

Geopolitical Disruptions and Pakistan's Export Vulnerability

Pakistan's economic history shows a deep-rooted connection with shocks coming from beyond its borders. From constantly developing reactive policies to struggling to effectively implement and sustain them, Pakistan's economic infrastructure has become one of crisis management. A major challenge Pakistan has historically faced is that of long-term sustainable reforms.

It does not take a deep dive into Pakistan's trade and export structure to understand that its exports are highly concentrated within a few goods and services. Another challenge of Pakistan's exports is the very limited buyer pool for its exports.

Export and Trade Environment

The share of exports in total GDP has been hovering between 10 to 11% for many years, showing a lack of development. Even though the ratio of total trade to GDP is higher at around 28%, Pakistan still relies heavily on limited export products and services. Imports consistently exceed exports, leading to a persistent trade imbalance.

Despite textiles being 60% of total exports, it contributes only 8.5% to total GDP. In recent decades, exports have steadily been declining as a share of GDP. In the 1990s, exports stood at around 15% of GDP and have now fallen to around 10%. This ratio is among the lowest among similar developing economies.

Pakistan in Regional Perspective

Compared to other countries in the region, Pakistan's export performance is still relatively weak, both in size and in how diversified it is.

- Bangladesh is also heavily dependent on textiles, but it has managed to perform much better in that same sector. Its exports contribute a larger share to GDP. Its ready-made garment sector accounts for upwards of 84% of total exports.
- India has a well-diversified portfolio of exports which spans across multiple sectors. Due to this, its export-to-GDP ratio is much higher, almost double that of Pakistan. This avoidance of relying too heavily on a select few industries helps to reduce risk.

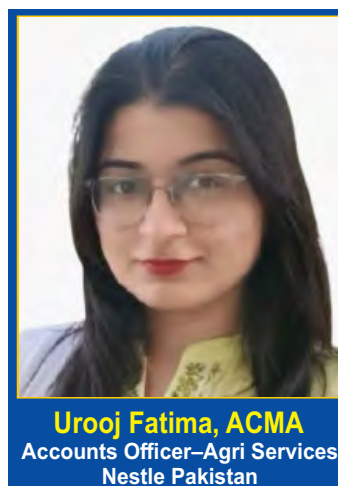


Table 1: Pakistan Export Structure

Sector	Share in Exports	Key Products	Key Risk
Textiles	60%	Garments, yarn, fabrics	High dependence
Agriculture	7–9%	Rice, cotton, mangoes	Climate risk
IT Services	3–4%	Software, freelancing	Growth potential
Others	25%	Leather, chemicals, sports	Moderate

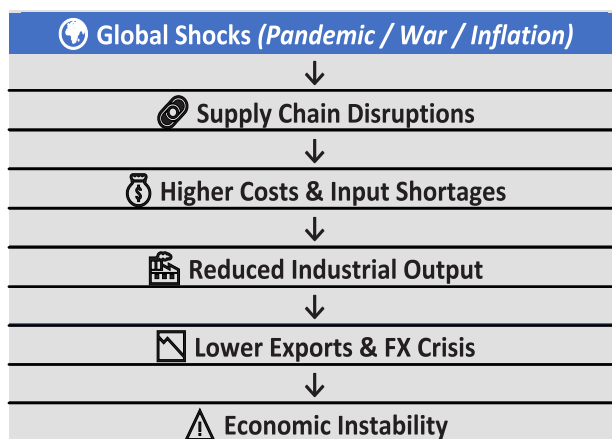
Table 2: Regional Comparison

Country	Export to GDP (Estimated)	Export Structure	Strength
Pakistan	10–11%	High Dependence + Low Performance	High Vulnerability
Bangladesh	13%	High Dependence + High Performance	Highly Specialized
India	22%	Low Dependence + High Diversification	Diversification
Sri Lanka	27%	Moderate Dependence + Strong Export Ratio	Balanced Model

- Sri Lanka's export base has developed a more balanced approach. Textiles are still a major portion of its economy, like its other South Asian peers, but the country has developed a more niche base for branded apparel. Its export-to-GDP ratio is one of the highest in the region.

While some countries succeed through specialization and others through diversification, Pakistan has yet to achieve either effectively. Its vulnerability to shocks is deep rooted in its trade structure.

Trade Vulnerability Cycle



Case Studies: Impact of Global Shocks

- 1) **COVID-19 and Russia-Ukraine War Disruptions:** Geopolitical disruptions like the COVID-19 pandemic and Russia-Ukraine escalations almost immediately impacted the global supply chain, delaying imports and exacerbating the costs for raw materials. These disruptions triggered a sharp increase in global energy and raw material prices. At the same time, Pakistan faced a foreign exchange crisis, which restricted the import of essential inputs such as cotton, dyes, and machinery. These directly affected Pakistan's largest export sector, and many textile units were forced to operate below capacity, some textile mills were operating below 50% capacity after failing to secure Letters of Credit.
- 2) **Demand Shocks in Export Markets:** Pakistan's export portfolio has traditionally been very limited, but so has its range of destination markets. The exports have mainly been concentrated in countries such as the US, UK, Germany, and Spain, showing a lack of geographic diversification in its already inadequate export portfolio. This lack of diversified consumer base causes instability and major fluctuations in exports, highlighting over-dependence on cyclical demand rather than secure and well-established markets.

- 3) **US-Pakistan Tariff Barriers:** In 2024, when the US introduced its reciprocal tariffs policy, Pakistan was charged with a tariff rate of 29%. Initially, Pakistan tried to correct the balance of trade by increasing its imports from the US. Later, the rate was re-negotiated and reduced to 19% by the US. This exchange highlighted how dependent Pakistan's economy is on preferential treatment and diplomatic relations.

- 4) **Red Sea and Suez Canal Disruptions:** The political tensions in the Red Sea area in 2023 led to many challenges for global shipping and maritime channels. Reports from UNCTAD state that the disruptions in the Red Sea and the Suez Canal resulted in a reduction of transit by more than 40% during peak times. These disruptions impacted transport costs as well as insurance charges for freight globally. Over 90% of Pakistan's trade is seaborne so this immediately impacted the costs, disproportionately affecting Pakistani exporters especially ones in the textiles industry.

Adapting to Disruption

Over the years, the government of Pakistan has proposed various short-term measures as well as long-term policies. These policies have had varying degrees of effectiveness. The COVID-19 period led to various export facilitation packages, including subsidized energy tariffs, concessional financing, and tax rebates.

The State Bank of Pakistan (SBP) expanded various financing schemes:

- *Temporary Economic Refinance Facility (TERF)*
- *Export Finance Scheme (EFS)*
- *Export Import (EXIM) Bank*

These initiatives helped firms maintain operations and invest in capacity despite rising costs.

Initiatives like URAAN Pakistan (2024–29) were also introduced, which aimed to:

- *Promote export diversification*
- *Encourage value addition*
- *Expand IT and non-textile sectors*

In the wake of an energy crisis, the government tried to ensure competitively low energy prices for the textile industry. However, fiscal constraints and IMF conditions made such measures unsustainable. This forced withdrawal of many policies and created uncertainty for exporters.

Implications for Accounting, Auditing, and Taxation

1) Accounting and Auditing Standards

Inventory and Impairment (IAS 2 & IAS 36): Under IAS 2, inventories are supposed to be recorded at the lower of cost or net realizable value. In a situation where export prices fall due to instability, firms may have to write down inventory values. This is a major point for Pakistan's textile exporters, since they are operating in an industry where prices shift quickly according to the latest trends and climate. IAS 36 is also relevant for a company that is heavily dependent on exports. Especially exporting to limited markets, since instability in any of its major destination markets can directly impact the exporter. They may need to reassess the value of its assets.

Financial Instruments (IFRS 9): IFRS 9 requires companies to account for expected credit losses (ECL). In uncertain global conditions, the risk of default increases especially when dealing with foreign buyers. This makes estimation more difficult and more conservative.

Exchange Rate and Going Concern (IAS 21 & ISA 570): Exchange rate movements are another major factor. Under IAS 21, fluctuations in currency values directly affect financial statements. Given how much the Pakistani Rupee has depreciated in recent years, this has had a noticeable impact on exporters' reported performance. ISA 570 (Going Concern) also states that in conditions like these which can cause much uncertainty, auditors need to assess whether such disruptions could threaten a company's ability to continue operating.

2) Taxation Implications

Income Tax Framework (ITO 2001): The Final Tax Regime under Section 154 is meant to ease tax-related compliance for exporters and to encourage inflow of foreign exchange during periods of external stress. Sections 65A and 65B of ITO 2001 provide tax credits for industrial undertakings and for investment in plant and machinery. These credits support exporters who are trying to meet their operational capacity even during global disruptions.

Sales Tax Framework (STA 1990): Exports are treated as zero-rated under Section 4 of the Sales Tax Act 1990. This allows firms to claim refunds on input taxes that they paid during production. The aim is to make exports more competitive internationally by removing the tax burden from exporters.



Practical Challenges

In practice, State Bank of Pakistan and Ministry of Finance reports state that external shocks amplify structural weaknesses and cause a delay in refund processing. During 2022–2024, exporters faced delays in sales tax refunds, struggled with liquidity shortages, and had to increase working capital requirements due to rise in freight costs and insurance premiums.

Internal Control System (ICS) in Pakistan's Export Sector

Internal control systems are those policies and procedures which are set in place by an organization to ensure smooth and efficient operations, compliance with local and international laws and regulations, and prevention of fraud and misstatement in accounts or inventory tracking.

In Pakistan's export sector, internal control weaknesses are frequently observed due to weak governance and lack of automation.

Key Weaknesses in Internal Controls

The main concerns affecting Pakistan's textile sector are:

- Poor tracking of raw materials
- Weak warehouse controls
- Lack of real-time inventory systems
- Lack of integrated ERP systems

Export processes require strict documentation. Weak internal controls result in:

- Delays in Letter of Credit (LC)
- Rejected export claims
- Foreign exchange settlement issues

Many export firms are still relying on semi-manual accounting systems, leading to incomplete transaction records, delayed financial reporting, and errors in cost tracking of exports. Since foreign buyers require financial transparency, weak internal controls become a significant hindrance for such exporters.

Internal Control and Financial Reporting

Weak internal controls directly affect financial reporting quality.

Conclusion

An overview of Pakistan's economy shows both the lack of diversity in its exports, and the fragility of its policy implementation. A major internal issue Pakistan faces is political unrest, where each new governing party brings a new set of policies. On the external front, organizations like the IMF and World Bank demand reforms and new policies to issue grants. These factors all affect the proper implementation and continuation of Pakistan's policies, causing delays and lack of confidence.

Many economies that wish to grow are now looking to expand globally through diversifying their exports or specializing in certain industries. Pakistan has yet to achieve either. Although its textile industry is the backbone of its

Internal Control Issue	Financial Reporting Impact
Weak inventory tracking	IAS 2 misstatements
Poor LC management	Revenue recognition errors
Currency exposure unmanaged	IAS 21 volatility errors
Weak credit policies	IFRS 9 underestimation of losses

exports, it is not something that is unique to Pakistan. As mentioned above, many South Asian countries alone have textile as their top export.

In order to improve its structure, Pakistan must adopt a balanced strategy, which is adaptive to external shocks. Rather than scrambling to correct the impact that geopolitical tensions leave on the economy, Pakistan should look to develop its trade and export sector with a strong consistent base of operations, whether that is by diversifying into other industries or simply by specializing in what we do best.

About the Author: Ms. Urooj Fatima is an Associate member of ICMA, also holding an M.Com degree from Hailey College of Commerce session 2019-2023. Her research publication titled "FinTech Based Financial Inclusion and its Impact on the Performance of Banking Sector: Empirical Evidence from Pakistan" was published in the Journal of Social Science Archives (Vol 3, Issue 2, 2025). She is currently working as an Accounts Officer at Nestle Pakistan.

