

Federal Budget 2026-27

Overview and Economic Implications

Policy Brief

The brief focuses on the description of the major economic numbers in the Federal Budget 2026-27, while highlighting key details and their implications. It also discusses the impact of the proposed budget on economic development, social welfare, and how well it truly reflects the country's long-term economic plans.

Executive Summary

The Federal Budget 2026–27 echoes the government's sustained commitment to fiscal consolidation while endeavoring to withstand economic growth and provide inadequate relief to taxpayers. With a total outlay of Rs.18.8 trillion, debt servicing, defense, and development remain the leading spending primacies. The budget targets GDP growth of 4.0 percent, inflation of 8.2 percent, and a rise in the investment-to-GDP ratio to 15 percent. On the revenue side, the government has set an ambitious FBR tax collection target of Rs.15.3 trillion, reflecting a 17.6 percent increase over revised estimates of the previous year. While fiscal discipline is reflected in a projected primary surplus of 2.0 percent of GDP, apprehensions persist regarding the continued dependence on indirect taxation and petroleum levy collections. Limited fiscal space, high debt-servicing costs, and constrained development spending may limit the economy's productive capacity. The budget highlights the need for comprehensive tax reforms, enhanced revenue mobilization, and more effective social protection mechanisms to support sustainable and inclusive economic growth.

Key Takeaways

- The federal budget outlay for FY 2026–27 is Rs.18.8 trillion.

- Debt servicing remains the largest expenditure item at Rs.8.1 trillion, accounting for over 42 percent of total spending.
- FBR tax revenues are targeted to increase by 17.6 percent over revised FY 2025–26 estimates.
- Defense expenditure has increased to Rs.3.0 trillion, reflecting prevailing security considerations.
- Development spending remains constrained despite growth objectives.
- Fiscal consolidation continues through a projected primary surplus of 2.0 percent of GDP.
- Continued reliance on indirect taxes and petroleum levy may increase the burden on lower- and middle-income households.
- Comprehensive tax policy reforms and evaluation of social protection programs remain critical policy priorities

Federal Budget 2026-27: An Overview

The federal budget 2026–27 generally reflects the marriage of difficult fiscal trade-offs with the desire to provide relief to segments burdened by extra taxation for two years. The total outlay of Rs.18.8 trillion is

shared equally among the three Ds: debt (42%), defense (16%), and development (5%). Pensions (6%), civil administration (6%), and grants to provinces and others are important expenses. Underlying macro-

framework targeted to increase the growth from 3.7% to 4% with additional investment of 0.6% points in an inflationary environment.

Table 1: Macro-framework of Budget

	2025-26		2026-27
	Target	Prov	Target
GDP Growth	4.2	3.7	4.0
Agriculture	4.5	2.9	3.6
Industry	4.3	3.5	4.5
Services	4.0	4.1	4.2
Investment	14.7	14.4	15.0
Savings	14.3	14.1	14.3
Inflation	7.5	7.1	8.2

Overview of Major Budget Numbers

Tax revenues (FBR) are targeted to increase by 17.6% over revised estimates of FY2026, which will enhance tax revenue by Rs.2.3 trillion in this fiscal year. The budget speech promised to mobilize it through efficient, data-based surveillance. Non-tax revenue will maintain its steady state path, with falling SBP profits and higher PDL. Net revenue of the federal government will increase by 12%, whereas transfers to the provinces will go up by 16.5%.

On the expenditure side, current expenditures are budgeted at Rs.17,495 (a 16.6% increase). Major expenses in current expenditure include: interest payments (Rs.8054 billion), defense affairs (Rs.3000 billion), grants and transfers to provinces (Rs.2680 billion), pension (Rs.1169 billion), subsidies (Rs.1091 billion), and civil government expenses (Rs.1071 billion), while PSDP stands at Rs.1000 billion. Important things to watch are rising interest payments and national economic Initiatives of Rs.360 billion placed in grants to others. Given the security situation, defense expenditure is jacked up by Rs.500 billion.

Table 2: Overview of the Federal Budget 2026-27

(Rs. in Billion)

Classification	Budget	Revised	Budget	%
	2025-26		2026-27	Change
- FBR Tax Revenue	14,131	12,983	15,264	17.6
- Non-Tax Revenue	5,147	5,093	5,336	4.8
Gross Revenue (FBR+NTR)	19,278	18,076	20,600	14.0
Less: Transfer to Provinces (-)	(8,206)	(7,592)	(8,848)	16.5
Net Revenue for Federal Government	11,072	10,485	11,751	12.1
Total Expenditures	17,573	15,642	18,771	20.0
Current	16,286	15,006	17,495	16.6
- Interest Payments	8,207	6,937	8,054	16.1
- Pensions	1,055	1,055	1,169	10.8
- Defense	2,550	2,588	3,000	15.9
- Subsidies	1,186	1,157	1,091	(5.7)
- Grants	1,928	1,971	2,680	36.0
- Running Civil Govt	971	1,021	1,071	4.9
Development Expenditure & Net Lending	1,287	636	1,276	
Federal Budget Deficit	(6,501)	(5,157)	(7,020)	36.1
Overall Fiscal Deficit	(5,037)	(3,778)	(5,226)	38.3
Overall Fiscal Deficit as %GDP	-3.9%	-3.0%	-3.6%	
Primary Surplus	1,464	3,159	2,828	(10.5)
Primary Surplus as %GDP	2.4%	2.5%	2.0%	
Nominal GDP	129,567	126,870	143,604	13.2
Provincial Surplus	3,170	1,794	-	

* Revised estimates for FY2025-26 are based on actual projections.

What Do Budget Numbers Imply?

- The budget numbers indicate that the government is pursuing contractionary fiscal policy for yet another year, which is detrimental to economic growth and is likely to lead to higher unemployment, poverty, and lower consumption.
- Another year with another ambitious tax revenue target. In the outgoing fiscal year, tax targets were revised from Rs.14,131 billion to Rs.12,983 billion, but it has so far (11 months of FY2025-26) collected Rs.11,232 billion. In one month, the government has to collect Rs.1751 billion – a huge task, which the government is planning to fill through increasing the petroleum levy. So, despite international oil prices now below \$90 per barrel, the declining impact may not be fully reflected in local fuel prices immediately.
- Instead of broadening the tax base, the government has continuously relied on indirect sources of tax revenue. The federal government's increasing focus on petroleum levy revenue in the last few years is for two reasons: collection through this source is easy, and secondly, it does not fall into the divisible pool, so all revenue goes into the federal government's pocket.
- Increased share of indirect taxes and petroleum levy is severely impacting the middle- and lower-income groups of the

country, leading to a reduction in consumption. Moreover, this higher burden would also lead to a shift in social classes, which subsequently leads to more people below the poverty line.

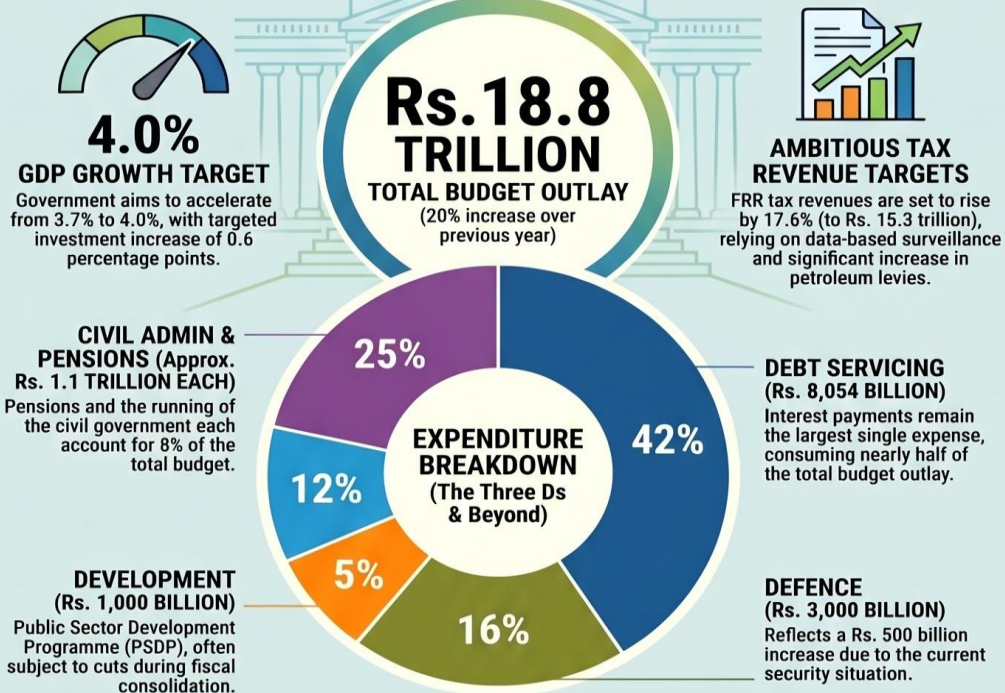
- The development budget is slashed for fiscal consolidation in the outgoing fiscal year, and this practice is most likely to be repeated in the upcoming fiscal year. Depriving development expenditure will curtail productive capacity in the economic activity.
- Pakistan has accrued economic costs from the US-Iran standoff, but could not leverage it for economic benefits.

Beyond Budget: The Bigger Issues that Require Attention

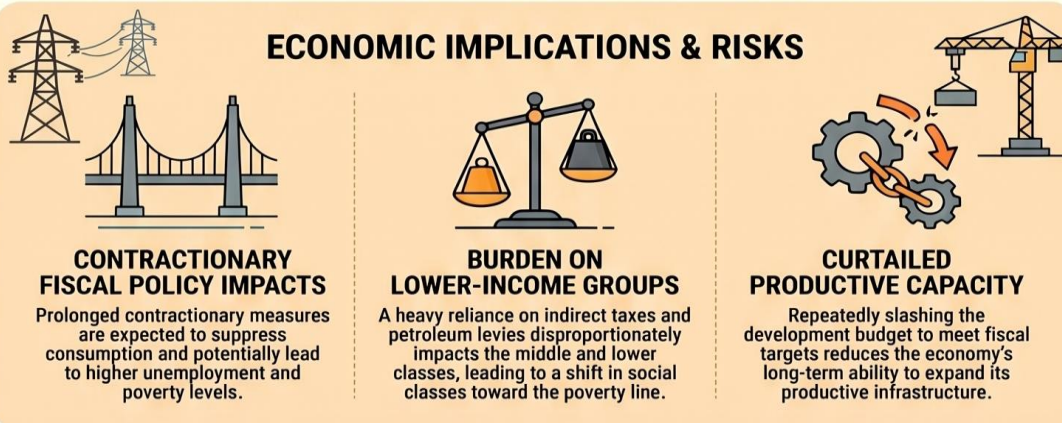
- There is no comprehensive tax policy in the country; only the finance bill is used to set taxes, which is not a policy document. Therefore, a comprehensive tax policy document should be developed, mentioning the importance of taxes, good taxation practice, the rationale of imposing each tax, and what mechanisms should be adopted in the imposition of new taxes and revising the number of existing taxes.
- The performance of the social safety program (i.e., BISP) and other programs needs to be evaluated while taking into account their graduation policy.

Federal Budget 2026-27: Fiscal Outlook, Economic Strategy, and Key Challenges

KEY DATA: MACRO-FINANCIAL FRAMEWORK & EXPENDITURE



ECONOMIC IMPLICATIONS & RISKS



STRATEGIC RECOMMENDATIONS



NotebookLM

Prepared by:

Dr. Zafar ul Hassan Almas

IPS Senior Associate and
Former Joint Chief Economist

Dr. Asim Ehsan

Senior Research Officer
Institute of Policy Studies, Islamabad

For Queries:

Shafaq Sarfraz

Head of Operations
Institute of Policy Studies, Islamabad.
shafaq@ips.net.pk | www.ips.org.pk