

# CPEC Phase II: From Infrastructure Corridor to China's Industrial Footprint in Pakistan

BY EARTH NEWS POLITICAL DESK

In January 2026, Pakistan's Board of Investment announced a significant expansion in the number of Special Economic Zones (SEZs) planned under the second phase of the China-Pakistan Economic Corridor (CPEC). The number of approved zones jumped from seven to forty-four, including thirty-seven newly notified industrial sites. On the surface, this announcement appears to be a technical update in Pakistan's economic planning. Yet, viewed through a wider geopolitical and economic lens, it represents something far more consequential — a transition in CPEC from a corridor of roads and power plants into an ecosystem of factories, supply chains and industrial networks closely tied to China.

This transition, often described as CPEC Phase II, marks a deeper integration of Pakistan's economy with Chinese manufacturing systems, technology standards and investment networks. While the first phase of CPEC focused on physical connectivity — highways, energy projects and the development of the port city of Gwadar — the second phase aims to embed Chinese industrial production inside Pakistan itself.

The implications extend beyond economics. Industrial ecosystems create long-term dependencies, influence technological choices and shape supply chains in ways that are difficult to reverse. For Pakistan, this transformation promises investment, employment and export potential. For China, it offers a strategic manufacturing extension beyond its borders. For India and the wider region, the shift raises new strategic questions about the evolving depth of the China-Pakistan partnership.

**The Evolution of CPEC**  
CPEC was launched in 2015 as one of the flagship projects of China's global Belt and Road Initiative (BRI). Its original objective was to connect China's western region of Xinjiang to the Arabian Sea through a network of highways, railways, pipelines and energy projects running through Pakistan.

With an estimated value of nearly \$70 billion, the corridor was projected as a transformative economic partnership. Pakistan hoped the investments would address long-standing infrastructure deficits, particularly in electricity generation and transport connectivity. For China, the corridor offered strategic access to the Arabian Sea and a direct route linking western China to international markets.

During the initial years, CPEC concentrated largely on infrastructure development. Energy projects were prioritised to reduce Pakistan's chronic electricity shortages. New highways and road networks were built to connect major cities and industrial centres. Gwadar Port was developed as a key maritime gateway intended to link Chinese trade with the Middle East and Africa.

These projects did produce visible results. Electricity generation capacity improved, reducing the severe power shortages that had previously affected Pakistan's industries and households. Road connectivity between major urban centres improved as well.

Yet, despite these infrastructure gains, Pakistan's broader economic challenges remained largely unresolved.

**The Limits of Infrastructure-Led Growth**

Infrastructure development alone does not automatically translate into industrial growth or export competitiveness. Pakistan's experience during the first phase of CPEC demonstrated this clearly.

While new power plants and highways improved physical connectivity, they did little to address structural economic weaknesses. Pakistan continues to struggle with low export diversification, weak manufacturing productivity and chronic shortages of foreign exchange.

In 2024, Pakistan's economy was valued at roughly \$371 billion, according to World Bank estimates. However, its exports of goods and services stood at only around \$40 billion. Compared to other emerging Asian economies, this export performance remains modest.

At the same time, the country's power sector became burdened with mounting financial liabilities. Many CPEC power plants were developed under Independent Power Producer (IPP) contracts that guaranteed returns through fixed "capacity payments." These agreements required the government to pay producers even when electricity demand was lower than expected.

The result has been a growing financial strain. Pakistan's circular debt in the



power sector crossed Rs 2.6 trillion, driven by transmission losses, poor bill recovery and rising subsidies. Since many payments are denominated in US dollars, the depreciation of the Pakistani rupee has further increased the financial burden.

These financial pressures now intersect with the ambitions of CPEC Phase II. Industrial zones require reliable and affordable electricity. Without reforming the power sector, the success of these zones could remain uncertain.

**The Strategic Logic of Special Economic Zones**

The core of CPEC Phase II lies in the creation of Special Economic Zones — designated industrial areas offering tax incentives, infrastructure support and simplified regulatory procedures to attract investors.

SEZs are not a new concept. Many countries have used them to promote export-oriented manufacturing and attract foreign investment. China itself used SEZs in cities such as Shenzhen to drive its own economic transformation in the late twentieth century.

What makes SEZs under CPEC particularly significant is the role Chinese companies are expected to play as anchor investors.

When large foreign firms establish factories in industrial zones, they rarely bring only capital. They typically introduce a complete industrial ecosystem: machinery, technology platforms, supply chains, quality standards, software systems and managerial practices. Local companies often adapt their operations to fit these systems.

Over time, this can generate several forms of economic dependence.

One form is technology dependence. If machinery and production systems are sourced primarily from Chinese manufacturers, local industries may remain reliant on Chinese technology and spare parts.

Another is standards dependence, where production processes align with Chinese technical standards and certification systems.

There can also be supplier dependence, as local firms begin to rely on Chinese components, inputs and service contracts.

Financial dependence is another factor. Expansion, maintenance and technological upgrades in such zones often remain linked to Chinese financing or joint-venture arrangements.

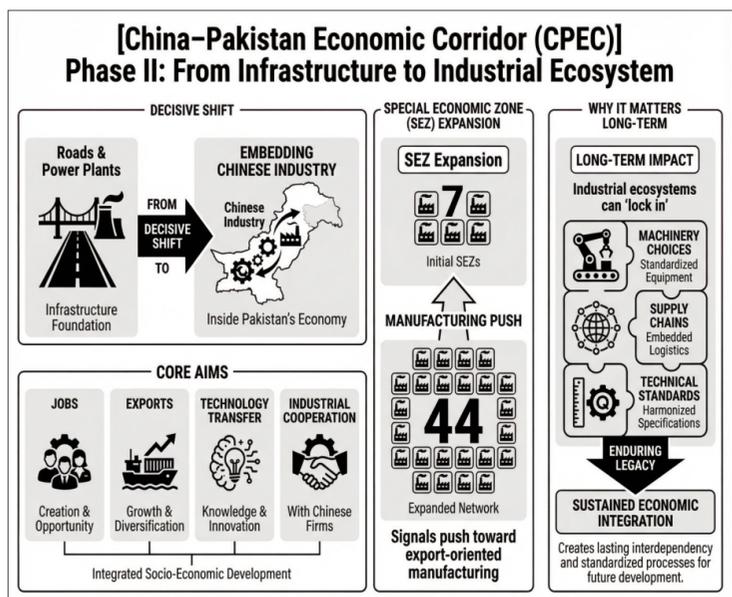
Finally, there is human capital dependence. Operating advanced industrial systems requires specialised skills. In many cases, Chinese technical instructors, training programmes and educational partnerships become embedded in local vocational institutions.

Together, these layers of integration create a durable economic footprint.

**Pakistan's SEZ Landscape**  
Pakistan's SEZ framework is governed by the country's Special Economic Zones Act of 2012, with the Board of Investment overseeing implementation. The government has attempted to create a "one-stop shop" model designed to simplify administrative procedures for investors.

However, many Pakistani SEZs still face practical challenges.

Reports indicate that several zones lack essential facilities such as dedicated electricity connections, water supply systems, sewerage networks and on-site customs offices. Without such basic infrastructure, attracting serious industrial investment



becomes difficult.

This is why the expansion from seven to forty-four approved SEZs must be viewed with caution. Announcing new zones is relatively easy; ensuring that they become operational industrial hubs is far more challenging.

A few zones are currently considered more advanced or strategically important.

One is Rashakai Special Economic Zone in Khyber Pakhtunkhwa, positioned near major transport routes. Another is Allama Iqbal Industrial City in Punjab, located close to established industrial clusters and supply networks. Dhabeji SEZ in Sindh benefits from proximity to Karachi's port infrastructure, while Bostan Industrial Zone in Balochistan is intended to promote industrialisation in a historically underdeveloped region.

These zones differ widely in terms of infrastructure readiness, investment potential and security conditions. Their eventual success will determine whether CPEC Phase II becomes a meaningful industrial transformation or remains largely symbolic.

**China's Industrial Push Abroad**  
China's strong interest in overseas industrial zones reflects changes within its own economy.

Over the past decade, China has developed enormous manufacturing capacity in sectors such as solar panels, electric vehicles and lithium-ion batteries. In many of these industries, production capacity now exceeds global demand.

For instance, global solar manufacturing capacity has expanded rapidly, with output projected to far surpass worldwide demand. Similarly, battery production capacity in China alone is close to the total global demand for electric-vehicle batteries.

Such overcapacity creates pressure on Chinese companies to find new markets and production bases abroad.

Establishing factories in partner countries offers several advantages. It allows Chinese firms to expand into new markets, avoid tariffs imposed on Chinese exports and reduce political pressure related to trade imbalances. Manufacturing in third countries can also help companies remain competitive in an era of increasing "de-risking" from China by Western economies.

CPEC Phase II therefore aligns with China's broader strategy of internationalis-

ing its industrial base.

**Emerging Industrial Projects**  
One of the most visible examples of this industrial push is the planned electric vehicle assembly plant by Chinese automaker BYD in partnership with Pakistan's Mega Motor Company.

Construction of the facility began near Karachi in 2025. With an initial annual capacity of around 25,000 vehicles, the plant is expected to begin operations by mid-2026. Initially, it will assemble vehicles using imported components, with gradual localisation of certain parts over time.

Such projects illustrate how Chinese manufacturing could gradually establish footholds within Pakistan's economy.

The solar energy sector provides another example. Pakistan's imports of solar panels increased dramatically between 2022 and 2024, reaching around 16.6 gigawatts. Chinese manufacturers dominate this market due to their competitive pricing and large-scale production capacity.

As renewable energy becomes more central to Pakistan's electricity mix, Chinese companies could expand from simply exporting solar panels to establishing assembly, maintenance and manufacturing facilities inside Pakistan itself.

**Structural Challenges for Pakistan**  
Despite these opportunities, Pakistan faces significant structural constraints that could limit the success of CPEC Phase II.

Macroeconomic stability remains a major concern. Pakistan has repeatedly faced balance-of-payments crises, forcing the government to seek financial assistance from international lenders including the International Monetary Fund (IMF).

Under IMF programmes, Pakistan must maintain greater transparency in its debt obligations and financial guarantees. This requirement complicates the financing of large infrastructure and industrial projects, particularly if they involve opaque financial arrangements.

Policy consistency is another challenge. Investors often cite unpredictable taxation, bureaucratic delays and regulatory uncertainties as obstacles to doing business in Pakistan.

Infrastructure gaps persist as well. Reliable electricity supply, efficient ports and streamlined customs procedures are essential for export-oriented manufacturing. Without improvements in these areas,

SEZs may struggle to attract sustained investment.

**Security Concerns**  
Security remains one of the most sensitive issues surrounding CPEC.

Several attacks targeting Chinese nationals have occurred in Pakistan over the past decade. Some of these incidents have been claimed by militant groups such as the Baloch Liberation Army, which opposes large infrastructure projects in Balochistan.

Although the number of casualties remains relatively limited, such attacks have heightened concerns among Chinese investors and workers.

To address these risks, Pakistan has deployed thousands of security personnel to protect CPEC projects. There have also been reports suggesting that Chinese private security companies may have been involved in protecting certain installations, though these claims have not been officially confirmed.

Industrial zones, unlike isolated infrastructure projects, require a continuous flow of workers, engineers and managers. This makes them more vulnerable to security disruptions and increases the importance of long-term stability.

**Strategic Implications for India**  
For India, the evolving nature of CPEC carries important strategic implications.

One longstanding concern relates to the corridor's route through Pakistan-occupied territories in Jammu and Kashmir. From India's perspective, projects passing through these areas raise sovereignty issues.

Beyond this territorial dimension, CPEC Phase II introduces new strategic factors.

Industrial ecosystems create deeper economic linkages than roads or power plants. If Chinese manufacturing networks become firmly embedded within Pakistan, the economic relationship between the two countries could become significantly stronger and more complex.

Industrial parks linked to ports and logistics networks may also acquire strategic value over time. Facilities developed for commercial purposes can sometimes support dual-use activities, including logistics support for maritime operations.

In the broader context of the Indian Ocean region, the development of industrial and logistical infrastructure around ports such as Gwadar could eventually contribute to a stronger Chinese presence in regional trade and maritime networks.

**An Uncertain Future**  
Despite ambitious announcements, the success of CPEC Phase II is far from guaranteed.

Pakistan's economic constraints, institutional bottlenecks and security challenges remain significant obstacles. Many of the newly approved SEZs may take years to become operational, if they develop at all.

The more realistic outcome may be a smaller number of successful zones rather than a nationwide industrial transformation.

Even so, the strategic direction is clear. The second phase of CPEC seeks to move beyond the construction of roads and power plants towards the creation of industrial clusters closely linked to Chinese production systems.

If even a handful of these zones become viable manufacturing hubs, they could anchor Chinese firms, technologies and supply chains within Pakistan's economy for decades.

**A Corridor Becoming an Ecosystem**  
The evolution of CPEC from infrastructure corridor to industrial ecosystem represents a new stage in the China-Pakistan partnership.

For Pakistan, the promise lies in industrial growth, employment opportunities and export expansion. For China, it offers a pathway to extend its manufacturing networks beyond its borders while strengthening a key strategic partnership.

For the region, including India, the transformation carries geopolitical implications that will unfold gradually over time.

The real question is not whether all forty-four proposed SEZs will materialise. Rather, it is whether a select few will succeed in creating sustainable industrial ecosystems.

If they do, CPEC will cease to be merely a network of highways and power stations. It will become something far more consequential — a deeply embedded economic architecture shaping the strategic landscape of South Asia for years to come.