Navigating the Post-Stabilization Crossroads

Pakistan's Economic Snapshot of July 2025

Federation of Pakistan Chamber of Commerce & Industry

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Date: 13th August 2025

Foreword

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As **Pakistan's foremost business voice**, the **Federation of Pakistan Chambers of Commerce and Industry (FPCCI)** remains steadfast in its mission to drive **business-friendly reforms** that promote **inclusive and sustainable growth**. By advocating for **clear policies**, forging **strong institutional partnerships**, and mobilizing **broad sectoral support**, FPCCI actively works to **stimulate trade**, **boost exports**, and **shape the nation's economic future**.

At the heart of FPCCI's advocacy is a firm commitment to **research-driven, evidence-based policy inputs**. The **Policy Advisory Board (PAB)** has emerged as a **credible and strategic arm** of the FPCCI — guiding internal policy dialogue while also extending **vital support to the Government** on matters of **trade, investment**, **taxation, energy, industrial policy, climate resilience, etc.**

Pakistan's economy stands at a **critical turning point**, facing **domestic and external challenges**. It is essential to **address economic risks** through **continuous reforms**, prudent management of **fiscal and monetary policies**, and proactive measures to **strengthen climate resilience**. These actions are not only necessary for **stability**, but also for building a **solid foundation** for **steady and inclusive growth**. The road ahead demands **meaningful reforms** to **boost productivity** and **reduce costs**. By taking these decisive steps, we can set Pakistan on a **clear path toward sustainable, long-term prosperity**.

The **FPCCI's Policy Advisory Board** has been actively engaged in broad-based consultative dialogues with stakeholders across Pakistan's business spectrum. Backed by a network of chambers and trade associations, it brings together diverse industry perspectives and plays a pivotal role in shaping **business-friendly policies** that foster sustainable economic growth.

This report, **"Pakistan Economic Report: Navigating the Post-Stabilization Crossroads"**, underscores that Pakistan's **modest economic recovery**, underpinned by prudent macroeconomic management, has achieved historic milestones — including record current account and primary surpluses. However, Pakistan's economy now stands at a **critical crossroads**. This recovery rests on a **fragile foundation**, with deep-rooted structural challenges that remain unresolved. The foremost challenge lies in **transforming these hard-earned macroeconomic gains into sustained, broad-based growth**.

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Executive Summary

In **FY25**, Pakistan achieved a **significant milestone** by recording its **largest current account surplus in 22 years**, driven by a sharp increase in **State Bank reserves** and **record-high remittances**. These developments strengthened the foundation for broader **macroeconomic stability**. Notably, the economy crossed the **$400 billion GDP mark for the first time**, reaching **$411 billion** in FY25 from **$372 billion** in FY24, breaking free from a long-standing **$300–$370 billion range**. **GDP growth** improved modestly to **2.68%** from **2.51%** last year, supported by **agriculture (0.56%)**, **industry (4.77%)**, and **services (2.91%)**, though still below the annual target of **3.6%**. **Average CPI inflation** fell sharply to **4.49%** in FY25 from **23.41%** in FY24, reflecting the combined effects of tighter monetary policy, fiscal discipline, and currency stability. A **historic primary surplus** and easing inflation enabled the **State Bank of Pakistan (SBP)** to cut the policy rate from **22% to 11%**, although private sector credit growth has yet to pick up. On the fiscal front, the **budget deficit** narrowed to **5.4% of GDP** (**Rs 6.17 trillion**) from **6.8%** last year, with revenue growth outpacing expenditure. The **primary balance** improved to **2.4% of GDP** from **0.9%** in FY24, underscoring improved fiscal discipline.

However, **risks to the macroeconomic outlook remain**. On **30 July 2025**, the SBP's **Monetary Policy Committee** kept the policy rate unchanged, citing emerging pressures such as **energy-driven inflation** from higher gas tariffs, the removal of temporary electricity subsidies, and rising fuel prices—all expected to increase household and production costs. **External fragility** persists due to **volatile global commodity prices**, climate-related risks, and **weaker export prices**, particularly for rice. The **trade deficit** is expected to widen as import demand rises and remittance growth slows, although the **current account deficit** is projected to stay within **0–1% of GDP** in FY26. Trade performance at the start of FY26 showed both promise and vulnerability. In **July 2025**, **exports** rose **16.9%** year-on-year to **$2.70 billion**, while **imports** surged **29.3%** to **$5.45 billion**, widening the trade deficit by **44.2%** to **$2.75 billion**. The sharp rise in imports—driven by **energy, raw materials, and industrial demand**—underscores Pakistan's **import-dependent growth model**, which leaves it exposed to external shocks. **Manufacturing's share of GDP** has declined to **18%** from **26%** in the 1990s, reflecting **structural weaknesses**. While large-scale manufacturing may see a short-term rebound, **sustained recovery** will require **deep reforms** to boost competitiveness and productivity rather than resorting to **import controls**.

Pakistan's **growth potential** continues to be constrained by **heavy reliance on imports**, **chronic difficulty in sustaining growth above 3–4%**, **rapid population growth** straining resources, and **high interest payments** consuming a large share of tax revenues. **Monetary policy alone** cannot deliver lasting recovery; instead, a **comprehensive 10-year industrial policy** is needed to promote **exports, entrepreneurship, and private sector–led industrialization**, alongside **tax reforms**, **energy sector efficiency**, and **infrastructure investment**. The government's **fiscal tightening** has achieved surplus targets but risks slowing the economy. Heavy reliance on **energy tariff hikes** rather than **structural reforms** may raise inflation and hurt **business competitiveness**. **Growth projections for FY26** reflect **cautious optimism**, with the **Planning Commission** forecasting **4.20%**, **SBP** projecting **3.25–4.25%**, **IMF** at **3.60%**, **World Bank** at **3.10%**, and **ADB** at **3.00%**. While growth is expected to improve, it will likely remain **modest** and contingent on **sustained macroeconomic stability** and **meaningful reforms** to unlock **higher, inclusive growth**.

1. The Macroeconomic Overview: A Fragile Stability

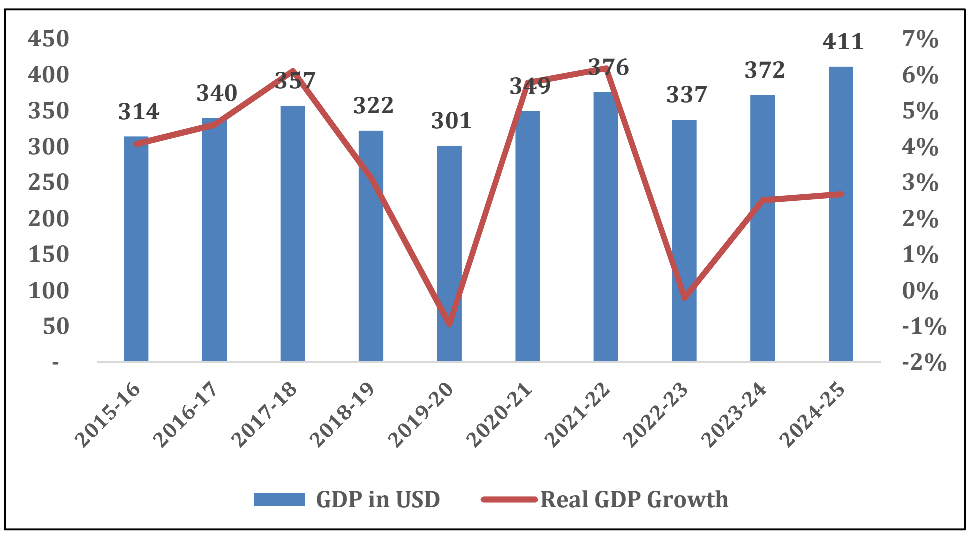
Pakistan's key challenge now is to **convert** recent **stabilization gains into sustainable, inclusive economic growth,** which is **essential** to **lifting living standards** and, in turn, **reducing poverty** — a pressing challenge given that **45% of Pakistan's population** still **lives** below the **poverty line**. This will require **high-impact reforms,** which include: **a) building a more efficient and progressive tax system, b) maintaining a market-determined exchange rate, c) lowering import tariffs to boost exports, d) improving the business climate, and streamlining the public sector**. This will require unwavering commitment from policymakers at both the federal and provincial levels, not just in announcing reforms, but in i**mplementing** them **consistently and transparently**. Such dedication would send a **clear signal** that Pakistan is serious about creating a stable, predictable policy environment. This, in turn, would strengthen investor confidence, attract both domestic and foreign capital, and lay a **solid foundation** for **sustained economic growth** in the years ahead.

According to the **World Bank**, Pakistan's **real GDP growth** is projected to rise to **3.1% in FY26 and 3.4% in FY27.** However, growth is likely to remain constrained in the near term due to tight monetary and fiscal policies aimed at rebuilding buffers and preventing macroeconomic imbalances. Moreover, significant downside risks remain, which could challenge this outlook.

1.1. Growth Trajectory: Tepid Recovery amidst Policy Constraints

In FY25, Pakistan reached a significant milestone, recording its **largest current account surplus in 22 years**, supported by a strong rise in State Bank **reserves** and record-breaking **remittances**. These achievements have helped lay the foundation for broader Macroeconomic Stability.

Figure 1: Pakistan's GDP crosses the $400 billion mark in FY25.

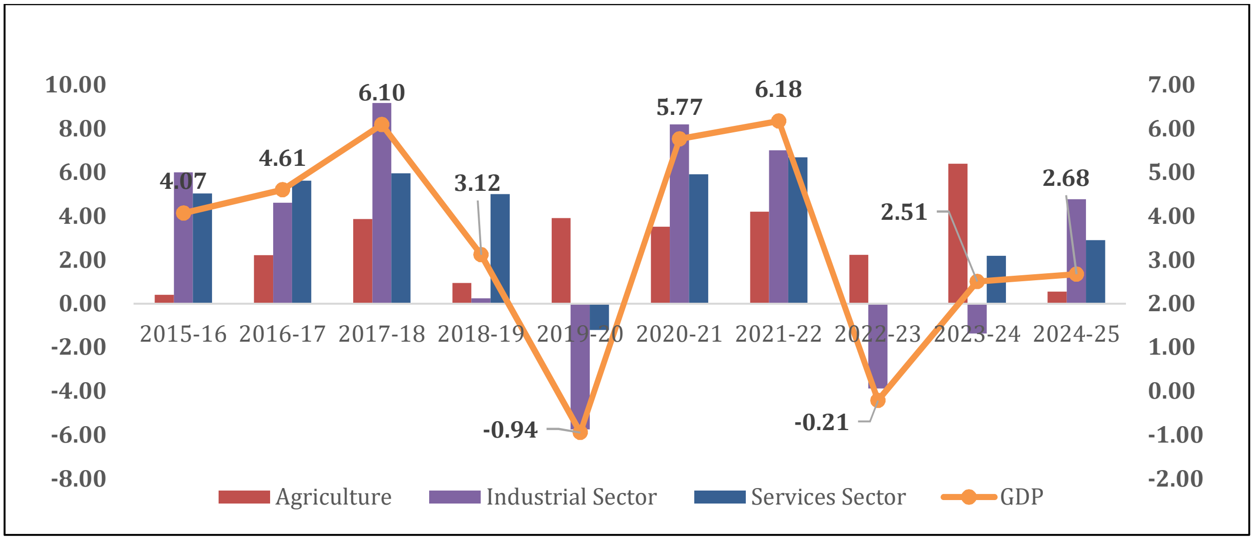


Source: PBS

Perhaps most notably, Pakistan's GDP has crossed the **$400 billion mark** for the first time, breaking the **$300–$370 billion range**, where it had **lingered** for many years. Pakistan's GDP skyrocketed to **$411** billion in FY25

With improvements visible on both external and fiscal fronts, recent trends point toward a **cautious** yet promising economic recovery, bringing a **renewed sense of optimism**. The economy grew by 2.68% this year, slightly higher than last year's 2.51% growth. The growth in the agriculture, industry & services sectors stood at 0.56%, 4.77% & 2.91% in FY25, respectively.

Figure 2: Real GDP growth & sector-wise (%)



Source: PBS

A closer look at 2024–25 reveals a mixed sectoral picture, highlighting resilience, offset by sluggish or uneven growth in others, shaping the year's overall economic trajectory.

a) **Agriculture**: The Agriculture Sector's share of the GDP stood at **23.54%** in 2024-25 (at constant prices). The agriculture sector grew by only **0.56%** compared to the **6.40%** last year. What's even more alarming is that Pakistan's agriculture sector grew by just 0.56% — its lowest growth rate in six years, since 2018-19. In the agriculture sector, *the production of major crops declined by **13.49%,** mainly due to lower yields of wheat by 8.91%, maize by 15.4%, rice by 1.38%, sugarcane by 3.88% & cotton by 30.7% respectively*. Meanwhile, minor crops delivered a solid performance, and the livestock, forestry, and fishing sectors also contributed positively, growing by 4.72%, 3.03%, and 1.42% respectively.

b) **Industrial Sector**: In 2024–25, the industrial sector accounted for **18.07%** of GDP and posted a growth rate of 4.77%, rebounding from a 1.37% contraction last year. However, the picture was mixed. Despite higher coal output, the mining and quarrying industry shrank by 3.38% due to sharp declines in natural gas production by 7.05%, crude oil by 14.72%, and other minerals. Manufacturing growth also slowed, easing to 1.34% from 3.03% a year earlier. Within the Manufacturing sector, large-scale manufacturing (LSM) production dropped by 1.53% during 2024-25. *It is interesting to note that although LSM, which accounts for over*

***70%** of the manufacturing sector, has **declined by 1.53%,** the **overall manufacturing growth** still shows a **positive increase of 1.34%** (So far, LSM growth contracted by 1.21% during Jul-May FY25 compared to the growth of 0.86% last year).*

c) **Services Sector:** Overall **growth in 2024–25 was largely driven by the services sector**, which expanded by **2.91%,** with all **10 of its key components contributing positively**. Wholesale and retail trade edged up by just 0.14%, reflecting the slower pace of growth in agriculture and manufacturing. Meanwhile, the transport and storage sector recorded a modest 2.20% increase, supported by higher activity across road, air, and water transport.

Pakistan's GDP growth projections for FY26 from various international institutions, the State Bank, and the Planning Commission are as follows:

Institutions	Expected GDP Growth FY26
Planning Commission	4.20%
State Bank of Pakistan	3.25-4.25%
World Bank	3.10%
International Monetary Fund	3.60%
Asian Development Bank	3.00%

***Source: Planning Commission, SBP, World Bank, IMF, ADB*.**

Growth forecasts for FY26 reflect cautious optimism about Pakistan's economic prospects. The **Planning Commission** projects the highest growth at **4.20%** for FY26. Whereas, **State Bank** is more cautious and expects a growth range of **3.25 - 4.25%**, reflecting both the potential for recovery and the uncertainty from external and domestic risks. International institutions remain more conservative — the **IMF** at **3.60%**, the **World Bank** at **3.10%**, and the **ADB** at **3.00%**. They have raised their concerns over **tight fiscal and monetary conditions, structural bottlenecks, and global headwinds**. Overall, while growth is expected to improve from previous years, these projections suggest that Pakistan's FY26 recovery will likely be **steady** but **modest**, heavily dependent on **sustained macroeconomic stability** and meaningful reforms to unlock higher, more inclusive growth.

1.2. The Fiscal Equation: A Historic Surplus with Future Risks

According to the Finance Ministry, Pakistan's **budget deficit** was recorded at **Rs6.17 trillion, i.e. 5.4% of the GDP**, during the fiscal year 2024-25, as compared to **Rs7.20 trillion or 6.8% of GDP** last year. This is mainly due to **higher revenue growth, which has outpaced expenditure growth**. While the primary balance recorded at Rs2.71 trillion or 2.4% of GDP, as compared to Rs0.95 trillion or 0.9% of GDP last year. **This reflects improved fiscal discipline in FY25.**

This **fiscal consolidation was fueled by strong revenue growth**, enabling the government to meet IMF targets, a result largely attributed to **greater fiscal discipline and an improvement in debt dynamics.**

Recently, Standard & Poor's (S&P) upgraded Pakistan's long-term sovereign credit rating from **'CCC+' to 'B-'** with a stable outlook, recognizing improvements in external liquidity management and progress on fiscal reforms. The upgrade signals that the country's strengthened fiscal position is expected to remain stable over the next year.

On the fiscal front, the **Primary Balance** (fiscal balance excluding interest payments) improved sharply from **0.9% of GDP in 2024** to **2.1% in 2025**, reflecting stronger fiscal discipline. However, S&P expects this gain to erode in the coming years, with the ratio expected to decline to **1.8% in 2026** and further to **1.2% in 2027**. This downward trend **poses a key risk**, as it signals the challenge of **sustaining fiscal consolidation** and **maintaining** hard-won **stability over the medium term**.

Table 1: Pakistan's Fiscal Indicators

Description	2024	2025	2026	2027
Primary Balance/GDP (%)	0.9	2.1	1.8	1.2
Revenue/GDP	12.6	15.7	15	15.2
Expenditure/GDP	19.5	21.3	20.1	20.1
Interest/Revenues	61.5	49	45.8	40.2
Debt/GDP	70	69.6	68	66.6

Source: Standard & Poor's Global Rating Report

Revenue as a share of GDP is projected to fall to **15%**, while **expenditures** are expected to remain largely unchanged, a **gap** that poses a serious challenge to **fiscal consolidation**. This makes it all the more urgent to rein in unproductive spending and push forward with the privatization reform agenda, helping to ease fiscal pressures and free up resources for more productive, growth-oriented investments. The **interest-to-revenue ratio** — a key measure of how much **government revenue goes toward interest payments**. S&P expects to fall sharply from **61.5% in 2024** to **49% in 2025**, and then further to **45.8%**, offering some **much-needed relief** on **debt servicing pressures**. At the same time, Pakistan's debt-to-GDP ratio is projected to edge down from **70% in 2024** to **66.6% by 2027**, signaling a slow but positive shift toward **fiscal sustainability**. However, the debt burden remains high and sustained, disciplined efforts will be essential to put public debt firmly on a downward trajectory.

However, the quality and sustainability of this fiscal success warrant closer scrutiny. The **heavy reliance** on **non-tax revenues**, which can include SBP profits, petroleum development levies, and other sources that are often **volatile & non-recurring**, raises **questions** about **the durability of the fiscal consolidation**. A more **sustainable path** would involve a **structural broadening** of the **direct tax base**, an area where **progress remains a persistent challenge**. The government has **tightened its fiscal stance**, achieving surplus targets but **at the cost of slowing the economy**. Instead of **focusing** on meaningful **tax, energy, and infrastructure reforms** or pushing ahead with **privatization and cutting unproductive spending**, the approach relies heavily on steep energy tariff increases. This may provide a **quick solution** but risks driving up inflation and harming both businesses and consumers, ultimately **weakening long-term growth**.

1.3. Monetary Policy at a Crossroads

Pakistan's CPI inflation dropped sharply from **23.4% in FY24 to 4.5% in FY25**. However, despite lowering the rate from **22% to 11%,** the economy struggled to gain momentum. GDP growth fell short of targets, private sector credit didn't pick up, and overall growth remained muted at 2.68%.

The **private sector's credit-to-GDP** ratio is an important measure that shows **how much credit is available to fuel economic activity**. Generally, there is a **strong positive link** between **private sector credit** and **economic growth** — when more credit flows into the system, the economy tends to grow faster.

However, Pakistan's private sector credit-to-GDP ratio has fallen from **over 15%** in 2017–18 to just **11%** in 2024-25. This decline has weakened demand in the economy and is notably low compared to other developing countries in the region, highlighting a key challenge for boosting growth.

The Large-Scale Manufacturing (LSM) has contracted by 1.21% in Jul-May FY25 so far, compared to a modest **0.86%** growth last year. This decline highlights deeper structural challenges that must be addressed to **convert hard-earned macroeconomic gains** into real, **sustained growth**. Pakistan's economy remains **heavily reliant on imports**, faces **weak domestic demand**, and continues to experience **inefficiencies**. While fiscal discipline has been maintained, it has often come at the expense of economic growth.

The external account surplus in FY25, along with timely disbursements from the IMF's Extended Fund Facility (EFF), enabled the State Bank of Pakistan to rebuild its foreign exchange reserves significantly. As of July 18, 2025, state bank reserves stood at **$14.5 billion**—a remarkable **60%** increase from $9.02 billion the previous year.

According to the State Bank, Pakistan faces **external debt repayments** totaling **$25.9 billion** in the current fiscal year, which includes **$22 billion in principal** and **$4 billion in interest**. Of this amount:

a) Approximately **$16 billion** is expected to be rolled over.
b) The remaining **$10 billion**—comprising $6 billion in principal and $4 billion in interest—will need to be repaid.
c) This year, Pakistan also has two bond maturities worth **$1.8 billion** as part of its external debt servicing.

Currently, foreign exchange reserves at **$14.5 billion** exceed the country's net annual external debt obligations of **$10 billion** by about **$4.5 billion** in **"surplus"** reserves. Since the trade deficit surged **by 44%** in July 2025 and is expected to stay **high with the rising import demand**, coupled with remittance inflows weakening, the optimistic target of reserves reaching **$15.5 billion by December** now depends heavily on the timely arrival of all planned official financing. **Any delays**, combined with **sustained high trade deficits**, would place immediate and **severe**

downward pressure on the Pakistani Rupee. This pressure could **trigger a challenging cycle**, where **currency depreciation raises import costs**, leading to **higher inflation** and prompting **tighter monetary policies**. These developments risk slowing economic growth, especially at a time when maintaining stability is crucial. Early signs suggest these risks may be starting to resurface. Monetary policy now stands at a critical crossroads. Reviving growth will require more than just cutting interest rates—it demands bold structural reforms to tackle the root causes holding the economy back.

Pakistan's growth model faces several deep-rooted obstacles, including;

a) Heavy dependence on imports, which leaves the economy vulnerable to external shocks.
b) Chronic struggles to push growth beyond 3–4%, leading to widening current account deficits, declining foreign exchange reserves, pressure on the exchange rate, and rising inflation.
c) A rapidly growing population that strains resources and limits economic resilience.
d) High domestic interest payments that consume a large share of tax revenues, limiting fiscal space.

Until these fundamental fiscal and structural issues are addressed, meaningful and lasting progress through monetary policy alone will remain out of reach. Well-calibrated rate cuts, if implemented thoughtfully, can support recovery—but only as part of a broader strategy that balances growth with economic stability.

1.4. Key Risks to Stability

Pakistan's economic **stability is hanging by a thread**, with **concerns** echoed by both **local** and **international institutions**, some of which are highlighted below.

To navigate these challenges successfully, it's crucial to address these **interconnected risks** through ongoing **reforms,** careful fiscal and monetary management, and strong climate resilience efforts. Doing so is not only vital to **safeguarding stability** but also to building a **solid foundation** for sustained and inclusive **economic growth** in the years ahead.

a) World Bank

i) Elevated debt levels limiting fiscal space and increasing vulnerability
ii) Uncertainty in policy and global trade affecting economic predictability
iii) High exposure to climate-related shocks threatens agriculture and overall resilience

b) State Bank of Pakistan

i) Resurgence of inflation outlook due to rising energy inflation from tariff hikes and the phasing out of temporary electricity subsidies, expected energy price adjustments, especially gas tariffs
ii) A widening trade deficit fueled by rising import demand, slower global growth, and weak export prices, particularly for rice

iii) External vulnerabilities linked to volatile global commodity prices, uncertain trade prospects, sudden energy price changes, and potential widespread flooding

c) Planning Commission

i) Geopolitical tensions and fiscal imbalances
ii) Slow pace of reforms and growing cyber threats
iii) Long-term vulnerabilities, including delayed climate action and slow adoption of advanced technologies like AI

d) International Monetary Fund (IMF)

i) Risks from recent tariff changes and geopolitically driven commodity price shocks
ii) Tightening global financial conditions and potential declines in remittances
iii) Rising trade barriers among key partners
iv) Risks of policy slippages under political and social pressure, including demands for tax breaks and subsidies
v) Significant climate-related challenges due to Pakistan's high exposure to natural disasters and urgent adaptation needs

2. Inflation Resurgence: Big Risk Ahead

Pakistan's inflation story has seen a dramatic shift over the past year. CPI inflation plummeted from a high of 23.4% in FY24 to just 4.5% in FY25. Several important factors drove this sharp decline:

a) A strong **"high base effect**," as inflation is measured against the record 38% peak from the previous year, naturally pushing year-on-year numbers lower.
b) **Suppressed domestic demand**, largely due to high energy prices limiting spending.
c) A drop in **global commodity prices**, which helped ease import costs.
d) **Lower domestic food prices**, which had been a key driver of earlier inflation.

The Govt. also introduced administrative controls and targeted relief measures to stabilize prices on essential items, including food, fuel, and utilities. However, these were **temporary measures** rather than **long-term fixes** to supply chain problems or energy costs. This rapid fall gave an impression of full control over inflation, but beneath the surface, price pressures remained fragile—mainly due to ongoing governance challenges.

Core inflation, which excludes volatile food and energy prices, stayed stubbornly high. As of July 2025, it was still 7% in urban areas and 8.1% in rural areas—well **above the general inflation rate of 4.1%.** This gap **suggests underlying inflation pressures** and expectations have **not fully eased** and may even widen.

The start of FY2026 revealed how delicate this disinflation was. Headline inflation jumped back to 4.1% year-on-year in July, fueled by sharp month-on-month increases in gas charges (22.9%), electricity (14.2%), transport services (4.8%), and motor fuel (4.5%).

The real concern now is that **rising energy costs** will push **core inflation even higher**. The businesses will then pass through on to the consumers. If **core inflation** continues to **climb**, inflation expectations could spiral, forcing the **central bank** to **raise interest rates** further. The State Bank itself has expressed **worries** about this surge in **energy inflation**, which threatens to slow economic growth and complicate the road to recovery.

3. Navigating Growth amid Cumulative LSM Contraction and External Risks

The new fiscal year began with robust growth in both exports and imports, reflecting a surge in economic activity and demand. In July 2025, Pakistan's exports climbed to **$2.70 billion**, up from **$2.31 billion** in July 2024 — a solid **16.9% increase** that highlights stronger global demand for Pakistani products. Imports also rose sharply, reaching **$5.45 billion** compared to **$4.22 billion** a year earlier — a **29.3% jump** — driven by higher energy costs, increased demand for industrial raw materials, and renewed momentum in domestic production. Consequently, the trade deficit widened to **$2.75 billion**, up from **$1.91 billion** last year — a **44.2% increase**.

This **upward momentum** in both exports and imports reflects a welcome boost to economic activity. However, sustaining this pace will require prudent management of the external balance, especially in light of the risk of a **rising current account deficit**, which is projected to stay in the range of 0–1% of GDP in FY2026. Sound fiscal and monetary management will be essential, as Pakistan's growth model relies **heavily on imports**, a dependence that leaves the economy **exposed to external shocks and vulnerabilities**.

External stability may come **under renewed pressure** as the **trade deficit** is expected to widen, fueled by **rising import demand**, a slowdown in global demand, and weaker export prices, particularly for rice. Worker remittances are projected to grow at a slower pace due to the high base effect, while the current account deficit is anticipated to remain contained within **0–1% of GDP in FY26**.

As highlighted by the State Bank, **CPI inflation** for July surged by 4.1% for July 2025 on a year-on-year basis in July 2025, as compared to 3.2% in the previous month and 11.1% in July 2024. On a **month-on-month** basis, it **increased by 2.9%** in July 2025 as compared to an increase of 0.2% in the previous month and an increase of 2.1% in July 2024.

Pakistan's industrial output has become increasingly **inward-looking** due to structural challenges, with a weak export base evident in the **decline of manufacturing's share in GDP, now at 18%, down from 26% in the 1990s**. While a fundamental transformation may not be on the horizon, a rebound in large-scale manufacturing (LSM) is possible in the coming months, supported by lower policy rates, rising imports of industrial inputs, and stronger demand from the industrial sector.

The policy decisions made in the months ahead — especially in addressing the widening trade deficit — will be pivotal. Resorting to import controls would signal a step back from structural reforms, whereas a determined effort to strengthen export competitiveness and revive industry through deep, and often challenging, reforms remain the only sustainable path to breaking Pakistan's stop-go growth cycle.

For a genuine industrial revival, Pakistan needs a **well-defined 10-year industrial policy** aimed at boosting **exports** and building a **strong manufacturing base**. This requires promoting entrepreneurship, fostering cluster-based economic integration, and implementing business- and industry-friendly policies that encourage private sector–

led, homegrown industrialization. Such an approach can create jobs, spur innovation, and enhance global competitiveness. Ultimately, structural reforms must shift the growth model away from import-driven consumption toward a more resilient economy powered by exports and investment.

3.1. Textiles Poised to Drive Export Growth in FY26

In FY25, **exports saw a modest increase of 4.45%,** reaching $32 billion, up from $30.67 billion in FY24. Imports, however, **grew more rapidly by 6.58%,** rising to $58.4 billion compared to $55 billion the previous year. This accelerated import growth contributed to a **widening trade deficit**, which increased by 9.3% to $26.3 billion in FY25, up from $24 billion in FY24.

A sector-wise analysis of exports reveals that Pakistan's textile exports demonstrated strong performance, increasing by **7.3% to $17.88 billion** from $16.65 billion. The **share of textile exports** to total exports surged to **56**% compared to 54% last year. Food group exports remained over $7 billion. However, it dropped by 3.4% to $7.11 billion. The share of food exports to total exports dropped to 22% compared to 24% last year. **Textile and Food exports collectively make up around $25 billion or 78% of total exports of the country**. Petroleum and coal exports experienced significant growth of 44%, rising to $573 million from $397 million. Additionally, other manufacturing exports expanded by 4.84%, which stood at $4.2 billion compared to $4.0 billion in the previous fiscal year.

The new fiscal year has kicked off on a positive note for Pakistan's exports. In July 2025, **exports rose to $2.70 billion**, up **16.9**% from $2.31 billion in July 2024, reflecting stronger global demand for Pakistani products. Building on this momentum, Textile and Apparel exports are expected to perform even better than they did in June 2025.

However, **maintaining this growth will depend heavily** on how the **government addresses** ongoing **challenges**, especially the impact of high energy prices on domestic industries. Pakistan **stands** at a **crossroads**—while its low minimum wages and favorable US tariff rates compared to regional competitors offer a **competitive edge**, this advantage is offset by high input costs, low productivity, and tight monetary policies, which limit its ability to compete effectively in the region.

To capitalize on its potential and attract long-term industrial investment, Pakistan must urgently i**mplement deep structural reforms** aimed at boosting productivity and reducing costs. This is crucial for the country's path toward sustainable economic growth.

3.2. Construction & Materials: The Cement Sector's Robust Start

According to the All-Pakistan Cement Manufacturers Association (APCMA), local cement sales surged to 2.988 million tons in July 2025, up 18.4% from 2.524 million tons in July 2024. Exports showed an even more impressive jump of 84.21%, climbing from 0.547 million tons to 1.008 million tons over the same period. North-based cement producers supplied 2.65 million tons, marking a 17.6% increase compared to last year, while south-based mills saw an exceptional 64.6% rise in dispatches, reaching 1.35 million tons.

Despite challenging weather conditions, the new fiscal year has **started positively** for the cement sector. Industry experts are optimistic that with improving macroeconomic indicators and effective utilization of the government's Public Sector Development Program (PSDP), the sector is poised for strong momentum in the coming months. This **robust export performance** is driven by factors such as stable international coal prices—a key input cost—and favorable pricing in global markets.

If the government successfully leverages the PSDP to stimulate demand, it will create a much-needed boost not only for cement production but also for several allied industries. This, in turn, will drive higher demand, generate jobs, and sustain economic momentum, providing a significant lift to the overall economic landscape. The growth momentum of the cement sector is crucial for overall economic progress. Its success will largely depend on the government's ability to encourage domestic producers to fully utilize idle capacity—an effort that can drive economic expansion, generate employment, and boost related industries.

4. Import-Driven Growth Model: The Widening Deficit Dilemma

Pakistan's external account showed a rare bright spot in FY25, posting a current account surplus of **$2.1 billion for the first time in 22 years**, a significant turnaround from a $2.07 billion deficit the year before. This surplus helped cushion the impact of a **widening trade deficit**, but was not driven by fundamental improvements in trade competitiveness. **Export growth** remained **modest**, and the core trade balance stayed deeply negative. Instead, the surplus largely reflected unusually strong workers' remittances and artificially suppressed import demand, leaving the external account's stability still very much uncertain amid persistent structural challenges.

This **fragile position** was laid bare by the July 2025 trade figures, which showed **the trade deficit soaring to $2.75 billion—up 44.2% from $1.91 billion in July 2024**. Looking ahead, the State Bank forecasts that the trade deficit will continue to widen through FY26 due to rising import demand, while remittance growth is expected to slow down because of a high base effect and recent policy changes. As a result, the current account is likely to slip back into deficit, estimated to hover between 0 and 1% of GDP.

These trends highlight the deep-rooted structural issues within Pakistan's external sector. The growing trade deficit and rising import demand are placing renewed pressure on the current account, making it one of the economy's most vulnerable points moving forward.

There's a **direct correlation between real GDP growth and import growth**—whenever imports go up, the economy tends to grow, and when they're restricted, growth slows down. This heavy dependence on imports makes the economy vulnerable. **Historically**, whenever Pakistan's GDP growth crosses the **3-4% mark**, **current account deficit tends to widen sharply**, straining **foreign exchange reserves**. This reveals how closely higher growth is intertwined with **external imbalances**. Simply put, the economy struggles to sustain growth beyond a certain level without encountering balance of payments difficulties. Ideally, reserves should cover at least three months of imports, but this cushion often shrinks as growth accelerates. When the current account deficit surpasses $500 million, it usually triggers noticeable pressure on the exchange rate, and history has shown a clear pattern: the larger the deficit, the weaker the rupee tends to become.

Breaking this cycle requires bold, meaningful structural reforms that shift the economy away from import-driven consumption toward export-led growth and investment. Only then can Pakistan build a more stable and resilient economic future. The current situation perfectly illustrates Pakistan's classic balance of payments constraint. The recent surge in imports is a natural outcome of the early stages of economic recovery. The data make it clear: Pakistan's import demand is far more sensitive to economic growth than its export capacity. In other words, even a modest uptick in GDP results in a disproportionately large increase in imports. So, the July trade figures are far more than just a snapshot—they are a clear signal pointing to the country's fundamental structural weaknesses that must be addressed for sustainable progress.

5. The Energy Sector: Cost Adjustments and Consumer Impact

Energy inflation is set to rise sharply following the recent steep increase in gas tariffs and the phase-out of temporary electricity subsidies introduced late in FY25. At present, Pakistan's **industrial electricity prices are nearly double** those of **regional competitors** like India and Bangladesh. Unless key challenges—such as heavy capacity payments, circular debt, and significant losses in distribution companies—are effectively addressed, Pakistani industries will continue to face a serious cost disadvantage.

Without tackling these underlying inefficiencies, the **higher tariffs risk pushing up costs** for the economy's most **productive sectors**, severely hurting their competitiveness. The industrial sector is becoming increasingly inward-looking, struggling to expand in export markets due to limited **innovation, weak integration into global value chains**, and rising production costs driven by frequent domestic and external shocks.

To protect and boost industrial competitiveness, Pakistan urgently needs fundamental reforms that improve energy efficiency, shift power generation toward more affordable renewable sources, and resolve the chronic circular debt issue.

Looking ahead, deep and long-term structural reforms are essential to attract industrial investment and sustain growth. A clear, focused 10-year industrial policy is critical to revitalize the sector and increase exports.

This **surge in energy prices** reveals a major **contradiction in Pakistan's economic strategy**. While the government promotes export-led growth as the key to recovery, rising energy costs are simultaneously undermining the industries expected to lead that growth. Energy expenses make up a large share of production costs, and higher tariffs put Pakistani businesses at a clear disadvantage against global competitors.

To fully capitalize on Pakistan's current edge of lower US tariffs compared to regional peers—especially important given that the US is the country's largest export market—the government must also **restore regionally competitive energy tariffs (RCET).** Without this, domestic industries will continue to face serious setbacks in their ability to compete.

Pakistan is at a critical **crossroads**. While low wages and relatively favorable US tariff rates offer some advantages, these are outweighed by high input costs, low productivity, and restrictive monetary policies that hold the country back in the regional race.

Moving forward, policy must focus on fostering entrepreneurship, encouraging cluster-based economic integration, and building a business-friendly environment. This approach can nurture private sector-led, homegrown industrial growth that creates jobs, sparks innovation, and strengthens competitiveness.

Breaking free from an import-driven economy demands a strategic shift toward growth powered by exports and investment. Only through this transformation can Pakistan truly unlock its economic potential.

6. Recommendations for Navigating Economic Recovery

6.1. Connecting the Dots: A Policy-Driven Crossroads

Pakistan's **economic growth model is constrained by deep-rooted structural challenges** that undermine its vitality and resilience to both domestic and external shocks. Until these fundamental issues are effectively addressed, sustainable and meaningful progress will remain elusive.

Firstly, there is a **clear link between real GDP growth and import growth**. When imports rise, the economy tends to expand; when import demand is restricted, growth slows. This **heavy reliance on imports** exposes the economy to significant **vulnerabilities.**

Secondly, under the IMF program, efforts to tighten the current account balance aim to stabilize the external sector, but this often comes at the cost of economic growth. Periods of rapid import growth place additional pressure on the exchange rate, often leading to currency depreciation. The economy struggles to grow beyond a certain threshold without encountering foreign payment difficulties. Ideally, foreign exchange reserves should cover at least three months of imports, but this buffer often diminishes as the economy accelerates.

Thirdly, Pakistan's growing debt burden is alarming—by 2024, interest payments alone consumed a major portion of the **government's total revenue**, leaving little room for critical spending on Productive Expenditures health, education, and infrastructure needed for human development. This squeezes development and holds back long-term growth

Without tackling these fundamental structural weaknesses through comprehensive reforms, fiscal tightening alone will be insufficient. The country risks remaining trapped in a cycle of recurring balance of payments crises and unsustainable growth patterns over the long term.

6.2. Strategic Recommendations for Stakeholders

Given this complex and tenuous environment, different stakeholders must adopt nuanced and cautious strategies.

a) For Investors:

i) **Sectoral Diligence is Key:** The idea of a "dual economy" means there are two separate parts: a modern sector and a traditional one, both running side by side. This means there are chances to grow, but you have to choose carefully. The IT and services export sector is doing well because it isn't too affected by local energy prices or slower spending at home. Value-added textiles are also doing well, but it's important to check if companies can handle rising energy costs and a possible drop in demand from important Western markets.

ii) **Caution on Domestic Consumption:** Industries that depend a lot on local consumer spending, like the automotive sector, are facing tough challenges. Rising inflation is making people's money worth less, and with interest rates no longer being cut, demand is expected to stay low.

iii) **Monitor Leading Indicators:** The construction and materials sector, led by cement, is a key indicator of domestic investment. Its continued strong performance could signal a more durable recovery, but it remains vulnerable to any future tightening of financial conditions.

b) For Corporate Strategists:

i) **Re-evaluate Cost Structures:** The new energy tariff regime is not a temporary shock but a new baseline. Businesses must urgently re-evaluate their cost structures, invest in energy efficiency, and explore alternative energy sources where feasible.

ii) **Enhance Supply Chain Resilience:** The July trade data is a clear warning sign. The risk of a deteriorating external account could lead to renewed, and potentially abrupt, import controls or significant currency volatility. Corporate strategists should review their supply chains to mitigate these risks, potentially by diversifying suppliers or increasing local sourcing where possible.

iii) **Scenario Planning:** Prepare for a more challenging macroeconomic environment in the second half of 2025. Scenarios should include higher-than-forecast inflation, further currency depreciation, and a potential slowdown in economic activity as policy constraints bite.

c) For Policy Watchers:

i) The **monthly trade deficit:** This is the earliest and most important indicator of whether the external account is spiraling out of control.

ii) The **SBP's foreign exchange reserve levels:** A consistent decline will signal rapidly diminishing policy space and increasing crisis risk.

iii) **Core inflation figures:** An acceleration in core inflation would indicate that the July energy shock is becoming embedded in the economy, forcing the SBP into a more hawkish and growth-retarding stance.

iv) **Observe the Policy Response:** The government's response to the widening trade deficit will be a critical test of its strategic direction. A move towards import controls would signal a retreat to short-term crisis management. Conversely, the announcement of concrete measures to boost export competitiveness would indicate a commitment to tackling the underlying structural problems. This response will be the most telling indicator of Pakistan's economic trajectory for FY2026 and beyond.