

Pakistan Economic Insights

(January 2026)

Executive Summary

Pakistan's economic recovery is gaining momentum faster than anticipated, with large-scale manufacturing rebounding from contraction to **4.8%** growth and agriculture expected to contribute positively. Fiscal consolidation of **Rs. 2 trillion** was achieved primarily through Rs. 1.6 trillion interest payment savings following rate reductions. However, external pressures are mounting as imports surge while exports contract sharply, widening the trade deficit. Remittances remain the only saving grace. Paradoxically, despite massive social protection spending, poverty incidence has risen to 28.9%, raising serious questions about the effectiveness of social protection programs. The economy shows improvement, but it still faces structural vulnerabilities that require comprehensive reform.

Key Points

Economic Growth & Activity

- Economic momentum is building faster than expected, led by domestic-oriented sectors.
- **Large-scale manufacturing (LSM) grew by 4.8%** in July-December 2025, a significant recovery from a contraction of 1.4% in the same period last year. However, this growth is narrow-based (92% from four sectors) and is more of a correction than a return to peak levels.
- Rising imports of consumer durables and machinery signal a pick-up in domestic demand.
- Risks to the agriculture sector have diminished, with positive growth now expected.

External Sector

- The trade deficit has widened due to a **9.8% increase in imports** and a **5.5% decrease in goods exports**.
- The surge in imports is heavily concentrated in **consumer durables (42% of the increase)** and food items (28%).
- Exports have plunged by 7.1% overall, with a catastrophic **40.5% drop in rice exports** and a 17.1% crash in non-textile exports.
- **Workers' remittances are the primary saving grace**, rising by \$2.3 billion and offsetting some of the trade deficit pressure.

- Net foreign direct investment (FDI) has **halved (down 41%)**, with significant outflows from the telecommunication sector.

Fiscal Development

- Fiscal consolidation of Rs. 2 trillion was achieved, driven by a **10.3% reduction in total expenditure**.
- This expenditure reduction was largely due to a **30.7% decrease in interest (markup) payments**, driven by lower interest rates.
- The fiscal space created was used for a **43.2% increase in development expenditure**, as well as a massive rise in subsidies and grants, indicating potentially imprudent fiscal management.
- The fiscal balance improved from a deficit of 1.3% of GDP to a **surplus of 0.4% of GDP** in the first half of the year.

Inflation

- Headline inflation is within the SBP's 6-7% target range, but **core inflation remains above the upper bound**.
- Food inflation is highly volatile, with food items dominating both the lists of items with negative inflation and those with double-digit inflation.

Poverty Alleviation (Issue of the Month)

- **Poverty incidence rose to 28.9% in 2024-25**, the highest increase between two HIES surveys since 1999.
- This rise has occurred despite massive increases in funding for social safety nets like BISP, raising serious questions about the effectiveness of these programs.
- Key issues with BISP and other programs include:
 - **Donor-driven agenda** with loans that are government liabilities but mandated for use through BISP.
 - **Institutional problems** like static beneficiary data and non-technical staff.
 - **Leakages and corruption** in fund distribution.
 - A focus on **consumption smoothing rather than sustainable poverty graduation**.
 - Lack of integration with provinces post-18th Amendment.



Section 1

Fundamental Macroeconomic Indicators of Pakistan's Economy

Pakistan's economy began to gain from fiscal consolidation, as growing business and consumer confidence is evident in higher growth in *large-scale manufacturing, which recovered from the persistent decline of the last two years and posted 6.1% growth during July-November 2025 against a contraction of 1.4% in the comparable period last year*. Economic activity continues to gain momentum faster than anticipated, mainly led by domestic-oriented sectors. Rising imports, especially of consumer durables (mobile phones and vehicles), machinery (construction, textile, office, electrical), and iron and steel, are indicating a rise in domestic demand. The risks of significant losses to the agriculture sector have also dwindled, and the expected positive growth in the sector will contribute to economic growth. This implied a significant improvement in growth outlook for the fiscal year.

The trade deficit has widened on the back of a substantial increase in imports and a decline in exports. The import volumes have substantially increased, but muted international prices have kept their intensity in check. Other factors, such as resilient workers' remittances and a benign global commodity prices outlook, have kept pressure on the current account deficit relatively tame.

Agriculture

The impact of floods on the agriculture sector dissipated, and minor crops like onion, potato, and vegetables produced good volumes, and important crops also managed to weather the major impact. During July-December 2025, agricultural credit disbursement increased by 11.4 percent to Rs. 1,411.6 billion from Rs. 1,266.7 billion last year. Moreover, the imports of agricultural machinery and implements increased by 21.6 percent to \$65.8 million during July-December 2025 from \$54.6 million the previous year. During Rabi 2025-26 (October-December), urea offtake remained 1,356 thousand tonnes (36.8% higher than Rabi 2024-25), whereas DAP offtake was 464 thousand tonnes (44% less).

Manufacturing

LSM posted nearly a double-digit growth of 9.8 percent in November 2025, which nosedived to 0.4% in December 2025. LSM grew by 4.8% in July-December 2025 compared to negative growth in the comparable period of last year. The growth is predominantly (92%) driven by auto sales, domestic cement dispatches, petroleum products, and wearing apparel. It implies that LSM growth is lopsided and touched only pockets of industries. The index is still well below its March 2022 peak of 153. LSM growth is more of a correction than growth. However, the growth in November 2025 was double-digit.

Inflation

Inflationary pressures on the economy are building, and while headline inflation remained within the SBP's medium-term range of 6-7%, core inflation remains above the upper bound. Looking at the dynamics of inflation, food inflation took the brunt of the adjustment. CPI Urban

Wearing Apparel	1.25
Petroleum Products	0.98
Cement	0.65
Automobiles	1.57
Total Contribution	4.45
Total Growth	4.82
Source: SBP	

is divided into 94 item groups; 17 recorded negative inflation, 13 of which belonged to the food group. Of the total 94 items, 12 recorded double-digit inflation, and of these, eight are from the food group. So, food has contributed to both higher and lower inflation.

Table 2: CPI Inflation (%)

	July-June		July-Jan	
	2023-24	2024-25	2024-25	2025-26
CPI National	23.4	4.5	6.5	5.2
Food	21.9	0.6	1.3	3.5
Non-Food	24.7	7.7	10.9	6.5
Core	17.9	9.2	10.0	7.4
CPI Urban	7.8	5.3	7.8	5.3
Food	2.2	3.2	2.2	3.2
Non-Food	11.9	6.7	11.9	6.7
Core	9.2	7.0	9.2	7.0
CPI Rural	22.5	3.3	4.7	5.1
Food	20.3	-1.2	-0.1	4.0
Non-Food	23.0	7.1	9.5	6.2
Core	22.4	10.7	12.4	8.1

Source: PBS

Table 3: Breakdown of Urban CPI (% Increase/Decrease)

	Negative Growth	Modest Increase (>0 to 5%)	Lower High >5 to 10%	High Increase (>10 to 20%)	Exploding (>20%)	Total
Food	13	8	10	6	2	39
Alcoholic Beverages, Tobacco	0	1	0	1	0	2
Clothing & Footwear	0	0	9	0	0	9
Housing, Water, Elec, Gas & Other						
Fuel	2	2	4	0	1	9
Furnished Household Equip & Maint etc.	0	3	5	0	0	8
Health	0	1	5	0	0	6
Transport	0	3	3	0	0	6
Communication	0	2	1	0	0	3
Recreation and Culture	2	2	0	0	0	4
Education	0	0	1	0	0	1
Restaurants & Hotels	0	0	3	0	0	3
Miscellaneous Goods & Services	0	0	2	1	1	4
Total	17	22	43	8	4	94

Source: PBS

Fiscal Development

Fiscal consolidation is primarily driven by the expenditure side, where a reduction in interest rates led to an adjustment of Rs. 1.6 trillion. So, modest revenue growth of 9.4% and a massive adjustment of 10.3% on the expenditure side resulted in a consolidation of Rs. 2 trillion. Interest

expenditure decreased by 30.7%, paving the way for a 28.2% increase in primary expenditures. Fiscal space is utilized for a massive increase in subsidies and grants, which implies imprudent fiscal management.

Table 4: Consolidated Fiscal Operations (July-December 2025-26)

(Billion Rs)

	Jul-Dec FY25	Jul-Dec FY26	% Change	As % of GDP	
				FY25	FY26
Total Revenue	9,764	10,684	9.4	8.5	8.2
- Federal	9,178	9,960	8.5	8.0	7.7
- Provincial	585	723	23.5	0.5	0.6
A) Tax Revenue	6,067	6,729	10.9	5.3	5.2
a) Federal	5,625	6,161	9.5	4.9	4.8
b) Provincial	443	569	28.4	0.4	0.4
B) Non-Tax Revenue	3,696	3,954	7.0	3.2	3.1
a) Federal	3,553	3,799	6.9	3.1	2.9
b) Provincial	143	155	8.4	0.1	0.1
Total Expenditure	11,302	10,142	-10.3	9.9	7.8
A) Current Expenditure	10,118	9,591	-5.2	8.8	7.4
a) Federal	7,643	6,770	-11.4	6.7	5.2
Markup Expenditure	5,142	3,564	-30.7	4.5	2.8
Non-Markup Expenditure	2,502	3,206	28.2	2.2	0.8
b) Provincial	2,475	2,822	14.0	2.2	2.2
B) Development & Net Lending	744	964	29.6	0.6	0.7
a) Development Expenditure	772	1,106	43.2	0.7	0.9
- Federal PSDP	133	156	17.0	0.1	0.1
- Provincial ADPs/PSDPs	639	950	48.7	0.6	0.7
Statistical Discrepancy	440	-413	-194.0	0.4	-0.3
Fiscal Balance	-1,538	542	-135.2	-1.3	0.4
Financing	1,538	-542	-135.2	1.3	-0.4
a) External (Net)	-79	34	-143.3	-0.1	0.0
b) Domestic (Net)	1,617	-576	-135.6	1.4	-0.4
- Bank Borrowing	-2,026	-250	-87.6	-1.8	-0.2
- Non-Bank Borrowing	3,642	-325	-108.9	3.2	-0.3
Primary Balance	3,604	4,106	13.9	3.1	3.2
Revenue Balance	-354	1,092	-408.2	-0.3	0.8
Provincial Surplus	775	1,179	52.1	0.7	0.9
GDP (Current Market Prices)	114,692	129,567			

Source: Finance Division

External Sector

The economy is exposed to new challenges in the external account; however, their intensity is currently muted due to supportive factors. In January, the current account surplus was recorded, which does not warrant complacency. Both an increase in imports and a decrease in exports are contributing to the widening of the trade imbalance. On the other hand, an increase in imports of services more than offset the impact of an increase in exports of services. Buoyancy in remittances is the only saving grace for the external account. This is yet another vulnerability and serious risk for this dependence.

Exports of goods continued their contraction by 5.5%, whereas imports increased by 9.8% in July-January 2025-26. Services exports increased by 18.8%, whereas imports also increased by 17.4%. The goods trade imbalance widened by \$4.4 billion, while the services trade imbalance deteriorated by \$250 million. Remittances are up by \$2.3 billion.

Imports

The surge in imports has become a serious issue, especially given its composition. Table 3 suggests that 42% of the increase in imports is contributed by consumer durables, and another 28% by food imports. Raw materials have contributed 35% of additional imports. The global POL price has provided much-needed relief, as POL imports have decreased in dollar terms.

Table 5: Causative Factors of CAD (\$ Million)

	July-January	
	2025-26	% Cont.
CAD Deterioration	-1,638	100
<u>Negative Contributions</u>	-5,493	
Trade Balance Deterioration	-4,346	-265
o/w Increase in Goods Imports	-3,279	-200
o/w Decrease in Goods Exports	-1,067	-65
Increase in Imports (Services)	-1,147	-70
<u>Positive Contributions</u>	3,855	
Income Account Improve	212	13
Increase in Exports (Services)	897	55
Current Transfers Improvement	2,746	168
o/w Increase in Remittances	2,351	144

Source: SBP

Table 6: Increase in Imports During July-January FY2026

	July-January		% Change	Increase in Imports	% Contr. in Increase
	2024-25	2025-26			
Total Imports	35,577	38,699	8.8	3,122	100.0
Food Group	4,614	5,502	19	889	28.5
Pulses	630	492	-22	(138)	(4.4)
Palm Oil	1,885	2,350	25	465	14.9
Machinery Group	2,386	3,000	25.7	614	19.7
Elect. Machinery & Appl.	1,839	1,555	-15.4	(284)	(9.1)
Power Generating Mach.	435	476	9.4	41	1.3
Textile Machinery	283	365	28.9	82	2.6
Consumer Durables	2,002	3,306	65.2	1,305	41.8
Mobiles Phone	868	1,140	31.4	272	8.7
Road Motor Vehicles	1,134	2,166	91.1	1,033	33.1
Textile Group	4,123	3,949	-4.2	(174)	(5.6)
Raw Cotton(M.MT)	1,400	860	-38.6	(540)	(17.3)
Raw Materials	4,728	5,437	15.0	1,092	35.0
Plastic Material	1,586	1,722	9	136	4.3
Iron & Steel Scrap	1,158	1,244	7	472	15.1
Iron & Steel	1,244	1,630	31	383	12.3
Medicinal Products	740	841	14	101	3.2
Petroleum Products	9,462	9,047	(4.4)	(415)	(13.3)
Petroleum Products (M.MT)	3,492	3,428	-1.8	(63)	(2.0)
Petroleum Crude (M.Barrels)	3,126	3,383	8.2	257	8.2
LNG	2,202	1,625	-26.2	(577)	(18.5)
Others	8,262	8,456	2.3	(189)	(6.0)

Source: PBS

Exports

Exports plunged by 7.1%, and non-textile exports crashed by 17.1%. Pakistan's main export, rice, decreased by 40.5%. The textile sector managed to grow by 1.2% in the period July-January 2025-26. In absolute terms, the economy lost \$1.5 billion in exports, whereas only the food group exports declined by \$1.6 billion.

Table 7: Group-wise Increase in Exports

Particulars			(\$ Million)
	July-January		Change
	2024-25	2025-26	(%)
A. Food Group	4,614	2,989	-35.2
Rice	2,194	1,305	-40.5
Meat and Meat Prep.	294	316	7.4
B. Textile Group	10,770	10,905	1.2
Cotton Yarn	430	427	-0.8
Cotton Cloth	1,130	992	-12.2
Knitwear	3,034	3,099	2.1
Bedwear	1,869	1,919	2.7
Readymade Garments	2,441	2,579	5.7
Synthetic	237	224	-5.3
C. Petroleum Group	339	516	52.3
D. Other Manufacturer	2,512	2,382	-5.2
Chemicals & Pharma. Pro.	936	769	-17.8
Engineering Goods	240	254	5.9
Cement	188	207	9.9
Leather Products	433	429	-0.8
E. All Other Items	1,348	1,398	3.7
Total	19,583	18,190	-7.1
Excluding Textile	8,812	7,285	-17.3
Share of Textile (%)	55.0	59.9	
Share of Non-Textile (%)	45.0	40.1	

Source: SBP

Net **FDI** has decreased by 41% during July-January 2025-26 from \$1661 million last year to \$981 million this year. Around 96% of this FDI came from China (\$495 million), Hong Kong (\$188 million), Switzerland (\$124 million), and the UAE (\$126 million). Two sectors – power

and financial business – attracted \$542 million and \$462 million, respectively, whereas the telecommunication sector alone witnessed an outflow of \$443 million. It is important to note that, within FDI in the power sector, \$260 million went to the coal sector at a time when the entire world is moving out of it, and hardly any country is offering foreign investment in this sector.

Outlook for Fiscal Year

Real GDP grew by 3.7 percent during July-September 2025-26 compared to 1.6 percent in the corresponding period last year, suggesting a marked improvement in growth prospects. The growth is mainly driven by buoyancy in auto sales, a rise in domestic cement dispatches, a surge in POL sales, higher fertilizer offtake, and significant growth in imports of machinery and intermediate goods, which indicate improvement in domestic demand. The latest available data on the agriculture sector, including information on sowing of the Rabi crop, is also very encouraging for overall growth. The half-yearly LSM growth figures of 4% plus are also supportive. Overall developments in the commodity-producing sectors are likely to provide further impetus to the services sector. The growth outlook has substantially improved in the current year, and the 4.2 percent growth target seems within an achievable range.

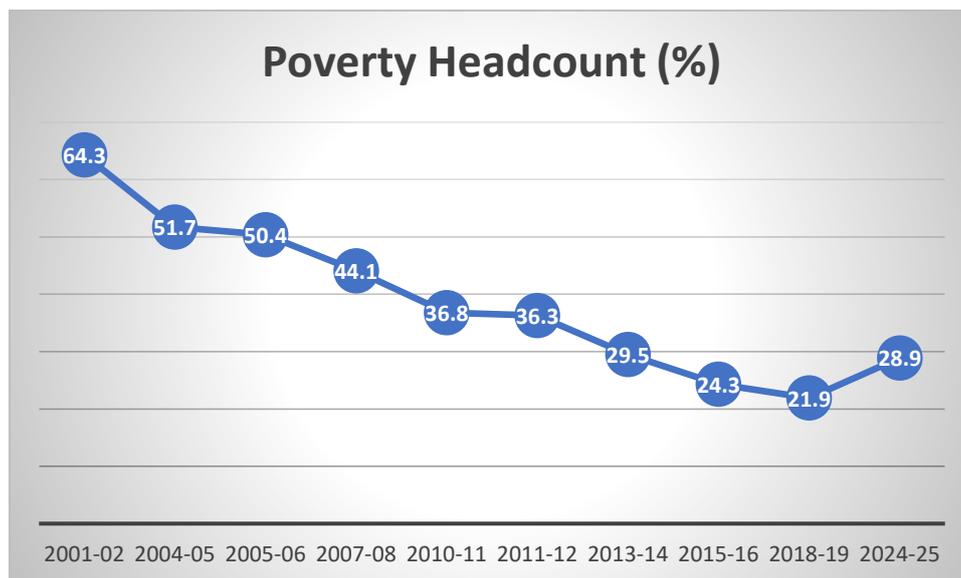


Section 2

Focus Issue of the Month

Effectiveness of the Poverty Alleviation Programs

According to recent estimates released by the Planning Commission, the poverty incidence has increased to 28.9 percent in 2024-25, up from 21.9 percent in 2018-19, a rise of 6.9 percentage points over six years. This is the highest ever increase in poverty incidence between two HIES surveys. The provinces have also witnessed a rise in poverty incidence across the board. Punjab and Sindh are forerunners, while Khyber Pakhtunkhwa and Balochistan also recorded an increase.



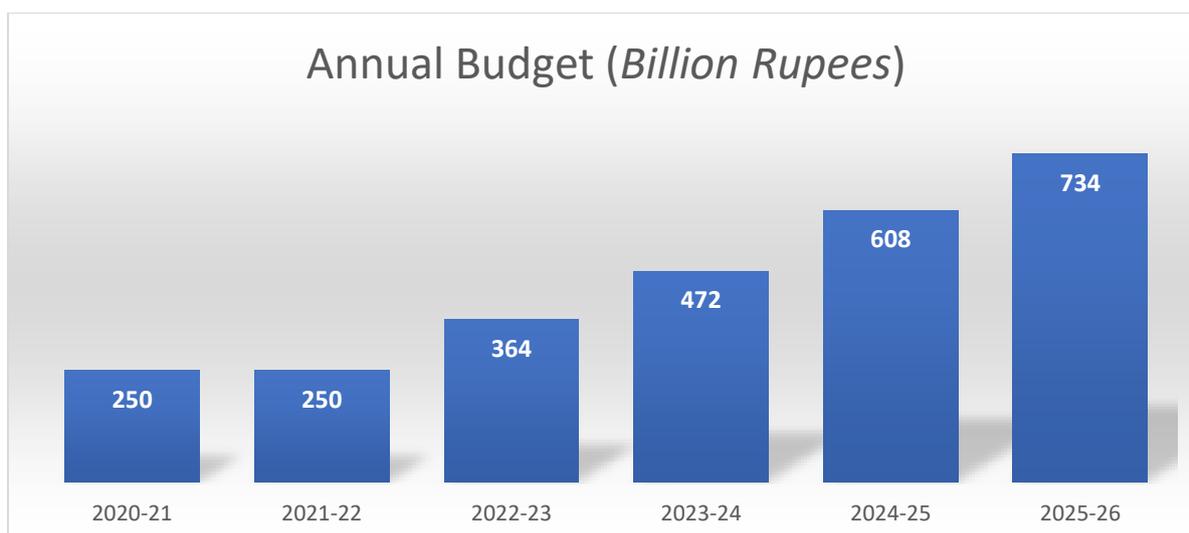
Source: PBS

Since 1999, poverty had shown a declining trend, but this reversed in 2024-25 as the headcount rose sharply over the six years. The last three years have witnessed the lowest average economic growth of 1.7%, which is the lowest in history for consecutive three years. Other factors include natural calamities, soaring inflation, Covid-19, and abandonment of wheat support prices. Interestingly, in this period, Pakistan has witnessed a massive surge in allocations for social protection and a rise in poverty incidence, raising serious questions over the effectiveness of the government's social protection policies.

Benazir Income Support Program (BISP): An Overview

Social safety programs in Pakistan have been in place for years, including the Zakat system (1980s), Pakistan Bait-ul-Mal (1990s), and microfinance initiatives (2000s). In 2008, the Benazir Income Support Program (BISP) was introduced as a large-scale social protection initiative, with a vision of eliminating poverty and empowering downgraded clusters, predominantly women, through inclusive social safety nets. Unconditional cash transfers, education stipends, nourishment programs for women and infants, *Waseela* initiatives, emergency shock response, and cash transfers during natural disasters are multiple protection instruments under the program's mission.

Over the past 17 years, BISP has expanded significantly, with annual budget growth.



Source: Federal Budget documents

International donors provide substantial loans and grants through government transfers as well as for specific projects. The 2023-24 audited statement states the contributions of the World Bank and the Asian Development Bank to government transfers to BISP. Another worth-mentioning aspect is that all loans are the liability of the Government of Pakistan (GOP), but are mandated by international donor agencies to be used only through BISP. Below are the details of international donor agencies that have given loans to BISP (2008-2023) through GOP:

Donor Agency	Funding Amount (million)
World Bank	\$972
Asian Development Bank	\$1571.5
Foreign, Commonwealth & Development Office (FCDO)	£300.3
USAID	\$217.5
KfW (German Development Bank)	€27
GIZ	€15

Source: BISP report “15 Years of Benazir Income Support Program.”

Issues with Social Safety Funds and BISP’s Poverty Alleviation Challenges

All social safety funds in Pakistan are donor-driven, raising concerns given the persistent poverty. Approximately 100 institutions work on 500 social protection aspects, but growth remains undiscussed, revealing a patching method rather than sustainable solutions. Despite BISP’s strong vision, poverty continues after 17 years due to multidimensional issues.

Institutional Problems: Beneficiary selection is dependent on static data, missing dynamism. A sole analysis tool cannot address Pakistan’s social multiplicity. Moreover, institutional capacity is imperfect, with mostly non-technical staff – a mounting tendency in government entities.

Leakages and Irregularities: Funds pass through several hands before reaching the beneficiary, which increases the likelihood of embezzlement. Field staff frequently charge beneficiaries for cash transfers, driving corruption. High operational costs consume considerable resources, and data manipulation additionally weakens effectiveness.

Intrinsic Problems: Social protection money merely smooths consumption rather than eradicating poverty. Microfinance programs are likewise unsuccessful in lessening poverty. Such representations may reduce productivity by encouraging dependence on easy money rather than work, thereby impeding national capacity development. Moreover, such programs lack a graduation strategy – a fundamental aspect of sustainable poverty alleviation models.

Structural Problems: Post-18th Amendment, social protection is a decentralized subject, but lacks provincial incorporation. Administrative hurdles persist with short secretarial tenures, while vested political interests obstruct institutional development.

Donor Involvement: Donors design most programs and broadly influence operations. International financial institutions dictate (*directly or indirectly*) to major ministries through consultants and funding. Moreover, the World Bank and the IMF's roles in BISP raise concerns. Donor programs often limit institutional and individual capacity development.

Economic Issues: Pakistan's irregular, region-specific development has been unsuccessful in reducing poverty effectively. Government overreach in markets generates blockades to social inclusion, further hindering poverty mitigation efforts.

What Should Be Done to Curb Poverty?

- Sustainable poverty alleviation requires a two-pronged strategy: sustained economic growth and social inclusion. As illustrated by poverty graduation strategies, economic growth must translate into productive capacity building.
- Regional disparities demand attention – high poverty in Balochistan requires targeted interventions. Economic growth should integrate every corner through region-specific solutions.
- When social protection contributes 15% to household income, it substantially improves well-being. Therefore, all philanthropic organizations should coordinate integrated efforts toward poverty alleviation. Social protection measures must align with the growth agenda to boost professional capacity and labor productivity.
- Decentralization of social protection programs would increase effectiveness through provincial integration.
- Donor involvement must respect national integrity, focusing on sustainable development over isolated projects serving political interests. The technical capacity of government institutions needs to be enhanced through institutional development and good governance practices. Short secretarial tenures undermine program continuity and require structural reform.

In conclusion, a comprehensive, integrated approach is essential – disintegrated efforts must be channeled into a virtuous cycle of sustainable societal and economic growth. Only through coordinated strategies linking social protection with economic opportunity can Pakistan achieve meaningful poverty eradication.



Conclusion

The Pakistani economy is at a critical juncture, exhibiting a fragile recovery built on the back of fiscal consolidation and a rebound in industrial activity. The reduction in interest payments has provided crucial breathing room, allowing for increased development spending. However, this positive trend is shadowed by significant structural weaknesses. The external account is deteriorating rapidly due to an import surge and an export collapse, making the economy vulnerable to shifts in remittance flows. Furthermore, the surge in poverty alongside increased social spending exposes the deep-seated failures of the current social protection framework, which is criticized as donor-driven, poorly implemented, and focused on temporary relief rather than sustainable poverty graduation.

A two-pronged strategy is essential for sustainable and inclusive growth. This requires: 1) fostering broad-based economic growth that translates into productive capacity, and 2) fundamentally overhauling social protection programs to align with a graduation strategy. This involves decentralizing efforts to the provincial level, ensuring donor alignment with national priorities, curbing leakages, and building institutional capacity. Only through a comprehensive, integrated approach that links social safety nets with genuine economic opportunity can Pakistan navigate its current challenges and achieve meaningful, lasting poverty eradication.



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