as yet there is no clear picture as to the final outcome. This project is of such strategic impact that it could be confidently stated that it would be cleared by authorities in other countries in under six months. Evidence exists of other major and apparently highly desireable projects not proceeding or being abandoned, because of delays and frustrations with the bureaucracy.

72. The complexity of the administrative procedures finds its roots in the socialistic approach to economic development adopted by Pakistan in the 1970s, but is also due to weaknesses in skills and information flow in the operations of the civil service, and the structure and complexity of the regulatory environment. It is clear that one of the major issues that needs to be addressed to enhance the investment environment in Pakistan is to overhaul the administrative procedure facing investors. In doing so, a careful consideration must be given to the roots of the problem, including weaknesses in the civil service and the regulatory environment.

IV. INSTITUTIONAL ARRANGEMENTS FOR FDI

73. The Government of Pakistan has introduced a number of institutional changes, as part of its recent effort to improve the climate for foreign direct investment. The Board of Investments has been removed, sanctioning procedures have been eliminated for all but those industries on the Specified List and the role of the Investment Promotion Bureau (IPB) is being altered from that of a regulatory body to that of an investment promotion agency.[9] The IPB is now charged with the responsibility of providing information to potential investors on a range of items, and of monitoring their investment activities. These new functions of the IPB are set out in an internal departmental administrative order from the Ministry of Industries, where the IPB remains as a department and operates within that ministry reporting through its Secretary.

74. International experience shows that several important issues arise for an organization like the IPB to function effectively as a national investment promotion agency. First, a national investment promotion strategy needs to be formulated, and specific investment objectives and targets set by the implementing agency. Then the form of agency to be established is critical together with its links and ties with Government. Also important are its functions, authority and responsibilities, budget and staff resources needed to fulfill its mission.

75. Viewed against international experience, the present arrangements in Pakistan fall short of what is likely to be required in the future to attract and implement FDI projects throughout the country. These arrangements are weak in a number of ways because of:

- the lack of an explicit investment promotion strategy setting out a targeted programme of activities and resources, which follow from recent policy changes;

- the limited scope of the powers and functions assigned to the IPB. This institution is not now required to facilitate investors' activities, or to engage in any investment generation or image building activities;

- the weak legal basis used to establish the institution, i.e., an administrative order within the Ministry of Industries;

- the absence of a clear independence from the day-to-day activities and decision making of its parent ministry;

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[9] In December 1991, the Government announced the establishment of the Industrial Promotion Board, to be chaired by the Prime Minister. The mission of the Board is to facilitate the industrialization of Pakistan, but its role and working relationship with the rest of the administration are not clear to us at this time.

- poorly defined internal organizational structures to execute the functions of investment promotion; and

- insufficient skilled staff and resources to carry out effective promotion when measured against those available to competitor agencies from other Asian countries.

A. The Elements of an Investment Promotion Strategy - The International Experience

76. The promotion strategies employed by countries to increase inflows of FDI typically involve a range of activities, which can be divided into three groups:

(a) Image-building activities, aimed at building or changing the image of a country in the minds of potential investors.

(b) Investment-generating activities, used to generate investment directly; and

(c) Investment services, directed at servicing existing and prospective investors.

77. It is from these three types of activities, each with its own goals and techniques, that a promotional strategy for any particular country is constructed. Governments with successful promotion programs tend to engage in all three types of activities to varying degrees most of the time. But they usually concentrate attention at any one time on either image-building or investment-generation, with the investment services function being a significant part of all promotion strategies.

78. The priority and emphasis given to any particular element varies depending on the country's requirements, its particular situation, available resources, policy and regulatory framework, market conditions prevailing in the country, and conditions in the international markets. When there has been a recent policy change to encourage inward foreign investment, the promotional organization may focus on image-building to advise the investment community about the governments's new attitude toward FDI and its interest in attracting investors. Image-building may also be used to inform the investor community of positive results or achievements, to highlight a particular event, or to emphasize an issue of strategic importance to investors.

79. When the managers of promotion organizations believe that an appropriate image has been formed in the minds of prospective investors, they often shift in focus to investment generation. Although they begin with a focus on image- building and then shift to a focus on investment generation, some countries continue thereafter to use image-building activities extensively as changing economic conditions within the country or in the external environment create a new need to change or build images.

80. In some situations image-building need not be the initial focus of a promotional program. For instance, if a country does not have a negative image as a potential site for inward investment, and if its strengths as an investment site are already well known in the international investment community, then there is little need to begin operations with a focus on image-building. At the opposite pole, countries with negative investment images that reflect reality may need to begin their efforts by placing the focus elsewhere. For instance, they might work with other government departments to improve the investment climate of their country, or seek to improve the level of service available to existing investors. Advertising a "poor product" is not only wasteful, but it is likely to reduce the credibility of future promotion of the product once improved.

81. Investment generation activities are necessary where the flow of new investments fall short of national objectives and requirements and where the economy wants to expand into new areas of investment because of the availability of resources, comparative advantage, or long term development potential. The techniques used in investment generation include overseas missions and seminars, mail and telephone campaigns, and direct marketing to targeted clients. Many countries have opened overseas offices as part of their investment generation programmes but this approach is expensive and demands substantial budget and staff resources. The financial demands of such a step require governments to be cautious and maximize the benefits from other investment generation activities before taking on responsibility for overseas investment promotion offices.

82. Investment services usually constitute a key element of all promotion strategies and focus on a) providing information on doing business in the host country to existing and prospective investors; b) granting some approvals and facilitating the provision of others, as well as the provision of essential infrastructure; and c) assessing the performance of the promotion agency itself and the effectiveness of the promotion strategy through monitoring project implementation. Services can be provided on an active basis, where staff from the promotion agency seek out investors and actively assist them in problems that arise, or on a passive basis where the focus is on responding to requests. Most promotion agencies find that a strong concentration on investment servicing is justified because it is cost effective, and it emphasizes investment realization as well as investment sanctioning. Also, clients satisfied with the services provided can become the best investment promoters for the country.

83. The service provided to potential investors can include information on the steps needed in obtaining government clearances nationally and locally; availability to raw materials together with any terms and conditions; availability of labor including skilled staff; a range of commercial information on topics such as transport, utilities, credit facilities and market conditions; availability of potential sites

and suitable infrastructure; and names and introductions to key government, business and banking personnel.

84. Facilitation services would help potential investors obtain necessary government clearances and would represent their interests in the different departments and agencies with which they must deal. Such services could also include assistance in setting up a project in a new country, such as arranging contacts with business and community leaders; offering guidance in obtaining necessary permits; accessing infrastructure services, and gaining the support of government agencies when delays or obstacles arise.

85. The performance of the promotion agency and of the promotion strategy must be monitored in order to manage and control the implementation of the promotion strategy, and to improve the services to investors. The principal mechanism used for this assessment is to monitor the progress of FDI projects. Such monitoring includes measuring the flow of approved and realized investments under such headings as source of origin, sector, scale, location within country, and of evaluating these outcomes against planned targets. Monitoring should not be conceived of as an activity to introduce restrictions on investors. Only the policy framework for FDI should define such restrictions, and the monitoring function of the promotion agency should not be used to introduce a hidden agenda of regulations.

B. An Investment Promotion Strategy for Pakistan

86. One of the gaps in Pakistan's investment policy is that it has not been translated into a detailed investment promotion strategy, which would set out and justify the priority promotion activities and techniques to be used in the future and how these might be altered over time. Such a strategy would also need to set out specific investment targets, budget and resource commitments, and evaluation measures for the years ahead. An investment promotion strategy is essential to direct the national investment promotion program and to provide the basis to manage, control and evaluate the agency charged with its implementation. Formulating such a strategy must rank high in the priority actions needed to be taken by the authorities in Pakistan in the future, taking into consideration the types and sources of FDI the country will be able to attract in the coming years.

87. Preparing an investment promotion strategy is a major undertaking and may require the Government to seek external expert assistance and substantial inputs from a number of organizations in the private and public sectors in Pakistan. It is a complex, time consuming and serious exercise that sets the country on a course of investment to meet developmental objectives. It has a number of critical elements, which must be balanced against each other over time.

88. Set against the policy framework now being formulated, and the FDI targets yet to be specified, this strategy should set out and justify whether the <u>initial</u> priority and focus of resources should be on

improving investor services or on image building, or on investment generation activities. It should specify these initial priorities and state how they would alter in the short, medium and long term as investment conditions change and as the flow of projects improve.

89. In the case of Pakistan, the priority should be put on the development of effective investor services. Experience shows that good investor services are essential to the success of any investment promotion strategy and the need for such services is particularly evident in Pakistan. Indeed, there is a great need to facilitate and expedite the administrative procedures foreign and domestic investors face when establishing and operating businesses. Also, there is a great need to provide economic and business information to potential foreign investors who are considering Pakistan as an investment location. These two services, if provided adequately, should contribute substantially to attracting new FDI to Pakistan and should be considered as priorities in its investment promotion strategy.

90. Most investment promotion activities are costly, but image building and investment generation activities are particularly expensive. In the case of Pakistan these two types of activities should be undertaken only after substantial and effective effort has been made to enhance the investment environment. Two key elements of that effort should be the streamlining of the administrative procedures and the creation of investor services. Investment service activities are relatively less expensive and, if properly implemented, can be highly cost effective. Delivering investor services however, while less demanding on budgets, requires highly skilled personnel. The priority activities specified in the investment promotion strategy, therefore, will affect the budget and staffing requirements of the promotion agency.

91. The government or the promotion agency need to use measures from time to time to evaluate the overall performance of the agency, of a specific organization unit or of a specific promotion activity. The main control and evaluation systems applied should reflect and be consistent with the objectives and content of the investment promotion strategy.

C. Institutional Arrangements for Promotion - The International Experience

92. Faced with the range of issues and activities required from investment promotion agencies, governments worldwide have given these agencies different powers and functions, and have established them with different types of links to the government structure. Some have been set up as parastatal bodies, others as direct Government institutions and still others have been set up solely by, or in conjunction with the

private sector.[10] The powers they exercise vary widely. A limited number of agencies have strong central powers, many, a range of coordinating powers, and some, little power, where the investment approval and realization process remains diffuse.

93. Functions also vary among agencies. Some, as in Ireland and Singapore, are responsible for a wide range of investment servicing, image building and investment generation activities, while others are constrained to a more limited set of activities. In most other countries, helping investors implement their projects is among the core investor servicing activities sought from the promotion agency.

94. Research suggests that parastatal bodies are the most effective form of institution for investment promotion because they can incorporate needed private sector promotional skills and procedures, and bring more flexibility to the organization by encouraging subcontracting and exchanging of employees with the private sector. As parastatal, the agencies are under pressure to be more cost effective by exposing them and holding them accountable to the types of risks usually involved in promotion activities. At the same time they maintain close links with government in policy making and investment implementation. Because of these advantages, the parastatal model has become increasingly popular around the world.

95. Experience with private sector promotion agencies is more limited, and, while those that exist have proven to be effective, they appear to require large donor funds for their operation. The private sector in most countries is willing to assist in the promotion process and welcome the chance to participate in it, but is generally reluctant to provide substantial funds for the establishment and running of a national investment promotion agency. An on-going promotion agency needs an alternative source of funds for its operation, and consequently parastatal bodies or direct government agencies are the more usual form of promotion organizations.

96. To implement their investment promotion strategies, most countries have established direct government bodies, when parastatal agencies are not used. When properly established with clear and

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[10] The term parastatal is used to describe a type of agency used widely by governments throughout the world to undertake specialized activities on behalf of the state. These agencies are answerable to the government but separate from it. They are set up and typically funded by the government. Their overall policies and plans are subject to government approval but their day-to-day operations are usually the responsibility of the board established to run them. They conduct their on-going business activities independent of government, although within established policy guidelines. They usually operate independent recruitment and personnel policies, but with limitations on the degree to which pay and conditions can deviate from public sector norms.

independent reporting procedures, such government bodies have been effective. Those that have been most successful have had their own board of directors, and have operated separately from the day-to-day activities of their parent departments. The presence of a clear and independent legal framework for the agency, a separate board for management and control, an exclusive focus and responsibility on investment promotion and realization, and a separation from day-to-day activities of parent ministries are all factors which help improve their performance.

97. Separate and independent investment promotion agencies work best for several reasons. Investment promotion is typically a high profile and reasonably risky activity, the results of which are of significant interest to political, government and business groups at national and local levels. The agency responsible needs to have the authority and responsibility, within policy constraints, to act decisively and with speed on the numerous day-to-day decisions required in promoting, facilitating and monitoring investments. Therefore, the agency needs a clear legal basis to work accordingly, and independence and security to win the confidence of investors and to attract and retain the qualified staff essential to its successful activities. If, as an alternative to a separate and independent structure, its actions are subject to normal department decision-making processes within government and to day-to-day interference in its activities by various interested groups, then the promotion agency cannot be effective in the commercial and competitive environment in which it must operate.

98. Many governments have established their promotion agencies as so-called "one-stop-shop" designed to undertake a range of promotion activities and to facilitate investors in their implementation of projects. The power and functions of these one-stop-shops are not standard but most, if not all, include a strong emphasis on investor servicing, especially on investor facilitation services. Promotion agencies in countries like Singapore and Ireland have consistently emphasized the facilitation element of their business as have the agencies in Thailand and Malaysia. The promotion bodies in Indonesia and the Philippines are moving towards devoting more attention to ways of increasing investment realization with more organization attention and resources devoted to facilitating investors' operations. This facilitation typically is designed to ease difficulties arising from the investors' unfamiliarity regarding the policy and institutional frameworks, from bureaucratic procedures required to establish and operate businesses, from lack of information on local conditions, and from difficulties in accessing infrastructure services.

99. One-stop agencies typically, do not have the power to issue all necessary permits or clearances for approval or to provide the facilities needed to implement investments. Rather, they seek to inform investors and assist them through the bureaucratic process; they help with important introductions to local people and organizations; they guide on local practices and procedures; and they assist in the numerous steps required to implement a new investment in a new community.

100. Strong central agencies, which come closest to matching the real meaning of one-stop agencies, exist in Ireland and Singapore. Even here, however, the agencies do not have the powers to issue all necessary clearances or to provide all necessary facilities to investors. Approvals from these central agencies are followed quickly by needed clearances from other government agencies and the central agency co-ordinates the process. These strong central agencies are particularly attractive to incoming investors as their direct and "assumed" powers enable the investors to overcome many potential bottlenecks.

101. Most governments seeking "one-stop-shop" mechanisms have preferred coordinating procedures to establishing strong central agencies. These coordination procedures have operated with varying degrees of success. Some which are based on tight coordination and strong leadership work well, others with diffused operating systems are often as much of a hinderance as a help. Countries such as Thailand and Indonesia have devoted considerable efforts to establishing coordination procedures that are effective. The results of these efforts are clear in both countries and particularly in Thailand.

102. The least preferred and least successful system for promoting FDI, is the diffuse system where in the absence of a centralizing agency, investors must go to all responsible agencies and obtain the necessary approvals. Where such diffuse systems are in operation they have been seen to be ineffective and are disliked by investors.

103. The overall performance of promotion agencies is also determined to a great extent by their internal organization structure, and the skills and experience of their staff. Internal structures should clearly identify internal units according to the functions and responsibilities required from the organization.

104. Ideally individual units should be assigned specific targets annually. For example, they may be required to deliver a specified level of investment, to organize a specific number of identifiable missions or other promotional events, or to develop organize and prepare specific information. These individual unit targets would collectively form the annual target for the agency, which in turn would be part of its medium-term investment promotion objectives. Internal structures should identify the units which carry the authority and responsibility for main tasks. Management and control systems must be installed to link, measure and evaluate the overall organizational objectives with the specific activities of individual units.

105. The skills and experience of staff in carrying out promotion activities constitute a determining factor to the agency's success and impact in winning FDI projects. Promotional skills and experiences are not normally found in government bodies and especially not in bodies whose established role has been in regulation rather than promotion. Properly skilled staff must be taken on board and existing staff need

extensive training both on and off the job, before satisfactory performance can be expected from any investment promotion agency.

D. Institutional Arrangements in Pakistan

106. The range of policy changes recently introduced in Pakistan substantially improves the framework for FDI in the country, but the proposals for institutional reform do not go far enough or may not in the end support the "Open Door" policy. To date no specific investment promotion strategy has been formulated. The agency responsible for investment promotion is part of a Government department, has a narrow mandate and is not familiar with the techniques of modern promotion: its staff has no background or training in the skills required for promotion.

107. In Pakistan, IPB's official mandate gives it a limited range of activities: providing information to investors and monitoring investments to help identify future investment opportunities. It does not have the full range of responsibilities typical of an investment promotion agency, i.e., investment generating, image building or investor servicing. For example, IPB is not responsible for coordinating or facilitating investors in obtaining the wide range of clearances necessary from different government bodies, although occasionally, its management have intervened on an ad hoc basis to speed up the issuance of permits when long delays had been encountered. With no established formal institutional arrangements to facilitate investors in realizing their projects, the investment implementation process in the country remains complicated and diffuse, an approach that has given disappointing results, according to international experience.

108. IPB now lacks a clear and separate legal status, supported by specific legislation. Its present existence and functions have been established through an administrative order, which does not provide it the degree of stability and permanence that legislation would. Furthermore, as the national promotion agency, IPB is called upon to attract investment in a variety of economic sectors in addition to industry, including agribusiness and food processing, tourism and infrastructure. As these sectors are outside the purview of any one ministry, it makes sense to house the investment promotion agency outside any one of the ministries, or alternatively to grant it enough autonomy and national status to allow it to function as an extra-ministerial body and to deal with the widest possible range of sectors. Furthermore, as a department within a ministry, headed by a vice-chairman who belongs to the line of authority of that ministry, the IPB lacks both the status, the authority and the autonomy needed for an investment promotion agency to operate successfully and lead the implementation of a national FDI policy.

109. At present, investment facilitation boards are operated by provincial governments in Pakistan, and at the national level the Economic Coordination Committee (ECC) of the Cabinet constitutes the highest level of economic policy coordination. Currently, no formal links exist between IPB and these boards or the ECC nor could they exist

in light of the IPB's current place and structure within the Government. These boards and the ECC can conceivably form with IPB the nucleus of institutional arrangements to help in the investment facilitation process at national and provincial level. For example, very difficult problems or undue delays can be referred for resolution to higher authorities, such as the ECC. Similarly, IPB can enlist the help of provincial boards to expedite many of the administrative procedures that investors face at the local level.

110. Also, presently IPB lacks the financial resources necessary for its operations as the national promotion agency, as it is purported to be. It appears that over 80 percent of its budget is needed just to cover its own payroll, leaving inadequate funds to conduct the variety of promotion activities such an agency is called upon to do.

111. IPB faces serious deficiencies in its staff technical skills. Very few of its staff have been exposed to any of the three main groups of promotion activities. Moreover, IPB has essentially and primarily been a regulatory and not a promotion agency. Its staff's mindset, experience and culture are bound to be colored by IPB's past experience.

112. Chart I outlines the main steps that need to be addressed in undertaking the fundamental institutional reforms required to win more FDI. A first step is the preparation of an investment promotion strategy for the country. The next step is to decide on the functions and structure of the promoting agency, including the role it should play in helping investors realize their projects in the country. Serious consideration is to be given on whether the investment promotion agency should be established as a parastatal body, as a direct but independent government body, or as a private sector body run exclusively or partially by the private sector.

113. In view of the Government's intention to attract FDI, all three major functions -- image building, investment generation and investor services -- of investment promotion must be developed in Pakistan. As the three functions are interrelated and mutually supportive, it is important to house them in one national promotion agency, which does not seem to be the case at this time. Also, the Government seems to emphasize image building, as attested by the major campaign that it has initiated in the international media since the mid-1991. Also, efforts have been made to generate new investments, the investment promotion conference held in November 1991 being an example of such an effort.

Chart I - INSTITUTIONAL FRAMEWORK SUMMARY: PAKISTAN

Prepare Investment Promotion Strategy

With
- Policy framework and targets
- Prioritized activities: investor servicing, investment generation, image building
- Resource and staff implications
- National criteria for evaluation

Establish Investment Promotion Agency

Define its:

- Structure:
  . Parastatal, Direct Government, or Private Sector
  . Board composition
  . Internal organization

- Legal Foundation:
  . Special legislation

- Functions and Powers
  . What promotion, facilitation, monitoring functions
  . What central or coordinating powers

- Private Sector Links:
  . Board
  . Staff
  . Operation/activities

- Staffing, skills, budget requirements

- Evaluation and Reporting Procedures for:
  . Investment sanctioning and realization
  . Promotion activities
  . Investor services

114. Given the poor experience with investment realization in Pakistan, its week physical infrastructure and its cumbersome administrative process faced by investors, FIAS considers that at this time priority should rather be given to the development of investor services to offer support to existing and potential investors. More specifically. a mechanism needs to be put into place to provide information to investors and facilitate the implementation of their projects. Some form of "one-stop-shop" organization should be established within the promoting agency. Efforts should be made to simplify and rationalize more the investment approval and realization process, including, where possible, eliminating some existing procedures, and assisting investors in obtaining prompt approval of government permits and clearances, and in accessing suitable sites, buildings and physical infrastructure facilities.

115. The promotion agency can help in ensuring that new investors receive reasonable priority in accessing limited but, available infrastructural resources. It can help set rules for restricted access to available resources as a short term solution. For example, firms can be granted one or two telephone lines, rather than their total requirements, limited access to water or power with appropriate provision for their own back-up support. This approach is used as a short-term solution to what is a common problem in many countries. In the medium to long term, the promotion agency can help establish and actively encourage the provision of infrastructure priorities, including the provision of industrial estates, if these are judged to be necessary.

116. To enhance its chances of implementing successfully its FDI policy, the Government may wish to grant the investment promotion agency a considerable degree of independence and a clear legal status, and have it supervised by a board of directors, whose composition, authority and responsibility should be set out in the enabling legislation. The board would be required to operate within established policy guidelines but would be free to decide on, and responsible for, the on-going operational activities and performance of the agency.

117. The composition of such boards elsewhere vary. Some are formed entirely with senior government executives, while others include a combination of state and private sector members. Countries like Ireland and Singapore use boards the majority of whom are from the private sector. Ideally, in Pakistan the composition should include the secretaries of key government ministries and selected members from the private sector. This combination links the key government authorities responsible for investment generation and for clearing new investments with private sector members who can help instill a culture and approach to the agency which is beneficial in promotion activities. Board appointments from government circles or from the private sector, including the appointment of a chairman, can be decided upon by government.

118. Private sector procedures and culture constitute a common feature of successful promotion agencies, and can be usefully developed at different levels in the organization. First, they are present at the

highest level of the agency in the form of the private sector membership on the board. Next, ongoing arrangements and assignments can be developed between the agency and the private sector, whereby senior staff can be recruited from the private sector. Finally, on a day-to-day basis, the agency can involve extensively organizations in the private sector, such as banks, consulting and accounting firms, and other well-established investors in its on-going promotion activities. The investment promotion agency should develop institutional mechanisms to tap into the private sector and benefit from it along the lines suggested above.

E. Recommendations

119. The Government has introduced a significant investment policy reform package which has been widely welcomed in the business community and offers overseas investors the beginning of a more transparent, automatic and simplified policy framework. Its impact is likely to depend on how confident investors feel about its stability and the consistency between recent changes and future policy moves. Creating this stable and competitive business environment is an important challenge facing the Government in its desire to attract more investment.

120. While the general policy reforms are regarded as positive, the proposals for institutional changes fall far short of what international experience shows is required for effective FDI promotion. These preliminary recommendations set out areas where further consideration and action by the Government is considered essential.

121. It is recommended that the Government:

- establish an autonomous investment promotion agency either as a parastatal or as a state body, with a full range of investment promotion functions, a clear legal framework, a structure headed by a board of directors, a provision for strong private sector links and culture, appropriate staff and adequate resources;

- include, as a priority function of the promotion agency, the service function to help investors realize their investments. This function requires establishing an institutional framework to coordinate the delivery of all necessary government permits and clearances, to assist in obtaining sites and essential infrastructure, and to provide essential and routine information useful to potential investors; and

- prepare an investment promotion strategy in the near future.

122. The Government faces two major options in establishing an investment promotion agency. The preferable option is to establish a new agency with the proper authority, board, functions and structure.

This agency could be staffed with personnel qualified in investment promotion and special training could be provided where necessary.

123. The second option is to transform an existing institution into a modern promotion agency. This again should be approached by establishing a legal framework specifying the functions to be carried out, appointing a Board and providing for required structures and reporting procedures. Special arrangements would be required in this case to provide for the transfer out of existing staff who may not wish to work in investment promotion, for the recruitment of investment promotion specialists, and for the training of existing staff.

124. If IPB is selected as the agency to carry out the national investment promotion task, then major changes are required to transform that organization into one which could realistically operate effectively in what has become a very competitive international environment. Without such a major transformation this agency as it is structured, staffed and resourced would be under severe disadvantages operating in competition with its counterparts in other countries. It would be unrealistic to expect IPB to operate effectively if it remains in its present form.

V. CONCLUSIONS AND RECOMMENDATIONS

125. FIAS has found that the FDI environment in Pakistan has both positive and negative aspects. There are clear signals that Pakistan's top leadership is committed to adopting an increasingly outward-oriented economic policy, and to giving the major role for economic development to the private sector. To that end, the Government has taken the first set of decisive and bold measures to improve the business environment in general, and enhance Pakistan's attractiveness to foreign investors in particular. These measures, which included the effective removal of foreign exchange controls and the liberalization of the transfer of technology, have earned the praise of domestic and foreign investors alike. The substantial increase in the number of foreign investors interested in locating in the Karachi Export Processing Zone for the 1989-1991 period provides an idea of the impact these liberalization measures could have for the rest of Pakistan if they are to be expanded and successfully implemented.

126. Despite these improvements in the investment environment, Pakistan still falls short of having the kind of business environment conducive for FDI that is found in Southeast Asia and Turkey, the countries with which Pakistan says it wants to compete. Pakistan has a weak infrastructure and suffers from law and order problems. Also, compared to these countries, Pakistan is still hampered by policies that have resulted in a protectionist and distorted economic environment, more likely to attract import substitution than the more coveted export-oriented, FDI. Pressures to raise revenues, and other conflicting objectives, have led to inconsistencies in investment and industrialization policies, and an _ad hoc_ and changing incentive system. Although

the sanctioning system has been essentially removed, investors face other numerous and cumbersome approval procedures. The modalities of introducing changes in policies through, for example, administrative orders and SROs, have caused confusion in the regulatory framework of investment. Many laws and regulations, including those related to labor and tax collection, need to be simplified and updated. Finally, the institutional arrangements for investment promotion are weak and fall short by international standards of what is needed for Pakistan to attain its objectives for foreign direct investment.

127. In light of these difficulties, it is important that Pakistan continue improvements in trade and fiscal policies to reduce the anti-export bias and thus greatly enlarge the range of foreign investments that might be viable in Pakistan. It is also important that attention be given to upgrading both physical and human infrastructure to provide the bases for viable investments. As the report notes, government expenditure on infrastructure is a more effective incentive to investment than tax holidays and other fiscal incentives (providing, of course, that normal tax rates are reasonable). In this context, it would be desirable to review the usefulness of investment incentives that are now in place. It is the preliminary view of FIAS that the level of incentives can be reduced, and the incentive system can be simplified without damaging the competitive position of Pakistan in relation to other countries.

128. More specifically, it is essential that the liberalization of investment policies and regulations be continued. The key improvements would be as follows:

- On the short term, the legal bases for the recent policy changes should be strengthened and the inconsistencies between policies and regulations should be eliminated. This would include clarification of local ownership policies (cf. para. 49), approval requirements (cf. para. 66), and investment protection (cf. para. 67).

- The administrative process for implementing investments must be simplified (cf. paras. 68-72).

- An independent investment promotion agency should be established as per recommendations in paras. 121-124 with the immediate mandate to develop investor services to help investors overcome administrative hurdles to implementing investments. Achieving this objective will require political support at the highest level.

- For the long term, the Government should undertake the streamlining of all laws and regulations relating to the business environment to remove inconsistencies among them and have them conform to the liberalized economic climate.

Once the investment service function is established, the promotion agency should move to develop and implement a longer term investment promotion strategy involving image-building and targeted investment generation activities. Presumably by that time most of the remaining problems in the investment environment will be solved, and Pakistan will have a good story to tell the investment community.