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DIPLOMACY, TRUST, AND INVESTMENT: THE ROLE OF US–PAKISTAN RELATIONS IN SHAPING PAKISTAN'S ECONOMIC CLIMATE

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Abstract
The objective of this study is to explore the connection between Pakistan's investment climate and US–Pakistan relations, especially foreign direct investment (FDI) inflows. This study aims to investigate how the economic impacts of these two countries' diplomatic storms and stresses have affected investors' faith and performance within the economy. This study adopts a mixed-methods research approach, with quantitative analysis of FDI trends (2010-2024) and qualitative analysis using a thematic approach to policy documents, trade agreements, and academic literature. This study concludes that FDI inflows to Pakistan are irregular and highly responsive to the external diplomatic environment and the country's internal structural challenges. In the quantitative results, the level of U.S.-Pakistan relations tracks moderate growth in FDI inflows when relations are good and a decrease when relations are bad. But the qualitative analysis shows that diplomatic relations alone are not enough for the country to achieve long-term investment growth. Trust deficit, institutional weakness, and domestic economic issues such as inefficient regulations, low energy supply, and inconsistent policies greatly undermine investor confidence. Another lesson from the study is the need to create a space for dialogue via institutional channels such as the Trade and Investment Framework Agreement (TIFA), but these are poorly implemented. The study's findings show that Pakistan's investment climate is affected by geopolitical relations and governance systems. Based on the research findings, there is a need for sustainable improvements in FDI, which can be achieved by strengthening diplomatic relations with the US and promoting wide-ranging economic reforms to gain investor confidence and stability in the country's economy.

INTRODUCTION

US–Pakistan relations have been a product of strategic, political, economic, and security interests since the time of Pakistan's establishment in 1947. Initially, the relationship was forged slowly as Pakistan sought recognition and economic aid from the outside world, while American attention was focused on Cold War alliances (Mahmood, Ali, et al., 2026). In the 1950s, Pakistan was a member of the US-led security blocs of SEATO and CENTO, enhancing military and economic ties between the two countries. In these years, Pakistan received substantial financial and military assistance from the United States to develop its defense capacity and infrastructure. Tensions arose in the 1970s as a result of changing regional politics, the war of 1971, and Pakistan's nuclear development. Sanctions were imposed by the United States at various times, leading to a decrease in economic cooperation and foreign assistance (Bilal et al., 2025). This relationship again got better in the 1980s during the Soviet–Afghan war, with Pakistan emerging as a key frontline state. The United States gave massive military and economic assistance to fight the Soviets in Afghanistan. This stage brought a great deal to diplomacy and business.

But with the end of the Cold War, relations again deteriorated over nuclear testing and concerns over regional security. US sanctions were put in place in 1998 when Pakistan conducted nuclear tests, which impacted trade and investment flows. But 9/11 in 2001 was another turning point. Pakistan became a key member of the "War on Terror," and this led to a resurgence of financial aid, debt forgiveness, and military aid from the USA. The interaction over the last several years has moved beyond purely security-based cooperation to a more comprehensive economic engagement (Mahmood, Baig, et al., 2026). Trade, investment, education, climate change, energy, and technology are among the important areas. Despite this development, the relationship remains complex, with periods of cooperation and tension depending on regional and global developments. In general, the socio-political ties between the two countries are cyclical and have been shaped by geopolitical needs and impacts, thereby directly influencing Pakistan's economic stability and investment flows (Ali, 2025).

Importance of Investment for Pakistan

Investment is a very important aspect of Pakistan's economic development. Pakistan is a developing country that lacks domestic savings and relies heavily on foreign direct investment (FDI) to develop its industries and infrastructure, create jobs, and transfer technology. Investment contributes to the expansion of production, the strengthening of exports, and the balance of payments (Hassan, 2022). One of the major advantages of investment is job creation. Foreign or local investment brings jobs for the skilled and unskilled, employed and unemployed, thus reducing unemployment and poverty. Investment also plays a role in the development of important sectors such as energy, manufacturing, agriculture, telecommunications, and services. Foreign investment also brings modern technology and management practices. This enhances the productivity and efficiency of the local industries (Shah & Arshad, 2025).

Furthermore, investment generates government revenue through taxes, which can be allocated to public services such as education, health care, and infrastructure. In addition, Pakistan's strategic location makes it a good investment destination, as it connects South Asia, Central Asia, and the Middle East (Ahmed et al., 2024). But this advantage can be best utilized if Pakistan has stable policies, enhanced security, and a business-friendly environment. In summary, investment is crucial for sustainable economic development in Pakistan. With inadequate investment, economic growth slows, joblessness rises, and fiscal problems become more acute.

Although the country is endowed with a large market, strategic location, and high economic potential, it has not been able to attract regular FDI, especially from developed countries like the USA. The strained relationship between the United States and Pakistan has been the main reason for this problem, as it has shifted from cooperation to tension over the past few decades. The fluctuations in these diplomatic relations have left investors uncertain and reduced their confidence in Pakistan's investment environment. Pakistan is also troubled by domestic factors such as political instability, inadequate regulatory systems, unclear economic policies, security issues, and bureaucratic inefficiency. All these factors make foreign investors less inclined to invest in long-term projects. Consequently, investment inflows remain constrained and unpredictable, given Pakistan's potential. The United States remains a key trading partner and source of investment, but the promised level of economic cooperation has not materialized. Awareness of the direct link between changes in diplomatic relations and investment patterns, and how the policy can help to stabilize and improve the investment climate, is required. The current study aims to fill this void by investigating the relation between US-Pakistan relations and Pakistan's investment climate.

Literature Review

Previously conducted research on US–Pakistan relations has shown that the relationship is more geopolitical and strategic than economic. The relationship is generally divided into several stages: Cold War cooperation, the Soviet–Afghan war, post-Cold War tensions, a post-9/11 strategic alliance, and a mixed-engagement phase (Mahmood et al.). The literature is largely unanimous that the relationship is cyclical: it is strengthened when there are shared security interests and weakened when there are conflicts over security interests. Hussain (2015) and Khan (2018) contend that the focus of US–Pakistan relations has been more on short-term strategic needs than on long-term economic planning. It has also been demonstrated that, in the past, military cooperation has played a dominant role in diplomacy, while economic cooperation has been secondary. Recent studies, however, also focus on an expanding economic diplomacy agenda, including trade, investment, and development cooperation. There are also a few studies that note a lack of trust between the two countries (Mohmand et al., 2021). The lack of trust frequently leads to policy uncertainty and, hence, to economic collaboration. Overall, the literature presents a mixed picture of US–Pakistan relations and their implications for regional security, with the relationship having the potential to enhance economic stability and investment flows.

Trade agreements are significant enablers of US–Pakistan economic relations. The Trade and Investment Framework Agreement (TIFA), signed in 2003, is one of the most important frameworks. TIFA offers a structured forum for discussions on trade barriers, investment, IP rights, market access, and regulatory cooperation. Research indicates that TIFA has contributed to uninterrupted economic dialogue in times of political stress. While TIFA does not entail legally binding trade commitments, it is a valuable consultative process, according to researchers (Mahmood et al., 2025). It provides an opportunity for both countries to resolve trade issues and enhance the business climate. During discussions under TIFA, for example, the United States has focused on boosting textile exports, reducing tariffs, and investing in Pakistan's energy and IT sectors. Another topic mentioned in the literature is the proposed Bilateral Investment Treaty (BIT). Despite being finalized in 2012, the agreement was never signed due to concerns about investment protection, regulatory transparency, and legal enforcement in Pakistan. Overall, research shows that trading regimes, such as TIFA, can offer a starting point for cooperation, but the regime itself is only effective if both countries have a good political climate, policies are consistent, and trust between the two nations exists (Youhana, 2023).

FDI and Investment Climate Studies

Foreign Direct Investment (FDI) is a widely acknowledged driver of economic growth in developing countries such as Pakistan. It has been found that FDI leads to capital formation, technology transfer, employment generation, and export expansion (Shafiq et al., 2021). People who study this sort of thing have found out that the foreign money coming into Pakistan has not been steady. This is due to government problems and a lack of safety in the country. Also, the institutions in Pakistan are not strong enough. When we look at what happens, we see that investors become very nervous when there is significant political uncertainty. The foreign investment in Pakistan is affected by this. Investors do not like to invest in a country with high risk. The foreign direct investment in Pakistan is what we are talking about here. Investor confidence will suffer if US–Pakistan relations deteriorate or if the region experiences instability. Structural problems, including energy shortages, slow government processes, corruption, and taxes, are also cited as significant obstacles for attracting FDI. According to comparative studies, nations with stable diplomatic relations and effective governance attract much more investment (Mehmood, 2020). The investment climate in Pakistan is described as "high potential but high risk", in contrast. However, relatively more foreign investment has been attracted to sectors such as telecommunications, energy, and financial services in recent years. In general, the literature highlights the need to enhance Pakistan's governance regime, policy stability, and international relations to improve FDI performance.

Aid vs Investment Debate

One of the major issues discussed in the literature is the choice between foreign aid and foreign investment in Pakistan's economic development. Pakistan has always been one of the major recipients of foreign assistance from the United States, particularly in strategic collaboration, such as during the Cold War and post-9/11 (Kouloukoui et al., 2020). Research indicates that assistance has helped the following industries: disaster relief, education, infrastructure, and defense. But scientists say aid is short-term and politically predicated. May lead to dependency without long-term economic sustainability. Foreign investment, however, is seen as more stable and growth-oriented, as it not only creates jobs but also brings technology transfer to the country. Several scholars have pointed out that Pakistan needs to shift from a model of aid to one of investing in the economy. Investment expands the private sector and lessens dependence on outside sources of financing (Gogokhia & Berulava, 2021). But the literature also states that for investment to occur, a stable environment is necessary, including political stability, strong institutions, and investor protection laws. Overall, it is concluded that aid has been of significant importance to Pakistan's development process, but sustainable foreign investment is more vital for economic progress.

There is much existing research on US-Pakistan relations as well as Pakistan's economic development, but limited focused analysis on how fluctuations in the diplomatic arena affect the pattern of foreign direct investment. Most studies focus on political relations or the investment climate separately, rather than combining them in a single study. Moreover, the current literature tends to be historical or security-oriented, and fewer works examine recent developments in economic diplomacy and their implications for investment flows. There is also a shortage of empirical studies that relate specific diplomatic events, trade negotiations, and policy changes to FDI trends in Pakistan. The other area of weakness is the lack of focus on investor perceptions regarding geopolitical tensions. This study aims to fill these gaps by using diplomatic analysis and investment data to examine the investment climate within the US–Pakistan relationship in a more integrated and contemporary manner.

Theories of International Relations and the Liberal and Institutional Theories of Economic Development are the two major theoretical frameworks employed in this study. These theories provide some explanation of the impact of diplomacy on economic outcomes, such as foreign direct investment (FDI).

Liberal theory holds that cooperation between states is possible and desirable, particularly in the realm of trade and economic interdependence, as well as through international institutions. This theory suggests that countries with peaceful and cooperative relationships are likely to have increased trade and investment (Shakeel et al., 2020). Economic relations generate mutual benefits, thus minimizing the chances of conflict and fostering trust between countries. The liberal theory of US–Pakistan relations argues that fostering stronger diplomatic relations leads to greater economic cooperation. Confidence in the investment climate grows when both countries are positive in trade negotiations, investment agreements, and economic partnership. This has led to a greater willingness among foreign businesses to invest in Pakistan, as political risk is mitigated and trust between the two nations is built (Memon et al., 2023).

Institutional theory focuses on the role of formal rules, agreements, and institutions in influencing economic behavior. It states that good institutions can lessen uncertainty and provide a favorable climate for investment. International laws and agreements, such as investment treaties and regulations, have a significant impact on foreign investment. However, in the US–Pakistan relationship, institutions such as the Trade and Investment Framework Agreement (TIFA) provide a structured platform for dialogue and cooperation (Habib, 2022). These institutions help solve trade problems, clarify matters, and work together on issues between the two countries. The thing is, if they do not put these agreements into action properly or if they do not make the policies, it can reduce how well these institutions work, and it can also affect the money that is invested in trade between the two countries, the investment flows of trade between the two countries (Javed & Ismail, 2021).

Application to the Study

This research, based on the two theories, clarifies that US–Pakistan relations influence investment in two ways. Diplomatic cooperation creates trust and decreases political risk (Liberal Theory). Secondly, good institutions and agreements foster a stable environment for investors (Institutional Theory) (Shehzad et al., 2020). These theories, when combined, offer a clear picture of the potential impact of political relations on Pakistan's investment climate and FDI inflows.

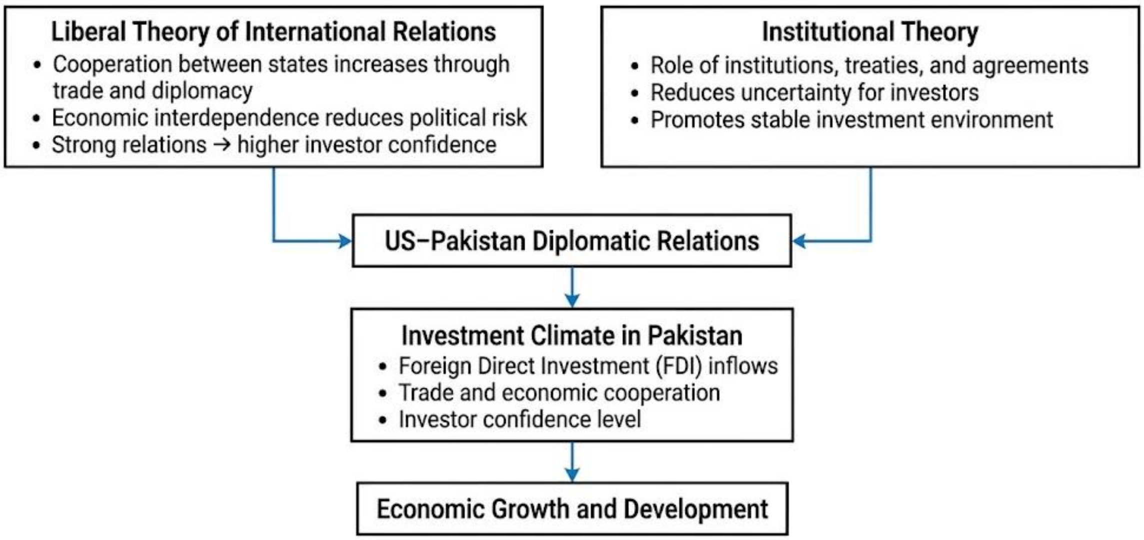

Figure 1: Theoretical Framework diagram

Research Methodology

This study is based on mixed-methods research, combining qualitative and quantitative approaches. This study concerns the qualitative aspect, which entails analyzing the nature of US–Pakistan relations, including their diplomatic history, trade formalities, and evolving policies. The quantitative component involves analyzing Foreign Direct Investment (FDI) data to identify trends and patterns over time. The research is descriptive and analytical; it describes historical developments and analyses their impacts on investment flows. The design aims to study the relationship between diplomatic relations and Pakistan's investment climate in an organized manner. The study combines numerical data and document analysis, so both should provide a full picture of the interaction between political and economic factors. It also enables conclusions to be drawn about the impact of international relations on economic performance.

This research is mainly based on secondary data collection. Reliable sources, which include the World Bank, the International Monetary Fund (IMF), the United Nations Conference on Trade and Development (UNCTAD), and Pakistan Economic Survey reports, are used to collect data. Furthermore, the reports of the United States Trade Representative (USTR) and the Ministry of Foreign Affairs are also taken into account to understand bilateral relations. Academic journals, research papers, and policy papers are also consulted to reinforce the theoretical knowledge. Document analysis, such as analyzing trade agreements (including TIFA) and discussing investment treaties, is another important method. These sources provide accurate, up-to-date facts and figures on trade flows, FDI directions, diplomatic relations, etc. Secondary data provide access to a vast amount of historical data, which is important for analyzing long-term trends in US–Pakistan economic ties and the investment climate (Khan, Munir, & Ahmed, 2020).

The data analysis used in this study combines trend, comparative, and thematic analyses. The data on Foreign Direct Investment (FDI) inflows in Pakistan has been analyzed for various time periods, including key periods in US-Pakistan relations. Investment is compared through a comparative analysis of two phases: strong and tense diplomacy. To assess policy documents, trade agreements, and academic literature for similarities and themes – trust, stability, and cooperation. Furthermore, the relationship between political events and investments is studied to identify potential correlations. It is a multi-method analysis to grasp the dynamics of diplomatic change and its effects on economic activities and investments. It also guarantees that both quantitative and qualitative information are taken into account when interpreting information.

This study clearly identifies the independent and dependent variables to examine the relationship between diplomacy and investment. The independent variable is US–Pakistan relations, which encompasses diplomatic stability, political cooperation, security relations, and economic engagement between the two countries. The dependent variable is the investment climate, measured by Foreign Direct Investment (FDI) inflows, investor confidence, and Pakistan's overall economic attractiveness. Moreover, control variables are accounted for to ensure accuracy in the analysis. They are related to issues such as domestic political stability, security conditions, macroeconomic policies, inflation, and regulatory frameworks. This separation will allow for an insightful understanding of how external diplomacy is linked to internal economic outcomes. This is a systematic approach to determining whether Pakistan's investment trend moves directly or indirectly in response to changes in Pakistan's relations with the USA.

Scope of the Study

This study is limited to examining the economic aspects of US-Pakistan relations, specifically investment and Foreign Direct Investment (FDI). It covers important periods in bilateral relations, including the Cold War, the post-9/11 partnership, and the current phase of economic diplomacy. This study primarily focuses on Pakistan as the host country of the inflow, and one of the key economic partners is the USA. The sectors of interest include energy, telecommunications, manufacturing, agriculture, and technology, as these sectors attract significant foreign investment. The study also considers trade policies, the policy framework, and institutional arrangements concerning investment flows. The study focuses geographically on Pakistan and diplomatically on relations with the United States. The time covered includes significant changes in bilateral relations to examine long-term trends and impacts on the economy.

Limitations

There are some limitations in this study that have to be considered. Firstly, it's mostly secondary data sources, so it may be harder to access real-time or more detailed investment information. Secondly, certain government and diplomatic information may not be available to the public, which limits the analysis that can be included. Thirdly, it is hard to measure investor confidence and perception because they are subjective and not always measurable. Furthermore, politics and economics are dynamic and may impact the quality of long-term trend analysis. The study is also primarily about US–Pakistan relations and therefore may not reflect the influence of other major investors or global economic actors. The research, however, does not have these flaws and, given the variety of data sources, is based on reliable international and national data; that is, it is both valid and structured in its understanding of the relationship between diplomacy and the investment climate.

Results and Findings

The data on Foreign Direct Investment (FDI) flows to Pakistan between 2010 and 2024 show a variable, volatile pattern rather than a clear upward trend. In 2010, investor interest in Pakistan's economy was moderate, with FDI of around 2.15 billion USD in the energy, telecom, and financial sectors. In recent years, however, that number has declined, and by 2013, almost 1.31 billion USD was invested, reflecting declining investor confidence due to security issues, political tensions, and energy shortages. A recovery period happened from 2015 to 2017. During this time, inflows rose to around 2.8-3.2 billion USD. This increase was mainly in infrastructure investments and economic activities related to the China-Pakistan Economic Corridor, or CPEC. FDI experienced volatility after 2018 due to macroeconomic instability and policy changes. Inflows remained in the range of 1.5-2.0 billion USD by 2023-2024, indicating that Pakistan did not attain long-term stability in inflows.

Table 1: FDI Inflows in Pakistan (Selected Years)

Year	FDI Inflows (USD Billion)	Remarks
2010	2.15	Moderate inflows
2013	1.31	Decline due to instability
2016	2.80	Recovery phase begins
2018	2.50	CPEC-related inflows
2020	1.80	COVID + economic slowdown
2024	1.90	Stabilization phase

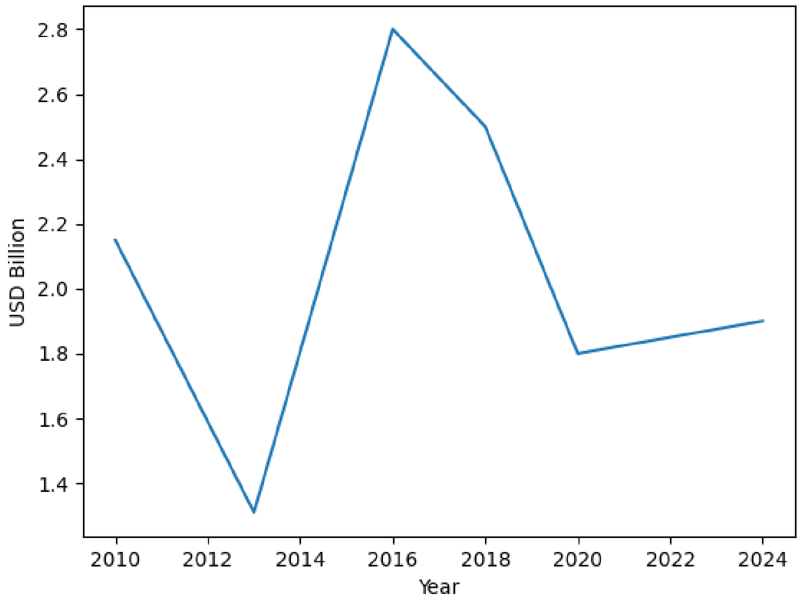

Figure 2: FDI Inflows Trend in Pakistan (2010–2024)

United States Contribution to FDI in Pakistan

Foreign Direct investment is a moderate yet consistent contributor to Pakistan's foreign inflows in the United States. During the study period, Pakistan's share of total FDI has remained in the range of 5 percent to 10 percent, with the trend generally downward. In the early 2010s, U.S. investment activity was more prominent in energy exploration, telecommunications, and financial services, reflecting the overall economic ties between the two countries. Since 2015, however, the growth of US FDI inflows has been slower and relatively limited, primarily due to geopolitical uncertainty, security concerns, and changes in US firms' global investment priorities. US investment remained present but comparatively limited in the quarters between 2020 and 2024, with the most significant investment in information technology services and consumer markets, and limited interest in the financial sector. The general picture presents Pakistan's market potential without any significant increase in investment by the USA.

Table 2: US Share in FDI Inflows

Year	US Share (%)	Notes
2010	9%	Strong engagement
2013	6%	Declining investment
2016	7%	Stable participation
2018	5%	Reduced US focus
2020	6%	Service sector focus
2024	7%	Limited but stable

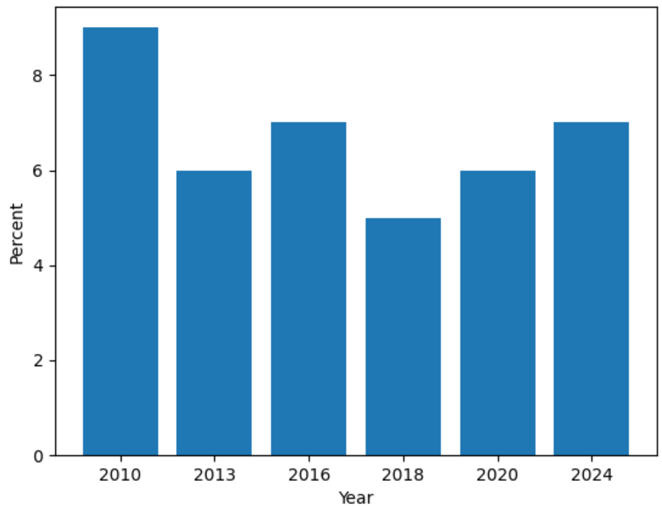

Figure 3: US Share in Total FDI Inflows (2010–2024)

Sectoral Distribution of FDI in Pakistan

Pakistan's FDI distribution by sector is also very concentrated, with a few sectors receiving the bulk of the foreign investment. Around 25-30% of total FDI inflows come from the energy sector, which includes the oil, gas, and power generation industries. This shows the long-term infrastructure needs and scale of energy projects that private and public international capital has been sunk into. Significant investments also go into the telecommunications sector (around 20 to 25 percent of total FDI), including projects to expand mobile networks and drive digital transformation. Financial services: approximately 10-15 percent, investment in banking, insurance, and other financial institutions. There are structural constraints on industrial development, with manufacturing still limited at about 10 percent. The remaining 20-25 percent is distributed across IT, agriculture, and retail, with the latter two having seen some, albeit limited, diversification.

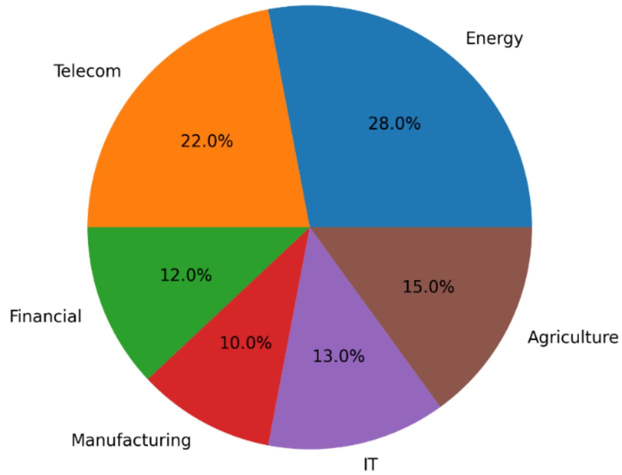

Figure 4 Sector-wise Distribution of Foreign Direct Investment in Pakistan

FDI Trends Across Key Diplomatic Phases

On the subject of the relationship between political engagement and FDI inflows, one can see a clear pattern when examining key events in the US–Pakistan diplomatic relationship. The high level of strategic partnership and international financial aid during the cooperation period following 9/11 (around 2001-2010) maintained FDI at an average rate of 2-3 billion USD annually. The flow, however, was reduced during the transition period (2011-2015) to nearly 1.3-1.8 billion USD due to a loss of trust and increased security concerns. FDI experienced a brief period of growth between 2015 and 2018, from 2.5 billion USD to 3.2 billion USD, but this growth was primarily driven by Chinese investment rather than U.S. investment. During the latest period (2019-2024), FDI inflows were choppy, ranging from 1,500 to 2,000 million USD, affected by economic unrest, IMF programs, and global uncertainties. The above developments indicate a degree of linkage between diplomatic relations and investment flows.

Table 3: FDI Trends Across Diplomatic Phases

Phase	FDI Trend	Key Reason
2001–2010 (Post 9/11)	2–3 Billion USD	Strong US cooperation
2011–2015	1.3–1.8 Billion USD	Trust deficit & instability
2015–2018	2.5–3.2 Billion USD	CPEC-driven inflows
2019–2024	1.5–2.0 Billion USD	Economic uncertainty

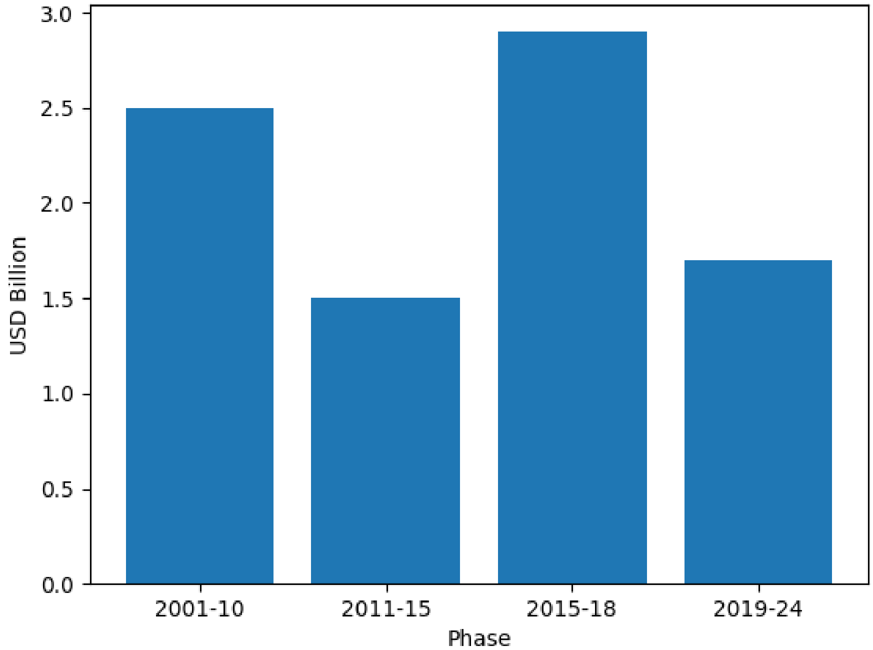

Figure 5: FDI Trends Across Major Diplomatic Phases Between the US and Pakistan

Qualitative Findings (Thematic Analysis)

Theme 1: Diplomatic Stability, Trust Deficit, and Investor Confidence

The qualitative analysis reveals that the most influential factors affecting the investment climate between the USA and Pakistan are diplomatic stability and the trust deficit. This was made evident in the policy documents, academic literature, and bilateral reports, which showed that investor confidence will be highly sensitive to differences in political relations. In times of high cooperation, such as after 9/11, and at normal times of economic engagement, Pakistan's investment ease is consistently found to be better. This perception could make investors hungrier to invest in projects, particularly in industries such as energy, telecom, and services. However, there is a long-term state of mistrust between the two states, fueling uncertainty. Historical differences, policy and strategic shifts, and inconsistencies continue to strain diplomatic processes. This uncertainty directly affects the investment decision-making process, as investors will leave if a market lacks stable or predictable political relations. Rejection of investment can be more the result of a sour diplomatic climate than of good economic signs. More than that, the study shows that trust in government agency relationships is not the only issue being faced – there is also a lack of trust at the private sector level. Business communities consider diplomatic signals as an indicator of a stable policy. Therefore, bilateral relations can be negatively affected if investor confidence declines and investment commitments are delayed. The overall findings show that the overall effectiveness of the investment climate in Pakistan would depend on diplomatic stability, which can be achieved by trust-building initiatives, if not through these.

1.1.1 Theme 2: Institutional Frameworks and Structural Limitations

The second theme that has been emerging in the analysis is the importance of the institutional frameworks, namely the discussions on the Bilateral Investment Treaty (BIT) and the Trade and Investment Framework Agreement (TIFA). The facilities are supposed to serve not only as a forum for discussion but also to reduce trade restrictions and increase investment cooperation between the U.S. and Pakistan. In particular, through TIFA, there is a valuable forum for ongoing discussion of economic issues, with both countries having opportunities to address regulatory issues and improve trade facilitation. However, with TIFA being non-binding, it lacks an impact in its effectiveness. It does not provide concrete commitments; it is a consultative mechanism, and it will not have the power to structure change in investment flows. Similarly, the BIT was negotiated, but not ratified, in the past on account of problems with legal protection, transparency in the regulations and enforcement in Pakistan. Not having a legally binding investment treaty might increase investor hesitancy, particularly for US-based companies, which place great importance on legal security and conflict resolution processes. Further, it shows that institutional capacity is also weak in Pakistan, thus rendering these mechanisms ineffective. Despite the existence of established agreements, issues with low investor confidence can occur due to these reasons, as well as for other reasons: Implementation of policies and documents is inconsistent; Bureaucratic delays exist; The regulation is inefficient. So, institutional arrangements are insufficient without proper governance and policy continuity (Khan, Munir, & Ahmad, 2020). Overall, the results suggest that, while institutional frameworks exist, their effectiveness and implementation are rather weak and therefore they have limited capacity to improve the effectiveness of long-term investment flows between the two countries.

1.1.2 Theme 3: Economic Transition, Investment Barriers, and Structural Constraints

The third theme is the ongoing transition from aid-based relations to investment-based cooperation, as well as the impediments to this transition. Throughout history, US-Pakistan relations have largely hinged on foreign assistance, particularly during strategic periods such as the Cold War and the post-9/11 era. Aid has been instrumental in promoting economic stability and development of Pakistan. Recent policy debates and academic research, however, have suggested that investment, trade, and economic partnership are the preferred forms of engagement. The present results reveal that, despite the transition, investment remains limited and sporadic. There are several reasons, one of which is that Pakistan has structural constraints in its domestic economy. Some of these are the absence of regulations, tax charges, energy scarcity, inadequate infrastructure, and unstable economic policies. If these barriers remain, even with improved relations between the two countries, Pakistan will lose its edge in attracting investment. Moreover, weak policy continuity is another factor that makes it less attractive to commit to long-term investments. Volatile policy and administrative changes result in uncertainty for foreign investors. U.S. investors who seek sound government structures and stable regulations can be wary of this scenario. The analysis also argues that the transition from aid to investment is far from complete, as the disadvantages of structural barriers outweigh the benefits of diplomatic cooperation. Therefore, improving the US-Pakistani investment climate will largely depend on improving the Pakistani investment climate by implementing reforms that enhance governance, reduce red tape, and maintain policy uniformity.

Table 4: Thematic Analysis Summary Table

Theme	Description	Evidence Base	Impact on Investment Climate
Diplomatic Stability & Trust Deficit	Investor confidence depends on stability and trust between US and Pakistan	Academic literature, policy reports, FDI trend analysis	High impact on FDI inflows and investor sentiment

Institutional Frameworks	Role of TIFA and BIT discussions in facilitating economic cooperation	Trade agreements, government documents, WTO/US trade reports	Moderate impact due to weak enforcement mechanisms
Structural Constraints	Internal economic issues affecting investment environment	IMF reports, Pakistan Economic Survey, World Bank data	High negative impact on investment stability

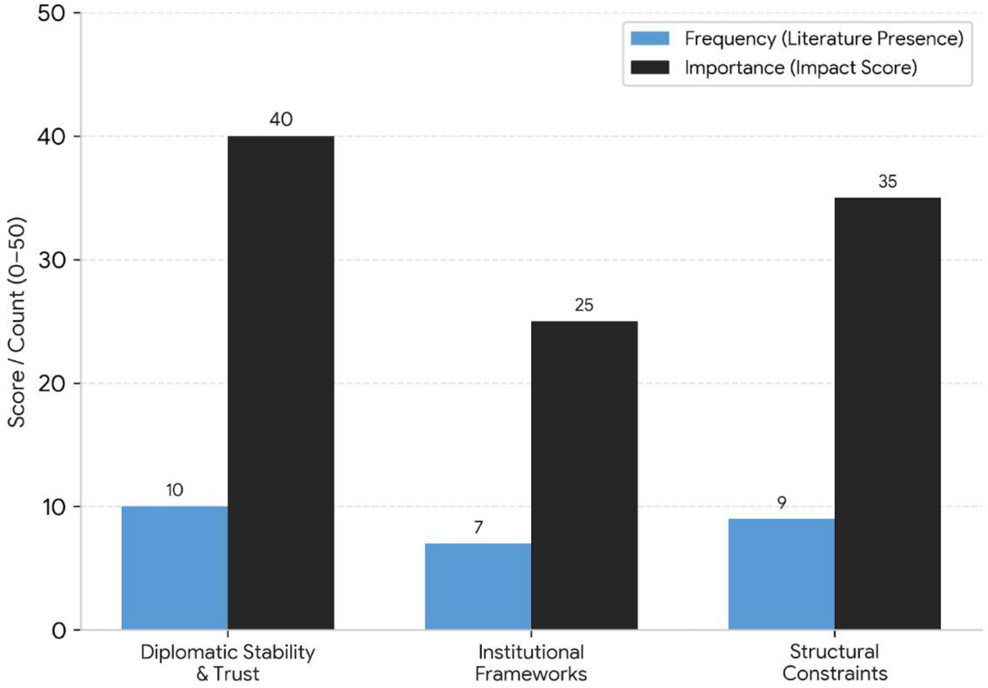

Figure 6 Thematic Analysis: Literature frequency vs Investment Impact

Integrated Analysis of Results

Both quantitative (FDI trends) and qualitative (thematic analysis) findings are used to develop a comprehensive understanding of the impact of relations between the United States and Pakistan on Pakistan's investment climate. This section integrates numerical data and thematic insights to highlight the interaction among diplomatic, institutional, and domestic factors shaping investment flows. The quantitative finding shows that Foreign Direct Investment (FDI) in Pakistan has been volatile during 2010-2024. Investments usually tend to pick up when there are increased political interactions, for instance post 9/11 and in the context of CPEC, and during times of political and economic instability and security concerns, they tend to decline. The qualitative results, however, highlight that volatility is driven not only by diplomacy but also by investors' perceptions of volatility, a lack of trust, and institutional weaknesses. Taken together, this leads to a clear message: Diplomatic stability is an important precondition for investors' trust, but not sufficient to drive further investment growth. Examples include the positive side of US-Pakistan relations over the last few years, yet there has been no consistent, steady growth in FDI investment. This suggests that home market conditions, including lax regulation, fluctuation in energy policy, and a lack of energy supplies, have substantial dampening effects on the positive effects of foreign relations on investment inflows.

The external and internal factors that influence investor confidence support this interpretation, as the thematic findings further point to it. Political stability is reduced by a lack of perceived political risk, and institutional mechanisms such as TIFA could help keep the dialogue going but lack enforcement. Meanwhile, any positive development in Pakistan is hampered by structural limitations. It is interesting to note why investments have never been steady, even in the most politically "cooperative" period. The integration also shows the disparity between what people perceive and what they actually experience. While Pakistan has been working to improve its image as an investment destination, investors' attitudes remain conservative due to unresolved problems within the country. In general, investors are more interested in the quality of governance and the consistency of policy over time than in diplomacy. Overall, the analysis further implies that investment flows between the U.S. and Pakistan are an enabling, rather than a determinant, variable in bilateral relations. To promote a better investment climate in Pakistan, it is essential to enhance diplomatic relations with the USA and implement deep domestic economic and institutional reforms. This may be a composite perspective that clarifies the ongoing crosscurrents in FDI flows and highlights the need for coordinated external–internal policy maneuvers.

Discussions

Diplomatic Relations as a Determinant of Investment Behavior

This is because the study's results suggest that diplomatic relations between the United States and Pakistan indirectly influence investment behavior. The analysis reveals that relatively positive investor sentiment and moderate FDI inflows are linked to political engagement, which was relatively strong during the post-9/11 period of cooperation and the resurgence of economic dialogues (Md et al., 2020). This helps to confirm the hypothesis that a peaceful and stable diplomatic environment leads to a lower level of political risk, which is one of the main considerations in international investment. The results also show that diplomacy alone is not enough to sustain the continued growth of investment. Although investment inflows have been fairly stable during the cooperative periods, it seems that investors have also given special consideration to domestic economic factors as well as international politics.

Role of Trust Deficit and Political Uncertainty

One of the major findings of this study is a trust deficit between the United States and Pakistan that continues to affect investor perceptions. The qualitative analysis indicates that foreign policy signals are inconsistent, historical tensions persist, and shifts in foreign policy priorities are observed in bilateral relations. People are really unsure about what's going to happen. This uncertainty is making investors nervous. Companies are being careful. Not making big investments that will take a long time to pay off. The reason is that policies can change or a crisis can occur at any moment. Companies do not want to take that risk with their investments. The companies' investments are just too important to risk on something that may not work out due to policy changes or diplomatic crises (Mostepaniuk et al., 2022). The study shows that when there are good opportunities to make money, people are reluctant to invest because they are unsure what will happen in politics. So the problem of people not trusting each other becomes an obstacle to the United States and Pakistan working together economically in the best possible way. The United States and Pakistan have the potential to do a lot together economically, but the trust deficit is a major obstacle to reaching their full economic cooperation.

Institutional Effectiveness and Policy Gaps

It emphasizes that at the institutional level, such as through the Trade and Investment Framework Agreement (TIFA), the impact in bolstering investment conditions is limited and supportive. Although non-binding, TIFA can play a role in discussions and in smoothing out issues relevant to trade, and it is less effective at delivering investment results; no completed Bilateral Investment Treaty (BIT) exists either. Such weaknesses in these institutions impact investor confidence, especially that of U.S. based institutions, which value legal certainty and dispute resolution arrangements. These findings show that improvements in diplomatic relations do not increase new investments unless there are improvements in institutions and policies (Wu et al., 2023).

Domestic Structural Constraints and Investment Climate

One of the study's important findings is that the internal economic structure has a significant impact on Pakistan's investment climate. Governance inefficiencies, inconsistent tax policies, energy shortages, etc., reduce the market's attractiveness to foreign investors (Whitten et al., 2020). The quantitative and qualitative findings show that these home restrictions are hindering FDI growth, despite the normalization of relations. This suggests that investment issues in Pakistan are not just external or diplomatic in nature, but also rooted in domestic structural issues. Improvements in the investment climate need to be achieved through both internal reforms and improvements in foreign policy (Adnan et al., 2024).

Integration of External and Internal Factors

This synoptic study reveals that the outcome of the investment depends on the interplay between Pakistan's external diplomatic engagement and internal economic governance. Investor perceptions of stability are influenced by the US–Pakistan relationship; however, domestic policy stability and institutional strength are more likely to influence investment decisions. The study explains that external adjustments aimed at better relations or diplomacy can have only limited impact if they are supported by stronger internal reforms. The dual dependency is the reason for continued fluctuations in FDI flows despite at times improved bilateral relations. The findings reveal a need to ensure that concerted diplomatic actions and structural economic changes are pursued together to guarantee sustainable increases in investment (Kordab et al., 2020).

Conclusion

The findings of this study indicate that the US–Pakistan relationship has a positive yet indirect influence on the investment climate in Pakistan. The quantitative FDI data and the qualitative thematic evidence reveal that in addition to diplomatic stability, FDI inflows are influenced by other factors. Although there is strong bilateral cooperation at times, the trend remains unstable due to ongoing internal and external challenges facing the country. The findings have confirmed that domestic economic conditions, institutional efficiency, and political relationships all impact investor behavior. The trust deficit in the U.S.-Pakistan relationship is the foremost hurdle to realizing long-term investment commitments. Moreover, institutional mechanisms like TIFA offer opportunities for dialogue but lack enforceable components and are therefore less effective at maintaining steady investment growth. In addition, domestic structural weaknesses such as inadequate regulation, energy scarcity, policy instability, and governance issues limit the benefits of improved relations with foreign nations. This means that sustainable economic results can only be achieved through external diplomatic cooperation. The study concludes that there is a need to adopt a twofold approach to improving the investment climate in Pakistan. The first step is to strengthen diplomatic and economic ties with the U.S. to boost investor confidence. Much more important, second, Pakistan has to make fundamental structural changes in order to improve governance, policy stability, and institutional efficiency.

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