

Informal Economy of Pakistan - the Way-forward

Outline:

I Introduction

Thesis: Pakistan is facing significant economic challenges primarily due to the vast size of its informal economy, which hampers the country's socio-economic development. However, through appropriate policy measures the informal economy can be regulated and documented, paving the way for long-term economic stability.

II Defining the term "Informal Economy"

III A Brief Overview of the Informal Economy of Pakistan

- i) Statement of Finance Minister
- ii) Report of World Bank

IV Factors Contributing to Informal Economy

A- Inefficient and ineffective tax collection mechanism

case in point: FBR's failure to meet revenue target 2024-25 Ghazi Paper

B- Structural fault lines in regulating businesses

case in point: Reference of Ishrat Hussain's book

C- Weak enforcement at borders contributing to unchecked smuggling

case in point: Report of Civil Intelligence Agency to PM on oil smuggling

D- Unregistered labour force in large and medium enterprises

case in point: 20 million labour force is undocumented - Labour Force Survey

E- Unsustainable economic policies of governments

case in point: Reference of S. Akbar Zaidi's book

V Implications of Informal Economy on Pakistan

A- Significant decline in revenue collection

case in point: Economic Survey of Pakistan 2025

B- Increase in money laundering and terror financing

case in point: Pakistan placed on FATF

C- Widespread corruption within government institutions

case in point: Report of Transparency International

D- Irregularities and inequalities in resource distribution

E- Rise in unemployment and poor working conditions

VI Way-forward to Bring Informal Economy into Documented Economy

- A- Embracing innovation, technology, and digitalization
- B- Encouraging adoption of digital economic transaction
- C- Capacity building and better training of tax collectors
- D- Comprehensive restructuring of tax collection policy
- E- Empowering Local governments to generate and manage revenues
- F- Use of AI in revenue tracking and collection
- G- Conducting financial literacy and awareness sessions about tax collections
- H- Investing in Human Capital to formally register undocumented economy

VII Conclusion

Since its inception, managing the economy has always been one of the biggest challenges facing Pakistan. Instead of stagnant growth, Pakistan has experienced a boom and bust cycle of the economy, characterized by periodic variations from

over-reliance on foreign aid to a capitalistic economy under Ayub, from Bhutto's nationalization policy to various economic models tested under successive governments; unfortunately, no model is succeeded in stabilizing the economic growth. Among all the factors contributing to the economic crisis, the informal economy appears to be the most prominent. Pakistan's significant economic challenges are primarily due to the vast size of its informal economy, which hampers the country's socio-economic progress. However, through appropriate policy measures, the informal economy can be regulated and documented, paving the way for long-term economic stability. Inefficient and ineffective tax collection mechanisms, unchecked smuggling, and unstable economic policies are the main reasons behind the growing informal economy. Furthermore, the widely undocumented economy results in several detrimental consequences such as a decline in revenue generation, easing money laundering, widespread corruption and unequal

resource distribution. However, there exists room for improvement and better outcomes. Certainly, by implementing robust measures, the unchecked economy can be brought into official records.

Embracing innovation and technology and capacity building of revenue officers can significantly reduce the informal economy. Additionally, restructuring the tax collection policy and empowering local governments can help bring the informal economy into formal sector.