

“Investment Opportunities and the Economic Future of Afghanistan” 26 October 2011, Brussels

Nine Points for Improving the Investment Climate in Afghanistan

With its position at the heart of South and Central Asia, entrepreneurial spirit, and impressive deposits of copper, iron, gold, lithium, rare earth elements, and other natural resources, Afghanistan holds significant potential for attracting the private-sector investment necessary to create diversified economic growth and jobs and broaden the government’s revenue base. Development of the natural resources sector and growth in the broader economy should reinforce each other and gradually put Afghanistan on strong economic feet. To unlock this potential, the Government of Afghanistan must act decisively in nine key areas to create an improved business climate:

1. Security

Stabilisation of the security situation is an essential pre-condition for more foreign investors to become interested and active in Afghanistan. The performance and professionalism of the Afghan National Security Forces, particularly in areas where they have taken over security responsibility, will be a key determinant of whether prospective investors gain the confidence necessary to consider investing in Afghanistan.

The Ministry of Mines has presented a proposal for the government to provide forces for securing industrial installations. This proposal should be followed up and implemented as quickly as possible.

2. Transparency

Transparent, competitive, and non-discriminatory tendering and bidding processes are a crucial requirement for attracting and building trust with international investors. Currently, Afghanistan ranks near the very bottom of the Transparency International’s Corruption Perception Index. To become more attractive for international investors, Afghanistan must significantly step up enforcement of its laws against corruption.

Afghanistan's candidate status under the Extractive Industries Transparency Initiative (EITI) is a welcome sign of its commitment to transparency; it should seek to achieve "compliant country" status as soon as possible.

3. Rule of Law

International investors must have the confidence that their investments will be protected by an independent legal system based on the rule of law and safe from arbitrary government action. The capacity of the justice system to apply the law consistently and fairly, handle claims and appeals efficiently, and enforce its decisions must be strengthened. Mediation and arbitration tribunals for dispute resolution should be further developed and their authority strengthened. Capacity building for institutions is crucial.

4. Legal and Regulatory Framework

Laws and regulations governing private-sector activity should be clear, transparent, and streamlined to reduce bureaucracy and discretionary decision-making to a minimum.

The revised Minerals Law represents a further strengthening of the legislative framework, aligned with international good practices. The proposed amendments (already submitted to the Ministry of Justice) need to be adopted to correct deficits in the law. For example, on security of tenure, prospecting, exploration, and extraction should be bid for at the same time, in a single process, as the lack of an automatic transition from costly exploration to extraction is unattractive for the industry.

The mining regulations should be further strengthened, streamlined, and aligned with legal procedures. Furthermore, protection from expropriation must be reinforced to increase investor confidence across the life of the operation.

5. Fiscal Regime

Taxes and royalties need to be transparent, predictable, stable over the long term, and stipulated by appropriate laws and regulations. While the government is understandably interested in increasing its revenue, a single-minded focus on maximizing revenue in the short term is more likely to drive off prospective investors and reduce the potential for stimulating growth in related sectors. Afghanistan's tax rates are internationally competitive, but current royalty levels are far higher than in other countries (in some cases four to five times higher), making many potential projects unattractive.

6. Infrastructure

While considerable progress has been made in the development and modernization of Afghanistan's infrastructure, significant gaps remain in the areas of transport and logistics, energy production and distribution, and water supply. Development should implement the resource corridors approach, combining key infrastructure elements such as road, rail, and energy, which are especially important for the development of the mining sector. Establishment of the relevant regulatory authorities and development of their capacity, for example a national railway authority, should be one of the priorities. Policy is also needed on public-private partnerships, specific to the development of the extractive industry.

7. Land Use

Although the Government of Afghanistan has already done much to strengthen the practices of land acquisition, resettlement, and compensation, the system for the issuing and the management of land titles remains cumbersome and in need of modernisation. The government should facilitate access to land by clarifying property rights, simplifying procedures for the transfer of titles, and allowing longer-term leases.

8. Labour

The development of a skilled indigenous labour force is the basis for economic diversification and can make Afghanistan a more attractive destination for international investors and increase the potential employment benefits of such investment. Afghanistan should establish a coherent policy to guide professional and vocational education, linked to the overall higher education strategy. The government, together with the international community, should strengthen vocational and professional education to meet growing current needs, while making parallel investments in the basic and higher education systems which will yield long-term results.

9. Financial Sector

Economic development cannot take place without a healthy financial sector. Development of the sector should focus on increasing access to credit and financial services and strengthening oversight to increase confidence in the banks.