



**Islamic Republic of Afghanistan**

**Afghanistan National Development Strategy  
(ANDS)**

**A Policy for  
Private Sector Growth and Development**

**June 4, 2007**



## 1. Objectives and Expected Results

*The Government's primary goal in encouraging the accelerated growth and development of the private sector is to substantially increase employment and to raise incomes, especially of the poor.*

The *private sector* in a market economy encompasses all economic activity where physical and financial capital is privately owned. An essential aspect of a private sector-led economy is that the key decisions associated with productive activities are made by private individuals, not the government, including, *inter alia*, what goods and services to produce, the method of production, the amount of investment, and the price for which the good or service will be sold.

Private sector growth and development is an essential part of the Government's strategy embodied in the Afghanistan National Development Strategy (ANDS) and the Afghanistan Compact. Specific benchmarks towards the establishment of an enabling environment for the private sector are given high priority in the Compact, including for example:

- Reform of commercial laws, regulations and procedures;
- Divesting state owned enterprises and land title reform;
- Strengthening financial regulations for banks and non-banks;
- Restructuring state owned banks;
- Increased regional economic cooperation, including measures to reduce transactions costs associated with cross-border trade;
- Increasing access to electric power; and
- Reducing impediments to the movement of skilled labor within the region.

The private sector development takes a central role in the ANDS. One of the major strategic objectives of the ANDS is to decrease country's dependence on donor assistance and to gradually transform the Afghan economy from donor-driven to a private sector-led economy based on the principles of free-market economy.

Private sector development will be one of the most important policy instruments for achieving vital ANDS benchmarks such as job creation and poverty reduction. It will lead to better livelihood for all Afghans and contribute to decrease of poppy cultivation. Moreover, private sector growth will strengthen Afghan competitiveness and exports; it will enhance security and contribute to macroeconomic stability. For a democratic, stable and prosperous Afghanistan a viable and self-sufficient private sector is required to create sustainable jobs and incomes.

This policy builds upon these commitments already undertaken by the Government and supported by the international community. It also reflects the close interrelationship with the other main pillars of the ANDS and the Compact: security and governance.

This Policy Paper reflects current draft of the ANDS Private Sector Development Strategy, which is the result of extensive consultations through a participatory process with the private sector, trade unions, donors, civil society and Government. These consultations were held both nationally and sub-nationally over the last year and were organized by the ANDS, Ministry of Commerce and Industry and Afghanistan Investment Support Agency (AISA). The Policy Paper represents a major commitment by the Government to accelerate and expand the process of private sector development in order to bring more quickly the benefits of economic growth and development to all Afghans throughout the country. The Government also recognizes that substantially improved economic performance is also integral to improving security and strengthening governance.

With this policy, the Government aims to substantially accelerate and sustain high private sector growth rates over the next ten years. The principal role of the Government is to ensure that there is a supportive economic environment in which a wide array of competitive productive activities can grow and develop. However, to generate the rapid growth in productive employment needed, the Government will identify a number of areas where Afghanistan is deemed to have a comparative advantage and which maybe attractive for profitable private sector investments. Examples of these sub-sectors include electric power supply, commercial agriculture (including medium and large scale farming), transportation infrastructure, mining and natural resource development and construction. These are sectors where there is currently very high demand, financial resources are available and there is ample scope for the private sector to play a leading role.

The Government will actively and substantially support private sector commercial investment with particular focus on the leading sub-sectors. This support will include, for example, considerably more focused investment promotion activities, more effective incentives, increased trade promotion activities and the expansion of opportunities for public-private partnerships. Potential investors will be provided with better information and data on business opportunities. Access to essential factors of production, such as land, skilled labor and financial resources will be substantially improved.

The Government recognizes that the economic infrastructure, including particularly the legal and regulatory framework needed to provide domestic investors with adequate access to investment finance through the banking sector will take time to fully develop. and implement. To immediately address the need for additional financial resources for investors, especially for small and medium scale businesses, the Government will explore the possibilities of establishing a new interim *Private Investment Fund* and seek the support of donors and the international financial institutions..

The Government is committed to substantially increasing opportunities for trade and investment with neighboring countries and with the region as a whole. Steps will be taken in the coming months to strengthen existing regional trade agreements and to fully implement the agreements embodied in the Kabul and Delhi Declarations agreed at the high level regional conferences. However, the Government also recognizes that some neighboring countries maintain highly protected markets that distort prices and impede Afghan export. In some cases these economic distortions have substantial negative impacts on domestic markets adversely affecting the ability of the Afghan private sector to compete effectively. The Government is committed to implementing measures to offset these negative impacts on Afghan businesses and consumers. For example, through the introduction of minimum product standards consistent with international standard

practices the Government will limit the import of goods that could threaten the health and safety of consumers. The Government, with the support of the international community is also investing heavily in strengthening customs and border management facilities to more efficiently manage the movement of goods into and out of the country.

The Government expects that this policy will yield the following key measurable results:

- Increased private investment leading to more rapid and sustainable job creation, poverty reduction, improved livelihood, increased incomes, as well as to greater economic opportunities for women;
- The establishment of effective and accountable public and private institutions necessary for the efficient functioning of competitive markets;
- The establishment of an enabling economic environment that will encourage increased investment in socially and environmentally responsible enterprises;
- Expansion and diversification of exports through increased access to regional and international markets;
- Development of a strong private sector to serve as the engine of growth of the Afghan economy.

## 2. Strategy for Accelerating Private Sector Growth and Development

Economic growth and development – of any farm, firm, industry or the economy as a whole depends on two essential factors: increased investment and productivity growth. Each of the initiatives included in this policy aims to enhance one or both of these factors.

The ability of private sector activities to grow and be successful depends upon the ability of business people to efficiently access and make productive use of the main factors of production – land, labor and capital – and their ability to sell the goods and services that they produce in Afghan and international markets. The public institutions that regulate and support competitive markets must also function efficiently. All of these elements must be available for effective private sector development. If any are lacking, the Government's objectives cannot be achieved. For this reason, this policy takes a comprehensive approach that addresses each of these areas.

### **(i) Accessing Commercial Land**

One of the greatest impediments to private investment is the acquisition of land. Difficulties in establishing clear title to private land are a major problem. The Government with the support of the international community is currently implementing land titling programs, but completion of this process, including the resolution of land disputes, will take time. In addition, the process of transferring and registering land titles is excessively cumbersome, time consuming and costly. It has been estimated that this process currently entails more than 30 steps, typically takes as much as six months and often requires legal fees that amount to as much as 10 percent of the land price. The Government is already committed to reducing the number of steps required to three or four and substantially reducing the transfer tax. These changes are yet to be implemented.

The Government is attempting to alleviate problems with investors' ability to access land required for investment through the rehabilitation of existing industrial parks and the establishment of new facilities. However, many of these industrial parks are not in commercially viable areas and there are still too few parks in appropriate areas to meet the current demand. In addition, land available in industrial parks does not confer title and entails terms that are often not commercially viable.

An additional impediment is that zoning and land use regulations are not well established and are often subject to variable interpretation. Related to this are the difficulties associated with obtaining building permits. If businesses are to invest in the construction of commercial buildings, they must have some assurance that they will be able to effectively utilize these investments.

### **Immediate Steps:**

- The Government will fully implement measures to substantially simplify the transfer of land and the registration of titles and reduce transfer taxes.
- The Government will introduce legislation that will make it possible for domestic and foreign private investors to lease government-owned land for up to ninety years for investment in agriculture and industry.
- The Government will establish an independent authority to accelerate the development of industrial parks that will facilitate private sector development and management of these facilities. Government-owned industrial parks will adopt market-based pricing and leasing terms that are more flexible and consistent with commercial needs.
- The Government will institute policies to reform and make explicit land use and zoning regulations and ensure that these are applied consistently.

### **Medium Term Initiatives:**

- The Government will seek substantially increased donor assistance to accelerate and expand land titling programs in order to complete this process more quickly.
- The Government will establish clear, simple measures required for obtaining building permits.

### **(ii) Facilitating the Employment of Labor**

Existing labor regulations make it relatively easy to hire workers. Employers are not required to incur social security payments or payroll taxes when a new worker is hired. Workers may also be terminated with one month notice. Despite the lack of regulatory impediments to hiring workers, a major constraint facing the private sector is the lack of skilled labor. In particular there are major shortages of workers with basic technical skills. There is also a lack of potential employees with training in basic office and managerial skills.

### **Immediate Steps:**

- The Government with donor support for capacity development will substantially expand publicly and privately provided vocational training and skills development programs. Programs to support management training will also be expanded. The *National Skills Development Program* is currently successfully providing market linked vocational education and training in 12 provinces offering training in over 40 trades, the Government will work with the international community to expand the program to 23 provinces by the end of 1386, and to all provinces by the end of 1387.
- The Government, in cooperation with the international community and the private sector, will immediately implement a review of technical and academic training programs to ensure they are meeting the needs of the private sector.
- The Government will seek assistance to support businesses to take on graduates through a pilot formal graduate training scheme.
- The Government will introduce incentives for private businesses to train their workers.

### **(iii) Access to Capital and Finance**

The financial sector has been among the fastest developing areas of the economy. There are now 17 banks operating, all but three of them privately owned. Despite this rapid growth, there are major impediments that limit the access of the private sector to credit, especially by small and medium scale enterprises. There is not yet adequate credit information and the legal rights of lenders and borrowers are not sufficiently established. The Government will strengthen the legal framework in this area, for example, through the introduction of secured transactions and mortgage laws, and create property registers to support the use of assets as collateral for loans. In addition, further steps will be taken to avoid scarce capital resources being left idle in failed or under-financed enterprises, such as the enactment of effective bankruptcy and leasing laws.

As a result of existing institutional shortcomings, nearly all investment is undertaken with internal (or personal) funds. The aggregate amount of finance currently available for business is insufficient to sustain the growth and development of the private sector. To meet the immediate need for investment finance, the Government will explore the possibility of establishing an interim *Private Investment Fund* to make available at commercial terms additional financial resources, especially for small and medium scale businesses. The Government will seek the support of donors and the international financial institutions in establishing and operating this Fund.

### **Immediate Steps:**

- The Government will explore the establishing a *Private Investment Fund*.
- The Government will introduce laws to enable secured transactions and mortgages for fixed and movable assets, including the establishment of appropriate property registers.

- The Government will introduce bankruptcy and leasing laws.
- The Government will support the expansion of microfinance and SME finance programs with donor assistance.
- The Government will work with donors to improve education and training of borrowers and lenders.

#### Medium Term Initiatives:

- The Government will support the establishment of a public credit bureau to strengthen the ability of banks to extend credit to the private sector.
- The Government will establish the necessary legal and regulatory framework to enable the efficient mobilization of idle and under-utilized capital for new investment opportunities.

#### **(iv) Strengthening Domestic Markets**

Most small and medium scale businesses aim to sell their products in local markets but face numerous obstacles in doing so. These impediments range from the high costs associated with transporting goods (including poor roads and the lack of insurance) to an absence of appropriate and effective product quality and safety standards. One difficulty facing Afghan SMEs is that there is insufficient information concerning the market opportunities available, both for potential buyers and sellers. Currently the major donor funded projects import many of the goods and services that they need when these products could be sourced locally.

#### Immediate Steps:

- The Government will introduce the law establishing the legal basis for the *Afghanistan National Standards Authority* (ANSA) and encourage the rapid development of this body.
- The Government will seek to increase opportunities for local procurement of goods and services by the public sector and internationally funded projects including military procurments.

#### Medium Term Initiatives:

- The Government will encourage the establishment of trade and commercial transportation insurance providers.
- The Government will accelerate investment in the road system to reduce internal transportation costs. Particular emphasis will be given to rural roads to enable more extensive development of commercial agriculture.
- The Government will support the establishment of facilities to provide technical engineering and scientific information on building standards, construction methods and the testing of construction materials.

## **(v) Greater Access to Regional and International Markets**

Afghanistan offers a relatively small market with which to attract investors. Future private sector growth will depend crucially on the ability to access much larger international markets, especially within this region. However, the ability to export competitively depends upon the ability to import goods cost efficiently. Most businesses in Afghanistan rely at least to some extent upon imported inputs and unless they can access these goods cost effectively, they will be unable to compete with imported goods or in export markets.

The Government is implementing reforms to modernize customs procedures. Efforts are also underway to ease the costs associated with the transport of goods. Nevertheless, the processes required for importing and exporting goods remain too costly and time consuming.

### **Immediate Steps:**

- The Government in consultation with the private sector will develop and present a comprehensive policy supporting the growth of regional and international trade.
- The Government with the support of the international community will expand resources available for trade capacity development for the private sector, providing assistance in identifying and for competing more effectively in regional and global export markets.
- The Government will more actively pursue increased preferential trade access for Afghan businesses through the strengthening of existing regional trade agreements.
- The Government will ensure that customs procedures are consistently applied and that set time-bound targets for reducing the time and transactions costs associated with the import and export of goods are in line with international best practice.

### **Medium Term Initiatives:**

- The Government will accelerate its efforts to complete the accession process for WTO membership and to deepen and expand the scope of regional trade agreements.

## **(vi) An Enabling Legal and Regulatory Environment**

An effective and predictable commercial legal framework is essential if sustained high levels of investment are to be attracted. As part of the *Afghanistan Compact* benchmark concerned with private sector development and trade, four key laws have already been passed and a number of additional commercial laws are being reviewed and will be ready for implementation this year. The laws that have been passed will make it easier to establish businesses and to resolve commercial disputes through arbitration or mediation.

To meet this need, the Government is taking steps to introduce new commercial laws that will better meet international standards. The Government is committed to ensuring that

these laws will be (i) clearly specified and transparent; (ii) streamlined, involving the minimum necessary steps, bureaucratic processes and institutions; (iii) less discretionary decision-making; and (iv) more predictably, consistently, competently, and impartially applied.

For new commercial laws to have an impact, appropriate supporting regulations must be put in place and the judicial system must be strengthened and operate more reliably. Regulations must be designed to meet the requirements of the law, but also to impose the minimum compliance costs on the private sector. For example, currently regulations require that businesses must register with a number of different ministries and agencies which takes time and adds to their costs. These requirements can be streamlined to make it simpler and less expensive for businesses to comply while still meeting legal requirements.

#### Immediate Steps:

- The Government will present to Parliament this year the pending key commercial laws, including laws relating to contracts, agency, intellectual property, standards, secured transactions, mortgages, negotiable instruments and commercial leasing of government land.
- The Government will establish a single, low cost registration process for establishing private entities (i.e., business partnerships and corporations; civil society organizations; and NGOs).
- The Government will make more readily available information to the private sector on regulations being proposed and in force and will solicit comments from the private sector and the international community on draft legislation and regulations before putting them in final form for approval. The Government commits to publishing in the press and posting all new regulations on the internet before they come into force.
- The Government will introduce a regulatory mechanism that will encourage private sector investment in power generation, natural resource development and transportation infrastructure.
- The Government will establish the Financial Tribunal to address disputes in the banking and telecommunications sectors.
- The Government will ensure that the steps required to enable domestic mediation of commercial disputes are made available under the recently passed Mediation Law are taken.

#### Medium Term Initiatives:

- The Government in consultation with the private sector will develop and introduce laws governing the ownership and sale of land, energy, bankruptcy and the regulation of insurance providers.
- The Government, with the support of the international community, will make resources available to considerably strengthen the commercial courts in order to

ensure transparent resolution of business disputes and to enhance contract enforcement.

- In consultation with the private sector, The Government will also establish a dedicated tribunal which will serve as a mechanism to quickly and definitively resolve disputes that arise between the private and public sectors with respect to the implementation of laws and regulations, including disputes that arise regarding public procurement of goods and services.

### 3. Private Sector Code of Conduct

It is the commitment of the Government with this policy and the initiatives being implemented as part of the *Afghanistan Compact* and ANDS to establish and maintain an enabling economic environment in which the private sector can invest and prosper, thereby creating employment opportunities and increased incomes for all Afghans. The Government expects an equivalent commitment by the private sector to a code of conduct in commercial practices.

#### **(i) Productive Use of Commercial Land**

While the Government will ensure that impediments to accessing land will be substantially reduced, it expects that land made available for commercial purposes will be quickly and fully utilized in productive activities. Land made available by the Government should not be held idle for speculative purposes.

#### **(ii) The Employment of Labor**

All Afghans should be able to compete freely for employment opportunities based on merit. If a market based economy is to succeed, the benefits of growth and development must be seen to be distributed equitably.

#### **(iii) Mobilization of Finance and Capital**

The growth and development of the Afghan economy will depend on a greater willingness to go beyond investment based on internal funding in order to expand ownership opportunities of commercial enterprises to both Afghan and foreign investors. Increased opportunities for equity participation will require maintaining higher accounting standards and protection of the rights of minority owners.

### 4. Delivering These Commitments

It is the Government's goal to quickly and effectively establish an enabling environment for the private sector in order to lay the foundation for sustained economic growth and development in the years ahead. It is the intention of the Government to implement the *Immediate Steps* included in this policy by the end of 1386; the *Intermediate Initiatives* will be implemented within two years. With the effective introduction of these measures, in conjunction with the implementation of the benchmarks included in the *Afghanistan Compact*, the country will substantially achieve this goal.

The Government recognizes that additional policy reforms and efforts to build and strengthen economic institutions will be required in the years ahead to build a strong economy. In particular, efforts to develop human capacity in both the public and private sectors will be essential to sustain economic growth sufficiently to eliminate poverty and reach our social and economic goals. To address the longer term measures that will be required, the Government, as part of the development of the full ANDS, to be completed by the end of 1386, will prepare its *Private Sector Development Strategy*. This strategy will form an important part of the full ANDS and will go through extensive national and sub-national consultations, including with the private sector.

To ensure timely implementation of the measures proposed in this Policy, the Government will put in place oversight mechanisms that will include a substantive role for the private sector. It is the Government's intention to use existing structures to implement these measures rather than create new overlapping structures.

- A *Private Sector Enabling Committee* will be formed to (i) advise the Government on policies affecting the private sector; (ii) strengthen contacts with foreign business leaders; and (iii) monitor and report on the implementation of this Policy to the President and Cabinet through the Senior Economic Advisor to the President. The Committee will be comprised of private business people and senior government officials and will be jointly chaired by government and the private sector.
- The ANDS and the Joint Coordination and Monitoring Board (JCMB) Secretariat will ensure that the initiatives included in this Policy and from private sector consultations are reflected in the final ANDS *Private Sector Development Strategy*. Primary responsibility for overseeing the implementation of these objectives will be included in the programs of the appropriate Technical Working Groups currently responsible for overseeing implementation of the *Afghanistan Compact* benchmarks. ANDS will ensure that adequate indicators are to be developed to enable efficient monitoring and follow-up. These Technical Working Groups will be strengthened where necessary to enhance efficient implementation. Technical Working Groups will report regularly on progress to the JCMB through the Consultative Group responsible for Private Sector Development and Trade (CG8).
- *The High Commission on Investment* will be strengthened through the provision of additional technical support and will be empowered to actively promote foreign and domestic investment, particularly in leading sub-sectors identified by the Government (e.g., electric power supply, commercial agriculture, transportation infrastructure, mining and natural resource development and construction).

The Government gives the highest priority to rapidly establishing an effective enabling environment for the private sector growth. To ensure that the implementation process proceeds efficiently, the Private Sector Enabling Committee and the ANDS/JCMB Secretariat will provide progress reports to JCMB, Economic Council and to the Cabinet. Quarterly reports to the JCMB will also include detailed reports on progress on the implementation of these initiatives. The Government also recognizes that this implementation process will be greatly strengthened through more active participation by the Afghan private sector. The respective government bodies will take steps to increase private sector involvement at all levels of the process.