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# Building legitimacy and state capacity in protracted fragility: The case of **Afghanistan**

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Commission on  
**State Fragility, Growth and Development**

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## About the commission

The LSE-Oxford Commission on State Fragility, Growth and Development was launched in March 2017 to guide policy to address state fragility.

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# Background

## 1

In late 2001, Afghanistan had a failed state, weak and fragmented, and unable to provide either effective services or protection to its citizens. The economy had contracted due to more than two decades of war. The World Bank in 2002, estimated the total cost over the period of conflict, measured in terms of lost growth and the cost of humanitarian assistance as well as military expenditure, to be \$240 billion.<sup>1</sup> More than two-thirds of the population were either displaced or took refuge outside Afghanistan, especially in Iran and Pakistan. A war economy had emerged which transformed the socio-economic dynamic of the country making post-2001 recovery and state-building a daunting task.

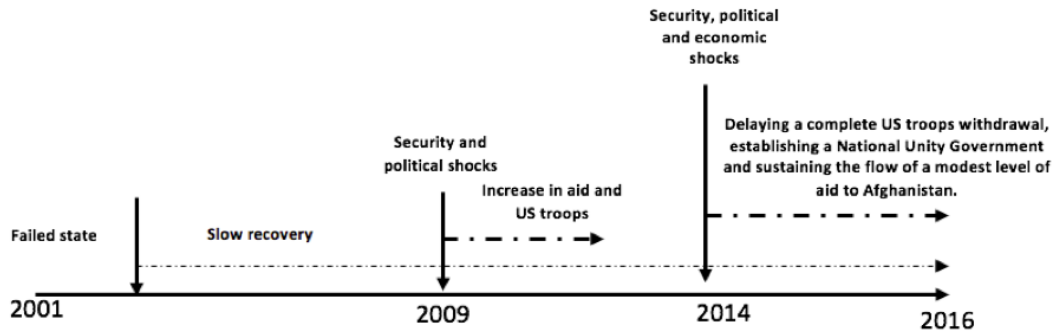
The immediate tasks in 2002 were to stabilise the country and build a legitimate and functioning state, and a viable economy. The war on terror, however, dominated the US and its allies' engagement in the country. Despite some significant progress in building state institutions and infrastructure as well as expanding public services, Afghanistan remains fragile and highly susceptible to shocks. In essence, it exhibits some of the characteristics of state fragility:

1. The Afghan government suffers from a deficit of legitimacy
2. The state has weak fiscal and legal capacities
3. Private investment and economic growth, especially since 2014, has fallen dramatically
4. Insecurity has reinforced both the state's weakness and deficit of legitimacy.
5. The state exhibits low resilience to political, security and economic shocks.

Therefore, despite the slow recovery since 2001, the security and political shocks in 2009 and 2014 were significant setbacks which increased the risk of collapse into a failed state. Nonetheless, the Afghan government and international community, in particular, were able to mitigate the risk by establishing a National Unity Government (2014) and committing to maintain the flow of a modest level of aid and military support for sustaining the gains respectively (see Figure 1).

<sup>1</sup> World Bank, "Two Decades of Conflict Cost \$240 Billion: Now Afghanistan Will Need \$27.5 Billion to Recover, World Bank Group, Press Release, March 30, 2004.

**Figure 1: Afghanistan transition since 2001**



It is crucial to note that some of the causes of state fragility have their roots in Afghanistan’s modern history. These include exclusive political institutions, the unsustainable fiscal basis of successive regimes, the subsistence-based economy, the landlocked nature of the country and its complex social mosaic, along with armed conflicts and the rivalry of great powers for domination of the region resulting in multiple invasions.<sup>2</sup> While the key dimensions of state fragility varied over time, in the last two decades following the Soviet invasion in 1979, state fragility deepened. State and non-state violence and repression became dominant, and state capacity deteriorated. These developments hampered private sector development and further increased the vulnerability of the country to political and economic shocks.

In late 2001, a new political order was established. A small number of US troops in alliance with the anti-Taliban resistance armed forces deposed the Taliban regime, which had hosted Osama Bin Laden – the leader of Al Qaeda, from power. The new government, with aid and technical assistance from the international community, implemented some major reforms. Efforts were undertaken to reform the public financial management system and key state institutions (e.g. finance, health, education, police, army, and judiciary). The delivery of public services was also expanded.

While Afghanistan was on an upward trend between 2002 and 2005, the upswing slowed down thereafter. The US and its allies’ attention in particular, diverted from Afghanistan after they invaded Iraq in 2003. The Taliban insurgents, with support from Pakistan, were able to reorganise and increase their attacks. In response to the deteriorating security situation, the US eventually increased the number of troops and its development and military aid directed to Afghanistan.<sup>3</sup> Additional aid and troops helped to stabilise the situation to some extent, but the plan to withdraw from Afghanistan by 2014 created a sense of uncertainty. This situation along with a sharp decline in the flow of aid to Afghanistan and a disputed presidential election in 2014, referred to as a triple transition, increased the level of threats and put many of the gains at risk. The international community in response, adopted some stabilizing measures, such as sustaining the flow of a modest level of aid and delaying the complete withdrawal of US troops. Afghanistan, however, still faces social-economic challenges predicated on

<sup>2</sup> Bizhan, N. (2014), “Re-engaging in a Fragmented Context: Development Approaches and Aid Modalities in Afghanistan, 2001-2004”, in *Failed, Fragile and Pariah States: Development in Difficult Socio-Political Contexts* ed. Anthony Ware (London: Palgrave), 205.

<sup>3</sup> “American Forces in Afghanistan and Iraq,” *The New York Times*, June 22, 2011.

underlying state fragility.

Afghanistan is highly dependent on foreign aid. Even though the country is potentially a resource-rich country, its resources, estimated to be around \$1 trillion,<sup>4</sup> have not been fully utilised – this takes time and enormous investment. Where resources have been utilised, however, it has fuelled local conflicts and rivalry over the control of such resources. The informal economy is huge, but is dominated by the opium industry that has fuelled and in some cases reinforced corruption and insurgency. Deteriorating security has increased the cost of investment and business. The recent fall in private investment and economic growth are some examples. This situation creates a sense of uncertainty and has forced a large number of Afghans to migrate, especially to Europe, leaving their communities inside the country. The following sections examine in detail the five key dimensions of state fragility including policy responses and outcomes post-2001 Afghanistan.

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<sup>4</sup> Risen, J. "U.S. Identifies Vast Mineral Riches in Afghanistan," The New York Times 2010.



# Reconstructing legitimacy

## 2

Two decades of war has severely undermined different sources of political legitimacy in Afghanistan. The reconstruction of legitimacy in 2002 was therefore a daunting task, which in particular, required a redefinition of legitimacy to take into account the socio-political changes. The different forms of political structures in the late twentieth century (constitutional monarchy, republic, communism, Islamic theocracy) failed to provide lasting stability. For most of its modern history, Afghanistan suffered from violent transfers of power, resulting in the deposition or killing of its predecessor leaders. Because of the role of political parties in armed conflict (since 1978), people lost confidence and trust in these parties, perceiving them as a major driver of factionalism and patronage.

External intervention has also affected state legitimacy. Both the Soviet invasion of Afghanistan in 1979 and the financial and military assistance by the US and its allies, including Saudi Arabia, to the mujahidin groups, who were fighting the Soviet-backed Kabul government, while on the one hand eroded the legitimacy of both the government in Kabul and the mujahidin groups respectively in the eyes of people, and on the other, created (or exacerbated) new forms of legitimacy through patronage and coercion. Conflict transformed both the economy and local actors. It replaced local notables, such as tribal chieftains and khans (landlords), with new actors and commanders, who had access to the international system and weapons. This situation helped the emergence of a war economy, in which military aid and revenue from the narcotic industry, enhanced the coercive power of local actors and their fiscal autonomy from local communities.

The two distinctive tasks in post-2001 were how to build legitimacy and, given the lack of it, how to manage it. Elite bargaining and consensus building through ad hoc mechanisms as well as traditional means of representation (Loya Jirga, tradition grand assembly) were used to achieve the latter, while elections were emphasised for the former. Reliance on traditional means of legitimacy partially presented the view of some of the local actors. But a belief in the building of state legitimacy through elections was something that donors, Afghan elites, and citizens by and large shared.

On December 5, 2001, the representatives of different Afghan factional groups in Bonn-Germany agreed on a new political order based on the principles of democracy and Afghanistan's national and Islamic values. The Taliban was excluded from the process, especially as there was a strong anti-Taliban mode

in Washington and in Afghanistan, because of its protection of Osama Bin Laden, the atrocities committed against minority groups and women, and its general repression of the population. The agreement aimed to establish a new constitution, an independent judiciary, a centralised security sector, free and fair elections, and the protection of the rights of minorities (including women and religious / ethnic groups). An Interim Authority for six months and a Transitional Authority for 18 months were established. The presidential elections, adaptation of a new constitution in 2004, and parliamentary elections in 2005 succeeded this process. The constitution envisaged a hybrid system. It emphasised traditional and Islamic values as well as people's right to elect their government democratically. The US and UN emphasised a light footprint with the aim that Afghans take the lead in political transition while the UN monitored the transition envisaged by the Bonn Agreement.<sup>5</sup> This approach was by and large adopted because of the Afghans' reputation for resistance against foreign invaders (e.g. the British Empire in the 19th century and the Soviet Union in the late 20th century).

The process of constitution making was swift. The participants of the Constitutional Loya Jirga, among others, had divergent views on two issues. First, whether Afghanistan should have a Presidential or a Parliamentary political system, with a Prime Minister and limited Presidential power. Second, the type of electoral system Afghanistan should adopt: a single non-transferable system or a transferable voting one. Finally, the Loya Jirga agreed on a Presidential and non-transferable voting system. The US supported this arrangement and had signalled its intention prior to the Jirga reaching an agreement.<sup>6</sup> The electoral system limited the role of political parties. It did not require candidates to be party members.

During the interim arrangement, the leadership in the new government represented different ethnic groups and regions. This arrangement helped to improve the image of the state and make it look somewhat more inclusive. For example, the Chairman of the Interim Authority, Karzai, had four vice presidents representing four different ethnic groups (Pashtuns, Tajiks, Hazaras, and Uzbeks). The balance of power therefore forced Karzai to mainly rely on consultation and consensus building through the cabinet in deciding on major national issues. However, most of the appointments in this period were made based on political allegiance and personal ties. To this end, elite bargaining and the existing mechanisms were used to improve the legitimacy of the new government. International military and development assistance, as well as international recognition, provided the interim government with new sources of legitimacy, especially by expanding its capacity to deliver services. Despite the shortcomings in advancing an effective state-building agenda, this situation created an atmosphere of hope and revival among people, and paved the path for building new forms of legitimacy through direct participation of citizens in the process, by electing the head of state and members of parliament.

<sup>5</sup> For more information about post-2001 political arrangement see United Nations Security Council, "Agreement on Provisional Arrangements in Afghanistan Pending the Re-Establishment of Permanent Government Institutions," December 5, 2011.

<sup>6</sup> Khalilzad, Z. (2016), *The Envoy: From Kabul to the White House, My Journey through a Turbulent World* (New York: St. Martin's Press).



Reconstruction efforts and the expansion of the delivery of services further helped to improve the image of the new government, as people had not witnessed a process with such a significant scale since the eruption of war in the late 20th century.

The political parties and the state mirrored each other. The state was neo-patrimonial and the parties represented more or less networks of patronage. Appointments and resource allocation in public organisations were made based on personal loyalty and political allegiance rather than merit, wherein political parties also suffered. The design of post-2001 state building was based on short-term objectives of stabilising the country. While such an approach helped with short-term stability, it had adverse implications on institution building in the long run. For participants of the 2001-Bonn meeting, it was important to accommodate different interest groups in the state. Each interest group would try to secure as many senior positions that were possible. The government neglected how to improve state effectiveness and define the key functions of the state. Many overlapping departments emerged. For example, post-2001, four agencies oversaw coordination of reconstruction efforts — Ministries of Finance, Planning, Reconstruction, and Afghanistan Authority for Coordination of Assistance. This, along with the rivalry among different ministers and senior government officials, made intergovernmental coordination much more difficult.

## The role of elections in building legitimacy

The next step was building a modern form of legitimacy through elections. This was a major innovation in building state legitimacy post-2004. People welcomed the idea of a transfer of power through ballots not bullets. Despite the shortcomings of the system, elections were seen as the desired mechanism by the people to building political legitimacy.<sup>7</sup> Elections were not something new in Afghanistan. The country had parliamentary elections during the 1960s but did not have a fully elected government. The first Presidential elections in 2004 (with 70% turnout including 40% female) and the Parliamentary elections in 2005 (with 50% turnout) were a major success.<sup>8</sup> With few registered complaints about irregularities and fraud, those who did not win accepted the results. A Joint Electoral Management Body, that included the Independent Election Commission of Afghanistan and the UN Assistance Mission for Afghanistan (UNAMA), administered and oversaw the electoral process during the transition period.<sup>9</sup> The role of the UN as an impartial actor helped build the trust of different local actors at a time when society was highly polarised.

Elections, by and large, changed the concept of power and authority in the country. However, while the first Presidential and Parliamentary elections were a major success, the subsequent elections did not achieve the intended outcomes. The electoral process soon lost its legitimacy because of fraud and

<sup>7</sup> See Larson, A and Coburn, N (2017), "Afghan Views of Government and Elections: Legitimacy Pending" Washington: USIP.

<sup>8</sup> Independent Election Commission (2004), "Afghanistan Presidential Elections Results - 2004," Kabul: Independent Election Commission.

<sup>9</sup> Katzman, K. (2005), "Afghanistan: Presidential and Parliamentary Elections," Washington: Congressional Research Service.

irregularities. State weakness and corruption, as well as the exclusive nature of the political system, presented major obstacles. Irregularities and fraud damaged the electoral process more than the threat that Taliban's insurgency posed. The government, however, failed to learn from "teachable moments" and deliver on its promise to implement necessary political and institutional reforms. The established political system increased both the incentive to commit electoral fraud and the probability to refuse the outcome of elections as the loss tended to be very costly. In addition, the electoral administration lacked capacity. Voters were not properly registered. By 2010, for 12.5 million eligible voters, 17 million voter cards were distributed. Moreover, the way elections were designed was very costly and depended on foreign aid. The 2004 elections' estimated cost (excluding International Security Assistance Force and NGOs contributions) was \$200 million for over eight million votes.<sup>10</sup>

The 2009 Presidential elections went to the second round because of widespread allegations of fraud. In the first round, Combatant Karzai, according to the Independent Election Commission of Afghanistan, secured 49.67% of the votes. But Abdullah Abdullah, who secured 30% of the votes, refused to run in the second round because Karzai did not accept his demands for reforming the Independent Election Commission of Afghanistan, including replacing the head of the commission. While Karzai was declared the winner, Abdullah refused to accept the outcome. This process severely undermined public trust in the Afghan government.<sup>11</sup>

The second round of the 2014 Presidential elections further exposed the weakness of the electoral system. Despite threats by the Taliban to kill or cut off fingers of those who would vote, voter turnout was high at 58% in the first round. The Taliban, for instance, cut off the fingers of 11 men in East Afghanistan because they voted in the first round of elections.<sup>12</sup> As none of the candidates secured over 50% of the votes, the election between Abdullah Abdullah and Ashraf Ghani went to the second round, who respectively secured 44.9% and 31.5% of the votes.<sup>13</sup> However, the allegation of fraud in the second round severely undermined the legitimacy of the upcoming government in which Ghani, according to the Afghanistan Election Commission (which announced the result after the two candidates reached an agreement), secured 55.2% of the votes and Abdullah 44.7%. Abdullah threatened to announce a parallel government under his leadership. The Electoral Integrity Project of Harvard University categorised Afghanistan's election of 2014 as the third worst elections worldwide after Bahrain and Syria.<sup>14</sup>

After pressure from Afghanistan's major development partners threatening to freeze their aid to Afghanistan and mediation by US Secretary of State – John

<sup>10</sup> Hess, M. Pearce Laanela, T. and Maley, W. (2012), "Preparing for Elections in Afghanistan: Prospects and Challenges," ANU College of Asia and the Pacific, 12.

<sup>11</sup> For more discussion on legitimacy in Afghanistan see Barfield, T (2012), "Political Legitimacy in Afghanistan," Middle East Institute.

<sup>12</sup> DW Dari, "Taliban Angusht Yazda Rai Dihinda Ra Qatae Kardand (the Taliban Cut Off the Fingers of 11 Voters)," June 15, 2014.

<sup>13</sup> The Guardian, "Afghanistan Presidential Elections Heading for Runoff," 26 April 2014.

<sup>14</sup> See Lanzarotta, M., "Afghanistan, Syria and Bahrain the Worst Elections of 2014," News Release, 2015, <https://www.hks.harvard.edu/news-events/news/press-releases/afghanistan-syria-and-bahrain-the-worst-elections-of-2014>.

Kerry, Ghani and Abdullah agreed to form a power-sharing system referred to as a National Unity Government, with Ghani as President and Abdullah as Chief Executive. This arrangement helped to mitigate the risk of conflict. But this type of arrangement in the absence of necessary political reforms in the electoral system and governance practices made the new government ineffective. Lack of electoral fairness as well as elite fragmentation, therefore, posed a major challenge to building legitimacy. By combining data from a randomised controlled trial designed to improve electoral quality in Afghanistan's 2010 Wolesi Jirga (lower house) elections as well as data from a post-election survey of affected citizens, Eli Berman et al. (2014) found that the fairness of "elections affects attitudes of citizens towards their government directly relevant to their willingness to be governed, a contributor to legitimacy."<sup>15</sup>

In addition, widespread corruption persistently eroded the legitimacy of public organisations. People needed to pay a bribe or rely on *wasata* (connection to government officials) for accessing basic government services. A student in Kabul described the situation as follows:



In reality, there is massive corruption in government organisations, and people are upset about the situation. Government officials at the local level think that government positions are their property and heritage, and they behave with people in a very rude manner. This is the main reason for the lack of cooperation between people and government officials in most parts of the country.<sup>16</sup>

Corruption emerged as one of the most important problems in the country. According to the Perception of Corruption Index, while Afghanistan moved up four points in its score from 11 in 2015 to 15 in 2016, it nearly doubled from 8 in 2013 (Figure 1). It continues to rank highly corrupt with the same score as that of 2011 and 2008. A survey by the United Nations Office on Drugs and Crime (UNODC) in 2012, found that after security, people perceived corruption as the second most important issue for Afghanistan.



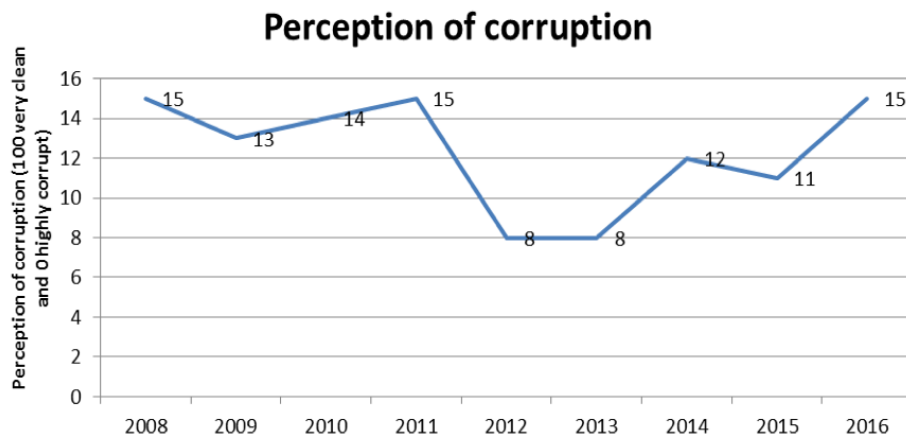
In 2012, half of Afghan citizens paid a bribe while requesting a public service and the total cost of bribes paid to public officials amounted to \$3.9 billion. This corresponds to an increase of 40% in real terms between 2009 and 2012, while the ratio of bribery cost to GDP remained relatively constant (23% in 2009; 20% in 2012).<sup>17</sup>

<sup>15</sup> Berman, E. et al. (2014), "Election Fairness and Government Legitimacy in Afghanistan," NBER Working Paper No. 19949, Cambridge: National Bureau of Economic Research.

<sup>16</sup> Larson, A and Coburn, N (2017), "Afghan Views of Government and Elections: Legitimacy Pending", Washington: USIP, p. 12.

<sup>17</sup> UNODC (2012), "Corruption in Afghanistan: Recent Patterns and Trends," Vienna: UNODC, p. 3.

Figure 2: Perception of Corruption Index - Afghanistan 2006-2015



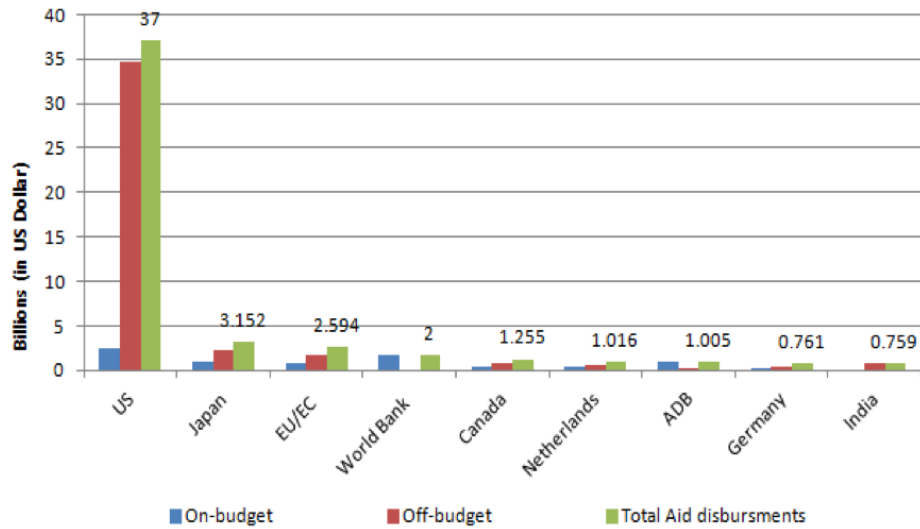
Source: Transparency International, 2015

From 2002 to 2010, donors disbursed \$57 billion in development and military aid to Afghanistan through the government budget and outside the state system.<sup>18</sup> This aid helped to expand public services, which the government was barely able to provide, having a positive effect on state legitimacy. However, while governance practices especially in the area of public financial management improved, these improvements did not significantly reduce corruption. Most of the transactions would take place outside of the formal public financial management system, which for example, did not include about four-fifths of total aid that flew into Afghanistan between 2002 and 2010. While each donor used a different approach, as Figure 3 shows, a large portion of aid was spent off-budget. The World Bank, Asian Development Bank, and International Monetary Fund channelled their aid through on-budget mechanisms while major bilateral donors mostly relied on off-budget funding mechanisms. Donors bypassed the Afghan state by and large because of state weakness and corruption. While this type of aid delivery helped to improve implementation of projects, it diverted much of political and financial resources away and the pressure to reform public institutions. In some cases, the delivery of aid outside the state system undermined the legitimacy of local state institutions. People would directly go to donors to negotiate for funding their priorities. Military Provincial Reconstruction Teams, which spent \$867 million from 2005 to 2008, used such a mechanism,<sup>19</sup> although this issue was not limited to the role of such Teams. Other types of off-budget spending, which bypassed the state and national mechanisms, also adversely affected government legitimacy.

<sup>18</sup> Islamic Republic of Afghanistan (2010), "Development Cooperation Report", Kabul: Ministry of Finance.

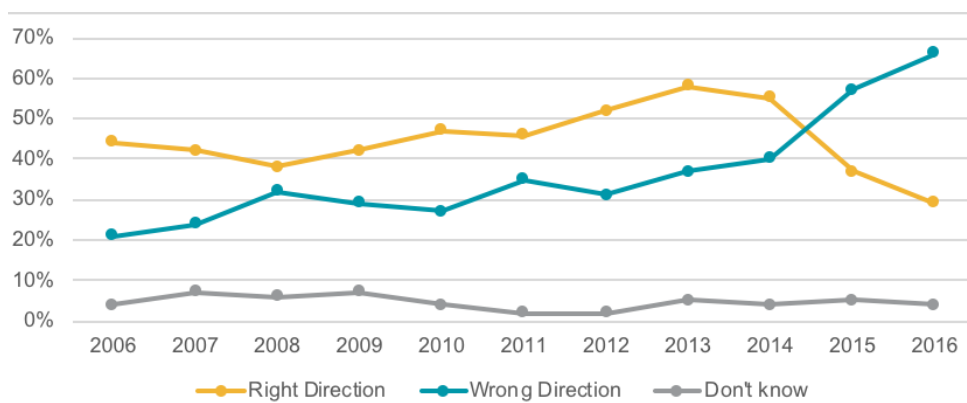
<sup>19</sup> Ibid.

**Figure 3: Top Nine Donors - Aid Delivery Channels, 2002-2011**



As a result of the nature of international intervention and the aid modality, the balance of power shifted in favour of donors. Donors therefore had greater fiscal leverage over both the government and societal actors. Both needed to negotiate for funding and report on individual projects to donors. However, overreliance on off-budget aid mechanisms, in particular, proved counterproductive. Parallel processes and mechanisms were created leading to the emergence of a parallel public sector which was fiscally much bigger than the permanent state institutions. The government, as a result, became increasingly accountable to donors to negotiate for further funding and report on aid spending.

**Figure 4: National Mode: Direction of Country**



Source: Asian Foundation, A Survey of Afghan People: Afghanistan in 2016, 18.

Security and economic outcomes had a major impact on the confidence of the public. This situation can be observed after 2005 in which security started to deteriorate and in 2014 because of the triple transition. International consensus and aid for stability in Afghanistan ignited the hope for improving stability in the country. The perception was that external and internal spoilers would be kept at bay. This situation also boosted the confidence of the private sector as well as of citizens. An atmosphere of hope and revival soared between 2002 and 2005. Private investment and foreign direct investment, as we will note in the next section, increased. But this situation did not last long. The deterioration of security after 2005 and then in 2014, including disputed Presidential elections, put the gains at risk and adversely affected the positive perception that people had about the direction of the country. In 2016, according to a survey of about 10,000 people by the Asia Foundation, only 29% said that Afghanistan was headed in the right direction, the lowest in a decade, in comparison to 58% in 2013 (Figure 2).<sup>20</sup> But even after 2007, as Figure 2 shows, the percentage of people with the belief that Afghanistan is headed in the wrong direction has steadily increased. A decline in the positive perception was also observed between 2006 and 2008.

<sup>20</sup> "Afghanistan in 2016: A Survey of Afghan People", Kabul: The Asia Foundation, 2016.



# Building state capacity

## 3

Given that the state suffered from an acute deficit of capacity, it was crucial to devise ways to provide public goods in this situation and build the state's capacity. To do so, three strategies were adopted. The first strategy was to buy capacity from outside the public sector and country by hiring national and foreign consultants, and by outsourcing some of the government's core functions. The second entailed donors to bypass the Afghan state and national mechanisms to deliver their projects directly through the private sector. The third focused on building the capacity of the various government departments through reforms, training, and new hiring. However, success has been mixed, and, as will be discussed later, these strategies in some cases proved counterproductive.<sup>21</sup>

The capacity of state institutions has improved significantly since 2002. Despite these improvements, however, the state remains weak; the state's fiscal, legal, and coercive capacities are very low. A low fiscal capacity is evident by the low extraction and distribution capacities of the state. While tax revenue as a total share of GDP increased from 4% in 2004 to 10% in 2015, on average it remained at 7% between 2003 and 2015. Since the late twentieth century, tax revenue as a total share of GDP has been very low in the country.<sup>22</sup> Aid, therefore, remained an important source of finance. Between 2002 and 2015, overseas development assistance (ODA), excluding military aid, on average comprised approximately 38% of gross national income (GNI). Development and military aid funded 90% of the national budget between 2002 and 2009, and 61% in 2017.<sup>23</sup> Another measure of state capacity is the government development budget execution rate, which was only 43% between 2002 and 2010.<sup>24</sup> This percentage did not change much in the ensuing years. In the first six months of 1396 fiscal year (2017/2018), the government development budget execution rate

<sup>21</sup> For more information about building the state capacity see Bizhan, N. "Aid and State Building, Part I, South Korea and Taiwan", *Third World Quarterly*, 28 March 2018, 1-16; Bizhan, N. "Aid and State Building, Part II, Afghanistan and Iraq", *Third World Quarterly*, 28 March 2018, 1-19.

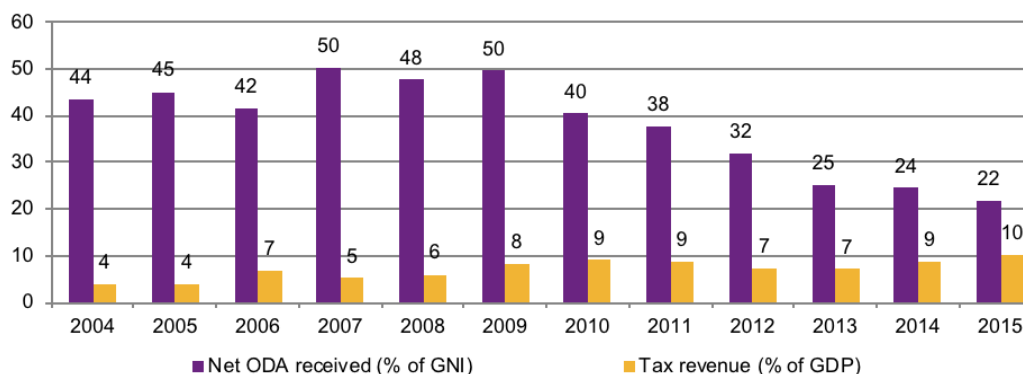
<sup>22</sup> Bizhan, N (2017), *Aid Paradoxes in Afghanistan: Building and Undermining the State*, Abingdon: Routledge, p. 37-64.

<sup>23</sup> Bizhan, N (2017), *Aid Paradoxes in Afghanistan*, pp.77; Islamic Republic of Afghanistan, "Fiscal Year 1396: Budget," ed. Ministry of Finance (Kabul 1396 (2017/18)), p. 8.

<sup>24</sup> Bizhan, N (2017), *Aid Paradoxes in Afghanistan*, p. 93.

remained at 20%.<sup>25</sup> Figure 3 below shows the inflow of net ODA as a percentage of GNI and tax revenue as a percentage of GDP. This figure, however, does not include military aid and some parts of the assistance that the US classifies as development assistance.

**Figure 5: The Flow of Net ODA (% of GNI) and Tax Revenue (% of GDP)**



Source: World Development Indicators, 2017

First, reliance on technical assistance was a part of the strategy to buy capacity. From 2002 to 2014, on average, donors spent between \$250 million and \$1 billion annually on technical assistance projects, recruiting national and international staff. However, a large portion of technical assistance programmes was off-budget. According to an estimation by the Finance Ministry of Afghanistan, as of 2010, 7000 Afghans were working with civilian ministries, referred to as externally funded staff and recruited through donor-funded projects outside the government budgetary process. In 2011, 5000 externally funded staff worked (almost all Afghans) in eight key ministries and one agency.<sup>26</sup> No reliable data is available on the total number of consultants that worked with non-state actors. However, the technical assistance programmes were ineffective. In 2008, a study sponsored by the Agency Coordinating Body for Afghan Relief found that even though “One quarter of all aid to Afghanistan has been allocated to technical assistance which is intended to build government capacity, much of this assistance has been wasteful, donor-driven, and of limited impact.”<sup>27</sup>

The government established an interministerial body for the coordination of capacity-building initiatives. In 2008, the government stated in the Afghanistan National Development Strategy: “the Government will ensure that technical assistance will be demand-driven and aimed at building Government capacity. In addition, it will ensure that it is delivered in a coordinated manner. All technical assistance channelled outside the [government] budget should have capacity-

<sup>25</sup> Ministry of Finance, “1396 Fiscal Year Execution Rate Report from First of Jaddi 1395 to 12 Saratan 1396 as of 03 July 2017,” ed. Directorate General Budget (Kabul 2017).

<sup>26</sup> Hogg, R, Nassif, C, Osorio, C G, Byrd, W and Beath, A (2013), Afghanistan in transition: looking beyond 2014, World Bank Publications.

<sup>27</sup> Waldman, M. (2008), “Falling Short: Aid Effectiveness in Afghanistan”, Agency Coordinating Body for Afghan Relief (ACBAR), p. 4.

building components and require Afghan counterparts.”<sup>28</sup> While the process improved slightly, the problem remained intact.

In addition, the outsourcing mechanism was used to overcome the state’s weakness. In the first few years after the fall of the Taliban regime, some government functions were fully or partially contracted out to the private sector. These included procurement, delivery of basic health services, and community development programmes. After building the initial capacity, the state restored some of these functions, such as procurement. But some services like the delivery of basic health services and community development projects continued to be delivered by NGOs, using the government budget and procurement system.<sup>29</sup>

The civil service law remained rigid and out of date, however. It barely allowed a civil servant, who on average received about \$50 per month in 2002, to receive a decent salary. But projects funded off-budget remained attractive for paying competitive wages. As a result of this type of intervention, civil administration became fragmented across ordinary and secondary civil services. The former included civil servants who were recruited under the existing law. The latter were recruited mainly through projects funded off-budget based on short-term contracts. Therefore, both the government and the donors relied on buying capacity from outside and contracted out some of the government’s functions to substitute for the shortage of skills.

The second strategy in overcoming the challenges emerging from corruption and state weakness was the bypass tactic, which relied on off-budget aid mechanisms. Donors by and large bypassed the state and delivered their aid through private companies and non-governmental organisations (NGOs). Off-budget aid created a parallel public sector to deliver public services and implement projects. The problem with the parallel mechanism and process was not that non-state actors implemented projects, but aid which flew through this mechanism was much larger and was poorly aligned with local priorities, and it induced institutional rivalry and fragmentation. There was also an intermediate approach using Trust Funds, such as the Afghanistan Reconstruction Trust Fund, which funded the private sector or non-state actors to implement projects. Unlike off-budget aid, however, the funding was channelled through the state treasury and was aligned with government priorities. This approach was relatively more effective. Between 2002 and 2012, on average, about half a billion USD was annually channelled through the Afghanistan Reconstruction Trust Fund.<sup>30</sup>

Both the bypass tactic and buying capacity had short time horizons. Even though these strategies helped to improve the delivery of aid, in some areas it led to the fragmentation of administration, creation of islands of inefficiency, and increased transaction costs. Bypass tactics had adverse implications for capacity building in the long-run. It made the government’s permanent institutions less attractive for competent candidates, and averted much of the financial and political resources from building and reforming the permanent state institutions.

<sup>28</sup> See Islamic Republic of Afghanistan, “Afghanistan National Development Strategy (ANDS), 1387-1391 (2008-2013),” Kabul: ANDS Secretariat, n.d., p. 160.

<sup>29</sup> Ghani, S, & Bizhan, N (2009), *Contracting Out Core Government Functions and Services in Afghanistan*, Partnership for Democratic Governance, pp. 97-113.

<sup>30</sup> Islamic Republic of Afghanistan (2012), “Development Cooperation Report,” Kabul: Ministry of Finance, p. 55.

The third strategy included direct intervention in building state capacity. This process had mixed impacts. Those government departments and ministries that had exposure to donors significantly improved. The Finance Ministry is a notable example. But even the capacity within the ministry varied and was less sustainable because of dependence on aid and technical assistance. The General Directorate of Budget of the ministry has significantly improved and reformed. However, it is important to note that line ministries and departments had to execute the national budget. Low budget execution rate, therefore, as will be discussed below, does not represent a lack of capacity at the General Directorate of Budget. The General Directorate of Treasury also demonstrated increasing capacity. But this was not the case with the Directorates of Revenue and Customs as corruption and nepotism have damaged their reputations.

Table 1 shows the capacity of Ministries of Finance and Interior as well as the Attorney General Office, representing the fiscal and legal capacity of the state, as these entities had important roles in post-2001 state building.

**Table 1: Capacities of the Ministries of Finance and Interior, and Attorney General Office**

Ministry of Finance	Ministry of Interior	Attorney General Office
Ministry of Finance did not use a computerised system for preparing the budget or making payments until 2002.	During the civil war (1992-1996), the ministry disintegrated, and its link with provinces hardly existed.	The Attorney General Office in 2002 had limited capacity and suffered from widespread corruption.
Most of the skilled staff of the ministry had left the country due to war, or key positions were given to political appointees who lacked required skills.	Police and civilian support staff did not go through a proper training process.	Post-2001, the Attorney General Office was re-established as an independent entity of the executive branch with authority to investigate and prosecute cases.
In post-2001, the ministry was reformed and restructured. Its budget department and treasury improved significantly.	Recruitments were based on political affiliation and patronage, undermining the loyalty of the officers and soldiers in terms of common goals.	In comparison to the Ministry of Finance, the reform of the Attorney General Office was slow and inefficient.
However, the ministry in the short term relied on technical assistance and aid from donors to sustain the reforms and build its capacity.	The reform of the ministry was amongst the most challenging tasks. Germany/European Union took the lead on behalf of donors to support reform of the police.	The Attorney General Office was significantly affected by domestic politics, where impunity became common.
As of 2016, the ministry had 8088 employees. <sup>31</sup>	As of January 2017, the total size of the Afghan National Police was 153,997, excluding the Afghan local police (28,724 by February 2017).	The Attorney General Office has 5,200 employees, among whom only 51 people have bachelor's degrees and two have master's degrees.
While budget formation and execution and payments have improved significantly, revenue collection has suffered from graft and inefficiency.	Despite the efforts to reform and restructure the ministry, the success has been mixed. People had little trust in the police, with corruption continuing to remain a major challenge.	People have little trust in the Attorney General Office.

The police is ineffective, weak, and under-resourced. Several factors contributed to this situation. First, the international community concentrated on war on terror, prioritising the building of the Afghan National Army. Second, political intervention and a culture of impunity, favouring short-term stability by appeasing powerful adversaries, made the police's weakness more convenient for politicians. In May 2017, President Ghani called the Ministry of Interior "the heart of corruption".<sup>32</sup> Insurgents increasingly attack police, finding police an easy target. The role of police, therefore, has inevitably expanded from enforcing the law to combat and defence. Unlike the Afghan army, for which the US remained the main donor, fragmentation of donors and the narcotic business as a source of corruption hampered the reform of police. Germany and then the European Union, on behalf of donors, took the lead in assisting the police's reforms. Key police positions, with possible illegal income, were mainly sold in exchange for a lump sum or regular payment. While it is difficult to estimate the exact amount of such payments, it depended on the type of positions and potential illegal revenue that an actor could appropriate. The failure of police reform was multifaceted. Legacy of weak institutions, police capture, ethnic favouritism, nepotism, low pay as well as donor fragmentation by and large undermined the reforms.<sup>33</sup>

The Attorney General Office has had the worst reputation because of corruption and mismanagement. The police say, "we risk our lives to arrest criminals, but the attorneys and judges free them in exchange for money." The Attorney General Office has also been overwhelmed by high demand, while its staff lacked skills, especially in dealing with complex cases (see Table 1). In 2016, the Attorney General Office received and investigated 2800 anti-corruption and 28,320 civil cases.

## Service delivery

The provision of public services since 2002 has significantly expanded. Access to a health facility within a one-hour walk has increased from 9% in 2002 to 57% in 2012.<sup>34</sup> The total number of enrolled school students increased from one million, despite girls being banned from school under the Taliban rule, to nine million in 2013.<sup>35</sup> New roads were built and access to electricity also increased. However, these services are less sustainable and have poor quality. The way the services were delivered had implications on state capacity and the cost of these services. The delivery of basic health services was subcontracted to NGOs. While this approach helped in improving service delivery, it increased the cost of

<sup>31</sup> Ministry of Finance (2017), "Chart Tashkilati Sal-E 1395 Wuzarat-E Malia (the Finance Ministry Organisational Chart)," Kabul.

<sup>32</sup> BBC Persian (2017), "Ghani: Wozarat-E Dakhila Qalb-E Fasad Dar Nehad Hai-E Amniati Ast (Ghani: Interior Ministry Is the Heart of Corruption of the Security Sector)".

<sup>33</sup> Singh, D. (2014), "Corruption and Clientelism in the Lower Levels of the Afghan Police," *Conflict, Security, and Development* 14, no. 5.

<sup>34</sup> See Ministry of Public Health (2016), "Istrategy Mili-E Sehat (1395-1399): Pishraft Motadawim Wa Talash Barai Sakhtan Fardai Behter (Health National Strategy [2016-2020]: Continuous Progress and Efforts to Better Future)," Kabul: Ministry of Public Health, p. 7.

<sup>35</sup> USAID, Afghanistan: Education, Accessed 11 April 2018, <https://www.usaid.gov/afghanistan/education>.

services which the government might struggle to sustain in the future.

The delivery of the bulk of aid outside the state system through parallel mechanisms and systems helped to improve project implementation. However, this type of aid delivery increased project costs because of multilevel subcontracting arrangements, as well as diverted financial resources and political attention from building permanent state institutions.

In addition to the strategies being discussed, the structure of the state itself as well as the neglect of local state institutions were the two major challenges for state building and service delivery. In particular, the state structure and lack of clarity within different departments and amongst staff presented an obstacle for effective service delivery. Excessive centralisation of public administration, beyond what the Afghanistan constitution envisages, and a blurred institutional role, adversely affected the delivery of public services. This challenge was compounded by the limited resources for building the capacity of government departments at the provincial level.

While government departments exist in both Kabul as well as the provinces and districts, the subnational departments at the provincial and district levels do not effectively participate in and contribute to planning and budgeting. The ministries and departments in Kabul perform or coordinate most of the state functions such as public financial management, water management, and policing. This process has had adverse implications for service delivery, implementation, monitoring, and downward accountability.<sup>36</sup>

The roles of the ministries in Kabul, the line ministry directorates in the provinces and districts, and the elected provincial councils, are not clearly defined. Senior officials are often not clear about their roles in the office. The provincial departments are dependent on Kabul for many of their day-to-day operations. These deficiencies have unintentionally led to waste and poor implementation.<sup>37</sup>

Post-2001 reforms initially focused on strengthening the capacity of the central government. The fragmentation of state institutions and the flimsy institutional link between Kabul and the provinces might have further encouraged the government to excessively centralise governance processes to extend the reach of the central government and curb the power of strong local actors. Donors also found a centralised administration more convenient to work with. While this approach seemed plausible at the beginning, it has undermined the ability to effectively identify and finance local priorities, build local capacity, and increase local participation in the long run. Moreover, it was a challenge to maintain the right balance between centralisation and decentralisation in Afghanistan, a situation that has also been observed in other fragile contexts.<sup>38</sup> A notable example was re-centralisation of the revenue collection process. In 2002 and 2003, regional commanders and strongmen controlled provincial revenue and customs. The government in Kabul recentralised revenue collection and allocation through a consensus building process, organising a meeting in Kabul to discuss the centralisation of revenue with the commanders and strongmen,

<sup>36</sup> Bizhan, N, Ferhat, E and Nayebkhil, H (2016), "Bringing the State Closer to the People: Deconcentrating Planning and Budgeting in Afghanistan", Kabul: AREU and GIZ.

<sup>37</sup> Ibid.

<sup>38</sup> Ibid, pp.1.



and issuing a decree after an agreement of sorts was reached with them.<sup>39</sup>

While the concerns regarding decentralisation in Afghanistan – that it may lead to corruption and empower local strongmen in some cases – seem valid, some of the programmes in which people fully participated and were managed in a decentralised manner were more effective. The National Solidarity Programme is a major success in the history of development in the country. By allowing people to participate in the design, implementation, and monitoring of their local projects, this programme mitigated the risk of corruption and waste. It also helped in building the capacity of local communities and establishing an extensive network of communities that practised power in a democratic manner. Another important aspect of this programme was that an appropriate mode of aid delivery was adopted. The National Solidarity Programme was entirely funded by donors through pooled funding, Afghanistan Reconstruction Development Fund which was managed jointly by the World Bank, the Government and concerned donors.<sup>40</sup>

<sup>39</sup> Bizhan, N (2017), *Aid Paradoxes in Afghanistan*, p. 104-132.

<sup>40</sup> For more information see Barakat, B. (2006), “Mid-Term Evaluation Report of the National Solidarity Programme (NSP), Afghanistan”, The York University and Ministry of Rural Rehabilitation and Development of Afghanistan.

# Establishing security

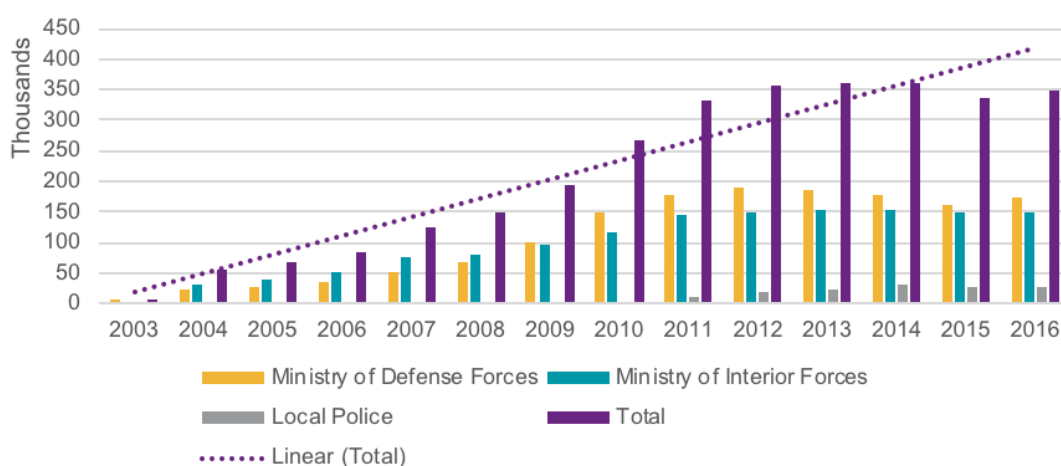
## 4

The Afghan government and international community relied on five strategies to establish security and prevent Afghanistan from again becoming the safe haven for groups such as Al Qaeda. The US and its allies focused on war on terror to defeat Al Qaeda and keep the Taliban at bay by relying on the International Security Assistance Force and private security contractors. In parallel, the building of the Afghan National Army and Police; the disarmament, demobilisation, and reintegration of illegal armed groups; and a counter narcotics strategy were initiated. However, the success has been mixed and in some cases these strategies, as will be discussed later, were either partially implemented or were paradoxical. Inadequate investment in the security sector in the first years after the international intervention in Afghanistan, a lack of balance between building the security sector and short-term objectives of the war on terror, as well as the neglect of the role of Pakistan in providing support to the Taliban insurgency, had repercussions on the security situation and the development of the security sector.

The US military intervention in Afghanistan was aimed at the war on terror. While US President George Bush campaigned against nation building in 2000, this rhetoric later changed to arguing that it was imperative to support a stable government in Afghanistan. The war on terror concentrated on short-term measures including the delivery of quick results to defeat Al Qaeda, keeping the Taliban at bay, and winning the hearts and minds of people. The building of lasting stability required the development of local institutions in which the Afghan national army was the key. The US took the lead in providing financial and logistics support for the development of the Afghan National Army. Out of the total aid (\$57 billion) that Afghanistan received from 2002 to 2011, 51% was allocated to the security sector, primarily the army. The army's strength gradually grew and became more professional. By 2014, the army had emerged as a credible institution with 178,617 forces in total (see Figure 5). By 2014, it had taken full combat responsibility from NATO and US forces. The army kept the Taliban at bay from capturing major urban centres. The US also relied extensively on private security contractors. As of March 2009, there were 90,339 US Department of Defence contractors in comparison to 99,800 uniformed

personnel in Afghanistan.<sup>41</sup> The Afghan government increasingly criticised the role these contractors played because of their adverse implications on the development of the security sector as well as the security situation in general. However, as the strategy for building the capacity of the army focused on counterinsurgency, the army was not adequately equipped to overcome the threat arising from a conventional war. This issue captured the attention when in 2015, the Taliban captured Kunduz city for a short period in the north of the country. The army did not have effective airpower to recapture the city. It, therefore, relied on the US and NATO for air support during their offensive before recapturing the city.<sup>42</sup>

**Figure 6: The Development of Afghanistan's Security Forces**



Source: Brookings Institute, 2016

Post-Bonn agreement, Afghanistan's disarmament, demobilisation and reintegration aimed to enable the government to establish a monopoly over the use of force, helping the former militias and commanders make a transition to civilian life, and breaking the linkage between commanders and militia forces. Japan became a lead donor for this programme. While there was a dispute over whether the total number of armed groups was 50,000 or 250,000, 63,380 armed militias were disarmed by 2008. A relatively calm security situation and a new Political Parties law (2004), which prohibited political parties from either possessing military organisation or being affiliated with armed forces, created some incentives for armed militias to participate in the process. A number of factors made this programme less effective: i) the capture of state security institutions by those who were affiliated with militia groups; ii) exclusion of the disarmament, demobilisation and reintegration programme from the Bonn agreement; iii) linking of this programme with the security sector reforms which resulted in delays; and iv) a deteriorating security situation after the first few years of the implementation of the programme. However, despite Afghanistan

<sup>41</sup> Schwartz, M and Swain, J (2011), "Department of Defense Contractors in Afghanistan and Iraq: Background and Analysis", Washington: Congressional Research Service.

<sup>42</sup> Ali, O. (2015), "The 2015 Insurgency in the North (3): The Fall and Recapture of Kunduz", Afghanistan Analysts Network.

being a difficult environment for the programme, it has achieved some preliminary results at the beginning which was generally supported by people.<sup>43</sup>

The narcotic business posed a major challenge for stability. Counternarcotics strategy proved ineffective. In the first years after military intervention, the US did not prioritise counternarcotics, especially as it had a limited number of troops on the ground; although this strategy later changed with increasing emphasis on eradication. However, there were diverging views between the US, UK, and the Afghan government. The US emphasised a more aggressive eradication approach, while the Afghan government and the UK emphasised a gradual intervention with more emphasis on alternative livelihoods to minimise the adverse implications of the eradication on farmers. Interdiction that aimed to target traffickers were also used which did not directly harm the local population. This process was complex making the counternarcotics strategy less effective, the failure of which further strengthened the insurgency as they were able to extract significant income from the narcotics business.<sup>44</sup> Increase in the illicit drug economy in Afghanistan has been associated with insecurity. In 2007 and 2008, “the drug economy reached levels that had thus far been unprecedented in the world, at least since World War II, with 2014 being another very high year.”<sup>45</sup> Some of the structural drivers of the poppy economy including insecurity, political power arrangements, and lack of economic alternatives, remained largely unchanged. The income from poppy became a major source of revenue for the insurgency. As of 2014, no major eradication measures were adopted; one can argue that increases in poppy production were in fact a key driver of the insurgency.

After a relative period of calm between 2002 and 2005, the security situation started to deteriorate rapidly. A gap that was left in the first few years after the fall of the Taliban regime mainly because of little military and economic aid that Afghanistan received, and the neglect of Pakistan’s support to the Taliban insurgency, contributed to this situation. In the two years following international intervention, Afghanistan received \$57 per capita, while Bosnia and East Timor received \$679 and \$233 per capita respectively.<sup>46</sup> The military sector was under-resourced. The target which was set for the Afghan National Army and Police in 2002 was not realistic (see Figure 5). Subsequently in 2009, in response to a deteriorating security, the US President Barack Obama ordered 30,000 more US troops to be sent to Afghanistan. The total number of American forces increased to more than 100,000.<sup>47</sup> The flow of aid to Afghanistan also increased. Total military and development aid disbursement rose from \$7.1 billion in 2008 to \$10.8 billion in 2010. Aid from the US comprised a significant portion of it. US military and development aid increased from \$4.5 billion in 2008 to \$8.1 billion in 2010.

However, in 2014, a triple transition — security, political, and economic –

<sup>43</sup> Hartzell, C (2011), “Missed Opportunities: The Impact of DDR on SSR in Afghanistan”, Washington: USIP.

<sup>44</sup> Felbab-Browne, V (2005), “Afghanistan: When Counternarcotics Undermines Counterterrorism”, *The Washington Quarterly* 28, no. 4.

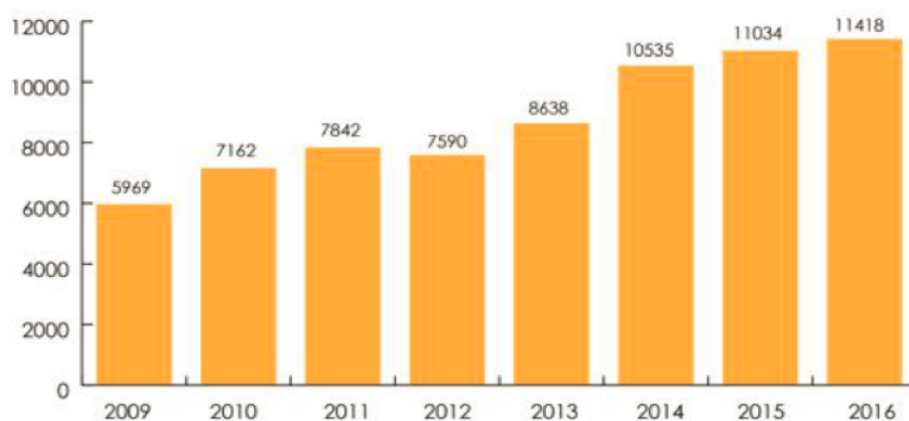
<sup>45</sup> Felbab-Brown, V (2016), “No Easy Exit: Drugs and Counternarcotics Policies in Afghanistan”, Brookings, p. 2.

<sup>46</sup> Waldman, M (2008), “Falling Short: Aid Effectiveness in Afghanistan”, Agency Coordinating Body for Afghan Relief (ACBAR).

<sup>47</sup> BBC, “Barack Obama Orders 30,000 More Troops to Afghanistan”, BBC, 2 December 2009.

again increased the risk of collapse. The withdrawal of the bulk of international troops from Afghanistan, a sharp decline in the flow of aid to the country, the resurgence of the Taliban, and the rise of IS (Islamic State), increased the level of shocks. Domestic politics in Washington and other donor capitals, rather than improving conditions on the ground in Afghanistan, were the main drivers of international troop withdrawal from Afghanistan. The US deciding to withdraw its combat troops from Afghanistan created a sense of uncertainty. This process was compounded by the fact that the US and its allies, who had greater leverage to keep regional spoilers at bay, failed to adopt an effective regional strategy. Subsequently, the Taliban increased its attacks, and in response to a deteriorating security situation, US President Trump introduced a new strategy for Afghanistan in August 2017. This strategy states that any future adjustments in US policy for Afghanistan would be made based on conditions in Afghanistan, a modest increase in American troops, and with an increasing emphasis on the region, especially Pakistan, to end safe havens for the Taliban and other similar groups. The Taliban attacks on civilians, military personnel, and public buildings have significantly increased. Civilian war deaths and injuries have steadily increased, reaching their peak in 2016.

**Figure 7: Civilian Deaths and Injuries, January 2009 - December 2016.**



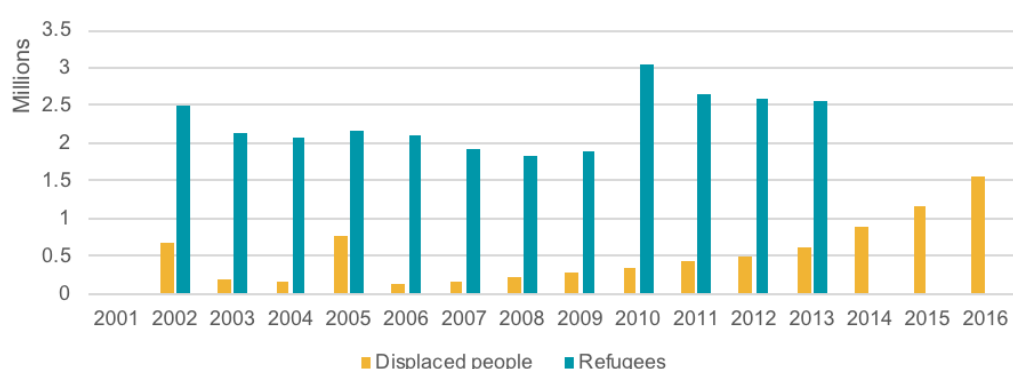
An expanded, well-resourced, and multifaceted insurgency poses a continuing threat to Afghanistan. The insurgents of the Taliban derive their income from the narcotic business, extortion, regional networks, and have safe havens in Pakistan. Pakistan perceives the Taliban and the Haqqani network, which the US classified as a terrorist organisation, as a strategic asset against the influence of India in Afghanistan. The Taliban leadership, called Quetta Shura, is based in the city of Quetta in Pakistan. These factors have sustained the insurgency and have increased the level of threats in Afghanistan. It is difficult to estimate the total number of Taliban fighters and how much financial support they receive. Some analysts estimate that at any time the Taliban can field up to 10,000 fighters, of which 2000-3000 seem highly motivated, full-time insurgents, and 200-300 are believed to be foreigners.<sup>49</sup>

<sup>48</sup> UNAMA (2017), "Afghanistan: Protection of Civilians in Armed Conflict, Annual Report 2016," Kabul.

<sup>49</sup> Altschiller, D. (2003), "Encyclopedia of World Terrorism," Reference & User Services Quarterly 43, no. 2: 237.

The US and its allies neglected to adopt a regional approach that could block the insurgent's sources of income and end the safe havens. This failure made the counterinsurgency strategy in Afghanistan ineffective and people eventually lost their confidence in the government. This failure and the memory of past wars encouraged a large number of people to leave the country. The total number of Afghan refugees in 2016 stood at two and a half million.<sup>50</sup> Afghans, after Syrians, comprised the second largest number of asylum seekers in the world, reaching their peak in 2014 (59,472).<sup>51</sup> The number of internally displaced people increased to close to two million people in 2016. Figure 8 below shows the pattern of internally displaced people in the country and Afghan refugees between 2002 and 2016.

**Figure 8: Internally Displaced People in Afghanistan and Afghan Refugees, 2002 - 2016**



Source: UNHCR<sup>52</sup>

In addition, the Afghan government initiated a process and established a High Peace Council in 2010 to negotiate with the Taliban on a political settlement. Burhanudin Rabbani, the former President of Afghanistan (1992-1996) chaired the council but he was assassinated by a messenger of the Taliban on 20 September 2011 in Kabul.<sup>53</sup> The Afghan government along with the US and its allies agreed on the setting up of the Taliban's office in Qatar in 2013. However, the Taliban persistently refused to negotiate with the Afghan government and increased their attacks instead.<sup>54</sup>

<sup>50</sup> UNHCR (2017), "Population Statistics", United Nations High Commissioner for Refugees.

<sup>51</sup> Ibid.

<sup>52</sup> Ibid.

<sup>53</sup> "Former Afghanistan President Burhanuddin Rabbani Killed in Kabul Blast", Telegraph, September 20, 2011.

<sup>54</sup> In February 2018, Ashraf Ghani Afghan President offered talks with the Taliban without preconditions. However, Taliban did not respond to this offer yet.



# Volatile private investment

## 5

In 2002, with poor infrastructure, weak public institutions/legal system, and insecurity, Afghanistan was a high-risk country for investment. Despite these challenges, the country offered an opportunity for investment with a high return because of a huge gap that existed in the market. One of the main challenges was how to increase investment and improve private sector development as a key driver of economic growth. The process, however, lacked a degree of pragmatism and the initial interventions were less effective as a result. A lack of balance between short-term objectives for the delivery of quick impact results and long-term development hindered the process. While early GDP growth was impressive (Figure 8), it was volatile and not sustainable. Afghanistan did not meet the expectations, especially concerning exports, investment, and employment.

Mid-20th century onward, Afghanistan somehow developed a mixed-guided economy that included elements of both market and command economies.<sup>55</sup> But a protracted war had left the economy in a state of collapse. The Afghanistan Constitution (2004) envisaged private sector as the engine of growth. The government also emphasised public-private partnership. The efforts to rapidly transform the economy without a proper strategy to appreciate the limits and opportunities neglected the fact that neither the government nor society was adequately prepared for the sudden introduction of the market economy. The government in 2008 emphasised that:



“[The government] objective is to enable the private sector to lead Afghanistan’s development within a competitive market-based economy in which the Government is the policymaker and regulator of the economy, not its competitor. The establishment of a strong enabling environment for a competitive private sector is an ongoing effort by both the Government and donors.”<sup>56</sup>

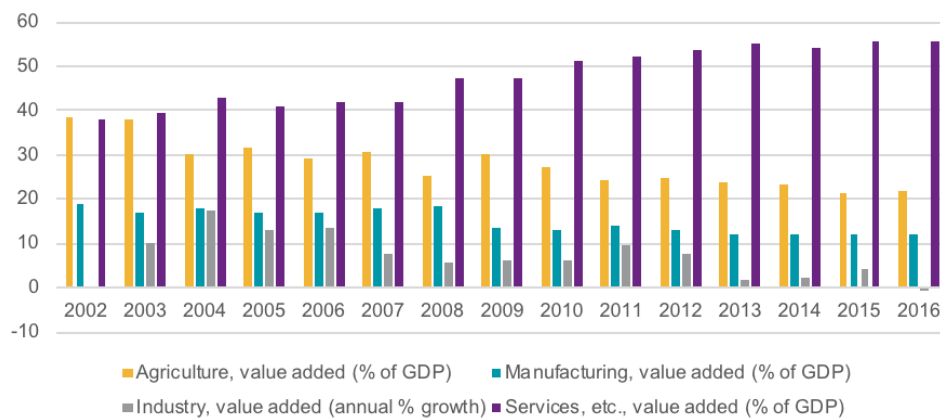
<sup>55</sup> Nyrop, R and Seekins, D M eds. (1986), *Afghanistan: A Country Study*, Washington, DC: American University, p. 145. Bizhan, N, Ferhat, E and Nayebkhil, H (2016), “Bringing the State Closer to the People: Deconcentrating Planning and Budgeting in Afghanistan”, Kabul: AREU and GIZ.

<sup>56</sup> Islamic Republic of Afghanistan. “Afghanistan National Development Strategy (ANDS), 1387-1391 (2008-2013).” Kabul: ANDS Secretariat, n.d, pp.11.

The government revised its policies and laws concerned with regulating the role of the private sector in the economy. After the introduction of a market-led economy post-2001, an early sign of resistance was apparent in some of the institutions, such as the Planning Ministry, which in the past had led economic planning. The ministry was, however, bypassed both by the government and donors. The Finance Ministry, instead, assumed most of the responsibilities that would fall under the purview of the Planning Ministry. Privatisation of state-owned enterprises was initiated. As it is also noted in other post-conflict countries, early constitution-making in Afghanistan despite its benefits posed a challenge: it did not forecast a proper framework for economic transition. Despite these challenges, there was no sign of organised resistance by the public. However, oligopoly, massive corruption, and fraud emerged as major challenges, and the relationship between politics and businesses became further blurred.

The confidence of individuals and companies was crucial. At the onset of the last decade, international support and consensus on Afghanistan boosted the confidence of people and private investors. While exact data is not available to confirm, many Afghans either returned to Afghanistan or sent money to invest in housing. In some sectors, such as telecommunication and services, investments were significant. Two telecommunication companies, Afghan Wireless and Roshan, are notable examples. Since 2003, Roshan has invested \$700 million in the country.<sup>57</sup> Between 2002 and 2016, the highest added value to GDP in annual percentage included services, agriculture, manufacturing, and industries respectively (see Figure 9). Eighty percent of businesses in Afghanistan were small and medium size, which employed one-third of the workforce.<sup>58</sup> In 2015, 678 firms existed in Afghanistan. The total annual production value of the main industries was estimated at \$109 million, showing 40% fall in comparison with 2013.<sup>59</sup>

**Figure 9: Value Added to GDP by Sectors (in %)**



Source: World Development Indicators, 2017

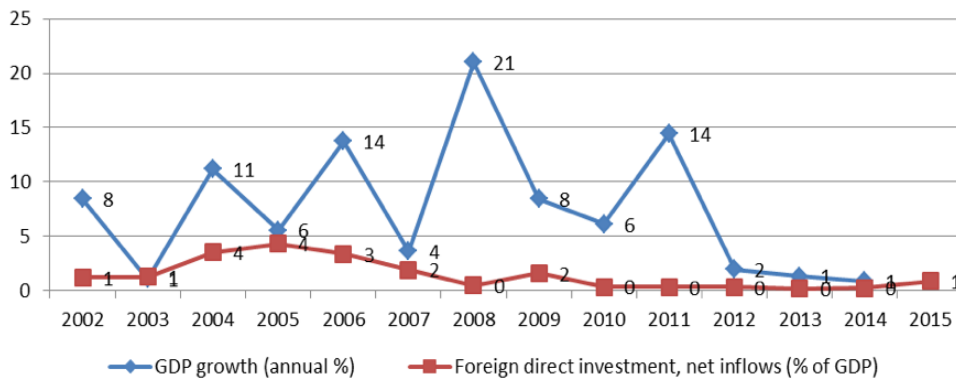
<sup>57</sup> About Roshan, accessed on June 14, 2017, from <https://www.roshan.af/en/personal/about/about-roshan/>.

<sup>58</sup> See ACCI (2017), “Business Monitor 2016”, Kabul; Afghanistan Investment Support Agency, “Afghanistan Country Profile”. <http://investinafghanistan.af/about-afghanistan/afghanistan-country-profile/>.

<sup>59</sup> Central Statistic Organisations, Afghanistan Statistical Year book 2015-16, Kabul.

Foreign direct investment has remained volatile. Its inflow steadily increased between 2002 and 2005, but declined sharply thereafter. While the legal framework for private sector development significantly improved, the strategies that the government followed did not relax other constraints. Poor infrastructure, lack of access to cost-effective electricity, corruption and insecurity have continuously constrained the development of the private sector.

**Figure 10: GDP Growth and Foreign Direct Investment Net Inflows (as % of GDP)**



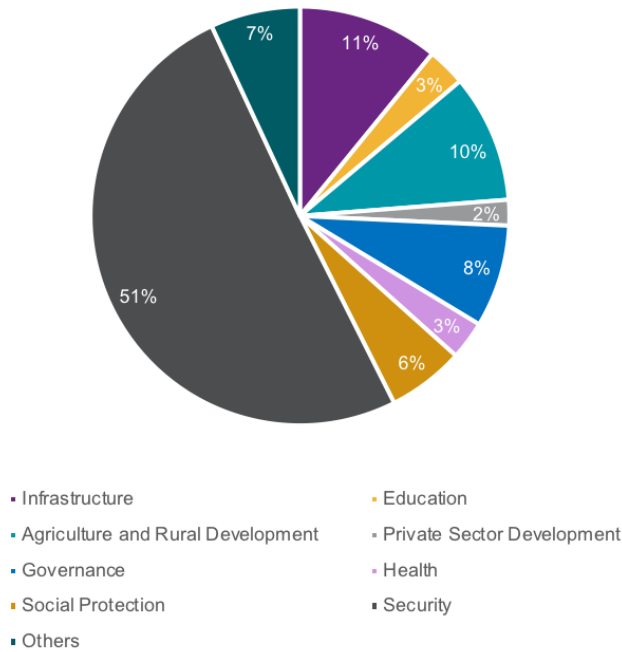
Source: World Bank, 2017

Afghanistan Investment Support Agency estimates that since 2002, the actual investment in Afghanistan has been 25-30 billion in construction (35%), services (31%), mining (19%), manufacturing (11%), and agriculture (4%).<sup>60</sup> However, this figure does not distinguish how much of the investment was made by private sector and donors. The flow of aid which funded infrastructure and services had a positive impact on private sector development. But in terms of direct public investment, the private sector was under-resourced. Between 2002 and 2011, out of \$57 billion being disbursed, only 2% was invested in programmes that directly supported the private sector (Figure 11). In addition, the flow of a large portion of aid outside the government budget and national mechanism, as noted above, deterred much of the resources that would help promote private sector development. According to an estimate by the World Bank, the local content, when using local goods and services, of on-budget was about 70–95%, compared to 10–25% for off-budget aid.<sup>61</sup>

<sup>60</sup> Afghanistan Investment Support Agency. "Afghanistan Country Profile."

<sup>61</sup> World Bank. "Afghanistan in Transition: Looking Beyond 2014." May 2012.

Figure 11: Foreign Aid by Sectors (in %), 2002-2011.



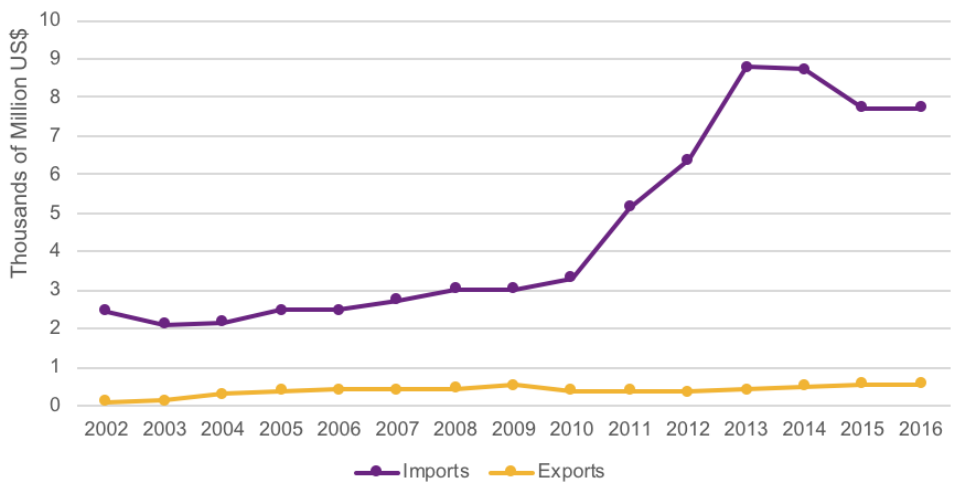
Source: Afghanistan's Finance Ministry, 2010, p. 98.

The US, UK, and Germany were the lead donors supporting private sector development. Germany has had a long history of private sector linkages with Afghanistan. However, in terms of their approach, there was tension between US and Germany. While the US emphasised building a market economy in Afghanistan, Germany preferred a European approach, envisioning a larger role for the public sector and played an important role in supporting the Afghanistan Investment Support Agency (established by a Presidential decree in 2003), with the responsibilities of registration, licensing, support, and promotion of investments. This situation created some tension with the US, for instance, over the characteristics of the reborn Chamber of Commerce in Afghanistan.

Public expenditure, mostly financed by aid, significantly increased the volume of Afghanistan imports (see Figure 12). But Afghanistan suffered from a huge trade deficit, by and large because of a lack of domestic production and high demand for imports. Afghanistan eventually became an important market for its neighbours. Afghanistan's top export destinations are Pakistan (\$373 million), India (\$242 million), China (\$21.3 million), Iran (\$18.1 million), and Turkey (\$16.4 million). The top import origins are Pakistan (\$2.2 billion), China (\$709 million), Iran (\$450 million), India (\$438 million), and Russia (\$407 million).<sup>62</sup> Pakistan therefore remains Afghanistan's top trade partner.

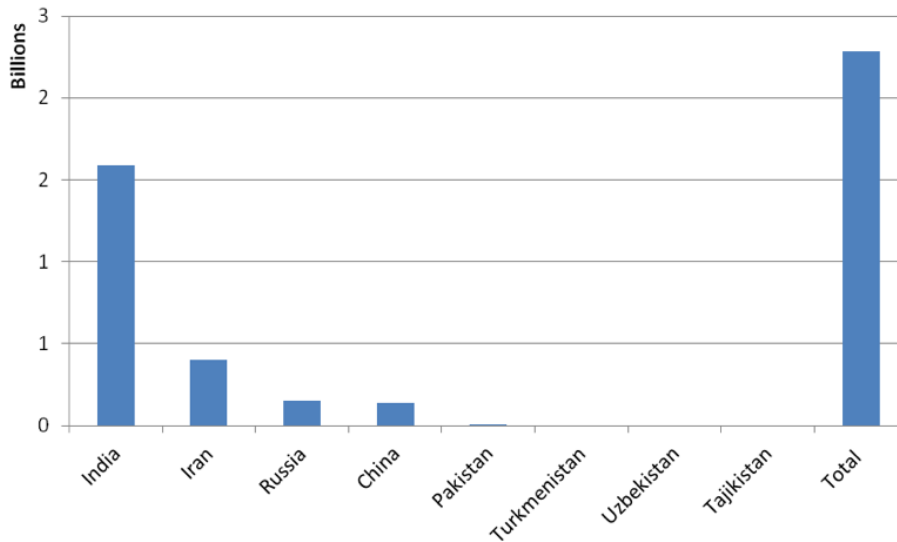
<sup>62</sup> Ministry of Commerce of Afghanistan, Kabul, February 2017.

**Figure 12: Imports and Exports in Afghanistan (in USD).**



Concerning the flow of aid from the region, investments by Afghanistan’s neighbours, except India, was low in comparison to major Western development partners of Afghanistan. As Figure 13 below shows, major regional development partners were India, Iran, Russia, China, Pakistan, and Central Asian countries.<sup>63</sup>

**Figure 13: Flow of aid from the region to Afghanistan, 2002-2011 (commitments in USD)**



Source: Afghanistan’s Finance Ministry, 2010

With China having political and commercial interest in Afghanistan, its efforts in expanding bilateral trade and investment have significantly increased. In 2008, the two state-owned Chinese companies secured the contract of Mes Aynak copper mine in the Logar province, worth about \$3 billion, and the world’s second-largest undeveloped copper deposit. This project is, however, stagnant

<sup>63</sup> Islamic Republic of Afghanistan (2010), “Development Cooperation Report”.

with three factors hindering its development: a deteriorating security situation, the existence of an archaeological site in the area, and drop-in prices of copper and other metal.<sup>64</sup> Delays in this project have deprived the government of an estimated \$390 million in annual revenue as of 2017. For the Afghan government, Chinese involvement in this project was essential both for implementation of the project and stability in the long run. The Afghan government expected that China, as a major economic power and close ally of Pakistan, would press Pakistan to relinquish its support to the Taliban.

India is involved in economic development both as a donor and contractor, and has focused on major infrastructure projects. Some notable projects include Salma Dam in the Herat province, Delaram Zaranj and Khost to Gardez highways, and installation of an electricity line that brought power from Uzbekistan to Kabul. An Indian consortium won the second largest mining contract in Afghanistan for the Hajigak iron mine in central Bamyan province. However, the status of the final contract and actual exploitation has been stalled because of concerns about lack of security and low world mineral prices.

As one of the most important neighbours economically and politically, Pakistan has played a dual role in Afghanistan. Karachi, the southern port city in Pakistan, provides land-locked Afghanistan with its main access to global and regional shipping. On the flipside, Pakistan has not only provided safe havens to Taliban insurgents and the Haqqani Network, it has also been criticised for predatory economic practices, such as product dumping and non-tariff obstacles. In addition, it has periodically closed its borders or imposed restrictions on the transport of goods to or from Afghanistan, which has adversely affected the relationship between the two countries.

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<sup>64</sup> Islamic Republic of Afghanistan (2008), Mining Contract for the Aynak Copper Deposit between the Government of Afghanistan and MCC-Jiangxi Copper Consortium (MCC), Kabul: Ministry of Mines and Petroleum.



# Resilience

## 6

Despite major improvements since 2002, the Afghan state lacks resilience and has low cushions. Historically, Afghanistan has been highly susceptible to internal and external shocks. However, external shocks as a result of power rivalry among major regional and global players had a major impact on political stability, economy, and society. The Cold War between the US and Soviet Union in the late twentieth century turned the conflict between the East and West into a conflict between state and society in Afghanistan. The Soviet Union supported the Kabul government, and the US and its allies supported the mujahidin armed groups. While it was expected that the consensus which emerged over Afghanistan post 9/11 might reduce external shock arising from power rivalry over Afghanistan, the situation somehow continued with the cold war actors being replaced by India and Pakistan for example.

While Afghanistan has made some important progress since 2002, it faced major security and political shocks in 2009 and 2014 that increased the risk of collapse. However, some short-term measures such as an increase in the number of international troops (2009 and 2010) and continuity in the flow of a modest level of aid (2014) helped to escape the collapse.

In particular, the 2014 shocks seemed massive. Some analysts and scholars compared these shocks with the period after the Soviet Union's collapse, in which the termination of the Soviet military and economic assistance to President Najibullah's regime in 1992 eventually contributed to the collapse of the government in Kabul. The subsequent events led to a civil war among different armed groups. Even though the situation in Afghanistan in 2014 was quite different, citizens, politicians and donors remained concerned about the risk of an armed conflict and political chaos. However, Afghanistan's experience helped to ignite an early warning. Donors on their part tried to mitigate the adverse effects of the troop's withdrawal, and a sudden cut in the flow of their aid, by pledging to sustain their support at a modest level. During the 2014 Presidential election crises, the US actively mediated among the two candidates which resulted in the establishment of a National Unity Government.

Moreover, patronage, elite fragmentation, and a lack of checks and balances have increased the risk of internal shocks. The crisis-ridden 2014 Presidential elections were one such example that increased the chances of relapse to a civil war. These factors, in the absence of a sufficient level of legitimacy and weak state capacity, further weakened the country's resilience. While elections were expected by Afghans and the international community to help a smooth political transition, and improve government legitimacy in the eyes of the citizens, they have turned into a source of political instability and societal division. This was,

by and large, because of a political system that incentivised the winner to do “everything” to win elections and the loser to reject the outcome, as well as the existence of an inefficient and impartial electoral administration.

In addition, political cushions are weak. Not only is there a lack of public consultation for policy change through the existing mechanisms, there is also a lack of consensus and coordination among the government leadership. On the other hand, the government seems increasingly preoccupied with donors both in negotiating on aid conditionality and aid flows as well as policy changes. While this process appears plausible because of the need for a sustained flow of aid, it has led to the neglect of pressing domestic needs by the Afghan government. Besides, lack of checks and balances have adverse implications. Powerful actors enjoy impunity, and those in key state institutions have high discretion in allocating resources and interpreting the law. While the National Unity Government promised an ambitious reform package to address some of these shortcomings, there is little sign of progress till date.

Persistent uncertainties and security threats have undermined growth and increased fiscal pressures. While Afghanistan has maintained macroeconomic stability, a stable exchange rate, and an increase in foreign exchange reserves (\$2.43 billion in 2008 and \$6.8 billion in 2016) and growth since 2002, it has been endangered by political, economic, and security shocks.<sup>65</sup> As we noted in Figure 10, economic growth decelerated from 14% in 2011 to 1% in 2014. While the efforts since 2002 helped to create conditions for recovery, the progress has been slow in large part due to conflict and an inappropriate mode of aid delivery. Because of Afghanistan’s high dependence on foreign aid, aid shocks matter for macroeconomic and political stability. Although Afghanistan’s location and its mineral resources offer potential for development and an alternative source of revenue to substitute for aid, to capitalise on these Afghanistan needs to make significant investments in these areas.

The terms of trade are also vulnerable to shocks. Afghanistan’s route through Pakistan to international markets has been closed on many occasions because of political tension between the two countries.<sup>66</sup> This process had immediate implications for increasing the price of imported goods and lowering the price of exported goods. This situation has also affected domestic production as most of the raw materials for production are imported. To overcome this constraint, Afghanistan has invested in diversifying its access to international markets, such as by using the Chabahar port in Iran that connects India and Afghanistan through Iran and India through Afghanistan to Central Asia. Afghanistan, India, and Iran signed a regional connectivity agreement centred around the Chabahar port in May 2016, calling it the “creation of history”. An initial investment of \$2.1 billion has been committed for building the rail connections to the port and from the Chabahar north to Zahedan on the Iran and Afghanistan border.<sup>67</sup> However, this project is susceptible to sanctions that the US might re-impose on Iran

<sup>65</sup> World Bank (2009), “Afghanistan Economic Update”, Economic Policy and Poverty Team, South Asia Region. See <http://siteresources.worldbank.org/AFGHANISTANEXTN/Resources/305984-1237085035526/AfghanistanEconomicUpdateOct2009.pdf>.

<sup>66</sup> UNAMA (2017), “Afghanistan: Protection of Civilians in Armed Conflict, Annual Report 2016”, Kabul.

<sup>67</sup> Watson, S (2017), “Does India’s Chabahar deal make sense?”, *The Diplomat*, May 24. <https://thediplomat.com/2017/05/does-indias-chabahar-deal-make-sense/>.

because of Iran's nuclear programme. The concerns have increased especially under Trump's administration in the US (2016 to date).

The poverty rate increased to 39.1% in 2013/14 up from 36% in 2011/12, with more than half of the population remaining at serious risk of falling into poverty. The unemployment rate has also increased to 22.6% in 2013/14, an increase of about 1% over the past two years.<sup>68</sup> The total number of war-affected disabled people is estimated at close to a million.<sup>69</sup> In addition, Afghanistan is highly disposed to natural hazards such as flooding, earthquakes, landslides, snow avalanches, and droughts because of its geographical location and environmental degradation. Since 1980, natural hazards have affected about one-third of the population and have caused over 20,000 fatalities. In 2017, natural disasters internally displaced 44,000 people.

A substantial proportion of the population is therefore vulnerable, disabled, widowed, and are elderly citizens who need carefully targeted and professionally managed assistance. However, the government's programmes in reducing poverty and vulnerability were not effective. In 2017, the government stated that it cannot afford large-scale national safety nets or tax-based transfer programmes, but committed to expanding pro-poor public spending. National systems for prevention, reduction, responding and adaptation to the shocks are extremely weak. The government mostly relies on humanitarian assistance from the international community.

Conflict and natural disaster internally displaced more than 202,000 and 44,000 people respectively. The return of 296,000 refugees from Iran and Pakistan added further pressure on humanitarian assistance in 2017. Afghanistan, therefore, suffers from uncertainty and unpredictable risks. Weak state capacity and deficit of legitimacy have increased the country's vulnerability to political and economic shocks.

Building resilience requires addressing the root causes of weak legitimacy, state weakness, insecurity, and lack of development. It is important to use the space for response to emergencies for building a long-term capacity by balancing the focus between short and long-term objectives. But any short and long-term response to be effective needs to build on the existing institutional and human capacity at local and national levels. As the threats which Afghanistan face are tremendous and the resources limited, a careful prioritisation is imperative.

<sup>68</sup> World Bank, Afghanistan Poverty Status Update—Progress at Risk, Accessed 11 April 2018, <http://www.worldbank.org/en/country/afghanistan/publication/afghanistan-poverty-status-update-report-2017>.

<sup>69</sup> Rasad News Agency (2017), Wuzarat-e Sehate Ama: Amar-e Malulin Ro Ba Afzaish Ast (The Number of Disabled People are Increasing), Kabul.

# Lessons learned and prospects

## 7

Some of the lessons learned from Afghanistan can be classified into six categories which are discussed below.

- 1. Too little investment in the first years after war.** While because of a protracted war, the economy had contracted and the state remained weak and fragmented, donors provided little aid for reconstruction and recovery and invested little in building public administration and the security sector in the first years following the fall of the Taliban. In the two years following international intervention, Afghanistan received 5 to 10 times less per capita aid in comparison to Bosnia and East Timor. The needs for building the security sector were underestimated. In particular, the target for the total number of army and police personnel was unrealistic. This negligence created a gap that the insurgents and other spoilers later capitalised on.
- 2. Overconcentration on short-term objectives.** The war on terror dominated the US and its allies' engagement in Afghanistan. This type of engagement and the subsequent state building strategies did not foster effective state building in the long run. While the focus on quick impact results that aimed to defeat Al Qaeda, and keep the Taliban at bay were crucial, it diverted much of the political attention and financial resources away from building the economy and state institutions. Therefore, a lack of balance between short and long-term objectives had adverse effects on building state legitimacy and effectiveness as well as the economy.
- 3. An extreme neglect of external adversaries.** A major caveat in the state building process and international support for Afghanistan was the neglect of external adversaries. The insurgency proved to be a major obstacle in relaxing some of the constraints that Afghanistan faced to get out of fragility. The support from Pakistan's state in the form of safe havens, impunity, and logistics enabled the Taliban and Haqqani Network to reorganise and fight against the Afghan government and international troops. Only in 2017 did the US administration prepare a new policy, in which it officially recognised that Pakistan's support to the Taliban has been a major source of instability in Afghanistan.

- 4. Ineffective aid modality and aid fragmentation.** While donors and the international institutions in Afghanistan adapted different aid modalities, as far as the total share of aid is concerned, a large portion of it bypassed the Afghan government budget and national systems to expedite project implementation in response to state weakness and corruption. However, overreliance on this method created a parallel public sector which was fiscally much bigger than the permanent public sector, unintentionally undermining the development of permanent state institutions, private sector, and in some cases state legitimacy.
- 5. Neglecting the legitimacy of state institutions.** Too much attention was paid to personalised politics and personal legitimacy. Corruption and a lack of impartiality in state institutions have seriously undermined the confidence of people in these institutions. Police and the Independent Election Commission are two notable examples. Widespread corruption in the police, and irregularities and fraud in the electoral process, severely damaged the legitimacy of the state. It shows that the process of building the state's capacity fell short in improving the quality and integrity of institutions, an important aspect in improving state legitimacy.
- 6. Underestimating the role of local public institutions.** Despite the fact that local public institutions at the provincial and district levels had to implement government policies and deliver services, they attracted little attention from the Afghan government and donors. This situation neglected the need for the development of these institutions.

These lessons are crucial for future developments. Afghanistan has the potential to pull itself out of fragility. This process, however, may require strategic rethinking. The following are a few feasible policy options that can help to relax some of the constraints that Afghanistan faces.

## **Strengthen political and institutional legitimacy**

To strengthen state legitimacy, the impartiality and credibility of the state institutions need to be assured. This could be achieved through policy intervention in four areas:

- 1.** The electoral system needs to be reformed to prevent future fraud and irregularities and be fiscally sustainable. This process requires consensus among the ruling elites, legislature, and the executive. In particular, as there is a lack of trust among different political actors, an increasing engagement by the UN, as an impartial actor in the election commission, may help in building trust.
- 2.** Citizen engagement needs to be strengthened. This could happen by deconcentrating power and enhancing downward accountability, wherein local participation in politics and development is increased.

3. Corruption has undermined both security and development. It has created a sense of unfairness and sentiment among citizens. To date, anti-corruption efforts have been ad hoc, ineffective, selective, and by and large politically motivated. Anti-corruption efforts, however, require adaptation of transparent and rule-bound measures in which media and civil society can monitor the progress.

### **Strengthen state capacity**

This process requires both short and long-term approaches. The strategies which the Afghan government and foreign donors followed to date were less effective and in some cases counterproductive. A lack of balance between building capacity and delivering public services as well as lack of a long-term strategy have hampered the development of state capacity. However, without the adequate ability to deliver minimum services and protect citizens, state legitimacy, economic growth, and security, among others, will be endangered. It is thus imperative to prioritise the building of state capacity with an aim to improve the quality of civil administration as well as the security sector. Four feasible policies can help:

1. Enhancing meritocracy and inclusiveness in order to shift the loyalty of public servants from their patrons, such as politicians and strongmen, to common interest.
2. Redefining the functions of and role of ministries and departments in Kabul and provinces. A blurred institutional role and overlapping agencies have undermined service delivery and implementation.
3. Increasing tax capacity, which is crucial to sustaining state building and expanding the reach of the state. To date, the success in reforming the tax system has been mixed. The government needs to rethink about the tax efforts beyond revenue collection. A comprehensive approach is imperative to use taxation as a tool to reinforce state building and state-society interactions. Given that Afghanistan has limited resources, national priorities needs be carefully identified.
4. Defragmenting state institutions and integrating a parallel public sector that was created by donors. Bypass tactics for delivering services while might improve implementation is not a viable and sustainable strategy. This has increased fragmentation and transaction cost. The defragmentation process requires that the bulk of aid to be channelled through the government budget and jointly managed trust funds or make them fully aligned with local priorities. This approach can increase the pressure to reform the state institutions and improve governance practices. While the situation has slightly improved in the last few years, the efforts were not adequate.



## Address external drivers of fragility

The resurgence of the Taliban insurgency and the Haqqani Network, by and large, has undermined security and state building efforts in Afghanistan. Since 2002, these groups have enjoyed impunity, had safe havens in Pakistan, and a great share of their revenue comes from narcotic business, extortion and contribution by regional networks. The leadership of these groups are based in Pakistan. To date, the US and its allies have failed to adopt an effective regional strategy that could convince Pakistan to change course. While the Afghan government expedited the process of a peaceful negotiation with the Taliban since 2010, no progress has been reported to date. The Taliban have refused to negotiate. While the US new policy for Afghanistan emphasise on the role of Pakistan and calls that it should terminate its support to the Taliban and Haqqani Network, it seems inadequate. There is an urgent need to adapt more comprehensive measures through multinational organisations, such as the UN Security Council, and regional organizations to build consensus and hold external spoilers to account.

## Targeted interventions to improve private sector development

The development of private sector in Afghanistan, by and large, depends on security conditions and the state capacity to promote rule of law and build the infrastructure necessary for economic activities, for instance, affordable access to energy. Until these conditions significantly improve, it is imperative to adopt targeted and conflict sensitive measures to sustain the gains and improve private sector development. There is thus an urgent need for a strategy to balance between short-term and long-term objectives in building the economy and private sector. The flow of aid through the government budget and aid with an emphasis on using local companies and domestic products can create jobs and provide a necessary incentive for the development of private sector.





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