


A man with a beard and glasses, wearing a white kurta, is holding a large Pakistani flag. He is standing on a grassy area with a building and trees in the background. The flag is green and white with a white crescent and star. The man is looking up at the flag.

# PAKISTAN'S MULTIPLE CRISES AND THE IMPACT ON BUSINESSES



The dispute between former Prime Minister Imran Khan, Prime Minister Shehbaz Sharif's Government and the powerful military has become one of the most serious political crises in Pakistan's recent history. Instability, violent civil unrest, and extreme political polarisation have only heightened since April 2022, when Khan was removed as Prime Minister. The prevalence of social unrest is likely to continue in Pakistan in the second half of 2023 and beyond. In addition to the political crisis, the country is facing multiple crises: climate, terrorism and economic. The country has been hit by unprecedented floods that have submerged a third of the country, and the return of the Taliban to power in Afghanistan creates heightened insecurity along Pakistan's borders.

While the International Monetary Fund (IMF) is considering a bailout package to prevent Pakistan's economy from collapsing, the risks of soaring inflation (officially at 36.4 percent in April 2023) and a default on foreign debt, could pose further challenges to Pakistan's economy. To avoid sovereign default, Pakistan needs continued support from the IMF, as well as financial assistance from China, Saudi Arabia, and the United Arab Emirates - Pakistan's closest allies. If Pakistan ultimately defaults, the country's imports could be interrupted, leading to shortages of some essential goods and commodities, which would likely lead to public discontent, civil unrest and even another change of government. An economic crisis would most likely and very quickly lead to further political instability.

Given Pakistan's demographic profile and internal security threat, the resulting crisis could lead to different scenarios. As a result, companies based in, or doing business with Pakistan should closely monitor developments in the country, understand the risks and threats, review their crisis management processes, and business continuity plans, and analyse the impact of different scenarios on existing systems, and likely consumer demands in Pakistan. This global risk monitoring and strategic foresight paper is an essential read for business leaders with operations and interests in Pakistan.

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# PAKISTAN'S MULTIPLE CRISES AND THE IMPACT ON BUSINESSES

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## POLITICAL CRISIS

Imran Khan became a national figure in Pakistan after leading Pakistan to its first and only cricket world championship in 1992. In 1996, Khan founded the Pakistan Tehreek-e-Insaf (PTI) or Pakistan Movement for Justice and in August 2018, Khan was elected as the 22nd Prime Minister of Pakistan as a leader of a coalition government and with the support of the Pakistani Army, which remains the most important institution of Pakistan since independence in 1947. However, during Khan's tenure, certain decisions and attitudes created tensions with the Pakistani Army, which eventually withdrew its support for Khan. Khan also lost his parliamentary majority when his allies quit the coalition government. Several opposition parties joined forces to move a no-confidence motion against Khan, accusing him of:



Poor performance in the management of the Pakistani economy, which was badly damaged after the COVID-19 pandemic.



Mismanagement of foreign policy. US-Pakistan relations were affected by Khan's proximity and trips to Russia.



Failure to deliver on promises to fight corruption.

On 10 April 2022, Khan was removed as Prime Minister of Pakistan by a no-confidence motion, days after Khan blocked a similar attempt. The motion's approval came after Pakistan's Supreme Court decided that Khan acted unconstitutionally by previously blocking the process and dissolving parliament. On 11 April 2022, Pakistan National Assembly elected a new prime minister: Shehbaz Sharif, from the Pakistan Muslim League, and brother of former Prime Minister Nawaz Sharif.

Since Khan's removal, he has encouraged his supporters to hold rallies and protests to pressure parliament to hold early elections. Several episodes of mass protests, attacks on military and government buildings, and violent repression by the Pakistani Army have raised security and human rights concerns in Pakistan. In return, the Government and military establishment have persecuted PTI members and brought nearly 160 corruption and sedition

charges against Khan to ensure that he cannot be elected prime minister again. Among others, Khan has been accused of making a quid pro quo deal with a major Pakistani real estate tycoon that cost the Pakistani treasury more than US\$ 239 million.

The last outbreak of mass protests and violence took place in May 2023. On 09 May, Khan was arrested when attending a corruption case, sparking nationwide protests and the deployment of the Pakistani Army, which arrested thousands and killed at least ten people. On 12 May, Khan was released and has escalated its criticism towards Pakistan Government and the military, accusing them of ordering his imprisonment and the assassination attempt. Pakistan's Government has accused PTI of inciting violence and Khan of orchestrating the 09 May protest and attacks on military facilities.

On 26 June, the Pakistan Army removed three senior officers, including a Lieutenant General, for failing to prevent violent attacks on military installations in May by Khan's supporters. The army has claimed that the burning of military installations was planned in advance by PTI party leaders and has named Khan in at least two criminal cases as an accomplice to the violence. Strict action has also been taken against 15 other army officers, including major generals and brigadiers. At least 102 people are currently facing military trials related to the violence that erupted in May.

*The protests have affected business operations and transport, disrupting supply chains. Businesses have also suffered financial losses as a result of material damage caused by the riots and the Pakistani security forces' response. Property damage has included looting, broken windows, and destruction of shops and warehouses.*

## Consequences for businesses

For example, the damage from violent protests in Islamabad and Lahore was around US\$ 0.9 million and US \$3 million respectively. In addition, Pakistani security forces blocked or attacked the permits of PTI supporters in the Punjab region, particularly in the capital Lahore, where Khan lives.

All this violence has had a disruptive effect on business in Pakistan and could have an impact on the supply chains of European companies.

**As the prevalence of civil unrest is likely to continue in Pakistan in 2023 and beyond, companies with business interests in Pakistan should invest in robust and comprehensive risk monitoring mechanisms that provide strategic foresight and alerts on potential event triggers, enabling the reallocation of business resources to avoid the worst impacts of emerging civil unrest risks in Pakistan.**

Pakistan's next general election is expected to be held in October 2023, and Khan continues to call for both provincial and general elections to be held soon, which he could win due to his popularity in many locations. However, if Khan is found guilty in any of the various cases against him or faces a military trial, it will most likely disqualify him from participation in the elections.

*Even if Khan participates in the October 2023 Pakistan general election, the Pakistani Army is likely to manipulate the ballot to prevent the PTI from governing again.*

Therefore, even though the popularity of the current ruling coalition in Pakistan has declined due to its fiscal reforms, which have led to an increase in the cost of living, the current Government is likely to win

the upcoming election. If the law-and-order situation deteriorates, the general elections could also be postponed.

As political instability and unrest continues, there is a small risk that the Pakistani Army will attempt to intervene taking control of the country. Military intervention again in Pakistan's politics would destroy Pakistan's constitutional system and likely result in a technocratic rubber stamp parliament.

Pakistan has not experienced such a major political and democratic crisis since 2008, when democracy was restored after years of dictatorship under Musharaff.

*For these reasons, European business leaders with interests in Pakistan should monitor and understand the complexity of the social and political landscape in Pakistan and conduct detailed scenario planning for possible eventualities, including the PTI coming back to power and pursuing populist economic policies, or a Pakistani Army intervention. Desktop, scenario-based exercises are valuable to ensure success and mitigate the most pressing risks in Pakistan.*





## HOW THE ECONOMIC CRISIS IN PAKISTAN IS AFFECTING BUSINESS?

The International Monetary Fund (IMF) had a US\$ 6.5 billion program with Pakistan that entered into force in 2019 and aims to disburse an additional US\$ 2.5 billion to Pakistan before it ends on 30 June 2023. The IMF is discussing fiscal policy measures to review the agreement.

On 25 June, Pakistan's Parliament approved the government's budget for 2023-24, revised to meet IMF conditions in a last-ditch attempt to unlock more bailout funds. The revised budget was approved a day after Pakistan's Finance Minister Ishaq Dar introduced new taxes, spending cuts, an increase in an oil levy and the removal of all import restrictions - which was one of the IMF's main concerns.

On 26 June, the Central Bank of Pakistan announced a further interest rate increase of 100 basis points to 22 percent. This measure was also in line with the IMF's demands. Since April 2022, Pakistan's Central Bank has raised its key interest rate by 12.25 percent. Businesses with operations in

12.25%

has raised the official interest rate of the Central Bank of Pakistan from April 2022

Pakistan should therefore closely monitor the economic measures to be introduced by the Pakistani Government, consider rising interest rates – which make business debt more expensive – and the impact on business operations and financing, and develop a strategy that incorporates higher debt costs for the foreseeable future.

*The IMF financing is crucial for Pakistan to avoid a default on its external payment obligations during a balance of payments crisis in which Pakistan foreign exchange reserves are insufficient to finance even just four weeks of controlled imports.*



## Pakistan debt

Pakistan announced in January that the United Arab Emirates would provide US \$3 billion in financial assistance, and in April that Saudi Arabia would provide US\$ 3 billion. Long-time ally China has renewed and refinanced its loans with Pakistan. However, it is uncertain whether the Saudi, Emirati and Chinese funding is sufficient, or whether Pakistan will still need more external support.

Pakistan has a large amount of private debt amounting to US\$ 7.8 billion. Much of this debt is in the form of private bonds, such as Eurobonds and global Sukuk bonds. Pakistan also has foreign commercial loans worth almost US\$ 7 billion, which is likely to increase to almost US\$ 9 billion by the end of the current fiscal year. A large part of Pakistan's commercial loans is owed to Chinese financial institutions. Pakistan holds about US\$ 27 billion of Chinese debt.

Pakistan's large external debt carries considerable repayment pressure. From April 2023 to June 2026, Pakistan must repay US\$ 77.5 billion in external debt. For a US\$ 350 billion economy, this is a considerable burden. The main repayments over the next three years are to Chinese financial institutions, private creditors, and Saudi Arabia. The Pakistani authorities hope to convince the Chinese to refinance and roll over debts, something the Government and Chinese commercial banks have done in the past. Even if Pakistan manages to meet these obligations, the next fiscal year will be more difficult, as debt service will amount to almost US\$ 25 billion.

**In 2024-25, Pakistan's debt service is likely to be around US\$ 24.6 billion and in 2025-26, the debt service burden is likely to be at least US\$ 23 billion.**

*To repay its debt and avoid a sovereign default, Pakistan's revenues from exports, foreign direct investment and foreign workers' remittances are vital. However, all three inflows are not expected to keep pace with the import bill and growing pressure on debt repayment. Foreign direct investment is also expected to remain subdued. In recent years, annual investment has averaged US\$ 2 billion, due to the difficult business environment and frequent policy changes. Investor confidence has also been affected by recent government restrictions on capital movements out of the country.*

Pakistan's economic managers have two options for dealing with its external debt burden. The first is to take new loans and seek debt rollovers, especially from its Middle Eastern partners and China, not only to refinance existing debt, but also to obtain new loans if they want to avoid default.

The precise amount Pakistan can borrow will depend on negotiations with the IMF. If the IMF programme is reactivated, the amount will be less than what it would request if the programme were to fail. Alternatively, Pakistan could seek a pre-emptive debt restructuring. This would reduce repayment pressures and save scarce dollars in the economy to finance the country's current account deficit.

The Pakistani Government has met with investment banks and advisors to explore restructuring options. However, for now, officials are reluctant, as a restructuring process will be painful and time-consuming, and because of the political backlash from the associated austerity measures.

## Devaluation of the Pakistani rupee

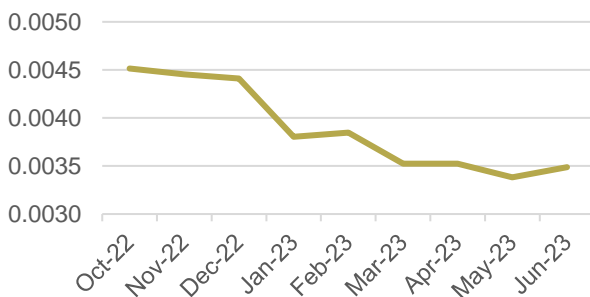
Several factors have contributed to the depreciation of the Pakistani rupee:

-  Trade imbalance
-  Inflation
-  Increased interest rates
-  Debt burden
-  Political instability
-  Lack of foreign investment

The rupee began to depreciate sharply on 26 January when it lost 10.6 percent of its value (24.54 Pakistani rupee, PKR) in the interbank market after the Government removed an unofficial cap on the USD-PKR exchange rate. The removal of the exchange rate cap was one of the IMF's conditions for resuming discussions on the ninth review of the economic package.

Since 26 January, the Pakistani rupee has lost 19.8 percent of its value. This sharp depreciation further highlights the vulnerability of Pakistan's economy, which is constantly at risk.

### PKR to USD Evolution

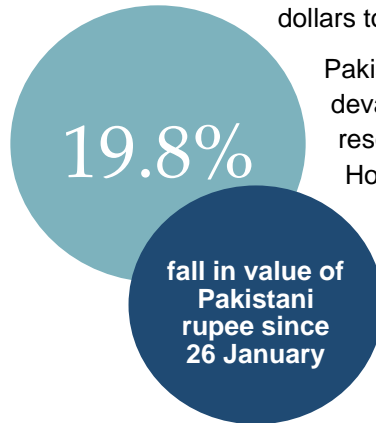


*Exchange rate fluctuations affect interest rates, production levels, prices and employment opportunities.*

Due to higher exchange rates and currency depreciation, more loans will be taken from the IMF to repay the previous ones, and then the country will have to convert a huge amount of rupees into US dollars to repay these loans.

Pakistan's exports will increase due to the devaluation of the currency, so more resources will be exported at a lower price. However, the increase in exports at lower prices and the increase in the price of imports will cause Pakistan's GDP to fall at an accelerating rate.

As the cost of imported materials rise, the cost of doing business, manufacturing and production in Pakistan will become more expensive. Conversely, the devaluation of the Pakistani rupee may have a positive impact on Pakistan-based companies involved in exports, as the price of their products and services will be reduced and demand for their products and services is likely to increase.



## Increased production costs

The persistent inflationary trend together with the continuing devaluation of the Pakistani rupee - which increases the costs of importing goods of all kinds - is exacerbating the rise in production costs and even leading to shortages of raw materials in Pakistan.

Pakistan is a major importer of fertiliser, oil, food, machinery and many raw materials.

As the price of imported goods has risen, the price of raw materials has also risen, and at a faster rate, increasing the cost of production. This affects the profitability, the competitiveness and the operations of companies based in Pakistan or with Pakistani suppliers.

*Businesses with operations or suppliers in Pakistan should therefore closely monitor commodity prices, consider increasing commodity prices in its business continuity plan, and develop a strategy that includes significantly higher raw material costs for the foreseeable future.*

## Inflation

To secure the IMF funding, Pakistan has taken measures such as increasing taxes, removing caps on the exchange rate which has led to the depreciation of the Pakistani rupee, removing subsidies, and raising key interest rates to 21 percent which supposed a record. All these measures have contributed to high inflation in Pakistan.

Pakistan reached an inflation of 36.4 percent in April 2023, with an increase of 2.4 percent from March to April. The persistently high inflation is mainly driven by food prices.

36.4%

inflation was reached in Pakistan in April 2023.

*Food inflation in rural areas has reached 40.2 percent and 48.1 percent in urban areas.*

This has resulted in further impoverishment of the population, which in turn has caused lifestyle shifts among Pakistani citizens and changes in consumption and demand for certain products, which is likely to have an impact on sales and revenues, especially for fast-moving consumer goods (FMCG) companies and their suppliers. Business based or with interests in Pakistan should therefore monitor and analyse trends and behaviours from Pakistani consumers.



## TERRORISM CRISIS

Pakistan faces a constant threat of terrorism due to political instability and a weak counter-terrorism strategy that sacrifices long-term peace to achieve cost-effective security goals, which has encouraged the development of terrorist militias in several parts of the country, particularly in Kashmir and Punjab along the border with India. The return of the Taliban regime in Afghanistan has led to the re-emergence of the terrorist group, Tehreek-e-Taliban Pakistan (TTP), who is violently opposed to the Pakistan military, and which officials in Pakistan say has its central command and training facilities in Afghanistan.

On 30 January, the TTP killed more than 80 people, all but three of them police officers, in the city of Peshawar, near the Afghan border. On 17 February, the TTP killed five people, one civilian and four security officials, in the city of Karachi. Insecurity has increased particularly in the Khyber Pakhtunkhwa and Balochistan regions bordering Afghanistan.

The political, economic, and terrorist crises are developing separately, although they will feed off each other if left unchecked. Pakistan's current approach of deferring IMF demands and implementing half-baked fiscal measures is likely to lead to economic failure, which will fuel public discontent. Political instability is already polarising Pakistani society. Moreover, the Pakistani Government's policy of downplaying the Taliban's support for the TTP will also provoke further terrorist attacks.

Following the Taliban takeover of Afghanistan in 2021, both the Pakistani security forces and conservative sections of the Pakistani population welcomed the withdrawal of Western forces from Afghanistan. However, ongoing clashes between Pakistani and Afghan security forces along the Durand Line and an increase in terrorist attacks in Pakistan have shown the Pakistani government the unpleasant side effects of a Taliban-led regime. The Taliban's military victory in Afghanistan has inspired those who seek to impose Sharia law in Pakistan. Pakistan's practice of supporting jihadist forces has only fuelled the religious fervour of much of its own population. Islamist and jihadist forces in Pakistan are now pressuring the Pakistani government to reaffirm the Islamic character of the country. Apart from a missile strike over Afghanistan in April 2022,

Pakistan has pursued a diplomatic policy to resolve the problem with the Taliban. Knowing that it needs the support of the Afghan Taliban regime to establish a transcontinental trade network with the Central Asian republics, Pakistan is keen to give the Afghan Taliban regime more political space. This ambivalence towards Islamist extremists on the part of the Pakistani government will continue to fuel Islamist radicalism in Pakistan and challenge the authority of the state. As a result, more terrorist attacks in Pakistan can be expected.

Terrorist attacks in Pakistan are not only targeting Pakistani security forces. On 20 January 2022, a terrorist attack killed three bank employees in Lahore.

*Companies with employees working in, and or travelling to Pakistan should ensure 24/7 emergency support systems. This should include real-time monitoring of security incidents, as well as proactive notification to employees of incidents in their vicinity. Travel risk management solutions are equally applicable for travelling personnel, as well as those employees permanently based in Pakistan.*

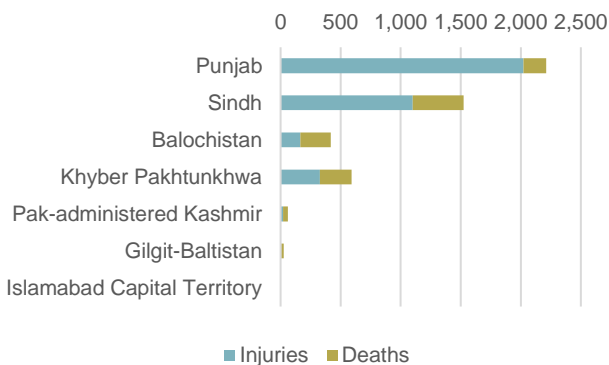


## OTHER RISKS AFFECTING COMPANIES IN PAKISTAN

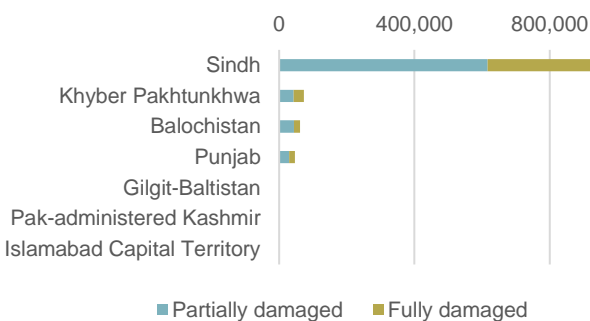
### Climate-related hazards

Pakistan suffered heavy flooding in mid-2022. The flooding sub-merged one third of the country and led to vast destruction of property, road networks, critical infrastructure, displacing effectively 32 million people and killing approximately 1,800 people. The floods affected especially the regions of Sindh, Balochistan and the south of Punjab.

#### Casualties from 14 June to 31 August 2022



#### Damage to properties from 14 June to 31 August 2022



The total economic losses are estimated to reach approximately US\$ 32 billion, whereas at least another US\$ 16.3 billion are required for recovery and rebuilding efforts.



### Pakistan is extremely vulnerable to different forms of climate change

Firstly, extreme monsoon rain and flooding continues to be one of the primary climate change related disasters. However, climate change has made Pakistan thirty times more likely to be gripped by extreme heat, such extreme weather leads to excess deaths, diminished working hours, lower productivity increased electricity costs for cool production and manufacturing facilities and reduced crop yields. Secondly, extreme heat will increase the demand for cooling by increasing input costs, but also lead to disrupted supply chains and productions processes, as supply networks and logistics process become stranded as a result of negative climate impacts. Furthermore, the effects of climate change might lead to increased economic and political instability in the country, which would further negatively impact the business environment, investor confidence and potentially supply and logistic networks.

In addition, as the adverse effects of climate change intensify, water security will become a growing concern as the demand for water increases due to population growth, and the rapid alternation between droughts and floods makes access to water and water rights an even greater concern in the region and a source of further regional instability. The adverse effects from climate change will lead to more human suffering, but it will also increase the costs for corporate actors with footholds in Pakistan.

**Climate-related extreme weather events will occur and need to be part of every company's risk register and business continuity plan. Advanced analytical procedures can help companies assess future climate conditions and therefore improve risk mitigation and pricing. Increased climate change information and predictive analytics also have a huge potential to significantly expand risk assessment.**



## Energy insecurity

The economic crisis, the devaluation of the Pakistan's currency, and the massive floodings have increased further energy insecurity in Pakistan, that is risking the country's demand for electricity. Pakistan imports most of its energy (oil and natural gas) and the devaluation of its currency has further increased energy costs in Pakistan, that were already high since latest Russian invasion of Ukraine.

*The lack of maintenance and investment in energy grids is also causing massive blackouts in Pakistan, affecting businesses, hospitals and schools.*

On 23 January, a massive electricity outage left almost all of Pakistan without electricity for around 20 hours due to a voltage fluctuation at a power station. In addition, shopping malls and markets had to reduce their opening hours in order to reduce 30 percent of electricity consumption in January. Such blackouts are becoming common in Pakistan and are likely to continue.

*Extended power outages will likely affect multiple industries with business interruption and increased costs. The power outages are also likely to affect the food industry production and force Pakistan to import more food when food prices are already soaring. After years of relying on food imports, power outages, inflation and the 2022 floods, that destroyed millions of hectares of farmland, are risking the Pakistani food industry.*

European businesses with interests in Pakistan may suffer supply chain interruptions, affecting costs. Moreover, businesses based in Pakistan should consider energy blackouts in their business continuity plans. Advanced analytical procedures can help companies assess energy blackouts and economic downturns in the future, and therefore improve risk mitigation, crisis management processes and pricing.

## Supply chain challenges

Political, economic, terrorist and climate crises have severely impacted supply chains in Pakistan:



**Automotive companies have suspended production:** Honda announced in March that it was closing a manufacturing plant in Pakistan due to higher taxes and the continued devaluation of the Pakistani rupee. Toyota has also suspended production in Pakistan at least four times in 2023 due to insufficient inventory.



Due to increased production costs and the inability to purchase raw materials to fulfil orders, **several companies in the textile industry in Pakistan have shut down their production centres.** In addition, the floods washed away 45 percent of Pakistan's cotton crop.



The **pharmaceutical industry in Pakistan has faced several supply chain challenges** due to reduced demand, price controls, raw material shortages, increased transportation costs and continued transportation delays.



The **floods destroyed or damaged farms and food production centres.** In particular, floods in Sindh and Punjab provinces washed away swathes of crops vital to the production of onions, tomatoes and chickpeas. The Lahore Market Committee confirmed that 80 per cent of Pakistan's tomato crop had been damaged by the floods.



In addition, Pakistan's supply chains face the following problems:



**Infrastructure:** Pakistan's roads, ports and airports are outdated, making transport slow. This often leads to delays and higher costs for businesses, especially those involved in importing or exporting goods.



**Poor use of technology:** The use of technology in Pakistan's supply chain is limited. This leads to inefficiencies and inaccuracies in inventory management and logistics, and can result in delays, disruptions and higher costs.



**Communication barriers:** Pakistan is a multi-lingual country with dozens of regional languages. Language barriers and cultural differences exacerbate communication problems between different parts of the supply chain. This can lead to delays and misunderstandings in the supply chain.



**Limited access to finance:** Many companies in Pakistan struggle to access finance, especially now with the country's economic crisis. Economic problems make it difficult for companies to invest in their supply chains.



**Lack of standardisation:** There is a lack of standardisation in Pakistan's supply chain, which can lead to confusion and delays in deliveries. This is a major risk for companies that need to meet strict deadlines or quality standards.

*To reduce supply chain disruption, it is critical for companies to be well prepared with cost-effective third-party oversight and risk management, maintaining a strategic and responsible partnership in Pakistan and across the globe. Third-party risk assessment includes key stakeholders screening, company ownership research, company diligence and third-party suppliers monitoring.*

# 2SECURE RECOMMENDS

1. As the prevalence of civil unrest and violent protests are likely to continue in Pakistan in 2023 and beyond, companies with business interests in Pakistan should invest in robust and comprehensive risk monitoring mechanisms that provide strategic foresight and alerts on potential event triggers, enabling the reallocation of business resources to avoid the worst impacts of emerging civil unrest risks in Pakistan, such as business interruption and supply chain disruptions.
2. As political instability and unrest continues, European business leaders with interests in Pakistan should monitor and understand the complexity of the social and political landscape in Pakistan and conduct detailed scenario planning for possible eventualities, including the PTI coming back to power and pursuing populist economic policies, or a Pakistani Army intervention. Desktop, scenario-based exercises are valuable to ensure success and mitigate the most pressing risks in Pakistan.
3. Pakistan faces a constant threat of terrorism due to political instability and a weak counter-terrorism strategy. Companies with employees working in, and or travelling to Pakistan should ensure 24/7 emergency support systems. This should include real-time monitoring of security incidents, and proactive notification to employees of incidents in their vicinity. Travel risk management solutions are equally applicable for travelling personnel and those employees permanently based in Pakistan.
4. Pakistan is facing a deepening economic crisis, a sharp devaluation of its currency and record inflation that have lead to increased production costs. Companies with operations or suppliers in Pakistan should understand the challenging economic landscape in Pakistan, closely monitor the Pakistani government's actions and develop a strategy that incorporates significantly higher costs for the foreseeable future.
5. Pakistan is suffering from severe flooding. Climate-related extreme weather events will continue to occur and need to be part of every company's risk register and business continuity plan. Advanced analytics can help companies assess future climate conditions and therefore improve risk mitigation and pricing. Increased climate change information and predictive analytics also have great potential to significantly enhance risk assessment.

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