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"DYNAMICS OF PAKISTAN'S ECONOMY AS A MUSLIM COUNTRY IN THE CONTEXT OF THE GLOBAL ECONOMY: A LITERATURE REVIEW"

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ABSTRACT

This study aims to analyze the economic condition of Pakistan, identify its challenges and opportunities, and examine Pakistan's role in the global economy and Islamic economy. The study employs a qualitative approach using a literature review method by analyzing relevant academic journals, books, and research reports. The findings indicate that Pakistan possesses significant economic potential supported by its strategic geographical location, demographic dividend, and opportunities for regional economic integration through international cooperation initiatives, including the China–Pakistan Economic Corridor (CPEC). Pakistan's economy is primarily supported by the agricultural, industrial, and service sectors, which play important roles in national economic growth. However, the country continues to face several structural challenges, including high inflation, external debt, political instability, corruption, and weak governance. From an Islamic economic perspective, strengthening zakat, waqf, and Islamic financial institutions may contribute to a more inclusive and sustainable economic development model. Therefore, comprehensive economic reforms and stronger regional cooperation are essential to enhance Pakistan's competitiveness in the global economy.

INTRODUCTION

Pakistan is a developing country in South Asia with the fifth largest population in the world, which is around 247 million people based on the 2023 census, which places it as one of the countries with the highest population density globally. The structure of Pakistan's economy is dominated by three main sectors, namely agriculture, industry, and services. Since the 1960s, the agricultural sector has been the main backbone of the economy, although its contribution has now declined to about 25% of GDP, while the industrial sector is around 20% and the service sector is the largest contributor to national GDP(Kamal & Fatima, 2023).

However, Pakistan's economy still faces various structural problems such as high inflation, trade balance deficits, fiscal deficits, and dependence on external debt and international financial institutions such as the IMF and the World Bank(Iqbal, 2024). In addition, the unemployment rate, labor market limitations, and political and security instability have also worsened the investment climate. Additional risks in the form of natural disasters and climate change, such as the major floods of 2010 and 2022, also further weaken national economic stability(Life, 2026).

On the other hand, Pakistan has a very strategic geographical position because it is at the crossroads of South Asia, Central Asia, the Middle East, and close to China, thus making it an important actor in regional and global economic dynamics. This position is strengthened by the China–Pakistan Economic Corridor (CPEC) project as part of the Belt and Road Initiative (BRI), which has the potential to make Pakistan an international trade and transit hub(Nawaz et al., 2024).

In addition, Pakistan also has great potential in the development of Islamic economics and Islamic finance. The country is one of the important case study centers in the development of the Islamic financial system in the member countries of the Organization of Islamic Cooperation (OIC), along with Malaysia, Indonesia, and Saudi Arabia(Sholeh & Singh, 2025). Pakistan's economic ties with Gulf countries, especially Saudi Arabia and the United Arab Emirates, are also very significant through labor remittances which are the country's main source of foreign exchange (Nadeem et al., 2019).

Although various studies have discussed the state of Pakistan's economy in terms of economic growth, international trade, and Islamic financial development, most of the research still focuses on certain aspects separately. Studies that integrate Pakistan's economic condition, its strategic position in the global economy, and its potential for Islamic economic development are still relatively limited. Therefore, this study aims to analyze the state of Pakistan's economy, identify the challenges and opportunities it faces, and examine Pakistan's role in the global economy and the Islamic economy.

METHODS

This study uses a qualitative approach with a literature review method (*literature review*). This method is carried out through searching, selection, and critical study of various relevant scientific sources, such as journals, books, and research reports related to research topics. Literature reviews are used to critically examine the knowledge, ideas, and findings contained in the academic literature, as well as formulate theoretical and methodological contributions to a particular topic(Ulhaq, 2018)

The research stages are carried out through several processes, namely determining the focus of the study, collecting relevant literature, selecting sources based on credibility and content relatedness, and then analyzing the content of the literature in a descriptive-analytical manner. The selected literature was then synthesized to find patterns, relationships between concepts, and research gaps. All sources used are listed in the bibliography with a consistent citation format, for example APA Style, so that the writing is more credible and in accordance with scientific principles(Mardin et al., 2020).

RESULT AND ANALYSIS

1. Overview of Pakistan's economy

Pakistan is the second largest Muslim-majority country in the world that occupies a strategic position in the global economy, especially in the context of the Islamic economy. Ghafoor et al. (2025) explained that Pakistan has a number of comparative advantages, including its strategic geographical position at the intersection of South, Central, and Middle East, the demographic bonus of a large young population, and a strong agricultural base to support the domestic economy. The information technology and telecommunications sector is also considered to have great potential in absorbing young workers and encouraging digital economy transformation in the future(Ghafoor et al., 2025).

Nevertheless, Pakistan's economy also faces various structural challenges that are quite serious. The main obstacles to Pakistan's economic growth include prolonged political instability, weak governance, widespread corruption, and a sharp inter-regional gap between urban and rural areas. In addition, the small and medium business sector, which accounts for more than 30 percent of national GDP, still faces serious obstacles in the form of limited access to financing and complex regulations, thus hindering their optimal contribution to the economy(Dogar, 2023).

From the perspective of Islamic economics, it highlights that even though Pakistan has declared itself as an Islamic republic since 1949, its economic architecture is still entangled in interest-based financial instruments (riba), asymmetrical distribution of wealth, and governance frameworks that are not fully aligned with the principles of maqasid al-Sharia. The macroeconomic instability and income inequality that occurred are considered not just technical failures of economic management, but are a reflection of the application of Islamic economic principles which are still partial and have not been fully institutionalized.

To affirm that Pakistan actually has a great opportunity to drive economic recovery and growth through the expansion of manufacturing capacity, the development of renewable energy, and the deepening of regional economic integration. However, these opportunities are still hampered by the high external debt burden, inefficient tax system, inadequate infrastructure, and security threats that are still a problem. Therefore, comprehensive structural reforms, including the strengthening of Islamic value-based economic institutions such as zakat, waqf, and the Islamic financial system, are considered key for Pakistan in realizing sustainable, just, and sovereign economic development(Watto, 2026).

2. Major sectors of Pakistan's economy

Pakistan's economy is supported by three main sectors, namely agriculture, industry, and services, each of which has a strategic role in supporting the national economic growth.

Agriculture Sector has been the backbone of Pakistan's economy since its independence in 1947. Dogar (2023) explains that agriculture contributes about 19.53 percent to Pakistan's GDP and absorbs more than 37 percent of the national labor force. The sector's leading commodities include wheat, rice, cotton, and sugarcane which are not only a source of domestic food security, but also the main raw materials for the processing and textile industries. Although its relative contribution to GDP has declined as other sectors have developed, Ghafoor et al. (2025) assert that agriculture remains the main breadth of the rural economy and a source of livelihood for the majority of Pakistan's poor. However, the sector still faces serious challenges, including low adoption of modern agricultural technologies, limited irrigation infrastructure, significant post-harvest yield losses, and vulnerability to climate change that threatens long-term productivity(Ghafoor et al., 2025).

Industrial Sector, particularly textiles, is the driving force of Pakistan's exports and the most dominant manufacturing sector. The textile industry has the longest production chain with potential added value at every stage, from cotton, spinning, fabrics, dyeing, to apparel, making it the most intensive sector with backward and forward linkages compared to other sectors. The industry contributes about 60 percent of the total national exports and absorbs about 40 percent of Pakistan's industrial workforce. Sattar (2023) added that although Pakistan is one of the largest cotton producers in the world, its textile sector still faces obstacles in the form of dependence on the export of low-value products such as raw cotton and yarn, as well as weak adoption of modern technologyAli (2025)In its study on the digital transformation of Pakistan's textile industry, it emphasized that the application of Internet of Things (IoT)-based technology and sustainable production is a must for Pakistan's textile industry to be able to compete in an increasingly competitive global market(Petrillo et al., 2024).

Service Sector now the largest contributor to Pakistan's GDP, noting that the services sector has taken over the dominant position in Pakistan's economic structure in line with the urbanization and modernization of the economy that has taken place over the past few decades. This sector includes financial services, telecommunications, trade, transportation, and information technology which continues to grow rapidly. The information and communication technology sector has great potential in absorbing Pakistan's growing young workforce, as well as being a gateway for a more inclusive and sustainable digital economy transformation. Therefore, the synergistic strengthening of these three sectors through policy reforms, infrastructure investment, and human resource capacity building is considered crucial for Pakistan to drive more stable and globally competitive economic growth.

3. Pakistan's economic challenges

Pakistan's economy faces a variety of complex and interrelated structural challenges, in a study published in *Asia Pacific Law & Policy Review* identified that Pakistan's main challenges include high inflation, persistent fiscal deficits, low investment in key sectors, currency depreciation, corruption, political instability, as well as widespread social inequality. These challenges are not new, but structural and have taken root decades ago.

On the fiscal and debt side, Pakistan's economic problems were further exacerbated by the massive floods in 2022 that drained the government's budget due to recovery efforts, thereby worsening the budget deficit, increasing public debt, and pushing inflation to record highs. Crop failures also weaken export earnings and exacerbate the current account deficit, prompting the government to mobilize foreign exchange reserves to meet external debt obligations.

Regarding inflation, Pakistan faces serious structural weaknesses in the form of prolonged political instability, which results in inconsistent economic policies and deteriorates governance. This condition is exacerbated by weak tax revenues, where Pakistan is recorded as one of the countries with the lowest ratio of tax revenues to GDP among IMF debtor countries, which is around 10 percent. As a result, the government does not have enough funds to modernize state-owned enterprises, improve public services, or pay debts on time, thus getting stuck in a cycle of deficit and debt that continues to repeat.

From the perspective of Islamic economics, Watto (2026) assesses that the inequality in the distribution of wealth that occurs in Pakistan is a reflection of the systematic non-application of Islamic redistribution instruments such as zakat and waqf. Meanwhile, widespread corruption and bureaucratic inefficiencies have hampered the influx of foreign direct investment that is urgently needed to drive long-term economic growth.

Nonetheless, the settlement of external debt obligations by 2024 is a crucial stepping stone for Pakistan in achieving macroeconomic stability and initiating structural reforms that have been hampered. Ghafoor (2025)asserting that without comprehensive reforms that include improving the tax system, reducing dependence on fossil energy imports, and strengthening the investment climate, Pakistan will find it difficult to get out of the trap of long-standing economic challenges.

4. Pakistan's position in the global economy

Pakistan occupies a strategic position on the global economic map, especially in the South Asian region. Pakistan is located at the crossroads of global trade routes connecting South Asia, Central Asia, the Middle East, and Africa, making it a potential hub between various dynamic economic regions. This position prompted Pakistan to shift from a purely security-focused foreign policy to a stronger emphasis on economic diplomacy and regional economic integration(Nawaz et al., 2024).

However, this potential has not been utilized optimally. Pakistan's trade-to-GDP ratio is only 30 percent, the lowest among developing countries of its size, indicating that there is still room for international trade growth(Nawaz et al., 2024). This condition is exacerbated by prolonged political instability, resulting in inconsistent economic policies as well as difficulties in governance that hinder the optimization of Pakistan's trade potential in the global market(Ghafoor et al., 2025).

In the context of regional initiatives, Pakistan has taken strategic steps through various multilateral cooperation. Initiatives such as the China-Pakistan Economic Corridor (CPEC) and membership in the Shanghai Cooperation Organization (SCO) offer real opportunities for Pakistan's geo-economic growth. (Nawaz et al., 2024). CPEC provides Pakistan with a great opportunity to optimize its geo-economic position, especially through the development of the Port of Gwadar which is the gateway for Central Asian countries that do not have direct access to the sea to the Indian Ocean. Pakistan is also involved in the Central Asia Regional Economic Cooperation (CAREC) program and the Turkmenistan-Afghanistan-Pakistan-India (TAPI) gas pipeline project, which reflects Pakistan's aspirations to strengthen regional economic ties and increase its geo-economic influence(Nawaz et al., 2024).

Through its relations with the Islamic world, Pakistan has significant economic ties with the Middle East region. Pakistan has signed free trade agreements with Gulf Cooperation Council (GCC) countries, including Saudi Arabia, the United Arab Emirates, Kuwait, Qatar, Bahrain, and Oman, in an effort to reduce the trade deficit and strengthen economic ties in the region. (Nawaz et al., 2024). Remittances from about two million Pakistanis working in Saudi Arabia reach $6.5 billion per year, making it one of the most important sources of foreign exchange for Pakistan's economy(Nawaz et al., 2024). Watto, (2026)adding that Pakistan's economic ties with Muslim countries in the Middle East also open up opportunities to strengthen cooperation based on Islamic economic principles, including the expansion of Islamic financial instruments and cross-border halal investment.

To be able to maximize its position in the global economy, Pakistan needs comprehensive reforms. Economic openness has proven to provide benefits in the form of specialization, expansion of market access, acquisition of new technologies, and formalization of the economy, thus presenting a real opportunity for Pakistan to improve its performance in the global market. Pakistan needs to harness the potential of digital transformation, renewable energy development, and deepening regional economic integration as key strategies to strengthen its position and competitiveness in the ever-growing global economy.

5. Pakistan's economic opportunities and prospects

Pakistan has a wide range of strategic opportunities that can be leveraged to drive long-term economic growth. Pakistan has a great opportunity to drive growth through expansion of manufacturing capacity, digital transformation, renewable energy development, and deepening regional economic integration which, if properly utilized, can be a key driver of economic recovery.

One of Pakistan's biggest opportunities lies in infrastructure development through CPEC. China's investment in CPEC infrastructure projects worth $13.58 billion has contributed to improved connectivity, job creation, and GDP growth, with GDP growth estimated at least 2 percent due to ongoing infrastructure development. Energy projects under CPEC are also expected to drive a 3.5 percent increase in GDP thanks to China's $60 billion investment, while creating about 30,000 jobs in the energy sector. The development of the Port of Gwadar is projected to be able to handle cargo capacity of up to 400 million tons by 2030, create around 40,000 jobs, and drive GDP growth by 3 percent through trade activities and foreign investment(Nadeem et al., 2019).

In terms of regional trade, Pakistan's opportunities are also huge. The potential for bilateral trade between Pakistan and India is estimated to reach 37 billion US dollars, while Pakistan's bilateral trade target with Iran is set at 5 billion US dollars in the five-year trade cooperation plan for 2023-2028. Pakistan's membership in the Shanghai Cooperation Organization (SCO) with India and Central Asian countries opens up opportunities for regional economic integration which, if realized, will benefit more than 1.5 billion people in Afghanistan, Pakistan, and India(Nawaz et al., 2024).

Based on the perspective of Islamic economics, Pakistan's opportunities can also be seen from the dimension of Islamic finance. Affirmed that the systematic implementation of Islamic redistribution instruments such as zakat and waqf, together with the expansion of the sharia-based financial system, is a viable path to encourage more inclusive and equitable economic growth in Pakistan. Investment in the renewable energy sector is also a strategic opportunity as it can reduce Pakistan's dependence on expensive fossil fuel imports, while opening up new jobs in green industries and strengthening national energy security.

To realize these opportunities, comprehensive and planned reforms are needed. A balanced and holistic approach that harnesses the positive impact of various economic initiatives while addressing challenges such as transparency, debt sustainability, and environmental impact is needed for Pakistan to achieve resilient and sustainable growth, macroeconomic reforms that include improving the tax system, governance, and investment in human capital are key prerequisites for Pakistan to convert its economic potential into a real and even growth(Burugupally, 2024).

Based on the results of the study, Pakistan has great economic potential supported by its strategic geographical location, demographic bonus, and regional economic integration opportunities. However, various structural challenges such as inflation, external debt, political instability, and weak governance remain major obstacles. In the context of Muslim-majority countries, strengthening the Islamic economy through zakat, waqf, and sharia finance instruments can be an alternative to encourage more inclusive and sustainable economic development.

CONCLUSION

Pakistan is a developing country that has a strategic position in the global economy because of its geographical location connecting South Asia, Central Asia, and the Middle East. Pakistan's economy is supported by the agricultural, industrial, and service sectors, each of which has an important contribution to the national economic growth. Despite the great potential in the form of demographic bonuses, CPEC projects, regional economic integration, and Islamic economic development, Pakistan still faces various structural challenges such as inflation, external debt, political instability, corruption, and low governance effectiveness. These challenges hinder the optimization of their economic potential. From an Islamic economic perspective, strengthening zakat, waqf, and sharia finance instruments can be an alternative to create more inclusive, equitable, and sustainable economic development. Therefore, comprehensive economic reforms, improving the quality of human resources, and strengthening regional economic cooperation are important factors in supporting Pakistan's future economic growth.

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