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Pakistan raises defence expenditure by 20% to $9 billion in annual budget

But slashes overall federal spending by a hefty 7%

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This is likely to invite close scrutiny from New Delhi that has accused Pakistan of diverting financial support from multilateral agencies towards unproductive defence spending targeted at India. (Illustration: Ajaya Mohanty)

Pakistan on Tuesday raised its defence expenditure by 20 per cent to $9 billion in the annual federal Budget for 2025-26 (FY26) over the preceding year, but slashed overall federal expenditure by a hefty 7 per cent for the July-June financial year. This is likely to invite close scrutiny from New Delhi that has accused Pakistan of diverting financial support from multilateral agencies towards unproductive defence spending targeted at India.

New Delhi last week vehemently opposed Asian Development Bank's (ADB's) financial assistance of $800 million to Pakistan, raising concerns about potential misuse of the funds. Last month, the International Monetary Fund (IMF) also approved a $1 billion loan to Pakistan despite India's strong objection.

Indian officials cautioned the ADB on Pakistan's increasing defence expenditure, its declining tax-to-GDP ratio, and the lack of demonstrable progress on key macroeconomic reforms.

At the ADB Board meeting, India highlighted that while Pakistan's tax collection as a share of GDP declined from 13 per cent in FY18 to 9.2 per cent in FY23, there has been a significant increase in defence spending during the same period.

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"This points to the possibility of diversion of funds made available to the country by external agencies, including financial institutions, especially those that are made available by fungible debt financing, through instruments such as policy-based loans, for increased defence spending," India stressed.
Tensions between India and Pakistan flared up following the Pahalgam terror attack of April 22, in which 26 civilians were killed. It culminated in the launch of "Operation Sindoor".

India has decided to submit a dossier at the upcoming Financial Action Task Force (FATF) meeting, calling for Pakistan to be placed back on the grey list of the global money laundering and terrorist financing watchdog.
New Delhi is likely to highlight multiple commissions and omissions by Pakistan, such as restitution of money, failure to pass anti-terror laws, hosting terrorists, and buying military equipment with development funding.

The FATF grey list flags countries with "strategic deficiencies" in countering money laundering and terror financing. Re-entry into the list could have far-reaching consequences for Pakistan, including diminished foreign investment, increased borrowing costs, and tighter scrutiny from global financial institutions.
Pakistan was removed from the grey list in 2022 after the FATF acknowledged its progress in strengthening its anti-money laundering (AML) and counter-financing terrorism (CFT) frameworks.

According to sources, Pakistan allocates around 18 per cent of its general Budget to "defence affairs and services", significantly higher than the average 10-14 per cent observed even in conflict-affected countries. Moreover, between 1980 and 2023, Pakistan’s arms imports reportedly rose by more than 20 per cent during periods it received IMF disbursements compared to the years when it did not.

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