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IMPACT OF TARIFF REDUCTION ON AUTOMOBILE INDUSTRY

Authors

- Mohammad Shaaf Najib
  Research Fellow
- Dr. Usman Qadir
  Senior Research Economist
  Director (CITDE)

1. Setting the Stage

For decades Pakistan has been experiencing boom and bust cycles and been hamstrung by a foreign exchange constraint that requires a bailout from the IMF and restricting economic activity each time the economy overheats. The economy invariably ends up at this crossroads every few years, back to square one and having to start all over again.

As part of its International Monetary Fund (IMF)-backed economic reform agenda, Pakistan has agreed to gradually open up certain sectors, including the automotive industry. Pakistan has embarked on a sweeping five-year tariff reform plan, unveiled in the federal Budget 2025–26, with the explicit aim of shifting from import substitution to an export-led growth model. In a nutshell, the reform aims to streamline the customs duty structure, reducing the number of slabs from five to four—0%, 5%, 10%, and 15%—and lowering the average tariff rate from 19% to approximately 9.5% by FY2030. Regulatory and additional customs duties across numerous tariff lines will also be phased out over the next three to five years. These reforms are designed to make Pakistan's tariff regime more transparent, predictable, and regionally competitive.

For the automobile industry in particular, tariffs on Completely Built Units (CBUs) will be reduced from 20% to 15% over five years, while used-vehicle tariffs will start with a 40% surcharge above new vehicle rates in FY26, decreasing annually by 10% and ending at parity by 2030. The government also intends to abolish the “Fifth Schedule” exemptions and eliminate protectionist regulatory complexities. However, stakeholders in the industry have expressed concerns. Local OEMs caution that the sudden surge in used-car imports, potentially reaching 70,000–80,000 units annually, could devastate domestic vehicle production and reverse hard-won gains in local content, employment, and investment.

Concurrently, these tariff reductions support broader environmental goals: the government plans to introduce a carbon levy and incentives for electric vehicles (EVs), with aims to achieve 30% EV penetration among new vehicles by 2030. A proposed petrol-diesel levy may raise PKR 25–30 billion annually over five years that can fund EV infrastructure development.

Automobile manufacturers and assemblers in Pakistan have been operating for over 20 years behind protected tariff walls with a captive market and demand throttled by a booking system. Higher tariffs and an unfavourable exchange rate are the primary cause of price increases of vehicles. Now they are being asked to step out from behind their protected walls and compete with firms that operate outside Pakistan. Are the concerns of the local assemblers justified, or is it an aversion to change and the nudge towards competition? For the consumer, the change can be a welcome one; access to better quality, more choice, lower prices. The focus of the government on shifting from ICE to EV vehicles can receive a boost. This policy viewpoint will assess the potential gains and losses for each of these stakeholders in the economy.

2. Impact Assessment

I. Domestic Industry

There is no doubt that the reduction in tariffs for the automobile imports along with easing up the CBU vehicle import regulations will have significant impacts for the local automobile industry, but it does not mean that the impact will necessarily be one sided. On the contrary, there could be some positives gained from the reduction in tariffs while some new challenges will certainly arise as well. The probable impacts on the domestic industry as a result of the tariff reduction can be categorized according to increased competition, tariff induced cost reduction, improved vehicle affordability and labor market impact.

Increased Competition

Reduction in tariffs and easing up import regulations will increase the competition in the local automobile industry as a wider range of vehicles will be available for the consumers to pick from. As a result, some of the local industry players may face difficulties in adapting to the new circumstances and be forced to either limit their operations or even exit the industry. For others, this could be an opportunity to improve their products and maintain their share of the market.

Some of the new players with weaker local industry groups or smaller global brands are expected to be on the suffering end and lose their market share. However, the older brands in Pakistan and the bigger global brands among the new entrants shall be able to deal with the new challenge by adapting and competing with imported vehicles.

A similar scenario has been faced by the automobile industry on two occasions over the last two decades, which further supports that while some may suffer, others will benefit and improve. Firstly, following the ban on use of carburetor engines in Pakistan, Suzuki Alto was discontinued as the sales volumes were not high enough to invest in latest engine technology for the vehicle. However, Suzuki successfully managed to shift its Mehran and Cultus variants to engines complying with emission standards.

Secondly, global brands like Kia, Hyundai and Chevrolet entered the Pakistan market during early 2000s but were unable to sustain operations and exited as the local partner groups were not strong enough to compete and gain market share in a smaller market like Pakistan.

Thirdly, following the introduction of Automotive Development Policy 2016-21, many new players entered the Pakistan market. Though a few of them such as DFSK, Proton etc. were unable to make their mark in the local market, other brands of Korean and Chinese origin have

made a great positive impact on the local industry. Following the entry of these new brands, not only have C-SUV category vehicles now been made available in Pakistan which were not locally sold before, but the consumers have also been presented with locally assembled hybrid vehicles, which have received great feedback from the consumers. Seeing this, the Japanese brands which have been operating in Pakistan for decades, have taken the challenge heads on and also adapted to the needs of the consumers and introduced their own C-SUVs and HEVs. Thus proving, increased competition does not necessarily kill the existing players but instead is an opportunity for them to adapt and improve.

Tariff induced Cost Reduction

The lowering of tariffs on automobiles must not be limited to just CBU vehicles, instead a similar reduction in tariff must be implemented simultaneously for CKD imports as well, to ensure a level playing field for the local manufacturing and assembling OEMs. Lowering of tariffs on the CKD imports translate into a reduction in the cost of production for the OEMs in Pakistan and therefore enable them to remain competitive in a market with increased competition from CBU vehicles.

Improved Vehicle Affordability

A large portion of the final sale price of the vehicles in Pakistan, whether locally assembled or imported as CBUs, consists of taxes. In case of CBU imports, the high import tariffs are the only source of taxation on the vehicle purchase whereas for locally assembled vehicles import tariffs on import of CKD as well as other taxes and charges such as sales taxes, FED, and now the NEV levy are charged which increase the on-road price for the consumer.

In recent years, when the taxes have remained high and production costs have also increased, vehicle affordability has becoming difficult for the general public. With reduction in import taxes on the CBU and similar reduction in import tariffs for the CKD kits as well, the prices of vehicles are expected to reduce. This will improve the vehicle affordability among the general public and possibly contribute to an increase in demand for the vehicles. As a result, the improved demand will certainly have a positive impact on the industry and vehicle ownership in the country.

Jobs Creation and Deletion

The number of employed labor in the automobile industry vary vastly, depending on who you include in the list. The automobile industry consists of the automobile OEMs, automobile parts vendor industry, sales and after sales services, and the secondary parts and services market. The total number of people associated in all these sub-industries are much larger, however, the real and foremost impact of any automobile policy changes is witnessed in the employment in automobile OEMs, and the reduction in import tariffs will before anywhere else have a significant impact in the same.

Currently, the automobile OEMs directly employ approximately 10,000 people. These include both the employees involved in manufacturing processes, and other firm operations. Once the tariff reduction policy is implemented, these will certainly be a change in the workforce of OEMs, depending on how the industry and consumers react to the new policy. At worse, if not all, majority of the 10,000 jobs could be at risk if the local industry is unable to compete with the new and used imported CBU vehicles. This, however, remains the worst possible scenario

as a result of the policy change. It is though expected that some jobs might initially be lost in the OEMs following the introduction of the policy but as the imported CBU vehicles businesses pick up, new businesses and jobs will also be created as a result of this policy. These would most likely be related to import services, sales and after sales services of CBU automobiles as well as auto parts in the secondary market.

The loss of jobs in the OEM industry in the short run might be off-set with job creation in the longer run if the OEMs are able to maintain their market share, compete against the imported CBU vehicles and the automobile market expands through increased ownership.

The exact net extent of the job loss and job recreation in OEM industry and new business and job formation due to increased CBU vehicle imports will depend entirely on how the OEMs perform under the new regulations and how the consumers react to the availability of a wider range of vehicles after easing up of import regulations and tariffs.

Transformation in the Industry

The automobile industry in Pakistan has on more than once occasion undergone significant transformations and technological updates as a result of regulatory changes and/or competition. Following the introduction of AIDEP 2021-26, the automobile OEMs in Pakistan have upgraded the safety and security features in line with the global standards, as mandated by the policy. Similarly, in accordance with environmental regulations, the automobile OEMs phased out the carburetor engines in 2010 and shifted to EFI engines. Similarly, when new players entered the Pakistan market following the ADP 2016-21, the older firms also adapted and introduced vehicles in the C-SUV category, HEVs and upgraded the features and specs in line with the competition and as per the consumer demand.

These instances from the last decade or two represent the automobile industry's ability to upgrade and transform as per the needs of the market, be it through regulation or increased competition. While vehicles in Pakistan have significantly improved in terms of quality, features and specs, it is also a reality that they still lag behind many other countries. As a result, with easing of import regulations and reduction in import tariffs, consumers will have the option to choose from vehicles with better specs, features and quality. Such competition, as recent historical instances show, will act more as an opportunity and much needed push for the local industry to improve their products rather than a challenge to their survival.

ii. External Sector

Once the tariff reduction policy is implemented for the automobile industry as well, the impact will not be limited to just the industry alone. Instead, the change of trends within the industry will affect the overall macroeconomic situation, particularly the country's external sector as well. Reduction of tariff and easing of import regulations, particularly for used vehicles, will mean an increase in the demand of imported vehicles both new and old. This could have any of the following impact on the overall vehicle sales in the country:

1. Increase in sales of vehicles in the country, of both locally assembled vehicles and imported vehicles (new and used collectively).
2. New and used imported vehicle sales increase but locally assembled vehicles sales reduce.
3. CKD imports become negligible as OEMs reduce vehicle manufacturing/assembling in Pakistan, and shift to sales of imported CBUs through 3S dealerships, in addition to commercial import of new and used CBUs elsewise.

Considering scenario 3, if Pakistan imports approximately 200,000 CBU passenger cars annually for an average cost of USD 20,000 then the total import bill for these vehicles would be around USD approximately USD 4 billion per annum. This would mean that the import bill for the automobile passenger cars would almost double as compared to the scenario where these 200,000 cars are assembled locally after CKD imports. If following the implementation of the tariff reduction policy the situation evolves into either one of the scenario 1 or 2 instead of scenario 3, then the import bill for automobile industry will be higher than even USD 4 billion per annum.

Though USD 4 billion or even a slightly higher amount does not seem too big of a figure in a country's annual import bill, in Pakistan's current macroeconomic landscape it can though be a massive challenge.

The first pertinent question, giving Pakistan's low foreign exchange reserves is how will the additional import bill be financed? It will not be just a one-time requirement, instead the additional will be required permanently every year once the policy is implemented.

Secondly, even if the required foreign exchange is made available for the imports of vehicles, an increase in the import bill without considerable increase in exports will put additional pressure on the country's external sector. This additional demand for foreign exchange without any significant forex earnings will further depreciate the Pakistani rupee and contribute to inflation and market imbalances in the country.

Thirdly, it must be recognized that this is not just an automobile industry tariff reduction rather the tariffs will be removed for all sectors. This means that similar impact shall be expected from multiple sectors, if not all. The impact of increased imports without increasing exports and increasing foreign exchange earnings will thus be magnified.

In such a scenario, if the government is forced to roll back the tariff reduction or limit imports through other NTBs, then this entire exercise will have a much more drastic impact on the overall economy, including the automobile industry of Pakistan, as compared to maintaining the status quo. While the initial tariff reduction will create a disruption in the automobile sector as explained in the three scenarios above, if the policy is implemented and continued with, then the industry can be expected to adjust accordingly. If, however, the policy is rolled back due to the unavailability of foreign reserves to finance the increase in import bill, it will not be possible to bring the industry back to the pre tariff-reduction stage. The policy inconsistency will also send a discouraging message to investors and business community related to the automobile industry.

It is therefore recommended that before implementing the tariff reduction policy, particularly in context of the automobile industry, it must be ensured that the country has the foreign exchange reserves to finance the import bill and that there must not be any policy roll back after a short period of time.

PIDE's book *"Driving Backwards: What is Wrong with Pakistan's Automobile Industry"* details the recommended way forward for expansion and global integration of Pakistan's Automobile Industry.[1]

iii. Consumer Welfare

The Pakistani automobile market functions in a manner that fundamentally undermines consumer welfare. Unlike competitive retail markets in most countries, where vehicles are available off-the-lot and pricing reflects supply-demand dynamics, Pakistan's market is characterized by persistent shortages, booking queues, arbitrary delivery timelines, and limited model availability. This structure is a direct consequence of a protectionist policy regime that restricts

imports through high tariffs and non-tariff barriers, effectively shielding domestic assemblers from competition. The result is a supply-constrained market that operates more like a quota-based allocation mechanism than a competitive retail environment. Consumers are not buying in a market—they are waiting in a queue, paying arbitrary premiums, and making choices within a narrow, outdated menu.

Perhaps the most visible manifestation of the anti-consumer nature of this system is the persistence of the so-called "on-money" or a black market premium. This is an undocumented, extra-legal amount paid by buyers to 3S dealership owners or private owners of vehicles who tend to be operating either alone and at times in union with 3S dealerships to acquire a vehicle earlier than the official delivery schedule. On-money thrives under conditions of chronic undersupply, long booking delays, and limited alternatives. It is an artificial premium extracted purely due to market inefficiencies created by policy. Based on empirical estimates developed by PIDE, consumers have paid approximately PKR 30-34 billion per annum as on money during the period 2016-2020[2]. This figure is not just an indication of rent extraction—it is a quantifiable loss in consumer surplus, representing the cost of regulatory failure and market capture.

At the heart of the issue is a structure where new car availability is limited not by production capacity alone but by a deliberate policy-induced scarcity. Imports are heavily restricted and prohibitively taxed, while local production has not increased despite entry of over 10 OEMs who have managed to break the nexus of the infamous Big-Three. These assemblers operate within a structure designed solely to reward indigenization and parts localization but without necessarily offering global models, features, or technology to consumers. Many of the vehicles on offer in Pakistan are discontinued abroad or are older versions of models that have been upgraded or replaced in international markets. For example, either a generation older vehicles are introduced in the Pakistan market as compared to the global market, or if the same generation is introduced in Pakistan then it lacks numerous features available in the other markets.

The market's constrained structure has had an impact on ownership trends, affordability, and the overall value proposition of owning a vehicle. Due to high tariff walls on imports—up to 100% for used vehicles in some categories—prices remain artificially inflated. Vehicle ownership remains low by international standards, with approximately 18 cars per 1,000 people in Pakistan compared to over 150 in neighboring India and well above 400 in upper-middle-income countries. Tariff liberalization has the potential to dramatically alter this equation. Lowering import duties would improve price competition, expand product variety, raise quality standards, and put pressure on local assemblers to offer newer technologies and better customer service. Cross-country experiences from countries such as Thailand and Indonesia, both of which liberalized their auto markets over time, show that tariff reduction coupled with competition enhances consumer outcomes without necessarily killing off local production/assembly (Doner, 2006).

More importantly, a liberalized market can evolve into a dynamic ecosystem where assemblers respond to consumer needs, not just to regulator-defined localization targets. The objective should be to create a market where consumers can walk into a dealership and choose from multiple globally competitive options, priced transparently, delivered immediately, and backed by efficient after-sales service. In such a market, on-money would have no space to exist, and assemblers would compete not on access but on quality, design, price, and innovation.

The current system, in contrast, suppresses both supply and innovation, while imposing a high and hidden cost on consumers. The magnitude of consumer welfare loss, as evidenced by PIDE's on-money estimates, is a sufficient policy signal to move away from protectionism and towards market liberalization. Tariff rationalization should be seen not only as an instrument of industrial competitiveness but as a necessary step to restore consumer dignity in a distorted market.

Consumer welfare must therefore be brought to the center of any serious conversation on the future of Pakistan's automobile sector. It is only when the sector operates freely, competitively, and transparently that it can generate the immense benefits it promises—not just for industrial policy, but for millions of Pakistani consumers to get value for their money, and the freedom to choice.

3. Way Forward for Pakistan

i. Developing a New Import Framework

Currently, in Pakistan, commercial import of used vehicles is not permitted. Instead, as per the rules, only Pakistani nationals living abroad can under following three schemes transfer a vehicle from abroad to Pakistan:

i. Personal Baggage

ii. Gift Scheme

iii. Transfer of Residence

Technically, any transfer of vehicle from abroad to Pakistan under these three schemes cannot be termed as an import of vehicle as no sale is supposedly occurring. Yet, a large number of vehicles every year are shipped to Pakistan under this scheme, exploiting the legal shortcomings and loopholes. Furthermore, a number of post-accident damaged vehicles are also shipped into the country and refurbished locally before being sold in the secondary market. It is possible as the import criterion is pegged against manufacturing date and not vehicular condition. Consequently, it raises valid concerns regarding the on-road safety, security and overall quality of these refurbished vehicles.

In line with the agreement with the IMF, as Pakistan steps towards decreasing import tariffs on the imports of new and used CBU vehicles, it is time that a new framework regarding import of used cars is developed. This framework will allow for a regulated import of used vehicles in Pakistan ensuring that safety standards and vehicle quality are maintained, a fair competition to the local automobile industry is presented and the consumers are provided with a wide range of quality yet affordable vehicles. Subsequently, PIDE proposes that commercial import of used vehicles must be allowed with reduced tariff as per the following framework:

1. Commercial import of used CBU vehicles must be allowed to private motor vehicle dealers.

2. Business registration with the FBR must be mandatory for private motor vehicle dealers to import used CBU vehicles into the country.

3. Commercial import of used CBU vehicles must be limited to only following four auction grades as per the Japanese Automotive Standards Organization (JSO) grading system[3]:

   I. Grade S
   II. Grade 6
   III. Grade 5
   IV. Grade 4.5

4. Attaching verified auction sheet must be mandatory for the registration of imported used CBU vehicles in the excise and taxation department.

5. In order to prevent the exploitation of three existing schemes, following measures must be taken:

   I. Vehicles shipped under the personal baggage, transfer of residence, and gift scheme must be taxed at a higher tariff as compared to commercial import vehicles.
   II. Vehicles shipped under the three schemes must not be sold in Pakistan for at least one year after excise registration.
   III. Vehicles shipped under the personal baggage or transfer residence scheme must be registered in Excise & Taxation department on the name of the shipper.
   IV. Vehicles shipped under the gift scheme must be registered in Excise & Taxation department only against the name of the gift recipient. Gift recipient must be specified in the shipment documents.

6. Import tariff must be higher for vehicles of bigger engine capacity to discourage import of high fuel consuming vehicles.

7. A lower tariff must be imposed on import of HEVs and PHEVs as compared to ICEVs of equivalent engine capacity, to promote use and import of environment friendly vehicles, in line with the new NEV Policy.

ii. Transitioning to an Electric Future

Pakistan, in line with the global efforts, is undertaking major reforms and initiatives to transition to Electric Vehicles. The recently launched New Energy Vehicle Policy (2025-30) has set aggressive and ambitious EV adoption targets, while the policy itself is a major step towards government's efforts for incentivizing industry and consumers alike to shift to electric vehicles in coming. It is essential that, as outlined in the NEV Policy as well, that tariffs on EVs and EV parts and components are aligned with the principles laid out in the NTP 2025-30.

However, tariffs are just one component of the crucial determinants of EV adoption in the country. While EVs due to the absence of an engine lack a massive number of mechanical and electrical parts as compared to the ICEVs, they are not necessarily maintenance free. Instead, the handling and maintenance of the batteries requires an entirely separate set of skills. As the EV technology is relatively new even on a global scale, and with limited adoption in Pakistan currently, effective after sales services are absent. In such circumstances, any EV breakdown could result in adding on to the narrative against EVs and further challenge their adoption in the country.

Consequently, it is pertinent that the government focuses not just on EV adoption but ensuring that abundant after sales services are present. For this purpose, more companies must be incentivized to not just import CBU EVs for sale in Pakistan, but to be present in the country through their dealership network and after sales services before vehicle sales are initiated. In the medium and long run, more OEMs must be targeted for manufacturing in Pakistan to facilitate the smooth transition towards EVs.

1. https://pide.org.pk/research/driving-backwards-what-is-wrong-with-pakistans-automobile-industry/
2. Ibid
3. ibid

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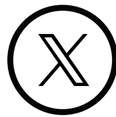

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