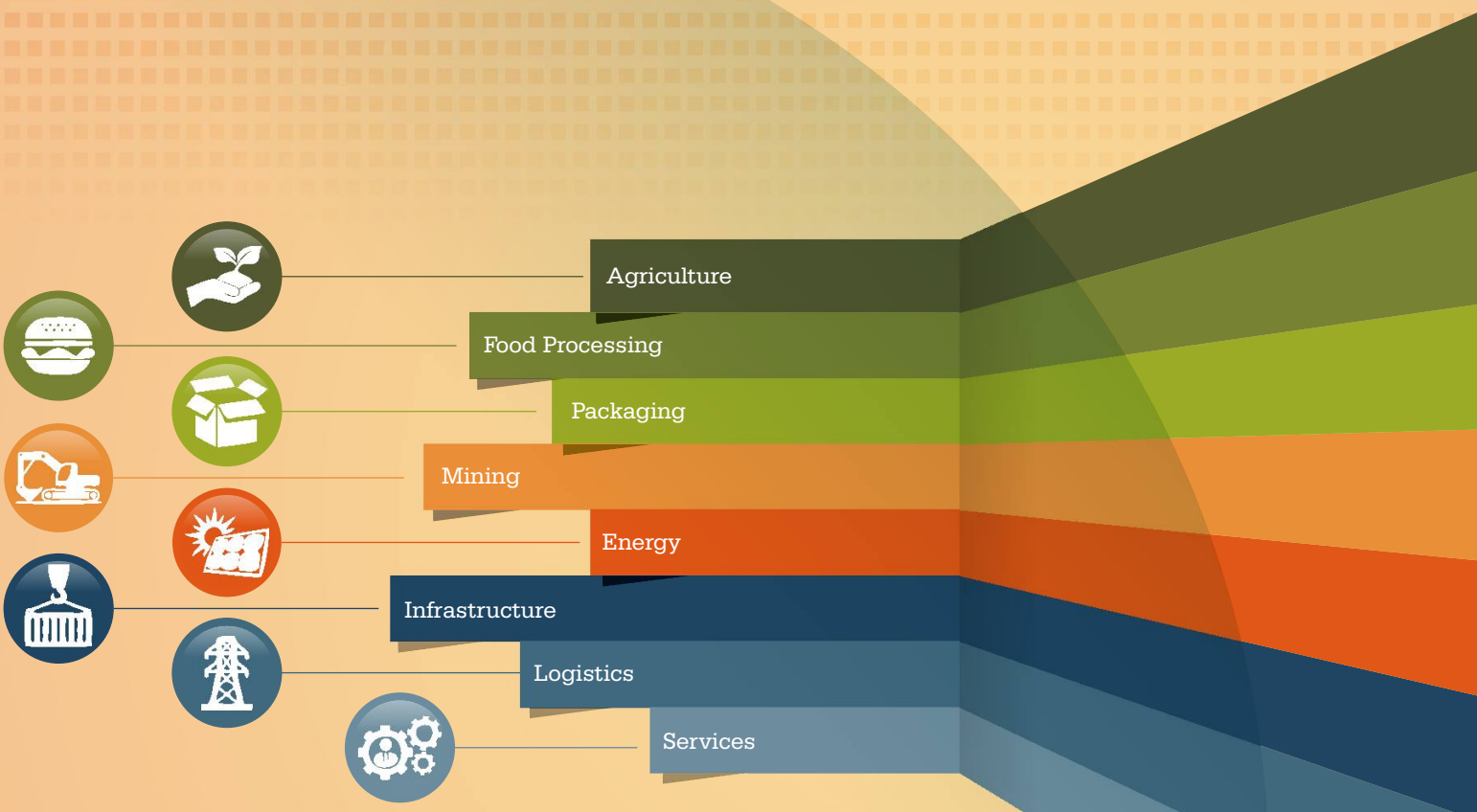
FICCI

UNITED NATIONS
ESCAP
Economic and Social Commission for Asia and the Pacific
South and South-West Asia Office



Doing Business with

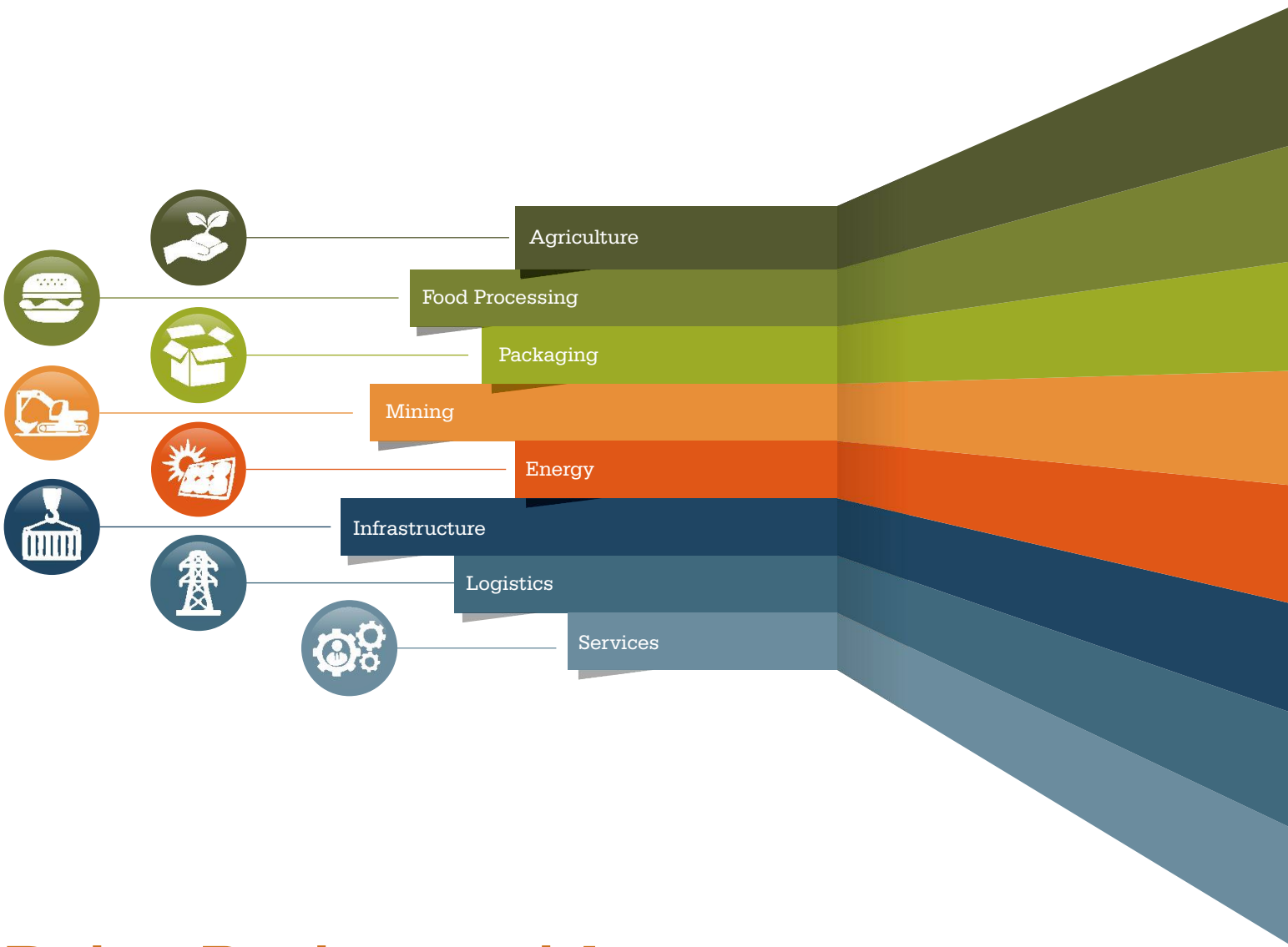
AFGHANISTAN

Harnessing Afghanistan's Economic Potential

NOVEMBER, 2013

FICCI

UNITED NATIONS
ESCAP
Economic and Social Commission for Asia and the Pacific
South and South-West Asia Office



Doing Business with

AFGHANISTAN

Harnessing Afghanistan's Economic Potential

NOVEMBER, 2013

Table of Contents

Chapter 1:	Afghanistan: Macro-Economic Setting	3
Chapter 2:	The Policy Environment for Promoting Investment	9
Chapter 3:	Sector Opportunities	15
Chapter 4:	Getting Started	31
Chapter 5:	Indo-Afghan Ties	35
Chapter 6:	Conclusions	43



Chapter 1

Afghanistan: Macro-Economic Setting

1 Afghanistan: Macro-Economic Setting



Emerging from twenty five years of conflict, Afghanistan, a landlocked and one of the poorest countries of the world, had performed better than the strong performers among the comparator countries in terms of broad macroeconomic indicators (Table 1).The economic growth has been robust; inflation has been low and public finance management made healthy progress[1]. Between 2002 and 2009, average per capita GDP increased by more than 75 per cent in real terms[2]. Debt- to - GDP ratio declined from 19.8 percent in 2008/09 to 8.1 percent in 2010/11 and debt service was 1.8 percent of exports of goods and services[3]. According to the IMF, the real GDP growth in 2012 has been 12 percent buttressed by a good agricultural harvest, which helped to moderate inflation at 6 percent year-on-year in December 2012[4]. Per capita income of Afghanistan in 2012 was estimated at about $680[5]. The net international reserves stood at US$ 6.35 billion equivalent to approximately 7 months of imports. The exchange rate has depreciated by 6 percent during 2012 and continued to depreciate at the same rate in 2013 since the beginning of 2013 and this is in line with other regional currencies. Bank deposits stagnated at 20 percent of GDP since 2010; 65 percent of it dollarized[6]. Substantial donor-support and international military spending had been crucial in Afghanistan's progress. Structurally, years of good growth have also been years of good harvest. Evolving gradually, the policy development during this period has been laying foundation for private sector development.

Comprehensive statistical information on Afghanistan is lacking. The statistical tables presented here are based on secondary sources and are therefore subject to the same limitations that apply to the original data source.

---

[1] *The growth of budget from US$ 346 million in 2002/03 to US$ 3.3 billion in 2010/11 demonstrated the rising absorptive capacity of the economy for the funds channelized through the budget. Over the same period, domestic revenue grew from 3 percent of the GDP to 11 percent due to the reforms in tax and customs administration. See, The World Bank, Afghanistan in Transition: Looking Beyond 2014, Volume 2: Main Report, May 2012. p.35.*

[2] *Ibid., pp. 5-8. Strong performing comparator countries include Cambodia, Lao PDR, Liberia, Mali, Mozambique, Nicaragua, Rwanda, Tajikistan, Uganda and Vietnam.*

[3] *Ibid., p.35.*

[4] *IMF, Statement by an IMF Mission on Afghanistan, Press Release No. 13/36, February 4, 2013 available at http://www.imf.org/external/np/sec/pr/2013/pr1336.htm accessed on 23/09/2013.*

[5] *IMF, Program Note: Islamic Republic of Afghanistan, 30 September 2013 available at http://www.imf.org/external/np/country/notes/afghanistan.htm accessed on 09/11/2013.*

[6] *US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, p.2.*

Table 1: Afghanistan's performance relative to the strong performers cluster

Variable/indicator	Afghanistan trend	Trend of strong performers	Comments
Real average per capita GDP growth	Very rapid	Rapid	Growth in Afghanistan has been faster than in virtually all comparators; needs to maintain robust growth even if at somewhat lower rates
Average per capita GDP level	Rising sharply	Rising	Avoiding recession and continuing growth, especially employment growth, will be key
Inflation (GDP deflator)	Very low	Not so low	Needs to maintain good performance in controlling inflation during difficult transition
Structure of the economy	Rapid change	Rapid change	Afghan structural change appears to a considerable extent aid driven; needs new growth drivers
Government consumption	Flat	Flat	Government consumption for Afghanistan substantially higher due to external budget

Source: The World Bank, Afghanistan in Transition: Looking Beyond 2014, Volume 2: Main Report, May 2012. Table 1.1, p.5.

Table 2: Sector shares in GDP, percent

Sector	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
Agriculture	38.5	36.8	28.5	30.2	27.2	27.3	22.4	27.0	23.3
Mining	0.1	0.1	0.2	0.3	0.3	0.5	0.5	0.4	0.6
Mnfg.	18.7	18.1	18.8	17.4	17.1	15.6	15.4	13.5	13.0
Construction	4.8	6.0	9.4	11.2	13.8	13.2	14.0	12.5	12.4
Other industry	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Services	37.8	38.8	43.1	40.9	41.6	43.4	47.6	46.5	50.7

Source: IMF and CSO, and World Bank staff calculations cited in The World Bank (2012), p.24. Note: Excluding opium production. Opium's contribution to GDP is believed to be one-third (including distribution).



Table 3: Economic profile of Afghanistan

Annual indicators	2008	2009	2010	2011
GDP at market prices (Af bn)	711.7	784.2	984.8	1,102.4
GDP (US$ bn)	14.2	15.6	21.2	23.6
Real GDP growth (%)	3.6	21.0	8.4	7.0
Consumer price inflation (average; %)	30.6	-8.3	0.9	10.2
Population (m)	27.0	27.7	28.4	29.1
Fiscal balance of Central Government (% of GDP)	-4.1	-1.6	0.9	-0.6
Exports of goods fob (US$ m)	2,465.0	2,517.0	2,836.0	2,908.0
Imports of goods fob (US$ m)	-8,945.0	-8,872.0	-9,139.0	-9,174.0
Current account balance (US$ m)	92.0	-347.0	267.0	18.0
External debt outstanding (US$ m)	2,069	1,150	1,303	1,242
Foreign Direct Investment inflows (US$ m)	94	76	211	83
Foreign exchange reserves excluding gold (US$ m)	2,430.8	3,501.4	4,174.4	5,268.3
Exchange rate (average) Af:US$	50.25	50.33	46.45	46.75

Source: (i) Economist Intelligence Unit, Country Report: Afghanistan, September 24, 2013, United Kingdom; (ii) Asian Development Bank, Asian Development Outlook 2013, Asian Development Bank, Philippines; (iii) UNCTAD, World Investment Report 2013, New York and Geneva. Notes: 'bn' stands for billion; 'm' stands for million; 'Af' is the sign of the domestic currency of Afghanistan.

Table 4: Donor assistance (US$ million)

Donor assistance	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11
Civilian aid	2,416	1,350	2,188	2,675	3,942	5,262
Security-related aid	988	1,905	7,028	2,750	5,470	8,594
On-budget support	720	717	1,069	1,024	1,275	1,886
Total	4,124	3,972	10,284	6,449	10,686	15,742
Percentage of GDP	66	56	118	61	86	98

Source: World Bank staff calculations. Available in The World Bank, Afghanistan in Transition: Looking Beyond 2014, Volume 2: Main Report, May 2012. p.28.

Note: The figures have been compiled from the actual disbursements reported by the largest donors. Data has been cross-tabulated with various sources. Civilian aid includes expenditure of the U.S.-financed Commanders Emergency Response Program.

Table 5: Components of Gross Domestic Product, 2011/12

Components	% of total
Private consumption	70.8
Government consumption	12.6
Fixed investment	13.0
Export of goods and services	6.9
Import of goods and services	28.5

Source: World Bank staff calculations. Available in The World Bank, Afghanistan in Transition: Looking Beyond 2014, Volume 2: Main Report, May 2012. p.28.

Table 6: Export, Import and FDI

Export	
Principal exports	Opium, fruits and nuts, medicinal plants, hand woven carpets, wool, cotton, hides and pelts, precious and semi-precious gems
Major destination of exports	Pakistan, India, Tajikistan, USA
Import	
Principal imports	Machinery and other capital equipment, food, textiles, metals, household items, petroleum and petroleum products
Major sources of imports	Pakistan, US, Russia, India, China, Kazakhstan, Germany
Foreign Direct Investment (FDI)	
Major sectors receiving FDI	Construction and construction materials production, transport and storage, mining and quarrying
Major investing countries in Afghanistan	South Africa, Turkey, United Arab Emirates, Canada, United States, Pakistan, Iran, England, China, Netherlands, India

Source: (i) Economist Intelligence Unit, Country Report: Afghanistan, September 24, 2013, United Kingdom; (ii) Central Intelligence Agency, The World Fact Book, http://www.cia.gov/library/publications/the-world-factbook/geos/af.html accessed on 23/09/2013; (iii) Why Invest in Afghanistan, http://www.dsafghan.in/pdf/why-invest-in-afghanistan.pdf accessed on 4/11/2013; (iv) Afghanistan Investment Support Agency.

Table 7: Major agricultural and industrial products

Agriculture and allied sector	Opium, wheat, fruits, nuts, wool, mutton, sheepskins and lambskins
Industry	Small-scale production of bricks, textiles, soap, furniture, shoes, fertilizer, apparel, food-products, non-alcoholic beverages, mineral water, cement, hand-woven carpets, natural gas, coal, copper

Source: Central Intelligence Agency, The World Fact Book, http://www.cia.gov/library/publications/the-world-factbook/geos/af.html accessed on 23/09/2013.

Table 8: Labour force, unemployment and

Labour force	**15 million (2004 estimate)**
Unemployment rate	35 percent (2008 estimate)
Population below poverty line	36 percent (Financial Year 2008/09

Source: Central Intelligence Agency, The World Fact Book, http://www.cia.gov/library/publications/the-world-factbook/geos/af.html accessed on 23/09/2013.



During the last decade, services sector has been a strong growth driver with significant boost coming from communications with an annual average of 66 percent followed by financial and business services (annual average 26 percent), Government services (20 percent) and transport (14 percent). Construction growth was strong generating demand for construction materials; mining contributes insignificantly[7] though believed to be a potential growth driver in the medium term.

Thus the main growth drivers are communications and transport, construction, and government services[8].

Table 9: Distribution of the employed population by economic sector, 2007/08 (per cent)

Sectors	National	Rural	Urban
Agriculture	59	67	9
Manufacturing	5	4	8
Transport and communication	3	2	4
Construction, mining and quarrying	8	8	18
Trade	11	8	18
Education	2	2	7
Public administration	4	2	14
Other services	9	7	18

Source: ICON Institute 2009 cited in The World Bank (2012), p.39.

[7] Mining contributed less than 0.5 percent of GDP in the 2000s. The World Bank (2012), p. 26.

[8] The World Bank (2012), p. 25.



Chapter 2

The policy environment for promoting investment

2 The policy environment for promoting investment



The Afghanistan National Development Strategy (ANDS) of the Islamic Republic of Afghanistan laid strong emphasis on private sector development as a cornerstone of growth and poverty reduction in Afghanistan[9]. The principles of free market have been incorporated in Article 10 of chapter 1 of Afghanistan's new constitution, which states that "The State encourages and protects private capital investments and enterprises based on the market economy and guarantees their protection in accordance with the provisions of law"[10].

Afghanistan Investment Support Agency (AISA) has come out with a detailed account of the enabling policy environment and identified sectors of opportunities for investment in Afghanistan[11].

The Law on private investment (2005) in Afghanistan does not discriminate between domestic and foreign investment. Foreign ownership to the extent of 100 percent is allowed in most of the economic sectors with full repatriation of profit. There is no restriction on capital flows and currency conversion. Afghanistan Investment Support Agency (AISA) acts as one-stop shop for investors and business license is issued within 2 to 3 days at AISA. Companies are not required to deposit any amount in a bank to start a business[12]. According to the World Bank's Doing Business 2013 report, globally, Afghanistan stands 28 in the ranking of 185 economies on the ease of starting a business (Figure 1). However, it should be noted that according to the World Bank's 2013 Doing Business Index, Afghanistan ranks 168 out of 185 economies in the ease of doing business[13].

Corporate income tax rate of 20 percent is low by regional standard and personal income tax ranges between 0-20 percent[14].

---

[9] Islamic Republic of Afghanistan, AFGHANISTAN: National Development Strategy (2008-13), 2008.

[10] http://arabic.cnn.com/afghanistan/ConstitutionAfghanistan.pdf accessed on 4/11/2013.

[11] Available in http://www.aisa.org.af/home_sectors.php accessed on 5/11/2013 and Why Invest in Afghanistan, http://www.dsafghan.in/pdf/why-invest-in-afghanistan.pdf accessed on 4/11/2013.

[12] This information is sourced from Why Invest in Afghanistan, http://www.dsafghan.in/pdf/why-invest-in-afghanistan.pdf accessed on 4/11/2013. According to the Doing Business 2013 Report starting a business in Afghanistan requires 4 procedures, takes 7 days, costs 22.5 percent of income per capita and requires paid-in minimum capital of 0.0 percent of income per capita. See The World Bank and the IFC, Doing Business 2013, http://www.doingbusiness.org accessed on 4/11/2013.

[13] US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, p.3.

[14] Ibid., p.11.

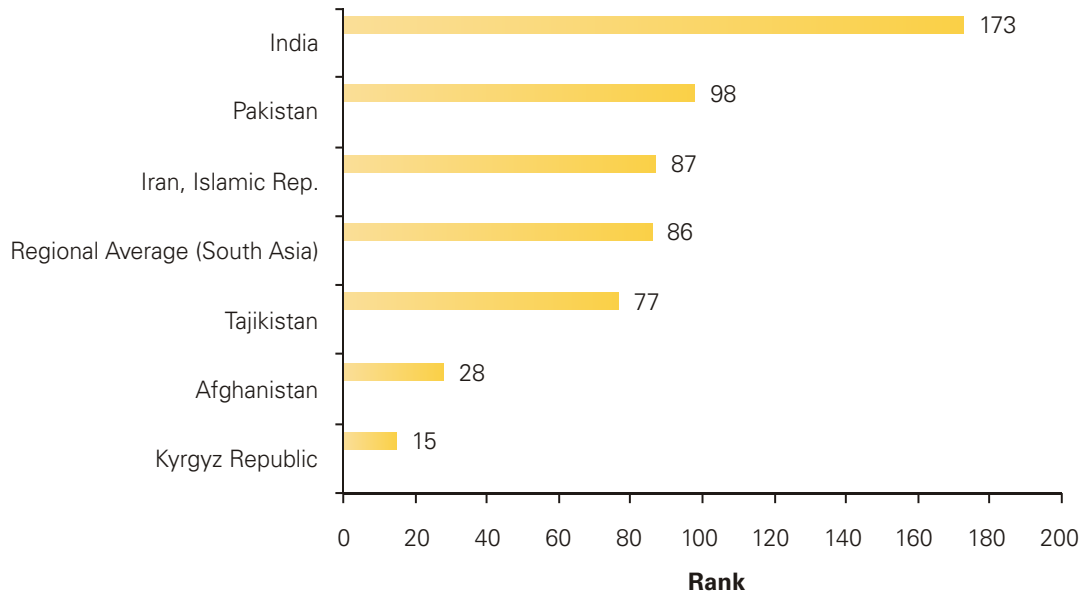


The number of commercial banks including public and private banks and branches of foreign banks reached 17 in 2012. Total assets of the banking sector increased from less than US$300 million in 2004 to more than US$4 billion in December 2011. Prime lending rate in Afghanistan at 15 percent is comparable to the neighbouring countries.

The share of private investment rose from 1.3 percent of GDP in 2003 to 8.6 percent in 2011[15]. Foreign Direct Investment accounted for about a third of the private investment. Construction has been the highest receiver of private investment (38.1 percent) followed by services. Industry received almost a quarter of total private investment. Agriculture had the least share.

The tax code was restructured and clarified in 2005 and the Income Tax Law was passed in 2009. Customs tariffs have been rationalized[16].

Figure 1: How Afghanistan and comparator economies rank on the ease of starting a business



Source: The World Bank and IFC, Doing Business 2013, http://www.doingbusiness.org

The Mineral Law (2005) and the Hydrocarbon Law (2006) were the major initial steps towards creation of a regulatory framework for the development of these sectors and creating an enabling environment for attracting and retaining private

[15] Total investment (public plus private) was 22.6 percent of GDP in 2011.

[16] US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, p.3.



sector investment[17]. Aided by the World Bank and the United Kingdom's DFID Afghanistan is making effort to achieve compliant status in the Extractive Industries Transparency Initiative (EITI) by October 10, 2014. Achieving compliance will send a positive signal to potential mining investors. Reportedly, the Ministry of Mines and Petroleum plans to release several mineral tenders following the passage of an investor friendly Mineral Law[18]. A Telecommunication Law (2011) has replaced the previous law and an Information Communication Technology Law seeking to lay the groundwork for a new industry in electronic commerce and cyber security is under revision with the Ministry of Communication and Information Technology[19].

Afghanistan is a member of a number of regional cooperation agreements, namely, SAARC, ECO, CAREC, APTTA and SAFTA. Under SAFTA, Afghanistan enjoys duty-free access to India and 5 percent to Pakistan on non-sensitive goods. Duty free and quota free access is also available to Afghan products under an LDC Market Access Initiative with Canada and a Generalized Preferences Treatment Agreement with Japan. "Everything But Arms" agreement (EBA) with the European Union grants duty free access to Afghan products. As a Least Developed Country, Afghanistan is eligible for duty free access to the U.S. markets for about 5,700 products under the Generalized System of Preference (GSP)[20].

Afghanistan has also signed bilateral Trade and Economic Cooperation Agreement with Russia and Turkey, a Bilateral Reciprocal Promotion and Protection of Investments Agreements with Turkey, a Bilateral Preferential Trade Agreement with India, a Bilateral Investment Treaty with Germany, a bilateral Investment Incentive Agreement with the United States and a Trade and Investment Framework Agreement with the U.S.A[21].

Afghanistan had applied for accession to the WTO and is taking steps to accelerate the process of accession with the goal of becoming a member by 2014. The Government of Afghanistan is working to bring legislation on patents, trademarks and copyrights in compliance with the WTO standards[22]. In line with the Istanbul and Almaty Programmes of Action for the Least Developed Countries and the Land Locked Least Developed Countries, the South and South-West Asia office of the UNESCAP, in collaboration with the International Trade Center, Geneva has launched

[17] Why Invest in Afghanistan, http://www.dsafghan.in/pdf/why-invest-in-afghanistan.pdf accessed on 4/11/2013.

[18] US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, p.5.

[19] Ibid., p.37.

[20] Ibid., pp.32-33.

[21] Ibid., p.32-33.

[22] Ibid., p.40.



a series of capacity building programmes for the Government and private sector officials of Afghanistan to support Afghanistan's accession to WTO. Three such capacity building programmes have already been held in 2012 and 2013. Besides providing a general overview of costs and the benefits associated with the WTO membership, the capacity building workshops covered a diverse set of negotiation topics and subjects related to accession process. The programme was also designed to continue the constructive policy dialogue between public and private Afghan officials to address knowledge gaps in the WTO negotiation process in select priority areas.

In July 2013 the Government of Afghanistan announced the Investment Incentive Policy focused on development of industry, construction, export promotion, agriculture and mining. The policy also aimed at strengthening confidence among the investors including the foreign investors and to reassure continued support of the Government to promote business to create sustainable employment even beyond 2014. The policy, subject to certain terms and conditions, liberalized allocation and renting of government land, granted tax holidays and exemption, subsidized power tariff, provided for concessional loan (in agriculture) and exempted small and medium mines from bidding[23].

Afghanistan is a member of the World Bank's Multilateral Investment Guarantee Agency (MIGA). The Overseas Private Investment Corporation (OPIC), a U.S. Government's development financial institution supports U.S. companies in Afghanistan by offering finance, political risk insurance and private-equity investment[24].

[23] Afghan Cabinet Approves the Investment Incentive Policy, http://www.acci.org.af/component/content/article/38-news/406-afghan-cabinet-approv... Accessed on 23/09/2013.

[24] US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, p.46.



Chapter 3

Sector opportunities

3 Sector opportunities



Situated strategically at the heart of Asia, Afghanistan is a land bridge connecting South Asia with Central Asia, Eurasia and the Middle East. Afghanistan is also a key transit route for oil and gas of Central Asia to reach the major sea ports and markets of South Asia and overseas[25].

Afghan diaspora worldwide are taking interests in investing from their home-base abroad. Apart from investing they also provide links with the overseas market[26].

Major sector of opportunities for investment include

Mineral resources

Afghanistan has rich deposits of copper, gold and iron, salt, industrial minerals (which could be used in the glass, ceramic, chemical and fertilizer industries), non-precious mineral such as lead and cement grade limestone, construction materials, dimensional stones and gemstones, coal and hydrocarbon (mostly natural gas).Known precious and semi-precious stones include emerald, jade, amethyst, alabaster, beryl, lapis lazuli[27], ruby, quartz, and sapphire. It is stated that more than 1400 mineral deposits have been identified so far. Most of these deposits have remained untapped. Over and above, there seems to be a vast area where the potential is not known and could be explored.

It is also claimed that Afghanistan's iron and copper deposits are of world-class quality[28]. Large investments are being made in copper deposits in Aynak (near Kabul) and iron deposits in Hajigak (Bamyan province).There are limited activities in the mining sector in small coal operations, limestone, construction materials, gemstones and dimensional stones[29].

---

[25] Why Invest in Afghanistan, http://www.dsafghan.in/pdf/why-invest-in-afghanistan.pdf accessed on 4/11/2013.

[26] MIGA, Investment Horizons: Afghanistan – A Study on Foreign Direct Investment Costs and Conditions in Four Industries, World Bank, Washington, DC, 2005, p.34.

[27] It is reported that the famous blue lapis lazuli mines date back to 5000 B.C. See Why Invest in Afghanistan, http://www.dsafghan.in/pdf/why-invest-in-afghanistan.pdf accessed on 4/11/2013.

[28] Ibid,.

[29] The World Bank (2012), p. 26.



Afghan marble is stated to be of good quality and in high demand and it is reported that there is a huge demand for Afghan marble in the gulf. The industry needs investment in equipment and expertise.

The development and exploitation of copper reserves including in copper smelting facilities offer another potential area of investment. There is a growing demand for copper in the region including in the large markets of China and India. Afghanistan has sizeable copper reserves in Kabul and Loghar provinces. The three major reserves identified are in Jawkhar, Darband and Aynak. Around 300 more deposits are known[30].

Major iron deposits in Afghanistan are located primarily between Herat and the Panjsher valley. Hajigak in Bamyan province is known to be the largest reserves in the Middle East. There are also deposits in Badakhshan and Baghlan provinces. There has not been any review of iron ore deposits for over thirty years; further exploration and assessment is called for.

Afghanistan's gold deposits are located in the northern provinces of Ghazni, Badakshan and Takhar and are utilized by artisanal miners. The best known sources are Zarkashan and Samty with an estimated supply of 20 to 25 tons. There is a significant investment potential in gold exploration activity.

Development of mining sector is essential for the 'reconstruction and rehabilitation' of Afghanistan. Mineral based construction materials like paving stones, cement and cement blocks, bricks, gravel, steel, sand glass and tiles are in local demand. Cement is now being imported from Pakistan and Iran and can be domestically manufactured in Afghanistan to replace import. Local manufacture, if produced in international quality, has the competitive advantage over import since import has other associated costs, which domestic manufacturers will not have to incur.

Afghanistan's unmet demand for energy translates into a big potential for investing in the country's coal reserves.

Today, mining resources are mostly occupied by the failed State Owned Enterprises (SOEs). Others are subject to small scale and mostly illegal operations. The opportunities in this sector are still governed by the system of government tendering though AISA offers guidance to interested investors in the bidding process and introduces potential investors to the relevant ministries. AISA has observed that "experience in other countries shows that private operators are, for the most part, more effective in the exploitation of natural resources and mining"[31].

[30] Why Invest in Afghanistan, http://www.dsafghan.in/pdf/why-invest-in-afghanistan.pdf accessed on 4/11/2013.

[31] AISA, http://www.aisa.org.af/home_sectors.php accessed on 5/11/2013.



However, the legal and regulatory regime needs to be fully developed to complete the privatization process. Some of the mineral rich areas of Afghanistan along the border of Pakistan is reportedly not fully in control of the Government and are vulnerable to attacks by anti-State actors. There is also shortage of skilled mining labour, which adds to the start-up costs[32].

To sum up, according to the AISA the following criteria are of particular importance to the investors in the mining sector[33]:

- Mining legislation, which includes clarity of ownership and terms of operations
- Clear criteria for granting private mining rights and title
- Competitive and transparent taxation system that adheres to international standards and best practices
- Security and political stability
- Mining potential and geological research and information

The challenges that should be addressed are:

- Transition to a market economy: this can unburden the Government from control over natural resources, subsidies to inefficient production in the SOEs and help to modernize the sector in the hands of the private investors
- Security: Many mines are located in areas where the Government control is ineffective
- Lack of infrastructure (power, water and transport): poor rural roads increase the shipment costs
- Obsolete mining practices: mining methods and practices are reportedly obsolete and date back to the 1980s and before
- Lack of investment in modern machinery: Replacement of outmoded machinery will increase start-up costs for investors; up-to-date quarrying and processing technologies/facilities are important and crucial
- Unexploded ordinance: Afghanistan is one of the most heavily mined countries in the world; security and precautions are most essential for exploration activities
- Shortage of skilled workforce: Due to the shortage of locally available skilled workers skilled manpower from overseas (engineers, managers and machinists) will have to be arranged and this will increase the star-up costs

[32] MIGA (2005), p.13.

[33] AISA, Market Prospects: A country abundantly rich in natural resources, available at http://www.aisa.org.af/brochures/Mining1.pdf accessed on 11/11/2013, p.3.



- Landlocked location: Landlocked status increases the costs of transport
- Research and Technology: Geological clarity is essential for directing investment
- Legal and regulatory framework: Implementation of the new Minerals and Hydrocarbon Law will be demanding on the capacity of the Government
- Access to Credit: Mining being capital intensive and high risk activity, access to institutional credit is essential for the growth of investment in this sector[34].

It is reported that the "Government of Afghanistan has identified key state-owned enterprises for privatization and financial institutions are building capacity and working alongside investors to provide reliable credit facilities. Security and de-mining is gradually improving"[35].

Agriculture, agro-business and food-processing

Afghanistan is known for the cultivation of high-end horticultural crops such as raisins, pomegranates, pistachios and almonds. Dried fruits and nuts from Afghanistan have traditionally established brand value in certain export markets. New companies can potentially take advantage of this traditional reputation and export such products. With some marketing effort the reputation for traditional fruit products could be extended to a wider variety of other processed food and beverages in large neighbouring markets of China, India, Iran and Pakistan. Afghanistan is naturally well endowed with appropriate climate and surface water to cultivate a large variety of fruits and vegetables, which can be dried, canned or processed. Reportedly, Afghanistan has about a million farms and 2,000 wholesalers in horticultural products. There is scope for investment in intensive commercial farming in horticulture crops. Besides, agricultural packaging provides another opportunity for investment. The current packaging is outdated and leads to significant waste of post-harvest agricultural products. Development of packaging industry for horticultural products is critical if Afghanistan has to develop export business in horticultural items.

---

[34] Ibid., p. 16.

[35] Ibid., p.16. Restructuring is also taking place in power sector. It is reported that the Government of Afghanistan, with the financial support from the World Bank is working on the restructuring of the state owned power enterprise "DABM", which owns and operates all existing power plants, distribution systems and transmission lines in Afghanistan. Similarly, the Government's effort to establish bilateral cooperation agreements for power trade with the neighbouring Central Asian countries has been supported with the assistance from the USAID. The USAID has also assisted the Government's effort to revitalize the North-East and South-West Transmission Systems through power utility companies. See Ibid., pp. 8-9.



Food processing provides another opportunity for investment. Afghanistan imports fruit juice in large quantity; the market size is big and growing and there is scope for investment in import substitution. In the vegetable oil industry the demand was once largely met through import. Several vegetable oil processors have come up in the domestic market. There are investment opportunities in processed fruits and vegetables, snack foods, packaged biscuits, fruits concentrates, pickles and fresh fruit jams. Investment in food-processing industry will generate demand for downstream industry in packaging, bottling, machinery for agriculture, agro-processing and food processing and chemicals.

It is important to tackle the transport and logistics challenges in order to develop this sector. Improved road conditions, seamless movement inside the country and along the transit routes, cold chain, refrigerated shipment, efficient border custom handling are important factors in promoting business in food processing. Establishing standards and inspections and improving sanitary environment for quality assurance are critical for business to succeed in this sector. Setting up of testing laboratories with facilities of internationally recognizable certificates of inspection will be a useful step. Availability of uninterrupted quality power (electricity) supply, storage facilities in controlled conditions and investment in the modern machinery and equipment replacing the old and obsolete ones are important prerequisites to promote investment in this sector. Many of the existing companies in Afghanistan in this sector, especially in the dried fruit industry are small and medium enterprises. Facilities for long term finance for the SMEs need to be developed[36].

Carpets

Carpet industry of Afghanistan enjoys traditional reputation as a handicraft and has a brand image, which offers the item "a good basis for improved marketing". A point of strength of this sector is availability of sufficient skilled manpower. Non-perishability of this product confers transport and storage advantages. However, companies have reported difficulties of availability of land for warehouses and other operational facilities. Non-availability of domestic sources of raw materials (wools, dyes and other inputs) primarily due to devastation of local sources makes the industry depend on import through Pakistan. Apart from adding to transport and customs costs, quality of imported raw materials is also sometimes not reliable. Many carpet traders, who primarily export this product, have reported high transport costs since it is not viable to ship large volumes of such heavy items by

[36] MIGA (2005), p.12.



air. Furthermore, shipping through Pakistan and Iran, reportedly adds costs and time.

It is stated that carpets from Afghanistan are shipped to Pakistan in semi-finished form for final finishing. Afghanistan's domestic finishing facilities are either destroyed or obsolete. This arrangement adds to the costs and could potentially infringe intellectual property. Finishing facility has reportedly come up in Mazar-e-Sharif[37] but there is still sizeable opportunity for investing in domestic finishing business.

Construction materials

Construction has so far been an important growth driver in Afghanistan and will continue to remain a major activity in times to come. Overseas contractors and imported machinery and materials are predominant in this sector and local contractors are shaping up gradually to takeover such projects. Concomitant with this development there is enormous opportunity for local sourcing of construction materials if investment is made into this sector. While domestic demand for construction materials will be robust, good quality construction materials, if produced locally, will also find their ways into export market.

Telecommunication and IT enabled value added services

Communication has been a significant growth driver in Afghanistan in the last decade. While telecommunication has expanded and there is still scope for further expansion of mobile telephony, a virgin area of investment remains in the field of Information Technology enabled value-added services like data processing and data transfer; process control; business processing operation and call centers.

Transport and logistics

Development of transport and logistics is vital for performance of other sectors in the economy. Afghanistan is strategically located as a potential transit hub connecting South Asia with Central Asia, Eurasia and the Middle East and provides the landlocked energy basin of Central Asia key transit route to the sea ports and the potentially large markets of India, China and other overseas destinations. Afghanistan is poised well to provide transit services at a price. Thus transport and logistics in Afghanistan are critically important from a regional perspective apart from their values as domestic utilities. The sector is open for investment and is a

[37] MIGA (2005), 2005, p.13.



growing market. The start-up costs are modest and overhead is low. Even a small operator can generate a large turnover. Demand for transport and logistics is high in Afghanistan and will continue to increase. The commercial transport is a high growth sector and far outpaces transport of donor materials. The need for transport of industrial and consumer goods will increase with the improvement of the economy. An important source of demand for logistics arises from the need for cold chains if agribusiness, agro-processing and food-processing have to be developed as a priority sector for investment. The country is deficient in cold-infrastructure at present.

However, improvement of road condition is critical for this sector to develop. It is stated that significant portions of the major highways and transit route needs repair and upgrading. Companies have expressed concerns regarding indefinite closure of important highways for security reasons without prior notice; this need to be avoided. Being landlocked, transport costs tend to be high and seamless access to sea ports of the neighbouring countries is important for this sector to comply with delivery commitments. This will require strengthening regional cooperation to facilitate trade and transit. Despite some progress achieved in the automation of customs processes full integration is yet to be achieved. It has been reported by companies that there are unofficial custom points and multiple custom checks. Authority of the central government is limited in certain regions and local warlords impose arbitrary taxes and custom charges on overland transport. Improvement of reliable electric supply is needed for sophisticated logistic services to operate; companies mostly depend on their own power backups[38].

Low-end (labour-intensive) manufacturing

Promoting low-end (labour-intensive) manufacturing for employment generation is a priority for the Afghan Government to attract investment. AISA is projecting Afghanistan as a potential hub of outsourcing in global system of production and a low-cost destination for FDI in low-end labour intensive manufacturing and manufacture of parts and components. Considering that Afghanistan is importing a whole range of items to cater to domestic demand, a select list of low-end manufacturing industries has been chosen from the list of imported items by the AISA to showcase as potential areas of investment. The list of such industries has been posted on the AISA web site[39]. The list includes tools and tool tips, toilet paper, matches, plastic wares, bicycles, plastic carpets, blankets, yarns (flax, silk

[38] MIGA (2005), p.10.

[39] http://www.aisa.org.af/home_sectors.php accessed on 5/11/2013.



wool, polyester, fiber, cotton), footwear(leather and plastic), clothing, tires and tubes, plastic wires, soaps and washing powders.

Cross Sectoral Challenges and Prospects

Several cross-sectoral challenges need to be addressed on priority in order to improve investment climate in Afghanistan.

Legal and regulatory framework

The work of establishing legal and regulatory framework to support a free market economy needs to be completed by bringing weak, poorly regulated and unregulated commercial activities within the framework. The judiciary has limited capacity and needs to be strengthened for effective enforcement of rules and regulations. Dispute resolution mechanism is not smooth and corruption creates serious challenge[40]. The Arbitration and Mediation Law (2007) established the foundation for an alternative dispute settlement mechanism. Afghanistan is a party to the Convention on the Settlement of Investment Disputes between States and Nationals of Other States and the New York Convention of 1958 on the Recognition and Enforcement of Foreign Arbitral Awards. Dispute resolution is also allowed in Afghanistan under the United Nations Commission on International Trade Law (UNCITRAL) rules, or any other mechanism that has been specified under contract by the investors. For Afghan business, commercial arbitration or mediation service is also provided by the Afghanistan Chamber of Commerce and Industries[41].

Box 1: Sectors/Projects of Private sector investment opportunity

Energy

1. Turkmenistan, Afghanistan, Pakistan, and India Natural Gas Pipeline – TAPI
2. Sheberghan Natural Gas Project
3. Compressed Natural Gas (CNG) for Automobiles and Generators
4. Afghan-Tajik Basin Tender
5. Central Asia-South Asia Regional Energy Market Project – CASA – 1000
6. Kokcha Hydropower Plant Irrigation Project

[40] US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, p.4.

[41] Ibid., p.37.

Minerals

7. Syadara Iron Ore Deposit
8. Cement Plant Opportunity

Transport

9. Afghan Rail System
10. East-West Road Corridor and upgrade Kabul-Jalalabad-Peshawar Highway to a Four-Lane Expressway
11. Rehabilitation of the Salang Tunnel and Construction of By-Pass Road

Agriculture

12. Fruit Juice and Concentrate Production
13. Saffron Processing and Marketing
14. Farm Machinery Manufacturing
15. Dairy Component Economic Development Package
16. Fresh Fruit Processing – Eastern region
17. Poultry development

Small and medium-Sized Industries

18. Moving Up the Value Chain in Carpets
19. Processing Cashmere
20. Processing and Exporting Marble
21. Production of Rolled Steel Products

ICT, Finance, Health Services, and Construction

22. Digital Broadcasting Nationwide Distribution Network (Broadnet)
23. Financial Services
24. Public-Private Partnerships for Regional Hospitals
25. Kabul New City

Source: Islamic Republic of Afghanistan, Ministries of Commerce and Industries, Investment Opportunities in Afghanistan, 28 June 2012



Anti-corruption laws exist in Afghanistan but implementation has been poor. In Afghanistan bribing can be charged as a criminal act.

Afghanistan acceded to the United Nations Convention against Corruption (UNCAC). High Office of Oversight for the Implementation of Anti-Corruption Strategy (HOO) has been created by the President to coordinate anti-corruption measures for the Government without any jurisdiction over fines and penalties and remained largely ineffective[42].

Pursuant to the commitments made by the Government at the London and Kabul conference in 2010, an Independent Joint Anti-Corruption Monitoring and Evaluation Committee (MEC) had been set up by the Government of Islamic Republic of Afghanistan and the international community to study areas of corruption and recommend measures for improvement. The MEC made an in-depth enquiry into the crisis of Kabul Bank and recommended a set of measures for improvement of governance in the financial sector. Similar investigations by the MEC in other sectors could be of help.

Reforms in customs and transport facilitation

Reforms in customs administration need to be strengthened in order to bring about transparency, consistency and improved coordination between the central and the provincial governments. The Single Administrative Document (SAD) for customs was initially introduced in December 2003 in five key provinces and is now implemented nation-wide. At several border crossings, facilities have been upgraded and plans for improvements of several others are underway. Border crossing facilities upgraded in recent years include Torkham Gate in the east, ShirKan Bandar and Hairatan in the north, and Islam Qalah in the west. Large scale reforms are underway to simplify exemption processing and establish standardized fees and streamlined procedures for import and export. The Automated System of Customs Data (ASYCUDA) has been implemented in six locations and is being extended to other locations[43].

In this context, adoption of UNESCAP tools for transport facilitation measures could be potentially beneficial for Afghanistan. One of these is a conceptual model of integrated controls at border crossing. This can be used "as an approach for technical design of information management and workflows at border crossings"[44].

---

[42] Ibid., p.42.

[43] Ibid., p.31.

[44] See UNESCAP, Model on integrated controls at border crossings, Bangkok, 2012, available at http://www.unescap.org/ttdw/Publications/TFS_pubs/MICBC- full text.pdf accessed on 12/11/2013.



For efficient cross border transport the UNESCAP had released a study that analyzed the solutions available for efficient cross-border transport in terms of improving operations, lowering operating costs and reducing the time spent at the border. Based on this analysis, the study offered suggestions to the private businesses and made recommendations to the public sector on how private business arrangements could be supported. The study provides models for efficient border crossing to develop trade and transport by reducing non-physical barriers. Adoption of this model does not entail replacement of international facilitation agreements[45].

Establishing Standards

The Afghan National Standards Authority (ANSA) was established in 2005. The development of a national standards regime is in process. Technical regulation on construction materials has been approved by the Council of Ministers in February 2013 and the technical regulation on food stuff is under review. Along with the development of essential national standards, the ANSA also seeks to enhance technical infrastructure for testing[46].

Tax regime

It has been observed that tax regime is cumbersome and tax compliance is low. Large formal companies complain that the more responsible and visible companies share disproportionate corporate burden of taxes.

Transport infrastructure

Developing quality transport infrastructure is critical. Afghanistan's road network is of poor quality and needs upgrading. Currently, shipping of goods through Iran and Pakistan adds another layer to the costs and delays in export-import. Arbitrary road closing creates another problem; highways are frequently closed for security reasons and remain closed for as long as several days. Apart from increasing transportation costs, this creates planning and timely deliveries difficult. Most trucks used in Afghanistan were imported often in poor conditions, maintenance is poor and spare parts are difficult to find and expensive. The trucks often breakdown en route and this causes delay and increase in transportation costs. The goods coming into Afghanistan would need to be offloaded from the trucks or containers at the Afghanistan border and reloaded onto Afghan trucks to be sent to the border

[45] UNESCAP, Efficient cross-border transport models, Bangkok, 2012, available at http://www.unescap.org/ttdw/Publications/TFS_pubs/ECBTM - fulltext.pdf accessed on 12/11/2013.

[46] US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, pp. 31-32.

to pick up goods. Unloading and reloading at the borders lead to extra costs to the importers for offloading and reloading operations and sending another truck to the border for reloading , delay in the process and damages[47].

Poor overland connectivity

Poor connectivity, both within the country and with the neighbouring countries is a serious bottleneck for Afghanistan to develop business and to harness the country's strategic location at the heart of Asia to act as a hub of business and commerce in the larger regional context. Afghanistan's landlocked status reinforces the criticality of this impediment.

Box 2: Poor overland connectivity

"Land transport in Afghanistan is hampered by difficult terrain and poor road conditions, although the government is making headway in improving them. The "Main Road" in the southern half of Afghanistan and the "Ring Road" in the northern half form the major network of highways through Afghanistan. Repairs are currently underway in several portions and the Main Road is in better condition than that Ring Road. Of all overland transportation, 60 percent is to or from Pakistan, yet the major road between the two countries (Kabul-Jalalabad-Torkham) is in poor condition. An additional 30 percent of land transportation comes through the Iranian border and a combined 10 percent through Afghanistan's border with the Central Asian Republic to the north.

As Afghanistan is landlocked, it depends on the Pakistani seaports of Karachi and Gwadar and the Iranian ports of Bandar-e Abbas and Chahbahar for its sea transportation. .." A lot depends on the transit agreements with Iran and Pakistan.

"There is no network of railroads currently operating throughout Afghanistan, however a system of railroads begin 10km to the south of the border with Uzbekistan in Hayratan and 10km south of the border with Turkmenistan in Turghondi for transit of goods to and from those two countries by rail."

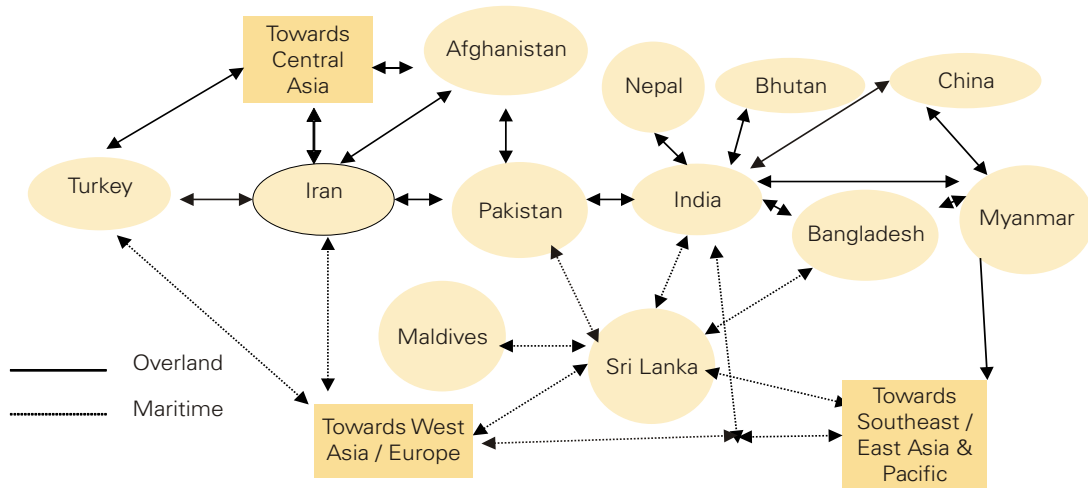
Source: MIGA (2005), p.29.

[47] MIGA (2005), p.31.

Seamless overland cargo movement in the region is also restricted by the Afghanistan's ability to send export consignment to India using land route through Pakistan whereas the import from India into Afghanistan is not allowed via Pakistan's land-route. Seamless cargo movement through least cost transit route potentially facilitates emergence of efficient cross-border production network, which Afghanistan is not able to take advantage of.

The UNESCAP has proposed an East-West Road Corridor connecting Turkey-Iran (Islamic Republic of)-Pakistan-India-Bangladesh-Myanmar (TIPI-BM) road corridor: Asia's new Southern Silk Route where Afghanistan can be a potential hub (Figure 2)[48]. Afghanistan can be a part of this corridor by connecting Kabul to Wagah and Attari through Torkham.

Figure 2: TIPI-BM Road Corridor – Potential Transport Hubs in South and South-West Asia



Source: UNESCAP-SSWA (2012), p. 90

The participating member states[49] of the Fifth Regional Economic Cooperation Conference on Afghanistan (RECCA V), held in Dushanbe, Tajikistan in March 2012, strongly committed towards the goal of development through building infrastructure. Several railway and highway projects were prioritized for implementation along with other projects in the area of energy; human resource development, vocational training, labour market facilitation; investment, trade, transit and border management; and fiber optic connectivity[50].

[48] UN-ESCAP South and South-West Asia Office, Regional Cooperation for Inclusive and Sustainable Development, South and South-West Asia Development Report 2012-13. UN Publications and Routledge, New Delhi, pp. 89-91.

[49] Afghanistan, Tajikistan, Pakistan and Iran.

[50] For details see Afghanistan Investment Support Agency, Report on Regional Economic Cooperation Conference (RECCA V) and the sideline Business Forum available at http://www.aisa.org.af/newsarchive/Report-on-AISA-Participation-in-RECA-V.pdf accessed on 11/11/2013.



A SAARC regional transit agreement is in dire need since several countries like Bangladesh, Bhutan, Nepal and Afghanistan would benefit from such arrangements.

Access to land

Property market in Afghanistan is complex and non-transparent. Procedures for leasing or selling vary widely, title disputes are common and recourse to judicial settlement is difficult. Standard and transparent procedures and efficient mechanism for allocation of land to investors are one among the foremost business requirements. In collaboration with the USAID, Afghanistan's land authority (a part of the Ministry of Agriculture, Irrigation and Livestock) is building up an archive of consolidated electronic records and paper documents on land titles. Legislation on mortgage and secured transactions has been signed by the President in 2009[51].

State capacity in public utility services

There is a need for improving the capacity of the State to provide basic public utility services like water supply, electricity, waste collection and waste water services. It is reported that the Government is addressing these requirements. There are investment opportunities in these areas where public-private partnership could be encouraged. Expeditious provisioning of these utilities will catalyze business growth and improve investment climate.

Undeveloped financial market

Financial markets are still undeveloped for supporting business and commerce. Conventional financial services are available from the international banks and the central bank. However, financial products like commercial loans or export finance need to be developed for domestic investors. Credit to private sector has remained within 4 to 12 percent of the GDP since 2008. Banks are highly centralized with 75 percent of total loans made in Kabul. Only 7.3 percent of Afghans currently holding bank deposits. Money service providers (or hawalas) are extensively used to access finance and transfer money. Although investment funds, leasing, micro-financing and SME-financing companies have entered the market, difficulties are being faced in securing repayment. Deficient legal and regulatory infrastructures that fail to protect property rights and development of collaterals also impede growth of formal banking and institutional credit culture. Firms' dependence on the informal

[51] US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, p.40.



credit market, family funds and retained earnings for conducting business limits growth of business potential. It is stated that access to credit is found to be one of the largest obstacles to investment in Afghanistan. The legislation for improving banking sector oversight drafted by the Government is awaiting ratification in Parliament[52]. Afghanistan has a small public debt market that allows participation by the commercial banks, money service providers and foreign exchange dealers[53].

Skills deficit

Afghanistan faces critical shortage of skilled manpower. This stands on the way of availability of local people to work. There are others whose skills are outdated and require reskilling to work with modern machineries. Widespread illiteracy also hinders people's participation in development process creating hurdles on the way to develop. One example is that of the initiative on the part of the Government to launch a system of Licensed Customs Brokers by screening through examination. The attempt was frustrated due to high level of illiteracy in the provinces and could not be enforced. The licenses are issued without taking the examination. Massive effort is called for in expanding education and training throughout the country.

Security issues

Finally, security environment will crucially determine the presence of investors. A lot will depend on the outside perception of security situation in the country.

[52] Ibid., p.41.
[53] Ibid., p.50.
[54] Ibid., p.31.



Chapter 4

Getting started

4 Getting started



AISA website offers step by step guidance on 'Getting Started' for a potential investor[55]. The first step is to undertake initial desktop research on general issues and on specific market segment. The website provides addresses of various internet sites and names of institutions and publications, which could be accessed by potential investors as useful resource. As the second step, the AISA recommends a business trip, which AISA can facilitate. It is stated that strong local knowledge and familiarity with key players in business and government are vital for business development in Afghanistan[56]. Combined with other purposes, business trip should also focus on acquiring as much local knowledge as possible along with developing familiarity and contacts. It is advised by the US Commercial Service that personal relationships are extremely important in Afghanistan for building business. Doing an assessment of the investment opportunities has been suggested in the third step. The AISA will help in making an assessment, which will include in-depth information regarding the priority sectors for investment, carrying out a financial feasibility analysis and advice on land-availability including availability of plots in industrial parks. The AISA will also provide support in the fourth step, for obtaining business license and company registration. However, in certain industries and for carrying out export-import business, licenses have to be obtained from other responsible ministries.

Several market studies are downloadable from the AISA website. The AISA website also provides URL of other useful and relevant sites[57].

Apart from AISA, the Afghan Chamber of Commerce and Industries (ACCI) and its U.S.-based affiliate, the Afghan-American Chamber of Commerce (AACC) and the trade associations like Afghanistan Builders Association (ABA) and those of the other countries like Federation of Indian Chambers of Commerce and Industry, the American Chamber of Commerce in Afghanistan (AmCham Afghanistan) and commercial sections of embassies of different countries are important sources of information and contacts. Most of these agencies are also engaged in business matchmaking activities.

---

[55] See http://www.aisa.org.af/gettingStarted.php accessed on 05/11/2013.

[56] US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, p.5.

[57] US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, frequently referred to in this paper also provides useful information .



Peace Dividend Trust (PDT), a Canadian non-governmental organization (NGO) maintains a business portal that includes details of 6,500 licensed, screened and verified Afghan owned businesses. Apart from business matchmaking activities PDT distributes tenders by e-mail, SMS alerts and official visits, conducts training on procurement processes, provides market information and engage in advocacy in support of Afghan First initiative[58].

The Export Promotion Agency of Afghanistan is engaged in promotion of processing, marketing and distribution of a range of commodities. The thrust area includes agricultural goods (especially dried fruits and nuts), carpets, and mined materials (especially marble and gemstones)[59].

MIGA is working with the AISA and encouraging information in the four key industries, namely Logistics and Transportation, Carpets and Textiles, Food and Beverage Processing and Mining. MIGA also releases studies and brochures on different sectors, investment climate, and potential areas of opportunities including those suitable for entrepreneurs and small companies. MIGA also provides political risk insurance[60].

The Procurement Unit of the Afghanistan government, which is a part of the Afghanistan Reconstruction and Development Services, handles government procurement (also of the municipality of Kabul). Information on project related procurement opportunities with the USAID could be found on the website of Afghanistan Infrastructure and Rehabilitation Program. United Nations Development Business is a useful source of information on procurement by the Multilateral Development Banks and other international donors[61].

---

[58] Afghan First initiative seeks to enhance Afghan participation in work and create employment. See http://sigar.mil/..accessed on 09/11/2013. See US Commercial Service, Doing Business in Afghanistan: 2013 Country Commercial Guide for U.S. Companies, p.14.

[59] United States of America, Department of Commerce, International Trade Administration, Afghanistan: Business opportunities, available at http://trade.gov/afghanistan/tg_aftf_003393.asp accessed on 10/11/2013.

[60] MIGA, Afghanistan Investment Guarantee Facility, available at http://www.miga.org/documents/IGGafghan.pdf accessed on 12/11/2013. Also see, Encouraging FDI in Afghanistan, available at http://www.fdi.net/investmenthorizons_afghanistan/ accesses on 28/10/2013.

[61] United States of America, Department of Commerce, International Trade Administration, Afghanistan: Business opportunities, available at http://trade.gov/afghanistan/tg_aftf_003393.asp accessed on 10/11/2013..



Chapter 5

Indo-Afghan Ties

5 Indo-Afghan Ties



India and Afghanistan enjoy a rich civilization and historical relationship that spans many millennia; a relationship that has gained strength from India's role in the reconstruction of Afghanistan. The principal objective of India's development partnership is to assist in building indigenous Afghan capacity and institutions and to ensure that development touches all the regions of Afghanistan and encompasses all the sectors of development.

India is involved in a wide array of development projects in Afghanistan. India's programmes cover four broad areas – infrastructure projects, humanitarian assistance, small and community based development projects, and education and capacity development. An illustrative list of India's projects in Afghanistan is presented below:

- In January 2009, India completed **construction of the Zaranj-Delaram highway in southwest Afghanistan near the Iranian border**, which links Iran to the Garland "ring road" highway that connects most major Afghan cities.
- **India constructed the 202 kms long 220 kV DC transmission line** from Pul-e-Khumri to Kabul and a 220/110/20 kV sub-station at Chimtala, bringing Uzbek electricity and lighting up the city of Kabul throughout the year. **This project was completed in collaboration with the Afghan Government, ADB and the World Bank, with inputs from USAID and international energy firms, and is an outstanding example of regional and international cooperation in Afghanistan**.
- **Building Afghanistan's new parliament building-** a US$83 million project.
- **Rebuilding the Salma Dam power project in Herat Province;** this will provide electricity and irrigation in western Afghanistan.
- Beyond the large infrastructure projects, India's investment in Afghanistan also extends to **food aid, rural development projects and healthcare**.
- Many **Afghan students** have been given **scholarships** to study in India.
- **Training of Afghan police officers, diplomats and civil servants**.



Indian projects have created further demand for such projects. In Jalalabad, there is an increasing demand for more Indian projects particularly in terms of infrastructure development, cold storage, health facilities, information technology and cultural exchange programs.

India is also one of Afghanistan's major trading partners, and the flow of goods has been strengthened by a "Preferential Trade Agreement" signed in 2003.

With more than USD 2 billion pledged since 2001, India is today the by far largest regional donor in Afghanistan and the fifth largest in the world.

In 2011, the Strategic Partnership Agreement (SPA) was signed during President Karzai's visit to Delhi in October. India and Afghanistan also signed two partnership agreements in the mining area and in the production of hydrocarbons.

In November 2011, a consortium of public and private Indian companies, led by the state-owned Steel Authority of India (the Indian consortium —also includes the National Mineral Development Corporation, Monnet Ispat and Energy Limited, Rashtriya Ispat Nigam Limited, JSW Steel Limited, Jindal Steel Power Limited and JSW Ispat Steel Limited) won a bid to mine in three states in Afghanistan's Hajigak iron ore deposits, which includes the construction of a six million-ton steel plant, an 800-megawatt power plant and 200 kms each of road, rail and transmission lines - as well as a pledge to set aside one per cent of profits for establishing educational and medical facilities. Total investment by the Indian companies was pegged at USD 10.8 billion. The Hajigak iron ore deposit is estimated to hold 1.8 billion tonnes of ore. Afghanistan's largely untapped mineral wealth is thought to be worth some USD 3 trillion, and is often talked about as key to ensuring the country's economy. Thus, the Indian involvement in Afghanistan is both in aid and investment.

In a step that is likely to boost peace and give new shape to regional energy cooperation, India, Pakistan, Afghanistan and Turkmenistan, in May 2012, entered into historic gas sale purchase agreement (GSPA) for the USD 7.6-billion Turkmenistan-Afghanistan-Pakistan-India (TAPI) gas pipeline, often touted as the peace pipeline.

In the last week of June 2012, the Indian government organized an international meeting in New Delhi for regional investors interested in Afghanistan. The conference featured over 50 Afghan firms. This was the first time that India had held a conference aimed at highlighting the investment potential of another country.

India has taken lead with respect to the Trade, Commerce and Investment Opportunities (TCI) Confidence Building Measures (CBM) envisaged under the Istanbul Process for Afghanistan. Federation of Indian Chambers of Commerce and Industry (FICCI) has been identified as the Secretariat for the merged CBM. The Ministry of Commerce, Government of India has been identified as the Government of India's Technical Focal Point (TFP).

India and Afghanistan trade relations

India and Afghanistan total trade amounted to USD 588.36 million in 2012-13, with Indian exports accounting for USD 472.56 million and imports worth USD 115.80 million. The current trade balance is heavily in favour of India.

Table 10: India-Afghanistan total trade (US$ Million)

	2005-06	2006-07	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13
Export	142.67	182.11	249.21	394.23	463.55	411.78	510.9	472.56
Import	58.42	34.37	109.97	126.24	125.19	146.03	128.06	115.80
Total trade	201.09	216.48	359.18	520.47	588.74	557.81	638.96	588.36

Source: Ministry of Commerce and Industry, Government of India

Table 11 shows the top five commodities exported from India to Afghanistan. The share of top 5 commodities (at 2 digit level) accounted for nearly 59 per cent of the total exports from India to Afghanistan.

Table 11: Top five export items from India to Afghanistan (US$ million)

Sl. No.	HS code	Commodity	2011-12	2012-13
		Total	510.9	472.56
1	54	Man-made filaments.	120.35	116
2	71	Natural or cultured pearls, precious or semiprecious stones, pre.metals, clad with pre.metal and artcls thereof; imit.jewlry; coin.	64.57	45.14
3	30	Pharmaceutical products	48.76	44.75
4	61	Articles of apparel and clothing accessories, knitted or corcheted.	28.22	36.78
62	62	Articles of apparel and clothing accessories not knitted or crocheted.	44.82	35.8

Source: Ministry of Commerce and Industry, Government of India



The top five commodities imported from Afghanistan are given in Table 12. The top 5 commodities accounted for around 96 per cent. This reflects that Indian's imports from Afghanistan are heavily concentrated in a few commodities.

Table 12: Top five import items from Afghanistan to India (USD million)

Sl. No.	HS code	Commodity	2011-12	2012-13
		Total	**128.06**	**115.8**
1	8	Edible fruit and nuts; peel or citrus fruit or melons.	85.19	69.14
2	13	Lac; gums, resins and other vegetable saps and extracts.	34.48	28.73
3	7	Edible vegetables and certain roots and tubers.	0.2	7.62
4	9	Coffee, tea, mate and spices.	1.92	3.16
5	84	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof.	0.46	2.68

Source: Ministry of Commerce and Industry, Government of India

Agribusiness and agro-processing, construction and construction materials, energy and natural resources, textiles and carpets, transport and logistics, chemical and pharmaceutical products, banking and financial services, telecom services, real estate and tourism, hydrocarbons, etc. are among various areas of cooperation between the two countries.

Afghanistan offers immense possibilities for Indian investments in its era of reconstruction which could help build export supply capabilities in Afghanistan. The strengthening of trade-investment linkages in the country would help building the transit infrastructure which would in the second round further facilitate trade and investment flows. Moreover, connectivity with Afghanistan would provide access to the West and the Central Asian markets and their natural resources. In this sense too, Afghanistan could prove to be a strategic partner which would also facilitate making the South Asian region as the hub of economic activities between the Western and Eastern parts of Asia.

Indian private sector in fostering India- Afghanistan Relations: the FICCI initiatives

The Federation of Indian Chambers of Commerce and Industry (FICCI), as India's apex national chamber of SAARC Chamber of Commerce and Industry (SCCI),

serving the industry voice for policy change, play an instrumental role in spearheading this process of Indo-Afghan engagement. The Kabul Ministerial Conference of June 14, 2012 laid down a common set of confidence building measures (CBM) ranging from political and security cooperation to economic cooperation, disaster management and education. India has taken the lead with respect to the 'Chambers of Commerce CBM' and the 'Commercial Opportunities CBM'. FICCI has been nominated as the Technical Focal Point from India, to work on these very important initiatives. FICCI works closely with Afghanistan Chamber of Commerce and Industry bilaterally and works regionally under the umbrella of SAARC Chamber of Commerce and Industry.

FICCI intends to develop a cooperative framework to bind the region in a web of trade, energy and transport linkages that will not only act as a major confidence building measure but will also contribute to greater economic synergies in the region and spur economic growth in Afghanistan and beyond.

Box 3. Participants of the Afghanistan TCI CBM

Participating Heart of Asia Countries	Afghanistan, Azerbaijan, India, Iran, Kazakhstan, Kyrgyzstan, Pakistan, Russia, Tajikistan, Turkey, Turkmenistan and UAE
Lead Country	India
Participant Supporter Countries	Australia, Canada, European Union, Egypt, Germany, United Kingdom and United States of America
Participant UN Agencies	UNDP, UNECE, UNESCAP and UNSPECA

An illustrative list of events that the FICCI had organized includes:

- A Capacity Building Programme for a batch of 10 Afghanistan Chamber of Commerce and Industry (ACCI) officials from June 17-24, 2013 in New Delhi under the TCI CBM. The module of the capacity building programme included training on organization of events, member engagement, and broadening membership base, problem solving and decision making, business development and export promotion.
- A Business-to-Business Meetings in association with the Export Promotion Agency of Afghanistan (EPAA), with a Fresh and Dry Fruits' Traders Delegation from Afghanistan in Mumbai and Hyderabad on June 24-25, 2013. The Afghanistan delegation comprised seven fresh fruit and four dry fruit traders. The aim was to give an opportunity to the Afghan traders to



explore further markets in India. The retailers and wholesalers in Mumbai and Hyderabad, usually buy from traders based in New Delhi, and do not directly import from Afghanistan. This event allowed the businesses on each side to directly connect with each other.

- Several sensitization programmes for Indian business community on the emerging opportunities in Afghanistan from time to time.

FICCI believes that India's immediate neighbourhood must be a primary focus of its foreign policy. As democracies in the region, parliamentarians must lead the synergy between government, civil society, industry, media and academia, and achieve an outcome in which we are all winners. Towards this end, in May 2012, FICCI had organized an interactive meeting with senior parliamentarians from Afghanistan visiting India. Commerce Secretary of India and President, SAARC Chamber of Commerce and Industry were also present at the meeting. The interaction provided an opportunity to Indian businesses to obtain information and clarity on several business opportunities emerging in various sectors in Afghanistan.

In collaboration with the Public Diplomacy (PD) Division of the Ministry of External Affairs, FICCI has launched a Monthly Foreign Policy Forum. The objective of FICCI – PD Monthly Foreign Policy Forum is to have a multifaceted and in-depth discussion of India's relations with its principal partner countries and regional entities. The Forum has been envisaged to provide a platform for generating debate, discussion and exchange of ideas on various aspects of India's foreign policy. Invitees include a cross section of stakeholders including government officials, former diplomats, industry representatives, academia, and think tanks, to arrive at a better understanding of the issues. Towards this end, the FICCI had organized a forum on "Rebuilding Afghanistan" in February 2012.

In the month of April 2011, FICCI organized a business meeting to sensitize the Indian business community on the opportunity in mining and infrastructure sector in Afghanistan.

In November 2007, FICCI had organized a "Seminar on Doing Business with Afghanistan". The seminar was inaugurated by the then Hon'ble Indian Minister of State for Commerce & Power. The seminar was attended by senior diplomats, government officials and leading businessmen from India and Afghanistan.

Early, since the beginning of the transition period, FICCI engaged with Afghanistan to promote business. To this end the FICCI had organized:



- A meeting with HE Mohammad Arif Noorzai, Minister of Small Industries of Afghanistan in 2002. The meeting was attended by over 50 top businessmen, representing different sectors of the economy.
- An interactive meeting with Mr S K Lambah, Special Envoy to Afghanistan in 2002. The meeting deliberated on issues pertaining to Afghanistan. The meeting was attended by various diplomats, senior government officials, representatives of multilateral institutions and more than 250 leading businessmen.
- A call on meeting with Dr Abdul Rehman, Minister for Civil Aviation & Tourism of Afghanistan in 2002. The Minister urged Indian businessmen to visit Afghanistan so as to obtain first-hand information.

Helping Afghan women in small business: SEWA in Afghanistan

Self Employed Women's Association (SEWA), India's largest union of women who run small businesses in the informal sector had trained Afghan women to run economically viable businesses appropriate to their cultural context[62].

SEWA has been selected by the Ministry of External Affairs, Government of India to help the Ministry of Women Affair, Afghanistan to develop a women's Vocational Centre for Training at Bagh-E-Zanana facility in Kabul. In an exposure visit, a delegation of 20 Afghan women including the ministry officials and NGOs visited SEWA in Ahmedabad. SEWA's senior coordinators visited the project site and prepared a feasibility report after conducting a study. The report recommended that the facility be developed into a vocational training centre for women to be developed further into a Community Business Resource Centre (CBRC). SEWA will train some Afghan women who will later on work as trainers and administrators at the vocational training centre. The subjects of training will include embroidery, stitching, garment manufacturing, nursery and plantation, processing and packaging of fruits and nuts, management and marketing. The project will economically empower women in Afghanistan, who do not have means of livelihood, including many war-widows[63].

[62] Civil Society, SEWA brings hope in Kabul, available at http://www.civilsocietyonline.com/Archieve/aug08/dec0844.asp accessed on 11/11/2013.

[63] Business Standard, SEWA to help Afghanistan develop center for vocational training, November 11, 2013 available at http://www.business-standard.com/article/economy-policy/sewa-to-help-afghanistan-... accesses on 11/11/2013.



Chapter 6

Conclusions

6 Conclusions



The World Bank has made a number of salient observations regarding Afghanistan's macroeconomic challenges and prospects in the near future. Afghanistan's aid dependency is one of the highest in the world and has increased sharply in the last decade. In 2010/11, total military and civilian aid[64] was US$ 15.7 billion, about the same size as of the GDP. The civilian component of aid was nearly 40 percent of the GDP. Aid contributed to domestic demand for construction and procurement of goods and services thereby contributing to economic growth. About half of the core budget of the Government was contributed by the donor grants in 2010[65]. Effort to improve local sourcing led businesses to retain some workers they employed[66]. Although capital inflows linked to investments in mining are expected, the decline in aid outweighs these inflows; particularly in the first years after 2014 (mining activities are expected to start only in 2016/17)[67]. Macroeconomic stability is heavily dependent on abundant aid flows. In 2010/11, the current account deficit (excluding grants) was estimated at 40 percent of GDP[68]. Targeted intervention by donors and the government are needed to support economic adjustment and companies may find it hard to cope with declining demand in transition-affected sectors. 'Shallow' financial sector limits the scope of flexible adjustments by the formal private sector. Adjustment will be harder as new pattern of future demand evolves. Construction companies that may have specialized in building roads or providing works for military purposes may not have the required skills for emerging sectors in mining and other infrastructure. Coping with the short term negative impact of the aid decline may require scaling up of workfare programme or training to prepare workers for new demands arising from emerging economic activities[69].

[64] Aid here does not include spending on international military forces.

[65] The World Bank (2012), p. 27.

[66] Ibid., p. 37.

[67] Ibid., p. 35.

[68] Ibid., p. 33.

[69] The World Bank (2012), p. 43.

The two important prescriptions emerge from this diagnosis. Any abrupt aid reduction has to be avoided. Channelising of aid through domestic budget needs to be calibrated a targeted improvement of absorptive capacity of the Government. The Government should strengthen and step up the reforms programme. The business opportunities in Afghanistan are unfolding and will open up further. It is for the stakeholders to accelerate the process.

About FICCI

Established in 1927, FICCI is the largest and oldest apex business organisation in India. Its history is closely interwoven with India's struggle for independence, its industrialization, and its emergence as one of the most rapidly growing global economies. FICCI has contributed to this historical process by encouraging debate, articulating the private sector's views and influencing policy.

A non-government, not-for-profit organisation, FICCI is the voice of India's business and industry.

FICCI draws its membership from the corporate sector, both private and public, including SMEs and MNCs; FICCI enjoys an indirect membership of over 2,50,000 companies from various regional chambers of commerce.

FICCI provides a platform for sector specific consensus building and networking and as the first port of call for Indian industry and the international business community.

Our Vision

To be the thought leader for industry, its voice for policy change and its guardian for effective implementation.

Our Mission

To carry forward our initiatives in support of rapid, inclusive and sustainable growth that encompass health, education, livelihood, governance and skill development.

To enhance efficiency and global competitiveness of Indian industry and to expand business opportunities both in domestic and foreign markets through a range of specialised services and global linkages.

ESCAP South and South-West Asia

Established in December 2011 in New Delhi, ESCAP South and South-West Asia Office (http://sswa.unescap.org) assists 10 member countries in the subrregion, namely Afghanistan, Bangladesh, Bhutan, India, Islamic Republic of Iran, Maldives, Nepal, Pakistan, Turkey and Sri Lanka, achieve inclusive and sustainable development through its normative and analytical work, policy advocacy and capacity-building activities and the promotion of regional cooperation.

Federation of Indian Chambers of Commerce and Industries

Federation House
Tansen Marg, New Delhi 110001
T : 91-11-23738760-70
F : 91-11-23320714, 23721504
E : saarc@ficci.com
W : www.ficci.com

UN-ESCAP South and South-West Asia

C-2, Qutab Institutional Area
New Delhi-110016 (India)
T : +91 11 30973701, F : +91 11 26856274
E : sswa.escap@un.org
W : sswa.unescap.org