FOREIGN INVESTMENT IN PAKISTAN
Innovation and Reassessment under the New Government

Abstract

This article examines the liberal investment policy of the Government of Pakistan and specifically examines new measures being adopted as a result of the Investment Promotion Strategy 2020 – 2024. A number of institutional reforms have been proposed by the Board of Investment to ensure efficiency in its operations and five sectors have been identified as priority areas. The new strategy is geared towards enhanced cooperation and facilitation for Chinese investors, on account of recent successful Chinese investments in Pakistan, particularly in relation to the China Pakistan Economic Corridor.

Keywords: Investment, Pakistan, China, Reforms, Automobile, IT sector, World Bank

INTRODUCTION

Historically, the Government of Pakistan has understood the importance of foreign direct investment (FDI) in the country and FDI has been studied at length by policy makers and economists since at least the 1960s[1]. The Federal Ministry of Commerce, relying on an earlier World Bank statistic, stated in a draft report[2] that Pakistan maintained "*one of the most liberal investment policy regimes and public-private partnership frameworks*" in South Asia.

To encourage FDI, the Federal Government has maintained a number of policies over the years and the latest one is the Investment Policy, 2013. The liberal approach to foreign investment coupled with a strong focus towards simplifying legal measures has resulted in Pakistan making significant gains in the World Bank's Doing Business 2020 study[3]. The World Bank has particularly noted the joint commitment of the Federal and Provincial Governments in the realisation of this goal.

THE INVESTMENT POLICY, 2013

The Investment Policy, 2013, (hereinafter "the Policy") provides a framework for attracting FDI to Pakistan and is premised on a guiding philosophy which is focused on reducing bureaucratic hurdles and costs of doing business for foreign companies, establishing special economic zones, and ensuring uniformity at the policy-level.

The Federal Government has identified three main sectors (with sub-divisions, thereto, provided for the sake of reference) wherein investment may be directed. These are:

(i) Manufacturing or Industrial

(ii) Non-manufacturing

a. Services sector

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[1] Mukhtiar, A & Malik, I. R. (2017) "Impact of Foreign Direct Investment on Economic Growth of Pakistan" – Vol. III Part 2 of Foundation University Journal of Business & Economics – Extracted from: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3104717

[2] Ministry of Commerce, Govt. of Pakistan (2018) – "Trade Related Investment Policy Framework" - http://www.commerce.gov.pk/wp-content/uploads/2018/10/Trade-Related-Investment-Policy-Framework-2015-23.pdf

[3] World Bank press release (2019) – "Doing Business 2020: Accelerated Business Climate Reform Agenda Puts Pakistan Among Top 10 Improvers"– Extracted from: https://www.worldbank.org/en/news/press-release/2019/10/24/doing-business-2020-accelerated-business-climate-reform-agenda-puts-pakistan-among-top-10-improvers

b. Infrastructure sector
c. Social sector

(iii) Other sectors

a. Tourism
b. Housing and construction
c. Information technology

Salient features

Pursuant to the Policy, foreign investors are allowed to hold full equity (100% ownership of shares) without the permission of the Federal Government. Moreover, wherever applicable, there are some incentives available to foreign investors in the form of reduced customs duty on certain imports and exemptions from sales tax. Additionally, foreign investors are allowed to repatriate the full extent of capital & dividends (subject to approval from the State Bank of Pakistan).

Generally speaking, the only restrictions on foreign investment in Pakistan, are related to the defence and national security sector and minimum investment amounts specified in relation to certain sectors[4].

The Policy works in conjunction with the Investment Promotion Strategy (IPS), the last such strategy was introduced by the Nawaz Sharif-led government in 2013 and was supposed to conclude in 2017.

THE INVESTMENT PROMOTION STRATEGY (2020 - 2024)

Following the general elections in 2018, the new Pakistani Government led by Prime Minister Imran Khan released a draft investment promotion strategy for the years 2020 to 2024[5]. This new strategy was developed in conjunction with the World Bank and is designed to further extend the goals and build on the lessons learnt under the previous IPS.

In the preparation of the IPS 2020 – 2024, the Board of Investment (the agency responsible to attract and manage FDI) conducted a thorough evaluation of all sectors which had initially been promoted by the Pakistani Government as part of its earlier strategy and reviewed the performance and competitiveness on quantitative and qualitative matrices. Following such review, the Board of Investment identified five sectors of the Pakistani economy which had performed exceptionally well and were ideally suited for FDI.

The following five sectors have been designated as priority areas:

1. Automobiles and auto-part manufacture
2. Food and beverage manufacturing
3. IT and ITeS
4. Logistics
5. Textiles

This paper shall examine the automobile and IT sector in detail (considered below). For recent developments in this sector, please visit [*insert hyperlink*]

Another core component of the IPS 2020 - 2024 is the internal reorganisation of the Board of Investment, itself, so as to provide a more effective and efficient means to facilitate foreign investors and to implement the goals of the IPS 2020 - 2024. Under the IPS 2020 – 2024, the Board of Investment will create region

[4] For a detailed review of the minimum investment amounts provided by the Investment Policy, 2013, the reader is advised to refer to the Policy, itself, for a clearer understanding.

[5] Investment Policy and Promotion Team, Pakistan Board of Investment (2019) – "*Investment Promotion Strategy: FY 2020 - 2024*" – Extracted from: https://invest.gov.pk/sites/default/files/inline-files/InvestmentGuide.pdf

specific units for the purposes of its promotional activities. However, on account of the high importance of the China Pakistan Economic Corridor (CPEC) to Pakistani policy makers, the Board of Investment shall maintain a specific country level focus on China, so as to allow the continued expansion of economic ties with Chinese investors.

Additionally, the Board of Investment will revamp its internal structure to be more transparent in relation to managing investor relationships and will take overt steps to improve the standard of information available to foreign investors. It is understood that the lack of sufficient information has hindered investor referrals in the past and the Government has understood this issue. Lastly, the new strategy envisages a stronger monitoring and evaluation mechanism for better coordination between the Board of Investment and all stakeholders on the Pakistani side, as well as at the international level.

THE AUTOMOBILE SECTOR IN PAKISTAN

As mentioned above, the automobile sector in Pakistan is among the most competitive sectors of the economy and routinely records positive indicators. In the financial year 2018, the automobile sector achieved the highest level of production and growth in this sector which is expected to continue on account of a variety of positive indicators and on the account of the entry of new players in the sector.

One such new entrant is the renowned Chinese automobile manufacturing company, Changan Automobile Investment (Shenzhen) Corporation, which entered the Pakistani market as part of a joint-venture with Master Motors Limited, a group company of the leading conglomerate, Master Group[6] in 2018. Our firm was directly involved in this transaction in its capacity as Pakistani counsel to Changan.

In connection with this transaction, Changan recognised Pakistan as a strategic export base for right-hand driven automobiles and the company intends to export vehicles manufactured in Pakistan to markets as far afield as Malaysia, South Africa, and Indonesia. This transaction marks the first time that an international automobile manufacturer has invested in the country with a view to export Pakistani-assembled vehicles. The venture is estimated to be worth USD 100 million[7].

The transaction is evidence of Chinese state-owned enterprises continued commitment to the Pakistani market and realisation of the untapped potential in the country. On completion, this business arrangement is set to introduce new automobile models in the Pakistani market at affordable rates, which has had a significant role in re-shaping the status quo in the sector.

Electronic Vehicles Policies, 2020 (“**EV Policy**”)

The Federal Government has also adopted two policies for introducing and encouraging electronic vehicles into the Pakistani market. The government has adopted different policies for heavy commercial vehicles and two & three wheelers on one hand and four wheelers, on the other.

In connection with the EV Policy for four wheelers, the Minister of Industries specified that the salient features[8] of the policy are:

a) The imposition of a flat 1% customs duty. The policy specifies that no additional custom duty, regulatory duty, or value-added tax is to be applied to electric vehicles’ specific parts for completely knocked down units. The removal of federal excise duty on electric vehicles. Toll tax for electric vehicles on national highways would be reduced by 50%.

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[6] “*Chinese auto giant Changan International enters Pakistan*” – The Nation (2018) – Extracted from: https://www.thenews.com.pk/print/382093-chinese-auto-giant-enters-pakistan

[7] Hussain, B. (2018) - “*China’s Changan and Master Motor to set up auto plant in Karachi*” – The Express Tribune – Extracted from: https://tribune.com.pk/story/1746047/2-chinas-changan-master-motor-set-auto-plant-karachi/

[8] https://www.pakwheels.com/blog/ev-policy-4-wheelers-approved-here-are-details/

b) The federal government will request provincial governments to exempt EVs from Registration Fee and Annual Renewal Token. Import of completely knocked down units in small cars and sport utility with 50kWh battery or below, and Light Commercial Vehicles (LCVs) with 150kWh battery would be exempted from Sales Tax, and VAT on imports, but with 1% Sales Tax on Sales.
c) The new policy will remain in force till **June 30, 2026.**

THE IT & ITeS SECTOR IN PAKISTAN

Another interesting area for Pakistan's foreign investment regime is the IT and ITeS sector. The IPS 2020 – 2024 stated that this sector generates approximately USD 2 billion annually for the country and had an average growth rate of around 30%. The Government has placed the IT sector at the very core of its Pakistan: Vision 2025 targets and also instituted the Digital Policy of Pakistan, 2018, which stands to further bolster the role of the IT sector as a driver of economic growth in the country. The Board of Investment has anticipated that the sector will be worth about USD 25 billion by 2025.

Under the Digital Policy of Pakistan, 2018[9], the Federal Government has identified a series of proposals which it plans on introducing into law to allow for greater incentives for FDI in the sector. Some of the fiscal incentives in the pipeline extend to exemption of certain duties, a favourable taxation scheme, and the establishment of special zones specifically for IT sector specific companies to operate from. In addition to the incentives available under the Investment Policy, 2013, the IT sector also benefits from the exemption of tax on venture capital investment until 2024[10].

Most importantly, the Federal Government has also identified a need to legislate to give the most effective implementation of the IT-sector specific projects. The overall state of the market for IT sector investments seems ripe for a greater level of involvement from foreign investors. This can be evidenced by the exponential rise of companies like 'daraz.pk' (an online retailer) which was purchased by the Alibaba Group in 2018[11]. Our firm regularly advises The Cheez Group, a Chinese e-commerce company, on its investments in the e-commerce industry in Pakistan.

In February 2021, the State Bank of Pakistan (SBP) notified revisions in Chapter 20 of the FEM to facilitate start-ups, fintechs and exports and to facilitate portfolio investments in the country. The new policy for equity investment abroad is aimed to attract foreign direct investment through the establishment of holding companies by Pakistani fintechs and startups; support exports by facilitating exporters to establish subsidiaries or branch offices outside Pakistan; and allow resident Pakistanis to acquire sweat equity.

Over the past year, despite its many challenges due to the COVID-19 pandemic, Pakistan has been engaged in adopting a number of important modernizing legislations and policies designed to further enhance the Pakistani legal framework with a technological focus in mind.

I. Digital Privacy in Pakistan

The incumbent Federal Government has been working on a draft of a data protection bill since at least 2018[12]. To this effect, the Ministry of Information Technology and

[9] Ministry of IT & Telecommunications, Govt. of Pakistan (2018) – "*Digital Policy of Pakistan*" – Extracted from: http://moib.gov.pk/Downloads/Policy/DIGITAL_PAKISTAN_POLICY(22-05-2018).pdf
[10] Ibid.
[11] "*China's Alibaba acquires Daraz*" – the Express Tribune (2018) – Extracted from: https://tribune.com.pk/story/1705095/2-chinas-alibaba-group-acquires-daraz/?amp=1
[12] Federal Ministry of Information Technology & Telecommunication, Draft Bill for Personal Data Protection (2018) – Extracted from: https://moitt.gov.pk/SiteImage/Misc/files/PERSONAL-DATA-PROTECTION-BILL-July-18-Draft.pdf

Telecommunication has been engaged with stakeholders on a number of fronts and has issued a consultative draft of a personal data protection bill in 2020[13].

Some of the salient features of the consultative draft are as follows:

- ***Consent:*** Personal data (including sensitive data) may not be processed without consent to the processing, unless the processing is necessary for a broad list of enumerated purposes.
- ***Lawfulness:*** The processing of personal data must be: (1) for a lawful purpose directly related to an activity of the data controller; (2) necessary for or directly related to that purpose; and (3) not excessive in relation to that purpose.
- ***Notice:*** Data subjects must be provided written notice that includes certain content when the personal data of the data subject is collected by or on behalf of the data controller. This notice must be provided when the data subject is first asked to provide the data, when the data controller first collects the personal data, or before (1) the personal data is used for a purpose other than the purpose for which the data was collected or (2) the personal data is disclosed to a third party.
- ***Disclosure and Transfer:*** Data controllers may not disclose personal data without the consent of the data subject (1) for any purpose other than the purpose for which the personal data was disclosed at the time of collection or a purpose directly related to that purpose, or (2) to any third party not within the class of third parties provided within its notice. In addition, personal data may not be transferred to any unauthorized person or system.
- ***Cross-Border Transfers:*** Where necessary, data may be transferred to a country that offers at least the same amount of protection of personal data, as long as the data subject provides consent where required and the data continues to be processed in accordance with the Bill's requirements.
- ***Data Localization:*** Critical personal data may only be processed in servers and data centers located in Pakistan.
- ***Data Security:*** Data controllers must take "practical steps to protect personal data" when collecting or processing personal data including, among other factors, taking into consideration the nature of the personal data and the harm that would result from loss, misuse, modification, or unauthorized or accidental access, disclosure, alteration or destruction. The data protection authority will prescribe standards that the data controller must comply with.
- ***Data Integrity:*** Data controllers must take reasonable steps to ensure that personal data is accurate, complete, not misleading and kept up-to-date.
- ***Sensitive Data:*** Additional limitations apply to the processing of sensitive personal data.
- ***Data Subject Rights:*** The Bill provides data subjects with the right to: (1) be informed about whether a controller has processed their personal data; (2) for a fee, make a data access request for the information being processed and to have a copy of their personal data provided to them in an intelligible form; (3) request correction of their personal data where inaccurate, incomplete, misleading or not up-to-date; (4) withdraw consent to process personal data; (5) prevent processing that is likely to cause damage or distress; and (6) erasure of their personal data when certain conditions are met.
- ***Breach Notification:*** Data controllers must notify the data protection authority within 72 hours of becoming aware of a personal data breach, unless the personal data is unlikely to result in a risk to the rights and freedoms of relevant data subjects.

[13] Federal Ministry of Information Technology & Telecommunication, Consultative Draft for Personal Data Protection Bill (2020) – Extracted from: https://moitt.gov.pk/SiteImage/Downloads/Personal%20Data%20Protection%20Bill%202020%20Updated.pdf

- ***Recordkeeping:*** Data controllers must keep and maintain a record of any application, notice, request or any other information relating to personal data that has been or is being processed. The controller also must maintain a record of personal data breaches.
- ***Retention:*** Data controllers may not keep personal data for longer than necessary to fulfill the purposes of the collection. The data controller must destroy or permanently delete the data when no longer needed.

The Federal Minister for Information Technology and Telecommunications stated as recently as January 2021 that Pakistan was seriously reviewing the implementation of a robust statutory framework for data privacy and protection laws for the country[14].

II. Reforms in the Pakistani financial sector: Digital financial services & e-Commerce

The State Bank of Pakistan has established the preliminary framework for the use of a digital finance platform called "Raast" (in English the word means "Direct"), developed in cooperation with the Bill & Melinda Gates Foundation, with support from the World Bank, Britain and the United Nations. The new system will be rolled out in three phases culminating in early 2022.

The government run instant digital payment system is a bid to boost financial inclusion and government revenue in the country where only a fraction of economic transactions occur on the books[15]. A major goal for the Raast payment system is to boost involvement of women in the formal economy.

The State Bank of Pakistan has specified that the core features of the digital payment system enable end-to-end digital payments among individuals, businesses and government entities instantaneously. The state-of-the-art Pakistan's Faster Payment System will be used to settle small-value retail payments in real time while at the same time provide a cheap and universal access to all players in the financial industry including banks and fintechs[16].

The State Bank's official website specifies that the key features of the new digital payment system are:

- **Instantaneous payments**: Near real-time digital payments across individuals, merchants, businesses, and government entities.
- **Low-to-no transaction costs for end users**: Raast is designed to operate at a cost recovery model in order to make digital payments affordable to end users of all socio-economic backgrounds.
- **Full sector-wide interoperability**: Raast will allow all financial institutions to seamlessly connect to each other via a single link to the central infrastructure, making digital payments accessible across any channel to customers of any financial institution.
- **Customer-centric innovative products/services**: Raast will be built on cutting-edge technological standards, allowing financial institutions to develop innovative and user-

[14] DAWN News (2021) – "Strong data protection law under study, says minister" – Extracted from: https://www.dawn.com/news/1600877/strong-data-protection-law-under-study-says-minister
[15] Reuters (2021) – "Pakistan government announces new instant digital payment system" – Extracted from: https://www.reuters.com/article/pakistan-economy/pakistan-government-announces-new-instant-digital-payment-system-idUSL4N2JM349
[16] State Bank of Pakistan (2021) – "Raast: Pakistan's Instant Payment System" – Extracted from: https://www.sbp.org.pk/dfs/Raast.html

friendly digital payment products and services (e.g. payment through phone number/email).

- **Reliability and enhanced security**: Raast will introduce more secure payment types, ensure that each transaction is authorized by the payer, and offer enhanced data protection and fraud detection services.

Additionally, in relation to e-commerce, the State Bank of Pakistan has introduced a number of amendments in the Foreign Exchange Manual of Pakistan ("**FEM**") which is the main regulatory framework pursuant to which the foreign exchange policies of the country operate. In December 2020, the State Bank of Pakistan issued amendments[17] in Chapter 12 of the FEM as it concerns to e-Commerce exports so as to align the existing framework with the changing business dynamics of e-commerce exports. In February 2021, the State Bank of Pakistan notified revisions in Chapter 20 of the FEM to facilitate start-ups, fintechs and exports and to facilitate portfolio investments in the country. The new policy for equity investment abroad is aimed to attract foreign direct investment through the establishment of holding companies by Pakistani fintechs and startups; support exports by facilitating exporters to establish subsidiaries or branch offices outside Pakistan; and allow resident Pakistanis to acquire sweat equity.

III. Geographical Indications Laws in Pakistan

The Parliament of Pakistan passed a much awaited Geographical Indications law in 2020 by the passage of the Geographical Indications (Registration and Protection) Act, 2020[18], and the subsequent promulgation of the Geographical Indications (Registration and Protection) Rules, 2020 by the Commerce Division of the Federal Government.

The absence of geographical indications, which are a distinct form of intellectual property protection, had been a critical failing of Pakistan's intellectual property regime. Internationally, Pakistan has suffered on a number of fronts, most prominently the issue of "Basmati" rice, which are a breed of rice grown specifically in North India and Pakistan[19].

CONCLUSION

While the Federal Government is still finalising a number of policy proposals, the general indication is that the Government is keen on enhancing the scope of its engagement with foreign investors and recent efforts by various institutions of the Pakistani state to stabilise the country have also borne considerable fruit. The Pakistani stock market has consistently been one of the strongest in Asia in recent years and is likely to benefit further from increased stability in the region.

The current government has been combating a complex array of economic problems and in the short term, the fiscal and monetary readjustment has been difficult for some sectors of the Pakistani economy. However, it is anticipated that the recent devaluation of the Pakistani Rupee and a more export driven economic policy will return Pakistan to a relatively stable economic position in the medium term.

While the exact policies and approaches being pursued by the current Pakistani government cannot be fully evaluated, on account of their still being in gestation on a number of fronts, the continued interest from internationally renowned brands in investing in Pakistan is a sign of the vast economic potential of the market in coming times.

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[17] State Bank of Pakistan – FE Circular 7 of 2020 – Extracted from: https://www.sbp.org.pk/epd/2020/FEC7.htm

[18] https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3609010

[19] https://www.dawn.com/news/1595139

It is important to remember that Pakistan is a jurisdiction which remains dynamic for investment and concerted efforts are underway by various stakeholders to simplify procedures and improve the ease of doing business, as evidenced by recent press statements by the World Bank in connection with its Ease of Doing Business 2020 study.