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Declining Trends of Foreign Direct Investment in Pakistan (Causes and measures)

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ABSTRACT

Pakistan reached a record FDI of 5.7 bn dollars in 2008 but they have experienced a steep decline since then and currently stand at 1.57 bn dollars. The share of foreign direct investment (FDI), flowing into Pakistan, is negligible when compared with the opportunities and economic fundamentals of the country. The inflow into the country is less than one per cent of the total FDI, made globally.

The study has made an in depth analysis of the factors that have been the main cause of this sharp decline. Our findings show that the main reasons for this decrease include political instability, law and order situation, energy crisis, corruption, lack of required infrastructure, lack of enforcement of contracts, comparatively less share of credit to non-govt. sectors and high corporate tax rates.

Political stability is vital for the implementation of long-term consistent policies but due to frequent govt. changes, inconsistent policies have been a strong threat to foreign investors. Pakistan's ongoing energy crisis has been an alarming issue for foreign investors. The demand for energy has far exceeded the supply causing a vicious cycle to start. The industries have to either put their productions on hold or resort to alternative energy sources. This crisis has impacted the labor market, causing hundreds of thousands of people to lose their jobs. Poor infrastructure facilities also contribute in pushing investors further away. Strong social and cultural factors have also been an issue to deal with by the foreign investors who misperceive Pakistan's image and so are reluctant to make investments.

Pakistan's corporate tax rate is 35% of net taxable income of a company. For nonresidents, a 15% rate is levied on the gross amount of royalties or technical service fees, and 30% for other payments under the presumptive tax regime. The tax structure needs to be reviewed in order to attract foreign investment.

The study suggests several practical policy measures to be adopted in order to pull FDI inflows back on the track to increment, if duly implemented.

KEYWORDS: Trends, Foreign, Investment.

1. INTRODUCTION

1.1 Definition

Foreign direct investment (FDI) refers to the net inflows of investment to acquire a lasting management interest (10 percent or more of voting stock) in an enterprise operating in an economy other than that of the investor

It usually involves participation in management, joint-venture, transfer of technology and expertise.

1.3 Who is eligible to be a foreign investor?

- An individual or a group of related individuals
- An incorporated or unincorporated entity
- A public or private company
- A group of related enterprises
- A government body
- An estate (law), trust or other societal organizations

1.4 How to invest funds

Foreign Direct Investment can be made in the following three ways:

- By incorporating a company in Pakistan
- Through acquiring shares in a domestic enterprise.
- Participating in an equity joint-venture with another investor or enterprise

1.5. Objectives of the study

The primary objective of this study is to determine the main factors responsible for the recent decline in the Foreign Direct Invest inflows and to recommend appropriate policy measures for addressing those factors and pulling the inflows back on the track to increment.

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1.6. Importance

Foreign Direct Investment had been increasing at an encouraging rate from FY 2000 onwards. It reached a record inflow of $5.4 billion in FY 2008 but then began a steep decline and is currently at about $ 1.57 billion. This sharp decline in a mere 3 years period is an alarming signal for the economy because FDIs are a major portion of the net inflows in the country. FDI is important for the growth of every economy and its importance cannot be ignored for developing countries in particular.

1.7. Scope of the study

The study focuses on the factors behind the declining trend of the foreign inflows for investment. This paper covers all the relevant areas that have been observed to have an impact on the inward investment in Pakistan. Major issues like the energy crisis, declining GDP, high corporate tax rates, lack of suitable infrastructure have been discussed in detail. Comparatively less mentioned issues like the impact of political instability on FDI, the law and order situation, the lack of skilled workforce and the over-all negative image of the country have also been analyzed in depth. All problems highlighted in the report have been supported with statistical evidence. The study also includes a range of expedient policies that can be practically implemented to achieve the desired results over time.

2. PAKISTAN'S FDI POLICY

The effects of Foreign Direct Investment are sometimes hardly perceivable, while other times these can be utterly transformative. Although many factors affect the impact of FDI in a country, well-conceived and well-implemented policies can play a major role in maximizing its returns. The positive effects of FDI include the constructive technological and trade effects along with a mixture of dynamic externalities like clustering and reputation of the country while the negative effects include a range of possible outcomes like anti-competitive impacts, bidding scarce resources away from domestic firms or squeezing out domestic supply networks.

Pakistan has designed its investment policy in a manner to make it attractive for the foreign investor by opening up the economy and marketing the potential for direct foreign investment. Earlier manufacturing sector was the only avenue for foreign investors interested in investing in Pakistan.

3. TREND OF FDI IN PAKISTAN

Currently, the total FDI in Pakistan is $ 1.57 bn. In order to analyze the FDI situation in Pakistan over the years and as percentage of GDP, the following graphs can be useful. The tables and diagrams provide a comprehensive view of the inflows coming in Pakistan, their composition, contribution in different sectors and the major participants in FDI in Pakistan.

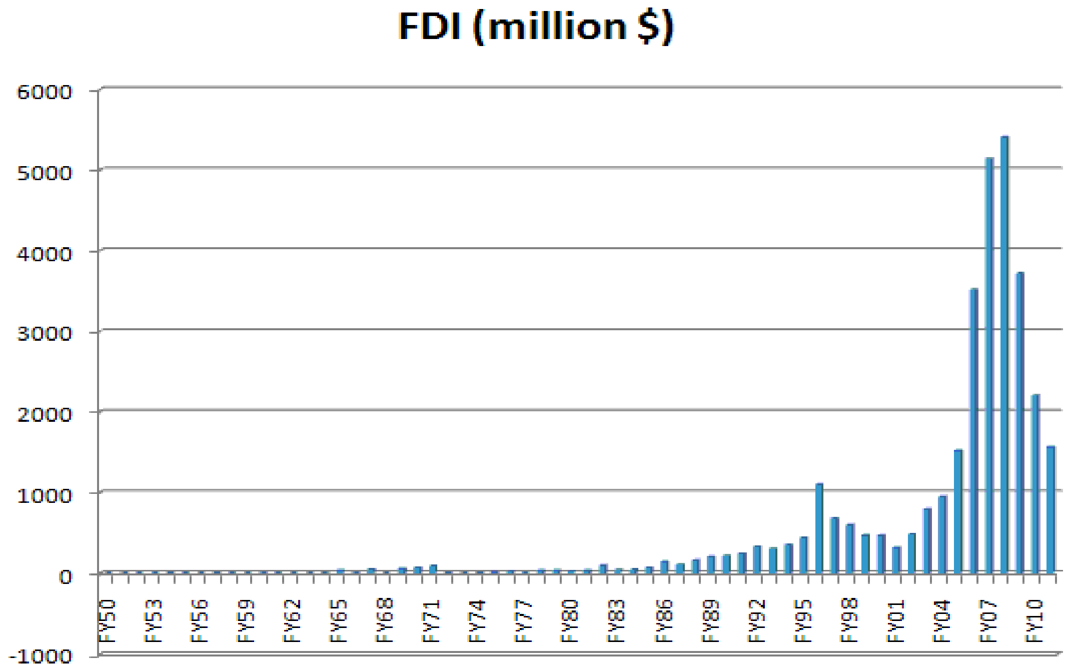


Figure 3a

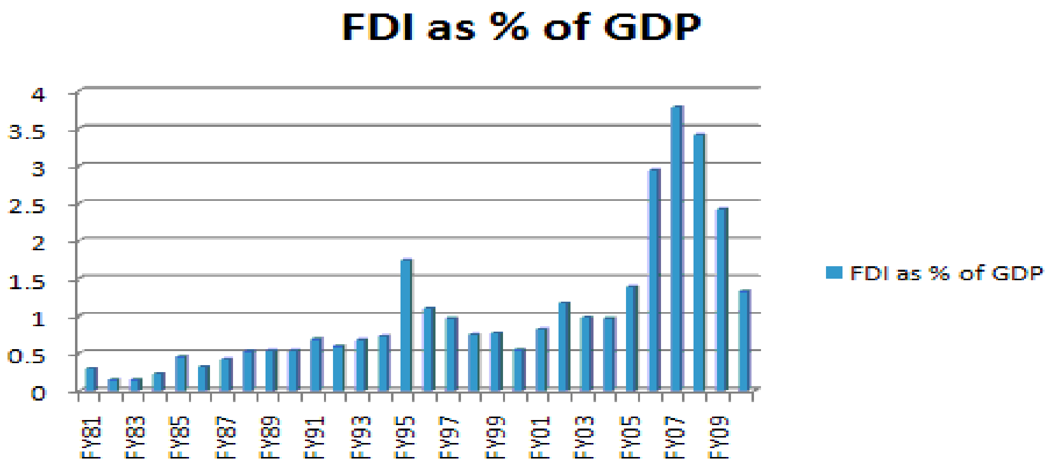


Figure 3b

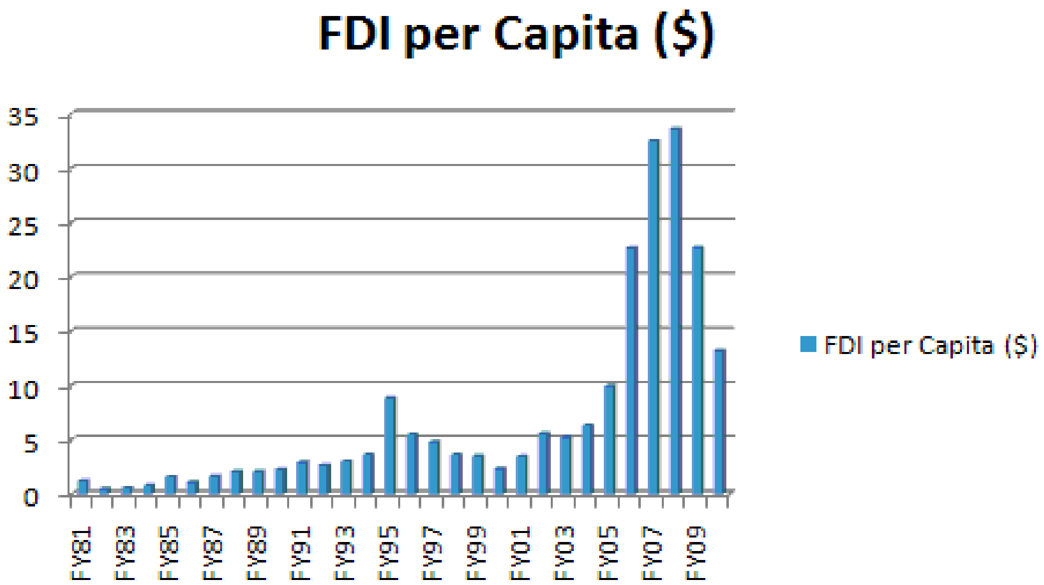


Figure 3c

Table 3a Foreign Investment inflows in Pakistan ($ Million)
Source: BOI

Year	Greenfield Investment	Privatisation Proceeds	Total FDI	Private Portfolio Investment
2001-02	357	128	485	-10
2002-03	622	176	798	22
2003-04	750	199	949	-28
2004-05	1,161	363	1,524.00	153
2005-06	1,981	1,540	3,521.00	351
2006-07	4,873.20	266	5,139.60	1,820
2007-08	5,019.60	133.2	5,152.80	19.3
2008-09	3,719.90	-	3,179.90	-510.30
2009-10	2,150.80	0.00	2,150.80	587.90
2010-11	1,573.6	0.00	1,739.40	344.5
Total	**22,465.10**	**2,805.60**	**25,436.50**	**2,749.00**

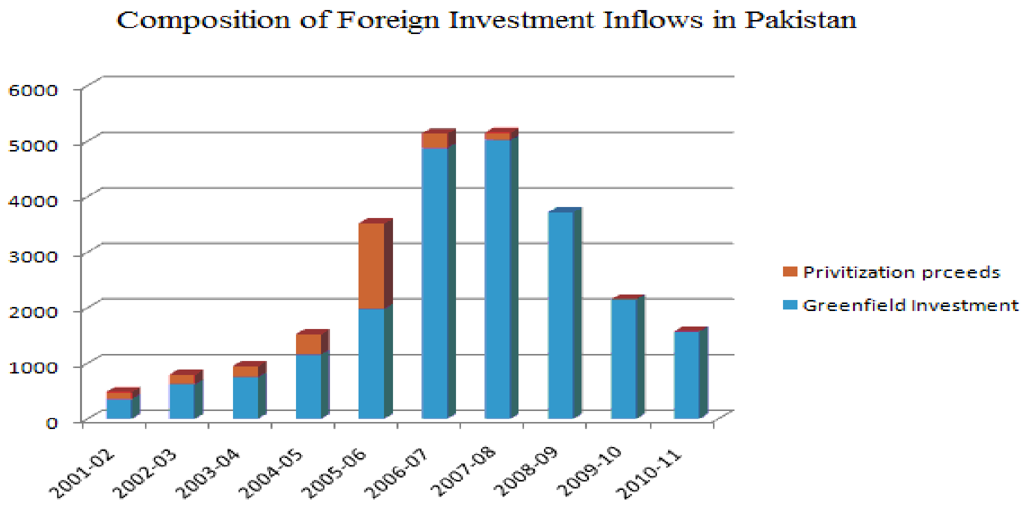


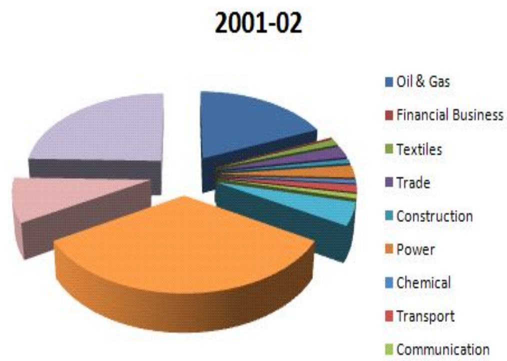
Figure 3d

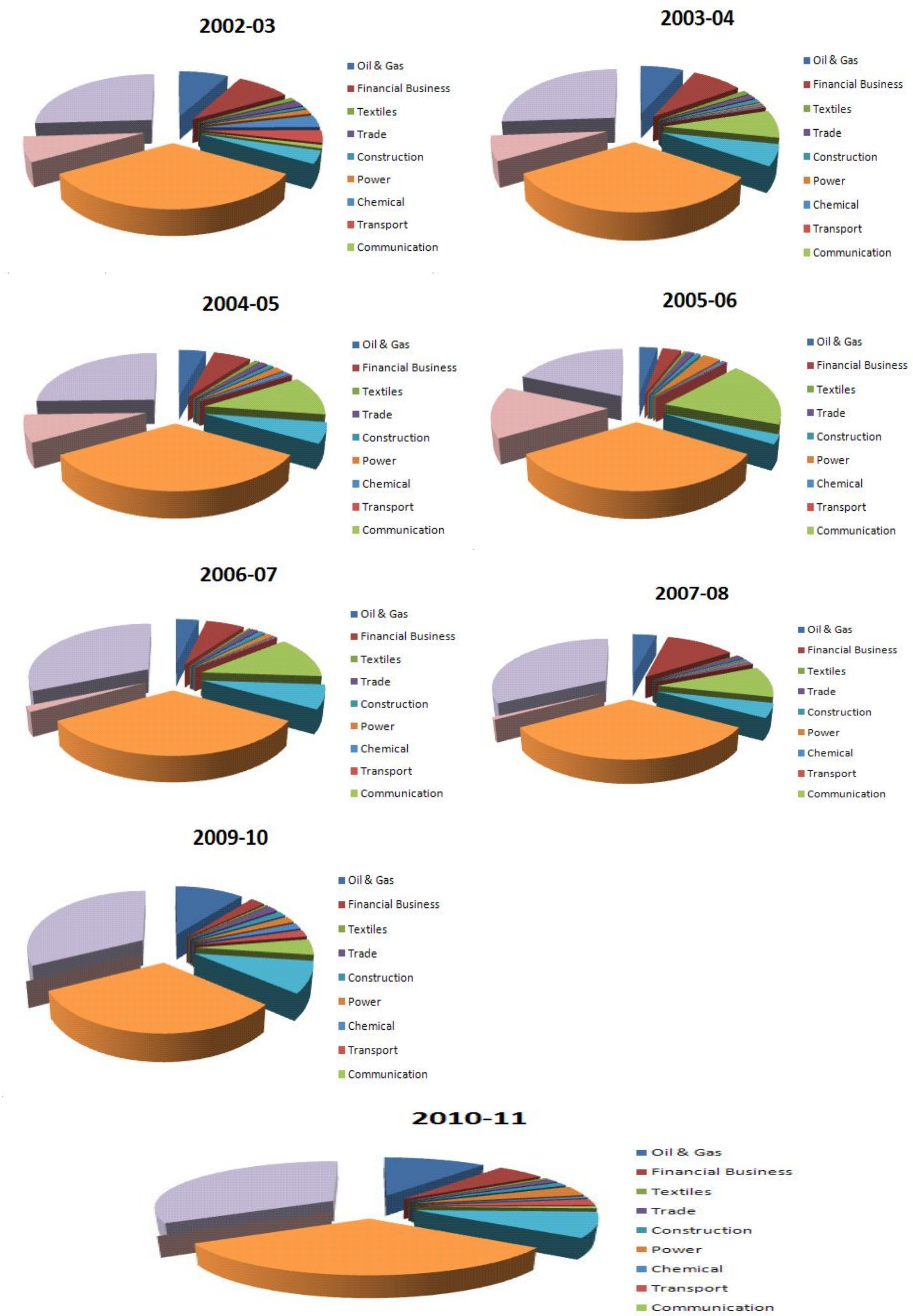
Table 3b Sector wise FDI inflows in Pakistan ($ million)

Sector	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
Oil & Gas	80.7	268.2	186.8	202.4	193.8	312.7	545.1	634.8	775.0	740.6	512.2
Financial Business	(34.9)	3.6	207.4	242.1	269.4	329.2	930.3	1,864.9	707.4	163.0	246.9
Textiles	4.6	18.5	26.1	35.4	39.3	47.0	59.4	30.1	36.9	27.8	25.0
Trade	13.2	34.2	39.1	35.6	52.1	118.0	172.1	175.9	166.6	117.0	53.0
Construction	12.5	12.8	17.6	32.0	42.7	89.5	157.1	89.0	93.4	101.6	60.8
Power	39.9	36.4	32.8	(14.2)	73.4	320.6	193.4	70.3	130.6	(120.6)	155.8
Chemical	20.3	10.6	86.1	15.3	51.0	62.9	46.1	79.3	74.3	112.1	30.5
Transport	45.2	21.4	87.4	8.8	10.6	18.4	30.2	74.2	93.2	132.0	104.6
Communication (IT&Telecom)	NA	12.8	24.3	221.9	517.6	1,937.7	1,898.7	1,626.8	879.1	291.0	(34.1)
Others	140.9	66.2	90.4	170.1	274.0	285.0	1,107.2	764.5	763.4	586.3	418.9
Total including Pvt. Proceeds	322.4	484.7	798.0	949.4	1,523.9	3,521.0	5,139.6	5,409.8	3,719.9	2,150.8	1,573.6
Privatisation Proceeds	-	127.4	176.0	198.8	363.0	1,540.3	266.4	133.2	0.0	0.0	0.0
FDI Excluding Pvt. Proceeds	322.4	357.3	622.0	750.6	1160.9	1980.7	4873.2	5,276.6	3,719.9	2,150.8	1,573.6

Source: BOI

Sector wise FDI inflows in Pakistan





Figures 3e (1-11)

Table 3c Country Wise FDI Inflows ($ Million)

Country	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11
USA	92.7	326.4	211.5	238.4	325.9	516.7	913.1	1,309.3	869.9	468.3	238.9
UK	90.5	30.3	219.4	64.6	181.5	244.0	860.1	460.2	263.4	294.6	208.1
U.A.E	5.2	21.5	119.7	134.6	367.5	1,424.5	661.5	589.2	178.1	242.7	284.2
Japan	9.1	6.4	14.1	15.1	45.2	57.0	64.4	131.2	74.3	26.8	3.2
Hong Kong	3.6	2.8	5.6	6.3	32.3	24.0	32.6	339.8	156.1	9.9	125.6
Switzerland	3.6	7.4	3.1	205.3	137.5	170.6	174.7	169.3	227.3	170.6	47.2
Saudi Arabia	56.6	1.3	43.5	7.2	18.4	277.8	103.5	46.2	(92.3)	(133.8)	6.5
Germany	15.5	11.2	3.7	7.0	13.1	28.6	78.9	69.6	76.9	53.0	21.2
Korea (South)	3.7	0.4	0.2	1.0	1.4	1.6	1.5	1.2	2.3	2.3	7.7
Norway	41.9	0.1	0.3	146.6	31.4	252.6	25.1	274.9	101.1	0.4	(48.0)
China		0.3	3.0	14.3	0.4	1.7	712.0	13.7	(101.4)	(3.6)	47.4
Others		76.6	173.9	108.6	369.3	521.9	1,512.2	2,005.2	1,964.2	1,019.6	631.6
Total including Pvt. Proceeds	322.4	484.7	798.0	949.0	1,523.9	3,521.0	5,139.6	5,409.8	3,719.9	2,150.8	1,573.6

Source: BOI

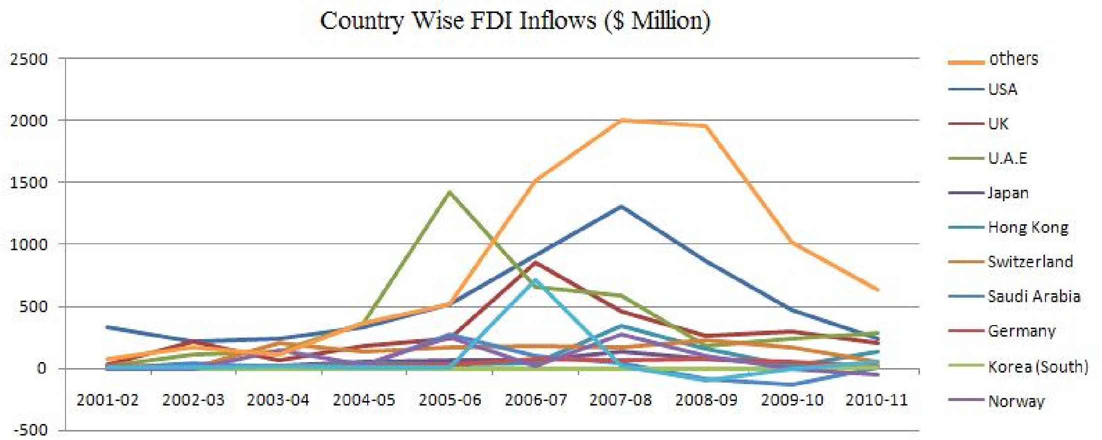
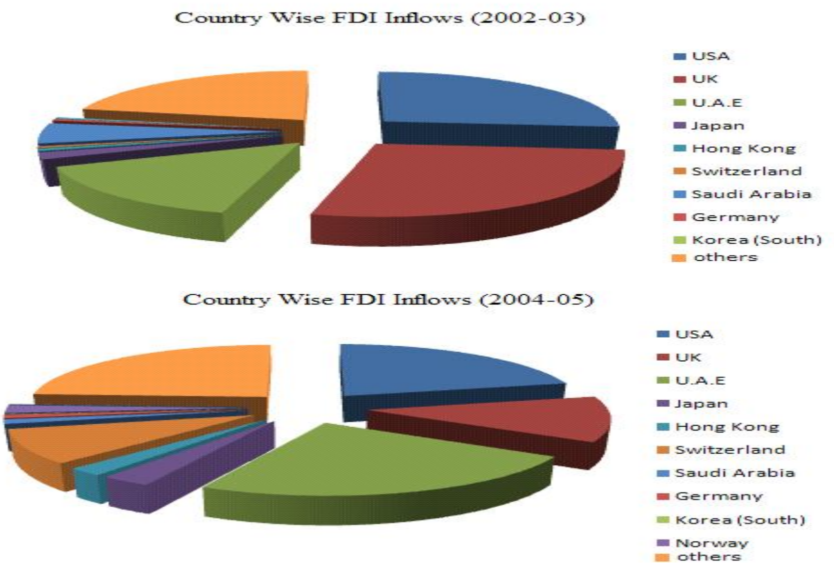


Figure 3f



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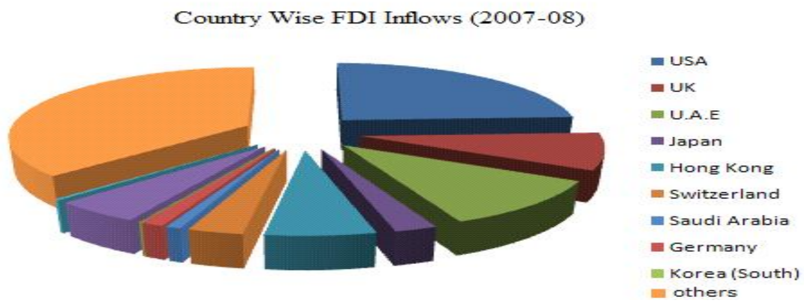

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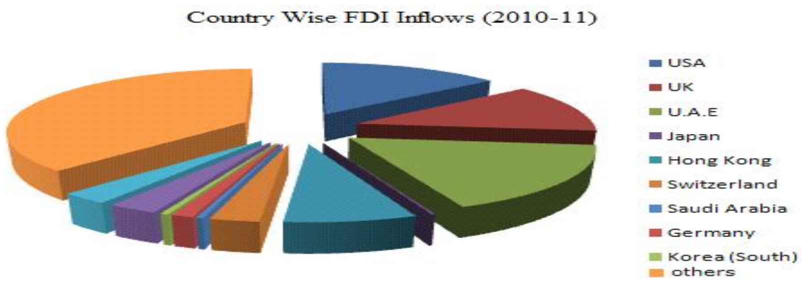


Figure 3i

4. ANALYSIS

4.1. CAUSATIVE FACTORS

The portion of foreign direct investment flowing into Pakistan is less than one per cent of the total FDI, made globally. The highest, Pakistan received, was in 2007-08. Ever since then, it has been experiencing a declining trend. The factors that have been observed are:

4.1.1. Political Instability

The components of the internal environment of the host countries play a significant role in drawing foreign investment. Chief among them would be the potential natural resources of a country, attractive cheap labor for international manufacturers, proximity to markets, economical, legal and infrastructural factors and above all political stability.

Political stability plays a vital role as an incentive to attract investors. Despite the immense potential and attractive business opportunities, the foreign investors doing business in Pakistan have major concerns. Key among these concerns are the frequently changing and unpredictable policies due to political instability, and the existence of religious extremism, spread by various unrecognized clerics, who are bent upon defaming the country internationally.

In Pakistan, unfortunately, policies have always been linked to individuals. These individuals are the fore-runners of their party's politics. As governments take their final bows, policies follow them out. Every new government, whether democratic or military, develops its own policies and implements them accordingly. This continuous experimentation has had its adverse effect on Pakistan's economy in general and Foreign Direct Investment in particular.

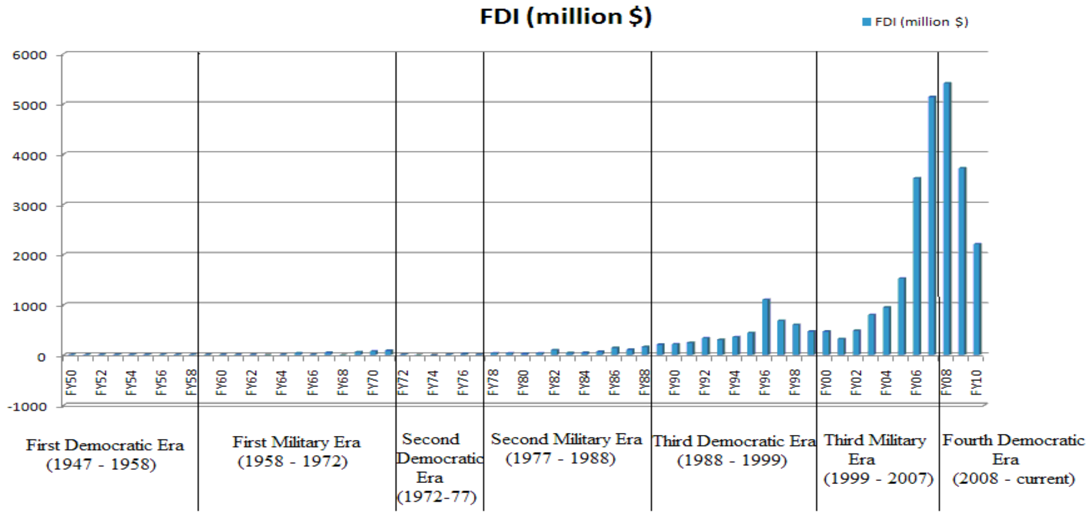


Figure 4a

The graph shows that in every military government, the FDI trend has moved for the better but in every democratic government, FDI has shown fluctuations and an eventual decline. Another important thing to note here is that the democratic era represents multiple governments but the military eras represent a stable long-term military rule.

4.1.2. Energy Crisis

Pakistan's ongoing energy crisis has been a red signal for quite some time for the foreign investor. The demand for energy has far exceeded the supply causing a vicious cycle to start. The industries have to either put their productions on hold or resort to alternative energy sources. Not everyone has this option. This crisis has impacted the labor market, causing hundreds of thousands of people to lose their jobs. This is an alarming issue for investors willing to make investments in a country.

Power sector in Pakistan is characterized as semi-public and semi privatized vertically integrated sector. The main players of the sector are:

WAPDA
KESC
NEPRA
PPIB
Ministry of Water and Power

The table below shows the composition of energy generation briefly:

Energy Generation by Source									
Fiscal year ending June 30	PUBLIC				IPPS				TOTAL
	HYDRO		THERMAL		HYDRO		THERMAL		
	GWh	%age	GWh	%age	GWh	%age	GWh	%age	
2000	1 9,288	34.5	1 9,157	34.3			1 7,428	31.2	5 5,873
2001	1 7,196	29.4	16,858	28.8	63	0.1	24,338	41.6	58,455
2002	18,941	31.1	18,684	30.7	115	0.2	23,120	38	60,860
2003	22,253	34.7	19,646	30.7	97	0.2	22,044	34.4	64,040
2004	27,372	39.67	21,054	30.5	105	0.2	20,563	29.8	69,094
2005	25,588	34.8	22,212	30.2	83	0.1	25,637	34.9	73,520
2006	30,751	37.4	22,519	27.4	104	0.1	28,851	35.1	82,225
2007	31,846	36.3	21,617	24.6	96	0.1	34,278	39	87,837
2008	28,536	33.1	20,509	23.8	131	0.2	37,093	43	86,269
2009	27,636	32.8	19,569	23.2	127	0.2	37,045	43.9	84,377
2010	27,927	31.3	19,632	22	565	0.6	41,113	46.1	89,238

Table 4a
Source: Power System Statistics

About 60 percent of the total population is estimated to have access to electricity. Rest of the population is using alternative sources of power such as oil and so on. The energy generation in 2010 can be seen by the following pie-chart

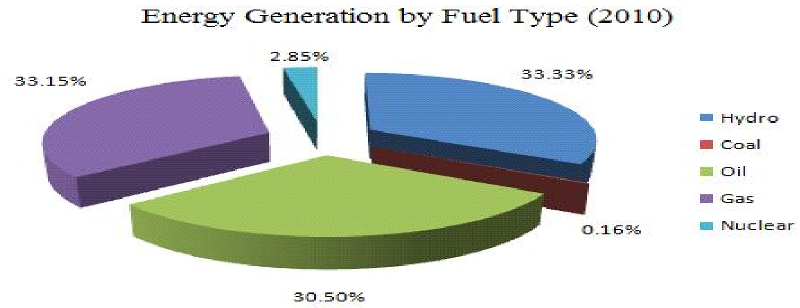


Figure 4b

In the private sector IPPs have 46 percent share while the share of nuclear capacity is around 3 percent. Currently energy demand is increasing at a high rate which has created shortage of electricity. Pakistan needs around 20,000 MW per day. Energy consumption increase in 2005 was 5 per cent higher than the real GDP growth rate which indicates that the energy consumption is significantly higher than the real GDP growth. Chairman WAPDA stated that energy shortage in Pakistan will last till 2018.

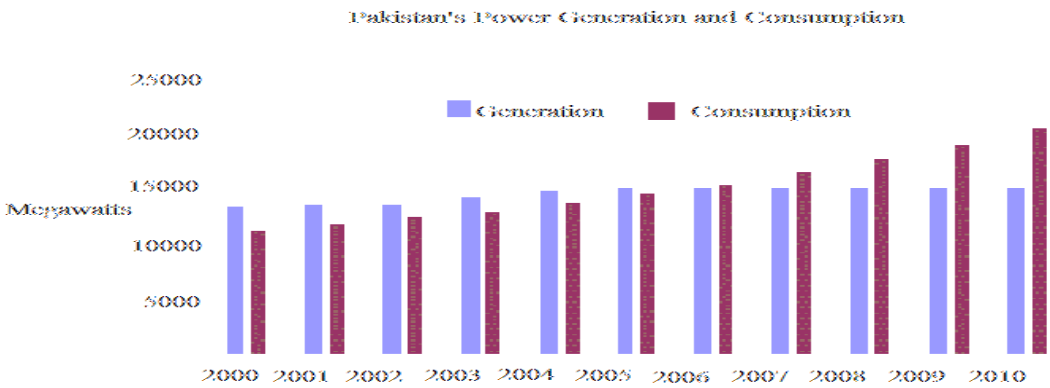


Figure 4c

During the past 25 years energy supply in Pakistan has been increased by about 40 times but still the demand outstrips supply. Pakistan recorded a shortfall of 40% between demand and supply of electricity in 2008. The table below also confirms that power consumption by economics groups is increasing since FY2000. The highest increase has been in domestic and commercial consumption.

Table 4b

Consumption of Energy by Economic Groups									
									(GWh)
Fiscal year ending June 30	**Domestic**	**Commercial**	**Industrial**	**Agricultural**	**Public Lighting**	**Bulk Supply**	**Traction**	**Supply to KESC**	**Total**
2000	18,942	2,003	10,773	4,512	150	2,676	15	1,840	40,910
2001	20,019	2,120	11,744	4,896	146	2,634	14	1,811	43,384
2002	20,549	2,285	12,637	5,582	149	2,662	12	1,329	45,204
2003	20,855	2,516	13,462	5,986	166	2,626	10	1,801	47,421
2004	22,668	2,884	14,476	6,624	192	2,796	9	1,843	51,492
2005	24,049	3,192	15,568	6,921	227	2,892	12	2,416	55,278
2006	27,009	3,768	16,596	7,873	279	3,031	13	3,836	62,405
2007	28,990	4,290	17,603	8,097	316	3,267	12	4,905	67,480
2008	28,751	4,358	17,299	8,380	340	3,332	8	4,072	66,539
2009	27,787	4,203	16,035	8,695	347	3,198	5	5,014	65,286
2010	29,507	4,466	16,371	9,585	372	3,367	2	5,208	68,878

Source: Power System Statistics

4.1.3. Lack of Infrastructure

Infrastructure is the essential physical and organizational structures needed for the operation of an enterprise, the services and facilities are necessary for an economy to function. The term typically refers to the technical structures that hold a society, such as roads, water supply, sewers, telecommunications, and so forth.

Table 4c Growth of Transport Demand (Inter-zonal Transport)

Years	Passenger		Freight	
	No of Passengers	Passenger-Km	Tons	Tons-Km
	Million/year	Billion-Km/year	Million/year	Billion-Km/year
2005	780	154	241	90
2015	1455	293	440	185
2025	2497	517	748	329

Source: JICA Study Team

The total length of road network in Pakistan is a little more than 260,000 km. 60% of this network is paved while the rest has remained unpaved, however, the share of paved roads has been steadily rising over the years which is a positive indicator for road quality. Despite this increase, Pakistan's position is not satisfactory in terms of road density which is only 3.2 km/sq.km. NHA maintains national highway and motorway accounts for about 12000 km which is 4.6% of the total roads network but carries 80% of the total commercial traffic of Pakistan.

Local freight and passenger traffic in Pakistan has been increasing at an average annual rate of 10.61 percent and 4.41 percent respectively. Currently the road freight takes four to six days from ports to the north of the country, which is two times the equivalent time in Europe / East Asia. There are delays in connectivity which are causing inefficiencies and losses to the economy.

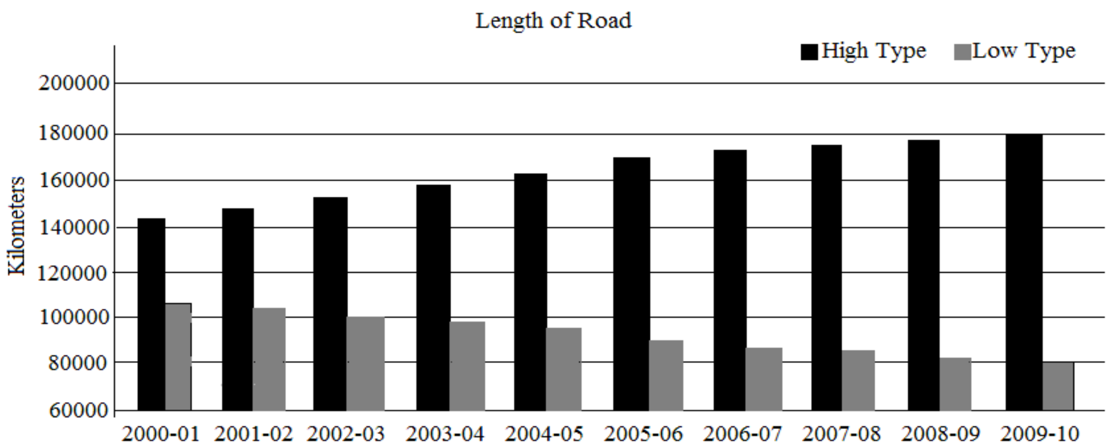
Table 4d

Description	No	Km
National Highways	20	9280
Motorways	7	1930
Expressways	3	384
Strategic Roads	3	262
Total	33	11856

Source: National Highway Authority

The key central Federal body responsible for all National Highways Motorways and Strategic Roads is National Highway Authority (NHA). Under NHA jurisdiction road network is about 12,000 km.

Figure 4d



Source: NTRC

There are six dry ports running under the management of Pakistan Railways.

- Lahore Dry Port
- Karachi Dry Port

- Quetta Dry Port
- Peshawar Dry Port
- Multan Dry Port
- Rawalpindi Dry Port

There are four Dry Ports established and running under the management of private sector

- Sialkot Dry Port
- Faisalabad Dry Port
- Pak-China Sust Dry Port
- NLC Dry Port at Thokar Niaz Beg Lahore
- NLC Dry Port at Quetta

Besides these dry ports, Pakistan also has four sea ports:

- Port of Gwadar - Gwadar, Balochistan
- Port of Karachi - Karachi (City Centre), Sindh
- Port Qasim - East Karachi, Sindh
- Port of Pasni - Pasni, Balochistan

Currently, only two of the sea ports handle 95% of the total external trade, which indicates the inefficiency of the other ports.

4.1.4. Cultural and Social Factors

An overwhelming majority of existing or potential MNCs in Pakistan are from the West. The people of the West have a lifestyle different from ours and want to continue that while staying here. Our cultural values serve as an impediment to their staying in the country to overlook their investment projects.

Pakistan's large population of illiterate citizens feels threatened by the entry of foreigners and sees even an attempt of investment as a chance to take over the govt. Another major impediment is that Pakistanis view foreign food products as "haram", particularly those associated with the west. This is a daunting phenomenon for the foreign investor. Furthermore, products that are prohibited by the religion of the majority of the population cannot be introduced in Pakistan and so have no market for a large no. of investors.

The recent issue of blasphemous images of the Holy Prophet has created a surge of hatred in the masses for all products with foreign affiliation. Any such issues serve to further fuel the negativity in the mind-set of the masses.

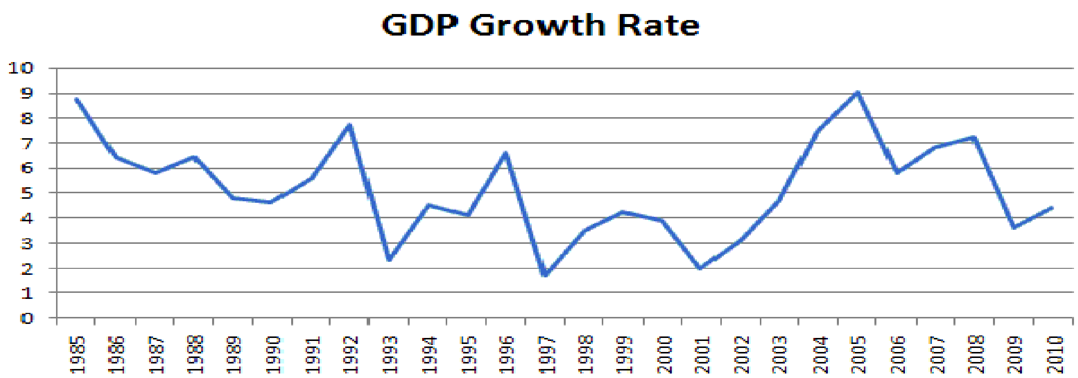
4.1.5. Lack of Skilled Work Force

Pakistan ranks 10th in the world in terms of the size of labour force, having about 55.8 million workers. Although Pakistan is the 6th largest country in terms of population, but the still a large number of people in Pakistan are unskilled or semi-skilled. Although wages in Pakistan are low but productivity is also low. While making investment decisions, MNCs take into account both worker productivity and wages.

4.1.6. Declining GDP

Research shows that FDI causes growth in the services sectors, while growth causes FDI in the manufacturing sector. Manufacturing sector accounts for 25% of the total economy of Pakistan. The declining trend of GDP in Pakistan in recent years has shaken the faith of foreign investors.

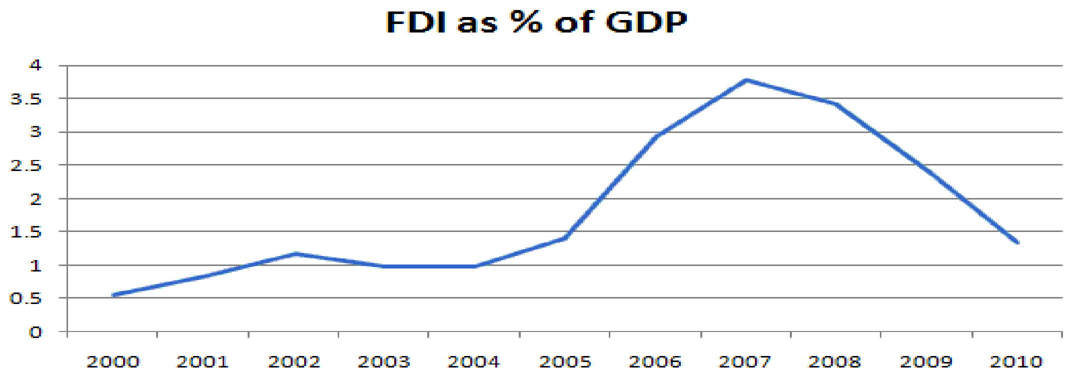
Figure 4e



Source: CIA World Factbook

GDP is an important indicator for the foreign investor because they enter a market to make profits and this can only be achieved if there is economic growth in the country. Foreign investors are only interested where markets are big and demand for their products or services considerable.

Figure 4f



Source: Statistics and DWH dept. SBP

4.1.7. Law and Order Situation

An adverse law and order situation crops up whenever there is insecurity, threat of violence or hostility arising due to host of factors disturbing the ordinary conduct of life and businesses in a society. This situation may be a product of external cataclysm, internal disorder, religious extremism, strikes or boycotts by labor unions and other such racial or ethnic disturbances.

This situation negatively affects the macroeconomic indicators that determine the state and growth of economy like the GDP growth rate, poverty incidence, and per capita income growth rate over a specific period of time, and level and nature of investment, whether portfolio or Foreign Direct Investment. Foreign Investors shy away from investing in regions where the law and order situation threatens their investments.

Table 4f

Bomb Blasts in Pakistan (2000 - 2011)			
Year	**No. of Blasts**	**Killed**	**Injured**
2000	14	79	316
2001	61	48	342
2002	34	68	299
2003	40	34	155
2004	137	255	1040
2005	245	210	571
2006	300	359	766
2007	648	1078	2848
2008	599	1251	3073
2009	500	1668	4283
2010	473	1547	3581
Jul-11	392	718	1757

Source: South Asia Terrorism Portal

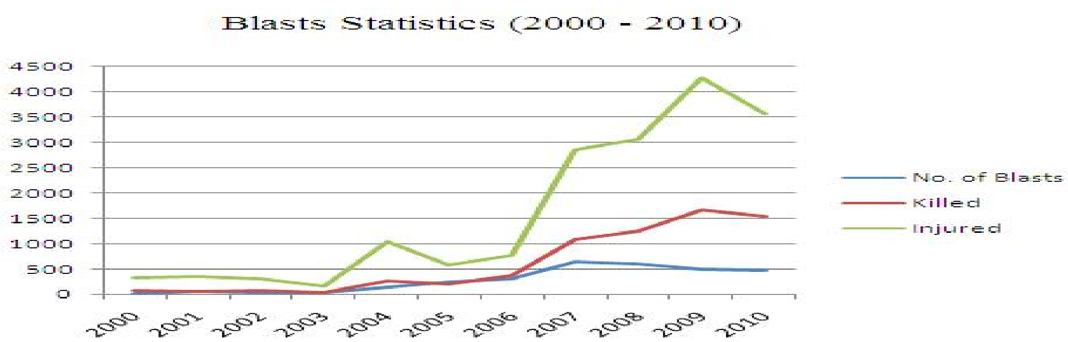
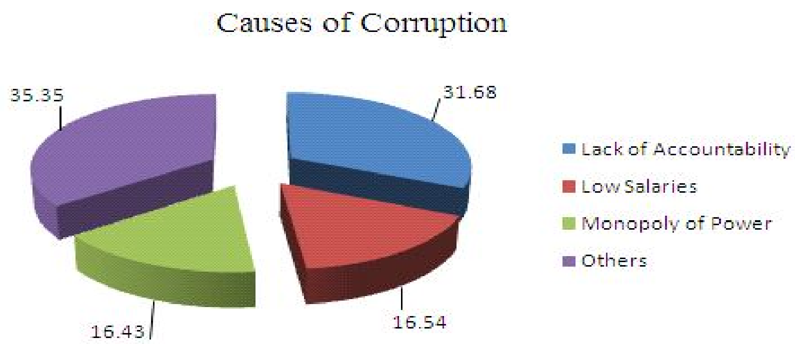


Figure 4g

The northern areas of Pakistan are considered to be a "safe haven" for Al-Qaeda terrorists and the ingoing NATO drone attacks in the tribal areas of Pakistan have further fueled the image of Pakistan as sanctuary for terrorists. which has scared foreign investors from injecting capital into the country.

The corruption rate in Pakistan is also quite high which threatens the foreign investors as regard to the enforcement of contracts with the government. There is always a chance that the government may embezzle the investment as it has been famously doing with the foreign aid. Transparency International has identified the following as the three major causes of corruption in Pakistan.

Figure 4h



Source: Transparency International Pakistan

4.1.8. Share of Credit to Non-Govt. Sector

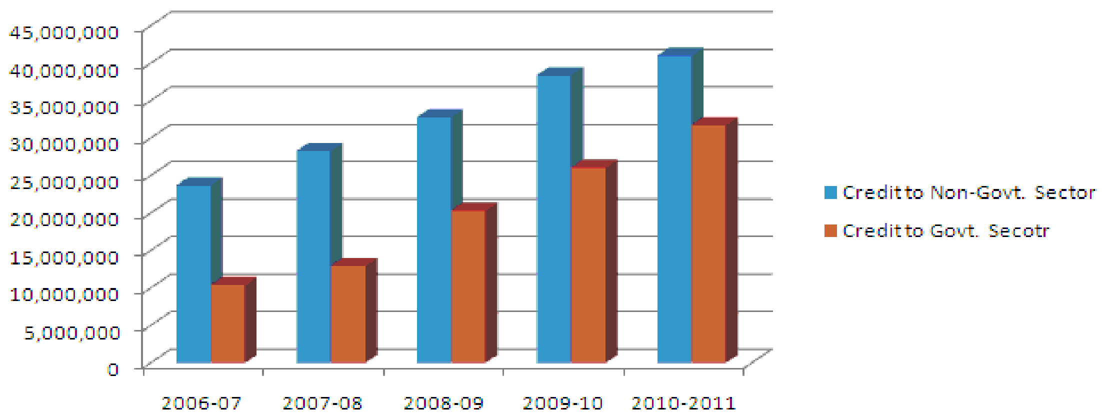
Credit to foreign investors is an investment incentive therefore as credit policies are made more flexible and investor friendly, foreign investment would be encouraged accordingly. The share of credit to private investors in the total credit has been decreasing which is a sign of decreasing investor interest.

Table 4h Credit to Govt. And Non-Govt. Sectors

Year	Credit to Non-Govt. Sector	Credit to Govt. Sector	Total Credit	Share of Private Credit to Total Credit
2006-07	23,724,040	10,422,482	34,146,522	69.47717838
2007-08	28,323,175	12,972,887	41,296,062	68.58565594
2008-09	32,803,666	20,379,682	53,183,348	61.68033272
2009-10	38,431,159	26,100,506	64,531,665	59.55395541
2010-2011	41,038,740	31,767,225	72,805,965	56.36727705

Source: SBP Economic Data for Credit Loans

Figure 4i



Source: Handbook of Statistics

4.1.9. High Corporate Tax

The Federal Board of Revenue issued procedures for the imposition of 15 per cent flood surcharge. This additional tax was charged on the existing 35 per cent tax liability, cumulating in an effective tax rate of 40.25 per cent on an annualized basis. The new measure were effective from March 15 to June 30, resulting in corporate earners paying an average 36.5 per cent tax rate for fiscal 2011. Such abrupt policies are a turn-off for foreign investors.

5. POLICY MEASURES

Many foreign investors are discouraged to invest in Pakistan due to political instability. Despite being blessed with abundant natural resources and having a great potential to be the next big emerging market, Pakistan govt. needs to make some concrete policies for attracting and retaining foreign investment. Policies should not abruptly change with the change in govt. Pakistan needs to have stable, long-term road map for encouraging FDIs. Policies should not be interfered with or amended every few months, this loses foreign investor's confidence and they become vary of every new policy being outlined. Moreover, policies should not be formed just for the sake of policy formulation; they should be practical and consider all the problems and conditions associated with particular phenomena.

An important element that could affect foreign direct investment and its development potential is the policy of government decentralization in some developing countries. This enables local governments within a country to compete among them to be more efficient which Pakistan badly needs

This multilateral agreement can be altered to safeguard the host country's rights and implemented accordingly. It is not necessary to implement an agreement as such; it can be tailored to fit the needs of a group and implemented thus. Furthermore, regulation of investment is only as effective as a country's ability to enforce it.

One of the most important reasons for declining FDI in Pakistan and found in research is the energy crisis being faced by the country. The funds spent on import of power generators and their fuel is an enormous drain on the economy. A solution is needed for the next 20 years to take care of Pakistan's power requirements.

A potential home-based, energy solution, based on wind and solar energy, can be used. . Though technology is still evolving for solar energy, a number of private businesses providing solar cells at small scale are flourishing. A number of Chinese companies have carved a niche in the solar energy market for themselves in our energy deprived country. Solar energy although requires more initial investment than other alternatives but then zero fuel cost is an advantage that is not available in other sources. An instant solution can be wind energy. The Karachi to Gwadar coastline has massive potential for generating wind energy more over it is a fast and cheap solution.

Pakistan does not only need to address such dire issues like the energy crisis but also minor problems like the lack of awareness of the foreign investor about the investment opportunities and investment protection in Pakistan. Foreign Private Investment (Promotion and Protection) Act, 1976 and the Furtherance and Protection of Economic Reforms Act, 1992 provides legal cover for protection of foreign investors/investment in Pakistan. This act should be highlighted at all investment conferences. Marketing this act and its individual clauses separately and extensively would result in greater investor confidence.

The challenge for host countries is to establish the right mix of institutions, incentives and infrastructure to create the enabling business and investment climate. Private sector involvement in transport development in Pakistan is an important tool to implement the projects. Particularly, private financing is vital to the development of the Motorway Network. Private sector investments in airport and port development should be further promoted.

Pakistan has one of the highest road fatalities per 10,000 vehicles in the world that warrant a widespread road safety plan covering emergency medical services being planned at the national level. Every developed country in the world has its own NRSC, the establishment of a National Road Safety Council is needed for Pakistan if highway safety and maintenance problems have to be solved. This should initiate with the formulation of a National Road Safety Plan with NRSCs at provincial levels to ensure financing of road safety. This would encourage competitiveness among the provinces to have the safest routes of distribution.

Highways, roads, railways and ports all need private participation to be efficient and effective. Policies for encouraging private participation should be formulated. Corporatization of railways would result in establishing a more commercial and high-service oriented network. A special network of efficient cargo trains with specified routes should be established. This can be done by inducting private sector capital and management expertise. The private sector will initially be allowed to operate freight trains on payment of track access charges. The private sector will initially be allowed to operate freight trains on payment of track access charges.

Measures should be taken to reduce port cost and enhance their efficiencies. Ports of Pakistan are over-staffed; a reduction in the port staff is needed. Private involvement in dredging, coastal navigation or piloting, tug boat and dock yard is expected to yield positive results.

Pakistani government ought to locate its sights lucrative in order to swap from a resource-to modernization -based economy. Special Economic Zones (SEZs) should be formed with preferential taxation and pre-existing infrastructure on production sites.

SEZs have been around in many countries and have helped develop those countries tremendously. Singapore can be taken as a case study by the govt. Tax and customs exemptions coupled with low labor costs make SEZ-based production a popular business model with world-class corporations and would definitely be an attraction for FDI.

FDI involving international competitors undertaking mutual investment in one another, e.g. through cross-shareholdings or through establishment of joint venture, in order to gain access to each other's product ranges should be promoted. This joint venture relationship would help the host country in capturing more of the benefits that the investing company has to offer.

Generally for developing country and particularly technology transfer can be very beneficial. When a foreign company engages in a joint venture, it exchanges technological know-how for host country's cultural and behavioral knowledge and practices. This serves as a two-way stream and is fruitful for both parties concerned. Besides this, local companies also get expanded access to external markets which wouldn't otherwise be possible. Policies for the encouragement of such joint ventures are to be focused on in order to mitigate risks involved in attracting FDIs.

. Research has shown that FDI has best effects on the manufacturing sector and the development of manufacturing sector is directly correlated with inflow of FDI.

6. ROLE OF STATE BANK OF PAKISTAN

Investment policy of the country is framed by the Board of Investment in consultation with other agencies. State Bank of Pakistan implements the portion of the policy covering Foreign Investment under foreign Exchange Regulation Act, 1947 and the rules framed there under.

<u>Designating Of Bank for Remittance of Dividend and Disinvestment Proceeds</u>

(Para 7 (v) and (vii) (I & II) Chapter XX)

For the purpose of remittance of dividend to the non resident investor, a bank in Pakistan who is authorized to deal in foreign exchange in required to be nominated by the company concerned, under Para 14 Chapter (XIV) of the Foreign Exchange Manual, 2002. Similarly the disinvestment proceeds can also be remitted through the designated bank under Para 7 (VII) (II) Chapter XX of the FEM.

Registration of Foreign Investment in Pakistan

Fresh/Right issue of Shares (normally at face value)

- Documents to be provided by the company through their bank:
- Memorandum and Article of Association of the company
- Certificate of Incorporation of the Company
- Proceeds Realization Certificate in original
- Declaration by the company on Appendix V-90 regarding the shares to be registered in favor of the non-resident

<u>Transfer of Shares</u>

Proceeds Realization Certificates in original for purchase price as well as share transfer stamp duty remitted by the non-resident purchaser

Breakup Value per Share Certificate of practicing chartered accountant at the time of transaction

Declaration by the company on Appendix V-90 regarding the share to be registered in the favor of non-resident.

<u>Transfer of Shares from one non-resident to other non-resident outside Pakistan</u>

In terms of Para 7 (VI) (j) Transferee Certificate (in original) PRC in original for share transfer stamp duty remitted by the non-resident transferee along with Appendix V-90

Besides above State Bank of Pakistan compiles statistical data of FDI through Statistics and Data Warehouse Dept. This data forms the core of policy formulation.

7. CONCLUSION

Pakistan's FDI inflows contribute a major portion to the net inflows in the country. These need to be managed well in order to keep the country on the road to development. Research has shown a positive relationship between FDI and Economic growth of a country. In Pakistan, for the past three years, FDIs have been displaying a downward trend. This is an alarming situation for Pakistan because in the little time to 3 years, FDIs have declined from 5.7 bn to 1.57 bn dollars.

The factors mainly responsible for this decrease have been analyzed in depth to gauge their effect on FDI. These have been found to include inconsistent policies, lack or infrastructure, energy crisis, lack of skilled workforce, law and order situation, high corporate tax rate, social and cultural factors and share of credit to non-govt. sectors.

Policy measures have been suggested to improve the current situation and make Pakistan a welcome haven for the foreign investors. The role of SBP has been influential in the implementation of policies and it has also been discussed in the study.

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