

Balkh's Economy in Transition

Paul Fishstein

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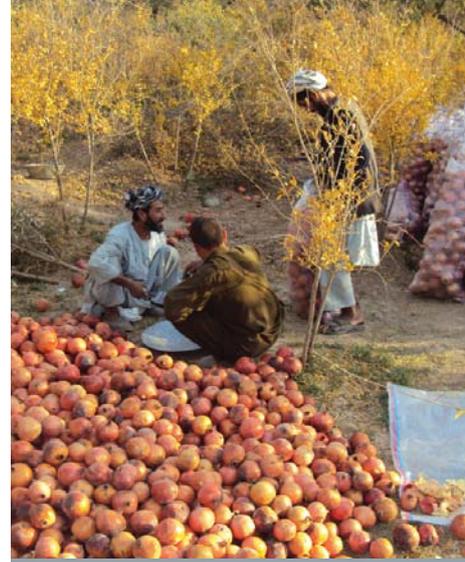
Islamuddin Amaki

and Mohammed Qasim

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Paul Fishstein
with
Islamuddin Amaki
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Table of Contents

Glossary	vi
Acronyms.....	vii
Executive Summary	1
Afghanistan’s economy since 2001	1
Balkh’s economy	1
Balkh’s economy in Transition	2
Positive factors and opportunities	2
Constraints and limiting factors	3
Recommendations	3
1. Introduction	5
1.1 Background: purpose and rationale	5
1.2 Previous work and analysis concerning effects on transition	5
2. Methodology.....	7
3. Economic Progress since 2001 and Prospects for the Future	8
3.1 Economy before 2001	8
3.2 Economy since 2001	9
3.2.1 Economic policy.....	9
3.2.2 Economic performance	10
3.3 Prospects for the future	12
3.4 The neighbourhood and regional initiatives	15
3.5 Labour market and employment.....	17
3.6 Afghan government policies and programmes on employment	20
4. Balkh Province	22
4.1 Basic information: geography, population, and social indicators	22
4.2 Brief recent historical overview	24
4.3 The business-political nexus in Balkh	25
4.4 Development assistance and the international presence: quantity and quality	26
5. Balkh’s Economy	29
5.1 Balkh’s economy before 2001	29
5.2 Balkh’s economy post-2001.....	29
5.3 Contribution of the major sectors	31
5.3.1 Agriculture	31
5.3.2 Construction	33
5.3.3 Land	35
5.3.4 Trade and transport.....	37
5.3.5 Carpets	40
5.3.6 Mining	41
5.4 Labour in Balkh’s economy	41

6. Looking Ahead.....	44
6.1 Security and political change	44
6.2 Uncertainty, risk and lack of confidence	45
6.3 Uncertainty about Transition reinforcing historical and current constraints	47
6.4 Likely effects of reductions in international spending and presence	48
6.4.1 Current and projected aid	48
6.4.2 Base employment, contracts, and contract-related employment	50
6.4.3 Private security contractors and militias	51
7. Summary, Conclusions and Policy Recommendations	52
7.1 Summary and conclusions.....	52
7.1.1 Positive factors	53
7.1.2 Additional factors.....	54
7.2 Recommendations.....	55
Request for Feedback	57
Recent Publications from AREU	58

Boxes, Tables, and Figures

Box 1: Popular views of the market economy.....	10
Box 2: Views on the quality of aid projects	28
Box 3: Views on competition, trade and the market economy.....	38
Table 1: NRVA provincial-level indicators on poverty for Balkh	23
Table 2: Provincial distribution of external assistance in 2002-10 and 2011, Balkh and selected provinces, total and per-capita (p/c).....	27
Table 3: Balkh companies, per registration with AISA.....	34
Table 4: Agricultural products exported via Hairatan and Aqina	39
Table 5: NRVA provincial-level indicators on employment for Balkh, percentages and rank	43
Figure 1: Price of plot of land at shahrak Khalid bin Walid	36
Figure 2: Wages for unskilled & skilled labour, 2003-13, annual average.....	42

Glossary

<i>arbaki</i>	Originally tribal security forces indigenous to the Loya Paktia region, but now refers to almost any irregular local security forces
<i>chai khana</i>	Tea house, often used as a social meeting place
<i>chars</i>	Hashish or the plant from which it comes (<i>cannabis sativus</i>)
<i>commission-kar</i>	Commission agent who extracts a percentage from transactions, often related to government permits; often used pejoratively
<i>esfand</i>	Wild rue, a perennial shrubby weed used as a carpet dye and or burned as a spiritual purifying agent
<i>hawala</i>	Method for transferring funds outside of the formal banking sector
<i>hing</i>	Asafoetida, a herb growing wild in northern Afghanistan and used for medicinal and cooking purposes
<i>jerib</i>	Measure of land area equal to 0.494 acre or roughly one-fifth of a hectare
<i>jihad</i>	Righteous struggle or holy war, usually referring to the 1979-92 war against the Soviet occupation
<i>inteqal</i>	Transition or transfer, used to refer to the transfer of security responsibility to the Afghan government at the end of 2014
<i>kunjara</i>	Oil seed cake – from cotton seed, flax (linseed), sesame, sunflower seed, mustard; used as animal feed
<i>lalmi</i>	Rain-fed (i.e. land, crops); also referred to as <i>daima</i> in the north
<i>mujahidin</i>	Guerrillas who fought in the 1979-92 war against the Soviet occupation (literally, those who fight jihad, or holy war)
<i>Nawroz</i>	Afghan new year, occurring on 21 March
<i>qarakul</i>	Type of lamb valued for its skin, sometimes known as “Persian lamb”
<i>Rowza-e Sharif</i>	Shrine of Ali in Mazar-e Sharif, erroneously referred to as the “Blue Mosque”
<i>sarai</i>	Enclosed compound, usually for commercial activity such as goods storage or light manufacturing
<i>selbord</i>	Culvert designed to channel water (literally, flood carrying)
<i>shahrak</i>	Planned residential development in which plots are sold or distributed
<i>shirkat</i>	System whereby ownership of factory is shared between government and private sector individuals
<i>tassady</i>	State-owned enterprise
<i>wasita</i>	Personal relationship or connection often used to obtain a favour such as employment or processing of paperwork
<i>woleswal</i>	District administrator or governor; one who administers a <i>woleswali</i>
<i>woleswali</i>	Administrative division within a province
<i>Wolesi jirga</i>	Lower house of Afghan parliament

Acronyms

ACCI	Afghanistan Chamber of Commerce and Industry
ADB	Asian Development Bank
Afs	Afghanis, the Afghan unit of currency. During the period of fieldwork the Afghani ranged between 51 and 55 to the US dollar.
AISA	Afghanistan Investment Support Agency
ANA	Afghan National Army
ANDS	Afghanistan National Development Strategy
ANP	Afghan National Police
ANSF	Afghan National Security Forces
COIN	Counterinsurgency
CPI	Consumer Price Index
CSO	Central Statistics Organization
DAIL	Department of Agriculture, Irrigation and Livestock
DDR	Disarmament, Demobilisation and Reintegration
GDP	Gross Domestic Product
GIZ	German Agency for International Cooperation
Ha	Hectares
IMF	International Monetary Fund
ISAF	International Security Assistance Force
MC	Mercy Corps
NGO	Non-governmental Organisation
PRT	Provincial Reconstruction Team
SHC	Samuel Hall Consulting
SME	Small and Medium Enterprise
UN	United Nations
UNFPA	United Nations Population Fund
UNODC	United Nations Office on Drugs and Crime
USAID	United States Agency for International Development

Executive Summary

While most analysis and discussion on the 2014 Transition has focused on security and fiscal issues, there has been increasing concern about the economic effects of the drawdown, both directly from reduced spending on goods and services and indirectly from the scaling down of development activities that have accompanied the military presence. There is little doubt that the reduction in international spending will negatively affect the Afghan economy, although there is disagreement over the degree and the extent. Analysis suggests there will be the most impact in conflict-affected provinces that received the most aid and in service, transport and other sectors driven by donor-related consumption.

Afghanistan's economy since 2001

Since 2001, Afghanistan's overall economy has performed strongly, with real growth in gross domestic product averaging over 11 percent per year between 2003 and 2012, and per-capita income more than doubling. Growth has been driven by dynamic sectors such as construction, telecommunications, trade and transport.

Despite overall economic growth, unemployment remains one of the most daunting problems facing Afghanistan. Critics charge that, despite the rhetoric of job creation and poverty alleviation, employment has often been pushed behind the political agenda, and other than stabilisation programmes which create casual or short-term employment to draw fighting-age men away from the insurgency, there has been a lack of focus on sustainable job creation and poverty reduction.

Fulfilling hopes for the extractive industries and trade sectors to create employment and broad-based wealth will require security, more harmonious regional political relations, infrastructure investment, institutional and governance reforms, and time

Even more than most countries, Afghanistan's political and economic trajectory will depend largely on the actions taken by its immediate neighbours, which are influenced in turn by those nations' relations with each other and with other nations. Political considerations, distrust, interest group capture, and in some cases a mercantilist or zero-sum mentality are likely to put limits on what can be achieved in the way of regional economic cooperation.

Balkh's economy

Balkh Province and its provincial centre, Mazar-e Sharif, historically the political and economic hub of the north, are seen to have thrived largely because of location, security, and relatively effective administration. In Balkh, there is an even stronger overlap than elsewhere between the business community, parliamentarians, provincial council members, and strongmen, with Governor Atta Mohammad Noor playing a central role.

The post-2001 economic expansion in Balkh has been driven largely by a number of key sectors, especially construction, transport and trade. While in recent years upgraded roads, reduced transport costs, and the relatively permissive security environment have facilitated the movement of outputs to markets, aside from low productivity, lack of markets remains one of the largest issues facing agriculture.

That construction companies make up more than half of the firms registered in Balkh underlines the weight that sector has had as a driver of the provincial economy. While the legality of the distribution of state lands around Mazar for *shahraks* (residential communities) and other projects has been questioned, land development has stimulated the private construction sector.

The post-2004 economic boom in Mazar, especially the construction sector, has attracted labourers not only from elsewhere in Balkh and its neighbouring provinces, but also from farther afield. Mazar's casual labour market is an important part of the livelihoods picture for many households even in rural areas; informal estimates are that 80 percent of casual workers

are from rural districts. In fact, there is evidence that due to better-paying construction-related opportunities in Mazar, labourers have been unwilling to undertake more strenuous agricultural work on the farm.

Balkh's economy in Transition

The 2014 Transition and the intensifying political activity at the national and international levels has put into play a set of dynamics which will affect the level and mix of economic activity in the province. The main factors that will affect the economy are security and political uncertainty. The international military in Balkh has been relatively low-key and unobtrusive, yet many believe that its presence off-stage has had the positive effect of keeping in check predatory local commanders and other potential sources of instability. Most respondents were therefore not eager to see a full drawdown.

Not surprisingly, uncertainty and lack of confidence in the future has affected economic behaviour, especially investment and consumer spending. Worrying indicators in Balkh include the 30-60 percent fall in the land and property market, decline in the private vehicle market, and increased caution in household spending. Economic actors noted the re-assertion of the historical preference for trade due to its shorter timeframe and lower risk. Given current levels of uncertainty, it is unrealistic to expect much if any improvement in the economic situation until after the 2014 international military drawdown and presidential elections. At the same time, uncertainty could become a self-fulfilling prophecy and affect economic decisions.

While precise calculations do not exist, informed sources estimated that construction activity has declined by 50 percent since 2010 and there has already been something of a shakeout of some of the smaller, less qualified firms. A reduction in construction activity affects employment at all levels, including those who rely on casual labour income and those who supply construction materials such as gypsum, lime, brick, and windows and doors. There are indications that labour wages might be stagnant or even declining in 2012 and 2013. Trade and transport sectors will also be affected by the reduced demand for construction materials as well as consumer goods.

Migration to Iran has become a less attractive livelihood option due to regional political dynamics, increasing restrictions on Afghans in Iran, and the roughly one-third fall in the value of the *rial* since January 2009 due to western sanctions. This will reduce remittances and may increase the number of unemployed in rural areas.

While Balkh has been counted as "poppy-free" since 2007, a decline in employment opportunities may also increase pressure to relax the suppression of opium poppy cultivation. This will hardly be an economic and political environment in which to maintain unpopular counter-narcotics policies on which there is already pressure; overall, it is hard to see any factors that would discourage cultivation.

There will be a number of direct and secondary effects on the local economy as a result of the drawdown of the military and development presence through reductions in base employment and contracts for base maintenance and off-base construction projects such as buildings and roads. However, the historically lower levels of spending by the international military in the province mean that Balkh will be less affected by the drawdown than other areas in the south and east.

Positive factors and opportunities

Balkh has a number of advantages, starting with its location, which position it to play a key role in external trade—should certain institutional constraints be relaxed. The upgrading and paving of the historical road between Khulm and Kunduz has potential to increase trade between Mazar and Kunduz, which at present must go via Pol-i Khumri. The pre-war industrial infrastructure in the province may provide some opportunities for rehabilitation. Upgraded roads, security, and infrastructure have contributed to expanded and reasonably well-functioning markets for agricultural commodities, and expanded production presents potential

opportunities for small- and medium-scale agro-processing industries. The somewhat revitalised international carpet market may create opportunity for the Balkh carpet industry, especially if it can find a way to increase the proportion of value added locally, and create backwards and horizontal linkages to suppliers of raw materials.

Germany and Sweden, key donors in Balkh, have committed to expanding aid funding to Afghanistan, with significant portions of this funding to be programmed in Balkh. It is not clear what proportion of USAID's reduced funding would go to Balkh. Under almost any scenario the next few years will see fairly steep reductions in the amount of international aid provided to Afghanistan, especially if failure to meet the indicators in the Mutual Accountability Framework are used to justify reductions in funding below the US\$16 billion for 2013-16 pledged by donors at the July 2012 Tokyo Conference.

Constraints and limiting factors

Some of the factors constraining the growth of broad-based economic activity in Balkh are common throughout Afghanistan, while some are specific to the province. Competition from cheaper regional imports is one of the most important constraints. To some extent, Afghanistan's massive trade imbalance reflects the highly uneven trading relationships enjoyed by the regional neighbours, who are accused of product dumping and predatory pricing explicitly targeting emerging Afghan industries that might compete with imports. In the intensifying political climate, increased concern about the intentions of the regional neighbours has economic dimensions, along with political, ethnic and sectarian ones. Due to geographical and historical factors, Balkh and northern Afghanistan in general are not as economically integrated with its northern neighbours as is eastern Afghanistan with Peshawar and Pakistan. The Afghan government is faulted for an inadequate response in providing infrastructure, imposing import tariffs, negotiating transport rights, and generally defending Afghan commercial interests.

Beyond that, there is the need for an effective institutional infrastructure for inspection and certification as well as industrial facilities for cleaning, sorting, drying and storage of agricultural production in order to create incentives and allow Afghanistan to add value in the types of processing currently done by its neighbours. The most consistent demand has been for construction of a major irrigation facility on the Amu Darya. The failure to take on this issue is invariably cited as evidence for the ineffectiveness of the government and its partners.

The caution with which Afghan economic actors are facing 2014 also reflects underlying and systemic characteristics of the economy that have historically limited broad-based growth, many of which are related to poor governance and the historical relationship between the public and private sectors, including non-enabling, anti-competitive, or even predatory behaviour by officials. The overall lack of faith in institutions helps to explain firms' reluctance to expand or even to go formal in the first place, lest they expose themselves and their assets to the risk of appropriation either through predatory corruption by government officials and their associates or, more catastrophically, through expropriation or re-distribution should a new government come into power.

Finally, a combination of factors—growth, poverty and weak institutions—has resulted in a number of serious environmental issues, including water scarcity with a rising population, riverbank erosion, environmental hazards created by the location of residential and commercial development, burning of dangerous substances (e.g. tires) for fuel, and the depletion of natural resources due to overharvesting.

Recommendations

Recommendations include:

- Avoid rapid reductions in international funding, which history has shown to be devastatingly destabilising, and which would discourage economic initiative.
- Be realistic about prospects for reform of both Afghan government and international institutions, recognising that under present conditions proponents of reform have limited leverage.

- Avoid creating opportunities for rent-seeking and opportunistic behaviour through careful consideration (including conflict analysis) of investments.
- Explicitly incorporate criteria such as job creation and on-the-job human capital development in project formulation.
- Explore possibilities for constructive de-concentration, which can free local officials and economic actors to act more nimbly while not undermining centre-provincial relations.
- Negotiate with international firms seeking to extract mineral resources in order to balance broader social benefits with competitiveness, while not creating opportunities for rent-seeking or protection.
- Encourage mechanisms for social accountability that can contribute to broadening the social benefits of future extractive and other economic activities.

1. Introduction

1.1 Background: purpose and rationale

As Afghanistan and its international partners prepare for the 2014 Transition (*inteqal*) to Afghan government responsibility, there is pervasive uncertainty about the country's political and security trajectory after the drawdown of international forces. Until recently, most analysis and discussion has focused on security issues, especially the readiness of the Afghan National Security Forces (ANSF). Other discussions have focused on fiscal issues, mainly the ability of the Afghan government to cover its costs, including of the massive security sector as well as services, through its own revenue. There has also been increasing concern about the economic effects of the drawdown, both directly from reduced demand for goods and services and indirectly from reduction in development activities that have accompanied the military presence.

There is little doubt that the reduction in international spending will negatively affect the Afghan economy, although there is disagreement over the degree and the extent. Previous research suggests that perceptions of poor economic performance, including inadequate job creation, have already created dissatisfaction and undermined the population's confidence in the state, and that anxiety is heightened as 2014 approaches. Based on the widespread belief in the link between poverty/unemployment and young men joining the insurgency, a decline in the economy could also lead to increased instability.¹

Balkh Province is significant because its economy is seen to have thrived, especially since 2004, and because it is the regional political and economic hub of the north. Balkh's success is attributed to a number of factors (as discussed in sections 5 and 6), but there has been insufficient empirical work and analysis on the extent of the growth, on how the benefits have been distributed and to what extent that growth will be sustainable.

1.2 Previous work and analysis concerning effects on transition

All observers, regardless of their level of optimism about the future, agree that Afghanistan's gains of the last ten years are fragile. The most significant analysis of the economics of Transition has been the World Bank's comprehensive study.² The "good news" is that because the benefits of aid were so unevenly distributed in the first place and so little actually reached the poor (partly due to the expatriation of significant donor financial resources), the impact of the reduction in the aid economy will be less than feared. Analysis suggests that larger (negative) impact will:

- Be in conflict-affected provinces which received the most aid;
- Aggravate underemployment more than unemployment;
- Impact more on low-skilled workers; and
- Have the largest effects on the service and transport sectors and other sectors driven by consumption.³

The World Bank's analysis emphasises the immense challenge of maintaining growth and increasing employment in an environment where aid resources, confidence and security may all be in decline. The analysis also identifies some of Afghanistan's strengths and weaknesses as it

1 The evidence base for this link and for the direction of causality is conflicting. Some believe that a strengthened economy is the key to stability, while others believe that it is stability that allows growth. See Dr. Björn Holmberg, et al. "Strategic Conflict Analysis of Afghanistan" (Reference Number 2011-000560, SwedePeace and CPAU, January 2012); Sarah Ladbury, in collaboration with Cooperation for Peace and Unity (CPAU), "Testing Hypotheses on Radicalisation in Afghanistan: Why Do Men Join the Taliban and Hizb-i Islami? How Much Do Local Communities Support Them?" (Independent Report for the Department of International Development, August 2009); Eli Berman, Joseph H. Felter and Jacob N. Shapiro, "Do Working Men Rebel? Insurgency and Unemployment in Iraq and the Philippines" (working paper for the National Bureau of Economic Research, November 2009).

2 Richard Hogg, et al. "Afghanistan in Transition: Looking beyond 2014" (World Bank, 2013).

3 Ibid.

approaches Transition and flags some of the relevant Afghan history, especially from the Soviet-era experience. Among the strengths relative to the period of Soviet withdrawal, it characterises the current economy as being in the process of recovering and growing rapidly, as compared with the state of destruction of the infrastructure and economic base 25 years ago.

The World Bank also flags the dangers of abrupt funding cut-offs or reductions, as well as undue optimism about the prospects for military victory and the consequences of a lack of a real peace settlement (i.e. 1988 Geneva Accords). On the positive side, the analysis notes that external financial support, when used carefully and strategically, may be more effective than military intervention and that military withdrawal in some cases led to stability.

A section of its Transition study lists “lessons learned” from other transition situations, comparing some of Afghanistan’s strengths and weaknesses with those of other countries. Strengths include high economic growth, relatively low inflation, good public sector financial management, and some effective national programmes that provide services. The much longer list of weaknesses includes an economy skewed toward services, low baseline for social indicators, poor governance and political variables, extremely high aid dependence, geopolitical strategic value and proxy involvements, and strong outside patrons imposing external agendas.⁴

More pessimistic analyses focus on the security situation, and question the relatively positive pronouncements on security issued by donor governments as well as the willingness of the Afghan state to take on institutional and governance reform,⁵ the prognosis for rapid progress in key sectors (e.g. minerals), and the cooperation of neighbours such as Pakistan. These critics also note the unreliable data on which the conclusions are based and dismiss analysis and estimates as dishonest political “spin” by interested parties. As noted by Anthony Cordesman:

Many US and European actions have already begun to look like a cover for an exit strategy from Afghanistan...Many aid agencies and NGOs are already making major cuts in their programs, and some are already having to eliminate programs or withdraw from the country (36)...A major cutback in the size of civil aid efforts seems inevitable, but so far, the emphasis seems to be on cuts and not finding some functional approach to phasing the civil efforts down that offers a reasonable path toward a stable Transition. The civil surge is on a path where it will be replaced by a rush to the exits.⁶

In advance of the December 2011 Bonn Conference, the Afghan government issued a brief paper presenting its view of and strategy to respond to the likely economic impact of Transition.⁷ To some extent the paper echoes the World Bank analysis. In advance of the July 2012 Tokyo Conference, the government further elaborated on its vision for 2025 and beyond, including the focus on the extractive industries sector, improving the investment climate, regional integration, private sector development, and jobs and employment.⁸ Many of the assumptions and assertions in both papers appear quite optimistic, especially those relating to the likelihood of institutional reform and the extent to which the government will be able to reduce its need for external financial assistance, which is based largely on assumptions about the potential of the minerals sector. The other development initiatives are described in the 22 National Priority Programmes (NPPs), which are discussed below.

4 Hogg et al., “Afghanistan in Transition.”

5 A case study on the political economy of state-building in Afghanistan cautions on the challenges of accomplishing institutional reforms that do not align with the personal interests of power-holders. See Louise Anten, Ivan Briscoe and Marco Mezzera, “The Political Economy of State-building in Situations of Fragility and Conflict: from Analysis to Strategy” (A synthesis paper based on studies of Afghanistan, Democratic Republic of Congo, Guatemala, Kosovo and Pakistan, January 2012), 4.

6 Anthony H. Cordesman, “Afghanistan: The Uncertain Economics of Transition” (Center for Strategic and International Studies: First Working Draft, 18 April 2012), 57.

7 The Government of the Islamic Republic of Afghanistan, “Towards a Self-Sustaining Afghanistan: An Economic Transition Strategy” (Kabul, November 2011).

8 The Government of the Islamic Republic of Afghanistan, “Towards Self-Reliance: Strategic Vision for the Transformation Decade” (Kabul, July 2012), 4.

2. Methodology

The study utilised primarily descriptive analysis to get a sense of the sources of economic activity in Balkh, how political structures either encouraged or discouraged economic activity, how formal or informal structures influenced the level and type of economic activity, informal state practices, the role of international trade, the respective roles of the public and private sectors, and issues related to competitiveness. The approach considered Afghanistan's well-documented market imperfections, including inconsistent enforcement of policies, weak infrastructure, insecurity, official corruption, differential access to business opportunities based on political and military power, and general uncertainty.⁹

The study drew on a number of primary and secondary sources. Primary data collection was done through key informant interviews with: government officials (both line ministry and local administration), aid officials, aid contractors, non-governmental organisations (NGOs), trade associations, private sector representatives (traders, businessmen, Chamber of Commerce), farmers, and journalists. Interviews took place mainly in Mazar, but also in the key border towns of Hairatan and Aqina (Faryab Province) and in the small towns of Khulm, Dehdadi and Balkh. Given the importance of construction and agriculture, Afghan consultants conducted individual mini-case studies of these two sectors.

Secondary data sources included a broad range of existing data and analysis, including official statistical reports from the Afghan government (Central Statistical Organization, da Afghanistan Bank, National Risk and Vulnerability Assessment [NRVA] provincial and national reports, Poverty Profile, Donor Assistance Database), economic reporting from multi-lateral institutions (e.g. World Bank quarterly Economic Update, International Monetary Fund [IMF] statistical series), programme and project-related documents (e.g. sector studies, evaluations, assessments), and other analysis.

As with most research in Afghanistan, the primary constraint was the lack of consistent and reliable quantitative data, especially data disaggregated to the provincial level. Both Afghan government and international donor information on resource flows are still incomplete and unreliable after nearly 12 years. (One respondent characterised available data as being "islands of information.") Some of the data issues related to specific sources are discussed below. The lack of disaggregated economic data limited the quantitative aspects of the study. Given the lack of systematic and reliable data (e.g. property values), in some areas the research relied on the expressed perceptions of individuals, whose personal and institutional agendas and biases must be taken into consideration.

The analysis largely ignores areas that have been widely covered elsewhere, including fiscal effects. Also, while the study is on Balkh Province, due to logistical, time, and resource reasons, the analysis has focused largely on Mazar and surrounding areas.

⁹ Analysis drew on a more explicitly political economy perspective in Antonio Giustozzi, "The Resilient Oligopoly: A Political-Economy of Northern Afghanistan 2001 and Onwards" (Kabul: AREU, December 2012).

3. Economic Progress since 2001 and Prospects for the Future

3.1 Economy before 2001

Historically, Afghanistan had what could be called a “mixed guided” (rather than “Soviet”) system. Before 1978, the economy was dominated by agriculture and small-scale trade, while a number of large economic enterprises were either 100 percent state-owned (later covered under the 1991 State Owned Enterprise [*Tassady*] Law), administered by the respective line ministries with shares owned by the Ministry of Finance, or under the so-called *shirkat* system, whereby the government controlled 40-45 percent of stock, with the rest in private hands. Government officials and members of the royal family (which were in many cases one and the same) were major shareholders in the *shirkats*, which simultaneously assured them personal profit and the enterprises’ support from the government.¹⁰ Critics of the *shirkat* system say that it allowed the government to control production and obtain an easy source of extracted income. The trading sector was primarily, although not exclusively, private. All economic enterprises were subjected to often-stifling government control. Critics feel that as much as the tight control it was the uncertainty created by the inconsistency and lurches in policy (from statist to private to nationalisation) which most retarded private sector development—with the state typically looking for a way to extract resources.¹¹ Major economic ventures such as the Spinzar Company, Afghan Nassaji (textile), Ariana Afghan Airlines, Shirkat-e Kamaz, Baghlan Sugar Enterprise, and the “silos” in the primary cities¹² were largely associated with the state, even if they were not completely state-owned.

In the early years of the People’s Democratic Party of Afghanistan (PDPA) government post-1978, economic policy further emphasised the role of the state, especially in its rhetoric, which stressed the plight of the rural, exploited masses of agricultural workers. The government’s rhetoric and actions were overtly hostile to the people they referred to disparagingly as “feudals” and “capitalists,” and many businessmen lowered their profiles, left the country, or in some cases were killed. The PDPA’s urban bias and its belief that the sooner peasants joined the industrial working classes the sooner Afghanistan would truly develop may have been reflected in the reduction of the proportion of financial resources allocated to the agricultural sector. In the 1982 annual plan, for instance, only 10 percent was allocated to agriculture, although at that time agriculture generated almost two-thirds of gross domestic product (GDP).¹³ The belief was also reflected in the greater investments made in the mining and industrial sectors, which were largely state-owned.

It was also during this time that the net of social services for the urban population greatly expanded, in part to reinforce the loyalty of the government’s main constituents, but also because the rural areas were in revolt and therefore were largely inaccessible to the state. (According to one estimate, social services made up a quarter of the development budget, and were twice the proportion of the development budgets in the previous decade.¹⁴) Rising prices, declining availability of goods, and overall deteriorating social and economic conditions as a result of the war outside the cities motivated the government to further strengthen support to the urban areas through price controls and consumer subsidies, the latter through a network of “cooperative shops” selling essential goods below market prices and the very popular “coupon” system. Under this system, a version of which began as early as the 1930s, public sector employees and their (loosely defined) families received coupons for a range of commodities, including wheat, cooking

10 Richard F. Nyrop and Donald M. Seekins, ed., *Afghanistan: A Country Study* (Foreign Area Studies: The American University, January 1986). Available at: <http://onlinebooks.library.upenn.edu/webbin/book/lookupid?key=olbp25396>.

11 See Maxwell J. Fry, *The Afghan Economy: Money, Finance, and the Critical Constraints to Economic Development* (Leiden: E.J. Brill, 1974), especially Chapter III, “A Fragmented Economy.”

12 Several “silos” or large-scale, industrial grain storage silos and bakeries were built in the major cities, including Mazar, by the Soviets during the 1970s.

13 Nyrop and Seekins, “Afghanistan Country Study,” 153. In an interesting echo, “The five-year plans reflected the wishes of the different ministries but did not attempt to lay down foundations for overall economic policies. The plans provided no priorities, nor did they give detailed descriptions of the ways stated targets would be achieved. They were, in fact, mere lists of projects designed to solicit foreign aid...The projects in the various plans were poorly formulated, in part because their foreign designers were ignorant of the Afghan environment,” 146.

14 *Ibid*, 154. Given the chaos of the war years, any conclusions based on the government budget or other government-provided statistics should be drawn carefully.

oil, and other essential items. According to one source, by the late 1980s coupons or ration books were supporting 340,000 families,¹⁵ and such non-monetary benefits were a significant proportion of total remuneration. The system also reinforced the idea that the state had a direct role in providing for the welfare of the population.

3.2 Economy since 2001

3.2.1 Economic policy

In 2002, Afghanistan adopted a liberal, free-market approach to its economy, subsequently formalised in Article 10 of the 2004 Constitution. The government's stated aim was the "development of an enabling environment that encourages the private sector to play a central role in the economic development of the country," and in which "government is the policy maker and regulator of the economy, not its competitor."¹⁶ This represented a new orientation to a society that historically relied on either state-owned or mixed public-private enterprises. During the previous decades, furthered by the collapse of the Soviet Union in 1991, there had been a worldwide shift toward private-sector based development and a set of policies often called "the Washington consensus." Given that during this period Afghanistan had mostly been at war and not so focused on economic policy, the policy shift to the market economy might have seemed more sudden to the officials and others whose formative recollections were from pre-1978. It should also be noted that many Afghan refugees in Pakistan and Iran, both out of necessity and opportunity, became highly entrepreneurial in an environment with fewer social constraints and regulation than they might have had at home. Regardless, the new economic policy was widely perceived as being, if not imposed, at least inspired by the western donors. (See Box 1.)

Within ministries, the neo-liberal policies backed by the donors have often conflicted with the more state-oriented attitudes held by Afghan civil servants, due either to beliefs or, in some cases, alleged self-interest. Moreover, the international community has not been averse to bending some of its market-oriented economic principles to fit the purposes of individual institutions, projects or persons.

Perhaps in reaction to the perceived hands-off approach, there has been criticism of the government among the general population and from the business community for not adequately supporting Afghanistan's interests, although in some cases these are clearly individual or institutional interests. For instance, there has been consistent pressure from businesses to support Afghan industries through subsidies, import tariffs, or outright bans on imports. According to the newly established Afghan Industry Union, "Afghan industries are now capable of producing food items, non-alcoholic beverages and plastic goods; therefore, the government should ban the import of such products."¹⁷ The Afghanistan Chamber of Commerce and Industry (ACCI) and other business representatives have also criticised the government for maintaining higher import tariffs on raw materials (e.g. plastic) and intermediate inputs than on final goods, thereby encouraging imports and discouraging domestic production.

Other than lobbying by political and business leaders for contracts or for slightly more diffused benefits, there has been a lack of a significant "Afghan first" campaign for Afghan products mounted by the government, and there is still very limited consumer consciousness in this area. While the companies under contract to produce boots and uniforms for the ANSF were presented as Afghan success stories, these contracts have apparently been terminated, and the ANSF was said to be procuring these items more cheaply from China.¹⁸ In a more pro-active move, at the end of 2012, the government indicated plans for a ten-year tax holiday for investments made during the next two years.

15 Martin Kipping, "Two Interventions: Comparing Soviet and US-led state-building in Afghanistan" (Afghanistan Analysts Network, January 2010).

16 Afghanistan National Development Strategy, 2008.

17 "Afghan Industry Union Calls for More Government Supports," *Ariana News*, 29 January 2012.

18 Afghan companies directly hired to support the uniforms and boots factory resulted from the "Afghan First Policy" adopted by the US Embassy, US Forces, and ISAF in 2010. This policy guided the US military and US civilian agencies to hire Afghans first, buy Afghan products and build Afghan capacity. In 2011, ISAF estimated that US agencies contracted over US\$4 billion directly with Afghan companies as prime contractors (out of \$17.3 billion in civilian and military contracts in 2011).

Box 1: Popular views of the market economy

A common critique expressed in the Afghan media and within civil society is about the negative effects of post-2001 economic policy, especially the adoption of the market economy. Many Afghans recall, however imperfectly, the pre-1978 era when the state built factories, infrastructure, and other job-creating modern assets, and when Afghanistan had experienced slow but steady growth.

After the fall of the Taliban there was a general expectation that the state would again take the lead in the economic sphere. Afghans have increasingly expressed dissatisfaction with what they perceive, accurately or not, to be the results of that free market policy (high prices, low-quality goods, and impunity by economic actors), especially the perception that the state has failed to create jobs. Even the NPP for integrated trade and small and medium enterprise support, focused on developing the market economy, takes a bow towards acknowledging this dissatisfaction by saying “market failures limit the ability of private enterprises to achieve socially desirable outcomes. For its part, the public is increasingly disenchanted with macroeconomic stabilization and reforms that have not led to sustained growth, and openly questions the costs of these pro-market policies.”¹

Critics have charged that the lack of government attention to the economy has led to corruption and the enrichment of a few individuals at the expense of many, which conveys the notion of a state that doesn't care. Exposure to markets that favour those in power and tolerate the predatory behaviour of state institutions has increased people's risks and undermined efforts to build a social compact. There is also a certain expectation, informed in part by Islamic notions of equity and the role of the state, that a government should ensure the general welfare. In all, “what was presented by the international community as promoting free market dynamism has often been perceived by Afghans as another unjust way in which the powerful and corrupt were strengthened at the expense of the public.”²

The spectacular rise of the class of businessmen and the symbiotic relationship with politicians, commanders, and leaders has led some to refer to them as “oligarchs,” “gangs,” or “mafia.” These terms do not have a precise meaning, and commercial activity is not quite so tightly organised as they might imply, but they are used to reference the consolidated market, political and ultimately physical power the elites have. In one analysis, “strongmen's power to influence and coerce is more real than that of the Afghan state—not least because strongmen have to a large extent infiltrated state mechanisms...Individuals and groups may hold power in different forms: some have financial power, others have political or military power, and a few accumulate a portion of all forms.”³

These views are representative of broadly expressed perceptions of the post-2001 market economy in Afghanistan. The younger urban generation, some of whom grew up in Pakistan, may be more sympathetic to such a system, but not entirely.

Western chiding of the Soviets for introducing a communist economic model alien to cultural and historical conditions and which “collided with traditional Afghan values and undermined state legitimacy”⁴ reveals a blind spot on how free market economic policy has been perceived in some sectors of society. While not explicitly God-less, it is similarly seen in some quarters as an affront to traditional values.

1 Ministry of Commerce and Industry, “Integrated Trade and SME Support Facility. Private Sector Development Cluster. National Priority Programme Proposal” (Kabul, Undated).

2 Paul Fishstein and Andrew Wilder, “Winning Hearts and Minds? Examining the Relationship between Aid and Security in Afghanistan” (Boston: Feinstein International Center/Tufts University, January 2011), 44.

3 Giustozzi, “The Resilient Oligopoly,” 12.

4 Dr Anton Minkov and Gregory Smolynec, “Economic Development in Afghanistan During the Soviet Period, 1979-1989: Lessons Learned from the Soviet Experience in Afghanistan” (Canada: Defence R&D, August 2007).

3.2.2 Economic performance

In many ways, the Afghan economy since 2001 has been a tale of two economies, or rather, of many economies. Journalists in search of stories can find either the sleek, modern shopping malls that represent economic progress, or the nearby shantytowns that reflect enduring or even growing poverty. As in most places, dualistic development is readily on display: while workers line up each morning in the hope of finding day labour, consumers are now able to pay their electric bills by mobile phone.

In the aggregate, significant real GDP growth has taken place, averaging over 11 percent annually between 2003 and 2012, and per-capita income has more than doubled. In 1388 (2009-10) growth was a record 22.5 percent due in part to agriculture, which rebounded following the previous year's drought-like conditions that had resulted in a weak 3.6 percent growth. Growth has come from dynamic sectors such as construction, telecommunications, trade and transport. Between 2002 and 2011, services increased from 38 to 51 percent of GDP. Exports have increased by 300 percent in value and 400 percent by volume, albeit from a very low base. High marks have been given to the government's management of the macro-economy, most notably the transition to the new currency, control of inflation, and management of exchange rates. The government points to the increase in the proportion of the private sector in total investment, rising from 51 percent in 2001-03 to 58 percent in 2006-08 and to nearly 70 percent in 2008-10.¹⁹

While there has been rapid economic growth and rising incomes, a number of issues detract from the overall strong economic performance. High levels of growth have masked the poor and variable performance of agriculture, which generally remains stuck at low levels of productivity and fluctuates widely annually due to changes in precipitation and other environmental conditions. In fact, in the first few years post-2001, the recovery of agriculture due to the cessation of conflict and the end of a multi-year drought contributed to growth, but became proportionately less important as aid-related activities accelerated.

One of the main critiques of the post-2001 economic growth is that it has been driven by unsustainable, donor-related consumption based on the massive spending connected with the international presence. Sectors such as construction are especially dependent on international funding. For instance, according to the US CENTCOM, "60 percent of current construction contracts are financed from military and development assistance accounts."²⁰ Given that dependence, obviously any reduction in that spending will reduce growth. Reductions in spending have already been felt in the construction and logistics sectors, as reported in both media and analytical accounts.²¹

Another critique of post-2001 economic activity is the lack of specific focus on job creation and poverty reduction. The 2007-08 NRVA, which is the most comprehensive measure of the incidence of poverty, showed that 36 percent of the population remains below the poverty line, with incidence even greater among certain groups and in certain geographic areas.²² An International Labour Office (ILO) study notes that what attention there has been on employment, especially that related to stabilisation programmes intended to take young fighting-age men away from the insurgency, has not been on identifying unmet demand for labour, but rather has had "strategies that mostly result in the creation of casual and short-term jobs, rather than leading to sustainable employment creation."²³ Kantor and Pain (2010) note that while the 2004 Human Development Report presented an effective definition of poverty, in the 2008 Afghanistan National Development Strategy (ANDS) the definition was much more narrow, individualistic and technical, and that moreover less attention was paid to poverty reduction and livelihoods. By the 2010 Kabul and London Conferences, poverty reduction had slipped entirely off the agenda, even rhetorically.²⁴

Finally, Afghanistan's massive trade imbalance with its neighbours is widely cited as a source of dissatisfaction with the market economy as implemented in Afghanistan, as it is attributed

19 NPP for Facilitation of Sustainable Decent Work Through Skills Development & Market-Friendly Labour Regulation.

20 CENTCOM Powerpoint.

21 Executive manager of the Afghan Builders Association, cited in Rod Nordland and Sangar Rahimi, "As NATO Nears Exit, Construction Dries Up," *New York Times*, 4 November 2012. <http://www.nytimes.com/2012/11/05/world/asia/as-nato-nears-exit-afghan-construction-dries-up.html>. See also "Economic Assessment and Labour Market Survey of Mazar-i Sharif, Pul-i Khumri, Kandahar City and Kunduz City" (Report commissioned by Mercy Corps, Samuel Hall Consulting, 2012).

22 Government of the Islamic Republic of Afghanistan, "National Risk and Vulnerability Assessment 2007/08: A profile of Afghanistan" (Kabul: October 2009). There are a number of questions about methodology, however, which argue for caution drawing conclusions. See DFID Afghanistan, "Data Quality Assessment of the National Risk and Vulnerability Assessment (NRVA) Survey 2007/08" (Kabul, December 2010), 9. Moreover, the volatility of agriculture (itself dependent on annual variations in precipitation) can add or remove large numbers of households from below the poverty line.

23 International Labour Organisation (ILO), "Afghanistan: Time to Move to Sustainable Jobs: Study on the State of Employment in Afghanistan" (Samuel Hall Consulting, April 2012), 8.

24 Paula Kantor and Adam Pain, "Poverty in Afghan Policy: Enhancing Solutions through Better Defining the Problem" (Kabul: AREU, November 2010).

to a combination of unfair trading practices by regional nations and the lack of government intervention to mitigate those practices. The role of the market economy and the government's alleged failure to adequately respond is discussed further below. (See also Box 1 above.)

3.3 Prospects for the future

At the national level, the World Bank has constructed six scenarios with varying levels of optimism, which depend on variables such as security, volume and modalities of international aid, sources of growth, and investment climate. Under the most optimistic scenario, which assumes "ambitious" development of mines and improvements in both investment climate and infrastructure, the economy would grow annually at an average of 7 percent from 2010-11 to 2018-19. The scenario considered more likely and which would generate 6 percent annual GDP growth during those years still makes optimistic assumptions about performance of existing mines, improvements in investment climate and agricultural productivity, and the gradual decline in international aid. The four other scenarios estimate annual growth of between just under 5 to less than 1 percent. It is also noted that under certain conditions (i.e. deterioration of security or governance) growth could turn negative. Centrally, the World Bank believes that the threat to growth and economic stability are not directly related to declining aid levels but rather indirectly from potential insecurity. The analysis also notes that with an estimated population growth rate of 2.8 percent, even the more optimistic scenarios will not have much of an effect in reducing poverty. Other analysis has been criticised for being excessively optimistic—fulfilling the political purpose of conveying a sense of progress.²⁵

Minerals

Optimism about the economy is based primarily on hopes for the mineral and trade sectors. The mining and extractive industries sector, with its estimated US\$3 trillion worth of copper, gold, iron, oil and lithium waiting to be exploited, has been touted almost evangelically. According to the ILO, the mining sector is "the most (if not only) promising driver of income growth and industrialization."²⁶ Several major contracts have already been executed, although progress in preparing for excavation has been lagging, in large part due to insecurity.

Much of the analysis contends that without the necessary conditions in place, the sector is not likely to create significant jobs and broad-based wealth, but rather is likely to be made up of a series of isolated enclaves: "If Afghanistan is to have more than a series of mining enclaves, albeit ones generating large amounts of fiscal revenue, it will be necessary to make a very concerted effort to maximize the local or national jobs generated by the industry, particularly with respect to sidestream linkages and infrastructure 'externalities'."²⁷ This positive outcome would require, among other factors, that the Afghan government, donors or the private sector make truly transformative infrastructural investments.

There are a number of additional reasons for caution. First, since the 1970s, internationally there has been a movement to shift the employment benefits of mining in favour of returns to machines and capital, as well as to increased outsourcing of contracts to international companies. This is especially likely to happen in Afghanistan, where there are limited local firms with experience in providing the types of goods and services that are required.

Second, whatever broad-based benefits are derived by communities from the establishment of mines will depend on the extent to which communities, civil society and the government can be proactive in forcing the mining companies to operate in a way that makes benefits widely available. Given the lack of experience with negotiating such agreements and some of the international companies' very limited best practice in socio-economic dimensions of mining operations, this seems like a fairly heroic assumption, especially considering the complexity of the environment and the current state of political economy. The Samuel Hall Consulting/Mercy Corps (SHC/MC) labour market survey suggests that "little government oversight, opaque

²⁵ See Cordesman, "Uncertain Economics of Transition."

²⁶ ILO, "Sustainable Jobs."

²⁷ The World Bank, "The Afghanistan Mining Sector as a Driver of Sustainable Growth: Benefits and Opportunities for Large-Scale Mining" (SEGOM, February 2011), 14.

ownership structures and community mining have ensured that the mines are a long way off becoming a stable source of tax revenue or even that they provide greater benefits, beyond day labour, to the local communities.”²⁸ Other observers note that large-scale operations typically require 7-20 years to become profitable.²⁹

International comparisons as well as Afghan experience suggest that the presence of natural resources can encourage conflict in the form of rent-seeking behaviour and redistributive struggles, which in turn increase socio-political instability. This notion of the “resource curse” is especially of concern given Afghanistan’s weak institutions and that in Afghanistan aid in general (and especially military-related aid) has not been delivered in a conflict-sensitive way. Unfortunately, the conditions needed to mitigate the negative effects include much of what Afghanistan is lacking: good governance, rule of law, effective judiciary system, transparency and accountability, clear and equitable property rights, contract enforcement, egalitarian and democratic rights, social safety nets, and institutionalised representation of minority groups.³⁰ Even if the contracts with the mining companies are well-written and adhere to international norms, it is far from clear that they will be enforced. In fact, there are incentives for everyone to take their cut and cheat.

The difficulties the sector faces have been underlined by recent public discussion concerning the new mining law, which is seen as necessary to attracting foreign investment. Given what is at stake, it is not surprising to see divergent interests and philosophies brought to the surface, and to see the Minister himself attacked by a range of pro-western reformers, former communists, religious personalities and self-interested businessmen.³¹ Concerns are underlined by the accusations of conflict of interest on the part of international consultants who are advising government, yet it is also difficult to distinguish legitimate Afghan concerns about exploitation from the special interests who would be threatened by transparent laws and processes. Discussions about finding a balance between foreigners profiting off Afghanistan’s riches and having international expertise raise issues of globalization as well as some traditional, mercantilist views on the economy.

Trade

Another touted potential driver of the economy and source for job creation is trade. This is based in part on updating Afghanistan’s historical role as crossroads and link between Europe and the Far East (i.e. the Silk Road). The extent to which Afghanistan can create a dynamic trade hub is dependent on numerous variables, starting with security and stability, and continuing with investment in infrastructure and creating effective institutions, but also regional political and economic relations. Critics also question whether the Central Asian States will be sufficiently interested in trading with their regional neighbours, or whether they may be more focused on developing trade with the developed economies.³²

Agriculture

Agriculture is the traditional driver of the Afghan economy due to its importance in livelihoods and food security for so much of the population. Official documents stress the importance of agriculture for Afghanistan’s development, including the “development of prosperous rural and pastoral communities” (ANDS Prioritization and Implementation Plan) and the objective of “achieving sustainable equitable growth” (NPP for National Comprehensive Agriculture Production and Market Development Program), but much independent analysis asserts that this is excessively optimistic and that in fact Afghanistan’s comparative advantage is limited.

28 “Economic Assessment and Labour Market Survey of Mazar-i Sharif, Pul-i Khumri, Kandahar City and Kunduz City” (Report commissioned by Mercy Corps, Samuel Hall Consulting, 2012), 16. See also “Afghan Parliament consults civil society on mining issues” (Integrity Watch Afghanistan: August 2012). <http://www.iwaweb.org/WebsiteMaterial/Newsletter/2012/Newsletter-August-2012.pdf>. Also http://www.iwaweb.org/extractive_industries_monitoring.html.

29 Steven A. Zuck, “The Role of China in Afghanistan’s Economic Development & Reconstruction” (Civil-Military Fusion Centre, March 2012).

30 Omar Joya, “Natural Resources: What Strategy for Afghanistan?” (Samuel Hall Consulting, October 2012).

31 Graham Bowley and Matthew Rosenberg, “Mining Contract Details Disclosed in Afghanistan,” *New York Times*, 14 October 2012.

32 See Cordesman, “Uncertain Economics of Transition” and “New Silk Road growth plan overlooks regional divide,” *Oxford Analytica*, 13 December 2011.

Despite the predominance of the agricultural sector, it has not contributed significantly to post-2001 growth. On the macro level, since 2002-03, the share of GDP from agriculture has declined from 39 to 23 percent, although this reflects in part the skyrocketing of the service sector, and the share would be expected to rise as services decline. Mainly due to the volatility of agriculture because of its reliance on precipitation, in four of the last eight years, agricultural growth has been negative. On a micro level, there is evidence that households that improve their human security often do so by diversifying out of agriculture, either proactively to increase resilience or as a coping mechanism in response to a shock.³³ Regardless of national potential, at a local level potential is highly variable, depending on topography, land quality, water availability and access to markets.

For a variety of reasons, the 2014 Transition may provide an “opportunity” for the illicit part of the agricultural economy. While the tone and intensity of the public discussion on the opium economy has been more subdued in the last several years (perhaps due to perceived success in reductions and a realisation that aggressive eradication might conflict with parts of the counterinsurgency [COIN] agenda such as winning the support of the rural population), Transition introduces an additional set of dynamics. It remains to be seen whether the reductions in cultivation achieved since 2007 (including 17 “poppy-free” provinces) largely through coercion will be sustainable in the longer term. Both the international community and the Afghan government may be preoccupied with other issues (e.g. elections, security), and therefore be less able and willing to apply pressure on local officials and communities, especially where there are shifting political dynamics at the local level and powerholders are trying to either consolidate or obtain control. With a reduction in international spending, powerholders will be looking for other means to maintain patronage and political power. Finally, with a broader contraction in the overall economy and the reduction in the attractiveness of regional migration (i.e. Iran), there will be additional pressure to relax the prohibition on cultivation.³⁴ Additional impetus for increased cultivation may come from higher opium/wheat price ratios brought about by falling wheat prices as well as households’ coping strategies as a consequence of Transition.³⁵ All things considered, it is hard to see any factors which could reduce the extent of opium poppy cultivation, and numerous factors which could increase it.

Development funding

Given Afghanistan’s dependence on external funding both for development and for maintenance of current services, the pledges of the donors at the July 2012 Tokyo Conference were considered a positive sign by most (although not by those who were looking for a ten- rather than four-year commitment). Whether or not the pledges of \$16 billion will be sustained, however, is an on-going question. A number of indicators are worrying, including the apparent lack of agreement or consistency among donors on holding to the Mutual Accountability Framework (MAF). Even during the Tokyo Conference officials noted that “it was up to each donor whether to make its aid contingent on such reforms and that the benchmarks could vary from country to country.”³⁶ With austerity a dominant theme in home-country budgets, it is easy to see how conditions in Afghanistan (corruption, inability to implement projects due to insecurity, violence against donor representatives, human rights abuses, suppression of women’s rights, the perception that Afghans were “ungrateful,” etc.) could be used to justify reductions in development spending. In a sense, the MAF is a sort of conditionality. In recent months, there has been some indication that donors have been seizing on corruption as a justification for cutting back on funding pledges.³⁷ Also, should conditions deteriorate, the need for increased humanitarian funding could compete with development funding.

33 See David Mansfield, “Managing Concurrent and Repeated Risks: Explaining the Reductions in Opium Production in Central Helmand Between 2008 and 2011” (Kabul: AREU, August 2011). Also Paula Kantor and Adam Pain, “Running Out of Options: Tracing Rural Afghan Livelihoods” (Kabul: AREU, January 2011).

34 See William Byrd and David Mansfield, “Drugs in Afghanistan—A Forgotten Issue? Implications and Risks for Transition” (Washington: United States Institute of Peace, May 2012), and David Mansfield and Paul Fishstein, “Eyes Wide Shut: Counter Narcotics in Transition” forthcoming.

35 World Bank, “Afghanistan Economic Update” (October 2012).

36 “Donors offer US\$16 billion Afghan aid at Tokyo conference,” *Reuters*, 8 July 2012. <http://uk.reuters.com/article/2012/07/08/uk-afghanistan-clinton-idUKBRE86602120120708>.

37 “From bad to worse? Afghan aid under the microscope” [https://www.devex.com/en/news/blogs/from-bad-to-worse-afghan-aid-under-the-microscope?mkt_](https://www.devex.com/en/news/blogs/from-bad-to-worse-afghan-aid-under-the-microscope?mkt_tok=3RkMMJWWFF9wsRovv67LZXKXonjHpfsX86u4sWaKg38431UFwdcjKpmjr1YYFT8N0dvyCMRAVFZl5nQhdDOWN)

[tok=3RkMMJWWFF9wsRovv67LZXKXonjHpfsX86u4sWaKg38431UFwdcjKpmjr1YYFT8N0dvyCMRAVFZl5nQhdDOWN](https://www.devex.com/en/news/blogs/from-bad-to-worse-afghan-aid-under-the-microscope?mkt_tok=3RkMMJWWFF9wsRovv67LZXKXonjHpfsX86u4sWaKg38431UFwdcjKpmjr1YYFT8N0dvyCMRAVFZl5nQhdDOWN).

A second question is how much will actually be channelled through the Afghan government—especially if corruption is not seen to be reduced and if relations with the international community become even more frayed due to the dynamics of Transition. The extent of corruption seems very unlikely to be reduced, partly because a time-limited process and a ticking clock reduce incentives to follow procedures, and officials may tend to discount the future in favour of the present.

One interesting but highly controversial prospect is whether donor funding can be given directly to provinces that are seen to be effectively led and managed, while bypassing the Kabul administration. In fact, this is happening in some activities (e.g. the US government's "Good Performers Initiative" for eliminating opium poppy cultivation) and government officials have at times stated that in theory the government is open to such direct funding, and even that it had been attempted in some form but that the donors had not delivered.

Sufficiency of security funding, currently estimated at \$4.1 billion per year, is not discussed here, except to note that western body politics largely don't distinguish between development and military spending, which means that some nations may feel that their contribution to security is sufficient to fulfil their obligations.

3.4 The neighbourhood and regional initiatives

Even more than most countries, Afghanistan's political and economic trajectory will depend in large part on the actions taken by its immediate neighbours, with those decisions influenced in turn by the state of those nations' relations with each other (i.e. India-Pakistan) and with other nations (i.e. Iran-US). While economic theory says that all of the countries in the neighbourhood can gain from regional trade, political dimensions, interest group capture, and in some cases a mercantilist or zero-sum mentality are likely to put limits on what can be achieved in the way of economic cooperation.

China

Due to its proximity, geographical and security concerns and need for natural resources, China is a key player in Afghanistan. Despite China's low political profile, some see China's activities in Afghanistan as part of the larger US-China competition, and that "China is slowly fulfilling its long-term objective of building an energy-based Eurasian security architecture stretching from Turkey in the west to China in the east to reduce US and western influence."³⁸ Most of the current relationship has been based on bilateral trade and investment (mainly in the extractive sector), although China has also provided some development aid to Afghanistan. Based on a 2006 bilateral agreement and a joint trade committee, the countries agreed to suspend customs duties on nearly 300 commonly traded goods, but the balance of trade remains heavily skewed in China's favour: between 2002 and 2009, Afghan exports to China were 1 percent of imports.³⁹ China is likely to be a key player in oil and mineral extraction, and some analysts put China's oil and gas focus in Afghanistan in the larger context of China's regional energy needs. The state-owned firm, Metallurgical Corporation of China, has acquired the rights to the Aynak copper mine in Logar Province under a \$3.4 billion contract, and some of the oil fields in Sar-e Pul and Faryab provinces. Another state-owned company acquired drilling rights in the so-called Amu Darya Basin, with their bid including plans to build a refinery. Although Chinese workers have been attacked in a number of places in Afghanistan, China's lack of military engagement in the country (despite some training of ANSF by the Chinese Ministry of Public Services) makes it more likely to be able to continue on course should the composition of the Afghan government radically change.

Pakistan

Pakistan's role in Afghanistan's economic and political affairs is exceedingly complex, multi-faceted, and, some would say, many-faced. Most of the public discussion relates to Pakistan's

³⁸ Dr Christina Lin, "China's Silk Road Strategy in AfPak: The Shanghai Cooperation Organization" (Berlin: Institute for Strategic, Political, Security and Economic Consultancy, 2011), 1.

³⁹ Zycck, "Role of China."

role in supporting Taliban and other insurgent groups, but increasingly on the economic side, on Pakistan's perceived role in discouraging Afghanistan's growth. Pakistan is Afghanistan's largest trading partner for both imports and exports, with imports outweighing exports by a factor of nearly five in 2011-12.⁴⁰ As the destination for 48 percent of Afghanistan's exports,⁴¹ Pakistan is the country's largest export market. Pakistan is alleged to be negatively intervening in the Afghan economy (as discussed below) through product dumping and restraint of trade. While the Afghanistan-Pakistan Transit Trade Agreement (APTTA) signed in 2010 was hailed as a major step forward to facilitate trade with India, China, and beyond, its full implementation remains stalled, and the transit of Afghan goods through Pakistan remains a major bone of contention, as it has from the establishment of Pakistan in 1947.⁴² As long as Afghan-Pakistani and Indian-Pakistani relations remain problematic, APTTA is unlikely to be fully implemented. While Pakistan development assistance has been low-profile, in Balkh construction has just been completed on the Pakistan-supported Liaqat Ali Khan Engineering Faculty of Balkh University, a major and very visible feature on the landscape on the eastern approach to Mazar.

India

India's support to Afghanistan's economy lies in part in the context of the competition between India and Pakistan. India has undertaken a number of fairly high-profile economic projects, including rehabilitation of the Salma Dam in Herat Province, building the highway from Delaram to Zaranj on the Iranian border, and construction of the electrical distribution line from Uzbekistan to Kabul. Some of these projects can be easily seen in light of competition with Pakistan, especially roads or other infrastructure which potentially reduce reliance on Pakistani ports by shifting access to Iranian ones (i.e. Zaranj lies on the way to the Iranian port of Chabahar). India also hosted the high profile June 2012 investment conference in New Delhi, and the Hajigak mine contract was awarded to an Indian consortium. India has been a historical key trading partner, and in 2003 the two countries signed a preferential trade agreement; India is currently Afghanistan's fifth largest source of imports and the second largest destination for exports, which in 2012 made up 19 percent of exports.⁴³ In recent years India has become somewhat more open and assertive in its support to Afghanistan, and in October 2011 the two countries signed a strategic partnership that includes security, economic and cultural elements. Subsequently an agreement was reached for more cooperation on security matters, including the training of some ANSF personnel in India. India has also had a visible presence through a number of health clinics in the major cities that have linkages with medical institutions in India.

Iran

Similar to India, some of the economic initiatives on the part of Afghanistan's neighbour to the west can be seen in the context of regional and international political competition, including Iran's oft-repeated objection to permanent US military bases. Iran has consistently touted the advantages of the Chabahar port as an alternative to ports in Pakistan. Iranian companies have also made extensive investments in the western city of Herat. These investments have been viewed with much suspicion by Afghans, who see this economic penetration coming at the expense of Afghan enterprises but also having an underlying political purpose. Afghanistan has been a market for Iranian consumer goods, which is especially important to Iran given the isolation imposed by western economic sanctions. Outside of Herat, Iranian products can be found in shops throughout Kabul and Mazar, including in entire stores devoted to Iranian goods. According to official government statistics, Iran is the third largest destination for Afghan exports and the third largest source of imports. Additional issues affecting Iranian-Afghan relations include the trafficking of opiates produced in Afghanistan, and the presence of 2.5 million Afghans in Iran, many of whom are economic migrants without legal documents.

40 CSO.

41 World Bank, "Economic Update" October 2012.

42 In late 2012 about 3,700 shipping containers were stopped in Karachi port. On top of the costs of spoilage of perishable food items and delays in receiving goods, Afghan traders were asked to pay demurrage charges that amounted to US\$50 million during the first three months. See "Afghan Traders Struggling to Pay Karachi Port Demurrage," Tolo News.com, 7 February 2013. <http://tolonews.com/en/business/9358-afghan-traders-struggling-to-pay-karachi-port-demurrage>.

43 Ibid.

Iran has periodically expelled groups of Afghans, acts that have been interpreted as hostile and based on political agendas. As 2014 approaches, Iran has been accused of upping its support to the groups that it supported during the war.

Turkey

Turkey is both an important member of NATO as well as a key regional power in Central Asia. Turkey has significant commercial interests in Afghanistan, especially in greater Balkh, where it also led the Provincial Reconstruction Team (PRT) in Shiberghan to the west. Turkey has been involved in a large number of infrastructure projects, including roads, bridges and schools. It has also supported the education sector, including a series of well-respected Afghan-Turk high schools, and provided medical equipment. Turkey's development activities are implemented through the Turkish International Cooperation and Development Agency, and many Turkish trade and construction companies. On the political side, Turkey has historically supported Uzbek political factions, especially General Abdul Rashid Dostum, but more recently Jawzjan Governor Mohammed Alim Sayee and up and coming Jumbish party reformers. As of early April, Afghanistan and Turkey were preparing to sign a strategic cooperation agreement that would include support to ANSF through equipment and training and economic cooperation.

Central Asian republics and regional initiatives

Although Afghanistan has a combined border of approximately 2,140 km with the Central Asian republics of Tajikistan, Uzbekistan and Turkmenistan, those relationships are affected by suspicion and by protectionist policies of the northern neighbours, sensitive water allocation issues from the rivers that flow from Afghanistan and make up most of the border, and tensions between the republics themselves.

Regional initiatives include the New Silk Road (NSR) and the Central Asia Regional Economic Cooperation (CAREC). The NSR was first articulated in September 2011 by US Secretary of State Hillary Clinton with the stated purpose of contributing to peace and stability in Afghanistan post-2014 through regional economic integration, in particular cushioning the effects of the reduction in international spending in the construction, security and service sectors. The most specific articulation of this US-led and German-backed initiative includes 81 proposed projects totalling \$47.2 billion, most of which would complement the extractive industries. Questions surrounding the initiative include interest in the Central Asian states and the private sector in making project investments; realism of the analysis upon which the projects were formulated; overall cohesion of the individual projects; the role of Iran in this US-led initiative; and, whether there is sufficient stability to implement the projects. While even proponents acknowledge that the initiative is "more of a vision than a strategy,"⁴⁴ sceptics believe it to be less a serious venture than political cover for the international community's exit from Afghanistan.

CAREC, begun in 1996 under the guidance of the Asian Development Bank (ADB), emphasises 1) expanding trade (through operational priorities transport, trade facilitation, trade policy, energy), and 2) improving competitiveness. For Afghanistan, CAREC specifies a master plan for each of three relevant corridors, and foresees the evolution of transport, logistics and economic corridors. CAREC assumes that increased trade within the region would have more benefits than trade with countries outside the region, an assumption that has been questioned.

3.5 Labour market and employment

In one way or another, all analysis confirms that employment is one of the most daunting problems facing Afghanistan. There is disagreement, however, on the exact nature and extent of that problem due to the lack of consistent and reliable data as well as the nature of technical definitions. There are no national data other than the NRVA, and data are not disaggregated by sector. Historical information on labour is also very limited or non-existent, especially for the period after 1978.

44 Andrew Hutchins, "Laying the Groundwork for Afghanistan's New Silk Road: How Washington and Kabul Can Turn a Vision Into a Plan" *Foreign Affairs*, 5 December 2011. <http://www.foreignaffairs.com/articles/136714/andrew-c-kuchins/laying-the-groundwork-for-afghanistans-new-silk-road>.

An ILO study on the need to create sustainable employment identifies the following significant issues:

- Lack of reliable information and data;
- Lack of long-term thinking and programming, due to short donor funding cycles and off-budget or parallel projects;
- Limited provincial or regional focus based on donor interests; lack of coordination among ministries and agencies;
- Lack of linkages with the labour market (too much focus on stabilization and on “direct and visible outputs”); and
- Relatedly, too much focus on creation of casual and short-term jobs.⁴⁵

The study asserts that despite the rhetoric of poverty alleviation and job creation, employment creation has not been given adequate weight in practice and has often been pushed behind the political agenda. The study recommends a “holistic approach” and the “mainstreaming of employment objectives in long-term programming cycles,” especially within the context of the NPPs that focus on job creation. The study recommends both pragmatic market-driven employment and capacity-building policies as well as social dialogue to encourage ownership by employers and workers’ organisations, but some of the more “interventionist” recommendations (e.g. revitalising Employment Service Centres) seem at odds with much of the more laissez faire, free market approaches that have dominated post-2001 policy and practice.

According to the 2007-08 NRVA, national unemployment was 7.9 percent, which considering the technical definition and the nature of employment in Afghanistan, is not a very useful measure.⁴⁶ As noted by the ILO report, “the majority of people simply cannot afford to be unemployed.”⁴⁷ Consistent with the World Bank’s analysis, the ILO stresses that underemployment, which it cites as 48.2 percent on the national level, is actually a much bigger problem and gives a more accurate picture of household welfare. Although it is similarly difficult to measure, underemployment includes most of the 60 percent of the “employed” workforce working in agriculture, which is generally low productivity; in fact, most households construct their livelihoods from a patchwork of sources, and few households with small landholdings can extract livelihoods from their land alone. Other underemployed persons include those working in unskilled jobs for which they are over-qualified (e.g. trained teachers working as guards for NGOs or international agencies because they pay better) and casual, temporary or seasonal workers. ILO classifies more than 90 percent of jobs in Afghanistan as “vulnerable employment.” The government has estimated that of the employment opportunities created from 2001-10, over 90 percent was in the informal sector, and over 75 percent of all non-agricultural employment was in the informal sector. Even in the urban areas, over 60 percent of employment is in the informal sector.⁴⁸

On the supply side, Afghanistan’s population is growing at a rate of 2.6 percent per year, the 19th highest in the world.⁴⁹ With 49 percent of the population under 15 years of age and 68 percent under 25, Afghanistan’s population is the youngest in the world,⁵⁰ which means that there will be high demand for jobs in the future. The ILO refers to the 400,000 persons added to the labour force each year as a “socio-economic time bomb.”⁵¹ Moreover, many of the recent graduates have internalised the heightened expectations of the post-2001 generation.

45 ILO, “Sustainable Jobs.”

46 According to the NRVA, a person aged 16+ was employed if during the reference period he/she had either paid employment or was self-employed for at least one hour per week. [Emphasis added.] As noted by a review of the NRVA, because of the lack of standard definition, the importance of underemployment rather than unemployment, and the lack of quantification of employment availability, “unemployment estimates are thus not meaningful, regardless of their reliability as a measure of what they claim to be measuring.” DFID, December 2010, 7.

47 ILO, “Sustainable Jobs,” 6.

48 Government of the Islamic Republic of Afghanistan, “Sustainable Decent Work Through Skills Development and Employment Policies for Job-Rich Growth,” National Priority Programmes, Human Resource Development Cluster, Final Draft for Endorsement. (Kabul, June 2012).

49 World Bank, 2009.

50 SHC/MC, 2012, 54.

51 ILO, “Sustainable Jobs,” 10.

Even before 2001, a combination of population growth, focus on industrial development, dislocations due to the war, and periodic drought had pushed Afghanistan's labour force increasingly towards non-agricultural activities—even if employment has not actually been available. According to one estimate, between 1966 and 1982, the number of persons engaged in industry approximately doubled, although agricultural workers still exceeded industrial ones by a six to one ratio.⁵²

Regional migration has historically been a safety valve for the unemployed and a source of sustenance for households who received remittances, even before the years of conflict. The Middle East oil boom of the 1970s was the high-water mark for migration; large numbers of Afghans, both skilled and unskilled, transmitted a significant volume of remittances from Iran and the Gulf using traditional *hawala* networks. Although exact numbers of migrants are unknown, estimates for the late 1970s ranged between 250,000 to 700,000 (2-4 percent of the population at that time), with remittances reaching as much as \$20 million per month.⁵³ In the years after the 1979 Soviet invasion, up to 6.22 million Afghans fled to Pakistan, Iran and elsewhere. Many built upon pre-established migratory networks in order to maintain livelihoods, or else established new networks. During the ensuing years, migration was motivated by a mix of economic, political and social factors. Despite the repatriation of more than 5.7 million Afghans following the fall of the Taliban in 2001, migration remains a key livelihood strategy for many.⁵⁴ Although Afghanistan is one of the countries that does not report remittance inflows to the IMF, according to one estimate, Afghan labour migrants in Iran alone were remitting approximately \$500 million annually, which was equivalent to 6 percent of national GDP. According to the World Bank, movement of workers between Afghanistan and Iran makes up the world's eighth largest migration corridor (excluding the former USSR).⁵⁵

As noted above, the employment situation is likely to worsen post-2014 because a number of the international community-funded activities which will be reduced (e.g. services, construction) are relatively labour-intensive. The projection is that this will have more of an effect on underemployment than on employment and that this will be especially pronounced in the insecure provinces that have received the bulk of aid. Also as noted above, the World Bank projects that because the domestic economic content of aid has been so low, the negative employment effects will be limited.

At the same time, there has been no clear picture of the effects of aid projects on employment, other than counting numbers who have been employed, regardless of duration. In one of the only rigorous studies, Peace Dividend Trust estimates that during 2010, 6.5-10 percent of the working population benefited from aid-related employment, although acknowledging the unavoidable problems with data (i.e. data are inconsistent, scattered, with various definitions, double-counting, and focused on easily measured metrics such as "jobs created" or "people employed" which convey no information on the length of employment).⁵⁶

In the relatively labour-intensive construction sector, companies have often imported workers from elsewhere in the region, in part because of the higher skills of foreign (i.e. Pakistani) workers, but also because foreign workers are considered cheaper because they demand less and as migrants they are not so distracted by family life. It is interesting to note the symmetry of regional migration: while other South Asian groups come to Afghanistan for job opportunities and higher wages, Afghans migrate to Iran for the same reasons, as well as to acquire new skills. It is also interesting to note, of course, that Afghans who migrate to Iran for job opportunities and higher wages are often preferred by Iranian employers for some of the same reasons that foreign workers are preferred in Afghanistan.

52 Nyrop and Seekins, "Afghanistan Country Study," 172. The picture is made more cloudy by the fact that due to the episodic and seasonal nature of agricultural work, industrial employment included off-season agricultural workers.

53 Nyrop and Seekins, "Afghanistan Country Study," 173.

54 For more on the complex factors which affect migration of Afghans, see Alessandro Monsutti, in collaboration with Mohammad Jalal Abbasi-Shavazi et al, "Afghanistan transnational networks: looking beyond repatriation" (Kabul: AREU, August 2006).

55 World Bank, "Migration and Remittances: Factbook 2011" (2nd Edition, 2011). As the other corridors with larger numbers include Mexico-US, China-Hong Kong, and China-US, on a per-capita basis, Afghan migration is much more significant.

56 Peace Dividend Trust, "Spending the Development Dollar Twice: The Local Economic Impact of Procurement in Afghanistan" (Kabul, July 2009).

Vocational training and employment generation programmes

Partly due to years of conflict, Afghanistan remains short on workers with technical skills. While this is generally (although not universally) regarded as a constraint to higher productivity, improved standard of living, and development,⁵⁷ there is no clear consensus on what the shortcomings of the last ten years have been or on what should be done in the future. As the ILO points out, most technical skills are learned on the job through informal “apprenticeships,” for lack of a better word. The ILO also points out the poor links between all work-related programmes, including training: “Government TVET [Technical and Vocational Education and Training] initiatives, as well as international and non-governmental organisations, tend to exclusively focus on direct and visible outputs (e.g. participation in training), without taking into account longer-term employment outcomes.”⁵⁸

Critics have claimed that if there had been TVET for the building trades (electricians, plumbers, carpenters) starting in 2002, there would not be the shortage of such trades that existed during the construction boom, and therefore less reliance on foreign workers. Given some of the reasons for the apparent preference for Pakistani workers, however, it is not clear how much of a difference this would have made.

In such a competitive job environment, a recurrent complaint from job seekers at all levels is that jobs are allocated through personal connections or *wasita*. Numerous studies have confirmed the preference of employers to rely on informal networks, usually immediate family or relatives. While this may be a natural preference, it also reinforces a lack of confidence in institutions such as schools. According to the ILO study, given the reliance on family and personal networks, “diplomas have no practical value on the labour market.”⁵⁹

As a separate but important issue, child labour is widespread in Afghanistan. UNICEF estimates that 30 percent of children are working, while the NRVA calculates a total number of at least 1.42 million children. The legal requirement that workers be at least 15 years old is not enforced, largely due to economic necessity and, perhaps related, the lack of widespread social stigma. The concentration in some sectors is notable; for instance, the ILO claims that more than half of those working in the brick kilns are less than 18 years of age.

3.6 Afghan government policies and programmes on employment

National Priority Programmes

The Afghan government’s current overarching strategy for development is the ANDS, released in 2008 and then reformulated into the 22 NPPs under six clusters in response to criticism that the ANDS was unfocused.⁶⁰ Despite the labelling of the government’s strategy as “pro-poor,” some observers have noted the absence of strategies within the ANDS NPPs that focus specifically on the poor.⁶¹ While employment is implicitly covered by all 22 NPPs, the two NPPs that deal most explicitly with employment are the NPP for “integrated trade and small and medium enterprise [SME] support facility,” and the NPP for “sustainable decent work through skills development and employment policies for job-rich growth.”

The skills development NPP focuses on the supply side of the labour issue—addressing the “skills gap between labour supply and market demand” through three components: employment policies and labour market information systems; occupational literacy in technical and vocational education; and improved quality and increased access to technical and vocational

57 Interestingly, in a recent series of labour market surveys, employers did not place job skills near the top of given constraints to expansion. See “Labour Market Survey,” 2012. This may simply mean that other constraints—power, rule of law, access to markets—feel more overwhelming.

58 ILO, “Sustainable Jobs,” 7.

59 Ibid, 32.

60 Government of Islamic Republic of Afghanistan, “ANDS: Prioritization and Implementation Plan, 2010-2013” (Kabul, 2010).

61 Paula Kantor and Adam Pain, et al. “Delivering on Poverty Reduction: Focusing ANDS Implementation on Pro-Poor Outcomes” (Kabul: AREU, January 2009).

education and training. While stressing the need to respond to market-demand for skills, it also states that “given that economic growth will not automatically bring decent and productive employment for all, ensuring policy coherence across the NPPs to maximize employment outcomes should be a common priority.”⁶²

The NPP for SME development focuses on building the private sector. The goal of the NPP is “legal, institutional and structural reform to strengthen the enabling environment for private sector” and has three components: facilitating trade and increasing export opportunities; developing resilient and competitive SME and industrial sectors, including through creation of National Quality Infrastructure; and reforming the public institutions charged with assisting the development of the private sector.⁶³ While focusing on improving “export productivity,” as noted above, the NPP bows in the direction of “a socially responsible market economy in Afghanistan.” Despite the supposed focus on jobs and employment, the few direct references to “jobs” and “employment” are in the background and descriptive text sections, and are mentioned as general outcomes, with no specific focus or language.

⁶² NPP for Facilitation of Sustainable Decent Work Through Skills Development & Market-Friendly Labor Regulation, 17.

⁶³ NPP for Integrated Trade and SME Support Facility, 5.

4. Balkh Province⁶⁴

Balkh Province is significant because of its position as a regional political and economic node, its location as a trading hub and gateway to Central Asia, and because it has been considered a success story due to relative security, effective administration, and suppression of opium poppy cultivation (“poppy-free” since 2007). The narrative of this success is tied closely to Governor Atta Mohammad Noor, who is seen either as an effective leader or clever warlord, depending on one’s perspective. He is often held up as a positive example of “strongman governance.”⁶⁵

With the exception of a few pockets of instability in Char Bolak, Chimtal, Dawlatabad, and Sholgara, which were classified by the International Security Assistance Force (ISAF) as “key terrain districts” in 2009, the province has largely remained peaceful, and has therefore provided a permissive environment for development and economic activity. In 2008, Balkh was the province with the sixth least reported number of attacks by armed opposition groups. Some observers say that the situation changed in 2008 and 2009,⁶⁶ although some of the violence was factional rather than insurgent-related; a number of security incidents west of Mazar were interpreted as being related to the presidential elections, in which Governor Atta supported Dr Abdullah against President Karzai. According to the International NGO Safety Office-Afghanistan, total incidents in the province increased by nearly half in 2010 and again by 13 percent in 2011, then decreased by nearly one-quarter in 2012. As of the halfway point in 2013, incidents to date are roughly one-third higher than half of the total for 2012.⁶⁷ The most notable incident was the April 2011 high-profile attack on the UNAMA office in which seven UN personnel were killed. On the other hand, the deployment of Afghan Local Police (ALP) in Balkh, Char Bolak and Chimtal districts during 2012 is seen to have led to an improvement in security, at least in the short-term.

4.1 Basic information: geography, population, and social indicators

Due largely to its strategic location bordering Uzbekistan and Tajikistan, Balkh Province has historically functioned as the political and economic capital of northern Afghanistan, a designation which has at times been a formal one. (At various times in history, the official designation has been “Mazar-e Sharif Province.”) With a population of 1.2 million, Balkh is Afghanistan’s fourth most populous province. Administratively, Balkh is divided into 14 *woleswalis* (districts).

According to the CSO, just over one-third of the province’s population lives in urban areas, of which the vast majority (82 percent) live in Mazar.⁶⁸ Balkh is ethnically heterogeneous, with Tajiks making up the largest group, followed by Pashtuns, Uzbeks, Hazaras, Turkmen and Arabs.⁶⁹ As elsewhere in Afghanistan, with the partial exception of the urban areas, settlements tend to be organised along ethnic lines.

Even during the years of open conflict, the provincial centre Mazar was relatively stable, and has continued to draw population into the city. It is currently the fourth largest city in Afghanistan, with an estimated population of 357,000, nearly three times the 1988 estimate. Mazar’s central landmark, the Shrine of Hazrat Ali (known as the *Rowza-e Sharif*), is one of

64 Provincial background on Balkh draws on Paul Fishstein, “Winning Hearts and Minds? Examining the Relationship between Aid and Security in Balkh Province” (Boston: Feinstein International Center/Tufts University, January 2011), which was informed by material prepared by Mervyn Patterson.

65 See Dipali Mukhopadhyay, “Warlords as Bureaucrats: The Afghan Experience” (Washington, DC: Carnegie Endowment for International Peace, August 2009).

66 Antonio Giustozzi and Christoph Reuter, “The Insurgents of the Afghan North,” (Afghanistan Analysts Network, April 2011).

67 Source: International NGO Safety Office-Afghanistan. Includes incidents initiated by armed opposition groups, ANSF, international military forces, and armed criminal groups.

68 Central Statistics Organization, “Population Estimation 2011-12” Accessed 26 October 2012 at <http://cso.gov.af/en/page/6070>.

69 “Arab” refers to groups who claim descent from the Arabs who brought Islam to Afghanistan starting in the seventh century. They have been assimilated, and speak Dari and/or, in parts of the north, Uzbeki. They do not speak Arabic.

the main reasons for Mazar's consolidation as a centre for tourism and religious pilgrimage. Additional significant towns are Balkh, Dehdadi, and the key border town of Hairatan.

Balkh's social indicators are mixed. The population has somewhat better access to schools than in other provinces, and the overall literacy rate of 44 percent (male 54 percent, female 32 percent) is slightly above the national rate of 28 percent (male 38 percent, female 19 percent).⁷⁰ In the delivery of primary health services, in 2011-12 Balkh ranked third of 33 assessed provinces, scoring above the national average.⁷¹ As elsewhere in Afghanistan, medical facilities are concentrated in the cities, especially Mazar, which has seen a proliferation of private sector hospitals and other health facilities. In 2007, the CSO and United Nations Population Fund (UNFPA) ranked Balkh ninth highest of 34 provinces on a compilation of indicators intended to represent social and economic well-being.⁷² While the provincial unemployment rate is above the national average, the under-employment rate is below, which conveys a conflicting characterisation of the labour market and perhaps the difficulty of measuring unemployment in Afghanistan. According to the 2007-08 NRVA, the incidence of poverty in Balkh and its depth is more severe than the national average, and worse than the majority of provinces (see Table 1). In looking at the ranking of provinces, for all three indicators that describe poverty, Balkh's ranking is in the bottom fifth. In addition, Balkh's gender-related and nutrition indicators are worse than the national average.⁷³ As discussed above and further below, strong caveats are in order when drawing conclusions about poverty or employment indicators.

Table 1: NRVA provincial-level indicators on poverty for Balkh

	Poverty rate (and rank)	Poverty depth (and rank)	Gini coefficient for consumption (and rank)
Balkh	60.3% (28)	17.4% (31)	0.27 (29)
National	35.8%	7.9%	0.29

Source: World Bank, Islamic Republic of Afghanistan. "Afghanistan: Provincial Briefs" (Kabul, June 2011).

In terms of infrastructure, Balkh is more advanced than the other provincial centres in the north, with one public and several private universities, technical training centres, a civilian airport and foreign consulates. Mazar is the location of regional commands for the Afghanistan National Army (ANA), Afghanistan National Police (ANP), and ISAF, as well as the United Nations (UN). The massive ISAF base at Camp Marmal/Mazar airport has supported the PRTs and other bases across the northern part of the country, and is now the focal point for the consolidation and withdrawal of international military forces across the north. There are currently more than 5,000 military personnel from Germany, the US, and 15 other NATO nations and Mongolia.

Most of Balkh's electricity comes from Turkmenistan or Uzbekistan. Outside of the main cities and towns of Mazar, Dehdadi, Hairatan, Balkh and Khulm, there are limited electrical connections. Diesel, micro-hydro, and solar power installations have been put in under the National Solidarity Programme (NSP) to cover less than 10 percent of the villages of Balkh, although some of these, especially diesel, have been found to be unsustainable. There has been on-going desire for the construction of hydro-power and irrigation fixtures on the Amu Darya and Sholgara River. The rehabilitation of the Shiberghan-Mazar gas pipeline is now

70 Central Statistics Organization and UNFPA, "Balkh: A Socio-Economic and Demographic Profile, 2004."

71 The Ministry of Public Health assesses delivery of the Basic Package of Health Services, the standardised package of primary health services made available to all citizens. See "Afghanistan Basic Package of Health Services: Balanced Scorecard National Report 2011-12" (Johns Hopkins University Bloomberg School of Public Health and Indian Institute of Health Management Research, 2012). Balkh's absolute score remained roughly the same as the previous year, but due to a sharp fall in scores of other provinces, its rank increased from 19th to third.

72 Indicators included geographic accessibility, access to social and cultural services (i.e. health, education, media), markets and economic activities. See Central Statistics Organization and UNFPA, "A Socio-Economic and Demographic Profile" (2007).

73 World Bank and Islamic Republic of Afghanistan, "Afghanistan: Provincial Briefs" (Kabul, June 2011). As the indicators are derived from the NRVA, the caveats mentioned above should be kept in mind.

under process under funding and direction from the US Department of Defense's Task Force Business Stability Operations (TFBSO), with the intention to bring gas to Mazar by summer 2013.

The prospect of Transition has created a set of dynamics that is both new but at the same time is based on recent and more distant history. Starting in 2009, the US put extensive effort and money into transforming the government-owned Mazar Hotel into a consulate, but abandoned the plan in 2012 because of security concerns.⁷⁴ The German government has now taken over the building as a diplomatic facility. It appears that the Swedish/Finnish Transition Support Team (TST, formerly PRT) will remain in place until summer 2014, with some reduction in military presence. The TST had been tentatively scheduled for an earlier closing, and discussions had been held about the possibility for the US to take over the TST facility for use as a consulate rather than their current location in Camp Marmal. Mazar was included under the first tranche of the security transition in July 2011, with the rest of Balkh Province following in the second tranche in late November of the same year.

4.2 Brief recent historical overview

While Balkh has thrived since 2001, and especially since 2004, some of the basis of that success as well as some of the underlying fault lines that could threaten it can be found in history, especially the recent decades.

During the *jihad* period (1979-92), Balkh could be characterised as politically heterogeneous. While all of the major Pakistan- and Iran-based *mujihadin* parties were present in the province, there was significant support in the cities for the leftist Khalq and Parcham parties, as well as for the more minor ones such as Shula-e Jawed and Setam-e Milli. The more leftist orientation, especially in Mazar, was due to the proximity of the Soviet Union and the presence of Soviet-built industrial establishments, which represented a modernising influence for much of the population.

The fall of the Najibullah government in 1992 was set in motion when a senior group of army officers, including General Dostum in Jawzjan, revolted and linked up with *mujihadin* groups.⁷⁵ While Mazar avoided the destructive violence between ostensible government partners that was destroying Kabul, the *mujihadin* groups, despite forming a multi-factional administration, continued to squabble over the distribution of appointments, patronage, and the material assets of the fallen government. While the parties were nominally allied with the political leaders in Kabul, relationships were unstable, and alliances were constantly made and broken as powerholders pursued their own interests.

Even after the emergence of the Taliban and their capture of Kandahar in 1994 and Kabul in 1996, Balkh remained relatively stable under the administration of Jumbish-e Milli led by General Dostum. The price of the stability, however, was abuse of the population at the hands of commanders who were given free rein to predate on the population.

The inevitably unstable status quo broke down in May 1997 when a re-alignment of commanders allowed Taliban groups to enter and capture Mazar city. The Taliban were expelled by local forces in September, but recaptured the city in August 1998. During this period the population experienced a number of cycles of street fighting and killings largely along ethnic, sectarian or factional lines, exacerbated by constantly shifting alliances and the arrival of outsiders. At this point, many senior commanders either fled the country or aligned themselves with the Taliban.

Taliban control held until November 2001, when local commanders (including those who had aligned with the Taliban) joined up with US forces to expel the Taliban from Mazar and

74 Ernesto Londoño, "U.S. abandons consulate site in Afghanistan, citing security risks," *Washington Post*, 5 May 2012. http://www.washingtonpost.com/world/asia_pacific/citing-security-us-abandons-consulate-site-in-afghanistan/2012/05/05/gIQA9ZkD4T_story.html

75 It is worth noting that the government forces commanded by these officers had originally been militias or local "self-defense forces" which, as part of Najibullah's security strategy, had been supported and incorporated into the official forces.

take control of the city. For the next three years, the main source of instability was the on-going conflict between Atta Mohammad Noor and General Dostum, backed by their respective political parties, Jamiat and Jumbish. During this period Mazar itself was relatively stable, but the rural areas experienced on-going conflict due to competition and shifting alliances. In the fall of 2003, in response to Jamiat-Jumbish confrontations in a number of areas of the north, Kabul and ISAF intervened by imposing a ceasefire and demanding the cantonment of heavy weapons.

With the demilitarisation of the three major political parties (Jamiat, Jumbish, and Hezb-e Wahdat led by Mohamad Mohaqeq) and the demobilisation of their senior commanders and disarmament of some of their forces, along with the appointment of Atta as governor in July 2004, Balkh Province entered its most stable period since 1978. The recent history of the province is often told as closely linked with the dominance of Governor Atta. While the underlying ethnic and political fissures remain, Atta has kept the province under close control. The core element of his strategy has been to “officialise” control over the province by ensuring the appointment at provincial and district levels of police and civil service officials who are in one way or another beholden to him. As one observer somewhat critically put it, “having transplanted his militia clients into powerful positions through the provincial administration, he maintains a monopoly over violence as well as control over illicit activity.”⁷⁶ The police and other security organs have remained under Jamiat control, although the behaviour of the police was maintained at a relatively benign level. Atta’s strategy has also been characterised as “dual track,” involving loyalty to Kabul and the concept of central government on the one hand, while maintaining local control and influence on the other. Atta has also established his bona fides as a “model governor” with the international community by suppressing opium poppy cultivation, despite lingering accusations that he and his colleagues had been involved in the trade, and successfully projected the aura of an efficient administration, which has garnered praise as well as additional funding of civil service positions.⁷⁷

Despite the periodic rumours that Governor Atta would be replaced, especially during the 2009 presidential elections when he voiced very public support for opposition candidate Dr Abdullah, he has so far remained in place. Most people assume that Karzai would be reluctant to remove a senior governor credited with bringing stability to his province, and risk the potential destabilization of one of the more secure areas of the country. However, it is not hard to imagine that approaching 2014, with both the security transition and presidential elections, could generate political pressures to replace the sometimes-maverick Atta with someone more reliably and firmly in the Karzai camp. At the same time, Atta himself could initiate change by making a move towards playing a more national role (i.e. as candidate for vice president).

Despite the end of overt conflict and the start of an era of stability in 2004, many of the underlying drivers of insecurity remain unresolved and could re-emerge at times of stress. The current political and security situation continues to be influenced by the above factors as well as by the legacy of the years of fighting, and many of these produced outbreaks of conflict through the 1990s and into the post-2001 period. One needs to look no further than the current physical and ethnic geography of insecurity (and in turn opium poppy cultivation) to see how these historical factors continue to inform the present.

4.3 The business-political nexus in Balkh

The Jamiat-centred political elite has derived significant benefits from the post-2004 stability, and provides an important part of the current economic and political context. In the business-friendly environment of Mazar, there is even stronger overlap than elsewhere between the business community, parliamentarians and provincial council members, as well as between businessmen and strongmen—with these distinctions often being meaningless. Governor Atta maintains a close relationship with the members of the provincial council

⁷⁶ Mukhopadhyay, “Warlords as Bureaucrats.”

⁷⁷ According to the Performance Based Governance Fund, the Balkh provincial administration has been in the average performer category; in 2011, the first year of evaluation, Balkh ranked 22nd, improving to 11th in 2012. See <http://www.pbgf.gov.af/evaluations.html>.

and *wolesi jirga*. According to some observers, seven of the 11 member Balkh delegation were from Jamiat with close links to Atta and 15 out of 19 provincial council members were affiliated with Atta.⁷⁸ Some have noted that the private sector has benefited greatly from public-private partnerships with the provincial administration, especially in the construction of public infrastructure, most visibly the highly ornamented roundabouts for which Mazar is well-known, which were built “voluntarily” by the leading business figures.

Atta’s symbiotic relationships with important businessmen such as Kamal Nabizada, Kamgar, Khalid Amiri, and Alam Khan Azadi run deeply and extensively. There are amicable relations even with those who are not quite so closely aligned, such as the Ghazanfar family, who have a complex of major and minor industries including fuel import and distribution and a bank, and an alliance of Hazara businessmen led by Ahmad Shah Ramazan.⁷⁹ Atta and his associates are connected with numerous projects and commercial ventures through a complex and opaque web of companies; the most visible venture is the enormous Khalid bin Walid land development (discussed below). Other major known involvements include the wide-ranging Khaled Noor Company, the Uhm-al Balad Noor construction company, and other enterprises.⁸⁰ As with government appointments in the province, all paths for commercial projects are said to eventually lead to the governor’s office, although extensive indirect ownership of economic ventures makes attributing influence difficult. There appears to be very little of the violent competition between contractors that has been observed in other provinces.

While it is still rare in Mazar to hear direct criticism of the governor, one does hear more private and indirect comments about “government officials” than was the case several years ago. This may be the result of discomfort with a clique that is seen as being too powerful, or it may be a case of rising expectations; it is plausible that several years ago most of the population was relieved enough to be living in a secure environment that they brushed aside the large inequalities which pervaded the system, whereas now they have come to be a source of irritation. It is also plausible that there is an increasing sense of “class consciousness”: a growing anger that the “haves” had already moved their cash and families to Dubai, while the “have-nots” would have to face whatever instability occurs after 2014. Those in areas of the province farther away from Mazar do not feel that they have derived the same dividends.

4.4 Development assistance and the international presence: quantity and quality

The geographical distribution of reconstruction funds since 2001 has been an on-going issue, raised both by the central government as an ostensible matter of principle and pointedly by provincial officials in Balkh. Officials, starting with Governor Atta, have argued that Balkh has incurred a “peace penalty” due to the lack of a major insurgency and (since 2007) opium poppy cultivation. Rather, development funding was seen to have followed the conflict to the south and southeast.⁸¹ Many make both the equity argument that the funding should have been more evenly distributed around the country and the pragmatic one that development resources would have generated a better return had they been invested in more peaceful areas. In particular, the failure to adequately exploit the natural resources of the north is seen as a major missed opportunity. Because of the Swedish government policy of putting money through government and multi-lateral channels based on Paris Agreement principles, the Swedish/Finnish PRT had especially been brought under public pressure by provincial officials, who complained that other PRTs had far more extensive resources to deliver locally while the Mazar PRT had empty hands. For instance, in 2009, Governor Atta noted publically

78 Antonio Giustozzi, 2012. Because elections in Afghanistan are competed on a non-party basis, party affiliations are mostly considered to be informal rather than official.

79 Ahmad Shah Ramazan is the brother of Ashraf Ramazan, a popular and aspiring politician who was murdered in 2005, most likely by potential rivals.

80 See Mukhopadhyay, forthcoming, and Giustozzi 2013, for discussion of other business interests.

81 There is an objective basis to this complaint. In 2009-10, 77 percent of USAID’s resources were allocated to the insecure areas of the south, southwest and east. The percentage was expected to rise to 81 percent the following fiscal year. Source: Majority Staff, Committee on Foreign Relations, United States Senate, “Evaluating U.S. Foreign Assistance to Afghanistan” (Washington, DC, 8 June 2011), <http://www.gpoaccess.gov/congress/index.html>. For a more extensive discussion of this issue, see Fishstein, “Winning Hearts and Minds.” Officials in Balkh are fond of citing the factoid that were Helmand a country it would be the third largest recipient of US assistance.

that the Jalalabad PRT had \$89 million for Nangarhar Province, while the Mazar PRT had \$495,000 for Balkh, Jawzjan, Samangan and Sar-e Pol provinces. (This does not include civilian aid or aid disbursed through other channels, which is somewhat less unbalanced, although still skewed toward the conflict areas.)

Given the complexity of funding sources and the lack of transparency, it is notoriously difficult to come up with estimates of funding allocated to or reaching certain areas, but keeping in mind a number of serious caveats,⁸² Balkh Province is estimated to have received the tenth-most of any province between 2002-10 and eighth-most in 2011 (Table 2). On a per-capita basis, however, Balkh is ranked 25th for 2002-10 and 12th for 2011, the latter perhaps reflecting recent investments. As these figures do not include military-related aid, the actual amounts of resources flowing into the provinces are even more skewed away from Balkh.

Table 2: Provincial distribution of external assistance in 2002-10 and 2011, Balkh and selected provinces, total and per-capita (p/c)

Province	2002-10		2011		pop million	2002-10		2011	
	US\$ m	%	US\$ m	%		p/c aid, USD	p/c rank	p/c aid, USD	p/c rank
Multiple	42,613	36.03%	11,500	88.94%					
Kabul	2,808	2.37%	252	1.95%	3.95	710	14	63	7
Helmand	1,409	1.19%	171	1.33%	0.88	1,602	1	195	1
Kandahar	1,131	0.96%	181	1.40%	1.15	983	8	157	3
Nangarhar	1,051	0.89%	69	0.54%	1.44	731	13	48	8
Herat	629	0.53%	40	0.32%	1.78	353	23	23	14
Kunar	494	0.42%	35	0.28%	0.43	1,152	5	83	6
Ghazni	471	0.40%	37	0.29%	1.17	403	20	31	13
Paktika	432	0.37%	22	0.18%	0.41	1,044	7	55	17
Paktya	420	0.36%	54	0.42%	0.53	800	11	104	5
Balkh	411	0.35%	43	0.34%	1.25	330	25	34	12
Uruzgan	357	0.30%	60	0.46%	0.33	1,073	6	180	2
Total other	4,607		460						
TOTAL	56,838		12,930						

Source: 2002-10: DCR 2010, 102; 2011: DCR 2012, 52; population estimates from CSO.

On the quality side, expressed perceptions of aid projects in Balkh are similar to those elsewhere in Afghanistan, with complaints about inequitable distribution, corruption, ineffectiveness, and lack of relevance to Afghanistan's fundamental problems, which were seen as primarily economic ones. (See Box 2.) More positively, other analysis has concluded that an indirect positive outcome of aid has been a general rise in productivity due to improved infrastructure and human capital, and that this effect has been more significant than the negative ones of price effects and overvaluation of the exchange rate.⁸³

⁸² After 12 years, the geographical and sectoral distribution of aid remains murky, especially for military-related spending. For instance, according to the 2012 Development Cooperation Report (DCR), of the US\$13 billion of ODA disbursed during 1390 (2011-12), only 10 percent can be assigned on a provincial basis. While instruments such as the Donor Assistance Database, Donor Financial Review, and Development Cooperation Dialogues have attempted to track aid flows, with approximately 50 bilateral donors (many with multiple institutions), inconsistent data definitions, budgeting complexity, and lack of transparency and willingness to share information, this objective has not been achieved.

⁸³ See Nicholas Lea, Joost Gorter and Juergen Ehrke. "Constraints to Growth in Northeastern Afghanistan. A Regional Growth Diagnostic. Balkh, Kunduz, Takhar and Badakhshan" (Kabul: GIZ, 2011).

Box 2: Views on the quality of aid projects¹

The main complaints about development projects were typically that aid was inequitably distributed due to the allocation of resources based on *wasita* or other forms of self-interest; riddled with corruption; low quality due in part to elite capture and corruption, but also to implementers' lack of knowledge of local conditions and needs and the inability of complex, bureaucratic, and often isolated institutions to deliver; and, most important, composed of the wrong type of projects, which tended to be non-sustainable stop-gap or even dependency-creating, and failed to address any of Afghanistan's fundamental long-term development needs.

Desirable projects were "economic" ones which created jobs through the construction of factories and major physical infrastructure, rather than community-oriented, "small is beautiful" projects. Respondents wryly pointed out that there was a limit to the number of poultry projects that could be implemented. There was a general lament about the lack of the types of large projects that the US and Soviets used to implement. In the north, two specific areas of complaint were the lack of investment in the development of the region's natural resources (natural gas, sulphur) and the lack of interest in rehabilitating Afghanistan's pre-war industrial infrastructure. Another on-going grievance was the lack of a major irrigation work on the Amu Darya, although there are technical disagreements on the actual potential for such a project.

Aid was mostly said to have induced no fundamental, positive economic change. On the contrary, respondents complained about aid dependency. For example:

We've become accustomed to aid. In the past when a canal in front of someone's house was blocked, people would come together to unblock it. Now, we'll wait for some NGO to come by with a food-for-work project.²

Afghan staff of counterpart agencies expressed even more frustration and less interest in what development projects have to offer; "capacity building" workshops, which had come in for the bulk of criticism several years ago, were currently seen to be even farther away from Afghanistan's essential needs. As one senior official noted:

We don't want so many workshops. They are also very expensive. We could also do ten years of workshops with what it costs them to do one. People go to them for the food and the free airfare to Kabul. The senior people won't go unless they need to go to Kabul at the same time and can get a free flight. Otherwise, they just send the junior staff.³

Of the 12 business development services companies developed by a large project focusing on SME development, only 1-2 appear to have survived.

There have also been complaints about the lack of continuity in programming and about the employment of different, competing strategies between projects funded by the same donor. For example, while US Agency for International Development's (USAID) IDEA-NEW project has stressed building markets, the Afghanistan Vouchers for Increased Production in Agriculture (AVIPA) project contracted with seed producers to purchase their seeds at a higher price and outside of market channels, which disrupted the seed market.⁴ Also, in USAID-funded projects in the agricultural sector, there had been vacillation between emphasising production on the one hand and creating infrastructure (i.e. markets, institutions, roads, storage) on the other hand. This was sometimes the case even within one project, as the focus changed when personnel changed in Kabul (or perhaps Washington).

1 For additional information, see Fishstein and Wilder, "Winning Hearts and Minds?" Also International Crisis Group, "Aid and Conflict in Afghanistan" (Asia Report N°210, 4 August 2011).

2 Interview with Afghan staff member of development project.

3 Interview with senior official of Afghan private sector institution, Mazar, September 2012.

4 Interview with international agricultural development workers, Mazar, December 2010.

5. Balkh's Economy

Balkh Province, especially the provincial centre Mazar-e Sharif, has thrived since the fall of the Taliban, and is often counted as a post-2001 success story with respect to security and economic development in general. The following sections provide an overview of the economy, including the contributions of significant sectors.

5.1 Balkh's economy before 2001

Due to its location on the border with the former Soviet Union, prior to 1978 Balkh was the site for a number of important industrial developments built or supported by the Soviets, including the Kod-e Barq industrial plant, Balkh Textiles, Balkh Cotton and Vegetable Oil, and the Mazar Silo. Most have become degraded or inactive due to a combination of conflict and neglect.

Balkh also benefited from two of Afghanistan's significant internationally traded commodities, *qarakul* pelts and cotton. Some of these commodities, along with gas from the Shiberghan fields, which in 1982 contributed 44 percent of government revenues, went to the USSR on a barter-trade basis negotiated annually.⁸⁴ While the government emphasised large industrial projects, small-scale private industry, including handicrafts, made a larger contribution to both domestic production and exports. In the agriculture sector, the PDPA government stressed the development of cooperatives and large, state-owned mechanised farms more or less along Soviet lines. While some of these initiatives did not get very far (e.g. state-owned industrial farms), the legacy of the cooperatives remains.

Although the province was not subject to the type of fighting that took place elsewhere, Balkh's economy was badly damaged by the outbreak of conflict. While no provincial data exist, there was a severe decline in national output of a number of products that were critical to Balkh's economy. For instance, between 1978 and 1982, ginned cotton fell by 73 percent, woollen textiles by 33 percent, and vegetable oil by 73 percent.⁸⁵ The export of *qarakul* pelts was likewise hit hard by a combination of conflict-related trade disruptions, extended drought that decimated the herds, and changing tastes in Europe away from the wearing of animal skins.

Mazar's economy got something of a boost when Najib turned to the private sector around 1986, and in the 1990s when it was a relatively safe haven from the fighting raging in Kabul and elsewhere in the country.

5.2 Balkh's economy post-2001

Post-2001, the process of accumulation and growth continued in Balkh in the context of the new national policy of the market economy and private sector-led growth.

Mazar city has seen unprecedented expansion and development, especially in the areas of fuel and general trade, transport and construction. As the northern commercial hub, Mazar has attracted entrepreneurs from the neighbouring provinces (i.e. the businessmen Ghazanfar and Kefayat, who come from Jawzjan). The relative security has also attracted economic actors from elsewhere in the country; traders have moved to Mazar from Helmand, Kandahar and Herat to avoid general insecurity or the kidnapping of businessmen by organised criminal gangs. Although there are no precise calculations of provincial growth, some estimate that the economy of Mazar has grown at a rate of 20 percent per year, nearly twice the national average of 11 percent.⁸⁶ Considerable domestic private investment has occurred, much of which likely involves the proceeds of non-legal activities (see below). The city has benefited from its proximity to the Uzbekistan border

⁸⁴ This arrangement was somewhat controversial. Some believe that this allowed higher prices for Afghan raw materials, while others believe that Afghanistan did poorly by receiving low-quality Soviet consumer goods. Also, the gauges to measure flow through the gas pipeline were said to be located on the Soviet side of the border, which made it difficult for Afghan officials to determine the volume being exported.

⁸⁵ Nyrop and Seekins, "Afghanistan Country Study." Note that these are official government statistics, which may even understate the declines.

⁸⁶ Balkh Provincial Development Council, "Balkh Economic Profile: A compilation of information on local economy in the Balkh Province" (Private Sector Development Sectoral Committee, June 2010).

and the trade that this generates, though the majority of cross-border trade is in the hands of a small number of businessmen, almost all of whom have political links with the local political elite. They appear, however, to have invested some of their profits in various ventures around Mazar, which have had a positive economic impact. State lands around Mazar have been widely distributed; while the legality of much of the distribution has been questioned, the effect has been to stimulate the private construction sector. Land has also been the proximate cause of much internal discord, particularly between Jamiat and Hizb-i Wahdat, with the latter alleging that the Hazara community has been marginalised and that its legal tenure, on the basis of presidential decrees from the 1990s, has been disregarded.

A much-speculated-upon driver of the (legal) economy in Mazar has been re-invested proceeds from the illegal drugs trade. Two years prior to becoming “poppy-free” in 2007, Balkh cultivated 10 percent of the country’s opium poppy area (third highest province, behind only Helmand and Kandahar), and was considered an important trafficking hub for the northern route to Europe. The role of the highest officials in the province was also much speculated on, with the general view that they were deeply involved. Regardless, it is assumed that some of the profits generated through the sector were subsequently invested locally and helped to drive the real estate, construction and other sectors. With the multiplier rippling through the rest of the economy, the consumer goods and other sectors were strengthened. Balkh has historically been a producer of *chars* (hashish), which has not been suppressed with the same level of enthusiasm.

While Mazar has been an “engine” of economic activity, it is not clear to what extent that “engine” has pulled the other provinces and areas along with it. Some observers take a critical view of the role that Mazar has played in the regional economy: “Mazar has been growing at the expense of the rest of Northern Afghanistan, sucking capital and human resources and turning the other provinces into mere markets. Rather than driving regional development, it has acted as a giant consumption centre, with little ripple effects.”⁸⁷ It seems more likely, however, that Mazar plays an important and positive role as distribution point for imports and exports, in processing of regional agricultural production, and as a market for local agricultural production in the other northern provinces,⁸⁸ as well as a source for construction materials needed in Mazar. The latter includes gypsum produced in Andkhui (Jawzjan) and marble quarried in Samangan. A 2012 study on the northern economic corridor between Pul-e Khumri and Andkhui noted the potential of the four sectors of transportation and logistics, light manufacturing and agro-processing, construction materials, and pilgrimage and tourism to spread growth up and down the corridor.⁸⁹

Afghanistan’s first real railway line⁹⁰— 73 kilometres from Hairatan to Camp Marmal, 18 kilometres east of Mazar—began formal operation in February 2012. Planning followed a 2008 memorandum of understanding between Afghanistan and Uzbekistan “to expand trade and economic opportunities by developing railway transport” between the two countries. In November 2009 the ADB provided a grant of US\$165 million to the Afghan government, which then awarded a non-tendered contract for \$129 million to Uzbekistan State Railways (UTY) for construction, followed by a three-year management contract. It appears that with the exception of security, Uzbekistan provided all materials and labour, with work crews transported across the border daily from Termez.

The railway was envisioned partly because the existing road over the Friendship Bridge could not cope with the increased volume of freight crossing the border. According to the ADB’s estimates, the railway will quadruple the capacity of the border. At present, trains bring in construction materials, petroleum products, wheat and other agricultural products, and machinery, but take out very little. There is an expectation, however, that it will facilitate the export of minerals as well as agricultural outputs, and that the railway will be linked with future lines to be constructed to Herat in the west and Pakistan in the east, including sections intended to carry iron, copper and other minerals. In March, Turkmenistan, Tajikistan and Afghanistan signed a tri-partite agreement

87 Giustozzi, “Resilient Oligopoly,” 36.

88 See SHC/MC, 2012.

89 USAID, “Northern Economic Corridor Study” (Afghanistan Small And Medium Enterprise Development (ASMED) Project, DAI, March 2012).

90 Technically, it is not true that Afghanistan has never had a railway. During the modernising reign of Amanullah Khan (1919-29), a 7 km railway was built between the center of Kabul and Darulaman, then on the southwestern limits of the capital. Locomotives were imported from Germany, with some of the carriages manufactured locally. See the extensive and valuable web site “Railways of Afghanistan” at <http://www.andrewgrantham.co.uk/afghanistan/>.

for a 400 km railway linking Aqina with the two central Asian states.⁹¹ Some analysts are sceptical about the economic basis for some of the more ambitious proposals that go beyond connecting border cities with neighbouring countries' rail lines in order to facilitate trade.

The Mazar airport is nearing completion of an extensive EU35 million (€) renovation, financed largely by Germany and the United Arab Emirates, to resurface the runway and enlarge the taxiways, construct a new terminal building with customs and immigration services, and expand passenger and cargo capacity. Upon completion, the airport will meet International Civil Aviation Organization standards and therefore be able to more easily accommodate international flights. At present, there are regular scheduled flights between Mazar and Iran through a collaboration between Kam Air (owned by local entrepreneur Kamgar) and Iranian Asseman Airlines, while during a brief period starting in 2009, Safi Airways was flying between Mazar and Dubai. The airport continues to accommodate flights for visiting regional and European dignitaries.

Mazar has two industrial parks, one (with 46 plots spread over 25 ha) in Gorimar 2 km from the new railway line on the eastern approach to the city, which was funded by USAID and is managed by the Afghanistan Investment Support Agency (AISA), and a second older one (with 119 plots spread over 190 ha) in the Dasht-e Shadian area to the south near the Silo, which is connected with the Ministry of Commerce. While the Gorimar park now appears to be filling up, during its first years of operation it did not meet expectations. Partly because of the need to rely on expensive generator power, the shared running costs were higher than most Afghan firms could afford. In addition, a number of the plots were purchased by speculators and sat empty. AISA was recently given the unenviable task of weeding out the speculators from the occupants who were using the space for productive enterprises. The Shadian industrial area, as it is older and more established, is connected to the grid and is the site of more active enterprises, although the power is not reliable. There are no other services there, which in some ways makes it more attractive to Afghan enterprises which don't require a high level of services. However, Shadian also has issues related to land titles, which have been given out over the years under different governments, as well as squatter houses built on approximately 40 of the sites. There is also apparently discussion about a third industrial park to be constructed at Kod-e Barq or elsewhere in the area.

Despite the growth that has taken place there are currently a number of worrying signs, including the fall in the price of land and contraction of the construction sector. Some of these were observed as much as three years ago, although most of the concerns are attributed to the approaching 2014 Transition. According to an economic profile published in June 2010, "investment growth of various types, including industry, manufacturing and construction has slowed down, raising concerns about weakening private investment power and the general investment climate."⁹² The following sections describe the contribution of the major sectors since 2001.

5.3 Contribution of the major sectors

The post-2001 economic expansion in Balkh has been driven by a number of key sectors, and influenced by geographical location and the political economy of the region. Similar to the national level, the key drivers of the Balkh economy have been the construction, transport and other service sectors. The following sections provide only a brief overview of the main sectors, as it is not possible to do each one justice with limited space.

5.3.1 Agriculture

The agricultural economy of Balkh is based mainly on wheat, fruits and nuts. According to the Ministry of Agriculture, Irrigation and Livestock (MAIL), cereals and fruits make up 77 percent of value of production, followed by oil crops at 19 percent. In 1384-85 (2005), local trade in agricultural produce was US\$126 million per year.⁹³ According to government statistics, in 2011-12 Balkh had the second largest area (after Herat) devoted to wheat, roughly equally divided

91 "Afghanistan, 2 ex-Soviet nations to build railway," Associated Press, 20 March 2013. <http://www.guardian.co.uk/world/feedarticle/10710404>.

92 "Balkh Economic Profile."

93 Ibid.

between irrigated land and relatively unproductive *lalmi* (rain-fed) land. Balkh also is among the leading producers of almonds (in 2011-12 seventh highest among provinces with 4 percent of national output) and pomegranates (second highest, with 12 percent of national output).⁹⁴ Balkh was also historically a major producer of cotton, although during the years of conflict and drought production collapsed to virtually nothing. There is some evidence, however, that cotton has been making a comeback; according to official statistics, in 2011-12 Balkh produced nearly one-quarter of the national total.⁹⁵ Some of the credit for the comeback is given to the Gino Press, one of the first state-owned enterprises to be privatised, and which was supposed to purchase raw cotton to produce cotton fibre as well as cooking oil and *kunjara* (oil seed cake used as animal feed). It also provided seeds, inputs and loans, although it is now closed, in part due to the inability to procure an adequate volume of raw cotton at the fixed prices. A number of small, private oil presses had opened around Mazar and hurt Gino Press by absorbing much of its supply of raw cotton. Balkh's other significant agricultural outputs include barley, rice, sesame, flax and melons, as well as a number of smaller volume, higher value niche crops, including liquorice, morel mushrooms, and *hing* (asafoetida), the latter of which has a good market in India, where it has both medicinal and cooking uses. According to one source, *hing*, processed in Mazar and Herat, is Afghanistan's largest agricultural export (550 metric tonnes [MT], \$37.5m), at more than twice the value of raisins.⁹⁶

At least until 2007 when Balkh became "poppy-free," opium poppy cultivation was a significant part of the agricultural economy, with linkages to other sectors such as trade and finance. It is widely believed that since 2007 *chars* (marijuana), which is under less government pressure, has replaced opium poppy for many households' livelihoods strategy.

Over the last several years, roads within the province have been upgraded, especially within the more productive agricultural areas. Also, the widespread use of the Zaranj (a type of motorbike which can be fitted with a variety of bodies and trailers) has substantially reduced the cost of transporting goods (and people) over short distances. These factors, along with the relatively permissive security environment, have facilitated the transport of outputs to markets, including exports. This has encouraged more extensive production of vegetables such as okra, onions and carrots. Despite that, however, aside from low productivity, the lack of markets, both domestic and international, remains the largest issue facing agriculture.

Saffron was introduced to Balkh around 2006, ostensibly as an alternative crop to opium poppy. Balkh is now second only to Herat in saffron cultivation in Afghanistan. Much of the work is done by women; the provincial Department of Agriculture, Irrigation and Livestock (DAIL) has distributed 2,000 kg of bulbs to 125 women, and there are 17 demonstration plots in nine districts of the province. There were also accusations that much of it was actually from Iran but packaged as Afghan saffron. Trading is done on a small scale, with no dedicated or wholesale traders. Some of the saffron makes its way to India.

Farmers and private sector actors have recently established a number of fish farms in the province. One successful enterprise in Dawlatabad is employing 12 persons, and selling output in markets in Khulm, Mazar and Hairatan. Production has apparently expanded to Hazrat Sultan in Samangan Province, with fish being sold elsewhere in the province. Especially in winter, there is a high demand for fish, some of which comes from the Amu Darya near Hairatan, while some is of unknown provenance, variously said to be Jalalabad or Karachi.

There are at least two private cold storage enterprises, which are considered successful, now that the initial electricity constraint seems to have been mostly resolved. These operate in two different ways. First, the owners of the cold storage purchase potatoes, turnips, fruits and other outputs at harvest time, then store them for selling at a later date when prices have risen. Second, cooperatives bring in their outputs at harvest time for storage, then take them out and sell at a higher price later in the year. Respondents claimed that this has helped to reduce the phenomenon of potatoes and onions being sold at a low harvest-time price to Pakistani

94 CSO, "Afghanistan Statistical Yearbook 2011-2012" (Kabul, 2012).

95 Ibid.

96 MAIL and partners, "Newsletter, Capacity Building and Change Management Program for the Ministry of Agriculture, Irrigation and Livestock" (Kabul: MAIL, December 2012).

traders who then would bring them back from Pakistan for sale when prices had risen.⁹⁷ DAIL has expressed interest in building at least one cold storage facility, and is planning one near the Silo with a capacity of 5,000 MT.

The most consistent demand has been for construction of a major irrigation facility on the Amu Darya, along with the stabilisation of the riverbanks against the erosion of productive agricultural land. The failure to take on these related initiatives is invariably one of the main issues cited as evidence for the ineffectiveness of the government and its partners. Several riverbank stabilisation projects have been undertaken near Hairatan, but these are seen as inadequate to the scale of the problem. Aside from constraining the development of agriculture, water shortages are likely to intensify conflict, especially given population growth. As in many areas of Afghanistan, the degradation of the environment through desertification, erosion and other factors due to growth in population and apparent shifts in precipitation patterns threatens the ability to strengthen agriculture.

In some cases the lack of effective and efficient institutional infrastructure for inspection and certification as well as industrial facilities for cleaning, sorting, drying and storage limit production incentives and allow Afghanistan's neighbours to benefit from adding value. For instance, there are reports that raisins are exported to Uzbekistan and Pakistan, where they are cleaned and packaged—then exported as a product of those countries. Similarly, while the northern provinces produce 70 percent of the country's wheat only 5 percent of the flour in the Mazar grain market was estimated to be from locally produced grain.⁹⁸ While local mills have been established, most have trouble competing due to Pakistan's highly subsidised wheat production, price policies, lower labour and power costs, and economies of scale. One international agency calculated that it was cheaper to ship grain to Pakistan to have it milled and bagged than to have it processed locally.⁹⁹ At the same time, the lack of material (fruit, cotton, sesame and other oilseeds) has constrained the development of agro-processing industries. One US government study estimates that Afghanistan's international world market share of the near-term priority crops of almonds and raisins could increase from 2-4 to 55-60 percent and 3-5 to 40-45 percent between 2008-09 and 2014 (at the national level).¹⁰⁰ These projections seem quite optimistic, but suggest possible areas for focus.

5.3.2 Construction

The construction and land sectors are among the most active in the country, and have been major drivers of Balkh's economy.

The main sources of funding for construction projects are the international military, international donor funding (either directly or through government departments), Afghan government from the national budget, and private sources (i.e. for business centres or residences). As in other sectors, contracts are gained through a mix of capacity and personal relationships (*wasita*) with those who have influence over their issuance. As shown in Table 3, according to AISA, there are currently 504 construction companies registered in Balkh, or 52 percent of the total companies.¹⁰¹ This does not include the significant number of companies registered in Kabul but that do work in Balkh, especially on the larger projects. That more than half of the registered companies and nearly half of the reported employment were in construction underlines the weight of that sector in the economic boom and in the international spending that has helped drive that boom.

97 Most consider this an urban legend, as the arithmetic doesn't support the idea, especially for low-value crops such as cucumbers.

98 USAID, "Northern Economic Corridor Study," 26.

99 Suresh Persaud, "Long-Term Growth Prospects for Wheat Production in Afghanistan" (Washington, DC: USDA ERS, January 2012).

100 "Afghanistan Agricultural Assessment and Framework Development" (Summary presentation, Global Development Advisors, April 2011).

101 A number of caveats need to be mentioned. Registration over-emphasises companies focused on international funding, as many register primarily to get access to international contracts. Also, reported investment capital is "intended investment," which may be wildly under- or over-stated for specific reasons pertaining to each reporting company and to AISA itself. Firms may also be spending on things which are not really investment. Finally, many of the companies in the database may in fact be bankrupt, but have remained "active" because closing the company would require them to get clearance from the government, which would then demand unpaid taxes. According to the World Bank's Investment Climate Report, while Afghanistan ranks near the top globally on ease of opening a business, it ranks near the bottom on ease of closing one.

Post-2001, many people responded to the opportunities provided by the international spending and formed construction companies. Some Afghan NGOs in fact converted to construction companies, in part because Article 8 of the 2002 Law on Non-Governmental Organizations prohibits "participation in construction projects and contracts." Also, that only 2 percent of the companies fell under "agriculture" underlines both the structure and characteristics of the sector as well as perhaps the limited emphasis that has been put on it, although a number of companies listed under "industry" were those which processed agricultural commodities such as animal feed, candy, cooking oil, dry fruit, ice cream, dairy products and tomato paste. Still, AISA's estimate that of total private investment at the country level, construction received 14 percent and agriculture 2 percent suggests where opportunities have been.¹⁰²

Table 3: Balkh companies, per registration with AISA

	Number	% of total	Initial capital (US\$ '000)	Avg capital per firm (US\$ '000)	Employees			
					Afghan	Int'l.	Total	% of total
Agriculture	23	2%	6,179.5	268.7	498	15	513	4%
Construction	504	52%	74,131.3	147.1	6,229	125	6,354	48%
Industry	242	25%	48,351.1	199.8	3,761	56	3,817	29%
Services	195	20%	38,795.1	198.9	2,220	323	2,543	19%
TOTAL	964	100%	167,457.0	173.7	12,708	519	13,227	100%

Source: AISA database, received January 2013. Note significant caveats in the footnote.

Although the exact proportions are not clear, international community spending is an important driver in the sector. The most commonly given estimate is that the international community accounts for roughly 60 percent of spending. A source within RC-North with extensive experience in the sector estimated that 60-70 percent of the economy was related to the international community, of which 40 percent was construction and 20-30 percent transport/services.¹⁰³

Sources in the construction industry reported that military projects were the most desirable, as they were usually over-designed and priced at double or triple the rate of normal construction projects. In addition, the US military was said to include additional security costs, regardless of whether they were needed, which increased the total cost (and profit) of the project. Some respondents claimed that military-funded projects are also tax-free from the Afghan government, but the law and practice related to this could not be confirmed.

Although there is a mix of local and Kabul-based companies operating in Balkh, most of the larger ones are registered in Kabul. A number of international companies (i.e. US, Turkish, or Dubai-based Afghan) take on the largest projects (i.e. more than \$50 million) and partner or subcontract with local companies. Even for government projects, in some cases where high technical capacity is needed, contracts will be given to international firms. For private projects such as residential buildings, business centres, houses, wedding halls, and restaurants, roughly half are implemented by the owner himself and roughly half through contracts with local companies.

As noted elsewhere, sub-contracting inflates the costs of construction projects beyond the actual costs of administration and overheads. Examples were cited of where the main contract amounts given to an international company were twice the value of sub-contracts issued to local companies. On the other hand, respondents noted the positive effects of sub-contracting: that in the last several years local companies that had worked as sub-contractors had improved their project planning, analysis, design and implementation skills through working with international companies and consultants. In addition, they were able to invest in construction equipment.

¹⁰² Afghanistan Investment Support Agency, "Estimating Business Fixed Investment in Afghanistan" (Kabul, May 2012).

¹⁰³ An audit of US\$654 million of "Afghan First" contracts found that 90 percent were in the construction sector. The audit excluded contracts openly competed, subcontracts, or CERP projects. Office of the US Special Inspector General for Afghanistan Reconstruction, "Afghan First Initiative Has Placed Work with Afghan Companies, but Is Affected by Inconsistent Contract Solicitation and Vetting, and Employment Data Is Limited" (31 January 2012).

Aside from being a major source of employment for both unskilled and skilled workers, (discussed below), the construction boom has also had positive backward linkages to extraction of minerals. This includes aggregate, which is needed for all construction. The largest source for unprocessed sand is Hairatan, which provides sand for virtually all construction projects in Balkh, as well as for the nearby provinces of Faryab, Jawzjan, Sar-e Pul and Samangan. There were previously no crushing plants and workers relied on natural gravel, but in recent years several crushing plants have been established in Mazar. In addition, lime is now produced in a number of factories. Similarly, the demand for gypsum has resulted in the establishment of a number of new factories, including one in Andkhui. The first factory was established in Khulm, and there are now at least ten between there and Mazar. Demand for baked brick has resulted in new factories that can produce 100 times more than traditional methods. While these factories generate income, they also have a negative impact on the environment, and are associated with the use of child labour.¹⁰⁴ More sophisticated brick-making plants include the government one at Kod-e Barq and a private one (Mazar Folad) in the eastern part of Mazar city. Finally, stone for construction is quarried in the mountains to the south of Mazar and from Khulm, while decorated stone from neighbouring Samangan Province is considered the best quality. To some extent manufactured tiles imported from Iran are replacing this stone.

Other construction materials and equipment are imported, mainly through Hairatan, Aqina, Torkham and Turghundi. Of the approximately 160-180 tonnes of cement produced at the Ghori cement factory in Pul-i Khumri, a small amount, about 100 tonnes, comes to Mazar, with the rest of local needs fulfilled by imports from Pakistan, which has come to dominate the market in part through manipulation of prices,¹⁰⁵ and, to a lesser extent, Russia. Steel bar comes from Russia, Uzbekistan and Tajikistan, while iron angle bar comes from China, India and Iran. There are currently about 20 factories in Mazar producing aluminium and PVC windows and doors, as well as tiles. Wood products also come from Russia. Driven by the overall construction boom and the current preference for glass in buildings, glass is imported from Russia, Iran, China, Central Asia and Europe.

The construction sector has helped create business opportunities and provides the government with significant tax revenues. In 2012, construction companies in Balkh paid 15.6 million Afs in taxes.¹⁰⁶ Between 1391 and 1392, the number of construction companies listed as paying taxes more than doubled from 359 to 790, which in large part reflects the government's increased ability to collect taxes.

Some companies have invested in small factories to produce construction materials such as PVC windows and doors, concrete blocks, and other concrete products, but most of the reports of re-investment of revenue from the construction sector are anecdotal, as there is no systematic collection of this information and personnel were reluctant to divulge details. Much of what is re-invested goes into land, houses, business centres, *shahraks* (residential communities) and factories. Some companies have established their main offices in UAE, from where they are positioned to diversify their work to other countries.

As discussed further below, the construction sector was said to have peaked in 2009-10, then contracted sharply after the announcement of the 2014 Transition.

5.3.3 Land

Closely related to construction, land has been one of the most lucrative sectors. The footprint of Mazar city has spread in all directions, especially to the east along the corridor between the city and the turnoff to Hairatan at Naibabad and to the south in the massive Khalid bin Walid residential development. Because land is closely tied to political hierarchy and often exists on the margins, at best, of legality, it is a sector not easily explored. The preferential distribution of plots of land based on personal relationships and in exchange for political favours is widely

¹⁰⁴ See "Buried in Bricks: A Rapid Assessment of Bonded Labour in Brick Kilns in Afghanistan," (Samuel Hall Consulting for ILO, 2011). While the study focused on Kabul and Nangarhar, anecdotal information suggests that conditions in Balkh are not significantly different.

¹⁰⁵ See ASMED, "Northern Economic Corridor Study."

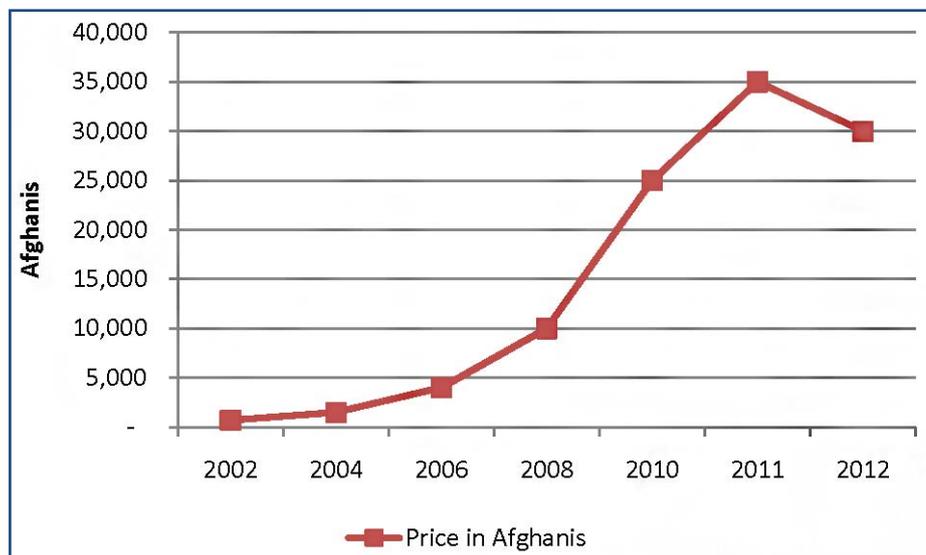
¹⁰⁶ Medium Taxpayer Office, Ministry of Finance, Balkh.

acknowledged and is discussed openly in the media.¹⁰⁷ Informed estimates are that 339,000 *jeribs* (67,800 ha) of government land have been appropriated by around 1,500 well-connected and powerful persons in the province. Roughly one-half of this is agricultural land, which has been taken out of production or converted to residential areas over the last ten years. An additional 230,000 *jeribs* of agricultural or grazing land has similarly been taken. This inventory is based on a list compiled at the line ministry level in response to a multi-faceted directive from President Karzai in July 2012 addressing government corruption and inefficiency. It is unlikely that much will be done with the list, unless there are some major political upheavals in the province and in national politics.

It is generally understood that the steady rise in land values until 2011 was driven by the high incomes provided by international organisations' salaries or by their contracts, along with ill-gotten gains in the government and NGOs or through trade in illicit commodities. When a low-grade official earning a salary of US\$100-200 per month manages within one year to construct a three-story building or purchase an expensive vehicle, he is assumed to have acquired the resources through corrupt means. Similar assumptions are made when construction companies acquire numerous properties whose value exceeds the value of their contracts to date. Ironically, the collapse of Kabul Bank in September 2010 further contributed to the rise in land prices in Mazar; when people withdrew their money from Kabul Bank, many purchased land, as trust in the entire banking sector was in question and they assumed that land would continue to rise in value. (See Figure 1.)

Shahraks, or residential communities, include Azadi, Intezar, Omar Farooq, Ghazanfar, Amiri, Rasul-e-Barat and Khalid bin Walid, many of which are named after their owners or developers. Several years ago it was sufficient to just provide land, but given the proliferation of developments, the *shahraks* began competing on services. By far the largest one is Khalid bin Walid, informally referred to as "Governor Atta's project," which is of truly stunning scale both geographically, covering an area of roughly 15 square kilometres, and with respect to its amenities. While supporters say that the land was developed "by the book," the true ownership and provenance of the land is somewhat murky. The project has allowed Atta to simultaneously reward loyalists and build credibility with the general population for such a visible project.

Figure 1: Price of plot of land at *shahrak* Khalid bin Walid



Source: Property agents, Mazar city

The fall in land prices over the last two years has affected all of the *shahraks*, albeit to different degrees. Many businessmen invested large amounts of money in building the *shahraks* or in purchasing them with an eye to having a solid investment which would increase in value over time. Now that land values have plummeted and people have become cautious, owners are not

107 See Hulab Shah Bawer, "Afghans frustrated by corruption at every level of government" (Institute for War & Peace Reporting, 17 October 2012).

able to sell them, even at a loss. Also, given the “land-rush” frenzy in which some of them were developed, the future of some *shahraks* may be further complicated by their questionable legal status and the existence of multiple claimants to plots.

One of the more egalitarian consequences of the patronage-related land and construction process has been that even persons of modest means who several years ago might only have dreamed of owning a home were now the owners of a house to live in, rent out or keep as an investment. At the same time, changing social preferences among the young generation to live away from the extended family have increased demand for separate housing. This along with the lack of zoning in most developments has often meant that modest houses were situated next to sprawling, ostentatious ones. As a separate but existential issue, there have been questions raised about whether or not water will be sufficient in the future to sustain these huge tracts of housing and increased population.

5.3.4 Trade and transport

Building on its history as a trading hub, Balkh, especially Mazar, has benefited greatly from post-2001 trade and commerce. (Mazar is sometimes referred to locally, with more than a bit of hyperbole, as “the Dubai of Afghanistan.”) The robust trade sector is partly due to the city’s relatively privileged position during the war years and its subsequent relative security; Kunduz traders are reported to travel to Tajikistan via Hairatan and Uzbekistan to avoid kidnapping threats on the road between Kunduz city and the border at Sher Khan Bandar. Most construction companies are involved in transportation as well. Until several years ago, almost half of Afghanistan’s in-bound trade entered through the border town of Hairatan, generating significant amounts of revenue through customs. Hairatan gained additional economic and political importance in late 2011 when it became the chief crossing point for NATO’s “northern distribution network.”¹⁰⁸ Approximately two-thirds of Balkh Province’s reported revenues come from taxes on imports and exports. Of that, most is likely to be from imports, as according to official trade statistics, \$500 million worth of goods were imported from Uzbekistan, while only \$2 million were exported.¹⁰⁹ At two locations in Mazar coal mined in Darra-e Souf in Samangan is transferred to Pakistani trucks for export.

Given the presence of NATO’s RC-North at Camp Marmal, NATO has been one of the biggest sources of funding for the transport sector, even more so since the northern distribution network became active. It is anticipated that the transport sector will continue to boom for at least the next couple of years due to the heavy requirements of both withdrawal (“retrograde”) and resupply for whatever international military presence remains post-2014, although procurement policy may be evolving to favour central Asian firms in order to curry favour along the northern extraction route. Regardless, post-2014 there will be a major decline in the transport sector. As with other international procurement activities, ISAF demands for transport may produce distortions in the transport market because they are willing to pay higher than prevailing market prices, in part because of their limited timeframe.

In addition to the official revenues, customs also generates significant amounts of “unofficial revenue” for individuals. While the facilities and systems at Hairatan have been modernised through investment by the European Commission and USAID in order to facilitate trade, as observed in one report, “the problems and bottlenecks in the customs system are less to do with inadequacies in the infrastructure and procedures and more with systemic corruption...currently there is little or no incentive for the users of the system to change it.”¹¹⁰ Key players in the system are the so-called *commission-kar* (commission agent), who maintain links between traders and officials and extract percentages from transactions. Although officially the customs system reports through Ministry of Finance channels to Kabul, in practice appointments, supervision, and extraction take place within the provincial power structures, which include other positions (e.g. mayor) that

108 The northern distribution network consists of road, rail, and routes through Central Asia which were developed by NATO in 2009 as an alternative to supply routes through Pakistan that were coming under attack. The network became active due to the closure of the border with Pakistan after the killing of 24 Pakistani soldiers by US forces in November 2011.

109 As with most official statistics, trade numbers should be taken with caution. In this case, the trade totals may include duty-free NATO imports and are for all of Uzbekistan, although the latter may not be so problematic given that Hairatan is the only direct crossing.

110 “Customs Reform in Afghanistan: Moving Between Introduced and Pre-existing Structures” (Kabul: Afghanistan Public Policy Research Organization, December 2011), 2.

are horizontally related. Recent reports that Hairatan had lost trade because other ports had a lower effective taxation rate due to the recent strengthening of Hairatan's procedures after an inspection by a local team were considered plausible "to some extent."

As in other sectors, corruption and poor governance constrain trade and other economic activity. Some analysis has noted the negative influence of poor "road transport governance" issues in inhibiting competition. For instance, in a survey of 1,000 truck drivers, 90 percent stated that "bureaucracy" (read "corruption") was the biggest obstacle to trade, while only 5 percent mentioned insecurity or poor infrastructure. In particular, they cite the domination influence of the "large stakeholders" in getting preferential access to the port facilities at Hairatan, and note that "trade and transport costs ...depend much more on operations and governance than on infrastructure capacity."¹¹¹

Box 3: Views on competition, trade and the market economy

Reflecting Afghanistan's extreme trade deficit, interviewees in Balkh showed scepticism about the benefits of international trade and expressed fears that Afghanistan would remain a "consumer nation." One pervasive explanation for the weakness of the economy was the introduction of the market economy and an open trade regime—both seen as externally imposed. The factors that led to Afghanistan's production being uncompetitive on the global or even domestic market have been well-documented (e.g. unskilled and expensive labour, expensive and unreliable power, poor roads and other infrastructure, inability to produce at scale). In Balkh, respondents noted that California almonds were selling more cheaply than some locally produced varieties.

The trade imbalance was attributed in large part to predatory activities by Afghanistan's regional neighbours and the lack of adequate defence by the Afghan government. The neighbours were blamed for product dumping, which was alleged to happen in a coordinated, conspiratorial way. Even more seriously, respondents noted a recent fire in a Herat ice cream factory, which had been competing with Iranian products, and the burning of 10 trucks of saffron bulbs headed for the Afghan border. Both of these acts were allegedly committed by "the Iranians" to suppress Afghan economic activities. In turn, the Afghan government was criticised for inadequately advocating for Afghan producers and traders. First, export tariffs on Afghan production and import tariffs for intermediate goods, which were higher than those on finished goods, were a sore point, as they contributed to making Afghan products non-competitive in regional markets. Second, Pakistani trucks were allowed to circulate in Afghanistan while Afghan trucks were not allowed to enter Pakistan. Third, Afghan businessmen complained that the lack of business visas to travel to other countries in the region kept them from adequately representing Afghan products; the government was said not to have been sufficiently aggressive in pushing on this issue.

Beyond that, products from the neighbouring countries were seen to compete with Afghan products in ways beyond the technical reach of Afghan businesses. For instance, imported products often had better packaging, including expiry dates (however whimsical), which conveyed the notion of quality. Dairy producers noted that UHT milk from Pakistan did not need refrigeration before opening, which provided a huge advantage, as the majority of shopkeepers don't have refrigeration facilities and reliable electricity.

According to one analyst, "Afghanistan is the country in the region least able to resist the pressure of Western advisers and diplomats on matters of economic policy. As a result, Afghanistan has the most liberal trade regime in the region."¹ Surveys have confirmed the fears that traders feel that international trade (which has largely meant imports) will hurt farmers and small-scale producers.²

1 Anna Paterson, "Common and Contested Ground: Russian Approaches to Security and Development in Afghanistan, 1991-2008," (London: Thesis submitted for the degree of PhD at the School of Slavonic and East European Studies, University College London, March 2010), 273.

2 See Chemonics International, Trade and Accession Facilitation for Afghanistan (TAFAs), "Knowledge, Attitude and Practice (KAP) Survey of Afghanistan Towards Trade: Summary of Findings for TAFAs" (October 2010).

Partly as a consequence of these governance issues, the number of companies directly engaged in foreign trade is relatively limited. According to the 2008 Investment Climate Report, relative to other places, a smaller proportion of firms in Mazar had made investments. This may reflect the easier gains from trade available in the favourable environment in Mazar, as opposed to making

111 ASMED, "Northern Economic Corridor Study," 20.

(risky) fixed investments.¹¹² As discussed below, the uncertainty of the environment may further encourage the focus on trading and other economic activities with a short horizon.

Despite the proximity of Uzbekistan, export trade with that country is limited. Traders and would-be exporters cited lack of visas, restrictions on Afghan vehicles, border bottlenecks, and extensive “informal taxes and fees” as impeding trade. Due to the semi-isolation during the Soviet period and the physical boundary created by the Amu Darya, and despite the existence of ethnic and family brethren on both sides of the border, northern Afghanistan is not as economically integrated with its northern neighbours as is eastern Afghanistan with Pakistan. These historical and physical facts also make it easier for the northern neighbours to maintain a restricted trade system. Unlike the porous eastern and southern borders where almost anyone can be a smuggler, the northern border is extremely difficult to cross without the complicity of a range of individuals who exert control over the border; not surprisingly, smuggling has come to be controlled by a clique of elites with powerful networks and connections within Uzbekistan.¹¹³

Information on internal trade is very limited, and even data on exports is unreliable. Table 4 presents data on agricultural products exported through the ports at Hairatan and Aqina (technically in Faryab, but “temporarily” administered by Jawzjan). While “most” are produced in Balkh, they do also include some production from nine northern and central provinces, including Parwan. Conversely, while the majority of production from Balkh is exported through the two ports, some clearly goes through Kabul and Torkham.¹¹⁴

Table 4: Agricultural products exported via Hairatan and Aqina

Item	1390 Quantity (MT)	1391 Quantity (MT)	Destination
licorice	462	2,133	France, China, Turkey
Esfand	276	320	Iran, Turkey
Dried apricot	550	1,066	Iran, Turkey
Raisins	6,091	3,066	Turkey, Russia
Almonds	21,006	23,000	India
Walnuts	43,004	41,200	Iraq
Plums	22	3	Iraq, Iran
Pomegranate	1,000	1,700	Dubai, Russia, Pakistan
Watermelon seeds	40	5	Iran
Potatoes	4,631	3,843	Uzbekistan, Turkmenistan
Onions	231	125	Turkmenistan
Sesame	6,241	7,230	Iraq, Iran, Turkey
Cotton	500	300	India, Pakistan
Chicken feed	-	300	Uzbekistan

Source: Quarantine supervisory office, Hairatan. Figures have not been verified against national-level information. Esfand (wild rue) is a perennial shrubby weed used in Central Asia as a carpet dye and, more commonly, burned as a spiritual purifying agent.

112 See Lea et al, “Constraints to Growth.”

113 See Giustozzi, “Resilient Oligopoly.” In 2007, national estimates were that smuggled exports and imports were, respectively, 36 and 11 percent of official ones. See IMF, cited in “Understanding Afghanistan, Growth Diagnostic Scoping Study Final Report -Technical” (DFID and The Recovery and Development Consortium, November 2008). This was seen as an improvement from 2002-03, when smuggling exceeded official exports by nearly a factor of two. More recently, the head of the ACCI estimated that smuggled imports were equivalent to official ones. (Mohammad Qurban Haqjo, speaking on Tolo News programme Kankash, 27 November 2012. <http://www.tolonews.com/en/video/kankash?start=39>) “Informal trade” also includes licit goods traded illegally in order to avoid tariff and other costs. Since 2001 various projects have aimed to improve border management, but massive incentives remain to trade outside of formal channels.

114 Informed but informal estimates were that 10 percent of Balkh production went through other ports, but this is subject to verification.

5.3.5 Carpets¹¹⁵

Northern Afghanistan has a long history of production of woven carpets, both for household use and as the country's most significant legal export. Although small relative to Faryab and Jawzjan, Balkh Province has historically been one of the centres of production and trade, contributing roughly 10 percent of the approximately 60 percent of Afghan carpets currently produced in the north. According to industry sources, there are 129,900 carpet weavers, many of whom are women, in northern Afghanistan, of which 12,000 are in Balkh Province, and around one million persons benefit directly or indirectly from carpet production in the north.¹¹⁶ Production was formerly the almost exclusive occupation of Turkmens and Uzbeks, but has been expanded to other ethnic groups. There are currently five carpet associations and two carpet unions. The German Agency for International Cooperation (GIZ) and others have provided training in marketing and modern designs to try to maintain relevance in foreign markets.

The 30 years of conflict resulted in huge structural changes in the industry,¹¹⁷ especially the establishment of production in Pakistan, where during the 1980s Afghan refugees from the north established a carpet industry in refugee villages and urban areas. Some of this industry was controlled by Pakistani entrepreneurs who set up factories and established trade links abroad. Many of the producers who returned to Afghanistan post-2001 have remained dependent on Pakistan for finance, marketing, washing and cutting, and shipping. It appears that the import of unfinished carpets into Pakistan is technically illegal but is tolerated because of the value that is added through the finishing process.

The fragmentation of the former Soviet republics as well as conditions and restrictions in Iran and Turkey on the trans-shipment of goods from Afghanistan have made the former land export route to Europe less practical. Therefore, there is a continued reliance on Pakistan, which has implications for border delays. The expansion of the Mazar airport may increase the options for direct trade with Europe and beyond.

Although currently dependent on imported inputs, carpet production has the potential for extensive backward, forward, and horizontal linkages to agriculture, including wool spinning and dyeing and the production of natural dyes based on pomegranate skins and other substances. One of the key issues for carpet production in Balkh and elsewhere in Afghanistan is increasing the proportion of value added in Afghanistan rather than Pakistan. It is estimated that 80 percent of Afghan carpets are finished in Pakistan. According to industry estimates, if those carpets were instead cut and washed in the northern region, an additional net income of \$7.3 million would be generated, of which \$684,000 would be in Balkh.¹¹⁸

There are indications that the international market for woven carpets is finally improving after crashing during the worldwide recession that began in 2008, and could present opportunities for Afghanistan and for greater Balkh. Labour costs are rising in some competitor countries as the population urbanises and adopts less rigorous employment. Even China, which created a low-cost industry copying Afghan and other carpets, is now reaching a stage of industrialisation where former producers are losing their enthusiasm for weaving.

Mazar is the location for one of the three carpet weaving parks in the north. Despite plans to develop finishing facilities near the Hairatan turnoff, at present facilities are inadequate, including one at Gorimar industrial park, which is underutilised.

There were accusations of economic and political involvement by regional neighbours, including money being provided by Iran and Pakistan to local weavers in remote rural areas to produce carpets that would then be shipped or smuggled. In the case of Iran, it was said that the carpets were smuggled to Iran and then exported under the name of Qom and Isfahan. Also not surprisingly, there were accusations of ethnic and regional bias and favouritism. For instance, the Minister of

115 This section draws on information and insights provided by Stephen Landrigan and Qais Akbar Omar.

116 Data for 2009 provided by Afghan North Carpet Buyer's Guild, which has a relationship with the Ministry of Commerce and Industries.

117 See Adam Pain and Moharram Ali. "Understanding markets in Afghanistan: a case study of carpets and the Andkhoy carpet market" (Kabul: AREU, 2004).

118 Ibid.

Commerce was said to be pushing to build up the carpet industry in and around Jalalabad because it fit with a political agenda, preferring to see the finishing done in Pakistan because it strengthened the economy of the Pashtun border areas. This was also seen as an attempt to nationalise the concept of Afghan carpets rather than having a northern identity.

5.3.6 Mining

Mazar would be the likely hub for oil and gas, which is currently under exploration in the Amu Darya fields and other areas in the greater Balkh area. So far there has been little economic activity generated in the sector, although following a 25-year contract signed in December 2011 with China National Petroleum Corporation Watan Group (CNPC-W), during 2012 the first oil production began in the Amu Darya basin in Sar-e Pul and Faryab, with an estimate for the year of 150,000 barrels.¹¹⁹ Other estimates of the 2012 production by CNPC-W were lower, 5,000 barrels.¹²⁰ As Afghanistan does not have a refinery, CNPC-W is looking to sell the oil to regional refineries, including possibly one under construction by CNPC in Turkmenistan. In March 2012, the Ministry of Mines put the Afghan-Tajik Phase I fields out to tender, and in November received one bid for the two Sanduqli and Mazar-e Sharif blocks submitted by a four-way consortium of regional firms, including Afghanistan's Ghazanfar Group. Some observers believe that the two blocks that were bid on have higher potential and lower risk than the other four blocks. There is also said to be a refinery under consideration near Hairatan on the Uzbekistan border. The pipeline between Shiberghan and Mazar is currently under rehabilitation, under the guidance of the US DOD's TFBSO as part of the larger rehabilitation of the Shiberghan gas fields. Other minerals such as sulphur, sand for glass, and industrial salt occur in the province; the latter is currently produced on a small scale and sold to tanneries for the curing of leather.

5.4 Labour in Balkh's economy

The post-2004 economic boom in Mazar has attracted labourers not only from elsewhere in Balkh and its neighbouring provinces, but also from farther afield. According to the SHC/MC survey of four urban areas, Mazar had a higher proportion of workers (and employers) who had come from outside of the province, roughly one-quarter. Although statistical information is hard to come by, semi-skilled workers have migrated from Kabul in search of work and lower living costs. While the high wages post-2001 have attracted workers from elsewhere in South Asia, foreign workers (i.e. Bangladeshis) are more common on construction sites in Kabul and in the south of the country. There are an estimated 70,000 Pakistani workers, mainly in the construction sector, in Afghanistan.

As noted above, construction has been one of the largest sources of labour demand in Balkh, both for skilled and unskilled workers. Technical experts are recruited from Pakistan, India, Bangladesh, Philippines, Nepal and China based on the needs of specific projects, while labourers are recruited from Pakistan. Afghan construction company managers consider Pakistani labourers to be both cheaper and more highly skilled, and therefore more productive. (Probably also of relevance is that being foreigners in an environment which may not be completely welcoming, Pakistani workers may be less likely to organise or make demands on employers.)

Informal estimates are that international spending creates roughly 40 percent of the employment in the construction sector. The demand for labour coming from the construction boom is reflected in the steady upward growth in wages (see Figure 2), although there was some indication that wages might be stagnant or even declining in 2012 and 2013. Information provided by construction sector sources indicated a similar trajectory, although with higher wages in recent years and a more pronounced decline in the last year.

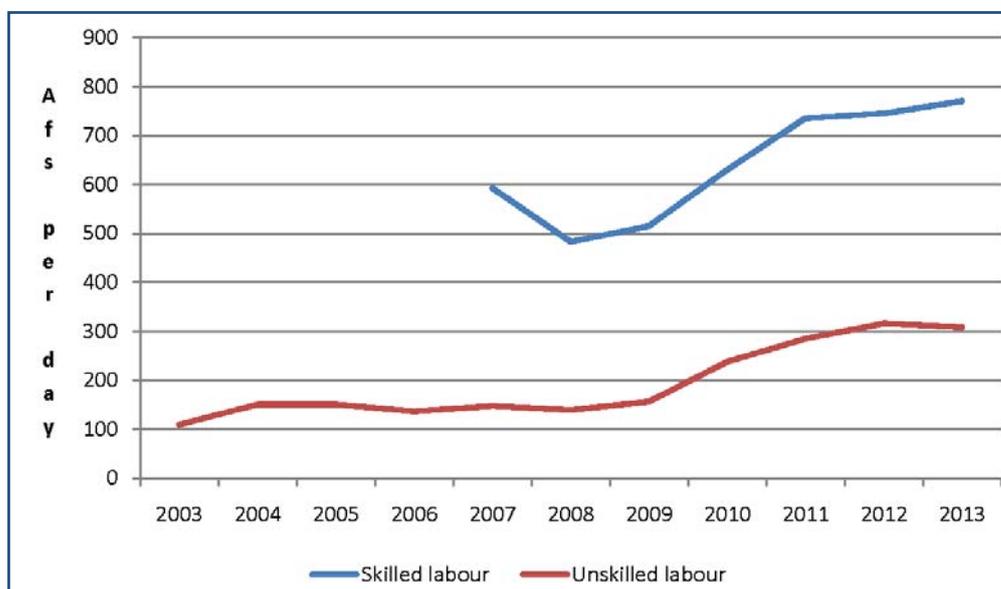
The high labour demand season in Balkh is May-July, due to agriculture and construction, most of which is suspended during the cold and damp winter. In 2012, there was a relatively favourable market for work for both skilled and unskilled daily labourers, at least relative to the previous year when poor agricultural conditions had reduced on-farm activity and sent men into the city to seek work, pushing down wages. Both demand as well as wages increased in 2012. During the second half of 2012, however, grain and flour prices were rising, in part due to similar trends on the

119 World Bank, "Economic Update," October 2012.

120 Special Inspector General for Afghanistan Reconstruction (SIGAR), "Quarterly Report to the United States Congress" (January 2013).

international market. This along with a fall in the labour wage led to a deterioration in the terms of trade between labour and wheat in much of Afghanistan. In Mazar the deterioration was less than elsewhere, and it is not clear whether this is a long-term trend.¹²¹

Figure 2: Wages for unskilled & skilled labour, 2003-13, annual average



Source: World Food Programme Vulnerability Analysis and Mapping¹²²

The casual labour market is an important part of the livelihoods picture for many households in rural areas, especially given the relatively good roads within a couple of hours of the city. Informal estimates are that 80 percent of casual workers are from rural districts outside of Mazar. Some from the close-in districts such as Balkh, Chimtal, Char Bolak, or even parts of Sholgara, will commute on a daily basis by Zaranj or other economical method of transport, while those from the farther districts (e.g. Kishindeh, Charkint, or Aqcha in Jawzjan) will stay with relatives, share a small house on the outskirts, or sleep in *chai khana*s. Even for many households who have agricultural land, income from daily labour helps to meet the financial shortfall, especially where the bulk of land is devoted to wheat as a food security strategy.¹²³ For such households, casual labour opportunities may provide a “safety valve,” which may take the pressure off the decision to migrate to Iran to seek work.

Although no precise figures are available, it is generally believed that construction has absorbed much of the labour that was previously occupied in poppy cultivation (weeding, lancing) prior to its suppression in 2007. Construction work is more remunerative than agricultural labour; for example, according to construction industry sources, in 2012 the typical daily unskilled construction wage was 400 Afs, while in agriculture it was, depending on source, 100-350 Afs, a difference of from 13 to 75 percent. Given the episodic nature of agricultural work, workers often come to Mazar or other towns to do construction work when they are free from agricultural responsibilities. This also leads to the apparent paradox that in rural areas labourers were complaining about the lack of employment and the consequent need to migrate, while landowners were complaining about a lack of workers. Shortages of agricultural labour may occur because in addition to being more remunerative, construction work is considered less strenuous.

121 According to WFP, despite significant increases in wheat flour and rice, the terms of trade between casual daily labour and wheat in Mazar in March 2013 were similar to the same period one year ago. World Food Programme, “Afghanistan Market Price Bulletin, March 2013” (Vulnerability Analysis and Mapping, April 2013).

122 Wages are in current Afghani. While wages and the CSO’s Consumer Price Index (CPI) have both increased by roughly the same percentage between 2004 and 2013, for much of that period the increase in CPI exceeded the increase in wages.

123 Among 30 land-owning households surveyed in Char Bolak and Chimtal districts in May 2012, 25 had males working off-farm either full- or part-time. For additional informal on casual labour in Mazar, especially with respect to opium poppy cultivation and livelihoods, see Paul Fishstein, “A Little Bit Poppy-Free and a Little Bit Eradicated: Opium poppy cultivation in Balkh and Badakhshan Provinces in 2011-12” (Kabul: AREU, May 2013).

Although these should be subject to serious caveats (see footnote 51 above), the 2007-08 NRVA suggests some outlines for the situation in the labour market in Balkh (Table 5). The measured unemployment rate of 8.2 percent is slightly above the national average and ranked roughly in the middle (18th best) of Afghanistan's 34 provinces. The measured underemployment rate is relatively better, estimated at 29.1 percent, below the national average of 48.2, and falling seventh from the best among provinces. The percentage of employment resulting from the four main sectors can be interpreted as consistent with Balkh's economic activity (i.e. the dominance of the construction and logistics sectors). In services, Balkh is third only to Kabul and Uruzgan in the proportion of employment measured to come from services, while it is fourth lowest after Kabul, Jawzjan and Faryab in the proportion coming from agriculture.¹²⁴

Table 5: NRVA provincial-level indicators on employment for Balkh, percentages and rank

	Unem- ployment	Under- employment	Sources of employment			
			Agriculture	Manufacturing	Services	Public administration
Balkh	8.2% (18)	29.1% (7)	38.5% (4)	16.2% (25)	43.2% (32)	2.1% (7)
National	7.9 %	48.2%	59.1%	12.5%	24.6%	3.9%

In a survey done in Mazar (and three other major cities) among employers and employees, manufacturing (non-handicraft) and wholesale and retail trade were reported as the primary source of income by the largest proportion of households (32 and 24 percent, respectively). These were followed by public administration (11 percent), transportation (8 percent), and manufacturing of handicrafts (8 percent). Interestingly, construction was fairly far down the list, given as the main source of income for only 6 percent of households.¹²⁵

Companies have complained about the lack of skilled labourers and the lack of specialised training for them. For this reason, some have opted to hire skilled labour and technical staff from the region. Some of the lack of training and upgrading might be attributed to the short-term, project focus of the companies, with companies focusing on the immediate task of completing the work, not thinking about the long-term need to build the skills and capacity of their workers and technical personnel. Companies tend to have small numbers of core staff, and expand employment on a temporary basis when they have acquired a contract.

The SHC/MC labour market survey confirmed the basic profile of the labour force: young and ill-prepared for career development. The survey particularly notes that workers were poorly educated or trained. While this may impose limits on individual development, as noted above, other analysis has suggested that the lack of trained workers was not a significant constraint to economic activity.¹²⁶ As an example of the disjunction between training and labour market demand, the Balkh University's Faculty of Agriculture has increased its annual number of graduates from 120 to 180, yet there are not likely to be jobs in what is supposedly Afghanistan's most important sector. According to a government employee:

What are they going to do? The 20-25 percent who know computers and English will join NGOs, 5 percent will join DAIL, and the rest will go work for their family business. Fifty percent will be jobless because they will be told "no experience". Without at least three years' experience, they won't be considered. The girls get jobs first, as teachers. Some now have internship programs, but the faculty are only now starting labs and practicum. They wanted to visit [industrial farm], but the farm's management didn't allow it because they were afraid of competition.¹²⁷

124 As noted above, provincial level data should be treated with great caution, as should the interpretation of the definition and characteristics of unemployment in Afghanistan. Moreover, in the case of the NRVA, some of the indicators at first glance do not make sense. For instance, the three provinces measured as having the lowest level of unemployment are Ghor, Uruzgan, and Badghis, three predominantly rural provinces where many of the issues concerning the nature of employment come into play. Likewise, that the agriculturally less-productive Zabul has an unemployment rate (3.0) estimated to be less than half of the national average (7.9) and is probably more than anything else a comment on the difficulty of measuring employment in Afghanistan.

125 SHC/MC labour market survey.

126 See Lea, "Constraints to Growth."

127 Interview, DAIL staff.

6. Looking Ahead

The key factor in all economic scenarios is, of course, what happens on the security and political fronts. In a national level survey of 400 firms conducted by AISA between December 2011 and March 2012, when asked about the likely effects of the withdrawal of international forces, 70 percent expressed concerns about negative impact, 25 percent thought it would have no effect, and 5 percent said it would have a positive effect.¹²⁸ As only 7 percent of firms said that they had directly benefited from donor agencies, this was likely due to the anticipated security effect.

While much of the public policy discussion of Transition has focused on building the capacity (and numbers) of the ANSF and the Afghan bureaucracy to resist insurgent challenges and to continue to deliver services, some analysts believe that stability will be more a function of what kind of deals and bargains are made among powerholders at local, regional and national levels.¹²⁹

As Balkh looks ahead, the immense amount of uncertainty about what the Transition will bring, both with respect to security and political change, along with on-going, chronic institutional and governance factors, have together translated into a lack of confidence in the future. At the same time, it is possible that the lack of confidence could itself become a self-fulfilling prophesy. In a reference to the experience of the 1990s, one provincial official used the Afghan proverb, "Once you are bit by the snake, you are afraid of the rope."

6.1 Security and political change

A number of factors will influence the security trajectory. First, there is a great deal of uncertainty about the extent of the military drawdown. Subsequent to the signing of the Afghan-US Strategic Agreement in May 2012, the US stated its intentions to retain a military presence until 2024, but it is not clear in what shape and form, and the Afghan-US Bilateral Security Agreement (BSA), which would set the conditions for an on-going presence, remains under negotiation.

It is not at all clear what is meant by "training, advising, assisting" as opposed to combat, but some Afghans believe that the international military forces will not leave, either for their own interests (i.e. minerals, geopolitics) or because they won't let everything go back to the way it was in the 1990s and jeopardise all that has been created. Under this scenario, there would be a reduction but not a complete withdrawal of forces. As described elsewhere, due to the lack of a context of conflict, Balkh has benefited from the presence of international forces without the punishing consequences of their military activities, so the population may be less eager for their departure. The major expansion of the base at Camp Marmal/Pratt reinforces doubts about the extent of the drawdown. Those Afghans who were more worried about a return to the old conditions seemed more willing to believe that the forces would in fact withdraw. The general sense was that ISAF might not have had an active role in maintaining security, but that its presence might have had a deterrent effect.

Second, there was a range of views on the extent to which Balkh would simply follow the path of the rest of Afghanistan. Consistent with the "Balkh is different" narrative, some said that Balkh would remain relatively peaceful regardless of what happened elsewhere in the country. This may be based on the relatively stability of the last decade as well as the experience of most of the civil war years. Most of those who expressed an optimistic viewpoint seemed to link it implicitly or explicitly to confidence in Governor Atta and his ability to maintain order. Others said that the province was not an island, and would naturally be affected by what happened in other provinces.¹³⁰

A third factor affecting security will be the 2014 presidential elections and the political deals expected to go with them. As elections approach, it is likely that Kabul will try to get more

128 AISA, "Estimating Business Fixed Investment."

129 See Goodhand, "Contested Transitions," Holmberg et al, "Strategic Conflict Analysis," and Matthieu Aikins, "Contracting the Commanders: Transition and the Political Economy of Afghanistan's Private Security Industry" (New York: Center on International Cooperation, New York University, October 2012).

130 Security perceptions of individuals may not be important analytically, but if they reflect attitudes towards the future they are relevant in pointing towards the types of economic decisions they will take in the years ahead.

loyal people in place in the provinces, which may lead to tensions. If the elections go well and produce a reasonably credible outcome and a legitimised national leadership, a certain level of optimism will be created. If, on the other hand, the elections more resemble the 2009 ones, with significant cheating, protracted wrangling over the results, and ultimately a polarized population, pessimism will be reinforced.

Finally, another potential source of instability is the disposition of the former militia fighters, some of whom have been bought off or co-opted and absorbed into private security companies or in some cases “officialised.” The persistence of the *jihad*-era militias in some form and their links to powerful players has been widely blamed on the shortcomings of DDR, which in turn have been ascribed to lack of political will and commitment on behalf of both Afghan and international interests, given the linkages of Afghan officials to armed groups and the use that international forces found for them in military/security operations in the south and east.¹³¹

While much of the population is wary of the consequences of the deployment of *arbaki*¹³² composed of elements of the former militias, there are differences in views between different actors. As summed up by Giustozzi:

*The debate concerning militia forces in the north mirrored the national one: the educated class, the traders and in general the urban population were worried about the re-emergence of ill-disciplined, factionally aligned armed groups legitimised by government support. The strongmen were on the other hand very happy to be able to re-mobilise at least in part their armed forces and have them legitimised by government sponsorship.*¹³³

Relative to urban Mazar, those in rural areas were more concerned about this factor. Many in Chimtal and Char Bolak said that the deployment of *arbaki* had improved the security situation, but that this was unlikely to be sustainable in the long run, especially without the international funds to pay for them. As an example, a number of persons mentioned that about three years ago in Alburz *arbaki* groups had been formed and received weapons from the government. After about a year, they had switched sides and were now opposing the government.

6.2 Uncertainty, risk and lack of confidence

Whether due to security or other factors, one of the most daunting problems that Afghanistan faces is the widespread lack of confidence in the future. At the national level, the sharp weakening of the Afghani-US dollar exchange rate (22 percent between October 2010 and May 2013) indicates an increasing demand for dollars. While in principle the weakened Afghani would help exports, higher prices for imports (i.e. fuel and wheat) will greatly outweigh the benefits.¹³⁴ There have also been reports that as early as mid-summer the Afghan government will be facing a cash-flow crisis, which is attributed to tax evasion by government officials and other well-connected individuals, increasing diversion of customs revenues by officials at the provincial level, and a contraction in the economy.¹³⁵ This in itself may reflect a lack of confidence and a decreasing willingness by provincial officials to play by the rules.

In Balkh, this lack of confidence was borne out in almost all interviews and by whatever empirical information was available. First, there has been the well-noted but empirically poorly measured crash in the land and property market, estimated at between 30 and 60 percent. With potential buyers waiting for 2014 and anticipated lower prices, many owners who purchased land as investments are unable to sell; many told personal and third-party tales of having cash tied up in real estate and losing significant amounts of money when the market declined. At present, households may prefer to rent rather than own, and thereby not have liquidity tied up. Additional uncertainty is created by the weak financial condition of many of the *shahraks* and their questionable legal status.

131 For an analysis of the shortcomings of DDR, see Mark Sedra, “Afghanistan and the DDR-SSR Nexus,” in *Monopoly of Force: The Nexus of DDR and SSR*, Melanne A. Civic and Michael Miklaucic, eds. (Washington, DC: Center for Complex Operations, Institute for National Strategic Studies, National Defense University Press, 2011), 252.

132 *Arbaki* were originally tribal security forces indigenous to the southeastern Loya Paktia region, but the term has been commonly used to refer to just about any irregular local security forces, including the ALP.

133 Giustozzi, “Resilient Oligopoly,” 44.

134 Shahla Murtazaie, “Afghan Currency Value Decrease Raises Concerns,” *ToLo News*, 30 April 2013.

135 Matthew Rosenberg, “Afghan Government Faces Cash Crunch,” *New York Times*, 2 May 2013.

Second, the contraction in the construction sector over the last 12-24 months has led to a number of companies becoming inactive or going on “stand-by,” which has meant termination of staff. Again, hard numbers are hard to come by, but informed sources involved in the sector suggested that there had been a 50 percent reduction in construction activity since 2010. The construction boom appears to have peaked in 2009-10, then fell off sharply when the 2014 Transition was announced. Without good data, it is not clear that the decline dates precisely from the announcement, but this is a very strong association in people’s minds, and it underlies a major part of the Transition narrative, which is likely in turn to influence economic behaviour. If the 50 percent estimate of reduction is accurate, this would reinforce the notion that the fall in confidence by itself would have real effects, as there has not yet been a 50 percent decrease in project funding. At a minimum, there will be a shakeout of some of the smaller, less qualified (or less well-connected) firms. According to one company owner:

The small construction companies that were established only for implementation of international donors’ funded projects without having professional staff will not be able to continue their activities, but those companies which earned a lot of money and have equipment and professional staff may continue their business with local projects for some time. They may also change their business inside Afghanistan or invest outside the country such as UAE. As a general idea when we discuss Afghanistan during the next 24 months and after 2014, everybody is pessimistic and can’t see a better future.¹³⁶

One of the largest architectural, engineering and construction companies in Afghanistan, which had completed US\$56.7 million in projects, said that they were thinking of leaving Balkh because they may not have projects in the future. Another large building and road construction company (Kahkashan) had recently established a cement factory in Uzbekistan, providing an example of firms diversifying but also how, under better conditions, they might build the cement factory in Afghanistan. Some companies noted that while there may be continuing projects through the government in the future, it was difficult to deal with the government, especially in obtaining payment for work done. Most likely the big players will remain active through their personal relationships and networks.

Third, there has been a sharp fall in the sale price of vehicles, especially personal luxury vehicles. Vehicles which two years ago cost \$8,000 are now on the market for \$2,500-4,000. Traders in Mazar reported that due to lack of demand there had been a decline in the number of vehicles coming from Dubai. The weakening of the vehicle market was attributed to consumer caution due to lack of confidence in the future, and to the idea that people cannot afford the running costs, so are therefore giving up their vehicles.

A number of middle-class respondents who worked for aid agency-related programmes also described the decision to withdraw their children from fee-paying private schools and re-enrol them in public schools, which provided an inferior education but were less costly. These decisions were made both by those who had already lost their jobs as well as those trying to cut down on household expenditures “just in case.”

Finally, virtually all respondents noted that there had been a hiatus in investment (used in the informal rather than technical sense of the term) and that this would persist until at least 2014. Large businesses were on “stand-by,” waiting to see what would happen. At the Balkh Chamber of Commerce and Industry, staff said that it was difficult to convince business owners and potential foreign investors that there would be any market at all after 2014. The one exception to this view was AISA, which said that there was more investment in 2012 than in the previous year; at the national level, AISA statistics showed a 26 percent increase in investment during 2012.¹³⁷ Others have cited AISA’s figures from earlier in 2012, which showed that capital spending by newly registered companies was at its lowest rate in at least seven years and that it was only about 13

136 Interview with construction company owner and engineering faculty member at a local university. At the national level, one report said that the number of construction companies had fallen from a high of 10,000 to 3,000. See Nordland and Rahimi, “As NATO Nears Exit.”

137 “Investments Increase 26% in 2012: AISA,” Tolo News.com, 8 January 2013. <http://www.tolonews.com/en/afghanistan/8997-investments-increase-26-in-2012-aisa>. As noted elsewhere, some have pointed out the weaknesses in AISA reporting. See AISA, “Estimating Business Fixed Investment in Afghanistan.”

percent as its peak in 2006.¹³⁸ While virtually all respondents linked the waning confidence to the military drawdown, other analysis had noted a slowdown at least one year earlier. (See end of Section 5.2.)

Respondents noted that at present the historical preference for trade over longer-term productive investment had re-asserted itself, as buying and selling with a quick turnover was a safer choice in an uncertain environment.¹³⁹ Other research and analysis has noted similar attitudes. For instance, SHC cites construction company personnel elsewhere in the north as saying “[businessmen] mostly focus on short-term benefits: [they] don’t want to invest money in complex structures, with multiple people, for several years. We don’t have enough business skills for it and it would be too risky in such a [volatile] environment.”¹⁴⁰ Another natural effect of uncertainty may be the deferral of repair and maintenance activities on capital equipment; as noted by one report, with a high discount rate, “many companies are uncertain of the future and would rather deplete assets than reinvest in them.”¹⁴¹

Many said that the Kabul Bank debacle in September 2010 along with the wider problems unearthed by a sector-wide audit which showed “considerable weakness at all levels of banking governance and operations”¹⁴² had a major negative influence and continued to cast a shadow. One specific measure of this is that at the national level commercial loans, which had nearly doubled annually prior to the crash of the Kabul Bank, have declined by 15 percent since then.¹⁴³ Similarly, over the last several years Afghanistan’s microfinance sector has faced its own difficulties, including a decline in the number of active borrowers and bankruptcy of several institutions.

6.3 Uncertainty about Transition reinforcing historical and current constraints

The caution with which Afghan economic actors are facing 2014 also reinforces underlying and systemic characteristics of the economy that have historically limited broad-based growth. In fact, often what is described as being a “security” issue is more appropriately described as an institutional or governance one (i.e. rule of law, influence of commanders). Interviews with Balkh’s business leaders revealed concerns that are consistent with the findings of other studies and of historical experience. The GIZ-funded regional growth diagnostic makes this point in a somewhat different way when it notes “it is hard to distinguish between the effects of corruption and insecurity because they have been co-dependent and self-reinforcing.”¹⁴⁴

Perhaps the most important factor is the lack of faith and confidence in formal institutions, whether banks, government regulatory bodies, or trade groups which should ostensibly be representing members’ interests. It has been widely observed that economic actors rely primarily or even exclusively on personal and family networks for a range of services and guidance. For example, according to SHC, among the 167 firms sampled in Balkh, more than one-third of full-time employees were relatives of the owner and most used personal channels (73 percent friends, 69 percent relatives) in recruiting.¹⁴⁵ (The concentration of relatives is likely to be even higher at more senior levels of the companies.) This is also reflected in the structure of businesses, which tend to be simple pyramid structures headed by own family without any specialisation (e.g. administration, human resources), and often are sole proprietorships which rely on their own internally generated funds for investment and operations. For example, SHC reports that in Balkh 89 percent of companies were either sole proprietorships or “partnerships,” and 95 percent of company owners either created it himself or inherited it. These characteristics reflect the lack of trust in formal institutions.

138 “In Afghanistan, Businesses Plan Their Own Exits” New York Times, 31 March 2012, www.nytimes.com/2012/03/31/world/asia/businesses-may-flee-afghanistan-after-troop-withdrawal.html?pagewanted=1&_r=2&ref=global-home.

139 Maxwell Fry notes a similar orientation throughout Afghanistan’s modern economic history. See Fry, “Afghan Economy.” This is discussed further below.

140 SHC, “Commercial Law Needs Assessment,” 24. SHC also mentions positive/encouraging levels of confidence, which is an apparent contradiction.

141 ASMED, “Northern Economic Corridor,” 19.

142 World Bank, “Afghanistan Economic Update,” October 2012.

143 Ibid.

144 Lea et al, “Constraints to Growth,” 43.

145 See SHC, “Commercial Law Needs Assessment.”

A recurrent theme in Afghanistan's economic history has been the moving back and forth between emphasis on the state and private sectors (e.g. Daoud's nationalisation of the banks in 1977), often backed by powerful individuals who are keen to protect or improve their interests against perceived rising threats. While much of the emphasis after 2001 has been on encouraging firms to enter the formal economy, historically in Afghanistan formalising or expanding has had risks, primarily in exposing assets to appropriation either through predatory corruption by government officials or their associates or more catastrophically through expropriation or re-distribution should a new government or administration come into power. Senior officials in Balkh described the successive generations of businessmen or traders which were created or strengthened from 1978 onwards, when many traders and businessmen left Mazar (and Afghanistan) because they were harassed and called "feudals." The new businessmen were created largely through political connections, and their personal benefits were often to the detriment of others and the larger economy. These included individuals and groups who had personal, political and ethnic affiliations with various factions and personalities. Assistance and preferences included allowing them to make purchases or take loans at the official exchange rate then sell the goods or exchange the currency at black market rates, which often resulted in a 20-fold profit. Another class of businessmen, albeit many of them highly inept, was created after 1992, when state property and resources fell into the hands of anyone who could grab them.

The GIZ 2011 regional growth diagnostic refers to some aspects of this as "appropriability - specifically by the microeconomic risks of the rule of law, taxation and corruption."¹⁴⁶ It attributed this to a number of factors, including the unforeseen consequences of creating the Large Taxpayer Office, namely "a predatory and unpredictable tax environment," and the more general increase in corruption. As another example, the 2010 roll-out of the city services tax to be collected by municipalities has been viewed sceptically in some towns; it is seen to discourage trade and in addition the disposition of the collected revenue has been questioned. Most analysis has noted the need to develop laws and regulations, but often does not emphasise that transparent and fair implementation is just as important as the laws and regulations themselves. According to one trader:

We in Afghanistan have a workers' union, labor laws, and international labor laws are present. But we cannot correctly implement the mechanism...The responsibility of the state is basically the formulation of laws, proposing policies, monitoring the execution of laws, extension of commercial linkages, laying the groundwork for commerce, laying the groundwork for investment in the sectors of production and supporting that, marketing, and execution of ease of market functioning and for produced goods. At present, the state has not functioned according to its own responsibilities. The presence of bureaucracy and widespread corruption is the source of all of the problems.¹⁴⁷

As an example, while most studies that have looked at the business or investment climate in Afghanistan have identified land as a major constraint, the GIZ study concluded that the real problem was related to insecure tenure, as well as price inflation in part due to commanders or drug traders purchasing at high prices as an outlet for their ill-gotten gains –factors which are ultimately related to poor governance. More broadly, the study concluded that finance, transport, or the lack of trained personnel/human capital were not significant constraints.¹⁴⁸

6.4 Likely effects of reductions in international spending and presence

6.4.1 Current and projected aid

In 1390 (2011-12), disbursements of foreign assistance in Afghanistan reached their highest level, \$12.9 billion in 2011, a more than doubling of 2009 levels driven largely by the US "civilian

¹⁴⁶ Lea et al, "Constraints to Growth," 5.

¹⁴⁷ Interview with head of trading company, Mazar.

¹⁴⁸ The study made the interesting observation that finance was not considered a constraint, which simply means that there were not the other opportunities for expansion that might render the lack of finance a constraint. Similarly, that firms in Mazar reported transport costs to be more serious than the other northern cities may indicate that they have progressed to a point where transport has become a binding constraint. For instance, Badakhshan firms do not report transport to be such a serious problem, despite the road links being the weakest in the region.

surge” which accompanied the surge in troops. While the commitments made at the July 2012 Tokyo Conference of \$16 billion for 2012-15 for the non-security sectors carried the message that development funding would continue even after the drawdown of military forces, under almost any scenario the next few years will see fairly steep reductions in the amount of aid provided to Afghanistan. Moreover, there is a fear that the donors will use shortcomings in anti-corruption, democracy, and human and women’s rights as an excuse to avoid their commitments. Also, in the absence of the approximately 100 civilian-military teams previously present, there may be a chain of reduced international forces leading to reduced ability to monitor and provide assistance, further leading to reduced assistance, and finally to reduced employment. This is likely to be less severe in provinces such as Balkh, however, where development projects have been less closely tied to and dependent on the international military.

Some broad strokes can be drawn with respect to the major donors in Balkh. The doubling of German development assistance to a projected EU430 (€) million per year (aside from humanitarian and emergency/transition aid of about €20 million per year) starting in 2010 made Germany Afghanistan’s third largest donor. Germany is involved in a range of sectors, including education, peace and security, economic development, water supply and sanitation, energy, health, governance and culture, and has been actively involved in police training. A significant proportion of the €430 million will go to Balkh, with major increases in GIZ and other agencies in the area. At the 5 June NATO defence ministers’ meeting a concept of operations for a post-2014 “Resolute Support” mission to train, advise and assist was announced. While this depends on the signing of the BSA, Germany, which currently has approximately 4,200 troops in Afghanistan, was the first to pledge its intention to station 600-800 troops, split between Kabul and Mazar, for 2015-16 without any reference to the BSA.

Sweden will also be increasing its bilateral development cooperation with projected amounts at the national level of US\$97 million in 2013, \$100 million in 2014, and \$133 million per year from 2015 onwards. Sweden currently focuses primarily on democracy and human rights, education and private sector development. In terms of funding channels, Sweden divides its funds so that 42 percent goes to support national programmes, 22 percent through the UN system and 30 percent through NGOs.¹⁴⁹ Until now, Sweden has earmarked a percentage of funds (27 percent in 2010) for the four northern provinces under the view of the Mazar PRT, channelled through some of the channels mentioned.

At the national level, the US request for USAID funding for \$1.85 billion for FY2013 was roughly the same as was appropriated in 2012, although it was 15 percent less than 2011 and only half of 2010. While some of the larger USAID programmes intended to improve the economy (e.g., IDEA-NEW, Afghanistan Small and Medium Enterprise Development) may be winding down, others such as Afghanistan Credit Enhancement and Financial Access for Investing in the Development of Afghanistan have continued. Estimates are that USAID has been spending \$24 million annually in Balkh between 2009 and 2012, with spending peaking at \$27 million in 2011. USAID has launched a number of major programmes, including Assistance in Building Afghanistan by Developing Enterprises, a four-year \$105 million national programme intended to encourage private sector job creation, investment, development of SMEs, and improvement of the enabling environment, and which will be active in Balkh, and has just put out to bid the Regional Agricultural Development Program - North and West (RADP), a five-year programme which will focus on Balkh and five other provinces, including Jawzjan, Samangan, and Baghlan, which are considered part of the “northern economic corridor.” RADP’s emphasis is on food security/wheat production, high-value crop value chains, livestock, and the enabling environment.

Additional programmes include the World Bank’s National Horticulture and Livestock Project, which was expected to start in early 2013 as a follow-on to the Horticulture and Livestock Project, and the UK Department for International Development-funded Comprehensive Agriculture and Rural Development Facility, which is working in Balkh and Dehdadi districts.

Regardless of the present or future levels of aid, there is a wide perception that existing projects are phasing out, and development agency staff complained about the lack of even minimal resources to accomplish programme objectives or start new initiatives.

149 “Donor Coordination Report,” 2010.

In discussions of the prospects for the economy, government officials tended to think in terms of projects rather than sectors. Respondents also noted that the current economy was based only on contracting – not on factories which would create employment. This sense has been borne out by other analysis.¹⁵⁰

As a very rough attempt to gauge the importance of development programmes in local economic activity, if Balkh's provincial GDP is \$878 million (based on a per-capita allocation of national GDP), development spending represents between 8 and 17 percent of the provincial economy, not including multiplier effects.

6.4.2 Base employment, contracts, and contract-related employment

As noted above, systematic information on international military spending is elusive, opaque, and notoriously unreliable. Obtained numbers were obscure, unverifiable and often contradictory. Still, it is clear there will be direct and secondary effects on the local economy as a result of the drawdown of the military and development presence through reductions in base employment and contracts for base maintenance and off-base construction projects for buildings and roads. At the same time, sources in NATO noted that assessing the effect of the closure of Camp Marmal might be a somewhat "theoretical" or speculative exercise, as base consolidation across the north might even increase its importance. The best-known source of funding related to the international military forces is the Commanders Emergency Response Programme (CERP), but there is also on-base employment, construction, and the supply chain for the international military. The two major categories of contracts are for base maintenance and off-base work such as construction. From the perspective of the construction companies, the US Army Corps of Engineers was considered the largest and therefore the most desirable source of contracts.

Based on the disparate pieces of information that are available, a very rough estimate is that a full closure of the military bases in Mazar (Camp Marmal and Camp Northern Lights [CNL]) would remove approximately \$45 million per year from the local economy. This includes estimates of \$18 million in salaries for the approximately 800-1,100 Afghans working at the two bases as well as \$27 million, which represents the roughly 50 percent of contract amounts estimated by informed sources to enter the local economy. Salary-related employment includes translators, assistants, advisors, analysts, and labourers (daily and contract), with the majority hired through Afghan human resource firms. Most of these are considered well-paying jobs, and some of the more senior ones also carry the possibility of resettlement outside of Afghanistan, a more and more attractive benefit given the increasing search for exit strategies.¹⁵¹ The main categories of on-base contracts are facility operation, maintenance, infrastructure, and local purchases. Services provided by local contractors include human resources, rental of non-tactical vehicles, and some base operations and maintenance. The extent to which this money has a multiplier effect depends on whether it is invested or spent locally or expatriated to Dubai or elsewhere. As a very rough indicator of magnitude, the \$45 million would represent approximately 5 percent of the above-mentioned estimate of \$878 million for provincial GDP, not including the multiplier. According to sources at the US Regional Contracting Command, there were \$2.2 million in unpaid contractor funds because of handover and communication issues.

Ironically, as discussed above, while there have been on-going complaints about the lack of military- and other international community-related spending in Balkh, the lower profile and spending of the PRT and other aid agencies will likely mean that Mazar is less affected by the drawdown than other areas in the south and east which were more reliant on PRT spending. This was noted by the World Bank Transition study and locally by sources within NATO. On the other hand, that 13 percent of respondents to the SHC/MC labour market survey believed that NGOs and international organisations were the largest employers in Mazar suggests that the international presence is psychologically a large one.

150 For example, in a survey of 621 firms in four northern provinces, including Balkh, SHC (Commercial Law Needs Assessment) found that only 2-3 were involved in production or transformation. Also, in fieldwork done by the author in 2010, "contracting" was regularly given as a sector.

151 While the base jobs are relatively well-paying, the special conditions are increasingly taking their toll on Afghan workers. Delays as long as 1-2 hours getting on and off the base along with long shifts require staff to leave from and return to their homes at times which are considered unsafe.

6.4.3 Private security contractors and militias

The other relatively good news for Balkh relative to other areas of the country is that because there had been less of an expansion of private security contractors to guard military bases, convoys, and development projects, there will be fewer of them made unemployed. Without a regular source of income, such fighters are likely to turn to drugs, thievery, intimidation, and other illicit activities that discourage mainstream economic activity. Relatedly, the reduction in the flow of development and reconstruction money may put strains on patronage networks, most of which were built up by accessing project-related funding to alleviate conflict or by what amounted to bribery to go along with the programme.¹⁵² Put simply, at present the networks are still being paid, including through the ALP and other irregular forces. Moreover, the dominance of one player in Balkh means that there have been fewer competing groups, as is the case in more contested areas (e.g. Badakhshan). One question, though, is what if any effect the development of the Afghan Public Protection Force will have on the security personnel (within the Balkh administration) which have been officialised from the ranks of Governor Atta's people.

¹⁵² For a detailed discussion of the dynamics of the private security sector, including how the transition of the US from counterinsurgency to counter-terrorism may exacerbate the situation, see Akins, "Contracting the Commanders."

7. Summary, Conclusions and Policy Recommendations

7.1 Summary and conclusions

While Balkh's economy has prospered for a variety of reasons, including location and relative security, the coming 2014 Transition has put into play a set of national and local dynamics that will affect the level and mix of economic activity. Interviews with actors in the private and public sector along with analysis of available empirical data suggest that, not surprisingly, uncertainty about the future has affected all aspects of economic behaviour, especially investment and consumer spending.

The main factors which will affect the economy are security and political uncertainty. While most respondents expressed concern that the security situation might not hold, a minority felt that a number of factors, including the improved capacity of the ANSF and strong provincial leadership, would allow Balkh to remain stable and relatively peaceful. Based on the current expansion of Camp Marmal/Pratt, statements of commitment by the international community to continue development aid in place of the military, the belief that the west would not wish to jeopardise the achievements of the last 11 years, and geopolitical factors, many Afghans expressed scepticism about the ultimate extent of the drawdown. Those Afghan respondents who were more optimistic said that no one wanted to return to the dark days of the 1990s. At the same time, given the discussions in the media and the *chai khanas*, it is possible that the lack of confidence could become a self-fulfilling prophecy.

Without the context of conflict that exists elsewhere in Afghanistan, the international military in Balkh has been relatively low-key and unobtrusive, yet many believe that its mere presence off-stage has had the positive effect of keeping in check predatory local commanders and other potential sources of instability. Thus most respondents were not eager to see a full military drawdown.

Intensifying political activity at the national and international levels as 2014 approaches were reflected in Balkh by increased pre-occupation and concern about the intentions of regional neighbours. Many issues have perceived economic dimensions, including the belief that the regional neighbours are engaged in predatory economic practices, as well as a political, ethnic and sectarian tinge.

Given the current levels of anxiety about insecurity and the national political trajectory, it is not realistic to expect much improvement in the economy until after 2014. This was stated categorically by nearly all respondents, who described how both investment and consumption were largely on hold, "in case something happens." This was indicated most clearly in the construction sector, which has already seen a contraction and a reduction in the number of active companies, and which will continue to contract due to reductions in the construction contracts fuelled directly or indirectly by international spending. The reduction in construction activity affects employment at all levels, including those who rely on casual labour income and those who have found work through the backward linkages created with suppliers of construction materials. The trade and transport sectors will also be affected by the reduced demand for construction materials as well as consumer goods, the latter as households limit their non-essential spending out of concern for possible future needs.

Another indicator is the fall in land and property prices, estimated at 30-60 percent. A number of the *shahraks* (residential developments) are in financial trouble, as are the individual homeowners who incurred debt to purchase land and build a house whose value is now less than the debt. The future of some of the *shahraks* may be further complicated by their questionable legal status and the existence of multiple claimants on plots, which has the potential to lead to conflict. Additional negative indicators were the decline in the market for private vehicles (especially luxury ones) and the decisions of some middle-class parents to withdraw their children from fee-paying private schools.

There is likely to be continued flight of human and financial capital, as those who are able to protect themselves and their assets keep their options open. There also seems to be a growing

sense of awareness of the differences between those citizens who have such possibilities and those who do not, and who will therefore have to face whatever instability occurs after 2014.

One of the historical safety valves for livelihoods in Balkh, migration to Iran, has become much less attractive an option because of regional political dynamics, increasing restrictions on Afghans in Iran, and the devaluation of the *rial* (one-third since January 2009) due to western sanctions. This will reduce remittances and increase the number of unemployed in rural areas, who may migrate into Mazar, where there is likely to be less demand for labour due to the contraction in the construction sector. As in the past, Mazar may be the destination of migrants from other less-secure areas.

A decline in employment opportunities and migration may also increase pressure to relax the suppression of opium poppy cultivation. Given the livelihoods and security situation in the areas of cultivation (e.g. Chimtāl and Char Bolak), including the ambiguous role of the *arbaki*, it is hard to see any factors which would discourage cultivation. Especially if the goodwill capital gained by the provincial administration for suppressing cultivation becomes less important in the overall political calculus, including with the international community, this will hardly be an environment in which to maintain unpopular and economically punishing counter-narcotics policies.

At a broader level, the government and the international community were blamed for the lack of fundamental economic change post-2001: an economy based on contracting, very limited investment in production and failure to expand agriculture by utilising water from the Amu Darya. Some of this is ascribed to the adoption of the market economy, which is seen by many as the state abdicating its role, especially in job creation.

Finally, extractive industries are still at their early stages, and the extent to which they create jobs and wealth locally will depend on whether the organisation of extraction is confined to enclaves or whether it is more broadly based.

7.1.1 Positive factors

On the positive side, Balkh has a number of advantages, starting with its location and potential key role in external and internal trade—should institutional constraints be relaxed. Two specific opportunities are the potential expansion of the railroad and the possibility of acting as a conduit for Turkmenistan gas needed by Tajikistan but restricted due to political problems with Uzbekistan. In order to facilitate trade in gas between Turkmenistan and Tajikistan, there has been discussion of establishing a border crossing to Tajikistan at Taghangozar, east of Hairatan, where the Soviets built a bridge and a pipeline crossing to connect with Shahtooz-Ewanj in Tajikistan, from where there is a railway connection. The enthusiasm for additional ports is understandable, given that alongside official revenues, customs facilities also generate significant “unofficial revenue” which circulates within the provincial power structures.

The upgrading and paving of the historical road between Khulm and Kunduz currently in process has potential to increase trade between Mazar and Kunduz, which at present must go via Pol-i Khumri. While it is unclear as to whether there would be a net increase in trade between the two northern cities, or whether it might simply benefit the town of Khulm at the expense of the towns along the existing highway, this has the potential to increase economic activity. Some donors (e.g. USAID) have touted the benefits of developing the “northern economic corridor,” which runs from Pul-e Khumri to Andkhui. Improved transport links can also potentially increase the number of religious and other tourists who visit the Shrine as well as other historical and religious sites in the province.

The province’s pre-war industrial infrastructure may provide some opportunities for rehabilitation, although it is unclear how much usable capacity remains. There are also different views on what should be done with these assets, which reflect different economic philosophies. For instance, donor reports have encouraged the government to follow through with plans to privatise the Silo, while civil society groups have complained that parts of the Silo have already been given out on an *ejra* (contract) basis, which is seen as being oriented only to profits and not creating jobs. The international community now appears to be more willing to consider rehabilitation of parts of the old industrial infrastructure than was the case several years ago, as suggested by the current

US government investment in rehabilitating the Shirberghan-Mazar gas pipeline, the discussion of investment in the Kod-e Barq facility, and the rehabilitation and reconstruction of eight gas wells in Shiberghan belonging to one of the state-owned enterprises.

Decent roads, security, and infrastructure have contributed to expanded markets for agricultural commodities that work reasonably well, notwithstanding certain forms of rent-seeking and non-competitive practices (see below). On the other hand, while roads enable outputs to go to markets, they have also allowed the wide distribution of imports. Despite that, however, aside from low productivity, the lack of domestic and international markets remains one of the largest constraints facing agriculture. Expanded production presents potential opportunities for small- and medium-scale agro-processing industries. After several years of greatly decreased demand, the international carpet market is again showing some signs of life, which creates some opportunity for the Balkh carpet industry, especially if it can find a way to add more of the finished product's value locally, establish marketing channels to reduce middlemen, create backwards and sideways linkages to suppliers of raw materials such as wool and dye, and use transport linkages (e.g. the expanded airport) to connect with export markets.

While the amount of funding available for programmes such as CERP may be reduced, given the ways in which this funding has been less than fully accountable and in cases may have contributed to conflict, this may actually be a positive thing, despite what it might mean for individual companies. Moreover, given the relatively diversified economy of the province and the smaller role of the international military in spending, Balkh is unlikely to face the same contraction as other provinces, where massive amounts of stabilisation funds have been distributed. According to very rough calculations, international development and military spending in Balkh is equivalent to 13-22 percent of the provincial economy, not including multipliers.

The growth of the last several years has also created a certain critical mass of human capital, expectations, and perhaps a bit stronger local identity. There has been a certain pride that the province has thrived, and most people wish for this to continue. Entrepreneurs have struggled to establish enterprises (e.g. manufacturing) in the face of many of the factors that make Afghan production non-competitive. This includes plans by an Afghan-American entrepreneur to build a glass factory at Sholgara or Dehdadi, which could be well-positioned depending on the state of the construction sector.

Compared to other areas of Afghanistan, attitudes towards the education of girls and women at secondary and tertiary levels and to their participation in economic activity are relatively supportive, with less sequestration of females within the household than in other provinces.

Among the key donors in Balkh, Germany and Sweden have committed to expanding aid funding. At the national level, Germany has committed to US\$550 million per year, while Sweden has committed to \$199 million in 2013 and \$133 million per year from 2015. Significant portions of this funding will be programmed in Balkh. USAID has requested \$1.85 billion for all of Afghanistan in 2013, but it is not clear what proportion of this would go to Balkh.

7.1.2 Additional factors

To realise the potential for broad-based economic activity envisioned by the government and the international community, a number of constraints must be resolved or relaxed. Some of these are common throughout Afghanistan, while some are specific to Balkh.

Competition from cheaper regional imports is seen as one of the most important constraints on economic activity, from agro-processing to plastic production. The massive trade imbalance reflects the highly uneven trading relationship enjoyed by the neighbours in the market for consumer and other exports. While Afghanistan's comparative disadvantages have been well documented, the regional neighbours are accused of product dumping and predatory pricing explicitly targeting emerging Afghan industries (e.g. biscuits, tomato paste, plastic containers, cement) which might compete with imports, while the government is faulted for an inadequate response in providing infrastructure, imposing import tariffs, negotiating transport rights, and generally defending Afghan commercial interests. The restrictions on Afghan vehicles from traveling on Pakistani roads and other places is ascribed to anti-competitive behaviour rather

than the official explanation of lack of insurance and the poor quality of Afghan vehicles. In the intensifying political climate, these economic issues are put in the context of suspicions of the regional neighbours.

At the same time, there is the need for an effective and credible institutional infrastructure for inspection and certification for outgoing products, especially for those shipping by air to destinations beyond the immediate regional neighbours, as well as industrial facilities for cleaning, sorting, drying, and storage of agricultural production in order to create incentives and allow Afghanistan to add value in the types of processing currently being done by its neighbours.

Aside from the uncertainty related to the 2014 Transition, many of the constraints to economic activity are related to poor governance and the historical relationship between the public and private sectors. This includes non-enabling or even predatory behaviour by officials and what is viewed as insufficient support for business activity. It also includes the sharp swings of support from one favoured set of actors or interest groups to another at times of political change. The overall lack of faith in institutions helps to explain firms' reluctance to expand or even to go formal in the first place.

Also, while the provincial leadership is viewed largely as a positive factor in the province's success and most would see Governor Atta's removal as a destabilising factor, the downside effects of anti-competitive behaviour (e.g. control of fuel imports, alleged extraction of "shares" in business activity, and the general land and business mafia) and the effect of poor road governance on the trade and transport sectors are hard to fully assess or measure, although they are certainly real.

Finally, a combination of factors—growth, poverty, and weak institutions—has resulted in a number of serious environmental issues. The largest environmental question hanging over the province is whether scarce water resources can support the growing urban population of Mazar. In addition, the location of the *shahraks* has been determined opportunistically by where powerful people have been able to obtain land, not by any careful planning process. The historic floods this spring just east of the city were said to have occurred in large part because landowners built petrol stations, *saraís*, and other buildings along the road and thereby blocked water diversion culverts (*selbord*) which would otherwise have channeled the water into the desert. Brick and gypsum plants also use dangerous substances such as old tires for fuel. Due to depletion of *hing*, the administration has banned collection for the last three years, although this was not likely completely adhered to. Riverbank erosion is reducing agricultural land and increasing the risk of flooding.

7.2 Recommendations

A number of basic recommendations emerge from the current research in Balkh as well as from the body of analysis that has been done on Transition more generally. While the uncertain time of Transition creates additional dynamics, it is difficult to disentangle those dynamics from the effects of the well-documented reality that poor governance has historically had a dampening effect on economic activity.

- **Avoid rapid reductions in international funding:** To reiterate the obvious and oft-repeated, the international community should avoid rapid reductions in financial resources, as the antecedents for this in Afghanistan's history have been devastating. Reducing the anxiety about the looming "fiscal cliff" of 2014 would do more to encourage investment and discourage capital flight (financial and human) than anything other than security. It would also potentially reduce the extent to which anxiety becomes a self-fulfilling prophesy. While a time of great potential change and pervasive uncertainty is generally not the time for major investments, given the role of uncertainty and lack of confidence, significant programmes and projects would contribute to the building of some confidence. For instance, the development of a long-term capital fund that could partially guarantee carefully evaluated and selected investments might help to build confidence and generate some activity.
- **Be realistic about prospects for reform—for both the Afghan government and international institutions:** While the dialogue continues between the international community and the

Afghan government on corruption, there has to be a realistic assessment of the extent to which institutional reform can happen under the present conditions. While the international community is insisting it will continue with a more conventional development programme post-2014, the writing is on the wall about reductions in funding, which will reduce the amount of leverage from the international community. Practically, this will mean less influence in appointments, in removing corrupt and ineffective officials, and in disarming and disbanding illegally armed groups. Aside from direct corruption, especially for officials who perceive that they are on the way out, as the 2014 presidential election approaches there is increased motivation to use resources as patronage. For the international community, the last 11 years are full of examples of the use of money as an instrument to achieve short-term objectives while unintentionally undermining long-term stability. While aid officials insist that lessons have been learned, there are doubts as to whether strategic thinking will override individual agency and institutional interests. Given the shortening timeframe, there may be even more of a tendency to focus on short-term objectives.

- **Avoid creating opportunities for rent-seeking:** Relatedly, development partners should be careful to make investments that do not provide openings for rent-seeking and opportunistic behaviour. As one of the constraints on economic activity is the tendency of the business-political nexus to enforce a type of limited access order, careful consideration (including conflict analysis) of investments should be encouraged. As one example, the need for a third industrial park in Mazar should be carefully examined to determine whether it would encourage economic activity or simply provide an opportunity for well-connected individuals to develop land using public resources.
- **Explicitly incorporate employment and human capital development in projects:** Development partners should proactively incorporate criteria such as job creation and on-the-job human capital development in project formulation. The construction of the Hairatan-Camp Marmal railway, which was constructed entirely with foreign workers, is perhaps a good example of a missed opportunity, and where public policy suffered from conflicting objectives or even took a back seat to personal or institutional interests. Incorporation of such criteria would avoid such missed opportunities for putting people to work and upgrading their human capital.
- **Explore possibilities for constructive de-concentration:** Despite sensitivities about fragmentation, in recent years there has been more willingness to tolerate discussion of centre-provincial relations. The division of responsibilities between the centre and the provinces may also become an item of discussion or negotiation during the Transition and election processes. While de-concentration is not a panacea, opportunities should be sought to free local economic actors to act more nimbly. Aside from the usual arguments of efficiency and local knowledge of needs, there has been a fraying of trust between the centre and the provinces, and therefore providing more scope for local decisions could reduce some of the resentment felt towards Kabul.
- **Negotiate broader social benefits with international firms:** To try to assure broad social benefits, encourage a firm negotiation process with international firms seeking to extract mineral resources in order to balance competitiveness with social benefits—while not creating opportunities for rent-seeking or protection. Given Afghanistan’s non-competitive position, a bit of “inefficiency” that allows for local procurement and training of Afghans should make up an implicit subsidy, although this should not be an excuse for blatant protectionism or special interests.
- **Encourage mechanisms for social accountability:** Relatedly, given the political and economic concentration of power and influence, help to encourage a non-destabilising role for social accountability mechanisms that can contribute to broadening the social benefits of future extractive and other economic activities.

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