

U.S. PROMOTION OF THE AFGHAN ECONOMY: IMPEDIMENTS AND OPPORTUNITIES

HEARING

BEFORE THE
SUBCOMMITTEE ON NATIONAL SECURITY
AND FOREIGN AFFAIRS
OF THE
COMMITTEE ON OVERSIGHT
AND GOVERNMENT REFORM
HOUSE OF REPRESENTATIVES
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U.S. PROMOTION OF THE AFGHAN ECONOMY: IMPEDIMENTS AND OPPORTUNITIES

TUESDAY, JULY 14, 2009

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON NATIONAL SECURITY AND FOREIGN
AFFAIRS,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,
Washington, DC.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2154, Rayburn House Office Building, Hon. John F. Tierney (chairman of the subcommittee) presiding.

Present: Representatives Tierney, Kennedy, Van Hollen, Murphy, Foster, Cuellar, Quigley, Flake, Duncan, Jordan, and Issa (ex-officio).

Also present: Representative Bilbray.

Staff present: Andy Wright, staff director; Elliot Gillerman, clerk; Talia Dubovi and Scott Lindsay, counsels; Brendan Culley and Steve Gale, fellows; Adam Hodge, deputy press secretary; Catherine Ribeiro, communications director, Hon. John F. Tierney's office; Mariana Osorio, Daniel Murphy, Ken Cummings, Cal Garner, and Robyn Russell, legislative assistants; Anne Bodine, fellow; Dan Blankenburg, minority director of outreach and senior advisor; Adam Fromm, minority chief clerk and Member liaison; Kurt Bardella, minority press secretary; Howard Denis, minority senior counsel; and Daniel Epstein and Jonathan Skladany, minority counsels.

Mr. TIERNEY. Good morning. I want to thank all of our witnesses for being here with us this morning, as well as our witness from Afghanistan. We appreciate all of the effort he has made to allow himself to be videoconferenced in today from Kabul.

I do note that the quality of the conferencing doesn't seem to be quite as good as some we've had in the past, so there may be a delay if we want to have an exchange on that basis. So we will leave some time for the answers and make sure everybody hears.

A quorum is present, and the Subcommittee on National Security and Foreign Affairs hearing entitled, "U.S. Promotion of the Afghan Economy: Impediments and Opportunities," will come to order.

I ask unanimous consent that only the chairman and ranking member of the subcommittee be allowed to make opening statements. Without objection, so ordered.

And I ask unanimous consent that the hearing record be kept open for 5 business days so that all members of the subcommittee

will be allowed to submit a written statement for the record. And without objection, so ordered.

Today, the subcommittee will take a look at the economic dimensions of the U.S. efforts in Afghanistan. Afghanistan's stability will depend in large part on what the United States, our partners and allies and, most critically, the Afghans themselves do over the coming several years to bring economic progress to a population ravaged by 30 years of war.

Observers note that the Taliban originally secured a foothold in Afghanistan, in part, because severe poverty continually dashed hopes for a better life. For the average Afghan, life was simply getting worse, with no good prospects for improvement anytime soon.

The Afghan government was unable to provide even the most basic services like electricity and potable water; justice was either slow, arbitrary or nonexistent; unemployment topped 50 percent; and police were either absent, or corrupt. Roads and irrigation canals had fallen into disrepair; and the once-productive agricultural base was so severely degraded that farmers, to make a decent living, chose to grow poppies rather than traditional products like wheat, dates, and pomegranates.

In short, following the Soviet withdrawal, the Taliban offered a different, albeit tyrannical, vision for Afghans increasingly weary of endless conflict and growing personal insecurity. And while the average Afghan was not supportive of the Taliban, per se, the post-Soviet era was so adverse economically that the Taliban were able to find a toehold, and eventually a safe haven.

After the fall of the Taliban and the arrival of the United States and NATO, there has been modest economic gain. Afghanistan has experienced rapid growth on the strength of the international donor community, especially the United States as its largest donor.

More than \$2.4 billion in new investment has been registered since 2003, two-thirds of which represent public investment financed through donor aid, and one-third foreign direct investment. As a result, in 2008, in terms of the GDP growth rate, Afghanistan ranked 24 out of 231 countries, with a 2008 real gross domestic product growth rate of 7.5 percent. Unfortunately, at present, this silver lining does not obscure the dark and ominous cloud over Afghanistan's economy.

Today, after almost 10 years, and \$37 billion of U.S. taxpayer funds, Afghanistan is still one of the five poorest countries in the world. Transparency International rates Afghanistan as one of most corrupt countries in the world, 176 out of 180. A 2009 World Bank report says Afghanistan is one of the most difficult places in the world to start a business. And in Foreign Policy Magazine's just-released 2009 Failed State Index, Afghanistan is rated as one of the least stable, most fragile states, 7th out of 177.

Last year, about 18,000 Afghans applied for asylum in Europe, nearly doubling the 2007 outward migration total. This was the largest spike in migration-seeking for any country in 2008, and one of the most common explanations offered by Afghans as to why they are leaving is that people can't find jobs.

This dismal scorecard and disturbing trend begs the question, what has been the net effect of the U.S. support to Afghanistan to remedy the underlying economic and social conditions that allowed

the Taliban to find an initial safe haven in the first place? Unless we begin now to improve the quality of life for the average Afghan, those dismal statistics are likely to be go unchanged and the security conditions will continue to deteriorate.

Everyone, from development professionals to counterinsurgency experts to senior ranking Afghan officials say the shift from combat operations, to counterinsurgency operations, to post-conflict operations is largely dependent on growing the Afghan economy. As former U.S. Commander in Afghanistan, General David Barno, recently put it, “Only if we solve the economic problems of Afghanistan can we ever hope to win the longer war.”

Accelerating economic development in Afghanistan is a central feature of the new U.S. Af-Pak strategy announced by President Obama on March 27, 2009. Reinforcing the importance of economic development to the overall strategy, National Security Advisor James L. Jones recently noted, that the Obama administration wants to hold troop levels here flat for now, and focus instead on carrying out the previously-approved strategy of increased economic development, improved governance, and participation by the Afghan military and civilians in the conflict.

Economic development is vital for a stable, secure, and prosperous Afghanistan. In other words, we must move—and the sooner the better—from policy pronouncements on paper to concrete actions on the ground.

I have just one final note. We originally envisioned having a second panel here this morning with administration representatives, but scheduling issues require that we reserve that prospective for a later date, probably at the end of the summer or in the fall. By then, we should expect that the administration’s new Afghanistan team will have had sufficient in-country experience to better shed light on the issues that are raised at today’s hearing.

So, with that, I refer to Mr. Flake for his opening comments.

Mr. FLAKE. I thank the chairman. He outlined pretty well, I think, the purpose of the hearing and what we hope to accomplish here.

What I am particularly interested in is the interplay between security and economic development. Obviously, much of the country is too dangerous for a lot of nonprofits or others to work in, absent security, so I am interested in your perspective on what we need to do moving ahead, and at what point we are likely to see economic growth and investment vastly improved.

As mentioned, I’m anxious to hear the administration explain their goals and objectives as well, and I guess we’ll have to wait a while for that, but I look forward to your testimony. Thank you.

Mr. TIERNEY. Thank you, Mr. Flake.

Now we are going to receive testimony from the panel that’s with us today. I will start by introducing all of them briefly.

Ms. Mildred Callear serves as the executive vice president and chief operating officer of the Small Enterprise Assistance Funds [SEAF], a not-for-profit manager of private equity funds investing in small- and medium-sized enterprises and emerging markets. She also serves on the board of Afghan Growth Finance Fund, a \$25 million investment fund which provides long-term capital to start-up enterprises in Afghanistan.

Prior to joining SEAF, Ms. Callear served for almost 20 years with the Overseas Private Investment Corp. She holds a J.D. from Georgetown University Law Center and a B.A. from the University of Illinois.

Welcome.

Dr. Mohammad Usman is an agricultural economist and a former senior advisor to Afghanistan's Ministry of Agriculture, Irrigation and Livestock. In that role, he focused on improving Afghanistan's agricultural policies and public resource efficiency.

Dr. Usman has performed similar work as a consultant with the World Bank and a number of other governments around the world, including Pakistan, India, and Egypt. Dr. Usman holds a Ph.D. from Colorado State University.

We are happy to have you with us, sir.

Mr. Aly Mawji—sir, I hope I pronounced your named properly—is the country director for Afghanistan with the Aga Khan Development Network, where he manages the Network's programs and relations with the Government of Afghanistan. He has served with the Aga Khan Network since 1996 and has held various positions around the world, including negotiating and operating a large-scale humanitarian program to Afghanistan in the late 1990's.

Mr. Mawji holds a degree from the University of London.

We are glad to have you with us, sir, and thank you, for surmounting the inconveniences imposed on you for video teleconferencing.

Mr. Jeremy Pam currently serves as a visiting research scholar for sustainable development at the U.S. Institute of Peace. Prior to that, he was co-director of the U.S. Central Command Assessment Team. From 2006 to 2008, Mr. Pam served in Iraq with the U.S. Department of the Treasury, both as a financial attache at the U.S. Embassy in Baghdad, and as a member of the Government Assessment Team.

Mr. Pam is a retired captain with the U.S. Air Force, holds a J.D. from Columbia Law School, an M.A. from Columbia University, and an A.B. from Harvard college.

Thank you for joining us, sir.

I want to thank all of our witnesses for being here today to share your substantial expertise. I also again would like to thank the folks at the U.S. Embassy in Kabul for helping us to arrange to have Mr. Mawji testify through their facilities.

We swear in the witnesses as a matter of course on this panel, so if you would kindly raise your right hands.

[Witnesses sworn.]

Mr. TIERNEY. The record will indicate that all the witnesses have answered in the affirmative.

I do want to say that all of your written testimony, which we appreciate greatly, has already been put on the record by unanimous consent. So we ask that you summarize, to the extent possible, or supplement, if you'd like. We like to allot each witness about 5 minutes to share with us their comments, after which we will have some questions and answers back and forth.

Ms. Callear, why don't we start with you, if we could, and invite you to give your remarks.

STATEMENTS OF MILDRED CALLEAR, ESQ., EXECUTIVE VICE PRESIDENT AND CHIEF OPERATING OFFICER, SMALL ENTERPRISE ASSISTANCE FUNDS [SEAF] AND AFGHAN GROWTH FUND, EXECUTIVE BOARD MEMBER; MOHAMMAD USMAN, PH.D., AGRICULTURAL ECONOMIST, FORMER SENIOR ADVISOR, MINISTRY OF AGRICULTURE, IRRIGATION AND LIVESTOCK [MAIL], GOVERNMENT OF AFGHANISTAN; ALY MAWJI, AGA KHAN DEVELOPMENT NETWORK [AKDN], AFGHANISTAN COUNTRY DIRECTOR; AND JEREMY PAM, ESQ., VISITING RESEARCH SCHOLAR, SUSTAINABLE DEVELOPMENT, U.S. INSTITUTE OF PEACE

STATEMENT OF MILDRED CALLEAR, ESQ.

Ms. CALLEAR. I appreciate this opportunity to talk about the role of small and medium enterprises, and what that means to Afghanistan's long-term economic development and to the security of the country, because we do believe that those are deeply linked and that they're mutually dependent on one another.

Jobs do have to be created and income has to be generated if you want to improve security; and, in our view, we are looking at where those jobs are most likely to come. What we are finding is that the SME sector, indeed, is where the largest proportion of the employment base exists today; and it also provides the majority of available goods and services. So, in our view, SMEs are a very critical part of the equation, for both economic development and security in Afghanistan.

Industry and products need to be improved. More value needs to be added in the country. And we think that, in fact, will come if we can do a better job of linking up rural farmers and others in the rural areas to more urban processing centers, distribution, warehousing, and other facilities that are needed to take those primary products and add the value that will ultimately bring economic growth to the country.

SEAF has done this type of investing in 25 different funds, 290 individual investments all throughout the emerging markets. We've been around for about 20 years. So, although we recognize that Afghanistan has some very unique challenges, we think that many of the challenges that small companies face throughout the emerging markets are, indeed, very similar; and we believe that you've got to approach this whole exercise not wearing your not-for-profit hat, but with a lot of commercial discipline. Because, in the end, only a commercially successful company is going to have long-term economic benefits for the country.

So a little over a year ago, in 2008, SEAF created Afghan Growth Finance as a nonbank financial institution in Afghanistan. We are providing growth capital anywhere from \$50,000 to \$2 million. So we are well above micro finance, but we are far below what the average target size for some of the larger projects might be. We are making medium- to long-term loans. We've got a fair amount of flexibility on how we can structure those loans, so that the companies can pay out of their cash-flow.

So far, we've committed \$5 million to 10 different loans. We expect \$10 million to be committed by the end of this calendar year, which would mean that we have effectively placed half of the \$20-

something million that we have at our disposal through cooperation with OPIC, through a risk credit facility they've made available to us.

The funds are being used to purchase machinery, to establish processing and manufacturing facilities, and to provide working capital. And what we're finding is that there is, in fact, a strong demand for the loans, because the commercial banking sector is not reaching this level of company.

What we also are finding is that the benefits go beyond just the financial benefits to the enterprise itself. We've done a fair amount of analysis in terms of what that developmental impact is in other parts of the world, and what we're finding is that Afghanistan is very similar and in some cases the benefits are even stronger. But what we have found is that every dollar that you invest into a small company, in fact, generates an additional \$12 in benefits to the broader stakeholder community. And that means customers, that means employees, it means government through taxes, it means suppliers, it means others in the broader community.

What we're seeing in Afghanistan is that, after a year in operation, some of the companies that we have funded have been able to increase their employment by as much as 50 percent; they have increased their wages by as much as 30 percent, and they have taken what are largely unskilled employees and trained them and provided them with a skill set that makes them much more marketable in the future.

We have invested in several companies in the agribusiness sector. We've got a licorice root and extract processor that is exporting to China. Dried fruit and nuts that were manually being processed and sorted, now we've helped them acquire production equipment, so they've got a processing line. Their daily production is 20 times what it was, their gross sales are up 400 percent, and we've helped them find a new export market in China. And we've also got a raise in export in the agribusiness sector. So we calculate that a thousand or more suppliers and farmers and input providers are now linked into these three or four agribusinesses that we've funded.

And, of course, the other message that is out there is that there are ways to make a good living, as an alternative to poppy cultivation.

We've got two companies that are producing construction inputs in-country. So instead of importing circuit panel boxes and metal pipe, they are being fabricated locally in Afghanistan, going into construction projects, so that more value again is being created in the country. The overall cost of the construction is going down, you're getting training in terms of the workers, and you're seeing better prices overall, in terms of the projects that are being built.

We have a renewable energy company that's quite interesting. They are producing wind and solar panels; and they have a new, unique design that is being deployed for the Afghan police in their border posts. They are doing it on a pilot basis now. They've got five under way. If that's successful in replacing diesel generators, we could see in the future that this company will be able to expand to 70 or 80 additional posts, which we think is a wonderful story,

not only for the economic benefit of this production and design in Afghanistan, but obviously from an energy standpoint as well.

We have a technology and Internet service provider that's providing cheaper, more reliable access to the Internet, outreaching to schools, hospitals, government, military, to a whole range of institutions that will make good use of it.

In the media area, we've got an Afghan-language local broadcasting program that we are funding through a media company. And they're also broadcasting to the United States and to the EU, so the Afghan perspective is getting out to the rest of the world.

Now, of course, there are challenges. You've mentioned many of them. I think one of the comments I would make on the challenges, whether it's security or the lack of infrastructure, is that SMEs do have ways of being very flexible and adaptable. They are less visible in terms of being targets, whether it's targets for corruption or targets for terrorism, they're not the big, high-profile entities that will gain a lot of publicity, and so they tend to be left alone a lot more regularly. But they are serious issues that all of our companies are dealing with.

The other thing they deal with is an untrained work force. What that means is they have to invest in that work force; and, overall, we're finding that is, in fact, what's happening. And they are taking low-skilled employees, they are training them, they become more productive, the wages go up, and then, overall, what we are finding is that you've got a low-skill base that's being raised and you've got wages that are growing. And as the work force is trained and companies become more productive, they increase, with capital as well. They are able to increase that overall size of the work force.

Mr. TIERNEY. Thank you. Do you want to wind up for us? We are going to get to questions and answers, too; and I am sure we will cover a lot of this.

Ms. CALLEAR. Absolutely.

So I think really, at the end of the day, lack of financing does remain a challenge, but more than capital is needed. It's a partnership. It's technical assistance. It is a variety of support. And we think that, overall, working with OPIC and others in the U.S. Government, we hope to expand the program; and we think that our initial year has been quite successful and had very good results.

Mr. TIERNEY. Thank you very much.

[The prepared statement of Ms. Callear follows:]

Written Testimony to the Subcommittee on National Security and Foreign Affairs.

"U.S. Promotion of the Afghan Economy: Impediments and Opportunities."

*Room 2154, Rayburn House Office Building
10:00 a.m.*

July 14, 2009

**Submitted by:
Mildred Callear, Executive Vice President and Chief Operating Officer
Small Enterprise Assistance Funds (SEAF)**



Chairman John F. Tierney and Members of the Committee:

Thank you for inviting me here today to discuss the prospects for private investment—particularly investment in small and medium enterprises (SMEs)—in Afghanistan and what this means to the security and sustainable development of the country. It is evident that Afghanistan’s long-term security and economic development are deeply linked and mutually dependent. In order to experience long-term sustainable security in Afghanistan, socio-economic conditions have to be improved throughout the country, especially in the rural areas.

Jobs have to be created, income has to be generated, Afghan industry and products have to be improved and promoted, and the reliance on foreign assistance has to be reduced. More importantly, the international community has to coordinate more efficiently to implement quick impact projects that maximize returns and sustainable outcomes.

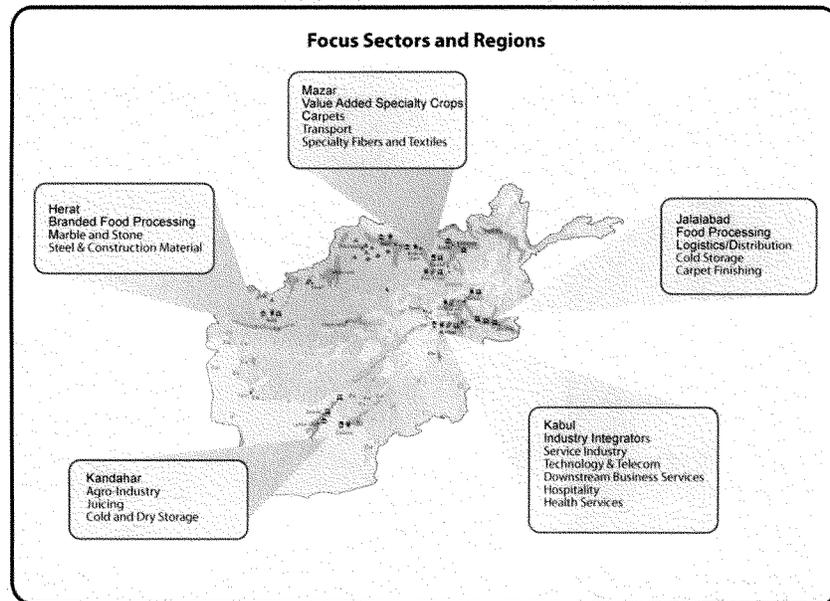
The mission of the Small Enterprise Assistance Funds (SEAF) is to further economic development by providing capital and needed technical assistance to create sustainable, for-profit small businesses in the emerging markets. SEAF’s experience in working on the ground in Afghanistan has reinforced our view that the best way to support economic development in Afghanistan is through direct investment in Afghan small and medium enterprises (SMEs). SMEs constitute the largest portion of the formal business base in Afghanistan and are the backbone of a growing and stable local private sector. The entrepreneurs behind these businesses could—and should—play a much larger role in development, but they are constrained by a lack of financing and technical assistance from both local and international sources.

Just over a year ago, SEAF created Afghan Growth Finance (AGF), a non-bank financial institution in Afghanistan, to focus on providing growth capital to SMEs in the country. With the support of the U.S. Government's Overseas Private Investment Corporation (OPIC), AGF has a USD 25 million lending facility that provides medium-term debt to growth-oriented SMEs in Afghanistan. We have seen firsthand that helping small companies grow by providing access to risk capital is a promising way to achieve sustainable development in Afghanistan by empowering the emerging private sector. AGF's success investing in Afghan SMEs demonstrates that SME investing not only leverages promising businesses, but also produces valuable economic and development returns to the local community, economy, and country.

SMEs are vital to the health and stability of Afghanistan as they constitute the largest portion of the employment base and provide the majority of available goods and services. Nevertheless, Afghan SMEs suffer from insufficient access to financing, crippling the small businesses from expanding their production and making a larger social and economic impact. While AGF currently meets a portion of the capital demands of SMEs in Afghanistan, there remains a large gap in access to structured debt financing for interested SMEs and no ability to access equity capital. Entrepreneurs seeking financing for their small businesses are up against the perception of local commercial banks that SMEs are too 'risky', for traditional loans as they lack sufficient collateral or connections, and yet they are too large for microfinance. This effective 'missing middle' in available financing drastically diminishes the prospects for sustainable development in Afghanistan by ignoring the necessity of cultivating a vibrant middle economy—a key element in job creation that is essential to poverty reduction, income equality, and general stability. In addition, SMEs need more than just lenders and capital—they need business partners. SEAF provides its portfolio companies with the technical assistance, access to markets and global knowledge they need to grow and succeed—all provided in a culturally sensitive manner using a local team that understands both the ways of local business as well as the potential for expanding well beyond the traditional ways to embrace the opportunities that globalization holds.

Since April 2008, AGF has committed approximately USD 5 million through ten loans to nine innovative and growth oriented Afghan SMEs, all of which received funding on market terms and are performing according to expectations. Investments range from USD 50,000 to 2 million with tenors of up to six years. AGF borrowers have used the funds to procure machinery, establish or create processing facilities, and fulfill their working capital needs. To date, AGF has invested in two construction component manufacturers, a licorice root and extract processor, a dried fruits and nuts processor, a raisin exporter, a media company, a printing and advertising firm, a technology and internet service provider, and a renewable energy corporation. An early assessment of the development and economic impact of AGF's investments has demonstrated that the benefit to the companies, employees, stakeholders and the local economy are consistent with results achieved

by and documented in SEAF investments in other parts of the world¹. Demand for our loans in Afghanistan is strong, as is the need for empowering local entrepreneurs to fill urgently needed products and services, providing sustainable employment opportunities, as well as creating economic success for entrepreneurs in a transparent manner.

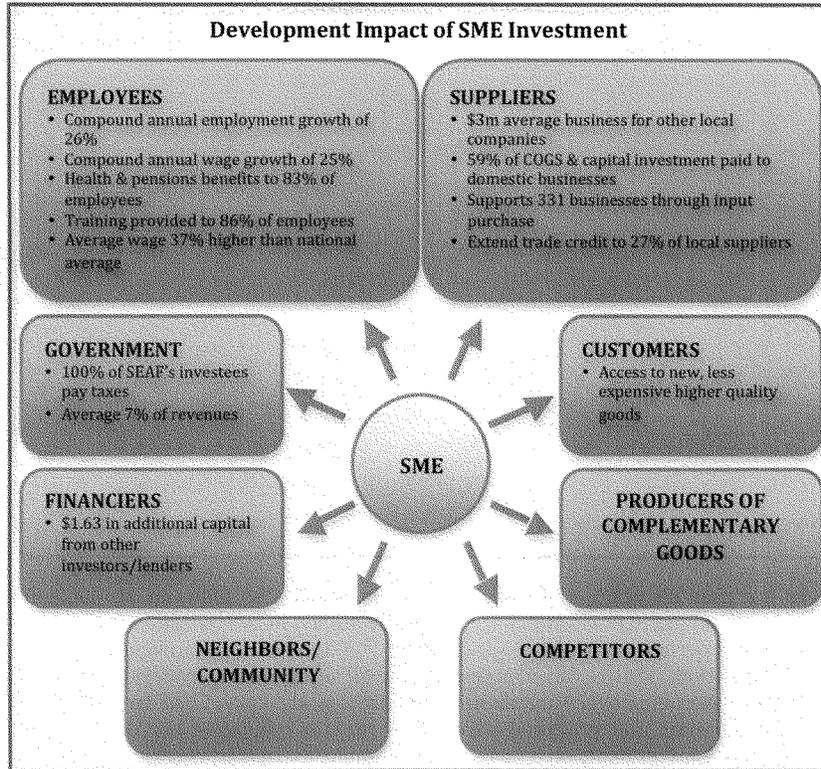


Over the past 20 years, SEAF has invested in nearly 290 SMEs in 30 countries through 25 managed funds and more than \$500 million in committed capital. SEAF's extensive experience has allowed it to identify and invest in promising companies that deliver both positive financial results, as well as significant economic and social benefits to their employees and their communities. Since 2004, SEAF has conducted in-depth analysis and produced a series of reports evaluating the development impact of our investments on a variety of community and government stakeholders.

We now have concrete evidence that growing small businesses create jobs for unskilled or low-skilled individuals who then receive training and see significant growth in their wages and overall benefits. In addition, each small company provides economic benefits to a host of other stakeholders—from its suppliers, customers, and competitors to local governments through tax payments and contributions to government social and pension schemes and to the local community through frequent philanthropic donations. SEAF's

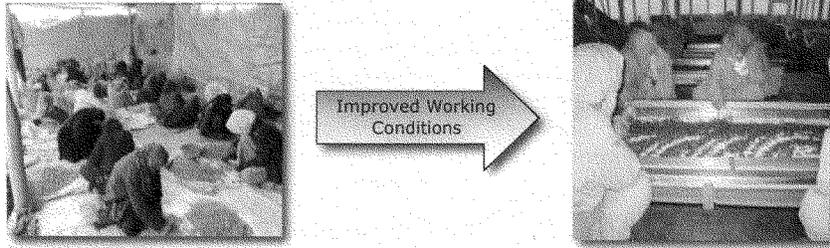
¹ See SEAF's Development Impact Report, October 2007, on our website (<http://www.seaf.com/impact.htm>).

analysis shows that for every \$1 invested in a small and growing business, an additional \$12 in benefits redounds to the local society. With stable and secure jobs and growing incomes, for the first time families can begin to plan for their futures—investing in improved housing, preventive health care and education for their children that can end the cycle of poverty and build the base for a more stable and secure society.



In the case of Afghanistan, AGF's portfolio companies have produced significant, measurable economic and social returns for the country, serving as a tool for poverty reduction and stability. Across the board, AGF's SMEs have expanded their workforces by approximately 50%, increased employee wages by an estimated 30%, improved working conditions, extended non-salary benefits among their workforce, and offered training opportunities for unskilled or semi-skilled workers. AGF's agro-processing SMEs have strong ties to over one thousand local farmers and input providers, to whom they provide consistent and reliable demand, assist in the extension of trade credit, bolster the market reputation for Afghan products, and encourage alternatives to poppy

cultivation for Afghan farmers. Two of AGF's borrowers manufacture construction components that have reduced the country's dependence on foreign imports by producing quality, locally manufactured products at lower prices that are then translated to the consumer and make local construction more affordable. AGF's media company disseminates important information throughout Afghanistan through public awareness programs and broadcasts to the United States and Europe, adding a locally broadcast perspective to the international dialogue on Afghanistan. AGF's renewable energy corporation is designing and building five renewable energy systems (wind and solar) for the border posts of the Afghan police, and, if successful, will expand this project to 70 other locations around the country. The success of this project can revolutionize the use of renewable energies in both on and off-grid regions throughout Afghanistan and the developing world. Finally, AGF's technology and internet service provider has expanded Afghans' access to more reliable and less expensive internet options, while making a deliberate effort to offer greater internet access to schools, hospitals, and government agencies.



As a result of the country's years of instability, compromised rule of law, and violence, Afghanistan faces a variety of unique challenges to sustainable development and greater stability. However, with the proper avenues for financing, SMEs have the potential to offer a promising solution to these challenges.

Afghanistan currently suffers from a lack of security that hampers foreign and domestic investment, compromises transportation and employee safety, and augments overhead costs. By virtue of their smaller size however, SMEs are more nimble, less visible and less attractive targets.

Years of instability in Afghanistan have led to poorly developed infrastructure for the country, including unreliable electricity and insufficient or poorly constructed roads. Inadequate infrastructure increases the costs of doing business, effectively reducing efficiency and competitiveness and deterring companies from starting or expanding operations in Afghanistan. SMEs typically begin their businesses locally, and as they expand, often make the localized investments in the infrastructure of their communities that are necessary for their businesses to prosper—clean water, improved access roads, lighting and improvements to the public spaces surrounding their businesses like parks, parking and playgrounds. In addition, a growing SME population means that more and more infrastructure development services can be provided locally rather than by foreign

contractors, effectively reducing costs to the government and bolstering community involvement.

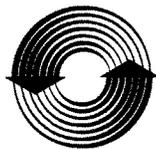
Corruption and bureaucracy are also major concerns for Afghanistan. Nuisance taxes and corruption are present at every level of the government, and an inconsistent application of laws and tax policy lead to a playing field that is not level for all companies. As formal enterprises, SMEs contribute taxes to local governments, in the form of corporate income tax, business receipts taxes, and other taxes. These taxes support the stability of the Afghan government, generate revenues for creating a social safety net and providing needed services and promote the establishment of a formalized Afghan economy. Additionally, formal SMEs encourage and demand greater regulation and transparency within their government and support greater equality in tax and other laws and regulations.

Instability and violence in Afghanistan has also left the country with depleted employment opportunities and a generally unskilled workforce. This makes it especially difficult for companies to recruit and retain qualified staff. Throughout the developing markets in which SEAF works, we have found that, on average, 87% of SME employees are unskilled or low-skilled workers. In Afghanistan, that number is likely even higher, but because SMEs are locally built and depend on their local workforce, these small businesses invest in their employees, promoting internally and providing training and skill-development that improves the skill level of the workforce. With increased skills, productivity and wages both rise and SMEs grow rapidly.

Rooted in their local communities, Afghan SMEs are positioned to identify unmet local consumer demands and, with proper access to financing, work with other stakeholders to address market deficiencies. Customers receive greater choice, improved quality, and lower prices and competitors benefit from demonstration, spillover effects, and improved reputations of local production. In addition, Afghan SMEs make valuable contributions to their surrounding communities. On average, each AGF portfolio company contributes USD 1,000 annually to charities and other local community causes. Such support has included contributions to local infrastructure and support for orphanages and community events. Finally, as formal enterprises, these companies contribute taxes to local governments, in the form of corporate income tax, business receipts taxes, and other taxes—averaging 5 percent of revenues in the year 2008. These taxes support the stability of the Afghan government and promote the establishment of a formalized Afghan economy.

There is little argument that Afghanistan will continue to need assistance from the international community to direct its country on a more stable, secure and sustainable path. SEAF's work throughout the world in conflict and post-conflict emerging markets has demonstrated that a key component of sustainable development is a thriving middle class, with formalized businesses, growing employment and greater ties to the international markets. Over the past year, AGF has proven that this type of risk capital investment can empower a company to overcome its country's challenges and produce higher value added and top quality products for both domestic and global consumers, while positively impacting the stabilization and growth of its community and country.

Access to capital is a key constraint to growth for promising Afghan SMEs, and while AGF is successfully meeting the needs of some of these businesses, the demand for both debt and equity capital exceeds the supply. SEAF applauds OPIC's willingness to partner with us to tackle the SME financing challenge in Afghanistan and we look forward to working with OPIC and others in the U.S. Government to expand the capacity of AGF to provide both the financing and technical assistance that SMEs need for growth and that Afghanistan needs to achieve its full economic potential.



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Mr. TIERNEY. Dr. Usman.

STATEMENT OF MOHAMMAD USMAN, PH.D.

Dr. USMAN. Chairman Tierney, Ranking Member Flake, and the members of the subcommittee, first of all, I want to thank you for giving me this opportunity to share some of my insights on this issue.

The agriculture sector has the potential to reestablish its historical role in nurturing growth and development in Afghanistan. However, as you mentioned, in the last 30 years, agriculture went through devastating effects. Most of the infrastructure of agriculture, which are rooted in research and irrigation systems, seed multiplication farms, and laboratories, have been completely destroyed. And as a result of all these are now gone. We once enjoyed food sufficiency, and now we have a chronic food deficit.

And the farmers, due to economic pressures, and pressures from the drug lords, have reverted to poppy production. Afghans lost a share of fruit and nut exports in the international markets. If the economy, of which agriculture is a vital component, would not be improved, the current situation of \$14 of import for every \$1 of export could not be continued without considerable food or aid, or revenue from the illegal crops.

In 2006, the Ministry of Agriculture, with the help of donors, established a comprehensive national development agricultural plan. And the plan priorities of agriculture have been identified: food security, expansion of high-value horticulture crops, production of livestock, and cultivation of natural resources.

Unfortunately, the master plan has not been fully implemented, due to the position of some donors insisting that: the development plan should be initiated at the community and village level, that extension and research should be conducted by the private sector, that current NGO's operation arrangements should continue, and that the focus should be on rural poverty alleviation, instead of focusing on increasing farm production. While these positions have merit and are necessary, especially in the long run, such efforts are not sufficient or useful in establishing the solid foundation necessary for agriculture to develop.

Based on my thorough review of the general political and economic situation in Afghanistan and potential problems with its agricultural sector, I would strongly recommend that these six actions must be taken immediately. These actions proved to be successful in Afghanistan during the 1970's; and, with appropriate modifications, they will solve the agriculture situation once again today.

First, the overriding objective of any project and program should be to enhance government credibility in assisting its citizens. Right now the government lacks visibility in the rural areas especially. While all parties in agriculture should work in a coordinated and coherent way, the government must play a leading role in the implementation of investment program? It is imperative that donors and NGO's take a back seat position by limiting their involvement to advisory functions, institution building, project design, and the establishment of proper accounting, monitoring, and reporting systems. Through this arrangement, transparency and accountability

would improve, government visibility would be strengthened, and the expenditures of the NGO's on security would be reduced.

Second, a coordinated effort by all parties should be made to strengthen the nation's research in extension capacities. Re-activate seven strategic research centers to serve as the hub of change for agriculture. The extension cadre will need to be strengthened, to disseminate improved practices to the farmers and to convey farmers' problems back to the researchers for resolution.

Third, it is strongly recommended that a viable regional agricultural credit system must be established, in order to gain farmer support, and to enable the farmers to finance modern technology to meet their needs.

Revitalization of the Agricultural Development Bank, with its past proven record, must be considered for channeling credit and deposits to the farmers.

Fourth, improving irrigation efficiency, and the rehabilitation of the irrigation system with the expansion of irrigation areas is very important. Afghanistan receives about 75 billion metric cubes of water in the form of rain and snow yearly, just 20 billion metric cubes of which is used mainly for agriculture, with water-use efficiency of about 25 percent. With efficient forms of irrigation techniques in farm water management, this water use efficiency could be doubled.

In addition, arable land in Afghanistan is about 3.3 million hectares. However, with proper investment, it could be increased to 5 million hectares.

Prior to the Russian invasion, there were several new projects in the investment pipeline, such as Khush Tepa, diverting water from Amu Darya, and irrigating 600,000 hectares, which was halted due to political unrest. These projects need to be reconsidered for investment.

Fifth, farmers should be encouraged to organize themselves in production, marketing, processing, and water use associations.

Six, consideration should be given to procurement of food and rations for foreign military and civilian personnel locally.

Thank you, sir.

Mr. TIERNEY. Thank you very much, Dr. Usman.

[The prepared statement of Dr. Usman follows:]

Testimony of Dr. Mohammad Usman
Formerly Senior Policy and Planning Advisor to the Minister of Agriculture in Afghanistan
Before the Subcommittee on National Security and Foreign Affairs
July 14, 2009

The Roadmap for Peace in Afghanistan Must Include a Plan
For Rejuvenating the Agricultural Sector of the Economy

The Importance of Agriculture in the life of the Afghan people

1. The agricultural sector has the potential to reestablish its historically prominent role in nurturing Afghanistan's growth and development. A robust agricultural sector would enhance employment, improve the trade balance, reduce poppy cultivation, and help maintain peace and prosperity in Afghanistan. Currently, however, the agricultural sector is suffering from a lack of adequate investment and the absence of an effective investment strategy and program. This paper attempts to identify some of the major problems with the agricultural sector in Afghanistan and offer recommendations for future development.
2. Farmers spend most of their income on non-traded, locally produced goods and services which are generated by part-time farmers and landless rural dwellers. As a result, increasing farmer income has a multiplier effect in creating jobs for non farm workers and local businesses. Currently, about 80 percent of Afghans live in rural areas and rely directly, or indirectly, on agriculture for their livelihood. Although three decades of war and upheaval have severely stifled growth in the sector, agricultural sector still accounts of about 50 percent of GDP, provides about 70 percent of employment, and makes up almost all the small export earnings for the country.
3. Prior to the Russian invasion of Afghanistan, the agricultural sector was moving forward. Its growth rate was keeping pace with the growth rate of the population. During this era, the country was almost self sufficient in wheat, the main staple food of the population. The export of agricultural products was expanding and foreign exchange earnings for fresh and dried fruits and nuts constituted about 40% percent of large and growing export earnings. The Central Bank enjoyed foreign exchange reserves of about \$500 million. Private sector activities in the agriculture had considerable support from public and semi-public institutions. The Ministry of Agriculture was able to attract and retain a relatively high caliber technical staff, establish a functioning adaptive research and extension system, and mobilize capacity for controlling contiguous animal and plant diseases. The Ministry of Irrigation was making significant progress in improving irrigation networks and bringing new land under irrigation. The Afghan Agriculture Development Bank established among international experts as an effective and efficiently run credit institution in the region.

4. Three decades of turmoil have inflicted a devastating blow to agriculture. Most of the agricultural infrastructure such as irrigation networks, research and training stations, and laboratory facilities have been destroyed or rendered non-functional. All 24 research stations (7 main and 17 sub-stations) are no longer functioning. The offices and laboratories of these research facilities have been destroyed. Almost 40 percent of irrigation systems are still not functional. Plant and animal diseases such as foot and mouth, render pest, and locust and sun pest have re-emerged and threaten Afghanistan's livestock and crops.

5. Of critical importance, the agricultural sector's technical staff and support system were hit hard by the loss of professional cadres and the break-down of the flow of modern technology transfer networks. Most of the professional staff were either killed or left the country. The small number that remains with the government is generally out of touch with recent technological breakthroughs, and their field activities are severely limited due to unavailability of operation funding and mobility. In addition, donors and Non Government Organizations (NGOs) provide uncoordinated assistance independently and directly to the community and villages, bypassing the line ministries administration structure and undermining the rebuilding of necessary capacity in the public sector-especially in the absence of other functioning institutions. The NGOs have further depleted the technical cadre of the line ministries by providing attractive employment opportunities with lucrative salaries and allowances. The government budget will not be able to support higher salaries until it has a stronger tax base, and it will not have a stronger tax base until economic activity recovers. Agriculture remains the most important and promising economic base in the near future.

6. Thus, while Afghanistan's neighbors made considerable leaps forward, doubling and tripling their productivity, agricultural production of licit crops experienced a downward trend in Afghanistan. Under economic pressure and the pressure of drug lords, farmers have resorted to production of illicit drugs, such as opium and marijuana. As a result, the country has moved to chronic deficit in the production of staple foods.

7. The continuing deficit in agricultural production of food supplies will have a negative impact on other tangible achievements that have been made in health, education, and security. These constraints in agriculture have contributed towards the present trade imbalance of one dollar of exports for every 14 dollars of imports. Without a major rejuvenation in the growth of legitimate crops and other agricultural products (e.g. from livestock and forestry) the country will remain dependent on considerable foreign aid or revenue from the illicit production of poppy.

Lack of Coordination Among Donors, NGOs and Government Agencies is a Major Obstacle

8. In 2006, the Ministry of Agriculture, Irrigation and Livestock (MAIL) identified the priorities and obstacles in the agricultural sector and developed, with the assistance of donors and the NGOs, a comprehensive Agricultural National Development Plan (ANDP) ("the Master plan") which was endorsed by the Cabinet. This Plan called for collaboration and coordination of all parties in the agricultural sector. Unfortunately, the ANDP has yet to be fully implemented due to resistance from some donors. More specifically, some donors insist that the action plan should start at community and village levels,

that extension and research should be conducted by the private sector, that current NGOs' operation arrangement should continue, and that the focus should be on rural poverty alleviation instead of focusing on agricultural production. While these positions have merit and are necessary-specially in the long-run, such efforts are not sufficient or useful in establishing the solid foundation necessary for the agriculture to develop.

9. The Country's present circumstances demands that the government must establish its credibility with its citizens through establishing security, the rule of law, accountability, and visibility in rendering public services. Establishing proper national advisory services in agriculture such as research and extension services, and provision of credit are essential in addressing farmers' problems and improving government credibility. These services would, for example, improve farmers' revenue, and thereby significantly contribute to alleviating poverty in rural communities and improve the government's visibility to a major segment of the population. Strengthening national advisory services will have an immediate and broader impact on improving national growth and productivity compared to the elaborate, time consuming method of designing a development agricultural plan for each village or community- especially when key problems require coordination at levels above and beyond the village or community. Even in the golden era of the late 70's, Afghanistan lacked adequate technical staff in the central government level to design a development project and usually relied on outside consultants for this type of work. One wonders how a coherent national development strategy and plan could evolve from 35,000 villages or even from 18,000 communities, where most people are not aware of modern agricultural technologies, and struggle daily with the difficulties of hunger, illiteracy, and fear of persecution for warring groups.

10. In the last seven years, a great deal of energy, resources, and precious time were wasted, with little impact on the agricultural sector's national performance. There is little doubt, that if all the parties jointly worked in a coordinated fashion with the government's technical institutions, accountability, transparency, and efficiency would have been established at many levels in the delivery of technical services by now. At the same time, on-the-job training for the technical staff would have been enhanced through learning-by-doing. Also, it should be emphasized that considerable local and overseas technical training is still needed for qualified staff to catch up with the current technology.

Priorities and Bottlenecks in Agriculture

11. The priorities in Agriculture have been indentified to be food security, expansion of the horticultural subsector, increased productivity of livestock, and preservation of natural resources. Food security implies that a majority of the population has access to adequate quantities and quality of food, either by growing it or by having sufficient money to buy it. Wheat is the staple crop of the country and it occupies more than 70 percent of irrigated land and almost all of the rainfed land. The yield per hectare of wheat which was once on a par with other countries in the region, at present is estimated to be about 1.6 to 2 tons per hectare for irrigated land and about 0.6 per hectare for rainfed lands. Neighboring countries get about 4.5 tons per hectare from irrigated land and about 2 tons per hectare from rainfed land. This low productivity is explained by the inefficient irrigation practices, poor quality of seed, low usage of chemical nutrients, the absence of modern technology, and inefficient traditional

cultural practices. Also many of the villagers most experienced in farming and horticulture or the breeding and raising of livestock were killed in the turmoil of the last 30 years, or fled to refugee camps where they were unable to pass on the requisite skills to the next generation, who have returned to the country but without the guidance of their more experienced but now deceased elders.

12. Unless proper action is taken to mitigate these problems, Afghanistan will remain a deficit country even under the conditions of normal rainfall. For example, in 2002, a normal rainfall year in the region, a significant number of farmers in the northern part of the country did not bother to harvest their crop due to the high cost of harvesting and the falling market prices as a result of cheap imports from neighboring countries- including the distribution of large quantities of food in the form of humanitarian aid that was imported from abroad rather than sourced in other parts of the country.

13. Afghanistan has a comparative advantage in horticulture, particularly dry fruits and nuts. About 188,000 hectare of the land area is under intensive, double cropping, cultivation. Although fruit and nut orchard area shrank by almost 50% from its pre-war years, it still occupies around 94,000 hectares. During the pre-war period, Afghanistan provided 20% of the global market for raisins and dominated the pistachio markets, earned about 40% of its foreign exchange from export of horticultural crops. A preliminary farm budget analysis shows that the revenue from two hectares of horticultural crops, such as almonds, would be equal to the revenue of one hectare of poppy. It would also take anywhere from 14 to 22 hectares of wheat to substitute for the revenue of one hectare of poppy. Afghanistan's dried fruits still enjoy premium prices in India's growing markets. Although the farmers receive higher revenue from the high value crops, the potential exists to double the productivity of the present orchards and expand substantially the area of high valued crops. To get the full benefit of precious irrigated land, the long-run strategy should be to free irrigated land as much as possible from wheat production and put it under higher revenue generating horticultural products. The lack of modern production and processing technology, transportation problems, inaccessibility of credit, and the unavailability of critical mass are the main obstacles to ensure the growth of this subsector.

14. Increased production and productivity of Livestock is another priority for improving rural income. Livestock provides draft power on the farm, milk and meat for household consumption, and foreign exchange from the sale of wool, hides and skins in international markets as well as raw materials for domestic carpet and leather industries. *Extensive* livestock production, dominated by nomads using grazing land that constitutes about 45 percent of the country's land area, is gradually shifting to *intensive* livestock production. The majority of farmers only keep a few animals as part of diversified subsistence farming and mixed farming systems, but a limited number of semi-intensive and specialized production units are operating where the feed resource base is sufficient to ensure a steady production.

15. Lack of adequate feed, degradation of natural range land, emergence of contagious and zoonotic disease has also limited the growth of this sub-sector. There is an urgent need to rehabilitate both public and private sector delivery and control systems, to seek viable programs that would arrest degradation of the grazing lands, and to promote private sector initiatives and investments in feeding industries.

16. The conservation and preservation of natural resources needs immediate attention to prevent food shortages and environmental degradation. Of Afghanistan's 65 million hectares, only 12 percent (7.8 million hectares) is arable, just 5 percent is irrigated, about 45 percent is permanent pasture, and 2 percent remains as forest cover. The remaining 40 percent is mountains or desert. The natural resource base suffered due to almost three decades of unrest, competing land uses, lack of appropriate policy such as governing grazing, harvesting of trees, and ownership of land. The forest cover is shrinking fast due to community demand for fuel-wood and illegal logging. Off take rates are estimated to exceed annual growth rates by about 30,000 hectares per year. 90 percent of forest cover which had been mapped before the conflict has been destroyed. It needs to be restored to ensure watersheds function correctly again with implications for downstream agriculture production.

Proposed Actions

17. Six policy and action programs must be taken immediately in order to achieve the sector's primary objectives. These actions proved to be successful in Afghanistan during the 1970's, and with appropriate modifications they could be used to address the realities of the present political and economic situation of the country. First, the over-riding objective of any project and program should be to enhance government credibility in assisting its citizens. Government institutions need to be strengthened at both the central and local levels through proper local and overseas training, providing essential operating funds, and streamlined accounting and reporting system. It is imperative that donors and NGOs take a back seat position by limiting their involvement to advisory functions, institution building, project design and the establishment of proper accounting, monitoring and reporting systems. Through this mechanism, accountability and transparency would improve as well as the capacity of the technical staff. Furthermore, the security risk for the expatriate staff would be minimized through their limited exposure to the rural community. Under this arrangement, administration costs for delivery of technical services would be reduced drastically as NGOs may not find it necessary to open field offices all over the country, paying high staff salaries, and being burdened with extra expenditure for their security.

18. Second, without adopting modern and up-to-date farming technologies, Afghanistan's farmers will neither be able to compete in the world market, nor be in a position to respond to the growing domestic demand for food. Individually, the farmers are financially too weak to bear the costs associated with research findings and the delivery of technology, and, as a group, farmers' organizations have not developed to the level necessary to assume this responsibility jointly. Afghanistan's geo-ecological and topographic situation is another obstacle that makes dissemination of production and marketing information to the producers difficult without public assistance. While donors and NGOs' have made some advances in the area under their command, their operations lacked sustainability and have not had any national level impact. As such, development and transfer of appropriate and modern technological services must remain under the domain of the public sector for at least the next 10 to 15 years.

29. The Ministry of Agriculture, Irrigation, and Livestock (MAIL) must reactivate its seven main research stations which could serve as hubs of change for each of the seven agro-ecological zones of the

country through serving as a center for responding to the farmer's technical problems, conducting adaptive research, and training extension and leading farmers to disseminate best practices. At the same time, the extension cadre of the Ministry needs to be strengthened through training programs, better coordination with the researchers, transportation facilities, provision of operational funds, and working jointly with NGOs' expertise. A two way communication must be established between researchers and extension agents and farmers. Extension agents must convey pertinent farmer's problems to the researchers for investigation and resolution. At the same time, each research station must provide appropriate cultural practices for the extension agents to be delivered the farmers. Among other things, researchers should be responsible for development of improved high yielding varieties-including production of breeder and foundation seeds, promoting mixed farming systems, efficient irrigation techniques. Extension agents need to disseminate improved marketing and production techniques through demonstration plots, mass media, and direct contact with leading farmers and farmer associations. In time as the level of farmers' education and access to internet and other information sources increases, the role of extension services can be scaled back. But it is vital and necessary catalytic service in the interim next one to two decades.

20. Third, establishing viable agricultural credit facilities is vital for gaining farmers' support politically and for enabling them to finance input and modern technology of their needs. Farmers all over the country are demanding access to a reliable credit source, and political pressure on the government is mounting. This demand is expanding due to the rise in the cost of agricultural inputs, and the depleted soil productivity, shortage of draft animals, high cost of automated farm machinery, and intensive crop cultivation which leaves little time- without usage of appropriate technology- for the farmers to harvest one crop and prepare the land for planting another crop. In addition, it is impossible to weaken the influence of drug lords on the client farmers without providing an alternative credit source for these farmers. It is estimated that the drug lords extend, as advance payment toward the purchase of drugs, approximately \$200 million to their client farmers yearly. Most of these farmers finance the required seed and fertilizer for their legal crops from these advance payments as well. Private banking services have not evolved to the point where they can assess and price risks that would help the bulk of farmers.

21. The micro credit field has received support from several donors. The costs of administering these loans, despite the highly participatory organizational structure and good risk management, are very high. In spite of subsidized hidden costs, the interest charges for these loans are about 18 percent. In addition, the size of these loans is too small to finance the needs of middle size farmers. It is no wonder that micro-finance tilted heavily toward the landless small rural enterprises and part time small farmer.

22. During the last seven years, almost \$100 million worth of seed and fertilizer were dispatched through voucher systems, generally to small farmers. The recovery of these funds, however, seems to be negligible and doubtful. In addition, several projects provide credit facilities in the small area of their commands, each with repayment, interest rate, and collection procedures of their own. It is time to focus on establishment of a viable national agricultural credit system that would complement the micro credit scheme and respond to the credit needs of other categories of farmers including the unseved

credit needs of middle farmers) , and follow a uniform policy based on procedures of prudential international banking system.

23. The Afghan Agricultural Development Bank (ADB) with its branches reached most governorates, provided credit facilities for the farmers during 1970's, and established an excellent reputation among the farmers all over the country. Unfortunately, this Bank remains in a lingering situation due to the strong opposition of some donors. The ADB included it in the list of parastatals to be dissolved, even though, it's general structures are still intact and some of its branches are still in operation. The strong position for liquidation of this Bank is surprising in view of the presence of such facilities for the farmers in most developed and developing countries alike, in spite of their well established commercial banking structures. In the context of Afghanistan such a position is also not pragmatic. Liquidating a weak institution before a functioning alternative system is in place does not serve the interest of agriculture in the country. Rebuilding it to the standards it had achieved in the past may be a faster and better transition strategy that is consistent with the long term goal of introducing a world class banking system in Afghanistan

24. Revitalization of Agricultural Development Bank (ADB) with the objective to serve as a credit and deposit institution must be given utmost attention. Years of upheaval, have taken its toll on ADB, like all other institution in Afghanistan. As such, ADB needs to be strengthened through sizable capital infusion, proper training programs, modern accounting and book-keeping training, and proper office technology. To reduce the banking administration's costs, group lending to legal farmers associations such as producers associations, water user associations, and marketing associations must be pursued.

25. Fourth, improving irrigation efficiency and the rehabilitation of dysfunctional existing irrigation systems along with the expansion of irrigation areas deserve close and proper assessment and investment focus. Out of 65 million hectares of the total land area in Afghanistan, only 7.8 million hectares are identified to be arable land. At the present time, 4.5 million hectares of arable land is classified as rainfed, and total irrigated land is estimated about 3.3 million hectare with proper investment it could be increased to 5.5 million hectares.

26. Afghanistan receives about 75 billion cubic meters of water in the form of rain and snow falls. Only 20 billion cubic meters of this is used through surface and under ground channels mainly for agricultural purposes. The water use efficiency of this is estimated to be about 25 percent. With improved irrigation techniques the water use efficiency could be increased to 50 percent. There were several new irrigation projects in the investment pipeline in the late 1970's which were halted due to political unrest. One of those projects was Khush Tapa , diverting water from Amu Darya , and bringing about 600,000 hectares in the North part of Afghanistan under irrigation. Except for yearly losses of thousands of hectares of land due to seasonal flooding, Afghanistan does not get any benefit from this river. So far, none of these major pipeline projects are under consideration for investment.

27. Improving farm water management, especially on current irrigated land, should be included as a top priority of any action plan. The creation of Water User Associations (WUAs) in several countries has proved to be an effective and efficient way of improving efficient water use and minimizing budget

costs. Under such an arrangement, beneficiaries would be responsible for repair and maintenance as well as the distribution of water. Also, in the case of Afghanistan, WUAs could be used as a vehicle for reducing the production of poppies.

28. Fifth, community organizations, promoted by the Ministry of Rural Development, have proved to be a suitable structure for distribution of subsidized relief operations and for the establishment of common goods such as road, drinking water, health and electricity. Similar democratically organized and managed farmers association would also strengthen the government politically; reduce technological delivery costs, and increase production and market productivity. As such, farmers should be encouraged to organize themselves in production, marketing, and processing associations. Already, about a thousand of these farmers associations exists in the country, however, substantial efforts is needed to properly train them in accounting, book keeping, and management fields. These farmers organization must have adequate autonomy to be able to compete in the national/international markets and to respond to their consumers' demand. As such, each association must be accountable primarily to its members- not to the government or community organization.

29. Six, given the present situation of Afghanistan, a tremendous boost in agricultural development can be provided by establishing a mechanism to procure food and rations for foreign military and civilian personnel in Afghanistan, and setting up the inspection and testing capabilities of local personnel and labs to ensure the quality and safety of the products procured. This can then gradually be shaped into the equivalent of the FDA to guarantee the quality of food products sold domestically, and certification process to meet internationally established criteria for high quality exports.

30. In summary, agriculture has the potential to enhance rural income and employment, to reduce poppy production, and to promote peace in Afghanistan. In pursuit of these goals, the country identified in the framework of its Agricultural National Development Plan the sector's main priorities to be food security, enhancing the productivity and production of high value horticultural crops, improving livestock production and productivity, preservation of natural resources, and improving irrigation efficiency and expansion of irrigated land. For the sector to realize its potential these six actions must be taken immediately. These actions proved to be successful in Afghanistan during 1970's and are still relevant given the realities of the present political and economic situation. First, the government must play a leadership role in the implementation of the investment program and in strengthening its visibility, especially through provision and delivery of services to farming communities and to its citizens. Second, a coordinated effort by all parties should be made to strengthen the national research and extension capacity. Third, viable agricultural credit facilities must be established for gaining farmer's support politically and for enabling them to finance input and modern technology of their needs. Fourth, irrigation efficiency and rehabilitation of dysfunctional existing irrigation systems must be improved and expansion of irrigation areas must be properly assessed for investment consideration. Fifth, farmers should be encouraged to organize themselves in production, marketing, processing, and water user associations. Six, consideration should also be given to procurement of food and ration for foreign military and civilian personnel in Afghanistan.

Mr. TIERNEY. Mr. Pam, we would be happy to hear your remarks.

STATEMENT OF JEREMY PAM, ESQ.

Mr. PAM. Chairman Tierney, Ranking Member Flake, members of the subcommittee, thank you for inviting me to appear before you today. I am pleased to have the opportunity to participate in this important hearing in U.S. promotion of the Afghan economy.

I know your time is limited, so let me start with a summary.

I recommend that we adopt an approach to economic development and governance assistance to Afghanistan emphasizing three pillars: an orientation toward Afghan public finance and budgets as a strategic focal point for the entire civil side effort; two, the collaborative development, with relevant Afghan experts, of road maps, setting out a few high-impact programs in key sectors, such as agriculture; and, three, a greater use of catalytic financial instruments, to share risk with Afghan entrepreneurs.

The written testimony I've submitted places the significance of the Afghan economy in the context of a broader legitimacy crisis of the Afghan state that has, at least three other, and arguably more important, dimensions: security, namely, the state's inability to protect the population; political, the reluctance of a critical mass of Afghans to identify politically with their government; and governance, the government's difficulty performing basic governmental functions and delivering essential services.

I thought the centrality of legitimacy to the current crisis was worth discussing at some length in my written testimony first, because it helps explain why past United States and international civil side assistance to Afghanistan has had so limited an impact as to be, in Secretary Clinton's word, "heartbreaking." If the problem is legitimacy, Afghan actors failing to do things Afghans expect them to do, then it shouldn't be surprising that international civilians trying to do those things directly—the default international approach—for reasons I discuss in my written testimony, has not worked as a solution.

As an aside, please note that all of my comments relate to the civilian and not the military effort, although I suspect there are points of overlap, when noted military expert like John Nagl publish op-eds with titles like "We Can't Win These Wars on Our Own."

The second reason it's worth framing things in terms of legitimacy is that seeing the Afghan crisis as a problem of legitimacy explains why improving the situation requires us to adopt approaches that deliberately structure international efforts in ways that improve Afghan legitimacy, by helping Afghans implement their priorities through their institutions, despite the many frustrations and inefficiencies of such an approach. This legitimacy analysis leads directly into the three-pillar strategic concept for civil side assistance that my colleagues, Dawn Liberry of USAID, Clare Lockhart of the Institute for State Effectiveness, and I developed this spring, which my written testimony describes in further detail, and which was also referenced by Patrick Cronin, of the Institute for National Security Studies at NDU, in his May 19th testimony to the subcommittee.

As already mentioned, these three pillars are: an orientation toward Afghan public finance and budgets as a strategic focal point for the civil side effort; the collaborative development of new road maps for key sectors; and a greater use of catalytic financial instruments to share risk with Afghan entrepreneurs.

I will return to the public finance pillar in a moment, but there is more on all three pillars in my written testimony.

More important for this discussion is the common idea underlying the concept as a whole, the requirement to use Afghan institutions or business enterprises as the focal point for international assistance, which should better ensure that our efforts are aligned with Afghan policy or business priorities and is consistent with Afghan institutional capacity, thus increasing the likelihood that the efforts will both be sustained by Afghans, and contribute to resolving the underlying legitimacy crisis.

My discussion thus far has emphasized explaining all of the current crises in Afghanistan, the limitations of past civil side international assistance, and the rationale for the alternative approach we've recommended, solely by reference to the Afghan situation and the dynamics of international assistance; in other words, without bringing recent experience of any other country into it.

I would like to now conclude by describing briefly how the U.S. experience in Iraq reinforces both the general component of this analysis and the feasibility and effectiveness of the particular solution proposed.

While Afghanistan and Iraq are, indeed, apples and oranges in many respects, perhaps no more so than in public finance and economic terms, where Afghanistan ranks near the bottom in terms of wealth and human capital indicators and Iraq has the second-largest proven oil reserves in the world; but the Afghanistan and Iraq efforts do have one major factor in common—us. In both countries, the same United States and U.K. civilian and military organizations operate according to broadly similar organizational dynamics, setting the stage for the same kinds of misalignment with local country priorities and institutional capacity, and the same tendencies toward a fragmented international effort.

Indeed, I am sure you will all recall that in 2004, 2005, and 2006, the Iraq effort was routinely condemned as seriously, perhaps even fatally, hindered by coordination challenges between civilians in the military, between different civilian agencies, and, most importantly, between the U.S. efforts and the Iraqis themselves. I think that stories about those coordination challenges are familiar to us from both efforts.

Both official audits and journalistic accounts produce story after story about how the left hand didn't know what the right hand was doing, and all of the ways in which this was undermining our efforts to get to the point when the Iraqi Government and economy could stand on their own. As it happened, the little appreciated but significant factor in addressing some of the most important coordination problems and improving the effectiveness of our efforts to support Iraqi self-governance was the belated recognition of the strategic importance of Iraqi public finance, particularly budgets. This led to a significant shift in emphasis across the U.S. assist-

ance effort toward helping Iraqi officials, at both national and provincial levels, execute Iraqi budgets.

As recounted in the Capstone report of the Special Inspector General for Iraq Reconstruction, "Hard Lessons," in 2006, most Americans in Iraq were still focused on spending U.S. money, largely independent of Iraqi government institutions. Consequently, in many cases, there was a lack of sufficient Iraqi participation in deciding how or what to reconstruct and ensuring that projects could be maintained afterwards.

The end of 2006, however, saw "the rise of budget execution as a U.S. civilian and military priority." By mid-2007, the standard for useful expenditure of U.S. funds had largely shifted to, "If it can't be done by Iraqis, we probably shouldn't do it. What is better is a project that takes 60 days instead of 30 days, but is done by Iraqi managers, and is sustainable by the Iraqis, and that their operations can support."

By mid-2008, the Iraqi public finance and budgets had become such a central organizing principle to the U.S. effort that the Embassy and Multinational Force Iraq created a civil military Public Financial Management Action Group [PFMAG], chaired by the senior civilian and military leaders responsible for governance and the economy and incorporating the participation of dozens of U.S. organizations working on the civil side in Iraq, in order to ensure that all civilian and military personnel, whether working with ministries from Baghdad or with provinces from Provincial Reconstruction Teams, would make assisting with the execution of Iraqi budgets a paramount civil administration mission priority.

By the end of 2008, in an independent U.S. Institute of Peace study, the PRTs had concluded, "The budget execution role is critical to the U.S. mission in Iraq and is the primary strategic justification to continue the PRT program."

I hope it goes without saying that nothing I have just said should be taken as suggesting that an approach having worked modestly in Iraq, is by itself, a reason to adopt it in Afghanistan. Indeed, I limited my written testimony to Afghanistan in order to avoid any such implication.

However, if we believe that there are some common, daunting challenges to finally establishing an effective civil assistance effort in Afghanistan, which have as much to do with the international challenges of providing effective assistance in this kind of environment as with Afghanistan, we might find some value in the idea of public finance as a strategic focal point. And in the broader idea of deliberately structuring our assistance to better align our civil side efforts in Afghanistan with Afghan priorities and institutional capacity, I believe that by strengthening the ability of Afghanistan state institutions and the private sector to recover from the current crisis of legitimacy, and stand to a greater degree on their own, such an approach would advance our national interest and greater stability in this region.

I thank you, Mr. Chairman, for giving me the opportunity to testify today. I look forward to any comments or questions you may have.

Mr. TIERNEY. Thank you, Mr. Pam. We appreciate your remarks. [The prepared statement of Mr. Pam follows:]

TESTIMONY OF
JEREMIAH S. PAM
VISITING RESEARCH SCHOLAR,
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BEFORE THE
SUBCOMMITTEE ON NATIONAL SECURITY AND FOREIGN AFFAIRS,
COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM
U.S. HOUSE OF REPRESENTATIVES
JULY 14, 2009

Chairman Tierney, Ranking Member Flake, Members of the Subcommittee:

Thank you for inviting me to appear before you today. I am pleased to have the opportunity to participate in this important hearing on U.S. assistance with respect to the Afghan economy.

The title of this hearing is "U.S. Promotion of the Afghan Economy: Impediments and Opportunities." I'd like to begin by stepping back to ask why promoting the Afghan economy is of interest to this Subcommittee on National Security and Foreign Affairs.

The Complex Legitimacy Crisis in Afghanistan

I would suggest that the Afghan economy is principally of interest to us because its performance is one element of a much broader crisis of legitimacy with which the Afghan state has been struggling. This broader legitimacy crisis has been playing a central -- perhaps the decisive -- role in the in the resilience of the insurgency that has plagued Afghanistan and threatens U.S. interests. As the Army/Marine Corps Counterinsurgency Field Manual puts it, "Legitimacy is the main objective. ... A [counterinsurgency] effort cannot achieve lasting success without the host nation government achieving legitimacy."

However, the economy is just one of a number of key elements of Afghan legitimacy. In my former legal practice as an adviser to sovereign governments in resolving debt crises, I observed a number of countries experiencing financial and economic crises where the economic crisis alone was the sole or primary factor that undermined legitimacy and (in some cases) brought down governments. That is clearly not the situation in Afghanistan. Instead, there are at least three other elements of government legitimacy that arguably play a more significant role in the current crisis. First, security: governments are expected to be able to protect their populations. Second, political: a critical mass of citizens must have a basis for politically identifying with their leaders, whether through elections or some form of traditional authority. Third: governance: the government must perform basic governmental functions and provide essential services (in accordance with local traditions and expectations).

Fortunately, the President's new strategy for Afghanistan has components that address each of these other elements, which are largely beyond the scope of this hearing (although I will return to governance below).

What the Centrality of Legitimacy Means for U.S. Assistance to Afghanistan

Nonetheless, I think it is useful to lead with this point about legitimacy for two reasons. To begin with, recognizing that the economy is only one element of a legitimacy crisis with multiple significant elements helps us to keep its significance in perspective. "Fixing" the economy (putting aside for the moment what that would mean in the context of Afghanistan) would not "fix" an Afghanistan in which the population is still living in conditions of extreme insecurity, in which the citizens regard the government as corrupt or having held on to power through unfair means and in which the government is seen as incapable of performing basic functions to even the most modest standards. While it is possible that economic development and improved economic prospects could contribute to making some of these other challenges a little easier to address (e.g., by decreasing the recruiting pool for economically-motivated insurgents), I have not been persuaded that the economy is the most important element of the legitimacy crisis in Afghanistan or the key to addressing all of the other elements just mentioned.

This is probably fortunate, because Afghanistan is, and is likely to remain, one of the poorest countries in the world – fifth from last according to the 2007 Human Development Report. While I will turn shortly to some things that we can do that could help improve the economic prospects of its citizens and increase its level of economic development, we should recognize that the changes possible are marginal improvements over time, leaving Afghanistan a very poor country for the foreseeable future. Consequently, I think there are uncertainties about any strategy premised on economic development producing dramatic changes in the situation, at least before the medium or long term. We should not overpromise about what even a substantial improvement in the Afghan economy would deliver in terms of the overall situation.

Shortcomings of Past U.S. and International Assistance to Afghanistan

The other reason I believe it is useful to frame the issue by reference to the Afghan legitimacy crisis is that it helps explain why it has been so difficult for the U.S. or other international actors to assist Afghanistan in ways that help solve the crisis rather than exacerbate it. On March 30 of this year at a conference on Afghanistan at The Hague, Secretary of State Hillary Rodham Clinton described the amount of money spent on Afghanistan over the past seven years without producing more visible results as "heartbreaking." "For those of you who have been on the ground in Afghanistan, you have seen with your own eyes that a lot of these aid programs don't work. There are so many problems with them. There are problems of design, there are problems of staffing, there are problems of implementation, there are problems of accountability. You just go down the line." Accordingly, the President's new strategy for

Afghanistan and Pakistan calls for both a significant increase of civilian resources and “a new model of how we allocate and use these resources.”

Why has past U.S. and international assistance to Afghanistan failed to produce more visible progress in economic development and a more secure country? I believe there are two fundamental explanations. The first is that our assistance has often been insufficiently related to Afghan priorities and institutions, substantially limiting both its effectiveness and its contribution to government legitimacy. Because international assistance is appropriated and planned back in capitals, and most often implemented by officials and contractors from the donor countries, getting detailed Afghan input about priority needs and the strengths and weaknesses of existing governance or civil society institutions is difficult, and setting up donor systems for implementing assistance that operate parallel to but distinct from existing Afghan systems is too often the default. Local capacity seen as weak (and alien) by Western donors and concerns about corruption further exacerbate this tendency.

The second fundamental explanation for the poor results from international assistance is that the international efforts themselves – originating in and driven by the varied national priorities and organizational dynamics of each donor nation and agency – naturally tend toward fragmentation. When development intervention A is the priority for donor X and development intervention B is the priority for donor Y, the normal outcome is for each to pursue its own priority. While particular donors can try to align their individual efforts with Afghan priorities and institutions, overall the multiplication of distinct donor efforts makes it more difficult for the Afghan government to keep track of and influence the assistance, so in practice this second problem (the fragmentation of donor efforts) tends to exacerbate the first (poor alignment with local priorities and institutions). Here, too, the consequence has been to limit both the effectiveness of assistance and its contribution to government legitimacy.

Afghan Business Impressions of U.S. Assistance

Confirming these general tendencies in U.S. assistance, below are some points made by Afghan businesspeople at a recent conference in Washington on “Making the Private Sector Work in Afghanistan”:

- *Afghan capacity (both private sector and governmental) is currently underutilized.* While corruption is a problem, it is hardly unique to Afghanistan and Afghan actors are capable of producing some results despite it. If Afghan companies are given more responsibility/empowered, their capacity will improve. For all the limitations of the Afghan government and private sector, in order to become stronger they have to be given more opportunities to perform, including the opportunity to make mistakes.
- *Traditional USG representatives too often lack the local knowledge necessary to support business activity.* Business is driven by and operates according to local

practices, from the bottom up. The U.S. effort needs to be more open to helping Afghans use their own rules of commerce.

- *There are plenty of Afghan entrepreneurs, the constraint is limited capital. Co-investing alongside Afghan capital is less risky and more successful because Afghans' own money is at risk. Consequently we need to find a way to connect international capital with Afghan entrepreneurial ideas. An enterprise fund should be considered (although the U.S. has implemented them less than optimally elsewhere).*
- *Inefficient and overly burdensome Afghan government red tape impedes business. Property titling is incoherent, taxes are too high, the High Commission for Investment is not meeting regularly, and the government is not doing enough to develop natural resources.*
- *We should provide more support of Afghan education and training, in and out of country. This is the investment sure to produce high and lasting returns.*

Assistance that Supports Legitimacy and Sustainability

If the two basic problems with past assistance have been insufficient alignment with Afghan priorities and institutions and the tendency among international donors toward fragmentation, one might describe the challenge of more effective assistance simply as finding approaches that organize international donor efforts around Afghan priorities and institutions. While that could in theory be accomplished by some kind of international coordinating body granted extraordinary authority sufficient to coordinate sovereign donors – authority UNAMA has never had – when we recall the central importance of the crisis of government legitimacy, however, it becomes impossible to avoid the conclusion that bolstering Afghan legitimacy requires an approach in which the Afghan government itself is responsible for this function.

To restate this in terms of the governance and economy dimensions of the legitimacy crises discussed earlier: the governance element of the legitimacy crisis will be sustainably resolved only when it is the government that is performing basic governmental functions, and the economic element of the legitimacy crisis will be sustainably resolved only when economic and business decisions are made by Afghan officials and Afghan businesspeople.

The objective of U.S. assistance, then, must be to support, and not undermine, sustainable resolutions of each of these elements of the legitimacy crisis. As World Bank President Zoellick recently wrote, “To achieve legitimacy, it is not only the services that matter, but who performs them: they should be undertaken by the government and local people as soon as is feasible. This strategic consideration should guide both the handoff from humanitarian aid to development and the design of transition services.”

I think an allied point was made by General McChrystal last month (as reported in the June 20th New York Times) when he suggested adding to the traditional counterinsurgency

formula of “clear, hold, build” a fourth element: “sustain”. If the requirement to “hold” sometimes constrains international military forces from acting directly in “clearing” until local security forces are ready to “hold”, the requirement to “sustain” may be interpreted as a similar constraint on international civilians from acting directly in “building” until it has been established that there is Afghan interest and capacity to “sustain” the initiative. In practice, this will usually mean that the Afghans have to be brought in on the original “build” decision.

Elements of a More Effective, Legitimacy-Focused Approach to Assistance

What does this mean in practice? As Patrick Cronin, Director of the Institute for National Security Studies, noted in his testimony for this Subcommittee’s hearing on May 19, my colleagues Dawn Liberi, Clare Lockhart and I have outlined a strategic concept for more effective development, economics and governance assistance to Afghanistan that is based on three pillars:

- Afghan public finance, especially budgets, as a focal point for our efforts to support improved Afghan governance and state functioning;
- Key sector roadmaps, developed jointly with Afghans and designed to reflect Afghan priorities and capacities (on the general model of the National Solidarity Program), to develop programs worth receiving funding; and
- Catalytic financial instruments (e.g., guarantees, risk insurance) as a focal point for our efforts to support the development of the Afghan private sector and economy

I will now briefly explain why each pillar of this concept should be better able to avoid the pitfalls of past assistance to Afghanistan described above and capable of making a significant contribution to a sustainable resolution of key elements of the underlying legitimacy crisis.

Public budgets, and public finance in general, are linchpins of public governance in all states. Budgets are how governments rank and tradeoff priorities and signal policy commitments. Once a budget is agreed, budget execution is how money flows to all legitimate priorities of the state, from paying the salaries of soldiers, police and teachers to making capital investments in schools, hospitals and roads. As such, Afghan budgets – at both the national and subnational levels – have the potential to be a uniquely authoritative and comprehensive statement of Afghanistan’s own objectives. By embracing Afghan budgets and Afghan institutions for public finance as focal points for U.S. assistance efforts, we would avoid the longstanding problem of our efforts being misaligned with Afghan priorities and institutions. Instead, Americans would largely be in the position of helping Afghans implement their priorities, which would both bolster government legitimacy and increase the chances that the Afghans will sustain initiatives started when we are ready to scale down our presence. At the same time, because there is only one Afghan budget for any particular governmental unit (e.g., nation, village), such a focus could effectively address the international fragmentation problem by binding all international

assistance to a single set of Afghan priorities and institutions. Among other virtues, adopting this approach could provide most Americans working on the civil side in Afghanistan (whether civilian or military) with the kind of simple, clear and nearly universal conception of their mission in Afghanistan that has until now stymied the effort: we are assisting the Afghans with their priorities as documented in their budgets, by helping them with any and all steps necessary under their institutions to execute those budgets. We should not underestimate either the value of a clear mission or the difficulty of imposing one on a fragmented effort after the fact. However, I believe that one lesson from Iraq applicable to Afghanistan is that a focus on local public finance and budget execution (an approach adopted in Iraq in early 2007 that continues successfully to this day) is one of the few demonstrated sources of such a unifying mission. Finally, because budget execution is fundamentally about spending money, our efforts to help the Afghans push money through their public finance system will stimulate the Afghan economy via channels more sustainable than those currently used for the large majority of international assistance spent via donor-specific parallel systems – namely public sector salaries that Afghan individuals and families rely on for buying power and public capital expenditures that can provide contracts for Afghan private companies and workers.

To implement this would require (1) a priority commitment throughout the U.S. effort (civilian and military) to working with the Afghans to understand and strengthen Afghan public financial management systems at all levels of government (together with other international actors already active in this area such as the World Bank), (2) serious discussions with the Afghan national government about introducing more fiscal decentralization and empowering at least some subnational authorities (e.g., provincial councils) with budgetary authority (supplementing, not replacing, the current national budget system) and (3) a willingness to provide a greater proportion of U.S. assistance as budget support. While the last point has sometimes been viewed as controversial, I believe there is an emerging consensus in favor of its utility among both Afghanistan experts (e.g., the Asia Society’s recent report on stabilizing Afghanistan-Pakistan) and public finance experts (e.g., recent World Bank research concluding that the case for budget support is strong in high-capacity and low-capacity reform settings alike).

The second pillar of this strategic approach is the collaborative design with relevant Afghan experts of roadmaps setting out high-impact programs in key sectors (e.g., agriculture, education, health, electricity, justice). While these roadmaps would be developed at the national level, individual programs will aim to exploit capacity wherever it exists, including all the way down to the village level (e.g., National Solidarity Program) and in non-governmental organizations. Rather than being an attempt at wholesale reengineering of the Afghan state, these sector roadmaps would be designed from the outset to reflect Afghan priorities and institutional capacity.

The final pillar of this strategic approach is a greater emphasis on catalytic financial instruments such as partial loan guarantees, risk insurance and microfinance that by their nature

bolster, rather than substitute for, bona fide Afghan businesses. I have already noted the Afghan business view that the binding constraint is not enterprises but capital to expand them and the eagerness to invest Afghan money in conjunction with international capital, credit enhancement or risk mitigation. Like the other pillars, this approach links international assistance to Afghan (business) priorities and institutions (enterprises), limiting any international donor temptation to invest money in private sector ventures with insufficient Afghan support and willingness to sustain.

The Way Ahead

What would be required for the U.S. to implement such a legitimacy-focused, three pillar strategy for governance and economic assistance to Afghanistan? A number of elements of the strategic concept are already implicitly or explicitly part of the President's new strategy for Afghanistan. In closing, I'd make just two final recommendations about communicating a clear and coherent approach throughout the U.S. effort.

First, leaders in the Administration and Congress should explicitly signal that the centrality of Afghan legitimacy to the current emergency situation requires that U.S. assistance be extraordinarily oriented toward supporting, and not undermining, Afghan legitimacy, even if this requires departures from normal foreign assistance modalities and the acceptance of greater than usual fiduciary risk. U.S. assistance efforts must support the Afghan government performing governmental functions, and Afghan officials and businesspeople leading on economic and business decisions.

Second, and making this general point concrete, all relevant U.S. officials should embrace Afghan budgets/public finance as the key civil-side framework for achieving this Afghan legitimacy focus. Both the legislative steps in Washington and the technical steps in Kabul required for a greater use of budget support should be a priority. New structures to coordinate the U.S. effort more closely with public finance experts at the World Bank and the IMF should be established. The focus on Afghan budgets should be a major theme of the training for all U.S. military and civilian personnel deploying, with an explicit objective of seeking to counter the temptation to do directly things better done indirectly (i.e., by working by, with and through Afghans). Data about budget-related assistance efforts – not how much we are spending, but how much we are helping them spend – should be made a key part of the metrics used to track the U.S. effort. Senior policy officials responsible for spearheading the public finance thrust should be designated both in Washington and Kabul. In sum, the entire U.S. effort – in Washington and the field, civilian and military – should explicitly adopt Afghan budgets/public finance as a central strategic focus, in the interest of the broader objective of bolstering Afghan legitimacy and thus achieving sustainable stability as quickly as possible.

Mr. TIERNEY. Mr. Mawji, again, we thank you for joining us from afar; and we look forward to hearing your remarks, sir.

STATEMENT OF ALY MAWJI

[NOTE.—The following testimony was delivered via video-conference.]

Mr. MAWJI. Thank you very much, Mr. Chairman; and thank you for the opportunity to be able to share some of our experiences here in Afghanistan with you.

May I, at the outset, also, coming from the field, pay tribute to the large number of soldiers here who are fighting on under very delicate circumstances, and my condolences and prayers to the families of those young men and women who have lost their lives in recent days and in the past.

The Aga Khan Development Network is founded and chaired by His Highness the Aga Khan. It essentially works in three pillars: the social, cultural, and economic. The social and cultural pillars are predominantly not-for-profit organizations, whereas the economic is a for-profit organization.

There is often confusion as to why we run for-profits and not-for-profits, but, for us, investment in the economic side of things is as important if we want to try and establish best practices, if we want to try and raise incomes, dual capacity, and so on and so forth. We draw no profits from these economic investments, even though they are for-profit companies, and these profits go back into social and cultural development as a cycle.

I welcome the opportunity to share with you some of our experiences here in the field, and to draw some conclusions of what we've learned from the large investments of over \$700 million across three pillars over the last 7 to 8 years. And if I might say, I find myself kind of trying to walk with one foot in a bucket of hot water and the other foot in a bucket of cold water, and I'll explain why in a second. And perhaps I can turn to the bucket of hot water first.

I would like to say that Afghans are inherently very entrepreneurial people. That is what has allowed them to survive 23 years of war. It's what has allowed them to rebuild Afghanistan in terms of businesses and so on since the war. And with that comes a huge amount of hospitality and warmth. And after 23 years of war in this country, there really is total devastation; and this devastation is not only just institutionally, but it's also in terms of the country. And I think we should not be shortsighted, but we're going to need a long and a very sustained engagement in Afghanistan if we are to make progress.

The second point I would make is that our focus and experience has shown that today we've got to move away from what I would sometimes call the "country of Kabul" to the country of Afghanistan. There is a lot of effort being placed in Kabul, in processes such as the Afghan National Development Strategy and so on, which is government-led, and which is important, but I think we have to ask ourselves, how does this translate in the field and benefit communities, people, and a society of lives in Afghanistan?

And, at this point, I would like to underline the huge importance of civil society. Civil society is not trusted in this country. It's seen

as something that's been perhaps under the scheming of financial resources that's being available in Afghanistan. Yet we see civil society as part of the private sector that plays a huge bridge between people and government, plays a key role in implementing the principle of democracy and state transparency that is accountable to citizens. Civil society creates an environment through which various segments of the population can take part in the process of decisionmaking.

In true home-grown programs like the National Solidarity Programme, we are essentially molding what has been traditional Afghan civil society and their leadership, the shuras as they call them, and modernizing it, getting them to prioritize. What are the key concerns around their community? How are they going to implement it? How are they going to be accountable toward developing their societies?

And, therefore, I think the importance of civil society and the private sector is something that needs to be recognized and enforced in the Afghan conflicts, particularly as we look at the bridge from moving from policy and government services to delivering on the ground.

And let's not be mistaken, while we all appreciate that Afghanistan is a sovereign state and we need to build the institutions of the state, it's going to take a while to do away with institutions; it's going to take a while to get the right kind of capacity to deliver. And we have seen over the last 4 or 5 years how ministries have crumbled, how corruption has come to set in, how Afghanistan's development budget has never been able to expand more than 40 or 45 percent per annum. And that, for us, should be a wake-up call in the way that we approach Afghanistan.

The next point I would make is that we tend often to talk about sectors, and we say we need to invest in agriculture, we need to invest in water, we need to invest in X, Y, and Z, which I think is absolutely right. But I think what we also need to understand is that where the rubber hits the road, where you start working and engaging with communities, you need to bring in what we in the Aga Khan Development Network call MIAD, which is a multi-input area development system, where you're looking at bringing in a package of interventions that are relevant, that come together in a way that is relevant and in an equation that actually affects the societies in which we are trying to operate. That calls for us to really look at provinces where the enabling conditions exist and ask ourselves, what is the political profile of these provinces? What are the economic opportunities? What are the social development needs and opportunities? And mesh them in an equation, bringing in a multi-input system that is relevant.

To date, I think we have been extremely busy in Afghanistan. We go in and say we're doing lots of work in agriculture, or we're doing a bit of work in microfinance. Roles are sometimes confused in provinces between the PRT, between civil society actors, between government, because there's no clear vision that really binds people together in a coherent fashion.

The next point I would make also is we need to continue to encourage public-private partnerships. Today, we are running a hospital with the French Medical Institute for Children, which has

just received the first-ever in the history of Afghanistan, as far as we know, ISO EPPP with the French government, with the Afghan Government, with two French NGO's and the ATVN. And we are able to deliver quality health care in the government; and we need to encourage much, much more of the PCPs, which have shown success.

Let me quickly turn to some of what I have addressed in the testimony; and that is, you know, my other foot, which is in the cold bucket; and let me return to the business side of things.

If you look at the whole business angle, I mean, we spent a year doing research before we held the Enabling Environment Conference in Afghanistan that really asked the deep questions, what is impeding civil society and business to go forward in Afghanistan? And you see, there is a road map that came out which has been submitted as part of the testimony.

But, you know, the issues are very, very clear. There is very weak policy enforcement. Creating policy and enforcing policy is a huge problem. In a recent survey done by the World Bank, they said 14 percent of the people surveyed report unpredictability of the laws, even though they exist, and poor provision of electricity. If we are going to try and rebuild Afghan's economy, there is no way that it can be cost effective if the cost of energy is so extremely high that the final cost of production makes it untenable in the region. So the major investments in infrastructure, water, power, roads, and so on.

Crime and security has become a major issue. Corruption is a phenomenal issue. I recall a young Afghan-American lady who had set up a business in Afghanistan, who made a statement as we were doing research for the Enabling Environment Conference; and she said, Aly, I went to the Ministry of Finance four times to pay my taxes, my income taxes, but nobody could tell me where I could pay these taxes. And then she said, finally, somebody said, I'll help you pay your taxes, but you need to pay me to help you pay your taxes, in which case she was paying corruption to pay her taxes, and this is completely bizarre.

Access to land has become a critical issue. Let me give you an example. An earlier colleague talked about the importance of microfinance. We have seen microfinance become extremely successful. We have \$100 million out in loans. We find there is 98 to 99 percent repayment of these loans. But when people hit a certain ceiling where microfinance is not enough, and they want to increase their businesses into small and medium enterprises, none of the banks are willing to give them the loans, because they have no collateral.

And what is collateral for Afghans today? It's land. But they can't use this land as capital because the land registration rights in Kabul are so corrupt that no banks will trust it. And there is a need for a whole land reformation and re-registration process, which is not difficult to do, but should be part of the priority that we address in the international community and the Afghan Government as outlined in the road map.

In the World Bank survey, 84 percent of the respondents said that the court system in Afghanistan is corrupt and unfair, and the Attorney General's Office has often been associated with high cor-

ruption. Now, I can't validate this, but this is what the feelings and the perceptions and the experiences of Afghan businessmen are in Afghanistan.

Business licensing and permits are also such issues.

If I were to conclude, Mr. Chairman, I would like to look at a few broad things that I think are completely fundamental sine qua nons as we look ahead and if we want to address the kind of issues that you made, quite rightly, in your statement in terms of the challenges that lay ahead of us.

No. 1, I strongly encourage that we put in resources to address the issues outlined in the Enabling Environments Conference road map, which are clear, and to push the Afghan Government to be able to prioritize these in a systemic fashion so that we can start addressing the primary concerns of private-sector development in Afghanistan.

No. 2, in the wake of what is a really highly insecure time in Afghanistan, where it is quite unlikely we are going to get huge amounts of foreign direct investments coming into the country, we would really propose that we take a hard look at local Afghan businesses. How can we really enable Afghan businesses to flourish within the context and the constraints that they're working in?

No. 3, work to rebuild and strengthen the institution of government. And in this I would strongly recommend that, in the interest of one who demonstrates progress very quickly, is that we identify five or six key ministries that are absolutely critical for us in order to deliver to the people of Afghanistan. And we can give conferences of those ministries to help them develop the kind of vision that's necessary and to implement the vision at that point.

Fourth, invest and encourage and nurture and build civil society. Because civil society is already demonstrating a tremendous role in Afghanistan, as it has in many, many countries around the world.

A wider investment in water and power and other infrastructure. We need to work hard at enabling regional opportunities, and we have focused on agriculture in Afghanistan as one of the key priorities. Let's not forget that Afghans will use 77 percent of the food that they actually produce. If you really want to rebuild the economy, Afghanistan should become traditionally what it was when it was thriving, and that was a land bridge in the Silk Route.

So how do we open up the corridor between Pakistan, Iran, Tajikistan, Uzbekistan? We've had three regional economic cooperation conferences now on Afghanistan, and I'm sorry to say we've made extremely little progress in terms of tangible outcomes.

The seventh point I will make is the equity of development investments. So far, if you look at Afghanistan, a recent survey shows that those areas that are most insecure, whether it's high military action, has received the largest amount of development assistance with the least amount of output. Whereas those provinces, like Bamian, for example, where we've had the most amazing conditions for success, has received the least amount of development assistance.

I think we need to readdress that balance, because if there's one other thing we have learned in our experience, it's that success stories spread very, very quickly in Afghanistan. And if you want to get three or four provinces and make them into success stories at

a provincial level, you would speak volumes to those insecure areas in the south to which you could respond to them in faith, you could create those conditions where it is profitable and stable. We would be able to help you to get to that point.

I would like to conclude by just drawing on a quote by the European Ambassador in Afghanistan, who I thought made a very interesting statement the other day wherein he said—his name is Ettore Sequi—when he said, “As long as Afghan institutions are perceived as being able to provide those basic services that the state should deliver to people—a clean and effective public administration, a functioning and fair justice, an effective police, a sound system of education, job creation capacity, economic opportunities, etc.—the confidence of Afghans in their own institutions will increase, leaving less room for insurgency propaganda and appeal.

It’s the institutional dimension of security which is key for an enduring security. It is this perspective that will be crucial to strengthen and better coordinate programs already in place in these fields, and in particular justice, the rule of law, etc.

It will also be necessary to actively and substantially support the strengthening of management in the administrative capacity of the Afghan public administration.

I would only add to that we look at strengthening the goal of the private sector in helping to deliver services for the government and the people of Afghanistan.

Thank you.

Mr. TIERNEY. I thank you very much, sir.

[The prepared statement of Mr. Mawji follows:]

THE AGA KHAN DEVELOPMENT NETWORK
AFGHANISTAN

“U.S. PROMOTION OF THE AFGHAN ECONOMY: IMPEDIMENTS AND OPPORTUNITIES”

TESTIMONY TO THE SUBCOMMITTEE ON NATIONAL SECURITY AND FOREIGN AFFAIRS, 14TH JULY 2009:

On behalf of the Aga Khan Development Network (AKDN), I thank the Subcommittee on National Security and Foreign Affairs for the opportunity to share with you our experience and thoughts about the Afghan economy, and the private sector in particular. I also wish to acknowledge and commend the considerable effort and assistance made by the US Government to bring about peace and stability in a country that has been ravaged by more than 20 years of war.

The Aga Khan Development Network (AKDN) is a group of development agencies operating within three primary pillars: economic, social and culture, with mandates ranging from health and education to architecture, culture, microfinance, rural development, disaster reduction, the promotion of private-sector enterprise and the revitalisation of historic cities. AKDN agencies conduct their programmes without regard to faith, origin or gender.

In Afghanistan, AKDN programmes include large-scale rural development that impact 1.2 million people; construction, management, human resource development and capacity building in health care including operating two major hospitals that are linked to the Aga Khan University Hospital in Pakistan; providing teacher training, school construction, and early childhood development in education; promoting and nurturing civil society and the rehabilitation of historic neighbourhoods in Kabul and Herat. AKDN is engaged in generating economic enterprise, wherein more than USD \$100 million has been disbursed to microfinance borrowers (61,000 clients); a rapidly growing mobile phone network with approximately 3.5 million customers and coverage across Afghanistan's 34 provinces, representing 41% of the market share; and the renovation and management of a five-star hotel in Kabul. With the support of its donors and partners, more than **US\$700 million** has been channelled through AKDN for Afghanistan's reconstruction. AKDN is one of, if not the largest, single private investor in the country, and its telecommunication network, Roshan, is the largest single tax payer contributing approximately 5% of total domestic Government revenues since 2003.

Enabling Environment for Private Sector development – Definitions, Impediments and Recommendations:

As a part of AKDN's interest in creating a conducive environment for the Private Sector in Afghanistan, **The Enabling Environment Conference** was convened by the Government of the Islamic Republic of Afghanistan and AKDN, in partnership with The World Bank, the United Nations Development Programme and the Asian Development Bank to foster significantly greater private sector participation in Afghanistan's development, and took place in Kabul on 4-5 June 2007. Twelve months of research prior to the conference - with extensive consultation with stakeholders - and the deliberations at the Conference, underlined some of the key impediments to enabling a healthy private sector to flourish:

Definitions:

Private sector – The private sector not only includes for-profit business but also not-for profit civil society and encouraging both is essential to Afghanistan's progress. While improving Afghanistan's state apparatus is essential for the country's development, experience from elsewhere demonstrates that contributions from private initiative are equally needed to make effective use of the country's human potential, generate material resources, and develop a vibrant and robust socio-economic base engaging Afghan citizens and diaspora as investors, volunteers, managers, employees and entrepreneurs, and thus creating a strong constituency for growth and development. In the form of both business and a diverse and engaged civil society, the private sector brings entrepreneurial energy

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and problem-solving capabilities, and the capacity to reach marginal and under-served populations quickly and effectively. In this way, contributions from the private sector can complement and make possible the Government's development agenda, spur economic and social development and strengthen governance.

Civil Society is committed to the public good and is powered by **private voluntary energies**. It is an array of institutions which operate on a private, voluntary basis, but are equally driven by public motivations. They include institutions dedicated to education, to culture, to health, and to environmental improvement; they embrace commercial, labour, professional and ethnic associations, as well as institutions of religion and the media. National Programmes in Afghanistan, such as the National Solidarity Programme have given rise to nascent civil society structures in rural Afghanistan. However, these institutions need to be harnessed, protected, and charged with responsibility and decision making that enables them to serve their society's needs and aspirations. During the Berlin Conference on Afghanistan in 2004, His Highness the Aga Khan drew attention to the role of civil society:

“Civil society makes an enormous contribution to human development, filling the gaps between government, the business sector, and the family. It does things the state cannot, and thus supports citizens in nation building. Most important, civil society underwrites human progress. Its acts as a stabilizer or buttress in times of economic slowdown or social stress. When democracies are failing, or have failed, it is the institutions of civil society that can carry an added burden to help sustain improvements in quality of life.”

Impediments:

- Lack of a basic legal and regulatory framework and the capacity to interpret and enforce new legislation.
- Need to strengthen the governance and operations of civil society organisations
- Poor capacity and leadership in public and private sectors
- Increasing insecurity
- Fragmented land and property rights frameworks
- The need for a broad range of financial services
- The lack of adjudication mechanisms to find resolution to disputes
- Weak culture of social responsibility and philanthropy
- A lack of consensus about the Private Sector's role
- Failure to empower the Private Sector in the reconstruction and development of the country and over-reliance on Government to deliver services:
- Young and weak Government institutions

Opportunities:

Afghanistan has the opportunity to move from a climate of fragility to creating an enabling environment leading to economic development and job creation, social progress and improved quality of life of the Afghan people that upholds its pluralistic nature as a source of strength, and a vibrant and engaged civil society. An enabling environment is characterised by political stability; confidence in the future; mutual trust, understanding, dialogue and collaboration amongst stakeholders; rule of law; protection of the rights of citizens; a diversity of stable, democratic institutions; and a streamlined legal, fiscal, regulatory, and administrative framework governing all spheres of private initiative, which is predictably, consistently and impartially applied.

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In response to the impediments identified, the Enabling Environment Conference recommended to:

- Enact and implement key laws and amendments to establish the basic legal and regulatory framework that will encourage Private Sector involvement in social and economic development in Afghanistan. The laws and regulations should: (i) be clearly specified and transparent; (ii) be further streamlined, involving the minimum necessary steps, bureaucratic processes and institutions; (iii) reduce discretionary decision-making; and (iv) be predictably, consistently, competently and impartially applied;
- Establish a framework to strengthen the governance and operations of civil society organisations to enhance their contributions to social and economic development in Afghanistan through, among other measures, the revision and clarification of laws governing civil society as well as the establishment of independent certification bodies for civil society organizations;
- Establish programmes (both privately and publicly-led) to build capacity to alleviate the binding constraints facing the private and public sectors;
- Involve the Private Sector in the provision of public services through Public-Private Partnerships (PPPs) and other modalities in areas such as power generation and distribution, water supply, transportation infrastructure, and social development;
- Implement measures to facilitate access to land by clarifying property rights, simplifying procedures for the transfer of titles, and allowing for longer-term leases;
- Work to expand significantly the outreach of a broad range of financial services throughout the country;
- Build the structures, systems and capacity of mediation and arbitration tribunals to ensure the efficient, effective and impartial resolution of disputes; and
- Instill an active practice of social responsibility and philanthropy which leads to the institutionalisation of private (business and individual) support for economic and social development through civil society.

AKDN experiences and best practices:

The AKDN's investments have demonstrated how the Private Sector, both business and civil society, can catalyse processes of stability: in creating and nurturing community development councils; facilitating self help groups; enabling group microfinance borrowing for impoverished women; and enabling community meetings to educate and empower them to safeguard and protect their urban environment. Roshan has pioneered corporate social responsibility programmes that link private business to community. As a commercial institution, it has endeavoured to establish best practices in the telecoms sector. From building parks in rural provinces and feeding street children, to providing business start-up opportunities for women, setting up public call offices and providing telemedicine opportunities to harness communications technology that now links Afghan hospitals to medical facilities around the world, Roshan has endeavoured to impact positively the society within which it operates. Similarly, the Kabul Serena Hotel has sought to revitalise the hospitality industry by not only creating the space for international visitors, but also training more than 700 staff, setting building

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and quality standards and bringing a new face to a city with pride and dignity that has suffered decades of war.

Wider Recommendations:

The approaches of the Afghan Government, and to an extent those of the international community to create an enabling environment for the Private Sector will have a bearing on the trajectory of peace and stability in the months and years ahead. Development experience from around the world has demonstrated that a framework for Governance calls for a mosaic of investments: participation of people and communities; delivery of perceived real benefits to the population through social services; encouraging and building civil society institutions and capacity which give people the ownership of processes, projects and decision making; collecting communities and people to come together for common cause both economic and social; preserving culture that enhances pride and dignity; and lastly but not least, connecting the poor to growth and growth to the poor.

The AKDN recommends:

1. More concentrated effort and resources be made available to address the priorities emerging from the Enabling Environment Conference;
2. In the wake of a worsening security environment, attention be centred on the impediments affecting indigenous Afghan businesses and address ways to encourage their growth;
3. While investments are made to build and enable the institutions of the Government of Afghanistan, equal attention must be centred at the rural grass-root communities to build and encourage civil society institutions which underpin people's participation in governance, especially in remote and highly marginalized areas;
4. Assistance be provided to the Government of Afghanistan to address corruption, counter-narcotics and criminality which is stifling progress;
5. Wider investments in energy, water management and regional co-operation are pursued so as to allow for investment and access to regional market opportunities; and
6. That development aid be undertaken in a fair and equitable manner. To date, the most insecure areas of Afghanistan have received the most amount of aid where as those provinces that present the conditions for successful development have received relatively little.

Mr. TIERNEY. I think the testimony here this morning has been excellent and very helpful. I notice that we didn't keep anybody within the 5 minutes, and I think that's fine. I think we all benefited from it.

Mr. Mawji, you win the prize because you couldn't see me fidgeting when you got to the 5-minute point, so we were able to get all of your information in, which was quite helpful. We appreciate that.

Let me start the questioning section, if I can.

I thought Mr. Pam framed this situation—and others also touched upon it quite well—on this crisis of legitimacy concept. And it was helpful to put it in that frame.

Mr. Mawji, when you were talking about that issue and about prioritizing different projects, can you tell me what your view is of Mr. Pam's comments, that he thought one way to best prioritize them would be to work through the public budget, in other words, to work with the Afghan Government's budget, allowing them to set the priorities, and then working through that, as opposed to each NGO or other entity trying to go off on their own deciding what they thought was important?

Mr. MAWJI. I would completely comply with the view that we need to work within the government priorities. There's no question about this. And I think those priorities are not rocket science. They are in health. They're in education. They're in rural development.

What I do fear, though, is that there is a role to be played or investments to be made to help deliver those services. So I think we do need to look at a concurrent and parallel process. And that's not to create a parallel system. It is to invest in the state, to build its institutions, its capacity, its thinking, but also then to empower civil society, the private sector, and others to be able to deliver some of those services, either through government funding or otherwise.

Mr. TIERNEY. Thank you.

Mr. Pam, I would like your reaction to that, first of all, but also the additional question, what about the corruption issue? We've all touched upon it here, and I think everybody has a concern that the investment might not get where either the governmental budgeting process of Afghanistan wants it to go or where individual investors want it to go.

Mr. PAM. Well, let me start by addressing the previous comment.

I think that the suggestion that government efforts to deliver services take advantage of all of the capacity that exists in Afghan society, including Afghan NGO's in places where the government doesn't reach, I think that is perfectly consistent with using public finance as a focal point for our efforts. I think that ties into the second pillar of the three-pillar approach of these new sector road maps which would create new national programs, sort of on the model of the National Solidarity Programme, which is a national program in the sense that there is a ministry in Kabul that is responsible for it, but it's implemented through, in many cases, through nongovernmental entities down at the village level. And so you've got to marry up the formal governmental structure with whatever capacity exists in Afghanistan, whether it's at the formal

or the informal level. And I think you've got—the answer to that will be context-dependent.

But I think what we've got to avoid is saying that, because a ministry in Kabul doesn't have officials that allow it to reach all the way down to a particular province or municipality or district or village, we should therefore give up on a state's structure and devote our efforts to parallel internationally funded efforts that go directly to NGO's at the district. I think there are ways of combining the two, but we can't give up on the public process if we want to address the underlying legitimacy crisis, which is, at bottom, a crisis of what the state can do.

On the corruption point, quickly, I think it's a central point; and I don't want to suggest for a moment that there are simple answers to it.

The suggestion that we place a greater emphasis on the Afghan budget, which entails greater United States and international financial support for the budget, greater use of budget support, for instance, is a risky proposition. And I think that one would do that as part of a multi-step process which would also involve some intensive technical assistance work, assessing the quality of the public finance systems. The World Bank and the IMF have already done a tremendous amount of work on those systems; and my sense from them, in general, is that those systems are actually in decent shape, but obviously the United States would want to hear that directly and see that directly and do some work preparing the national budget and then, if there's going to be a degree of fiscal decentralization, subnational budgets to receive additional money. Some money will be lost, but some money is lost when it's done through parallel systems, too.

The argument is that, only by putting money through their system and concentrating our efforts on making that system work—which it will only do imperfectly at the beginning—will we ever get to the point where there is a functional system that can respond—that can perform all of the functions that the quote from the EU Ambassador just described.

Mr. TIERNEY. Thank you very much.

Mr. Flake.

Mr. FLAKE. Thank you, Mr. Chairman. I appreciate the testimony.

Regarding the question of security, is the situation improving over the past several months in terms of, particularly, agricultural production and the need for outside investment? But in so many areas of the country we have difficulty operating, or at least other organizations outside of government.

Mr. Usman, do you want to address that? Is that situation improving?

Dr. USMAN. Yes, sir. I think it is improving, but I want to come to, if I may, the question of corruption a little bit.

You see, once, according to a rough estimate, our Ministry of Agriculture had something like 11,400 or 11,500 staff. However, at this time, probably the Ministry of Agriculture system has something like 4,000 to 5,000 staff.

And the salary of these people are something like \$50 or \$60 or \$80 maximum, and rent and everything else in the Kabul area is

\$100, \$200. Then to expect that these people could live on that salary, it is impossible.

It is a symptom—I am not critical of NGO's, but NGO's are paying lucrative salary allowances to their staff. There is a sort of jealousy we've developed with the NGO's. NGO's actually get the cream of the experts of the government staff at their employment.

I was thinking of that. I said, OK, if from this 5,000 pool that we need in the Ministry of Agriculture supposedly, then probably, based on a good selection criteria, we should supply them with some sort of hardship allowances and put some tough sort of requirement there; and I think they would function best. According to my experience, when the Agricultural Development Bank functioned properly in the region, it was a successful bank.

The bank was giving, compared to the rest of the employees of the government, some 50 percent more salary to their staff and good selection area and good selection character. And all the staff were working perfectly, and they were sort of appreciating the jobs, and the corruption reduced.

Mr. TIERNEY. Our apologies. These are notices with regard to what is going on, on the floor of the House. So we'll wait 1 second, and then they will stop, and we will give you extra time.

Dr. USMAN. OK. If we are completely sort of ignoring that—OK, there is corruption. Therefore, we do not want to deal with it. In the Ministry of Agriculture, while I was there, we wanted to align our financial system with international accounting procedures. For 6 months, I was looking for an expert to come and fix the system. An expert was not available. And then the ministry for some reason, had something like \$3 million. They gave it to SAO, if I remember correctly, for a 35 percent fee, to spend it on their accounting procedures.

Therefore, accounting, bookkeeping, financing, reporting need a lot of work. And I know it is difficult, but we have to do it. We have to reconstruct the system.

As far as agriculture is concerned right now, you know, as I said in my written testimony, that the crop production per hectare is something like 1.6 to 2 tons per hectare. And for the dry land, which is around 4.5 million hectares of the dry land, this is 0.6. In the regions, they are getting 4.5 from irrigated and 2 tons from dry land. This is for staple foods like wheat. But we have to work on reducing the cost of production. Otherwise, we cannot compete with the neighboring countries.

In 2002, Afghanistan was supposed to have a bumper crop, but similarly several of the neighbors had more bumper crops, and the farmers would not even bother to go and harvest the crop.

Therefore, research—bringing back the research, bringing back the extension system is really, really necessary, putting the engineer expert along with the ministry expert to complement each other.

Mr. FLAKE. Thank you.

Mr. Pam, with regard to so much emphasis on public finance going through the Afghan government, for a body like this, the U.S. Congress that has to appropriate the money to the extent that we are talking about direct assistance, there is a point at which you simply say we cannot tolerate so much money being drained off

with significant corruption. But you seem to be making the point that we have no choice, that we have to funnel through that system and not through a parallel system.

But, I mean, give us some guidance here. What kind of strictures or mandates or whatever can we put in place? And if they are not met, what are our choices at that point? Because it is a difficult thing, I can tell you, to sell foreign aid in general. But when a significant chunk of it will be drained off, it is tough to just accept that as a matter of doing business.

Mr. PAM. I understand, Congressman. I think I would give three answers to that question.

The first is what the alternative is. We have been in Afghanistan for 8 years. The chairman gave a figure for the amount of money that has been appropriated to Afghanistan during that time. It has been a very large number. The question is, what results have we received for that investment? It is my sense that there is a broad consensus that we haven't received a very good return on that investment by the U.S. taxpayer. This is why Secretary Clinton said that looking at the effort, looking at the results achieved was heartbreaking.

And I mentioned the Iraq case, because that is another case that has happened contemporaneously with our investment in Afghanistan where we appropriated—Congress appropriated \$20 billion, \$40 billion for civil side assistance and it produced very poor results.

Now—so the advantage of that investment thus far has been greater accountability. We appropriated it through the standard modalities for foreign assistance, which meant that it went to U.S. agencies who used U.S. contractors who were used to the U.S. rules for accounting for the money. The problem with it is that, too often, the investments made with that money were not synched up with Afghan priorities and institutional capacity in such a way that it moved the Afghan government toward greater capacity and self-sufficiency and self-governance. In other words, further toward a point at which we could eventually scale down our presence, both military and civilian.

So the first point is what the alternatives are. I am suggesting that business as usual has not worked very well. I think this is consistent with the President's new strategy for Afghanistan and Pakistan, which calls for a new approach.

My second point is what the approach that I am recommending would entail. Again, I am not suggesting that we simply transfer all the money that we would have appropriated through the systems we know and trust directly into the Afghan budget, by no means. I think this is something that has to take place, has to be done gradually. And I think it is already—the first steps of it may already be in motion.

There have been some cases where intensive work with particular ministries has given our agencies comfort that ministry is now ready to receive a greater degree of budget support. And I think USAID's work with the Ministry of Health is one of the examples there. But my argument is that we need to do that on a broader scale, and doing that is something that will require intensive technical assistance in public financial management.

Fortunately, we are not starting from scratch. As I said, the World Bank and the IMF have been working on this since 2001, have produced reams of documents about it. There are detailed assessments of how—the state of the system and the confidence that we can have in it.

And we have a further advantage in that we appear to be in the process of sending over a significant number of additional civilians and/or military reservists to focus on civilian side assistance. Many of those people could be used to help enable this public finance focus, stationed at every level of the Afghan government, given sufficient training in public financial management, and they could help us track it.

But the point is that the money has to go through the Afghan institutions, with us on the outside helping the institutions work, rather than going through us on the outside providing the benefits to the Afghans.

Mr. TIERNEY. Thank you very much. Thank you, Mr. Flake.

Mr. Foster, you are recognized for 5 minutes.

Mr. FOSTER. With unanimous consent, I would like to enter this into the record. This is a document which is volume one of the Afghan Judicial Reports.

Mr. TIERNEY. Without objection, so ordered.

Mr. FOSTER. Which my father was involved in producing in 1975 and 1976, where he essentially rode circuit in a Land Rover to the local—whoever it was who was in charge of making legal decisions at the time. And I recommend it to anyone that—it is very sobering reading to understand the huge chasm that exists between a modern functioning western legal system and what was in place at least in 1975 and has probably gone backward, is my guess, because of the wars and the time period.

So my questions to Mr. Pam and Mr. Mawji are, what is the structure of the Afghan legal system today, and what are the useful alliances that could be encouraged to build a functional legal infrastructure? Are the alliances with Western or Islamic countries going to be more valuable in this? And if Islamic alliances are the best, with whom? Where are the Islamic partners that might have high-functioning legal systems that could be most easily culturally adapted to Afghanistan?

Either one.

Mr. PAM. Well, I will answer briefly. I am a lawyer, but I have never worked on legal issues with respect to Afghanistan.

I would just say that I think you raise an excellent point in distinguishing between, and asking the question of whether Islamic—technical assistance on the legal system might be more effective coming from Islamic lawyers than from Western lawyers. And I think that is—the larger point there—we face a decision generally in providing assistance of whether we want to—our goal is to set it up to look like our system—which in many cases implies a Herculean effort, because they are coming from very different starting points not only in terms of economic development but culturally, religiously, legally—or whether we want to focus on what is there and what other resources are much closer to what is there in order to produce incremental improvements.

Mr. FOSTER. Mr. Mawji, did you hear the question?

Mr. MAWJI. Yes, I heard the question; and I think it is an excellent question.

I think we have to divide the legal system or the rule of law into various parts. I think there are certain parts of the legal system which we can associate with internationally. You know, do we have a policy for investment? Do we have a policy for trade? And so on and so forth.

I think when the Islamic issues come in is when it comes into conflict resolution amongst communities, amongst personal wealth, and so on. And the constitution of Afghanistan certainly makes provisions for the Islamic system to be used under different interpretations of the faiths—for example, the Salafi and the Shia.

Now, while there might be particular areas that need to be developed specific to this case, but in the context of why there is Islamic law or how it has been used in Islamic countries, I think we need to draw on countries like Malaysia, for example—Malaysia is an extremely progressive Islamic state—some countries like Bahrain in the Middle East, who has also sort of made progress. And I think your point is extremely valid, because we should welcome or draw in the inputs of these countries in trying to help Afghanistan shape its legal system.

Mr. FOSTER. Mr. Mawji, I was interested also in your discussion of the difficulty of obtaining clear title to many plots of land as being an impediment to economic development. I remember my father talking about a plot of land that was claimed by six different people, and they have been arguing about it for generations as to who actually owned it. And it strikes me there may be an opportunity for us to make a contribution by actually establishing a central data base of who owns what. This is a sort of technical project that the United States actually could help out with. And then, of course, you would have to go through and make all the independent verifications. And I was wondering if you thought that was a promising avenue for United States or foreign assistance.

Mr. MAWJI. I would agree with you, sir. I think that is an extremely needed area in Afghanistan. Land registration or land ownership goes under the title deeds here. They call them Khawalas. And you have a huge set of issues. You have corruption and faith Khawalas. You have had two administrations in Afghanistan, the Taliban and the pre-Taliban. And a lot of refugees have moved over to Pakistan. Iran's land was taken over by the Taliban, resold, and new Khawalas given.

And the system of land rights amongst families here: Your father would then pass it on, divide the land equally amongst children, and there is often disputes amongst children as to how much land is owned by who because there is no clarity of documentation.

And I think any effort that can be made regarding trying to bolster up the municipality and other areas of governance, is very valuable. The Ministry of Urban Development should look at land administration, so that it becomes a credible document from which they can turn land into capital.

Mr. TIERNEY. Mr. Murphy, you are recognized for 5 minutes.

Mr. MURPHY. Thank you very much, Mr. Chairman.

I missed the opening remarks, so, Mr. Chairman, I don't know if you mentioned this, but, Dr. Usman, in our trip that Chairman

Tierney and myself and a few other members of the committee took earlier this year, we heard stories about farmers who were spending more money paying customs, charges, paying tariffs, paying different forms of extorted payments as they transported their goods through the country to whatever port the goods were going to, to an extent that it essentially canceled out the benefit of producing the good in the first place, which was consequently driving people to the illicit trades in which they were not responsible for the transport of those goods.

Can you talk a little bit about where we stand today in terms of the difficulty of transporting agricultural products throughout the country and what we need to be doing as a government in terms of trying to make that process easier?

Dr. USMAN. I think the situation from the time I was there has been, as I heard, improved a lot. And generally, the observations that you had, were true. But especially in the case of Buddhist trades, supposed trucks that are taking fruits through Pakistan, and several times the truck is unloaded and loaded. By the time it reaches India, its cargo is completely—especially grapes—rotten. And lately there has been some agreements to improve the situation.

And one of the things that implicitly I indicated in my testimony was that these farmer associations, producer associations, marketing associations have to be firm, because farmers in Afghanistan are small and weak. That way, through their association and in direct contact with the final customers, then they will find a sort of political pressure, which they can utilize to see these things improve. And at the present time, we have something like 1,000 of these associations, but they are so weak financially, technically, that they could not stand and fight for their benefit. I think it needs both from the government side and from the grassroots side, and we have to mobilize the people.

Thank you.

Mr. MURPHY. Let me ask a more general question to the panel, and that is this: I think whether we are talking about our military or diplomatic or economic progress in countries in which we occupy, benchmarks continue to be a problem in terms of trying to identify our levels of success. So as you look 5 years out, maybe even 10 years out, to the Afghan economy, what are the benchmarks for success that we should be looking at to try to decide whether our investment there has made the kind of gains that we hope? What are the indicators that we need to be looking at in a 5- or 10-year timeframe that help us understand the success or failure of our mission there?

Dr. USMAN. I think the benchmark from, let's say, agriculture—80 percent of the population lives in the rural area, and their life is directly and indirectly connected with agriculture—the benchmark there would be productivity in agriculture.

Supposed, we have 95,000 hectares of land which is devoted to orchard. If we see that the benchmark is to double that hectareage, and according to the expert, even the present orchard could be increased, yield could be increased or could be doubled, if that would happen, if the production of wheat per hectare reached the level of neighboring countries, then we are really successful on the national

level. Not on the small project here and there, that would be temporary and not long-lasting sorts of indicators that would make that country stand on its feet.

Thank you.

Mr. MURPHY. Mr. Pam or Ms. Callear.

Mr. PAM. Well, I would like to, with your permission, interpret your question more broadly than just benchmarks for the economy, but benchmarks appropriate to the civilian side effort more broadly.

The benchmark that I—in my written testimony—suggest is budget execution performance. Which is to say how much they are spending through their system. It is—obviously, just merely spending money is a very gross measure, as we know. But in my experience, using a metric like that would have the benefit of focusing the Americans working in the country who are supposed to be building the capacity of the Afghan institutions, focusing them on ways to improve that specific element of performance. And it is something that everyone understands.

And if the number will start out low—I think there was a reference in previous testimony to the Afghans only being able to spend 40 percent of their development budget. Those numbers, numbers like that, are common in the developing world. Budget execution is a problem in every emerging market.

But you start with a number like that, you give the effort, the objective, the task of doing what is necessary to improve that number so that money does flow more effectively through the system with less leakage and producing more results at the end. And I think what you end up with is both a more focused and effective U.S. effort on the one hand, and an Afghan government which is producing more results on the other.

Mr. MURPHY. Thank you.

Mr. TIERNEY. Thank you, Mr. Murphy.

I look at the testimony of all of the witnesses and I see one common tie about credit, availability of credit.

Mr. Usman spoke about it, about enhancing government credibility with better credit in the agricultural realm on that.

Mr. Pam talked about the need to better use Afghan capacities, that there was plenty of entrepreneurial spirit out there, but capital was a problem on that.

Mr. Mawji talked about expanding significantly the outreach of a broad range of financial services throughout the country.

And, Ms. Callear, you talked about it as well and talked about the Afghan Growth Fund and expanding the capital flow to small and medium enterprises in Afghanistan.

So let me start with you, Ms. Callear, because we haven't heard enough from you. Does the infrastructure exist to increase that flow of capital? Is there enough structure there, for the writing of these types of loans to the administration of the loans? What about security or collateral on those loans? And just round that out for anybody to comment. What would a well-run enterprise fund look like if we decided to go in that angle?

And then, at the end, I will ask Mr. Pam to talk a little bit about his comment that enterprise funds have failed elsewhere.

Ms. Callear, can you help us there?

Ms. CALLEAR. Yes. Well, we are certainly—I think what we are finding is a surprising level of demand. So there are—as many have said, there is a real entrepreneurial culture. But what has been missing is the ability to really apply that desire in a very practical way, because access to capital has been lacking.

But it is more than just the capital. It is also providing the various other kinds of support. We were talking about the need for proper accounting and so on. So it is a business-building effort that requires capital, but also various types of technical support.

And I think we have also said it is important to make sure that the reach is beyond Kabul. We are trying at a limited way to do that. I think, in order to reach some of the other areas, we would certainly need some additional support. But it is a very important thing. Because I think otherwise, in answer to one of the other questions, a lot of the potential economic benefit is being left on the table because you are not doing the value addition in country. You are exporting raw product, or you are not getting the distribution to the places where it needs to go.

So the demand is there. It is challenging. But these challenges are not all unique to Afghanistan. And I think in terms of what is needed, whether it is an enterprise fund or more—for larger investments or more smaller investments, it is the combination of the capital and technical assistance, and then trying to structure it all in a way that is culturally sensitive in an Islamic culture, as well as dealing with the constraints that one has in the legal system. But there are ways to do it, and you can get good repayment rates at the micro finance level, and we found at the SMA level, as well.

Mr. TIERNEY. Dr. Usman, what would that loan situation look like in Afghanistan, that might be different than a Western loan? Ms. Callear just mentioned that it might be good to be culturally sensitive in the way that we are getting this money out to the entrepreneurs, and the terms in which it is distributed. How might that differ from what we, in the West, would consider a loan prospect?

Dr. USMAN. Well, you know that in Afghanistan—let's say, for the example, at the time of the king—we had three or four specialized banks. There was Agriculture Development Bank, AID Bank, and Industrial Development Bank. And I don't know who went there and came with the idea that this specialized banking—we don't have experience worldwide. This comes from Afghanistan, too. And without actually considering the idea, we look for experience, that actually, this Agriculture Development Bank received three loans, from the time of the king and the time of Daoud, from the World Bank, and they are handling it fine. The people, repayment was picking up and the farmers were really healthy in Afghanistan, you know.

And now all—the Minister of Agriculture, everywhere they go, the people ask, where is credit for us? And in the form of vouchers, the government gave, I think, with the help of donors, something like \$100 million in vouchers, and collection of that is negligible. But the people are used to getting the loan, like here, and paying the interest and paying it back.

If you have the technical capacity, if you improve the accounting system, improve the banking system, and especially, in agriculture,

if you connected these associations—farmer associations—with—the bank board and put them to work, eventually they would become the owner of the bank. It would be a really a good system.

The system is working here. In some other countries that I have seen, it is working. Supposedly it is working in Egypt. The Agriculture Development Bank there, they were giving \$5 million a year as lending to the farmers and to the agribusiness people, and they were successful.

Mr. TIERNEY. Thank you, sir.

Mr. Flake.

Mr. FLAKE. Thank you.

Mr. Usman, just to followup, to what extent are the NGO's that are operating locally purchasing food from local vendors and farmers?

Dr. USMAN. Well, there was—for national security purposes, I think at one time they—if I can remember correctly, they bought something like 10,000 or 15,000 tons locally. But Hindus, so far as I see, they don't buy from local markets. And that is a difficulty; but I say there are international markets right in Afghanistan. In Afghanistan, like the soldiers are there and the foreign community is there. Then, if we built the standards, laboratory facilities, certificates, and all the documents, then that would open up for Afghanistan products inside the country. And then later on, like FDA, you could establish quality control checks for both domestic and international products. Right now, the difficulty is that even wheat is imported from Afghanistan's neighboring countries.

Mr. FLAKE. Mr. Pam, how realistic is it to move significantly from poppy production, over a sustained period of time? And in that question is the problem the government—I sensed it in the couple of visits that I made to Afghanistan. From the first visit to the second visit, there seemed, at least with the President's office, less of a commitment to fight the drug war, if you will, and less candor, in terms of what is going on outside of Kabul.

To what extent—is it going to be difficult to offer incentives? How long is it going to take to move to—whether it's pomegranate or whatever else—to offer something sustainable, particularly if the government doesn't seem as committed as perhaps they should be to move away from poppy production?

Mr. PAM. Congressman, I am not an expert on the agricultural sector and that issue.

Mr. FLAKE. In terms of the government though, in terms of the government's commitment there, do you sense—and this goes back to the problem of how much do we run these programs through the government. Do you sense an increased commitment or lessened commitment over the last couple of years to transition away from poppies?

Mr. PAM. I am not sure. I haven't had any discussions with the government on that subject.

Mr. FLAKE. Dr. Usman, you look like you are itching to answer. Go ahead.

Dr. USMAN. I think, based on my experience, the government is fully competent to actually find alternatives to poppy production. But we have to—you know, there is one commitment on the paper, one actually that work would be done toward accomplishing it. But

the government has to build the right infrastructure to actually conduct that activity. The infrastructure is not there.

There was at the time of the King and the time of Daoud, when we had 26, or 24 such stations, 14 sub research and 7 main research stations. None of those research stations are working now.

You have to produce seedlings. You have to produce seedlings somewhere. You know, it is a good idea to provide free seedling for the farmers. But then you have to provide proper technical support to the farmers after they grow. There is new variety of almond that would bear fruit, I think, in 3 to 5 years. Then, with that, then you have to teach the farmers how to do mixed farming.

But the unfortunate thing is that a lot of experienced farmers that migrated outside of Afghanistan, they died; and they could not pass their skills that they had to the new generation. And the government, does not have capacity and means to do it or the commitment. But we have to establish, as you said, the infrastructure for it. The infrastructure is not there now.

Mr. TIERNEY. Thank you.

Thank you, Mr. Flake.

Mr. Kennedy, we passed you up on the first round because you stepped out for a second. We apologize for that. We recognize you for 10 minutes.

Mr. KENNEDY. No problem. Thank you, and thank you for your commitment to this issue and your work. I welcome the panelists.

Just following up on that past question, it is hard for me to think that the government is really committed to the restriction of poppy growth when you see the enormous economic value that it provides for the country of Afghanistan. What is currently the percentage of poppy crop in Afghanistan as a percentage of overall poppy growth in the world? Do you know?

Dr. USMAN. Well, I know I have my information from the newspaper, probably so does Congress. It is 92 percent or something like that. But I think we have to give to the farmers an improved agriculture package.

And Ms. Callear was mentioning—you know, the time I was there, even the dry fruit and nuts, which could compete with the poppy—because in India they really appreciate and pay higher prices for the almonds of Afghanistan—if they made a rough budgeting analysis, it was two hectares of, supposed, almond that could substitute on a profit basis for one hectare of poppy. And with the value added, and you would have that processing, packing, cleaning, grading right in the farmer field and involve the farmers there, then probably it could compete on economic terms.

But, right now, 70 percent of the irrigated land is devoted to wheat production. And with wheat, it takes one hectare of poppy to substitute it with 14 to 24 hectares of wheat.

Then, with this divergence, there would be problems all the time; and sometimes, for the politician, it would be difficult to convince the people to actually apply new methods. But if you go in this other route, then probably the government would make their argument clearly with the people.

Mr. KENNEDY. Then why are we not doing that, the nuts and the fruits?

Dr. USMAN. Well, as I was saying, sir, we don't have the infrastructure to do it—the research, the extension, the technology, the technical know-how of the work. We have to build it.

In the last 7 years, you know, I have said that you would see in two districts, the Hindu is involved in sort of upgrading the wheat. But then the proper seed for it was not there to actually give to the farmers.

Mr. KENNEDY. Well, they have done it. In Pakistan, from what I understand, we have been working with the agricultural sector—because Pakistan had a huge, huge poppy crop. And they have worked very hard to try to eradicate it doing exactly what you said, substituting with the nuts and fruits.

Ms. CALLEAR. And I can see—

Mr. KENNEDY. And they have successfully done that in many parts of Pakistan. So—and if it takes so long to do the wheat and the wheat is a “no-go” in terms of the farmers, then I think we should just move right on to what the local people think works best. And if it takes the infrastructure, that is what we need to do. So I think we should listen to that message loud and clear and get with the program.

Ms. CALLEAR. And the nut processor that we have lent funds to is telling us that they cannot meet the demand in the Indian market for the higher-value, better-quality processed nuts. And that goes directly to his point, that the agricultural infrastructure needs to be there to support the production, so that when you have the capital for the processing facility and the ability to bring that value added back to the farmer level, you will be able to do it if you invest it at the agricultural level.

Mr. KENNEDY. What I am trying to figure out, Mr. Chairman, is why there is a missing connection here. Why we are forcing this wheat thing on them, when it is clear that the locals are not really into it.

Mr. TIERNEY. If the gentleman will yield, that is exactly why there are two parts to this hearing. One part is to talk to these folks that are with this morning, and the second part is going to be talking to the administration. I don't think they can answer for the last 7 years, but by the time they come in at the summer, the fall, they will have to answer for January 20th until now whether or not they are following the wiser course, or continuing on the less wise course.

Mr. KENNEDY. Let me ask you just another question on health care.

Dr. USMAN. And in continuation of your answer—You know, we have 4.5 million hectares of dry land for farming. If we supposedly gave to the farmers—provide to the farmers—technology to increase the yield, average yields from 0.6 to—dry land Afghanistan is getting to 2 tons that the neighbor is getting it, this 4.5 million hectares would come—would bring something like 8 to 9 million tons of grain. Afghanistan only needs something like 6 million tons. But that technology unfortunately, actually, is not there.

Mr. KENNEDY. Let me ask you with respect to land mines. Is there a problem when you are doing any of this agriculture with land mines left over from the former Soviet war?

Dr. USMAN. Well, I think that has been the main problem. Farmers are doing this with a lot of casualty anyhow, because of the necessity. But land mines in some parts are still there.

Mr. KENNEDY. Would it be useful for us to try to get the Physicians Without Borders, those who do the rehabilitative medicine, to try to help do more satellite communications, so forth, help consult with doctors there for more rehab medicine, so the farmers and the families and the like that happen to get—

Dr. USMAN. Sure.

Mr. PAM. Could I say something on this point about agriculture? I think Dr. Usman makes an excellent point in emphasizing the need for infrastructure. And I think the need for infrastructure that he is referring to it is worth noting that it's state infrastructure. The need to rebuild an agricultural extension system within Afghanistan is the need for a national program. This could be part of the—this could be one of the key sectors that the road maps described.

Mr. KENNEDY. Can you get us some of the statistics on these entries as a result of land mines, and what would be your proposal to see what NGO's could help in terms of rehabilitative medicine for those farmers and the like who get injured as a result? Because I understand Afghanistan is littered with land mines, and I just want to know what we are doing to help in rehabilitative medicine.

Mr. PAM. I wasn't saying anything about land mines.

Mr. KENNEDY. I know you weren't. I am asking you now, because you are part of the Sustainable Development of the U.S. Institute of Peace to help us with this.

Mr. PAM. Certainly.

Mr. KENNEDY. And in terms of infrastructure for health care, there is very little drinking water and sewage. What is going on with that for the farmer and for the population there in terms of public health? Could you tell us about what is going on there, in terms of building infrastructure? I mean, you can't have much of the farming life and community if people can't have drinking water.

Mr. PAM. Yes. I am afraid I can't give you any detail on the efforts that—the water efforts in particular. But I can look into it, along with land mines.

Mr. KENNEDY. OK.

Mr. MAWJI. Could I make a comment?

Mr. KENNEDY. Please.

Mr. MAWJI. Just a couple comments. One referring to the question on health and water. The other one also on narcotics. And just to say that, on the narcotics side, our experience has been in Afghanistan that it is very, very difficult to compete with any kind of agricultural productivity in the wake of just the sheer income revenues that are coming in from narcotics.

And, for example, we would pay \$2 a day just to build a canal or a road for unskilled laborers, and the narcotics poppy growers will pay \$15 a day plus three meals to harvest the poppy in the same construction period, during the year. And we really have to ask ourselves, do we compete with narco wage prices?

And I fear that while the point has been made on agriculture—and some are absolutely valid, and I do believe that the infrastruc-

ture needs to come into play in terms of improving the agricultural prospects—we will not be able to really address the narcotics issue until there is a sense of consequence for the people who grow it. And I fear there is a large amount of impunity at this point in time and with very—we have various carrots, but very, very little sticks to stop them.

And experience has also shown that large-scale eradication doesn't really help. It makes the poorer, poorer. It doesn't affect the rich.

So we really need to look at a multi-pronged strategy that looks at targeted eradication, but that also looks at naming and shaming bad actors, interdicting routes that are quite traditional—I mean, I could tell you in areas where they operate in northeast in Afghanistan, and people—farmers are able to tell us what kind, how much narcotics cross and at what point in the border. And the reason they can do it is because it is such common knowledge. There is pure impunity. There is no stick to go with narco production.

With regards to the second question on water and health care, I have to say that the basic package of health services provided by USAID have gone a long way in terms of reaching out to basic health care in the villages.

The whole notion of water has been less well tackled. Yes, it is one of the smaller investments that one makes, \$100,000, \$200,000 in a village or a cluster of villages, and you drop child morbidity by 14 or 15 percent; and it is something that we have been not pioneering, but certainly advocating for, with other colleagues working in Afghanistan, that providing basic water supplies is extremely important. But the government also needs to look at the whole issue of water supply in a much broader policy level and at how we are going to tackle the needs for water in what is a very, very diverse geographic landscape in Afghanistan, from the Pamirs and the Hindu Kush going north-northeast, to almost a desert situation in the south, where the solutions to the problems are going to be very different.

Thank you.

Mr. TIERNEY. Thank you for that; and thank you, Mr. Kennedy, for your questions. They were well placed.

One of the interesting notes that our expert on the staff here says: Of the \$37 billion spent in Afghanistan, \$37 billion, less than 1 percent has gone to agriculture. Less than 1 percent. And that was 80 percent of the economy. So for all of our witnesses, I guess the staggering point—if I can speak for Mr. Flake as well—to us would be, who is doing the central planning here? Who is doing the overarching view of what needs to be done that is important? Who is deciding what projects are the ones that ought to be prioritized? And then making sure that something is done.

I know that Agha Khan has done significant work there. They are the largest private investor in Afghanistan. So is there any functioning entity, comprehensive planning group that pulls all of the NGO's, all the private investors, all the government investors together and says this simple thing like spending a couple hundred thousand dollars on a cluster of villages is going to be that helpful for public health? Who talks about the land mines and what we might do on that effort, that talks about putting more than 1 per-

cent of all the money that is coming in toward 80 percent of the project? That talks about, as Ms. Callear indicates, getting more capital into the flow.

Just from each of the four of you, very briefly, because I understand we are back in session on the floor. But what do you know about whether or not that kind of an entity exists, what the work has been doing or what has been planned in that regard?

I will start with you, Mr. Mawji, please.

Mr. MAWJI. It is a very, very valid question.

I have to say that there is much better, increased coordination in recent months, particularly under the leadership of the United Nations. And I think the United States, together with the Government of Afghanistan, has tried to look at much more concerted, coordinated mechanisms that allow us to be more accountable, but also look at specific priorities within the rural areas.

But I have to say a caveat, because I do believe that, while there is a lot of rhetorical thinking and coordination about it, we don't really, say, have a Kandahar development forum or we don't have a Helmand development forum or a Badakhshan development forum that sits in Kabul, that sits in the province in a systematic fashion and says what the tactics are that we need to bring in, and how the investment is going to come in to make a real difference in the quality of the people's lives.

Mr. TIERNEY. Thank you.

Ms. Callear.

Ms. CALLEAR. I would have to say that we have worked fairly independently in terms of what we have done. We have gotten good support in terms of access to the credit line that we are now using for lending through OPIC. But in terms of broad-based interaction on the ground with the eight agencies there, there really hasn't been much. We try to stay in contact. But trying to figure out what exactly you are asking, what's that strategy, it is not—

Mr. TIERNEY. I am not saying it's your responsibility, because I commend the work that you do. But the fact of the matter is, commending the work that you do, you may not be doing the highest priority work for that society. So as much as you are doing, and as well as you are doing it, and as hard as it is, nobody has helped you focus on what their needs are.

Ms. CALLEAR. And I think there can be more coordination, for sure.

Mr. TIERNEY. Absolutely.

Dr. Usman.

Dr. USMAN. Yes, sir.

I actually was working in the Ministry of Planning before the Russian invasion. And at that time, one, it was our responsibility to see that priority is taken into consideration; and based on the priorities, we controlled the budget and then controlled the budget quarterly, how much they spent, how much work was accomplished. But that ministry—now I think they call it the Ministry of Economy, and that is getting quite weaker and probably could not do this job.

And at the time I was there, President Karzai's government under the proviso that came by name of his authority, they were

doing that job. But they didn't have that much expertise to actually conduct that job properly.

Now the U.N., with the help of Afghans, are doing it. I think it is really a good step to actually create something like that, to actually see and coordinate the activity. Even in each ministry there should be—you know, like one of the difficulties we had in Ministry of Agriculture, there were 20 donors, and each one of them based on their country policy, one of them going one direction, another going another direction, another going another direction. There was not that much coordination, and there was not that much capability to coordinate with the ministry. And I think that should have to be done and that capacity has to be stringent at the macro level, and also the micro and the factual level.

Thank you, sir.

Mr. TIERNEY. Part of my understanding is that Mr. Holbrooke is supposed to be working in this effort, and we certainly want to find out how this is going.

Mr. Pam, do you want to just wrap that up, with Mr. Flake's indulgence?

Mr. PAM. I thank you for the question. I think it is one of the most important questions that we have to ask, and I agree with the way Dr. Usman has just framed it. I addressed this in my written testimony.

When development intervention A is the priority for donor X, and development intervention B is the priority for donor Y, and in the case of Afghanistan you have to multiply that A through Z, double A through double Z, to include all of the countries, all of the NGO's operating in the country, what you have is everyone doing A through Z and double A through double Z and a very incoherent approach.

Now, in theory, you could have an international body like the U.N. Assistance Mission in Afghanistan performing that coordinating function, and UNAMA has tried. But UNAMA doesn't have the authority to direct the programs of individual donors.

So my conclusion is that the only way to accomplish that kind of coordination is to fall back on the entity that has the strongest authoritative claim to be responsible for coordinating and prioritizing, which is the Government of Afghanistan itself. The system worked when it was the Ministry of Planning, but the Ministry of Planning and the Ministry of Finance have both been taken out, have been disempowered. And my recommendation to focus on Afghan public finance and budgets is in part motivated by the desire to find a way to put them back in the loop, in order—in substantial part—to solve this coordination problem.

Mr. TIERNEY. I guess that is part of the tension that we find up here. If we are to look at trying to put the money through the Afghan Government, because that is the way they are coordinated around their budget priorities, and then to see that one of their priorities is to weaken those 30 agencies that would probably be best at coordinating all of the various sorts, puts a conflict up there. And the Karzai government in particular, having weakened those agencies, as Mr. Mawji said, you know, having no punitive aspect at all to those people that are transporting the opium, like not necessarily the growers but those on the chains above that, just letting

them get away with impunity, those kinds of decisions make it difficult for us up here to say, OK, let's put all our eggs in that basket.

It seems to us it is going to take a lot of work, particularly where Dr. Usman had testified earlier, a lot of that human capacity no longer exists. They are either moved out of country for fear of their physical condition, or their families have been killed in some of the conflicts, or have gone because there were no jobs—nobody was taking advantage of their skills and moved on.

Mr. PAM. May I just throw in one more?

Mr. TIERNEY. One more frustration? Go ahead.

Mr. PAM. Well, a potential part of the problem, which is—I understand your reservations about putting all your eggs in a basket that you have finite confidence in. But this is why I think that part of the solution might lie with fiscal decentralization.

And, in my terms, creating multiple entities that have budgets and that have some—that are closer to the people and that have responsibility for providing some of the—performing some of the governmental functions, providing some of the essential services, that then creates a competitive environment where we are not solely reliant on the national government. Neither we nor the people of Afghanistan are solely reliant on one government, and instead can sort of go to multiple governments and try to encourage at least some of those governmental entities to perform.

Mr. TIERNEY. And I guess that focuses even more importance on the number of civilians and the nature of the civilians' experience that the President has recommended sending in, as well as members that the international community is sending in.

Mr. Flake.

Mr. FLAKE. No further questions. Just to comment.

I think you hit on the most relevant point here. There seems to be testimony and need—and we have heard this again and again and again—I think, for greater coordination. And so I am very anxious to hear the administration's plan, come the fall. I hope that they are monitoring this hearing to get a taste of your testimony and what you have said here. So thank you.

Mr. TIERNEY. Thank you, Mr. Flake. Thanks for your participation in the hearing and your ideas.

I want to thank all of our witnesses. Mr. Mawji, thank you from afar. We have really benefited from having your expertise and congratulate you on the work that your agency is doing in Afghanistan and elsewhere.

And the witnesses that are here today, thank you very, very much for both your written testimony, your conceptualizing of this, helping us frame the questions as well as some of the answers and your time spent here this morning.

I agree with my colleague, Mr. Flake, that we really want to grill the administration on where they are or where they are going on this. I think we might expand it out, too, as to where some of the international organizations are playing in this. Where is the U.N. in terms of coordination? What other international agencies might be playing a role in that? Or at least if Mr. Pam says that nobody seems to have the authority to do it, who has had the best capacity

to step up and suggest that we all volunteer to work together and set up some framework up for that?

Thank you very much. We are privileged by your testimony and appreciate it a great deal. Meeting adjourned.

[Whereupon, at 11:56 a.m., the subcommittee was adjourned.]

[The prepared statement of Hon. Mike Quigley and additional information submitted for the hearing record follow:]

Statement for the record from
Congressman Quigley

Rep. Quigley
- for the record

I want to thank Chairman Tierney for holding this hearing today to discuss an often overlooked element of Afghanistan's recovery: its economy.

Our focus, all too often, is on our military strategy in Afghanistan, and it's easy to put our blinders on and discuss only troop levels and security.

But security is not enough.

Security must be developed concurrently with economic opportunities, or the Afghan people will never be able to restore their nation to its former stable and vibrant state.

Economic development and security are inextricably linked - you cannot have one without the other.

World Bank President Robert Zoellick argues aptly that "fragility and poverty alone do not necessary lead to conflict, but low and stagnant incomes, unemployment and ineffective government can create an environment that sparks violence."

With unemployment in Afghanistan hovering at 40%, the country is certainly vulnerable to violence.

As we discussed in our last subcommittee hearing on the "civilian surge" in Afghanistan, the war there will not be

won with military power but through the hearts and minds, and today we might add through the pocket books, of the Afghan people.

We have numerous hurdles to overcome before we can claim success.

Roads need building, infrastructure needs repairing, loans need granting, and laws need developing –

But all this can be achieved if, as Jeremiah Pam explains, we counter the “temptation to do directly things better done indirectly.”

The U.S. and foreign allies cannot rebuild Afghanistan

Only Afghans can rebuild Afghanistan.

I look forward to learning from our witnesses today how we can better support these indigenous efforts to spur economic development.



JULY 11, 2009

HOUSE OVERSIGHT AND GOVERNMENT REFORM COMMITTEE
SUBCOMMITTEE ON NATIONAL SECURITY AND FOREIGN AFFAIRS
UNITED STATES HOUSE OF REPRESENTATIVES
**“THE UNITED STATES – AFGHANISTAN BUSINESS RELATIONSHIP AND THE
STRENGTHENING OF THE AFGHAN PRIVATE SECTOR”**

Mr. Chairman and Members of the Subcommittee,

Thank you for providing the Afghan-American Chamber of Commerce (AACC) the opportunity to submit testimony to the Committee for this most important hearing. Mr. Ajmal Ghani, Chairman of the Board AACC and the Honorable Don Ritter, President and CEO of AACC, would specifically thank and congratulate you for highlighting this issue. Our experience with the Afghan private sector dates back to 2002 when AACC went to Kabul to promote America’s philosophy and practice of a free and open market economy. AACC, in collaboration with Afghan partner institutions and individuals led the way in creating the first nationwide, independent-of-government chamber of commerce in Afghanistan; led in the creation of public forums on issues critical to a market economy like tax and tariff policy, banking and credit, price controls; promoted investment and access to capital critical to fueling private sector growth; all the while, AACC Members have been creating and building companies in Afghanistan across the spectrum of economic sectors.

AACC’s *Annual U.S.-Afghanistan Business Matchmaking Conferences* are recognized in the U.S., Afghanistan and Dubai as constituting the leading edge of U.S. business and economic policy engagement in Afghanistan. AACC was the motive force behind the recent (June 10, 2009) full-day symposium, attended by Subcommittee staff, entitled the *Role of the Private Sector in Stabilization* in Afghanistan held in collaboration with the National Defense University – Near East South Asia Center headed by General David Barno (US Army, Ret’d.), who served as former Coalition Forces Commander in Afghanistan and attended by those engaged in the Afghan private sector, DoD, State, Commerce,

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Holbrooke Team representatives and many others engaged in the stabilization issue. The main point emanating from that Joint Symposium was the acknowledgment that it will be the Afghan private sector which provides the sustainable employment, goods and services to the Afghan people that are essential to achieving stability in Afghanistan. It is not "security first" as a prerequisite to development of a market economy; rather, security cannot be achieved without concurrently providing economic opportunity to the Afghan people – and this can best be done by the private sector. The views of the Symposium participants and AACC of how that might best be achieved are summed up in the following text. The Agenda of the June 10th AACC/NDU-NESA Joint Symposium is also included as an Appendix to this testimony.

To our knowledge, this hearing marks the first opportunity by Congress to specifically identify the challenges, impediments and opportunities associated with mobilizing the critical private sector element of the economy of Afghanistan and the business-enabling environment to support stabilization. The idea of linking economic progress to security in Afghanistan has been a hallmark of AACC since our inception. As National Security Advisor, General Jim Jones was quoted in the July 1st, 2009, edition of The Washington Post, "[t]he piece of the strategy that has to work in the next year is economic development. If that is not done right, there are not enough troops in the world to succeed."

While the U.S Government now has a new strategy and is providing increased resources, specifically in the military and diplomatic pillars, to date, far too little attention has been focused on building the Afghan economy, the third pillar critical to Afghanistan's stability and the concomitant role of an indigenous private sector in this process. In our testimony, we identify several concerns about past approaches and suggest ideas that would, in our view, stimulate immediate economic activity and growth in Afghanistan directly contributing to security efforts. That would mean goods, services and sustainable employment across the length and breadth of the country. This is really what the people of Afghanistan need and want and how they will judge the success of their government and the contributions of the U.S. and other Donors.



Top-Down vs. Bottom-Up:

Government programs and projects operate in top-down fashion while private businesses operate as bottom-up phenomena. Thus, government programs to 'help' business from the top down often disturb the basic and normal operation of private companies by encumbering them with activities not necessarily relevant to their actual operation in the marketplace. For example, our experience with external training programs, offered at low or no cost to businesses, is that they take valuable time and energy away from internal and market exigencies while providing only a general level of information not of significant help to local businesses; yet, they consume substantial Donor resources that could better be deployed by the private sector entrepreneurs who best understand the needs of their own businesses.

Additionally, the current contract and grant economy in Afghanistan, the primary means by which U.S. Government and Donor money enters into the country, results in an allocation of goods and services, that is not subject to market discipline, and therefore are inefficiently distributed and overly expensive. More significantly, such an economy enhances corruption and the buying and selling of contracts at every level of society. In our experience, corruption is embedded in the contract and grant economy, which provides a very good reason to shift at least some reasonable amount of resources away from it and into direct support of the more efficient and less corruptible market economy by supporting programs that operate on a more direct business-to-business basis.

Government Programs Compete with the Market Economy:

No matter how creative and innovative they may be, Donor programs and projects often compete on many levels with the local private sector. Donors have the money, and the best people are literally 'plucked out' out of the private sector by donor-based organizations. The private sector cannot compete with relatively-speaking, gigantic "donor" salaries, which are paid regardless of whether a profit is made or not. Making a profit is a discipline that is simply not a part of the contract and grant economy. This is a glaring reality. Thus, Donor-agency leaders and employees in Afghanistan make far more money than entrepreneurs and their employees in the private sector who are actually taking risks with their money and resources and are assuming a responsibility unknown to those in the chain of contract and grant funds. Understandably, there is a need and role for traditional development assistance but the key to success in Afghanistan is in recognizing that it is the Afghan private sector which is the main driver of economic development and creator of sustainable jobs essential to security. Moreover, the U.S. government must

3



take the initiative in designing the innovative business initiatives that support the private sector's needs. To do so, it must ask the private sector what it needs and work with the private sector on a business-to-business basis.

Supporting the Private Sector: Capacity Building or Credit?

It is the business community's experience that capacity building in the private sector is far less beneficial than reasonably-priced credit or equity financing for entrepreneurs. Technical assistance can best be devoted to supporting the specific commercial activities of an individual borrower/partner rather than the more easily procured technical assistance programs that offer "business and management training" for the general business population. Creative initiatives that finance the creation and building of businesses with credit, equity capital and targeted technical assistance need to be established for Afghanistan, now.

It is our view that before security can be achieved in Afghanistan, resources will need to be channeled into starting up and building individual businesses. To do so, additional funds must be made available immediately to finance growth of the private sector. An AACC Working Group on *Access to Capital/Private Sector Investment* has been developing an Afghanistan-oriented, enterprise-type, revolving trust fund to deploy capital professionally and is targeted toward agriculture, agribusiness and priority regions like the Afghanistan-Pakistan border; however, other similar models could also be used along the length and breadth of the economy to "jump-start" the local private sector. The key is widespread professional deployment of capital and engagement of the stronger capabilities of the Afghan banking system. History demonstrates this must be done by private sector business and investment professionals to have a chance of success.

Greater Focus Required

Finally and perhaps most importantly, there needs to be far greater Donor attention to, and the related-institutional capacity to deal with, the issues of the market economy and what is needed to build it in Afghanistan. At the very least, if there are programs and projects that impact on the Afghan private sector, input must come from those people working directly in the Afghan private sector. This, unfortunately, rarely occurs whether it's the Donors or even the Afghan government. *As such, a robust United States Government institutional capacity focused on the development of the Afghan market*



economy as its primary mission is desperately needed. To do all or even part of the above-mentioned initiatives, we believe there needs to be a reasonably independent entity with market-economy dedicated capacity and resources, so as not to be a sidebar to the political mission of the State Department or the military mission of the Department of Defense. If we truly believe that legitimate employment is critical to stability, supporting the private sector at a far higher level is a necessary way to go.

US-Afghan Business Relationships: The Visa Issue

The Afghan-American Chamber of Commerce continuously monitors the economic situation in Afghanistan, and continually looks for avenues of potential market development. To promote investment opportunities, the Afghan-American Chamber of Commerce organizes an annual business match-making conference every year for the U.S. and Afghan investors, the success of which has been recognized by the US Department of State and the US Department of Commerce. This year's conference, the fifth annual, will be held on October 18-20, 2009 in Washington D.C. Major United States investors, government representatives, and prominent Afghan and Afghan-American businessmen are invited to come together to discuss business challenges, opportunities and to network.

Despite the conference's high degree of recognition, most of our Afghan businessmen from Afghanistan (and Dubai, the location of significant Diaspora wealth) have in the past, faced expensive, time-consuming and frustrating problems obtaining visas to attend the conference. The title of the Hearing today is the "U.S.-Afghanistan-Business Relationship," yet the enormity of hurdles faced by Afghan businesspeople to obtain visas allowing them to come to the U.S. to discuss and build partnerships and joint ventures act as a significant deterrent to a viable U.S.-Afghan Business Relationship and are much in need of remedy. Afghan businesspeople need to speak with players in the U.S. market for their products; they need to discuss plans with potential investors and partners, and so much more,

Recently, visas have begun to be issued out of Kabul but the process needs to be monitored carefully to ensure it is working to get a critical mass of Afghan businesspeople to the U.S. There may need to be an extra engages with the visa issuance process. Otherwise, there will not be a significant difference from the previous hard times faced by business people in Afghanistan or Dubai seeking visas to the U.S. and they numbers will continue to be a trickle. It is not only important for AACC to be able to bring businessmen and women and related government officials to our forum for promoting investment



opportunities in Afghanistan and so join up with U.S. businesspeople and investors, it is important to both nations' mutual economic policy and stabilization goals to do so.

The Afghan-American Chamber of Commerce would appreciate any assistance that Members of this Subcommittee could give to ensure that all those wishing to attend our October Business Matchmaking Conference are granted visas and beyond AACC, that the general process of judging the merit of visa applications rise to a level of refinement that truly permits, again quoting from the title of this Hearing, a meaningful "U.S.-Afghanistan Business Relationship".

Again, Mr. Chairman, we thank you for providing the Afghan-American Chamber of Commerce the opportunity to submit this testimony. Our Members are businesses and business owners who either own or operate businesses in Afghanistan. We have tremendous expertise and are passionate about Afghanistan. Perhaps now, with the focus this Subcommittee is bringing, we can help you highlight the keys to developing an Afghan economy that will truly compliment what our troops and treasure are working toward.

Enclosed: Biography for
Mr. Ajmal Ghani, Chairman of the AACC Board
Honorable Dr. Donald Ritter, President and CEO of AACC

The Washington Post

U.S. Pursues a New Way To Rebuild in Afghanistan

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By Rajiv Chandrasekaran
Washington Post Staff Writer
Friday, June 19, 2009

The idea to transform a vacant tract near the Afghan city of Mazar-e Sharif into a sprawling commercial farm, with miles of strawberry fields and thousands of cashmere goats, began with an entreaty from President George W. Bush to the billionaire chairman of Dole Foods at a 2006 Republican Party fundraiser.

Go to Afghanistan, Bush urged David H. Murdock, "to see what you can do to help."

After a tour of the country the following April, Murdock told U.S. officials he wanted to build a 25,000-acre plantation modeled after Dole's vast holdings in the Philippines. But a few months later, he concluded that transportation and security challenges made the project unsuitable for the company.

That did not dissuade the U.S. Agency for International Development. Mindful of the president's interest in the project -- and convinced that Murdock dropped out because he did not receive a thank-you call from Bush -- USAID decided to go it alone. It allocated \$40 million in reconstruction money to the venture, and it directed a contractor to hire workers and purchase equipment.

It was not until a year later, after several million dollars had been spent, that agency officials realized why Afghans had not cultivated the land themselves: The water and soil were too salty to grow crops.

"It was a total waste of resources," said Frauke de Weijer, a development specialist who worked with USAID contractors building the farm. "It was a diversion of reconstruction money from other more effective and beneficial projects."

The barren farm embodies some of the challenges confronting President Obama as he tries to fulfill a campaign promise to turn around the deteriorating situation in Afghanistan.

Members of his national security team have concluded that the country requires not just more money and personnel for reconstruction but also a fundamental overhaul of the U.S. approach to development. They want to implement broad-based initiatives aimed at improving the lives of as many Afghans as possible, shifting away from an approach employed during the Bush presidency that focused on generating discrete "success stories" and creating long-term economic sustainability through free-market reform.

Bush administration officials contend that their method was necessary to win financial support from Congress, and to build a degree of self-sufficiency that the country desperately needs, but Obama's advisers maintain it resulted in few tangible improvements for most Afghans, leading many of them to shift allegiance to the Taliban.

The consequences of the Bush approach have been most evident in U.S. efforts to help resuscitate

Afghanistan's agricultural economy, which has been severely degraded by years of war, according to internal government documents and interviews with dozens of officials involved in the country's reconstruction. Instead of emphasizing programs to help meet domestic food needs by increasing farm yields, U.S. aid officials focused much of their resources on countering the growth of opium-producing poppies through projects that encouraged other ways to make a living in rural areas. The projects often had little to do with agriculture and did not address the root causes of why farmers became part of the drug trade.

Those agriculture programs that did not involve counternarcotics were run for the past three years by a USAID official who believes the desires of private businesses should determine development strategy. He opted to steer U.S. aid toward agriculture fairs and marketing ventures instead of initiatives aimed at increasing crop production, an approach he says helped stimulate much-needed business development.

"The aid program has been driven at the operating level by people who are very ideologically private-sector, by people who have an antipathy toward government programs to assist farmers," said John W. Mellor, an agriculture economist who is an expert on farming in Afghanistan. "We are insisting that Afghanistan have a free-market economy of the sort we do not have for our own agricultural sector."

Officials at USAID, which has spent almost \$7.8 billion on Afghan reconstruction since 2001, maintain that their programs have been effective. They note that they have funded the construction of 1,600 miles of roads, the building or refurbishing of 680 schools and the training of thousands of civil servants. In the agricultural sector, the agency has pointed to a number of achievements: the transport of Afghan pomegranates to markets in Dubai, the opening of rural farm-supply stores and the restoration of pistachio orchards. "This program has had a remarkable success," said Bill Frej, the agency's director in Kabul.

But Richard C. Holbrooke, Obama's point man for Afghanistan policy, has a less sanguine view. The new administration, he said, needs "to fix what we have inherited."

Holbrooke intends to revamp the entire U.S. reconstruction effort, starting with agriculture aid and counternarcotics. He has decided to curtail campaigns to eradicate poppy crops -- which he believes have driven poor farmers to support the Taliban -- and restructure USAID's alternative employment programs, which together have cost the U.S. government almost \$3 billion since 2004.

"In my experience of 40-plus years -- I started out working for AID in Vietnam -- this was the single most wasteful, most ineffective program that I had ever seen," he said in a recent interview. "It wasn't just a waste of money. . . . This was actually a benefit to the enemy. We were recruiting Taliban with our tax dollars."

Although farm projects lack the cachet of building schools and roads, Holbrooke and other administration officials believe that assisting Afghans in improving food production must be at the top of the U.S. reconstruction agenda. More than 80 percent of working-age males in the country are small-scale farmers. Helping them grow more food will improve the quality of their lives and -- administration officials hope -- reverse a sense of hopelessness that has contributed to Taliban recruitment.

Holbrooke's aides are still drawing up a detailed strategy for how to restructure the agriculture program. But it is already clear that there will be far more money: Congress agreed yesterday to add \$100 million for agricultural reconstruction, and the administration has asked lawmakers for an additional \$235 million for fiscal 2010, a more than fourfold increase from 2008.

There will also be a fundamental realignment of power in Washington when it comes to shaping development policy. Holbrooke has wrested control of the program from USAID, making it clear that the agency will now be just one of several players involved in Afghanistan. He has reached out to Agriculture Secretary Tom Vilsack, who has agreed to send more experts from his department to Afghanistan, and is seeking to more closely coordinate with the Defense Department, which has 350 National Guard members with farm

experience serving on agricultural development teams in six provinces.

The new plan, according to officials involved in the process, will involve smaller contracts, more involvement of Afghan development organizations and more money funneled through the Afghan government. USAID's private-sector development policies will be realigned, the officials said, to include a greater focus on helping farmers increase production.

"They need the kind of soup-to-nuts agricultural support that Roosevelt gave the farmers during the Great Depression -- roads, markets, irrigation, seeds, fertilizer, educational materials," Holbrooke said. "Afghans are smart farmers. . . . They just need the right kind of help from us."

'Alternative Livelihoods'

Soon after the U.S. military overthrew the Taliban government in 2001, a debate broke out among senior Bush administration officials over the best way to rebuild a country so impoverished from decades of strife that its rates of malnutrition, illiteracy and infant mortality were among the highest in the world.

Officials at the White House and the Pentagon favored projects with a quick impact, such as schools, roads and health clinics that could be completed in a year or two and build the goodwill among the Afghan people that they believed was necessary for the American public to support a continued military deployment.

Some development specialists at USAID preferred a longer-term approach. Focus on agriculture because it is the key to economic sustainability, they said, and on "capacity building" -- training the Afghans to do things themselves. But the White House and Pentagon prevailed.

The bulk of reconstruction funding in the first few years was devoted to building schools, roads and clinics. A particularly prized project was a highway from Kabul to Kandahar that Bush requested be completed in less than a year. USAID met the goal, but to do so, it allowed its contractors to place such a thin layer of asphalt in some places that it washed away when snows melted the following spring.

It was not until mid-2003, almost 18 months after the Taliban government fell, that USAID started its first national agriculture program. It received less than 5 percent of the annual reconstruction budget.

"Investments in agriculture take time. They don't produce results overnight -- and that's what the administration wanted," said Mark Ward, a former senior USAID official who participated in high-level discussions about Afghanistan with White House officials.

By 2004, administration officials had become alarmed by reports that poppy cultivation was reaching record levels, particularly in the country's east and south. When the White House agreed to spend \$775 million the following year on counternarcotics programs, USAID saw an opportunity. It pitched a program called "alternative livelihoods" that was based, in part, on the belief that poppy cultivation would drop if young men are offered short-term employment around planting and harvest time that pays better than working in the fields.

USAID got the money: \$120 million for an alternative-livelihoods program in the south, and \$108 million for one in the east. Then it looked for help. Because the agency no longer has people on its staff who implement development and reconstruction programs -- all of them left in the 1980s and 1990s because of budget cuts -- it turned to contractors.

Roadblocks

Chemonics, a for-profit development firm based in Washington, received the contract for southern Afghanistan in late 2005. It was one of many contracts won by the company, which has become a principal

instrument of U.S. development policy in the country.

One of its first alternative-livelihoods projects was to build a road. And for that, it flew in 11 Bolivian engineers.

Andrew S. Natsios, the USAID administrator at the time, had recently viewed cobblestone roads in Bolivia's Chapare rainforest that were built under a U.S.-funded alternative-livelihoods program to discourage coca planting. He figured that such roads, which are inexpensive but require extensive manual labor to build, could be a new tool in the fight against poppies in southern Afghanistan because the construction effort would result in thousands of short-term jobs. Chemonics readily agreed.

The Bolivians trained 46 Afghans in the art of placing fist-size river stones on the ground. Then they set about constructing a road from the capital of Helmand to an archaeological site on the outskirts of the city. Once a sixth of a mile was complete, Chemonics held a celebration that featured speeches from local officials and the U.S. ambassador to Afghanistan.

Chemonics had plans to build additional cobblestone roads across southern Afghanistan, but local Afghan leaders objected. They said that they were willing to humor the Americans with the path to the ruins, but that what they really wanted were gravel and asphalt roads. They complained that the cobblestones hurt their camels' hooves.

"It wound up being a huge waste of time and money," said one person who worked on the project. "Nobody did the due diligence."

Natsios maintains that the cobblestone roads were a good idea, but he said he could not comment on the implementation because it occurred after he left the agency. A Chemonics spokeswoman said the company "can't comment on the decision-making process that took place before the work began." A senior USAID official, speaking on the condition of anonymity, said Afghan officials initially supported the project but then changed their minds because they believed they could extract kickbacks from gravel and asphalt construction.

After the cobblestone venture, Chemonics shifted to other cash-for-work projects, including cleaning irrigation canals, that were more palatable to local officials. Although it allowed USAID to claim that it had generated hundreds of thousands of days of labor, the overall impact was the development equivalent of a sugar rush: It didn't last. Poppy farmers always managed to find enough help -- largely because unemployment is so acute -- and cultivation in southern Afghanistan reached all-time highs.

In 2007, the poppies grown in Helmand province alone could have more than met the world's demand for opium. And when U.S. funding for short-term labor dried up, many participants went to fight for the Taliban, according to some Chemonics specialists who worked on the cash-for-work projects.

Several Afghan development experts advising the Obama administration believe the fundamental mistake with the U.S. alternative-livelihoods approach is that it did not concentrate on agriculture. The Chemonics contract, which USAID increased to \$166 million in 2007, included money for the construction of a business park, a women's center, an Internet cafe and a recreational facility designed to demonstrate, according to a USAID report, that Chemonics was "a good neighbor within the municipality."

What the U.S. strategy should have addressed, the experts maintain, were the basic reasons why poppy is so attractive to poor Afghan farmers.

Drug middlemen often provide farmers with a cash advance at the beginning of the planting season, and they routinely promise to buy the crop at a set price. Some merchants even offer technical assistance to help farmers increase their yields. For subsistence farmers, such aid is vital, and it leads them to plant poppy even when other crops -- including pomegranates, grapes and almonds -- can fetch higher prices.

"Our whole concept of alternative livelihoods is conceptually flawed," said Barnett R. Rubin, an Afghanistan expert at New York University and a consultant to Holbrooke. "Poppy is not a crop, it's an industry. You're not going to compete with it with day-labor projects."

But USAID declined to include agricultural credit and price supports in the alternative-livelihoods program for southern Afghanistan. Agency managers regarded price supports, which exist for some crops in the United States, as unsustainable for the Afghan government over the long term. The agency did decide to offer credit, but it did so through a separate program that would seek to establish private credit unions and small lending institutions. That program was not focused on agriculture, and security concerns have limited its operation in southern poppy-growing areas.

The few farm-related activities that USAID funded through the alternative-livelihoods program sometimes generated results counter to what the agency wanted. Several former Chemonics specialists involved with the project said that some of the farmers who accepted U.S.-sponsored wheat seed and fertilizer handouts simply sold the seeds in Pakistan, or ground them to make flour, and they used the fertilizer to nourish their poppy fields.

But the specialists contend that their superiors at Chemonics, which has received more than \$430 million worth of Afghanistan reconstruction contracts from USAID since 2003, did not complain about it to USAID project managers because of concerns it might jeopardize future work with the agency.

Michelle Millard, a Chemonics spokeswoman, called the allegation "simply not accurate." She said the firm "has worked closely with USAID to refine the design and scope of programs to ensure their effectiveness." Agency officials say they rarely find out about problems in the field, unless the contractor informs them, because agency managers seldom leave their fortified compound in Kabul to independently assess projects.

"We're all sitting in this bubble," said one agency official stationed in the Kabul headquarters. "We have no idea what's really happening out in the rest of the country."

Cotton Proposition

Soon after the cobblestone-road project, Yosuf Mir, an Afghan American who lives in Fairfax County, approached Chemonics with what he thought was a no-lose solution to wean thousands of farmers off poppy cultivation: cotton, a crop widely grown in southern Afghanistan until the Soviet invasion in 1979.

When he asked farmers why they were growing poppies instead, he said, "They told me, 'What else can I do? We don't have the seeds. We don't have the fertilizer. We don't have anyone to sell to. There's nobody to give us credit except for the drug dealers.'"

The solution seemed obvious to Mir. The Afghan government was seeking to sell the state-run cotton ginning factory in Kandahar. He would buy it.

He consummated the transaction in 2005, pledging \$1 million of his family's land in exchange for a 20-year lease. With that investment -- and with USAID's help in distributing cotton seeds -- he estimated that 35,000 farmers would resume growing cotton, and his factory could employ as many as 12,000 people. "We would," he said, "create a real alternative livelihood for the Afghan people."

When Mir approached Chemonics, leaders of the alternative-livelihoods program expressed support for his proposal. Charles Grader, a former senior manager of a USAID agriculture project run by Chemonics, said a study commissioned by the firm deemed cotton "one of the better alternate crops." But for cotton to be economically viable, he said, USAID or the Afghan government would have to provide a subsidy to the farmers, in much the same way the U.S. government aids domestic cotton producers.

In April 2006, Chemonics asked USAID for authority to help rehabilitate Mir's cotton factory. USAID rejected the request within weeks -- the notion of agriculture subsidies was anathema to free-marketers at the agency.

Mir eventually received a fuller explanation for the decision: U.S. law prevents the government from aiding foreign cotton producers because doing so could help them compete against American growers.

Several U.S. officials familiar with the matter said that USAID could have asked the White House to issue an exemption, given the national security importance of stabilizing Afghanistan, but that senior officials at the agency opposed funding a program to promote a crop in which Afghanistan did not have a comparative advantage on world markets.

"Their thinking is all about free trade -- that Afghanistan is better suited to produce pomegranates and raisins than bales of cotton," said one USAID official who disagrees with the agency's stance. "But what about the goal of keeping people from shooting at our troops?"

Late last year, Mir had to let go of the last 200 employees of the cotton factory, several of whom had worked there through the Soviet occupation and the Taliban years.

Most of them, Mir said, have since joined the Taliban.

"Even the Taliban knew the value of keeping the factory open," he added.

Sales and Marketing

In late 2006, Chemonics won another USAID contract, initially worth \$102 million, for an initiative called the Accelerating Sustainable Agriculture Program. Agriculture experts recruited by the firm to work under the contract figured it would be a chance to implement the sorts of assistance projects that Afghanistan badly needed but that USAID did not want under the alternative-livelihoods program.

They proposed setting up a commercial poultry operation that would employ women in 50 villages and produce as many as 45 million eggs a year, reducing the country's reliance on imports from Pakistan and Iran. And they urged extending a project that had been set up under an earlier USAID contract to establish and restore vineyards.

"It would have produced real change in the lives of hundreds of thousands of Afghans," said Gary Kuhn, the executive director of Roots of Peace, a nonprofit organization that would have done the vineyard work for Chemonics.

But Loren Stoddard, director of USAID's Afghan agriculture and alternative-livelihoods programs, believed the contract should concentrate on promoting "buyer-led development." That meant sales and marketing activities, not field-level work to help farmers increase production.

The grapevine project was killed. So, too, was the egg venture.

Stoddard had worked as a produce salesman before joining USAID in 2002. Before arriving in Kabul in 2006, he spent four years with the agency in Guatemala, where he earned plaudits from his superiors for helping to facilitate business deals between local farmers and Wal-Mart.

He wanted to do more of the same in Afghanistan. The key to resuscitating the economy, in his view, is for farmers to specialize not in wheat, which is a staple of the local diet, but in what the country grows best -- and what buyers in other nations want to import: pomegranates, almonds, pistachios, raisins and fruits such as apricots that can be dried or turned into juice. He is fond of noting that Afghanistan was one of the world's

largest exporters of dried fruits and nuts before the Soviet invasion. But the first step in making that happen, he believes, is to line up purchasers, not focus on farmers.

"Rich farmers sell first and then grow," Stoddard said in an interview. "Poor farmers grow first and then hope somebody will buy it."

To implement his vision, Stoddard ordered Chemonics to use the contract money to hold a series of agriculture fairs that would give Afghan farmers a chance to display their wares to foreign buyers, to organize promotional shipments of pomegranates to supermarkets in the Persian Gulf region, and to establish "agribusiness brokerage centers" to facilitate business deals.

"In 2006, nobody had heard of an Afghan pomegranate," he said. "We've put the light on the fact that there's a lot of great stuff here to sell."

The 25,000-acre farm Murdock envisioned at then-President Bush's behest was going to be Stoddard's flagship project. He was convinced it would "help Afghans realize there was a bright future ahead of them" by demonstrating modern agricultural techniques and generating an appetite around the world for Afghan-grown products.

Stoddard said Murdock wanted the farm built on a vacant parcel because he feared tenant disputes. After Dole exited, USAID decided to stick with the empty-land strategy, despite concerns from some at Chemonics that the site might not be suitable for commercial agriculture.

USAID had planned to rely on underground aquifers to irrigate the farm. But every well that was drilled brought up water that was too salty.

The agency is using the remaining money allotted for the project to help develop private agricultural projects in the province.

Even if there had been enough water to run the farm, several agriculture specialists familiar with the venture contend it would have been out of place in a country where most people grow crops on small plots of land.

"It was one man's pipe dream," said another specialist who worked on the project for Chemonics. "It made no sense."

Until recently, Stoddard had relatively free rein to design and implement agriculture projects as he wished, according to several U.S. officials. That was because "nobody -- nobody at the White House, nobody at USAID headquarters, nobody at [the] State [Department] -- really understood agriculture in Afghanistan. And USDA was almost never at the table," said Ward, the former senior USAID official. "Loren had a vision for what would work. We may not agree with it, but at least he had a plan. Nobody else had one."

At USAID, which once had dozens of agronomists and agriculture economists on staff, only a handful of people with specialized training in agriculture development remain. Although the agency does not provide an exact count, most of its scientific and technical experts were sent packing in the 1980s and 1990s as budgets were cut and the workforce shrank.

"This is what happens when you eviscerate a federal agency," Ward said. "There's a consequence. You may not see it right away. In this case, we're seeing it a generation later, when we need AID to help us win a war -- and it can't."

Left Hanging

Late last year, when Mohammad Asif Rahimi, Afghanistan's newly appointed agriculture minister, visited his

office for the first time, he was shocked by what he found -- or, rather, what he didn't. There was no phone. No Internet connection. No secretary.

"It looked like the Taliban left a week ago," he said.

To Rahimi, the reason was obvious: USAID had focused its money and attention on its own programs instead of helping Afghans assume responsibility for their own affairs. Agency officials said they did not provide more assistance to the ministry because they regarded Rahimi's predecessor as an ineffective leader.

As Rahimi learned more about the U.S. agriculture strategy, he said he became increasingly angry.

"This 'leave it to the hands of the private-sector' approach -- it's absolutely unrealistic," he said. "The agriculture sector needs a lot of support from the government."

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The Washington Post

Key in Afghanistan: Economy, Not Military

By Bob Woodward
Washington Post Staff Writer
Wednesday, July 1, 2009

CAMP LEATHERNECK, Afghanistan -- National security adviser James L. Jones told U.S. military commanders here last week that the Obama administration wants to hold troop levels here flat for now, and focus instead on carrying out the previously approved strategy of increased economic development, improved governance and participation by the Afghan military and civilians in the conflict.

The message seems designed to cap expectations that more troops might be coming, though the administration has not ruled out additional deployments in the future. Jones was carrying out directions from President Obama, who said recently, "My strong view is that we are not going to succeed simply by piling on more and more troops."

"This will not be won by the military alone," Jones said in an interview during his trip. "We tried that for six years." He also said: "The piece of the strategy that has to work in the next year is economic development. If that is not done right, there are not enough troops in the world to succeed."

Jones delivered his message after a 30-minute briefing by Marine Brig. Gen. Lawrence D. Nicholson, who commands 9,000 Marines here, nearly half the new deployments Obama has sent to Afghanistan.

The day before in Kabul, Jones delivered the same message to Gen. Stanley A. McChrystal, the new overall commander in Afghanistan. McChrystal has undertaken a 60-day review designed to address all the issues in the war. In addition, Jones has told Secretary of Defense Robert M. Gates and Adm. Michael Mullen, the chairman of the Joint Chiefs of Staff, that they should focus on implementing the current strategy, completing the review and getting more Afghan forces involved in the fight before requesting additional U.S. troops for Afghanistan.

The question of the force level for Afghanistan, however, is not settled and will probably be hotly debated over the next year. One senior military officer said privately that the United States would have to deploy a force of more than 100,000 to execute the counterinsurgency strategy of holding areas and towns after clearing out the Taliban insurgents. That is at least 32,000 more than the 68,000 currently authorized.

Nicholson and his senior staff, 20 Marine colonels and lieutenant colonels, sat around a table made of unfinished plywood the size of at least three ping-pong tables in a command headquarters that stands where there had been nothing but desert six months ago. The headquarters is located in Helmand province in southern Afghanistan, 370 miles from the capital, Kabul, in a region known as the Desert of Death because of its scorching heat and choking fine, dustlike sand. The province is facing a rising and lethal Taliban insurgency.

During the briefing, Nicholson had told Jones that he was "a little light," more than hinting that he could use

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more forces, probably thousands more. "We don't have enough force to go everywhere," Nicholson said.

But Jones recalled how Obama had initially decided to deploy additional forces this year. "At a table much like this," Jones said, referring to the polished wood table in the White House Situation Room, "the president's principals met and agreed to recommend 17,000 more troops for Afghanistan." The principals -- Secretary of State Hillary Rodham Clinton; Gates; Mullen; and the director of national intelligence, Dennis C. Blair -- made this recommendation in February during the first full month of the Obama administration. The president approved the deployments, which included Nicholson's Marines.

Soon after that, Jones said, the principals told the president, "oops," we need an additional 4,000 to help train the Afghan army.

"They then said, 'If you do all that, we think we can turn this around,'" Jones said, reminding the Marines here that the president had quickly approved and publicly announced the additional 4,000.

Now suppose you're the president, Jones told them, and the requests come into the White House for yet more force. How do you think Obama might look at this? Jones asked, casting his eyes around the colonels. How do you think he might feel?

Jones let the question hang in the air-conditioned, fluorescent-lighted room. Nicholson and the colonels said nothing.

Well, Jones went on, after all those additional troops, 17,000 plus 4,000 more, if there were new requests for force now, the president would quite likely have "a Whiskey Tango Foxtrot moment." Everyone in the room caught the phonetic reference to WTF -- which in the military and elsewhere means "What the [expletive]?"

Nicholson and his colonels -- all or nearly all veterans of Iraq -- seemed to blanch at the unambiguous message that this might be all the troops they were going to get.

Jones, speaking with great emphasis to this group of Iraq veterans, said Afghanistan is not Iraq. "We are not going to build that empire again," he said flatly.

A Question Not Settled

Obama sent Jones last week to Afghanistan, Pakistan and India to make an assessment and explain the president's thinking.

As a presidential candidate and as president, Obama stressed that the Afghan war was neglected in the Bush administration. In announcing the first additional 17,000 troops on Feb. 17, Obama said that "the Taliban is resurgent in Afghanistan" and that al-Qaeda "threatens America from its safe haven" in neighboring Pakistan.

"We don't need more U.S. forces," Nicholson finally told Jones. "We need more Afghan forces." It is a complaint Jones heard repeatedly. Jones and other officials said Afghanistan, and particularly its president, Hamid Karzai, have not mobilized sufficiently for their own war. Karzai has said Afghanistan is making a major effort in the war and is increasing its own forces as fast as possible.

In an interview, Nicholson said that in the six months he has been building Camp Leatherneck and brought 9,000 Marines to the base, not a single additional member of the Afghanistan National Army (ANA) has been assigned to assist him. He said he needed "Afghanistan security forces -- all flavors," including soldiers, police, border patrol and other specialists.

The evening before the Jones meeting, a Marine was killed during a patrol in Now Zad, a town in Helmand where people had fled the fighting.

"If we had several ANA in Now Zad, we might not have lost that Marine," said one civilian official, noting that the Afghan army could supply the "eyes and ears" that were badly needed to sound warnings and scout on patrols. One senior U.S. diplomat in Afghanistan estimated that the military needs one member of the Afghan security forces for every 10 U.S. troops to operate safely and stabilize the area. That would mean Nicholson should have approximately 900 Afghans, and he effectively has none.

At the briefing for Jones, Nicholson pointed to the mission statement, which said that "killing the enemy is secondary." His campaign plan states, "Protect the populace by, with and through the ANSF," the Afghanistan National Security Forces, which makes the absence of the additional Afghans particularly galling to Nicholson.

Though the United States supplies most of the funding for the Afghan army, the force is controlled by the Defense Ministry. Jones said he would press Karzai and others to deploy more of the Afghan soldiers to work here in Helmand.

'The Razor's Edge'

Jones said repeatedly on this trip that the new strategy has three legs, all of which he said had to be dramatically improved: security; economic development and reconstruction; and governance by the Afghans under the rule of law.

"The president realizes it's on the razor's edge," Jones said, suggesting not only a difficult, dangerous time but also a situation that could cut either way. "And he's worried that others don't."

The National Security Council is developing a series of measurements to assess the effectiveness of the strategy and the capability of the Afghan government and Afghan security forces. This is expected to be presented to Congress soon.

Jones made it clear in his visit to Afghanistan that it is a new era and that Obama will not automatically give the military commanders whatever force levels they request -- the frequent practice of President George W. Bush in the Iraq war.

"This is a decisive moment," Jones told U.S. military leaders, diplomats and the presidents of Afghanistan and Pakistan, "a strategic moment, and we better get it right."

In early 2007, when Gen. David H. Petraeus took command in Iraq, he declared that the situation, nearly four years into the war, was "hard" but "not hopeless." Jones and his staff use similar words to describe Afghanistan today.

The U.S. military and the 32,000 other NATO troops are engaged in a robust effort to improve security in Afghanistan, but insurgent attacks have escalated, reaching an all-time high of more than 400 attacks during one week in May.

Though that does not rival the violence in Iraq, which peaked at 1,600 attacks in one week during the summer of 2007, it represents a trend that has alarmed U.S. military leaders.

'The Golden 500'

It is a 25-minute helicopter ride from Camp Leatherneck to Lashkar Gah, the capital of Helmand, where Jones met with the leaders of a provincial reconstruction team, a unit of about 160 British, U.S., Afghan and other civilians and military officers working to rebuild the economy, improve security and increase effective government.

In a meeting, the reconstruction team leaders told Jones that there had been 58 makeshift-bomb attacks in the past week in the province. They stressed that the biggest problem was "Afghan capacity" because the government had not provided sufficient Afghan military, police and civilians.

The British, who lead the team, said the key to progress in Helmand, the largest Afghan province with 1.2 million people, has been provincial Gov. Gulab Mangal. They said that in the past 15 months, he had moved on nearly all fronts to modernize, improve governance and launch a war on corruption.

The British have identified what they call "the golden 500" -- government and other officials beginning with Mangal whom they want to stay in their positions in Helmand so progress can continue.

U.S. and British officials believe that Karzai, who is running for reelection in August, plans to replace Mangal. To ensure his reelection, one official said, Karzai is making deals with a number of Afghan politicians.

Jones and the British voiced their distress at the possibility that Mangal would be ousted, and Jones promised to intervene personally with Karzai. As a first step, Jones called in about a dozen Afghan reporters and sat down on a couch next to Mangal for a news conference at team headquarters. Mangal, 52, is a soft-spoken leader with black hair and a neatly trimmed beard.

First, Jones publicly embraced Mangal's leadership and said he was there "on behalf of the president, who is committed to a new strategy. I know of no place in Afghanistan that has more potential."

He said "the cornerstone is the Afghan people, the Afghan military and the Afghan police," adding, "We want to make sure Afghans control their own destiny."

Jones noted that he had been coming to Afghanistan since 2003. He was NATO commander when the alliance took over the Afghanistan war. "I know what to do," Jones said glancing at Mangal.

In a brief interview, Mangal said of Karzai, "He sent me as a soldier to Helmand province." Mangal noted that he had previously been a governor in two other provinces. Did he hope to continue? Mangal nodded yes.

After retiring as NATO commander in 2007, Jones became co-chairman of the Atlantic Council, a Washington think tank. In 2008, the council issued a report that began, "Make no mistake, the international community is not winning in Afghanistan."

Flying back from his three-country trip Friday night, Jones cited the report and said most of its bleak conclusions still apply -- insufficient reconstruction, weak economic development, the continuing "epidemic in opium production" and "disorganized, uncoordinated and at present insufficient" international efforts.

"We are doing the same things well and the same things poorly," he said. It was not mission impossible, he said, causing him to feel "urgency but not panic."

Researcher Evelyn Duffy contributed to this report.

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A Jump Start For Iraq's Private Sector

By JOHN NAGL and DANIEL RICE

Now that we've withdrawn U.S. troops from Iraqi cities, American strategy must shift its emphasis from combat to post-conflict operations. As in post World War II Germany and Japan, economic development through employment is key to maintaining stability.

Yet current development programs in Iraq -- like the Commanders' Emergency Response Fund, which lets senior military officials spend money on "urgent humanitarian relief and reconstruction" projects -- focus largely on short-term job creation, not on sustainable economic development that reduces unemployment in the long term. A more appropriate weapon would be an enterprise fund to help Iraqis invest in long-term growth.

American counterinsurgency doctrine recommends that the majority of effort be spent on economic development and governance, not on direct combat operations. To date, however, we have not followed our own advice: The U.S. still spends more than 90% of its investment dollars in Iraq on troops, equipment, weapons and logistics.

True, as security has dramatically improved, U.S. commanders on the ground have expended more than \$4 billion in emergency response funds to provide Iraqis with jobs such as street cleaning, repair and garbage collection, and on essential services such as medical care and water treatment. But this pot of money was never intended to create long-term jobs, and commanders are restricted from investing the funds in private-sector enterprises.

Most of Iraq's businesses were formerly state-owned enterprises. But we have dealt with this problem before. After the fall of communism in 1989, the U.S. helped Eastern European and Russian state-owned enterprises transition to the demands of a free-market economy. Ten enterprise funds were created in 10 different countries for a total of \$1.3 billion. The United States Agency for International Development (USAID) made loans to private-sector fund managers who invested the funds in small to medium-sized businesses. In essence the U.S. government became a very large limited partner in a private-equity fund to create sustainable jobs. Twenty years after the fall of the Berlin Wall, Eastern Europe has a prosperous private sector in no small part because of the impact of these enterprise funds.

Private capital is already at work in Iraq, demonstrating the validity of this model both for economic development and for increasing employment. For example, Iraq currently imports over \$100 million of tomato paste from its neighbors every year, despite the fact that it has enormous agricultural potential in the irrigated farmland between the Tigris and Euphrates rivers. Until recently, Iraqi farmers had no incentive to grow tomatoes on a commercial scale because there were no tomato-paste processing plants within reasonable transportation distances. In 2008, a private-equity fund invested in the Harir Tomato Paste and Juice processing facility, which had been defunct since the invasion in 2003. With only one Western employee and 200 direct Iraqi employees, the Harir plant is now profitable and has given thousands of Iraqi farmers a market for their

produce.

This model could be replicated in factories throughout Iraq in multiple industries if an enterprise fund is approved by Congress. We suggest a \$250 million Iraq enterprise fund. While this would only account for one-third of 1% of annual U.S. spending in Iraq, it would have an important amount of financial leverage; the sum could open 10 \$25 million enterprises strategically located throughout the country. Instead of spending billions of taxpayer dollars for short-term programs, the enterprise funds could create long-term growth and employment in Iraq while giving U.S. taxpayers a return on their investment in the form of a share of profits going back to the USAID -- while appreciably diminishing support for the insurgency.

As we withdraw from Iraq's cities we must seek to replace our bases with businesses. An enterprise fund for Iraq is a good way to start the process of achieving victory through economic development.

Mr. Nagl is the president of the Center for a New American Security. Mr. Rice is a partner and co-founder of The Marshall Fund. Both are graduates of West Point who have served in Iraq.

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