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COMBATING ILLICIT TRADE IN PAKISTAN: A STRUCTURAL AND POLICY ANALYSIS

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The Transnational Alliance to Combat Illicit Trade (TRACIT) is an independent, private sector initiative to drive change to mitigate the economic and social damages of illicit trade by strengthening government enforcement mechanisms and mobilizing businesses across industry sectors most impacted by illicit trade.

This Brief is part of TRACIT's project "Pakistan's Battle against Illicit Trade: An Analysis of Challenges and Pathways to Resilience"

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Published by:

Policy Research Institute of Market Economy (PRIME)

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Prime Research Brief No. 89

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April 2025

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EXECUTIVE SUMMARY

Illicit trade has emerged as a critical challenge for Pakistan's economy, undermining formal businesses, eroding government revenues, and jeopardizing consumer safety. From smuggled petroleum and counterfeit pharmaceuticals to non-tax-paid cigarettes and under-invoiced consumer goods, illicit trade has entrenched itself across key sectors. The gravity of this issue is manifested by an estimated annual tax revenue loss of Rs. 3.4 trillion on account of an estimate of $123 billion informal economy. According to the 2025 Illicit Trade Index, Pakistan ranks 101 out of 158 countries, performing below global and regional averages, highlighting systemic weaknesses in governance, enforcement, and economic policymaking.

The drivers of illicit trade in Pakistan are both economic and institutional. High customs duties, complex tariff regimes, inflation, and a growing informal economy incentivize businesses and consumers to move away from the formal sector. Regulatory inconsistency and protectionist trade policies further add to the cost of doing legal business. Simultaneously, porous borders, outdated customs infrastructure, and limited inter-agency coordination allow the unchecked movement of illicit goods. Enforcement mechanisms, though partially effective at the borders, remain weak within domestic markets, especially at the retail and distribution levels. The suboptimal performance of the Track and Trace System, adopted to monitor tax compliance, reflects weak implementation, with only a fraction of cigarette brands complying.

To address these multifaceted challenges, a comprehensive and coordinated strategy is required. Based on extensive consultations, data analysis, and technical review, the report proposes the following key recommendations:

1. Fully implement the Track & Trace system in sectors which are prone to counterfeiting and smuggling (e.g. 95% of cigarette brands are selling openly without the affixation of tax stamps).
2. Improve retail-level enforcement by conducting regular spot checks at points of sale and strengthening the visibility of enforcement actions to deter illegal trade. Law enforcement agencies should be equipped with the necessary tools to authenticate tax stamps. Strengthen and evolve tax stamps as they play a crucial role in distinguishing between tax-paid and non-tax-paid goods.
3. Avoid unplanned tax increases as they encourage illegal trade to thrive. All tax increases should be aligned with inflation.
4. Ensure stricter border control and monitor the flow of goods coming from neighboring countries and non-tariff areas such as AJ&K, ensuring that products coming into Pakistan are duty paid.
5. Launch consumer awareness campaigns by educating the public on the risks of counterfeit and tax evaded goods with support from industry and international partners.
6. Enhance inter-agency coordination by facilitating information sharing and joint operations between FBR, provincial Governments and border security forces.

1. INTRODUCTION

Illicit trade has emerged as a significant threat to Pakistan's economy, undermining documented and legitimate businesses, incurring losses to the state revenues, and compromising consumer safety. It includes several activities such as smuggling, tax evasion, counterfeiting and unauthorized manufacturing. In Pakistan, illicit trade is prevalent in several sectors including petroleum, tobacco, tires, food, pharmaceuticals, and electronics, resulting in economic and social costs.

The prevalence of illicit trade not only distorts market dynamics but also erodes the foundation of fair competition, creating an uneven playing field where compliant businesses are penalized, and illicit actors thrive. Firms operating legally are often unable to compete with informal market actors who bypass taxes and regulatory costs. This discourages investment, limits job creation, and reduces government revenue that could otherwise be used for public services.

The scale of illicit trade in Pakistan is deeply concerning. According to industry estimates and research studies, billions of rupees in government revenues are lost annually due to unaccounted and untaxed economic activities. The extent of illicit trade can be manifested by the 101 rank of Pakistan out of 158 countries according to the Illicit Trade Index 2025[1]. This can also be illustrated by an estimate of the size of informal economy of around $123 billion and annual tax revenue loss is estimated to be Rs. 3.4 trillion[2] (PBC 2023[3]). Moreover, the loss of revenues from smuggling of tobacco is estimated to be more than Rs. 300 billion[4], Rs. 1 trillion from Afghanistan Transit Trade and Rs. 270 billion[5] from smuggling oil.

The persistence and stronghold of illicit trade in Pakistan can be attributed to a combination of policy distortions, weak enforcement mechanisms, and economic incentives that favor informal transactions. High tax rates, complex and inconsistent regulatory frameworks, and protectionist trade policies often incentivize market players to evade compliance. Additionally, porous borders, limited coordination among enforcement agencies, and the lack of effective tracking and monitoring systems have created an environment in which illicit activities flourish with minimal risk.

The Government of Pakistan also acknowledged the distortions emanating from growing illicit trade and constituted a Joint Committee in October 2024 to address revenue leakages due to illicit manufactured trade and smuggling of manufactured tobacco.

This report aims to examine the underlying factors driving illicit trade in Pakistan, particularly those arising from policy distortions and enforcement gaps. Two research questions will guide

[1] Illicit Trade Index is a publication of Transnational Alliance to combat Illicit Trade (TRACIT). The report can be accessed at https://www.tracit.org/illicit-trade-index.html

[2] https://tribune.com.pk/story/2466307/illegal-trade-short-term-gains-long-term-economic-decline

[3] Framework to Combat Illicit Trade, November 2023. The Pakistan Business Council. The report can be accessed at https://www.pbc.org.pk/research/framework-to-control-illicit-trade/

[4] Sakib Sherani, 2025. Towards an optimal tax regime for Pakistan's tobacco sector.

[5] https://tribune.com.pk/story/2466307/illegal-trade-short-term-gains-long-term-economic-decline?utm_source=chatgpt.com

the analysis:

- How do government policies distort sectors and inadvertently incentivize illicit trade?
- How does the absence of effective control mechanisms contribute to economic losses?

Through sectoral cases, stakeholder consultations, and policy reviews, this report seeks to propose actionable reforms that can curb the incentives for illicit trade, enhance regulatory enforcement, and restore confidence in the formal economy.

2. METHODOLOGY

This study adopts a mixed-method approach, incorporating both qualitative and quantitative analyses. The choice of this approach is based on the complexity and multifaceted nature of the issue under examination, which demands a comprehensive analysis of data trends, regulatory frameworks, and stakeholder perspectives. The combination of empirical evidence and qualitative insights ensures a holistic understanding of the challenges posed by illicit trade and the formulation of actionable policy recommendations.

2.1. Primary and Secondary Data

The quantitative component of the study relies on secondary data sourced from government agencies and independent research institutions. Key data sources include Federal Board of Revenue (FBR), Transnational Alliance to Combat Illicit Trade (TRACIT), Social Policy and Development Centre (SPDC), Pakistan Business Council (PBC), and reports authored by independent subject-matter experts. These sources provide valuable insights into revenue trends, enforcement gaps, and the scale of illicit manufactured trade.

Primary data for the qualitative component was collected through a series of structured consultations with industry stakeholders and relevant government departments. These interactions were instrumental in capturing on-ground realities, policy implementation bottlenecks, and industry perspectives on enforcement challenges and regulatory inefficiencies.

2.2. Consultations with the Stakeholders

2.2.1. Composition of a Committee

In the context of revenue shortfalls and hike in illicit trade, the Government of Pakistan constituted a Joint Committee in October 2024 to investigate the underlying causes of declining revenues following an increase in the federal excise duty on cigarettes. The Committee comprises 13 members representing a broad spectrum of stakeholders, including public representatives, officials from the Federal and Khyber Pakhtunkhwa governments, industry participants, and independent experts. The Committee was chaired by the Minister of State for Finance and Revenue, highlighting the gravity of the issue and a resolve to address shortcomings.

2.2.2. Technical Committee Review

Under the guidance of the Joint Committee, a subcommittee was formed to undertake in-depth technical evaluations. The technical committee engaged in targeted discussions to identify critical issues related to tax policy design, tariff structures, and enforcement mechanisms. The

subcommittee's assessment highlighted key regulatory and operational deficiencies contributing to a contraction in the documented economy and a surge in illicit trade activities. The findings from the technical reviews and deliberations of the consultations form an essential basis for the policy recommendations proposed in this report.

3. ILLICIT TRADE IN PAKISTAN

3.1. Insights from Illicit Trade Index Report 2025

The Illicit Trade Index[6], a publication of TRACIT, monitors the performance of countries in preventing illicit trade by taking into account six broad categories comprising 37 indicators. The index covers progress of 158 countries, 82 percent of United Nations member states, based on Taxation and Economic Environment, Trade, Customs and Borders, Criminal Enablers of Illicit Trade, Regulatory Framework and Enforcement, Sectoral Illicit Trade Indicators, and Supply Chain Intermediaries, each category having multiple indicators (Table 1). The index acts as a diagnostic tool to identify and highlight risks and threats, guide policy decisions and foster collaboration regionally and globally. The results are expressed in the form of a 0-100 scale, with higher score indicating higher resilience against illicit trade.

Table 1: Categories and Indicators of Illicit Trade Index

Category	Name	Indicators
Category 1	Taxation and Economic Environment	1. Excise tax rates 2. Tax burden 3. Inflation 4. Sovereign credit ratings 5. Informal economy
Category 2	Regulatory Framework and Enforcement	1. Commitment to illicit trade-related treaties 2. Interagency collaboration 3. Regulatory quality 4. Government effectiveness 5. Business environment 6. Consumer protection 7. Government enforcement
Category 3	Criminal Enablers of Illicit Trade	1. Corruption 2. Rule of law 3. Money laundering 4. Organized crime 5. Trafficking in persons
Category 4	Trade, Customs and Borders	1. Logistics performance 2. De minimis levels 3. Accredited Economic Operator Program 4. Customs recordal system 5. Container profiling 6. Advance Electronic Information 7. Goods in transit

[6] https://www.tracit.org/illicit-trade-index.html

Category	Name	Indicators
Category 5	Supply Chain Intermediaries	1. Cyber security / Cyber security preparedness 2. E-commerce framework 3. Free trade zones commitments 4. Postal security
Category 6	Sectoral Illicit Trade Indicators	1. Illegal flora crime 2. Illegal fauna trade 3. Non-renewable resource crimes 4. Intellectual property rights protection 5. Trade in counterfeit goods 6. Illicit trade in excisable goods 7. Illicit trade in alcohol: 8. Illicit trade in agrochemicals 9. Illicit trade in pharmaceuticals

The average global score in 2025 was 49.9, highlighting the challenges in curtailing illicit trade even by the developed economies. Denmark ranks 1 in the Index with a score of 76, followed by the United States (75.4) and Germany (73.5), while the lowest ranked are Central African Republic (29.7), Venezuela (27.1) and Yemen (25.7). Countries with strong regulatory frameworks, efficient customs systems, and well-coordinated interagency responses show high scores.

The report shows that illicit trade continues to thrive due to systemic issues: weak enforcement, porous borders, under-regulated e-commerce, and inadequate supply chain oversight. The Index shows that only 4% of the world's population lives in countries classified in the top quartile, underscoring that most people remain vulnerable to the harm of illicit markets.

Figure 1: Top 10 Performing Countring

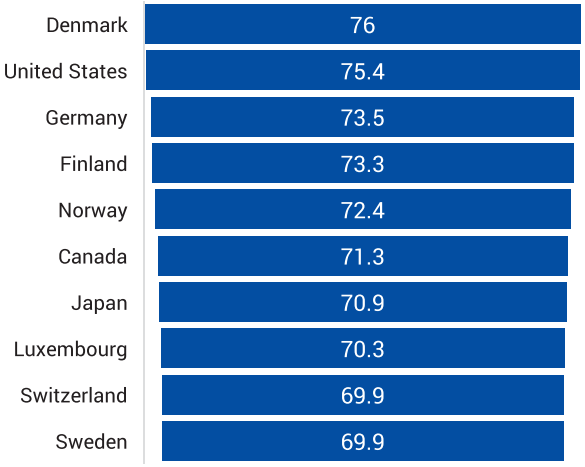
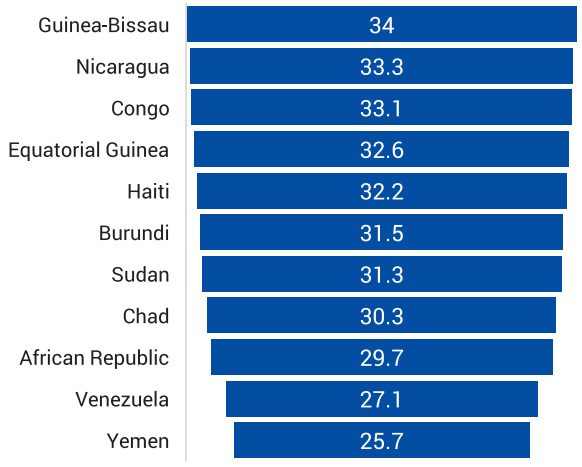


Figure 2: Lowest 10 Performing Countries

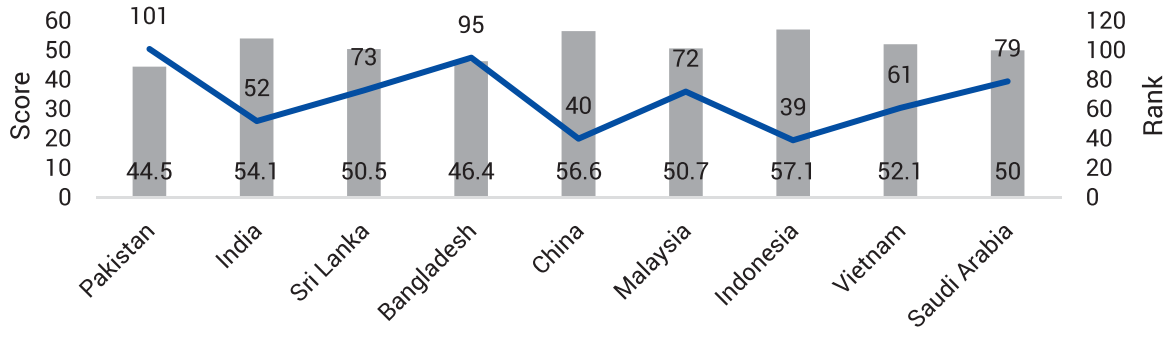


3.1.1. Pakistan's overall performance according to report

Pakistan ranks 101 out of 158 countries, with a composite score of 44.5, placing it below the global average of 49.9. In contrast, the neighboring countries have fared well with China at 40th rank, India at 52nd, Sri Lanka at 73rd, and Bangladesh at 95th. Similarly, comparison with emerging economies also shows that Pakistan is lagging behind all of them. It is a cause of

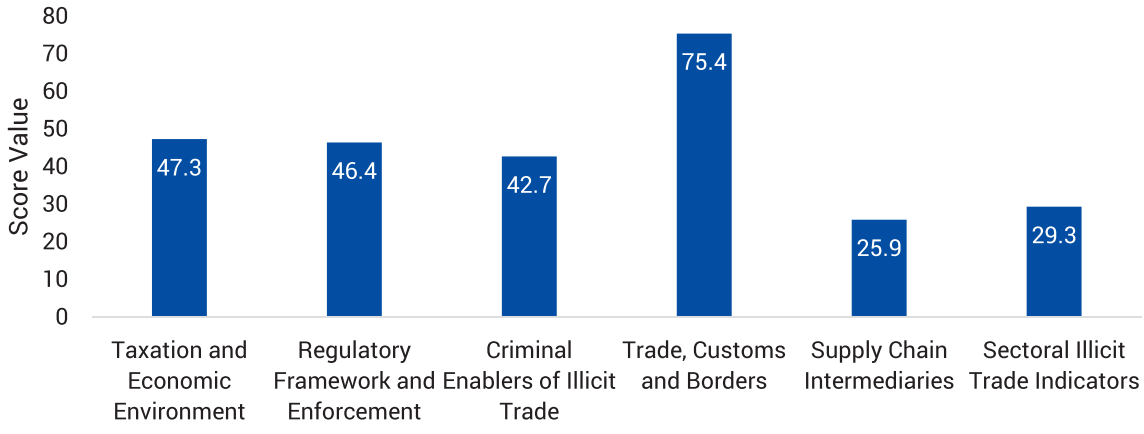
concern that Pakistan is among the only few developing economies falling at the bottom of lower-middle income countries. This ranking reflects risks and vulnerabilities across multiple dimensions of trade governance, enforcement, and economic regulation. Pakistan's performance is also weak when compared to regional peers and other developing economies (Figure 3).

Figure 3: Performance of Regional Peers



Pakistan's performance across six dimensions of the Index is illustrated in Figure 4. The highest score is observed in Trade, Customs and Borders (75.4), indicating relatively strong border controls and customs management mechanisms. However, Supply Chain Intermediaries (25.9) and Sectoral Illicit Trade Indicators (29.3) score notably low, pointing to serious vulnerabilities in internal trade networks and sector-specific compliance. Moreover, moderate scores in Taxation and Economic Environment (47.3), Regulatory Framework and Enforcement (46.4), and Criminal Enablers of Illicit Trade (42.7) suggest systemic weaknesses in policy implementation and enforcement capacity. Overall, while Pakistan shows slight competence in managing its borders, the internal regulatory and economic environment still facilitates illicit trade, underscoring the need for comprehensive reforms beyond border controls.

Figure 4: Pakistan's Score in the Index



In this report, only two categories will be analyzed in detail based on their significance and coherence with our research questions.

3.1.2. Discussion on Category 1: Taxation and Economic Environment

This category evaluates countries on five structural indicators: excise tax rates, inflation control, tax burden, sovereign credit ratings, and the size of the informal economy. The average global score in this category is 60.5. Top performers like Switzerland scored as high as 82.6, while countries like Sudan scored as low as 21.6. Pakistan's score in this category is 47.3, significantly below the global average. The dismal performance in this category relates to weak economic fundamentals, which represent structural issues in economic policy making and lack of implementation.

A deeper look into the components of this category highlight the reasons behind the unsatisfactory score of Pakistan. To begin with, inflation has remained a challenge for governments in Pakistan and in last few years, it hovered around 12.15 percent in 2022, 29.18 percent in 2023, and 23.41 percent in 2024. Although the inflation has come down to 5.25 percent in the 9 months of FY 2025, the fall in purchasing power in the last couple of years still creates demand for cheaper, illicit alternatives.

The exact size of the informal economy is difficult to calculate, however, different estimations have been put forth by institutions and independent experts. The independent experts consider the size of informal economy to be one-third of the formal economy. According to the Small and Medium Enterprise Development Authority, the informal economy has a market share of more than 40 percent of the GDP[7].

In terms of taxation policy in general and excise taxation in particular, significant distortions have been observed. For instance, the government of Pakistan increased the Federal Excise Duty on tobacco products by up to 150 percent to generate additional revenues for budgetary support in February 2023. Since then, the market share of illicit cigarettes has increased manifold from 30 percent to 56 percent, causing a loss of more than Rs. 300 billion[8] annually. High tax rates create incentives for evasion and smuggling. Due to high tax rates, whether personal income tax, corporate tax, sales tax or FED, Pakistan has a low tax-to-GDP ratio, hovering around 9 percent to 10 percent and creating incentives for some sectors stay out of the tax net.

[7] https://tribune.com.pk/story/2449373/pakistans-undocumented-economy?utm_source=chatgpt.com
[8] https://www.brecorder.com/news/40353594

3.1.3. Discussion on Category 4: Trade, Customs and Borders

This category measures a country's ability to prevent the entry and movement of illicit goods through border controls, customs procedures, and trade facilitation systems. It includes seven indicators: logistics performance, customs recordal systems, de minimis[9] levels, accredited economic operator program, container profiling, and use of advance electronic data filing (AEI/EAD), and goods in transit. The global average score is 56.5, with Canada leading at 96.4, and Burundi at the bottom with 14.4. Pakistan's score in this category is 75.4, significantly above the global average.

Despite the good score, Pakistan continuously faces challenges in stopping the smuggling of goods, which is manifested by the reports of FBR on seizures of smuggled goods, and drugs. FBR seized Smuggled Contraband goods and drugs of more than Rs. 3,052 million in 2022, Rs. 860 million in 2023[10], and Rs. 2,400 million in 2024[11].

The porous border with neighboring countries especially with Afghanistan and Iran creates challenges for the government to stop smuggling of goods, particularly petroleum, electronics, tobacco, spare parts and drugs. The prevalence of smuggling and recent hikes also results from weak infrastructure and systems in place. First, the outdated border control infrastructure and limited automation in the customs processes make it difficult for the government to prevent smuggling of goods. Pakistan is also lacking in the risk-based profiling systems, and modern container scanning technologies. Another area where attention is required is coordination among different government agencies. The weak interagency coordination especially between the Pakistan Customs and security agencies leads to prevalence of illicit trade and hinders effective enforcement.

[9] De minimis rules allow shipments below a certain value threshold to bypass customs inspections, rendering the border more vulnerable to illicit trade in small parcels.

[10] https://www.fbr.gov.pk/pr/2022

[11] https://www.fbr.gov.pk/pr/2023

4. SECTORAL ANALYSIS ON EXTENT OF ILLICIT TRADE IN PAKISTAN

Table 2: Sectoral Analysis on Illicit Trade

Sector	Illicit Trade	Taxes and Duties	Revenue Loss
Tobacco	56% of market share	• FED on Rod: Rs. 80,000 per kg • FED on Acetate Tow: Rs. 44,000 per kg • FED on Tobacco: Rs. 390 per kg Minimum legal price of cigarettes jacked up in 2023 • Tier 1- Value: Rs. 119 per pack (S.T. +FED) • Tier 2- Premium: Rs. 389 per pack (S.T. +FED)	Rs. 300 billion[12]
Pharmaceuticals	40% of medicines are counterfeit/substandard[13]	Low rates for essential imports, but require approval from DRAP	Rs. 60-65 billion[14]
Tires and lubricants	Over 60% of tires sold are smuggled[15]	35 percent customs duty and 17 percent sales tax	Rs106 billion[16]
Petrol/Diesel	2.8 billion liters smuggled from Iran	Customs duty of Rs. 16 per liter[17] and petroleum development levy of Rs. 60 per liter.	Rs270 billion[18]
Tea	Around 30 percent of Market share	Minimum Retail Price of Rs. 1,200 per kg and 18 percent Sales Tax	Rs. 10 billion[19]
Total			**Rs. 751 billion**

[12] https://www.dawn.com/news/1893534
[13] https://profit.pakistantoday.com.pk/2021/09/12/pakistans-counterfeit-medicine-problem/
[14] https://www.thenews.com.pk/print/1078058-report-shines-light-on-rs956bn-tax-evasion-in-five-sectors
[15] https://tribune.com.pk/story/2455591/smuggled-tyres-cause-annual-losses-of-over-rs70-billion
[16] https://tribune.com.pk/story/2500915/tax-target-may-be-met-by-curbing-illegal-trade
[17] https://www.dawn.com/news/1897566/petrol-may-see-rs14-per-litre-reduction
[18] https://www.dawn.com/news/1830884
[19] https://www.thenews.com.pk/print/1209436-pakistan-loses-rs10bn-annually-due-to-illicit-tea-trade

5. ECONOMIC POLICY AND ILLICIT TRADE

There exists a strong relationship between economic policy and illicit trade. Policies that are carelessly designed without considering the unintended consequences, and halfhearted implementation not only create incentives for illicit trade but also create acceptance among the masses.

i. Inflation and product affordability

The most important economic factor contributing to illicit trade is inflation. High inflation implies lower purchasing power, motivating the consumers to look for cheaper alternatives including smuggled and counterfeit goods. The affordability gap between legal and illicit goods is identified as a primary driver of black-market activity. When income levels stagnate and prices rise, illicit trade becomes a more accessible and attractive option for consumers seeking affordable substitutes for daily necessities.

ii. Taxes and illicit trade

The desire to generate more revenues for unfettered expenditures motivates governments to raise revenues without considering the consequences and distortions. The market participants develop business practices around policies. If the policies are not conducive and extortionist, then market participants prefer to operate informally. This is corroborated by the Laffer Curve which states that an increase in tax rates increases revenues up to a certain point after which revenues start to decline. At higher tax rates and number of taxes, the tendency to evade taxes and illicit trade increases manifold. For consumers, when the tax rates increase, the price of goods increases while income remains constant. This fall in purchasing power creates incentives to look for alternate goods. For sellers, a higher tax rate implies lower profits or lower demand, creating an incentive to find alternatives that are not taxed and might have higher demand.

Also, when there are barriers to trade in the form of tariffs and compliance requirements, the cost of trade and traded goods increases, making it unaffordable for a significant proportion of population having low incomes. Moreover, the barrier to trade hinders competition, incentive to innovate and improve, reducing options for consumers and forcing them to settle for expensive and lower quality local products. This is a consequence of a highly protected economy where tariffs and duties make trade of goods expensive and out of the reach of many. Therefore, inefficient tax and tariff policies not only incentivize tax evasion but also illicit trade.

iii. Illicit trade and stagnation of private sector

An unconducive business environment characterized by high taxes, elevated tariffs, and the widespread prevalence of illicit trade significantly undermines private sector growth. When formal sector firms are burdened with excessive costs, including high duties and compliance obligations, their products become uncompetitive in price compared to illicit goods that evade such costs. As a result, consumers naturally gravitate towards cheaper, untaxed alternatives, eroding the market share of legitimate businesses. In response, many formal firms are

compelled to compromise either by engaging in tax evasion, smuggling cheaper inputs, or by reducing product quality to remain competitive. This not only perpetuates a vicious cycle of low-quality production and minimal innovation but also weakens the overall integrity of the business ecosystem. Ultimately, both businesses and consumers suffer—firms lose incentives to invest and grow, while consumers are left with inferior and often unsafe products. Without coherent and balanced economic policies that reduce distortions and curb illicit trade, sustainable private sector development remains unattainable.

iv. Investment climate and illicit trade

A country with weak economic fundamentals has low credit ratings and a reluctant investment climate. The prevalence of illicit trade further exacerbates this uncertainty, as it distorts market dynamics, reduces the profitability of compliant businesses, and signals weak enforcement of the rule of law. Investors perceive such an environment as high-risk, discouraging both domestic and foreign direct investment. Moreover, persistent policy failures and the inability to curb illicit economic activity negatively impact on a country's creditworthiness. International credit rating agencies assess not just macroeconomic indicators, but also institutional strength and governance quality—both of which are compromised by unchecked illicit trade and erratic policies. Pakistan's Long Term Issuer Default Rating[20] by Fitch is B-, which means highly speculative. Moody's[21] has given CAA2 rating, which means substantial risk and S&P has given CCC+ for Long Term Sovereign Credit Rating, which indicates substantial risks. A deteriorating credit rating raises the cost of borrowing, limits access to global capital markets and restricts fiscal space for development spending. Consequently, the country enters a cycle of low investment, sluggish growth, and limited capacity to finance long-term development goals.

[20] https://www.fitchratings.com/search/?query=Pakistan%20credit%20rating

[21] https://tradingeconomics.com/pakistan/rating

6. INEFFECTIVE CONTROL MECHANISMS AND ILLICIT TRADE

Pakistan continues to face a persistent challenge in controlling illicit trade, largely due to porous border, and institutional and procedural weaknesses in its customs and enforcement mechanisms. The country's structural deficiencies, particularly in border management and customs enforcement, have enabled the unchecked movement of illicit goods, undermined the legitimate trade and caused significant fiscal and security implications.

The enforcement gap is more prominent in Baluchistan, where the requirement of officers to perform anti-smuggling duties and monitor the international border is much greater. Due to this severe resource constraint, enforcement agencies are compelled to prioritize inland operations along major roadways rather than intercepting goods at the border, effectively allowing illicit consignments to enter unchallenged and flow freely through domestic trade routes.

In addition, Pakistan's Customs lacks modern surveillance technologies, data integration tools, and real-time tracking systems necessary to counter modern smuggling tactics. This technological lag leaves the country vulnerable to evolving concealment methods such as hidden vehicle compartments, altered shipping documentation, and digital platforms used to distribute illicit products, according to the World Customs Organization's Illicit Trade Report 2023[22].

The limited coordination among different government agencies further complicates the enforcement landscape responsible for restricting illicit trade. Weak inter-agency cooperation has hindered comprehensive policy responses and allowed enforcement efforts to remain fragmented and reactive rather than strategic and sustained. This is especially concerning in sectors such as pharmaceuticals, tobacco, and petroleum products, where overlapping jurisdictional mandates demand synchronized action.

In this context, the FBR introduced a Track and Trace System (TTS) in 2021-22 for curbing tax evasion, illicit production and monitoring movement of goods. However, the system's enforcement and adoption have been far from effective. A study by the Institute of Public Opinion and Research (IPOR) in 2024 found that only 19 out of 264 cigarette brands were compliant with TTS regulations, with 56% of the market comprising non-compliant and untaxed products[23].

[22] https://www.wcoomd.org/en/media/newsroom/2024/june/wco-releases-illicit-trade-report-2023.aspx
[23] https://www.dawn.com/news/1872410/loopholes-detected-in-compliance-of-fbrs-track-and-trace-system

7. RECOMMENDATIONS

To effectively combat the rising threat of illicit trade and address the structural enforcement and policy gaps identified in this report, the following set of actionable recommendations is proposed. These measures aim to enhance enforcement capacity, improve regulatory coherence, and promote market compliance across all levels of the supply chain.

Addressing Demand-side Issues:

1. Increase budgetary resource allocation significantly for effective enforcement mechanisms. Any investment done by the government has a revenue upside of 750 billion, however this goal can be met in phases.
2. Enhance enforcement quality at the trade level (retail / wholesale) by increasing spot checks and making it a regular exercise throughout the year. Grant concurrent enforcement powers to the provincial government to conduct raids on retail and wholesale channels, ensuring proper implementation of the Track & Trace system. Law enforcement agencies should be equipped with necessary tools to authenticate the tax stamp. Strengthen and evolve tax stamps as they play a crucial role in distinguishing between tax-paid and non-tax-paid goods.
3. Organize consumer awareness campaigns against illicit trade and tax evasion, complemented by media amplification of raids conducted by law enforcement agencies. The government should instill a sense of deterrence across the trade sector to ensure compliance and discourage illegal activities. Additionally, the government may seek support from the legal industry and international organizations, as sufficient resources and collaboration will be essential to successfully carry out this initiative.
4. Increase penalties and fines for those involved in illicit trade, and streamline and fast-track judiciary procedures to create a significant impact.

Addressing Supply-side Issues:

5. Crack down on clandestine facilities and strictly monitor the flow of goods coming from non-tariff areas such as AJ&K to ensure the stoppage of illegal, tax-evaded goods
6. Enforce controls on key raw materials. In the case of cigarette manufacturing, excise duty is placed on tobacco leaf purchases, acetate tow, and filter rods. Despite these measures, the government has not yet achieved the desired results as illegal cigarettes are widely available evading ~ 300 billion taxes annually. Therefore, it is essential to conduct regular audits and control the smuggling of key raw materials.

7. Ensure acknowledgment and design a reward structure for minimizing illicit trade for officers and staff from FBR and provincial governments.
8. Continue the policy to confiscate and destroy non-duty paid goods stock and disseminate the actions for wider awareness.

Additionally,

9. Acknowledging the importance of unbiased measurement of illicit trade, FBR should commission a survey to monitor the market share of illicit trade under its own supervision and seek financial support from credible international organizations for conducting this survey.

8. CONCLUSION

Illicit trade in Pakistan poses a grave threat to the country's economic stability, regulatory integrity, and public welfare. The persistence and expansion of illicit markets are closely tied to structural weaknesses in tax policy, trade regulation, and enforcement capacity. High taxation without due consideration of market dynamics, protectionist tariff regime, and complex regulatory environment have created strong incentives for market actors to operate outside the formal economy. The consequences are not only the loss of revenues for the government, but also unfair competition for formal businesses, compromise of consumer safety, and erosion of trust in public institutions.

Despite some progress, particularly in border and customs management, the country continues to lag behind regional and global peers in terms of its overall resilience against illicit trade. Sectoral analysis of tobacco, petroleum, pharmaceuticals, and other goods reveals systemic governance failures and a lack of coherence between economic policy and enforcement mechanisms. Moreover, the Track and Trace System needs to be strengthened to bridge institutional and technological gaps that hinder effective monitoring and compliance.

To disrupt the cycle of illicit trade, Pakistan must adopt a coordinated and reform-oriented approach that realigns tax and tariff policies with economic realities, strengthens enforcement at all levels, and leverages technology to enhance transparency and accountability. Importantly, the political will to act must be matched by institutional capacity, inter-agency collaboration, and public awareness campaigns that foster a culture of compliance and lawful economic participation.

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