

Event Transcript

**Pakistan's Economic Turmoil:
Strategic Challenges, Consequences, and Contingencies**

October 2, 2018 | 2:00pm -3:30pm
The Stimson Center

Featuring:

Shamila Chaudhary, Senior Advisor to the Dean, School for Advanced International Studies, Johns Hopkins University

Arif Rafiq, President, Vizier Consulting

Yun Sun, Co-Director, East Asia Program, Stimson Center

Uzair Younus, Director, South Asia Practice, Albright Stonebridge Group

Sameer Lalwani, Director, South Asia Program, Stimson Center

Elizabeth Threlkeld, Deputy Director, South Asia Program, Stimson Center

More information and event video available at:

<https://www.stimson.org/content/pakistan%E2%80%99s-economic-turmoil-strategic-challenges-consequences-and-contingencies>

- Sameer Lalwani: Okay. Well good afternoon, everybody. Thanks so much for joining us here at the Stimson Center. My name is Sameer Lalwani. I'm the Director of our South Asia Program here at Stimson. I'm just here to briefly introduce the panel, and then hand it off to my colleague Elizabeth Threlkeld to take it away from here. But basically I just want to introduce this general area of discussion, the topic for today and my colleague Elizabeth.
- Sameer Lalwani: First, the broad topic, we've been spending a lot of time in the Stimson Center and our program, thinking not just about South Asia but Southern Asia, in which China is an essential part of that story. We've had a series running in collaboration with *War on the Rocks* for a little over a year now, which is evaluating the levels of competition at the military, strategic, economic and political levels, where China is a key player in the Indian Ocean, Southern Asia region.
- Sameer Lalwani: It clearly has implications for strategic stability in the region and for US foreign policy, particularly a US foreign policy that's oriented around an Indo-Pacific strategy. That is where we would nest this conversation within this broader discussion of Southern Asia and the Indo-Pacific.
- Sameer Lalwani: Today's topic on Pakistan's economic turmoil, strategic challenges, consequences and contingencies, is looking at a range of things that have come together in recent months that make this an interesting topic. There's what we believe to be some balance-of-payments crisis ongoing within Pakistan; the inability of Pakistan to cover two months' worth of exports, because of its foreign exchange levels have dipped below a certain level, which is leading to the consideration of an IMF loan.
- Sameer Lalwani: We have new challenges with the China-Pakistan Economic Corridor. There are new players coming into the mix; some successes of CPEC but also some shortfalls that have risen to the surface in terms of the discussion of whether this is, in fact, advantageous for Pakistan and its economy going forward.
- Sameer Lalwani: Then, most importantly, we have a new government in power in Pakistan, led by Imran Khan's PTI Party, with a reform agenda, a "Naya Pakistan" reform agenda. The brief survey evidence that you see out there in Pakistan suggests there's a lot of optimism in Pakistan today. A recent survey done by Gallup Pakistan found that 76% of Pakistanis are hopeful that the National Assembly will be able to solve major national issues, so a great deal of optimism.

- Sameer Lalwani: At the same time, this reform agenda has some challenges. There is obviously a welfare agenda about improving the quality of lives in Pakistan, increasing jobs, employments and housing. But also, there's some structural challenges; for example, taxation, which has been a perennial problem in Pakistan, increasing the number of people who pay taxes in Pakistan.
- Sameer Lalwani: Interestingly enough, there was a survey by Pakistan Gallup in June that found that even though there's only 1% of Pakistanis who pay income taxes, 53% of Pakistanis think that paying taxes are unjustified. It was quite a startling figure to me. How, for example, is Pakistan going to be able to weather these reform challenges, when there might be high expectations, but at the same time, a fundamental opposition to the basic requirements for economic reform? All this has strategic implications, again, for China, the United States, and a number of other regional parties.
- Sameer Lalwani: I'm going to turn this over to my colleague, Elizabeth, but I want to briefly introduce her because this is her first public event. Elizabeth Threlkeld is no stranger to competitive, challenging environments. She has joined us after having lived or worked in Iraq, Mexico, Pakistan, Turkey, and of course, the most competitive cut-throat environment of all--the US bureaucracy and interagency process. With that, I'll turn it over to Elizabeth, and to introduce the panel and the format for today. Thank you.
- Elizabeth Threlkeld: Fantastic. Thank you so much, Sameer. I want to start by welcoming you all and thanking you so much for making time in your afternoon to join us for what has proved an interesting and I think very timely conversation as well. This is something we've been wanting to do at Stimson for a while. I'm looking forward to hearing from our distinguished panelists on these issues, especially as they've been in the news, particularly over the last week or so. Also, I want to welcome the folks for joining us via live stream as well.
- Elizabeth Threlkeld: As we get started here, I will just briefly introduce our panelists. In terms of format, we will then ... I'll ask a couple of questions to get the conversations started. And we'll open it up to the audience for questions after we get to hear their remarks.
- Elizabeth Threlkeld: To my far left, we have Uzair Younus who is a Director with Albright Stonebridge Group's South Asia Practice where he helps clients develop strategies for long-term growth in the region. Uzair previously worked as a consultant with IBB Consulting and Deloitte, as well as with 32Advisors, which is a boutique consulting firm based in New York City. Uzair had

conducted research on infrastructure projects proposed by Prime Minister Modi's government in India, and he regularly publishes on South and Central Asian politics and trade.

Elizabeth Threlkeld: To my immediate left is Arif Rafiq who is President of Vizier Consulting LLC, a political risk advisory company, focused on the Middle East and South Asia. He's also a non-resident fellow at the Middle East Institute here in Washington, D.C. Arif previously worked for the Saban Center for Middle East Policy at the Brookings Institution, as well as in public relations.

Elizabeth Threlkeld: Arif's scholarly work focuses on political reform, religious extremism and terrorism in Pakistan, Afghanistan, and India, as well as on great power politics in South Asia. Very relevant to today's discussion, he recently completed a grant-funded study on the economic, political, and strategic implications of the China-Pakistan Economic Corridor.

Elizabeth Threlkeld: To my right is Yun Sun who is Co-Director of the East Asia Program and Director of the China Program here at the Stimson Center. Her expertise is Chinese foreign policy, US-China relations and China's relations with neighboring countries and authoritarian regimes.

Elizabeth Threlkeld: Previously, Yun was a visiting fellow at the Brookings Institution where she focused on China's national security decision-making processes and China-Africa relations. She's also served as the International Crisis Group's Beijing-based China analyst and has additional experience working on US-Asia relations here in Washington, D.C.

Elizabeth Threlkeld: Finally, to my far right is Shamila Chaudhary who is Senior Advisor to Dean Vali Nasr at the School for Advanced International Studies at Johns Hopkins University. She's also a senior South Asian fellow at New America. She has extensive experience in South Asia, both in and out of government, including from 2010 to 2011, when she served as Director for Pakistan and Afghanistan on the National Security Council.

Elizabeth Threlkeld: She previously worked on the Department of State's Policy Planning Staff where she advised Secretary Clinton and the late ambassador Richard Holbrooke on Afghanistan and Pakistan. She's held additional postings with both the State Department and with USAID. More recently, Shamila worked on Pakistan, Afghanistan and Sri Lanka for the [Eurasia] Group, a political risk consulting firm.

Elizabeth Threlkeld: Thanks very much to you all for joining us this afternoon. For the remarks, what we have planned this afternoon is to start with a zoomed-in picture

on what's happening right now in terms of macroeconomic issues in Pakistan, the issues with CPEC, a lot of the new developments that we've seen, even just from the last week, as Sameer was laying out.

Elizabeth Threlkeld: Then, we'll zoom out a little bit. We'll look more from a regional standpoint to help us think through issues on China and China's perspective, and China's goals with CPEC, and then Pakistan. Then, finally, Shamila will help us think through other regional implications, most notably India, how India have used these developments, and then from a US foreign policy standpoint as well. With that, I will turn it over to Arif who will get us started. If you can all remember to just turn on your microphone, that would be great.

Arif Rafiq: Thank you, Elizabeth. Good afternoon, everyone. Thank you, Elizabeth and Sameer, for organizing this event and inviting me to share my thoughts. Thank you all for being here. I'm going to provide a brief overview of Pakistan's economy, where it stands, what are the causes of the present challenges, propose some potential remedies, and then discuss the broader political and strategic impact, including potentially on CPEC. So all that within about eight minutes, hopefully.

Arif Rafiq: Pakistan's economy is on shaky ground. Balance-of-payments crisis is looming. Despite a number of policy interventions over the past year, including the influx of around \$3 billion from China, floating of the exchange rate, net foreign exchange reserves have declined to \$9 billion as of mid-September. That's below the threshold for covering three months of imports.

Arif Rafiq: In August 2016, the State Bank of Pakistan held \$18.1 billion in net foreign exchange reserves. That was when Pakistan completed a three-year IMF program. Within two years' time, the net foreign exchange reserves essentially halved. Again, that's after several policy interventions. By comparison, the State Bank of Bangladesh or the Bank of Bangladesh has around \$30 billion in foreign exchange reserves. We have comparable countries, comparable economies and vastly different external situations, external accounts situations.

Arif Rafiq: Pakistan's current account deficit just continues to widen. It was around \$15 billion in the 2016-2017 fiscal year. The previous fiscal year grew to \$18 billion. In the current fiscal year, it's likely to widen to at least maybe \$20 billion or more. This stems from a surge in imports that overlapped with a 33-month period in which the exports experienced a net decline. Imports are growing. Exports were in decline over this large period.

Arif Rafiq: The surge in imports has been driven by two major factors. One is the growing volume and cost of energy imports. Pakistan is a net energy importer, and fuel is the largest commodity import for Pakistan. It constitutes around 20% to 30% of Pakistan's imports, at least in terms of goods.

Arif Rafiq: Machinery imports have also grown in recent years. This machinery has been used for electric power and infrastructure projects, much of which has been through CPEC, but not all has been through CPEC. The machinery imports have leveled off this year. But as the price of oil continues to rise, and with that LNG, Pakistan has begun importing LNG, and it's pegged to Brent. The import bill continues to balloon.

Arif Rafiq: Energy is a major contributor to this disequilibrium in Pakistan. Again, Pakistan's top imported commodity is energy. Compare that to Bangladesh, its largest import is textile material. Pakistan essentially sells more raw cotton than it does finished garments. That's at the lower end of the value chain. Bangladesh is not a major cotton producer. But it's the world's second-largest exporter of garments; second only to China.

Arif Rafiq: Energy is also a big part of why Pakistan's exports are not competitive. Electricity rates are around 30% cheaper in Bangladesh, which has leveraged its domestic natural gas reserves for its export-oriented garment industry. Natural gas is about 50% cheaper in Bangladesh. The minimum wage is also about half of ... in Bangladesh, it's about half of that in Pakistan. Garment exporters in Bangladesh are taxed at rates around 12% to 15%, compared to 25% to 30% in Pakistan. Bangladesh also has a special police force for its economic zones to thwart labor unrest.

Arif Rafiq: My point is that public spending, at least in terms of subsidies or security, in Bangladesh, it's oriented around an industry that generates foreign exchange. In Pakistan, public subsidies and public goods are oriented around domestic consumption. That's a structural problem in the Pakistani economy. It's a byproduct of decisions that policymakers there make.

Arif Rafiq: Pakistan's problem with the current account is in many ways an energy problem. As a net energy importer and as a country that has comparatively expensive energy and electric power rates, as exports are less competitive, and so the country tends to find itself in a balance-of-payments crisis when oil prices rise. Pakistan needs around \$9 billion to prevent a full-blown balance-of-payments crisis. Total external financing needs, this year may total, will likely total over \$30 billion. We'll probably see a current

account deficit that approaches \$20 billion. Then, there's also \$9.3 billion in terms of external debt servicing.

Arif Rafiq: Public debt is also rising. We can get into those details a bit later. The budget deficit is also expanding. It's about at least, as of the middle of this year, it would be about 6.6% of GDP. The government is taking efforts, taking measures, to reduce that to around 5%, but it's going to be a very tough task.

Arif Rafiq: There are also liabilities in the electricity and energy sector that exceed \$10 billion. There's a liquidity problem in the energy sector. That's another structural issue that has taken a lot of attention in town here since the post-2008 period. There hasn't been decisive change in that regard.

Arif Rafiq: The new government has proposed an amended budget aimed at reducing both the fiscal and current account deficits. It's deferred major issues, major challenges, like tax reform. That's probably going to tackle those in the next budget. But the near-term impact is that growth will slow, those will likely be in the upper 4% range. Interest rates and inflation will approach or exceed double digits. The rupee could be devalued once again.

Arif Rafiq: An IMF bailout looks quite likely. The question for me seems to be, what size of a bailout will Pakistan receive or ask for? There's a certain threshold it may seek to avoid, in which it would have an extraordinary status and be the target of more, stiffer conditionality. It has an array of options it can potentially use to avoid that scenario. It could attract more foreign direct investment.

Arif Rafiq: Perhaps, if the markets stabilize, if there's a perception that exchange rates will reach a natural point that portfolio investors could return to the country, certain measures such as subsidizing natural gas for textile exporters could boost exports, and we could see a couple of billion dollars in terms of the net in the current account.

Arif Rafiq: As far as decision in respect to the IMF, Pakistan will likely make a decision by the end of this month. The Finance Minister had said last week that Pakistan will make a decision in mid-October, but Pakistan has a bit of a challenge with doing things on time, so we can just be a bit more liberal and say, "Maybe by the end of the month."

Arif Rafiq: How will this impact some public sector development, Pakistan public sector development program, and more specifically, the China-Pakistan Economic Corridor? I think most observers have clearly realized this

would probably be a slow year for CPEC. You have a new government in power. It has to acclimate itself to developing and to holding power. It has to develop a policy framework. It has more immediate priorities in terms of stabilizing the macroeconomic situation.

Arif Rafiq: But at the same time, this is a government that has a markedly different approach, at least notionally, in terms of what its allocation should be or what spending priorities should be. I think they will reassess CPEC, and instead of making it a supply-side-driven program, look to make it something that addresses actual demand of both in the country and in the region, in terms of transshipment and energy and all that.

Arif Rafiq: I think large-scale projects like there's a railroad. The main railroad line that connects Karachi to Peshawar will likely be deferred, the realignment of that. We could see China maybe take steps to either restructure or re-profile some CPEC-related debt. They should try to renegotiate some of these power agreements. But the big challenge is stabilizing the economy. I think there's a challenge in terms of staying committed through CPEC, not showing a sort of negative, avoiding negative signaling with respect to the China-Pakistan relationship, which is the target of great international scrutiny.

Arif Rafiq: But at the same time, it's a country that has some real fiscal challenges. I think it's going to have to figure out, in a very public way, how to address some of these CPEC, which has largely, I think, embellished some of Pakistan's structural flaws. Many of the electric power projects are quite expensive. It's contributed to this widening of the current account.

Arif Rafiq: CPEC has to become a bit of a transformative framework. It actually needs a set of ideas to govern it and then impact how Pakistan spends or borrows. That's going to take some time. I think, in the next year or so, you're going to see a bit of a slowing of the implementation and conception of CPEC. There are these attempts to multi-lateralize it. But that will also take some time.

Arif Rafiq: But I think, just going back to the issue of Pakistan's economy, I would say in a lot of, I think there's been a lot of focus on taxation and the weakness of exports. But energy seems to me to be a common issue, both in terms of making exports uncompetitive, and then also expanding and being quite vulnerable to fluctuations in global commodity prices. That's something maybe we can discuss in the Q&A, but that's just my food for thought. It may be unconventional in terms of how we look at Pakistan's economy, but I just thought it'd be worthwhile to start that way.

- Elizabeth Threlkeld: Fantastic. Thank you so much, Arif. We really appreciate those insightful remarks, and certainly, a lot to consider. Next, Uzair, you want to take [crosstalk]?
- Uzair Younus: Thank you, and thanks, Elizabeth and Sameer, for organizing this. I'll sort of take a step back. What Arif described are really challenges that the Pakistani economy is facing and challenges that we saw coming, about 18, 24 months ago, towards the tail-end of the Nawaz Sharif administration.
- Uzair Younus: But the larger question that I think we need to ask ourselves is, "Why is it that Pakistan's economy feels like Groundhog Day?" I was talking to my friend yesterday, last night, preparing for this talk. He said, "This feels like Groundhog Day, time and time again." I said, "I agree with you." But why is that? Why is it that there are 18 plus IMF programs, only one of which was successfully completed by Pakistan? But time after time again, every four to five years, there's another talk of another IMF program.
- Uzair Younus: I think the reason for this is that, at its core, Pakistan's economy is a rent-seeking extractive state that is both rent-seeking externally, so the outside powers takes advantage of its geopolitical location and its interests, and internally; where an elite extracts wealth out of it, the masses, in a way that, frankly, no other country in South Asia does.
- Uzair Younus: At that core of that rent-seeking state are the three B's, as I would describe it; the interests of the boots, the interests of the bureaucrats and the interests of the businessmen. Within those businessmen, some of you might be thinking, "Well what about the agricultural feudal elite?" They're part of that business group.
- Uzair Younus: What you have is that the structural flaw in the system that, when you have an IMF program, the elites are fine with what happens. It's the poor man and the poor citizen of the country that suffers. Time after time again, there is no incentive for the elites to make the tough policy choices that fix this Groundhog Day problem.
- Uzair Younus: Sameer mentioned at the start of his talk, 1% of Pakistanis pay income taxes, and 53% of them say, according to Gallup, that the taxation is unfair. I actually say, like, people talk about taxation in Pakistan as if it's a problem. Fundamentally, every Pakistani pays taxes. It's just that the taxation system is aggressive and extractive in nature. When you buy your cell phone card in Pakistan, you used to pay at least, until the Supreme Court turned it off, 40% withholding tax. You pay 40%, 50% in taxes in

the form of surcharges, and television fees, and power plant surcharges for your electricity bill.

Uzair Younus: You've had in, even if you look at, from the taxation perspective in the last five years, a doubling of tax revenue, under the Nawaz Sharif government, primarily through the extractive, aggressive taxation regime in the country, which has been expanded under every IMF program.

Uzair Younus: When you look at every IMF program, going back to the 90s, at least, the issues that the IMF explains are time and time again, to the sentence, exactly the same, but they don't get solved. They don't get solved because there has been a failure to invest in sustainable growth in the country, a failure of imagination, a failure to think out of the box about what this country can do.

Uzair Younus: Arif talked about textile exports and the fact that Pakistan exports more cotton than finished garments. I'd say there's only so many towels and bed sheets you can sell to the world. You got to sell something else as well, like what is it that Pakistan can sell? We don't know. We end up in this situation where industries that are uncompetitive by any stretch of the imagination, let's look at the auto manufacturing industry in Pakistan--wholly uncompetitive--continue to be protected by these business elite interests that do not allow a structural reform to the system. To make problems even worse, the policy is always behind the curve.

Uzair Younus: When you look back, as Arif talked about, the energy sector challenges, in the 90s, everyone will tell you the IPP policy was started under the Bhutto regime. It fundamentally hollowed out Pakistan's economy because energy costs were too high. Well in the last five years, we've had an energy policy regime reliant on imported coal. At a time when the rest of the world is running away from coal, including China, Pakistan has gone and generated about 30% of its energy mix coming from coal.

Uzair Younus: Those coal plants are not even located on the coastal line where the imported coal is brought in. They're shipped all the way into Sahiwal, through the agricultural belt of the country, where no one thought about coal dust problems or anything like that, into the Punjab where, November through January, you end up with toxic air, both on the Indian side of the Punjab and on the Pakistani side of the Punjab. But there are more coal power plants in the country.

Uzair Younus: Without resolving those structural issues, you cannot have an economy that is competitive, that is sustainable, that can grow and become stronger. The data that I want to share with you, I think, to showcase the sort of the

slide of the Pakistani economy is its productivity, labor productivity levels.

Uzair Younus: If you look at labor productivity in Pakistan in the 1980s, it grew by about 4.2% per annum, at a time when Pakistan's economy was considered a success story; 90s, it dropped to 1.8% per year; 2000 to 2015, it was 1.3% per year. If you look at since 2007, if you sort of ... the century's, the last eight years or so, it's about 1% per annum. In that same period, in India since 2000, a country right across the border, next door, 5% per annum growth in total productivity.

Uzair Younus: You run into this problem that you're not competitive. There is nothing to grow the economy sustainably. You end up in a debt trap. You end up in an IMF program. You end up being unable to sell anything to the rest of the world. I think, even now with the PTI and its "Naya Pakistan" agenda, there is nothing really that talks about structural reforms of the economy that make it competitive.

Uzair Younus: The last government had a vision: 2025 plan. The aspiration was to boost exports to about \$150 billion a year. I was like ... I laughed at it when I looked at that figure. I asked the then-Planning Minister Ahsan Iqbal what the government was doing to achieve this goal. His answer was, "We're investing in power plants." Power plants don't just give you the competitiveness to have exports upon it. What are your investments in total factor productivity? None.

Uzair Younus: One third of the workforce remains illiterate in Pakistan, 40% have under 10 years of schooling. You cannot compete in a 21st-century globalized marketplace with that kind of imbalance in your workforce. Those investments have to be made in Pakistan.

Uzair Younus: I was talking to a friend of mine who has a textile export business in Karachi. She said that they used to lose orders because of uncompetitiveness on the energy side. That uncompetitiveness still remains. But now, they have an issue where their labor that they hire cannot ... They have to spend a lot of money training them to stitch the modern garments that are needed because the fits have changed. The fits are much more ... they require some math, basic understanding of math, because the shapes are different. It is no longer the box t-shirt or the box jeans anymore, right? You don't get those at H&M anymore.

Uzair Younus: She cannot compete because, once she added the high energy cost, which is about 12 to 13 cents per kilowatt hour, Arif, right? You add that, on top of that, add about 20,000 to 25,000 rupees a year on training of your

workforce to make them competitive, so they can stitch the garments, it's uncompetitive.

Uzair Younus: The current government, what it's done, which is about a 2.1% fiscal adjustment, in terms of cutting the deficit is like telling a household, and I said it at another event with Shamila a couple of weeks ago, it's like asking a family to take out your children from school and not pay for healthcare, while the head of the household gets to spend on their new toys.

Uzair Younus: I think all of you here know what the head of the household is and what the toys are in Pakistan. Until and unless there is that conversation about what is it that the country is spending its money on and what is it that it needs to spend its money on? We will be here, three, four years down the road, talking about another IMF program.

Uzair Younus: I think my hope from this government is that it invests in education and skills development and fundamentally tackles the very structural interests at the heart of this rent-seeking extractive state, because if it doesn't, CPEC or no CPEC, a Saudi Arabian bail-out or no Saudi Arabian bail-out, this economy is not going to go anywhere. We can talk over what some of the solutions are, but I'll just stop there for now. Thank you.

Elizabeth Threlkeld: Great. Thanks so much, Uzair. We definitely want to follow up in the Q&A on what some of the potential solutions would be, but thanks so much for highlighting those issues. Next, we'll go to Yun for her thoughts on how China views this whole situation and across [inaudible] for CPEC.

Yun Sun: Thank you, Elizabeth. I really enjoyed both Uzair and Arif's comments. It's so sobering. I think if there's anything to say about China's perception and China's presence in Pakistan, I think the Chinese have been very much sobered at this point, as for what kind of challenge that they are faced with.

Yun Sun: Before I talk about CPEC, I think there's a question that needs to be answered as to why is this so important for China. I think there are primarily two reasons. Of course, on one hand, there's a strategic consideration on China's part that Pakistan is seen as China's pivotal state in the sub-region of South Asia. That's China's pivot. When you look at China's policy towards Pakistan and China's policy towards India was that they're the two side of the same coin; that the support lent to offer to Pakistan is the counterbalance or the balance to India.

- Yun Sun: Of course, there has been debate in China as for which country should be the priority of China's South Asia policy. That if China treats India better or with more friendliness, maybe that will determine the nature or set the course of China's policy towards South Asia.
- Yun Sun: But I would say that, to settle this debate, eventually, people would still come to the conclusion that China needs to seek a friendly relationship or a better relationship with Pakistan, in order to check and balance India; but on the other hand, that China also needs to seek a friendly relationship with India, in order to prevent India from seeking alliance or alignment with the United States.
- Yun Sun: We've talked about these sort of three layers of China's policy towards South Asia here at Stimson before. Basically, within South Asia, within the south region, China supports Pakistan, China supports other countries in South Asia, in order to counterbalance what the Chinese perceive as a regional hegemony of India.
- Yun Sun: Then, within the Asia region, China tries to preen, get closer, in order to prevent an India-US alliance or alignment in the region. Because on the global level, China seeks alignment or seeks of cooperation with India, in order to counterbalance a global north, both as a leader or a member of the emerging power or a developing country block.
- Yun Sun: That's the strategic-level consideration. But then, specifically, coming to China's vision for Pakistan's future. The hope that China has is to build Pakistan, or to help Pakistan, become a what they call the 3M country, 3M. The 3M stands for Modern, Muslim and Moderate. Because of the challenges that Pakistan has encountered in recent years, politically, economically, strategically, in terms of the security, so for China, Pakistan remains a fragile state, and it's a country that's become destabilized.
- Yun Sun: For everything that China has planned for the region, including as a regional strategy, including as future of Sino-Pakistan relations, Pakistan will only be a liability, and that the more destabilized it is, the bigger liability it is for China. That alone, there is also the national security, the homeland security concern that China has in terms of the Xinjiang and the Uighur issue.
- Yun Sun: If Pakistan remains a liability for China, then the support that Pakistan can lend to China's strategic vision is really going to be limited. Therefore, for the Chinese government, how to achieve or to help Pakistan to achieve its political stability and economic stabilization is really a priority.

- Yun Sun: The answer that, I agree with Arif, that CPEC is seen as a transformative effort in Pakistan. Also that view is not only prevalent in Pakistan, but it's also prevalent in the Chinese policy community, when they think about what CPEC is really trying to do in Pakistan.
- Yun Sun: Looking at it on the surface, it seemed that CPEC is really just a huge liability or a huge debt accumulation for Pakistan. But if you look at the specific projects of what China is trying to do, I would say there's more depth to the strategic consideration. I fully agree with Uzair in terms of the whole basket of challenges in Pakistan, systematically, politically, and elite politics, and the business, the environment and the labor issues. But you have to start somewhere.
- Yun Sun: For the Chinese, when they look at Pakistan, the design of the CPEC is primarily focused on the infrastructure of the country. I would say that it's focused on the most basic capacity building of the national economy. If you look at the design of CPEC, so energy and the power projects are seen as the priority area for the CPEC, and in terms of the scale of the investment, energy and power basically occupies about 70% of CPEC, and the other 30% is reserved for mostly transportation infrastructure.
- Yun Sun: There are various reports and discussions about CPEC. First of all, there's now seems to be one number to describe that how big the financial pledge really is. From the very beginning, I think it was somewhere around US\$ 46 billion. But now, the more popular number that we see is somewhere 62 billion or 64 billion, so much bigger than the original report.
- Yun Sun: But in the Chinese narrative, the one thing that is consistent, that has been consistent since 2014-2015, is the total number of projects. That number has been 22, including five hydropower projects, four fire power plants, four wind farms, four contracting services, four ... I'm sorry. Another three is the irrigation and the water project, and one port project and one highway. That 22 number has been relatively consistent in the Chinese narrative.
- Yun Sun: The Chinese Foreign Minister Wang Yi just visited Pakistan earlier this month. His statement, these 22 cooperation projects, according to him, nine have been completed and 13 are still under construction. The total volume of the investment is US\$19 billion. Of course, he also added other very positive numbers like 2% contribution to the GDP growth of Pakistan and something like 70,000 job opportunities that has come out of these projects.

- Yun Sun: Apparently, for the Chinese government, for Wang Yi, most specifically for his visit to Pakistan this time, the issue of that is the very emphasis or the very priority that he was focusing on. He specifically pointed out, while this is a Chinese government rhetoric, I should point it out, within these 22 projects, 18 of them are based on direct investments or the aid from Chinese; from the Chinese side, and only four of them uses the concessional loans from the Chinese side.
- Yun Sun: Then according to a report that Pakistani Finance Minister delivered, the data to the Parliament earlier this month, among the about US\$69 billion of foreign debt that Pakistan currently has, Beijing, China occupies around US\$8.4 billion. Within that 8.4, about US\$6 billion is concessional loans or loans for the CPEC projects.
- Yun Sun: What does this number; the Chinese number and the Pakistani number add up to? What do they mean? I'd say the first thing is that, yes, China is making a pretty significant financial contribution into Pakistani economy. However, the total number is not as high as the media or the original report had proclaimed.
- Yun Sun: We know that the disbursement of the Chinese financing is really made a step-by-step. It's not a one-time disbursement that completely goes into the project, so which means that, for this US\$19 billion of total investment that Wang Yi, the Foreign Minister was talking about, not all these investments are disbursed.
- Yun Sun: Even if it is completely disbursed, the total input that China has put into the CPEC is 19 plus 6. That's something around US\$25 billion. That's around half of the original financial pledges from other media reports since day one. It's pretty much aligned with the conversations that we have had with a Chinese policy analyst that about 50% is dispersed at this point, while the other 50% will be disbursed, and how soon that will be disbursed is another question. I think that's the first point that these data really illustrate.
- Yun Sun: I think the second issue that the data really illustrate is that when we look at China's financial pledges and input into Pakistan, not everything is limited through CPEC. CPEC has a lot of the loans and investments towards infrastructure. But if we look at other type of financial pledges or the financial contribution that China has made into Pakistan, there seems to be quite a significant chunk of money as well.

- Yun Sun: For example, according to the report by Reuters, during the first 10 months of the current fiscal year, China provided US\$1.5 billion of bilateral loans to Pakistan. At the same time, Pakistan also received around US\$3 billion of commercial loans. Most of these loans are from Chinese banks. We know that most of these Chinese banks are not privately-owned either.
- Yun Sun: Before the current fiscal year in 2016, China provided US\$900 million to Pakistan as a loan. But then, in the first three months of 2017, China also provided US\$300 million as a bilateral loan. This US\$1.2 billion of financial support that China provided to Pakistan is divided equally between CDB, China Development Bank, and ICBC. Both are not policy banks. CDB is a policy bank, but ICBC is more of a mix. But it is believed that the Chinese banks were at least operating under the auspices of the Chinese government to provide these loans to the Pakistani government. That's what the data is telling us.
- Yun Sun: I think now the key question is whether the investment or the concessional loans associated with CPEC is going to affect Pakistan's ability to seek loans from IMF. I think, here, there's a couple of factors that determine China's position. Of course, when the media reports first came out in July, the narrative that we hear is that, if Pakistan wants to seek this loan from IMF, it's going to affect the implementation or the advancement of CPEC. There's going to be a negative influence for CPEC.
- Yun Sun: I wouldn't say this is a strange or new perspective because I think China in the past has had experience with a similar situation. Back in 2009-2010, when China was doing the resources for an infrastructure project in DRC, IMF was concerned about the debt sustainability of the country. As a result, China had to cut the size of the project in DRC. If this same example is going to repeat itself, then there is going to be an impact, to say the least. But it also depends on the details and the negotiation.
- Yun Sun: I think the second factor for China or for Pakistan is that, to what extent the US will strongly object or reject Pakistan's application for this IMF loan? US decision seems to be not only related to CPEC, or to the economic decision-making, or the economic policies of Pakistan that is all related to the security policy, Pakistan's policy towards Afghanistan, but there's a much broader frame of issues that's being discussed here. Whether CPEC really forms a significant or the deal-breaker for the IMF loan, I think that's another question.

Yun Sun: The third question is then, say, the worst comes for the worst: will China pick it up? Does China have a choice? I think that's a more interesting question, as a China analyst, that that's a more interesting question, because I particularly appreciate Sameer's argument coming to CPEC that, yes, on one hand, it is ... But you could argue with [inaudible], that's a problem for Pakistan. But debt trap and lending trap, they're the two sides of the same coin, right?

Yun Sun: The more China contributing to Pakistan, the less able China will be able to, the less able China can afford to Pakistan to fail. If China has enough stake in Pakistan, that it decides that, no matter what, China needs to prevent the state from failing, and Pakistan is too important for China to fail, then I think China will make a decision to come to Pakistan's rescue, if it is needed.

Yun Sun: But from the Chinese perspective, I think the Chinese also have their complaints and grievances about what they perceive as unrealistic expectations from the Pakistani government and from the Pakistani community about China always being there and China willing to pick it up whenever Pakistan needs them to.

Yun Sun: I think the implication of that grievance or of that complaint is that China is also becoming more picky or stringent, coming to their conditions. In terms of some of the power plants that China has built or is building in Pakistan, if you look at the payment terms, look at the requirement that China has put into place for Pakistan to be able to pay China for the power generated, I think there is the element of social engineering coming to China's policies towards Pakistan.

Yun Sun: Of course, China also wants to invite in other investors in Pakistan in order to diversify the risk. I'd say, ADB and AIB, they're both seen as possible partners. Actually, they're having cooperation between China and these multilateral banks, multilateral development banks in terms of projects in Pakistan.

Yun Sun: Last but not least, the Saudi Arabia's joining the CPEC more recently is regarded as a very positive development for the Chinese side, that China is not the only country who is spending by Pakistan. Other countries also have their stake on the ground. I'll stop there and look forward to a discussion, I guess. Thank you.

Elizabeth Threlkeld: Fantastic. Thank you so much, Yun. It's really helpful. Very often, the conversation seems to center on Pakistan, but it's really helpful to hear the

Chinese perspective on these issues and how these look from Beijing.
Shamila, last but not least?

Shamila Chaudhary: Thank you. My friend here has done my homework for me. She said ... Or done my work for me, actually. Thank you. She said, “Pakistan is too important to fail, so we must bail it out.” Does that sound familiar to anyone? I think the last 10 minutes of what you said, I could probably just repeat it and replace the United States in it.

Shamila Chaudhary: This is actually like one of the worries/ideas that was going around the minds and conversations of US policymakers that we were looking at the Chinese and the prospects of this huge investment in Pakistan as both an opportunity but also a curse, right? Both for the Chinese but also for the international community which, from time to time, when Pakistan goes through these economic crises, will converge to figure out, how do we help them this time around, because it’s not in anyone’s interest to have Pakistan fail economically, right?

Shamila Chaudhary: As I was preparing for this presentation, I was writing. I was being very logical about it. Then, I realized that there are these tropes that were guiding my thinking that I just forgot to even question anymore. One of them was Pakistan’s economic stability is important to the international community. It’s vital, right? That’s something we tell ourselves. It’s like common knowledge now. But we don’t unpack it anymore. What does that mean?

Shamila Chaudhary: That’s what I ... What I really liked about the questions that I’ve been asked to address are, what are the implications of Pakistan’s economic challenges on US interests? Well to answer that, to answer if the Pakistani economy is important to us, we have to think about what the US, or not us, because I’m not part of the US government anymore. I can only speak for myself.

Shamila Chaudhary: But what’s important to the United States in Pakistan, whether in regards to the economy, we have to look at just what the basic priorities are there and how much are those basic priorities even related to the economy. Okay? We’re going to go big picture. Then, we’re going to go even bigger. Okay? Because I think that there’s ... We’ve got a lot of the background now. But I think, moving forward, there’s going to be a lot of questions that we’re going to have to ask that it’s going to take time because Pakistan is in transition. The region is in transition and so is the United States.

Shamila Chaudhary: Let's start with the vision laid out by Imran Khan. It's huge. He wants to create an Islamic welfare state. When I hear that, I think expensive; when I hear welfare state. Okay? I'm not even thinking about, what does an Islamic welfare state look like? I'm just thinking welfare state, given the state of tax collection in Pakistan; that just sounds impossible to me, right? He's really only going to be able to do a couple of things in whatever time he has.

Shamila Chaudhary: The US vision of Pakistan and strategy towards Pakistan, on the flipside, is much more limited in scope. If we look at what the strategy laid out by Donald Trump, was, when he announced it, several months ago now, it's very limited. I don't even know that he mentioned economic engagement in it, right? It was very much focused on Afghanistan and its security, and getting what the US needs to get out of the situation and not being tricked by this like duplicitous partner. Okay? Those were the ... That's what we have to work from. Those are the values, as reiterated by the President and expressed in the policy.

Shamila Chaudhary: Now, the history behind that is something that Uzair mentioned, which I think is really important. That's another foundational ... It's like a piece of the foundation for our analysis, which is, Pakistan is a rent-seeking state. That is how it's set up by design. The US has been a very much active participant in that, right?

Shamila Chaudhary: Now that the US is transitioning out of that dynamic with Pakistan, how does it deal with these periods of economic instability that Pakistan has had in the past, right? If its own behavior is shifting, but then the old behaviors are repeating themselves in Pakistan, what do you do? What questions do you ask of yourself? I'm putting that out there as just ... It's we have to have it in the background.

Shamila Chaudhary: Then, finally, like something in the background that we always have to remember is whatever the US does on Pakistan, vis-à-vis the economy, it sends signals to the outside world. Whatever the US says to the IMF, what the IMF says about Pakistan, it sends signals to the market, right?

Shamila Chaudhary: All of the capital that's out there, the investments, et cetera, everyone is watching to see if this is a go or no-go, right? Of course, it's not like high on the list of like financiers. There's a very small community for this sort of thing. But they are watching. Okay? Then, even development partners are watching because this impacts them. I'll get into that a little bit.

Shamila Chaudhary: But I want to make two big points. Then, I'll go into what the actual US interests are. I've laid this out as if I were writing a memo, if I was in the US government answering this question. But, of course, it's in the US interest that Pakistan be economically stable, both short and long-term. If not, these periodic economic crises will pull the United States back into this rent-seeking relationship orbit that it's actually trying to extract itself from.

Shamila Chaudhary: It does not want to be the lender of first, middle and last resort, when there's a crisis every five or six years, right? Especially, if the two countries keep finding themselves in opposite sides, on the biggest issues between them, which are Afghanistan, or the relationship with India, or just broader national security issues. I hate to say, it all goes back to Afghanistan, because I know that there's a much bigger story out there to be told. But that's how the relationship is defined now. If you look at the strategy, it's really based on that. We have to be very pragmatic about it.

Shamila Chaudhary: I actually think an economically stable Pakistan means that the United States and Pakistan can have a more normal relationship with each other because, especially, when it comes to Afghanistan about other issues because it's not based on a separate relationship of bailing each other out, should a crisis come along every five years, right? That's just like a basic relationship dynamic, I think. You could argue that US assistance is actually preventing Pakistan from making these tough economic decisions in some ways, because the US has always been there.

Shamila Chaudhary: All right. The second big point I want to make, and I just want to acknowledge, that Foreign Minister Shah Mehmood Qureshi actually said he talked about self-sufficiency in reaction to the US withholding certain assistance recently. I think this is a really interesting theme that he just threw out there. He's only talking about it in the context of the United States. We're not talking about it in the context of Saudi Arabia, or China, or anyone else, right? It's a very interesting theme that I think is ... We'll see if it has any legs. But I'm not very optimistic.

Shamila Chaudhary: But I do think that the self-sufficiency issue is like at the core of this discussion because there's also another trope that we've told ourselves, which is, "Well if Pakistan wasn't so dependent on foreign aid, it could actually do what it wanted, what it wants to, and it could take care of its people. It wouldn't be beholden to these conditions and requirements set on it by the loans and the grants and the development aid that it has, right?" I think that will be an interesting theme to explore, as we see what the Khan government focuses on and how their priorities unfold. Okay?

Shamila Chaudhary: I'm going to focus mostly ... You'll see it will be focused mostly on national security issues and politics. But that's not to suggest that economic and business affairs aren't important. There is a community within the US that focuses on these issues. They do a really good work. But that's just not rising to the top at this point, based on how the strategy is defined by the US government. Okay. Let's go through some of these themes. I'll do it really quickly. Okay.

Shamila Chaudhary: The first big interest, I would say, if I was asked this, and I was working at the White House again is, "We want an economically stable Pakistan because we want a stable partner that can facilitate the war in Afghanistan, right?" We don't want a country in economic chaos that's supposed to help us facilitate the movement of material or any other logistics that we rely on them for, because we need them to have the political space to maneuver and to deal with these contentious issues.

Shamila Chaudhary: The more Pakistan gets pulled into this economic chaos, the less they're able to work on any other issues, especially foreign policy issues and regional issues. They're just too ... It's just a no-go zone, right? It's just too complicated. Especially when you have such a weak coalition government dynamic, I think it's even harder to negotiate those things.

Shamila Chaudhary: The question for the US would be, "If Pakistan's economy collapses, which it won't, or if it goes into a balance-of-payments crisis, can we still get our material through the routes that we're using in Pakistan into Afghanistan? Can we get the Pakistanis to collaborate with us in the ways that we envision on reconciliation? Does economic chaos actually impact their ability to help us in X, Y and Z, on these national security issues?"

Shamila Chaudhary: I think that those things are really far apart. I'm not even sure that that's a realistic question to ask. But that's what I think we need to be thinking about. We're looking at what the US cares about and these economic challenges. I would say that, in general, like this relationship persists, despite the economic challenges, and despite the political challenges. I think it's shown itself for that.

Shamila Chaudhary: I wanted to make the point earlier that when I started first working on the Pakistan desk, it was at the tail-end of the Musharraf administration, or Musharraf government and the Bush administration. There was very little aid in general. It was all ... It was coalition support funds and security focus. The economic aid came after, right? The investment in Pakistan's economy and the people came after.

Shamila Chaudhary: It was a reflection of US values or of US priorities in the policy. You want to follow that, right? I think that answers the question. Now, we're at the opposite. The levels of US assistance are actually lower than they were in 2001. It's never been this low, right? I think that tells us exactly where we're at. Okay.

Shamila Chaudhary: The other issue when it comes to having a stable Pakistan or a stable partner is that the United States doesn't want to be the only one invested in the stability of Pakistan. It can't be the only one, especially because the level of assistance and the engagement is in transformation. It actually needs the IMF, right? It needs development partners, because it knows it's going to be able to function less and less, as this lender of first, middle and last resort, right?

Shamila Chaudhary: The irony here is that the coalition support funds from the United States, they no longer really exist. They've been actually used as a line item in the national budget. In fact, they've come to depend on those. I'm not suggesting that those funds were what got the country through the economic crises. By all means, they were not. They're a small amount in the larger scheme of things. But it's just another example of diminishing lines of revenue or streams of revenue that the government had in the past when they periodically came into this balance-of-payments crisis. Okay.

Shamila Chaudhary: The second interest is based on this idea of preserving the civilian government or making sure there's a strong civilian government in Pakistan. It's based on this idea that economic stability prevents coups from happening, because in the past, throughout Pakistan's history, they tend to happen when the country is in some balance-of-payments crisis. There's some really scary interesting research done on it.

Shamila Chaudhary: It's not that they're related. Uzair and I, we've talked about this at our event a couple of weeks ago. Economic instability is used as an excuse when there are other constitutional political crises happening in Pakistan. It's a way for the military to maneuver quickly against a weak poorly-performing civilian government, right?

Shamila Chaudhary: But the US and also India, because we're talking about the regional interests as well, and others will watch this, right? If the civilians are not doing their job, first and foremost, which is stabilizing the economy, then the military is always waiting in the wing. Ask any Pakistani and they'll tell you this.

Shamila Chaudhary: I don't think that this is just an American or an Indian perspective. It is the state of play there. I think the US will want to watch that carefully, right, when there's questions about economic stability. I don't think saying that Imran Khan is supported by the military is enough to like defuse this threat, right? You got to think about it.

Shamila Chaudhary: Yun talked a lot about China already, so I don't want to get too much into that. But I do think another US interest, with regards to Pakistan's economy is containing China/keeping an eye on China? Yeah. I don't think they've quite figured it out. It's a combination of all of the above. China can definitely be helpful on certain US interests related to security. But as you mentioned, that's changing. China's own foreign policy engagements aren't flexed. I do think CPEC has hypothetically created some breathing room for the United States to draw down certain kinds of assistance.

Shamila Chaudhary: But it needs to be ... I think it still needs to be watchful of how intertwined the economy becomes with Chinese investments. For the obvious reasons, with like China and like with its relationship with India, and also what it's done in Sri Lanka and Bangladesh, but also because of we don't know how these predatory lending practices will manifest over time and what political dynamics they might lead to internally in Pakistan, right?

Shamila Chaudhary: It's already been very destabilizing in terms of domestic political relationships, patronage, all of that, right? I don't think we know it enough to actually have too many concrete examples. But we don't want to get into like another repetitive cycle with balance of payments. Then, the CPEC is just another big factor there, whereas in the past, it was like high oil payments, for example.

Shamila Chaudhary: Then, finally, like the other risk related to China and Pakistan and for the US would be on the political culture angle. It's something that I've heard a lot about from media and a civil society in Pakistan who basically say that with donors come values. When the US was the biggest donor in town, the US likes to get involved in certain issues and wants to have a say on certain things, not even related to the assistance.

Shamila Chaudhary: China is no different, right? There's a view that if the Chinese are the biggest partner, and they're working closely with the military as they have been that that will shape how the Pakistani military or the government treats its media or its political opponents, and how it deals with insurgencies, right? There's this fear of the Chinese way becoming part of the Pakistani way, right? I think this is a little bit more of like this

amorphous challenge. But I think it's worth thinking about because that's all I hear now from journalists and other thinkers. It's also seeping into the mindset of other parts of society.

Shamila Chaudhary: There was this article I read today about Samiul Haq, the cleric who is basically saying like, "This is a trap. We're going to ... This is a debt trap from the Chinese." I just thought that was like, "What world am I in?" It's like an episode of Black Mirror. My whole life. Okay. Now, I'm going to be in trouble with the Chinese for saying that. But that's okay. Okay, really quick, because I know we want to get to discussion.

Shamila Chaudhary: But I think security and counterterrorism obviously are big priorities for the United States and Pakistan. I think that there's this idea out there that if Pakistan was just economically successful, there would be no terrorism. There would be no militants. There would be no madrassas. Everything would be a lot better. Let's get rid of that idea because that doesn't exist, right?

Shamila Chaudhary: But I do think that there's ... The question of does economic chaos create a more favorable environment for extremism, there's something in there to think about, right? There's something in there to think about. We are in a place now where the youth bulge in Pakistan is so large that we're actually seeing it manifest politically.

Shamila Chaudhary: Imran Khan is one of the manifestations of the youth bulge. They made him Prime Minister essentially, with the help of some other friends, of course. What could happen in an economic crisis this time around is different than ten years ago, now that you have this huge population which has very high expectations of this fan favorite who's become a politician, right? I think that's really the question. It's about the street game and what happens on the street rather than terrorism and extremism. We need to get away from that.

Shamila Chaudhary: Promoting business and commercial affairs, that's a really ... It's a low priority, I think, for the US, when it comes to Pakistan's economy. There is a trade relationship. I wouldn't say it's ... You could call it strong, I guess. It's not quite large, but it's there. But will Pakistan's economic challenges affect bilateral trade ties? I think that's very ... There's minimal impact there. The biggest ... There's a big consumer products market. That would be ... But again, there are challenges to like actually working in Pakistan that American businesses have had. I don't think that's going to be high on the list.

Shamila Chaudhary: There'll be some interesting questions about how does economic instability in Pakistan affect development programs? From donors, not just the US but others, it actually like increases the burden of development programs essentially because they're picking up where the state has left off. There will be ... At a time when the US is doing less and a lot of countries are doing less, what does that imply? I think that will hurt socio-economic indicators over a long period of time.

Shamila Chaudhary: I think I'll leave ... I'll end on just a quick India note. I said that ... I think India is mostly in the same category as the United States where it's thinking about economic instability in the big picture. They're not obviously going to get involved in helping Pakistan stabilize its economy. But they don't want a basket case on its border, right? They just don't. They can't afford it. I think that sentiment was what guided a lot of the conversations with Manmohan Singh.

Shamila Chaudhary: But that time period has passed. We're now dealing with Modi, and elections, and also elections in Afghanistan. There's just too much political transition in the region, I think, for any political leadership to take on some regional economic integration approach, or even just basic India-Pakistan rapprochement which we saw that in practice when Imran Khan's letter was rebuffed by the Indians. I hate to be a pessimist on that. But I don't really see anything. I would love to see something new. But I just don't see anything. I'll leave it at that.

Elizabeth Threlkeld: Fantastic. Thank you so much. Just to ask a quick question, to get our discussion going before we open it up to the audience, I actually wanted to pick up on the theme that you were mentioning, in terms of these parallels that seem to have emerged between what was once the US strategy in Pakistan is increasingly the position that China is finding itself in, in some ways. Yun, you mentioned the three M's. I was thinking back to Peaceful and Prosperous Pakistan, which was always something and it still is, that the US was interested in.

Yun Sun: Yeah, exactly.

Elizabeth Threlkeld: It's all about the alliteration. I just wonder, reflecting a little bit on the experience that the US has had in its relationship with Pakistan, over the past couple of decades, whether there are any lessons that can be learned in Beijing, looking at the US-China relationship? Are government officials in Beijing taking notes and seeing how they can adjust their strategies in Pakistan, the relations in Pakistan, in order to try to avoid some of the pitfalls that the US found itself in?

Elizabeth Threlkeld: Then, the other side of that coin, in terms of Pakistan, how is Pakistan viewing its relationship with China versus the relationship that it's had and continues to have with the US in these terms? Any lessons learned in Pakistan from the US experience that we might see applied in future years in China?

Shamila Chaudhary: Beijing. She asks about Beijing.

Elizabeth Threlkeld: What lessons that Beijing should learn, and is it too?

Yun Sun: Well, what lessons, well I think, from the Chinese perspective, they are very inclined to very much differentiating their relationship with Pakistan and not even compare this side of Pakistan relations to the US-Pakistan relations. I think that history does matter here. In the memory of the Chinese government and the Pakistani government, I cannot recall a major fallout between the two. I cannot recall a major period in the history that where these two countries really had a very hostile perspective on each other.

Yun Sun: You could argue that there's a geography here. There's a proximity. There's a factor of India. Neither side really was able to afford to have a hostile relationship. I would say the general atmosphere, when you think about this bilateral relationship and compare that to US-Pakistan relations, maybe there's some technical resemblance there like Pakistan, of course, their cooperation with China on the Uighur issue sometimes is also qualified. But on the rather higher political spectrum, the nature is very different.

Yun Sun: I would say that the extractive or rent-seeking policy that Uzair described that the US participated pretty much in that process, I don't think China sees itself as having participated in that, because regardless of what rent that is available in Pakistan, China's support, or maybe you could argue that the level of support may have varied historically, but the support or the nature of that support has been consistent.

Yun Sun: They understand ... I think the Chinese understand the challenges operating in Pakistan. But on the other hand, there's also an emotional element to it that because of the India factor, and because of ... Even, obviously, the counterterrorism or the US factor that China and Pakistan at different times feel that they share a sympathetic look at each other when they look at the regional politics or the global politics.

Yun Sun: If you look at what China follows from, China follows a non-aligned position, as it does not seek alliance with any country. But there are normally, well historically in the past 20 years, two decades, there are three countries that have been described as having a pseudo-, or semi-alliance relationship with China; North Korea, Burma and Pakistan. Among all these three countries, Pakistan has always been regarded as unquestionably, without any doubt, China's buddy. I would say that that's the difference.

Elizabeth Threlkeld: Anything on the US perspective?

Shamila Chaudhary: Well I just think that the issue of geography is very strong here that China in some ways doesn't need to learn some of the lessons that the US learned because its whole approach has been different. I think if there's one lesson to learn, like a very specific one, which would be to not give coalition support funds, because it's like a cash-in-your-pocket situation where it got better over time, of course, where there were more reporting requirements and follow-up and looking at how things were spent. But when it started it was so loosey-goosey. I just think that that set us up really poorly.

Arif Rafiq: Well on the issue of the coalition support funds, I think the Chinese have a different approach. They're actually making the Pakistanis pay for the security of their own personnel.

Shamila Chaudhary: That's right.

Arif Rafiq: Maybe they learned a lesson there. It's actually the Pakistani electric power consumer who will be ultimately paying or maybe the Pakistani state through issuing bonds and all that. I think that deals with some of the changing aspects of the Sino-Pak relationship, since the launch of CPEC. Initially, it was a highly military-to-military relationship. But now, there is this economic angle.

Arif Rafiq: There have been some discussions in Pakistan, both in the civil and military space, about becoming overly dependent on China. I think this pivot towards China in terms of the economic relationship perhaps began maybe notionally as a hedging strategy to indicate to the United States that we have options. But nobody else came to the table. It wasn't a rallying cry for other investors to come in, partly because of the singular commitments or privileges that the Pakistani state afforded to Chinese investors. But maybe there are other issues as well.

Arif Rafiq: There is this issue of economic dependence, and then also securitization of the relationship, in terms of physical personnel or Chinese nationals that are on the ground. I think that's something that relates to, what are China's ambitions in Pakistan? Does it really want tens of thousands of Chinese workers to be present in the country to move around freely?

Arif Rafiq: What are their expectations for security? Are there supposed to be security personnel that guard every single Chinese national across the country? Or is it simply dedicated for these very specific CPEC projects where you have, let's say, several hundred Chinese engineers come in; and then, after three years, they go back home?

Arif Rafiq: That's one element of uncertainty that reflects similar dynamics; that reflects some of the dynamics that animated the US-Pakistan relationship during the height of the Kerry-Lugar period.

Uzair Younus: Yeah, I would just add, I think the one thing to watch out for, and I saw this about six months ago when I was there in Pakistan, is the mutation of terrorist radical ideology, and that's beginning to sort of include the Chinese and sort of the apocalyptic prophecies in radical Islamic groups, and the ideologies around Gog and Magog. I won't get into the details of it.

Uzair Younus: But I saw a video which had about a quarter of a million views on YouTube, which was a mullah in Urdu talking about how CPEC is a part of this plan of Gog and Magog to come from China all the way into the Middle East. It's harebrained. But it fits into this ISIS ideology, if you follow it. I think what Samiul Haq said is sort of, for me, caught my eye, because it sort of links to that. That mutation is something worth watching out for and the CPEC security forces essentially to guard against that risk. We don't know where this will go.

Uzair Younus: But the amount of investment the Chinese are making and particularly in Balochistan and KPK though, the feathers that they're ruffling, you may see a weird mutation of like the Uighur movement which we are seeing some issues around in Pakistan on. There's this mutation of apocalyptic ideology that may have an impact, but it's too early to say that. But I've seen some videos that are showing there's evidence that they're transitioning towards that.

Arif Rafiq: You watch some strange videos.

Uzair Younus: Don't tell the NSA.

Arif Rafiq: They already know.

Shamila Chaudhary: Or Albright Stonebridge.

Elizabeth Threlkeld: Well thank you guys so much. That was really good to get your perspectives. I think there's a lot there; a lot that we need to dig into too in the Q and A, so I want to open things up to the audience for questions. A couple of housekeeping notes, if you can please wait for a microphone to come around before asking your question, and remember to identify yourself, that would be great. All right. Please, go right ahead.

Ken: Can we have the mic?

Elizabeth Threlkeld: Right there.

Ken: My name is Ken [inaudible]. I'm with the Pakistani Spectator. My question is that if Imran Khan is able to change the perception about Pakistan in terms of achieving, i.e. corruption is not ... It doesn't take trillions of dollars on changing the perception of Pakistan that it's not one of the most corrupt nations on earth. Do you think that could help?

Ken: Because the way you described Pakistani economic situation, there is no econometric model that would improve the situation of this country. On a technical basis, it's only perceptions that change that Pakistan is not radical. Then, you have issues [inaudible] in the context.

Ken: According to your statistics, Pakistani labor is not worse off than Bangladeshi labor. I could tell you, knowing a little bit about India, Pakistanis are not worse off than Indian average person. Things are not really that dire that we, kind of, going into details about your economic statistics.

Ken: If Imran Khan is able to do, let's say, something about land reform, some changing perception about corruption, and expanding the tax base in Pakistan, do you think it would decrease that; it would help to get Pakistan out of this economic crisis? Thanks.

Elizabeth Threlkeld: Great. Let's take a couple more questions in the interest of time. Sure. On the left?

Ibrahim: I'm Ibrahim. I'm a student here in NYU. I just want to say, first of all, thank you to all the panelists for the insight that you provided. My question was, so since partition, Pakistan seems to have always been in

this like perpetual self-perception as a security state. Because of that, there's a very popular narrative that security and defense have been the main beneficiaries of whatever financing that Pakistan has received.

Ibrahim: Do you think that that has contributed to the unsustainable nature of like whatever growth that Pakistan has tried to achieve? If so, would an improvement in relations with, I suppose, India, a country to like help or allow Pakistan to invest in education, infrastructure, technology, for a more sustainable model of economic growth? Thank you.

Elizabeth Threlkeld: One more on the back?

John: Hi. I'm John Dan Lowitz. I'm here on behalf of Barak Group Asia. My question ties into the question on corruption a bit; in the last six months, especially, maybe to a year, with the example of Hambantota and Mattala in Sri Lanka, and Bangladesh, of all country, taking a strong stand against CHEC. We've seen, in the South Asia region, a pushback on sort of this state-level corruption coming out of Chinese-backed projects.

John: Do you think that this is having an effect on the narrative within Pakistan, and that it's leading to a greater awareness of the corruption threats from CPEC, and whether that's having a greater trickle-down effect on addressing corruption, writ large, or if that's just a very specialized focus on we don't want China to securitize its investments in Gwadar?

Elizabeth Threlkeld: Great. Thanks. Our first question on whether Imran Khan will be able to improve the perceptions of Pakistan and that potential impact, any thoughts?

Arif Rafiq: Well some of the reforms that you'd mentioned, land reform, anti-corruption measures, those are important for investors. But I think one of the major concerns they have is the security of their investments inside the country; legal protections. Unfortunately, you have a highly interventionist judiciary which has overturned or nullified certain major deals that the Pakistani state specifically has been a net loser out of that.

Arif Rafiq: But if you go back to the 1990s, in terms of some independent power projects, to Reko Diq and some of these other deals, the judiciary is a big factor. I think when countries want to make large-scale investments inside Pakistan, I think one of the biggest challenges is the role of the interventionist judiciary and the change of government.

Arif Rafiq: Corruption, anti-corruption, land reform, those issues are important to helping the Pakistani economy thrive; evolve; giving capital to the

common citizen; land and their title rights and all that. That will help in terms of the economy's long-term growth. But I think these other issues such as the courts and the actual security of their investments are probably more important.

Elizabeth Threlkeld: The second question is on the impacted growth of the [inaudible].

Uzair Younus: It definitely has contributed to it. It is a problem, right? You've had a security state where the Armed Forces makes DHAs. They run amusement parks. I grew up eating Fauji cornflakes. Maybe some of you did. Why was the Army making cornflakes? I don't know.

Arif Rafiq: But you're very healthy, so yeah.

Uzair Younus: Not because of that.

Arif Rafiq: It's fortified; iron-fortified.

Uzair Younus: It definitely has had an impact. I would not just talk about just the security state itself and not just the military. It's, again, what I described as the three pillars of the rent-seeking state. It's the boots. It's the bureaucrats. It's the business interests. They have aligned in such a way that you cannot have a sustainable growth period.

Uzair Younus: Imran Khan, for example, has to grow Pakistan, if you look at the examples of all governments in the country, even over here, the administration, they can add mostly two bigger major things; maybe three, if they have a great time. But one to two is big.

Uzair Younus: What can Imran Khan do out of those one or two things that can sustainably set Pakistan on a path of growth? My view is like solve the energy sector problem because the circular debt in the system and the uncompetitive nature of the energy markets means not only that you're uncompetitive globally, but the crowding-out effect on investments is huge like hundreds of billions of rupees a year are pumped into this sector from the banking system that can be spent elsewhere.

Uzair Younus: Then, secondly, improve the skills development program of the country. You cannot have 20, 25 million children out of school and run a 21st-century industrialized state. It's just not possible. Those two would be my priority areas for his government. Hopefully, they can do something about it.

Shamila Chaudhary: Can I just say something on that? Well your question points to the US-Pakistan case study, which is like the biggest example of how foreign funding can prop up the military and create this imbalance between civilians and the military. We've seen it, since the 50s, essentially. It got pretty extreme after 9/11, and I think now that the US security assistance is basically at zero, I think. I don't think it's going to go back to the War on Terror levels ever again.

Shamila Chaudhary: I do think that there are questions about how the military will maintain that position, just based on what they were getting from the US. It wasn't just like coalition support funds, there was all sorts of equipment, and training, and assistance. I'm sure they can get it from the Chinese too, which I think that's clearly been the replacement for the US. But Chinese equipment is not as good as the American equipment, right? They're ... Sorry. All of these ... The devil is in the details, in some ways, right?

Shamila Chaudhary: For another example to just ponder is when the Obama administration passed that Kerry-Lugar-Berman legislation which basically gave like ... It was a multi-billion-dollar package to strengthen the civilian government. That's really what it was for. It was all development focus.

Shamila Chaudhary: The military really was outraged by that. They saw that as a threat, a direct threat to their supremacy, and within Pakistan at that time. It was a lesson for the US that, even though we felt like we had consulted everyone that needed to be consulted, it didn't matter, right? There are all these other politics associated with it. But I don't see that dynamic going away. If it's not the US, it's someone else. The institutional interest will still persist.

Yun Sun: I should say I'm a China analyst, but I don't speak for China.

Shamila Chaudhary: I know. I know. I didn't mean to like point at you.

Yun Sun: No, no, no. Not at all. [crosstalk]. On the issue of corruption on the Chinese projects in Pakistan, I will say that ... Well I worked a lot on China-Africa. There's even more discussion as well, whether China's is contributing to corruption. I think China certainly is.

Yun Sun: But I think it is also fair to say that China did not create a problem. The extractive rent-seeking system in Pakistan was not set up by the Chinese. But the Chinese play along. They certainly would like to play along and to make business opportunities more prosperous and more feasible, when they do business on the ground. This certainly has not contributed to the improvement of the problem.

Yun Sun: But then, to give you almost like a joke, in the Chinese answer to the ... If you look at how the Chinese government officials or some of the policy analysts answer the question of corruption, for example, in the case of Africa, the Chinese actually have an argument that because our concessional loans and our investments have been primarily used to purchase, to procure Chinese services and products. We are contributing to the elimination or the mitigation of the corruption problem in Africa or on the ground because money doesn't go there.

Yun Sun: The money only ... Because the money only changes accounts in a Chinese bank, from this bank account and to another Chinese bank account, so we're certainly not contributing to the corruption problem. But I think, for serious analysts, we don't really pick that as a very logical argument.

Yun Sun: But in the case of Pakistan, I would say that simply because of the scale of the Chinese input into the country and the many projects that the Chinese are involved in, I think the issue of corruption certainly is not rare. Based on the complaints from the civil society and from observers and media, it's certainly not a rare problem. It has gotten more attention. It has invited more scrutiny.

Yun Sun: But I think, from the Chinese perspective, will this issue become a threat to China's current projects in Pakistan? I think there, the Chinese perception is as long as they maintain a very good relationship with the head of the household, they will be able, and also provide the new toys. I think they're relatively comfortable and feel relatively secure about their economic investment, at least more than other countries.

Arif Rafiq: I think in terms of the pushback against Chinese corruption or alleged Chinese corruption, they've seen that when there's been a change of government, so in Bangladesh and Malaysia. Then, there's been a change of government in Pakistan as well. I think that reflects the, I don't want to say anxiety, but something akin to anxiety, at least in terms of the Chinese presence in Pakistan.

Arif Rafiq: They're very keen to meet with the new government; all the major players early on; soon after the elections. The Chinese ambassador to Pakistan wrote a letter to the incoming parliamentarians inside the country and pledged that China would emphasize investments that facilitate Pakistan's exports and bolstering its agricultural sector.

Arif Rafiq: I think there's a recognition that when there's a change in government, people open the books from the previous five years or whatever, the previous tenure, and look at it with great scrutiny. That's why, for example, with the Hambantota case, the New York Times had a very detailed exposé earlier this summer, and it's because the new government was exposing all sort of the dirty deeds of the past, previous government.

Arif Rafiq: There has been that discussion in Pakistan. PTI was the leading opposition party or one of the two leading opposition parties in the previous government. But now, it's in power. It has its own rent-seeking interests as well.

Arif Rafiq: Then, also the Chinese, when CPEC was initiated, there was a debate as to whether sort of the spoils of CPEC or the funds were being evenly distributed across the country. In December of 2017, there was sort of a joint China-Pakistan meeting that was held in Beijing. They essentially spread the [inaudible] and allocated some projects for public transport, basically in each province. I think the Chinese mission in Pakistan has an ability to really manage these diverse constituencies inside the country. It's very much similar to what happened after 2008 with Kerry-Lugar; all these people.

Arif Rafiq: The largest number of Chinese ... China hosts the largest number of Pakistani foreign students now. It exceeds that of the United States. There are Pakistanis studying in Chinese medical schools and business schools, and so on and so forth, and in some very good schools. I think they know how to sort of manage some of the challenges there; reputational challenges.

Shamila Chaudhary: Can I just add one thing on perception that you mentioned? When I speak with businesses, all non-Chinese businesses, the only thing they really ask is, "How long is he going to stick around?" when they're talking about like the government, right? It could be Nawaz Sharif. It could be Zardari. It could be Imran Khan. It doesn't matter. How long is he going to stick around? Because they know that, as Arif mentioned, like there's political transition, and they know what the challenges are. The Chinese are more immune to those kinds of things. They're in it for the long game. But the rest of the world is not in it for the long game, right?

Shamila Chaudhary: There's a totally different calculation that goes along with investing in Pakistan, if you're a non-Chinese business. Political stability sends a very powerful message to the outside world. It's not enough that he's a favorite of the military. It's not enough that he's talking about corruption which,

by the way, looks like he's going after his political opponents, right, if you are looking at it from this side of the ocean. Expanding the tax base is great. But that's never going to happen, right? That's such a big picture thing.

Shamila Chaudhary: I think that like there are other things that can answer those questions. A strong political government can often give more confidence than saying, "We're going to have a whole new tax regime," for example, right, because we're thinking short-term. We're not doing long-term.

Yun Sun: Can I add to that?

Elizabeth Threlkeld: Please.

Yun Sun: I'm sorry. Just to follow up on that, so it is true that during the government transition period in various countries, not only Sri Lanka, but also Malaysia, Burma and Zambia, especially during the campaign and election season, the Chinese deals with the incumbent government this year may be scrutinized. Yearly, it becomes a much bigger issue.

Yun Sun: But we just mentioned that China's here for the long game. The Chinese understand very well that after the new party or the new government comes in, guess who has the most cash in town? I think the Chinese are more or less adapting themselves to this new reality that during the political transitional period that they are going to be scrutinized and that there are going to be bad publicity associated with the Chinese projects. But after that new government assumes office, they will still come to China with a proposal that would need this much funding from the Chinese.

Elizabeth Threlkeld: I'm afraid that is all the time we have this afternoon. It is safe to say I think this is going to be the start of many conversations that we hope that you all and our panelists as well will join us again at Stimson and follow up on more of these issues in the future. But thank you so much for attending and please join me in thanking our panelists.