



BULLISH MARKETS, BEARISH EXPORTS: AN EMPIRICAL INQUIRY INTO PAKISTAN'S ECONOMIC DIVERGENCE

Dr. Zahid Iqbal

Assistant Professor, Department of Commerce, University of Kamalia, Punjab, Pakistan.

Email: zahidiqballak@gmail.com

Rabia Aslam

M.Phil. Sociology Department of Sociology, University of Okara, Punjab, Pakistan.

Email: rabiaaslamab4@gmail.com

Mr. Khalid Mehmood

PhD Scholar, Department of Education, University of Okara, Lahore, Pakistan.

Email: chkhalidgujjar56@gmail.com

Shazia Akram

PhD Scholar, Time Institute, Multan, Punjab, Pakistan.

Email: shaziaakramnayaab98@gmail.com

Abstract

This paper explores structural reasons for the discord between the economic fundamentals of Pakistan and the performance of the Pakistan Stock Exchange (PSX), focusing on the country's export sector. The author conducts a thematic analysis of the market, the macroeconomic and institutional frameworks, and identifies a 'Dual Economy' phenomenon. Although the PSX index shows a bullish trend, the driving PSX index construction constituents are non-export-oriented sectors (i.e. banking, energy, and fertilizers). These sectors are further driven by nominal market distorting variables (i.e. inflation and currency depreciation). The author argues that market growth is entirely liquidity driven. It has created a highly speculative market, rather than one that promotes industrial upgrading and export competitiveness. The author examines the institutional preoccupations of the bias towards the stability of the capital markets over the development of the real economy, regulatory capture, and the high costs of production on the export-oriented and SME sector, and argues that these created conditions that allow the capital market to function as an isolated financial loop. Therefore, the author argues that the PSX does not contribute to Pakistan's sustainable development. The author argues that unless the PSX is reformed to allow for export-linked capital market incursion, and the present speculative trading is restructured to allow for productive investment, the PSX will continue to be a narrow economic indicator of wealth for the elite of the country, and will offer little to the country's economic resilience over the long run.

Keywords: *Pakistan Stock Exchange (PSX), Export Competitiveness, Dual Economy, Financialization, Macroeconomic Instability.*

1. Introduction

The growth of the Pakistan Stock Exchange across the past decade could be indicative the significant economic evolution of the country. Major leaps in the indexes occurred dual in correlation and causation with decreased regulatory limits, enforcement of restraining interest rates, increased both institutional and retail stake purchases in dwindling currency/decreasing economic stability hedges, and currency depreciation, among others. (Hussain et al., 2024). In the past and present, Pakistan Stock Exchange continues the historical trend and ignorant of the poor economic fundamentals, employs the speculators, and of poor economic fundamentals drives the assets beyond the reasonable economic justification (Verma and Bansal 2021). In



general, expectations are that market performance, reflected in the indexes, is substantiated by the industrial and economic performance. Expectations of the market performance in the PSI is the performance of the economy as a whole and economic stability and justification reflects in the overall economic performance. Most analysts believe that, in the case of Pakistan, market optimism is largely the result of temporary policy changes, IMF program announcements and liquidity positions, rather than lasting improvements in the country's productive capacity and/or its competitiveness (Rashid, Jehan, & Kanval, 2023). Thus, the continuing increase of the PSX, in comparison to the persistent increase of the PSX, suggests an analysis of other economic fundamentals, especially the most critical components of sustainable growth: exports.

The stagnation of the export sector and the cyclical declines stand in contrast to the strong performance of the stock markets in Pakistan. While stock markets are performing well, the export sector is stuck in structural stagnation (Seven & Yilmaz, 2021). Exports lack diversity and continue to be heavily concentrated on low value-added textiles and apparel. This concentration drives Pakistan to be export competitors like Bangladesh or Vietnam, and drives Pakistan to be vulnerable to global demand fluctuations and price competition. Policy reversals, trade incentives which are not consistent, and a lack of recognition for the dire need of increasing regulations cause a lack of planning for exporters. Time and again, Pakistan has been hit with episodes of currency depreciations. The expectation is that exports will logically rise with depreciations since Pakistan will be in a position to sell cheaper than competing countries. However, Pakistan has never achieved even a minimal level of export led growth, thus showing the need for better supply side constraints. External factors really took a toll on the already struggling export sector. Neither the COVID-19 pandemic, inflation, or the current geopolitical tensions are helping the struggling export earnings. The structural trade weaknesses continue to be highlighted by the balance of payments pressure (Mubarik, Devadason, & Govindaraju, 2020).

The problem becomes even more complex when we consider the presence of a rising PSX index alongside stagnant or declining exports, which goes against the basic principles of economics. Most growth theories suggest that as markets develop, so too do the real sectors of the economy by way of investment, productivity, and international competitiveness (Qasim, Rizov, & Zhang, 2021). In Pakistan, we observe the opposite phenomenon, a greater emphasis on financial markets but worse performance in trade. This creates a big paradox for us: does the growth of the Pakistan stock market reflect real economic growth, or is it growing for the sake of growth with no economic foundation (Tabash, Babar, Sheikh, Khan, & Anagreh, 2022)? In the current study, we tend to answer this paradox by examining the variety of patterns that constitute this paradox. To this end, the study will explore the integration of long-term patterns with the PSX index and export performance, the correlation between export growth and financial market performance, and the variables that cause the absence of this correlation. The aim is to ascertain, in the context of Pakistan, whether the growth of the stock market has had a real economic effect, or if the economy has only witnessed an increase in the prices of financial instruments. This will add value to the conversation around financial market growth strategies in developing countries and their effectiveness (El-Diftar, 2023).

Thus, a review of available studies shows that most previous research regarding Pakistan has focused on stock market performance and export behavior as two different phenomena. Most of the research done on the PSX has focused on the correlation of the PSX with macroeconomic factors such as inflation, interest and exchange rates, and political instability (Shaikh, Channar, Shaikh, & Ullah, 2021). Similarly, export research has focused



on issues of competitiveness, diversification, and trade policy, often ignoring developments in the financial markets. Although some studies done internationally look at the relationship between overall economic growth and financial market development, the empirical studies analyzing the divergence of stock market indices and export performance in Pakistan are very few (Erdoğan, Gedikli, & Çevik, 2020). Furthermore, very few studies ask the question of whether the increase in stock market indices in developing countries truly reflect an increase in productive capacity. The lack of such studies shows the most important gap in the field of research. This study, by examining the bilateral relationship between PSX trends and export dynamics for the first time, enriches the literature on financial economics and international trade on Pakistan in a unique way (Khan, 2024).

In Pakistan and similar developing economies, the implicit reshaping of how economic performance is perceived is one of the most important facets of this research. It is the first research of its kind to identify and specify the gap between stock market growth and export performance, and criticize Shabbir, Kousar, and Batool (2020)'s assumption that increasing stock market indices is a sign of economically strengthening the country. For the policymakers, the stock market indices are believed to show the level of the investors' confidence and the stability of the economy, which, in this study and others, economically, are proven to be deficient. These present various degrees of growing economies that are characterized by a declining or underdeveloped financial sector, and a developed, or strengthening, financial market. This study is for the investors, as well, as stock market increases without export growth are economically unsustainable (Hashmi, Chang, Huang, and Uche, 2022). This emphasizes the gap between financializations and structural transform of developing economies, which is a growing body of literature in the developing economies. Kahn and Ullah (2021) corroborate this study in compelling developing economies to undertake structural financial developments to improve economic stability and resilience.

The sequence of the study proceeds as follows: Chapter two reviews the literature on judicial review, nullified judgments, and the operational bottlenecks of the lower judiciary, while chapter three describes the research framework, including the methodology, criteria for case selection, and the phases of data collection and analysis. In chapter four, findings and analysis are discussed, focusing on the principal and sub themes concerning the lower courts' voided decisions. Chapter five focuses on the implications and limitations of the study, including suggestions for further research.

2. Literature Review

There has been much research conducted on the correlation between stock market growth and economic growth in developing as well as developed countries; however, the research has been inconclusive. Some of the earliest research proposed that stock markets should stimulate economic growth by encouraging the mobilization of savings, allocation of capital, improvement of corporate governance, and diversification of risk. (Alamgir and Amin 2021). Most research conducted in this emerging economy population group has found positive correlations between stock market growth (i.e., greater market capitalization and greater liquidity) and GDP growth. Financial development and real sector growth (expansion in the developing real economy) are tightly linked (Ghani and Ghani 2024). Most recent research has also pointed out that this relationship is, in most cases, neither spontaneous nor the same among all countries. In developing nations with lower levels of institutional development, the growth of the stock market is specked by unproductive, speculative trading and short-run capital mobility that are, in most cases, devoid of economic sustainability (Kose and Unal, 2020). In



the case of developing economies such as Pakistan, stock market development is significantly influenced by monetary policy, politics, and speculation and does not contribute much to the growth of the real economy. It is these circumstances that gives much cause for concern in most developing economies.

The export-led growth theory explains the mechanics of how a country can achieve sustained economic growth by adopting trade policies that are ‘outward-oriented’, i.e. policies that promote exports because they create a widening of the productive base of the economy and thus generate employment and foreign exchange. In the classical and neo-classical trade theories, when countries export, they are said to be able to attain comparative advantage, economies of scale and also gain access to modern and superior technologies through competition on a global scale (Tabash, Sheikh, & Asad, 2020). East Asian economies are extensively documented to support the ELG hypothesis. In these countries, diversified exports of value-added manufacturing drove sustained growth (Shehzad et al., 2022). Yet, the applicability of this theory to developing countries, in particular to Pakistan, has been contentious. Research shows that the primary, low-value, and even below primary exports, technological low-intensity, structural constraints, and restricted markets of these countries export levels do not optimize the economic growth enhancing potential of the exports (Hayat, Hussain, & Lohano, 2020). In Pakistan, a lack of sufficient export growth means that there are only limited backward and forward linkages to the domestic economy, and so this has restricted overall economic development. Export performance in this country is documented as a critical, albeit relatively ignored, sustainable growth dimension (Habiba & Zhang, 2020).

There is a rich body of literature on financialization and economic decoupling which helps make sense of the differing performance of financial markets and the underlying economy. Financialization is defined as the increasing control of financial motives, markets, and institutions over the productive investment and trade (Khan, Ullah, Alim, & Haq, 2022). It is argued that as financialization deepens, there is a tendency to decouple asset prices from underlying economic fundamentals, and the economy begins to grow from speculation rather than production (Peng et al, 2021). Numerous studies document the existence of stock market booms alongside stagnating wages, slow industrial growth, and worsening export performance in a number of developing countries (Naseer, Khan, Popp, & Oláh, 2021). Such decoupling is exacerbated by short-term capital inflows, financial liberalization, and a permissive monetary policy stance that inflate asset prices and do not build the productive capacity of an economy. In Pakistan, there is very little work to examine the stock market–export relationship through the lens of financialization. This is an important gap in the literature. This study seeks to fill this gap by demonstrating the integration of financialization theory, export theory, and stock market theory that is aimed at understanding how an expanded financial sector may negatively impact real sector and trade related growth in developing economies (Kumar, 2020).

3. Methodology

In this case, a qualitative research design is utilized to comprehend and analyze the possible reasons for the divergence between stock market performance and export dynamics in Pakistan by focusing mainly on perceptions, the role of institutions, and policy narratives. Primary qualitative data were collected via key informant interviews with stock exchange brokers and exporters, who were identified through purposive sampling to ensure the inclusion of informed market participants who are active in the finance and trade sectors. Brokers’ insights were valuable in understanding the investment behavior, market sentiment, and other factors that drive the growth of the PSX index, while exporters tackled the structural, competitive, and



policy-related constraints of negative export performance. Interviews of this type are described as semi-structured to allow the respondent to give a more elaborate response regarding his/her experience while maintaining a degree of uniformity on the central themes (Creswell & Poth, 2018). The interviews were analyzed through qualitative thematic analysis, a method which entails the transcription of interviews and rigor in coding, categorizing, and interpreting recurring themes and patterns in the data (Kashif, Palwishah, Ahmed, Vveinhardt, & Streimikiene, 2021). In order to see more data patterns and more outstanding variables, more careful analytical techniques were utilized. The textual data were analyzed using word clouds and word trees to determine the most salient narratives, the most frequently used words, and the most important logical connections between the main ideas (Asad, Tabash, Sheikh, Al-Muhanadi, & Ahmad, 2020).

The study also includes a detailed policy and document review, beyond primary data, to frame the interview findings within specific institutional and macroeconomic perspectives. The author analyzed documents relating to policies, such as trade, export incentive, monetary policy, and stock market regulation, to understand the alignment of strategies concerning the development of financial markets and export-led growth. This document analysis, along with the qualitative evidence, helped to address the gap between the policy and the resultant outcomes of the economy (Zahid, Khurshid, Waheed, & Sanni, 2022). Thematic analysis of the policies concerning financialization, investment promotion, and export competitiveness was also applied. Using a combination of interview data and documentary evidence meant that the study achieved credibility and validity through methodological triangulation (Chang et al., 2021). This qualitative study, in particular, describes the phenomenon of financial market optimism and the challenges within the export sector in a manner that quantitative study findings may not present. The complexity of the phenomenon of economic decoupling in developing countries is particularly well captured using this methodology, especially with the institutional complexity and the stakeholder attitudes that underpin them (Naz & Gulzar, 2023). The respondents were asked the following questions.

- Why is Pakistan's stock market index rising while exports are declining?
- What structural and policy factors explain the disconnect between financial markets and export performance?
- Does PSX growth reflect real economic strength or financialization?

4. Results and Analysis

The themes presented in Table I collectively reveal that the growth of the Pakistan Stock Exchange is largely driven by sectors that are either weakly connected or entirely disconnected from export performance. The dominance of banking, energy, cement, fertilizer, and telecommunications companies in the PSX index indicates that index movements are primarily influenced by domestically oriented or regulated sectors rather than export-intensive industries. These sectors often benefit from administered pricing mechanisms, government protection, or domestic demand expansion, which allows profitability to increase independently of international trade conditions. As a result, export-oriented firms remain underrepresented or unlisted, limiting the ability of the stock index to capture developments in Pakistan's trade sector. This structural composition of the PSX explains why index growth does not translate into improved export outcomes, as financial performance is anchored in non-tradable or inward-looking segments of the economy. Consequently, the stock market reflects internal



liquidity conditions and sector-specific rents rather than the country's external competitiveness or productive export capacity.

The second critical insight from the table has to do with the speculative and macroeconomic pressures influencing stock market rallies, which further aggravates the disconnect between financial parameters and the real economy. Excess liquidity, a result of a highly accommodative monetary policy and inflationary pressures, has transitioned most investors to equities to protect their investments from a depreciating currency with real returns on savings decreasing. This scenario has given rise to short-term capital inflows, herd mentality, and momentum trading, thus worsening the inflation of financial assets which has no direct correlation with increases in real output and foreign exchange (forex) earnings. In addition, currency depreciation directly inflates stock prices in rupees, which creates a false perception of real growth in a declining economy. In periods of pronounced nominal effects, real economic activities are left to withdraw and stock markets enjoy the effects of the nominal. In the stock market, nominal effects are a result of real currency depreciations and increased flexibility.

The last few themes point to fundamental structural and institutional weaknesses that are perpetuating an illusion of economic growth, with the primary symptom being the rising stock index. Weak export competitiveness, which is the result of high production costs, low levels of technology, and narrow diversification of products, hinders Pakistan's ability to adjust to shifts in global demand or respond to the growing levels of competition in international markets. The divergence of policy priorities toward the stabilization of the financial markets, in place of financial market policies that promote exports, has caused incoherent industrial policies, policy lags in the provision of incentives to exporters, and the under-provision of institutional support for trade. In addition to the above, the under-developed, poor articulation of, and compromised linkages between the financial markets and productive investment means that financial assets are frequently used for debt servicing or speculation rather than enhancing the country's export capacity. The combination of institutional fragmentation, lack of effective governance, and absence of any long-term vision for the industrial sector has exacerbated the misalignment between trade and financial development. Collectively, these characteristics point to the Pakistan Stock Exchange (PSX) index being a shallow and, in all likelihood, misleading indicator of economic performance as it fails to capture the underlying weaknesses in the real economy and the worsening state of Pakistan's exports.



Table-I: Themes Descriptions

Sr.	Main Theme	Sub-Categories / Sub-Themes
1	Financial Market Growth Driven by Non-Export Sectors	<ul style="list-style-type: none">• Dominance of banking, energy, cement, fertilizer, and telecom sectors in PSX• Limited representation of export-oriented firms in the index• Stock index growth reflecting domestic demand or regulated profits• Export-intensive sectors underrepresented or unlisted• Index performance not linked to trade outcomes
2	Speculative and Liquidity-Driven Stock Market Rallies	<ul style="list-style-type: none">• Stock market growth driven by excess liquidity• Short-term speculative capital inflows• Interest rate expectations and monetary policy signals• Herd behavior and momentum trading• Disconnect between stock prices and productive activity
3	Macroeconomic Distortions and Inflationary Effects	<ul style="list-style-type: none">• Inflation pushing nominal asset prices upward• Currency depreciation inflating rupee-denominated stock values• Real economic contraction masked by nominal index growth• Stock market acting as an inflation hedge• Decline in real export competitiveness
4	Weak Export Competitiveness and Structural Constraints	<ul style="list-style-type: none">• High cost of production (energy, inputs, finance)• Low productivity and outdated technology• Limited value addition and product diversification• Dependence on low-value exports (textiles, rice)• Inability to meet international quality and compliance standards
5	Policy Bias Toward Financial Stability Over Export Growth	<ul style="list-style-type: none">• Policy focus on stabilizing financial markets• Incentives favoring capital markets rather than exporters• Delayed export refunds and rebates• Inconsistent trade and industrial policies



6	Exchange Rate and Capital Flow Dynamics	<ul style="list-style-type: none">• Weak export-promotion institutions• Exchange rate managed to attract portfolio investment• Overvaluation or volatility harming exporters• Capital inflows boosting stock prices but not exports• Exporters facing uncertainty in pricing and contracts• Short-term capital favored over long-term trade competitiveness
7	Global Demand Shocks and Trade Environment	<ul style="list-style-type: none">• Global economic slowdown reducing demand• Increased competition from regional exporters• Protectionist policies in importing countries• Shifts in global supply chains• Limited market diversification by Pakistan
8	Weak Linkages Between Capital Markets and Productive Investment	<ul style="list-style-type: none">• Capital raised not invested in export capacity• Retained earnings used for debt servicing or speculation• Limited IPOs from export-oriented firms• Poor access of SMEs and exporters to capital markets• Financialization without industrial upgrading
9	Institutional and Governance Constraints	<ul style="list-style-type: none">• Ineffective coordination between trade, finance, and industry ministries• Regulatory focus on market confidence rather than export performance• Corruption and rent-seeking behavior• Lack of long-term industrial strategy• Absence of export-linked capital market reforms
10	Illusion of Economic Growth and Misleading Indicators	<ul style="list-style-type: none">• Stock index as a narrow indicator of economic health• Export decline signaling real-sector weakness• Growth without production or competitiveness• Misinterpretation of financial indicators by policymakers• Disconnect between financial optimism and trade reality



QUALITATIVE RESEARCH JOURNAL FOR SOCIAL STUDIES

ISSN Online: 3006-4686, ISSN Print: 3006-4678

Volume No: 02 Issue No: 04 (2025)



Figure-1: Word Clouds



Figure-2: Word Mapping



Figure-3: Word Tree

5. Discussion

These study results validate and build upon the existing literature concerning the weak and non-linear relationship between stock market performance and real sector growth in developing economies. The absence of export-oriented sectors in the PSX, combined with a liquidity-driven and speculative market behavior, underpins scholars' arguments that stock market growth in Pakistan is a reflection of financialization, rather than a reflection of economically productive growth. The results, similar to other studies, suggest that stock market indices can increase as a result of a monetary relaxation, coupled with inflationary hedging and short-term speculative capital, even in the absence of export competitiveness (Mroua & Trabelsi, 2020). This decoupling is consistent with the prevailing theory that excessive growth of financial sector can misallocate capital by distorting the poorer investment choices, particularly in non-export-oriented and industrial upgrading (Sheikh, Asad, Ahmed & Mukhtar, 2020). In addition, the inflationary and exchange rate impact that were observed in the study suggests



that growth in nominal stock indices could be hiding a real economic contraction, which reiterates the warning from scholars that indicators of financial growth should not be taken as economic growth (Masrizal, Sukmana, Al Mustofa & Herianingrum, 2021). The trade and policy implications of the findings challenges the tenets of export-led growth, particularly with regard to the assumption of the absence of structural and institutional constraints. Hussain et al. (2022) state that while export-led growth is successful in countries that have a diversified portfolio of exports and a diversified industrial policy (Hussain et al. 2022) - in the case of Pakistan, a developed (or expanding) financial market cannot substitute a robust export framework and an actionable export policy. The author's state that the policy bias, which focuses on financial market stability and ignores the promotion of exports, combined with the insufficient relationships between the capital markets and productive investment, defines the stagnated potential of exports becoming an engine of growth. These analyses suggest that in order to pivot economic policy in a productive manner, the integration of capital market development with export development is necessary. This includes the promotion of export-oriented listings, the enhancement of financial accessibility to exporters, and the synchronization of monetary and trade policies. This study, by highlighting the absence of export growth for the stock market to grow, contributes to the understanding of the growth dynamics in developing countries and presents policies that can be adopted in order to effect positive change (Hussain et al. 2024)

5.1. Practical/Managerial Implications.

The results of this study show possible impacts of study results to different actors within the economy such as policy makers, regulators, investors, exporters, and stakeholders within financial markets, showing the adverse effects and the pitfalls of using stock market performance solely as a barometer of the economy. For policymakers, evidence of a disconnect between the performance of the Pakistan Stock Exchange and the performance of exports serves as a signal to reframe economic policy in a way that focuses more on real economy and exports driven growth, as opposed to prioritizing short-term stability in the financial markets. In this study, the government institutions are the intended audience when it comes to the suggestions on integrated market development policies that are in synch with the industrial development, export diversification, and productivity enhancement. The findings of this study are also useful for regulators and market managers in the promotion of a higher degree of representation of export-oriented companies on the stock exchange, the provision of a more equitable and subsidized finance for exporters, and the promotion of policies for the capital market that are more preferential to productive investment. The findings of this study are useful to investors in that it improves their understanding of investment and market risks by showing that rising stock market indices in an economy are subject to liquidity, inflation and other speculative activities, rather than to the underlying economic fundamentals of the country. Exporters and business associations of Pakistan are also important stakeholders of this research, as they would use this research to support consistent trade policy, timely market interventions, and reforms that reduce production costs and improve competitiveness. Additionally, the qualitative methodology of this study can be used by development practitioners and researchers to gain insights into structural distortions in other developing economies. From this perspective, the study contributes a practical blueprint to facilitate the creation of a more balanced growth model whereby the expansion of financial markets, in support of export competitiveness, substitutes for and fosters the long-term economic resilience.



5.3. Limitations and Avenue for Further Studies

This research study, like all others, has some limitations. First, the research is based mainly on qualitative data coming from a handful of brokers at the stock exchange and some exporters. While this data is rich and insightful, it does not capture all the possible perspectives from the various sectors and regions of Pakistan. Second, this research study has concentrated on thematic interpretation and document analysis, foregoing the quantification and econometric testing attributable to the assessment of the stock market performance and export trends. Third, the findings of this research study are context-specific and applicable only to Pakistan and cannot be generalized to other developing markets and economies that may have different structures and market systems. The limitations of this research study can be addressed by future researcher implementing a mixed-method design, or purely quantitative methodology, such as time-series or panel data analysis, and empirically testing the relationships between stock market indices, exports, and economic growth. Besides, expanding the sample to include policymakers, regulators, and manufacturing firms would give a richer perspective of the institutional dynamics involved. Finally, the emerging markets that have recently experienced a decoupling of financial markets from exports would be of interest to this research in ascertaining whether such decoupling is a broad structural shift or is a country-specific occurrence.

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