

CHAPTER 1: THE POLICY CONTEXT

1.1 *Since the fall of the Taliban in 2001, Afghanistan has made real progress in re-establishing political institutions and pushing ahead on economic reform.* A new Constitution has been adopted, nationwide elections have been held to select both a President and a Parliament, and there are moves toward establishing more effective forms of sub-national government.

1.2 *Economic growth has been high at an average of over 10% per year.* Although data on the Afghan economy are weak, overall economic growth has been at double-digit rates. Private investment has risen sharply from an estimated US\$ 22 million in 2003 to over US\$ 400 million in 2006. Gross Domestic Product is estimated to have risen by 47% between 2004 and 2006 and government fiscal revenue increased by 85% (DFID 2007). The Government of Afghanistan (GoA) estimates that sustained real growth rate of licit GDP of 9% per year is required to provide tangible improvements to the country's population while compensating for the contraction caused by the progressive phasing out of narcotics (Islamic Republic of Afghanistan 2007a: 9). Priority investments for growth are high-value agriculture, the productive use of state assets, mining and extractive industries, and regional cooperation and transit trade in energy and goods.

1.3 *However, structural conditions for sustainable growth are largely absent.* The challenge is significant. Afghanistan remains one of the poorest countries in the world. Per capita GDP is estimated at only \$325 and social indicators are some of the worst in the world. And whilst economic growth rates are high, approximately 80-90% of economic activity is estimated to be informal (World Bank 2005a: 5), human capital is poorly developed, and the bulk of investment and development activity as well as a large portion of recurrent expenditures are still financed through international aid. Corruption is considered endemic, and Afghanistan is currently ranked 172 out of 180 countries included in Transparency International's corruption perceptions index.

1.4 *Insecurity is on the rise and represents a major impediment to development.* Growing insecurity is perhaps the biggest constraint on reconstruction and development efforts. Government officials estimate that 35% of the country is currently inaccessible due to deterioration in the security situation.¹ And whilst the security situation is at its most acute in the southern provinces, particularly Kandahar, Helmand and Uruzgan, development agencies are finding it increasingly difficult to operate in a range of provinces, including among others Balkh, Badakhshan, Wardak and Logar.

1.5 *Ominously, the links and synergies between opium poppy and insecurity are becoming increasingly apparent.* Estimates suggest that the size of the opium economy is significant at approximately 30% of licit GDP, and opium is thus Afghanistan's leading economic activity. UNODC's recent Opium Poppy Survey for Afghanistan reports that cultivation is becoming increasingly concentrated in the insecure south and east of the country whilst declining in the relatively more stable north (UNODC 2007: i). ***There should be no illusions about the prospects for quick success against opium, particularly if conflict and insecurity continue in many parts of the country.***

1.6 *Clearly, security, application of the rule of law, better governance, and political leadership, as well as sustained international support, will play a critical role in reducing opium production over time.* In this regard, there is a strong case for interdiction actions against larger and medium-sized drug traders as well as opium processing laboratories, and for removal of figures associated with the drug industry from positions in government (see, for example, Ward and Byrd 2004, and Byrd and Buddenberg, 2006). Eradication (destruction of poppy while it is growing in the fields) is a blunt instrument that must be used cautiously and judiciously, and aerial spraying – which is currently

¹ Personal communication with senior government official, 3 September 2007

being advocated in some quarters – would be counterproductive as it would further alienate the rural population, increase the gap between Afghans and their government, likely stimulate popular support for anti-government interests, and further worsen insecurity (Mansfield and Pain 2007).

1.7 *But without changing economic incentives and expanding opportunities for rural households currently dependent on the opium economy, real progress against the drug industry will continue to be elusive.* If the underlying economic incentives and (in many parts of the country) lack of other opportunities for the rural population are not addressed, any short-term gains against the opium economy will prove ephemeral. This has been demonstrated by experience in Afghanistan and elsewhere (Commission for Narcotics Drugs 2005; GTZ 2005; Mansfield and Pain 2006, 2007). Thus even though it is by no means the whole picture, the economic development side is an essential component and prerequisite for sustained success against drugs in Afghanistan. As emphasized in the Government of Afghanistan's National Drug Control Strategy (NDCS, see 2.2 below), it is only through a holistic approach that encompasses all of the components of the strategy that the country will escape from its dependence on opium.

1.8 *This report is about how to progressively reduce over time Afghanistan's dependence on opium through development initiatives and by shifting economic incentives toward sustainable legal livelihoods.* These changes will form an essential component of the broader counter-narcotics strategy, the other elements of which are not covered in detail in this report.

1.9 *More specifically, the report identifies additional investments and policy and institutional measures to support the development responses that can counterbalance the economic advantages of opium.* It is the purpose of this report to analyse ways to change the relative incentives between licit and illicit cropping and to improve rural livelihoods for the poor, under better governance and security conditions. The report puts forward concrete recommendations in this regard, and the expected impacts on growth, poverty reduction and the opium economy are assessed.

1.10 The rest of this report first provides an overview of the opium economy (Chapter 2), focusing on how different segments of the rural population interact with it. The report then analyses the scope for increasing value added, competitiveness and productivity in agriculture (Chapter 3) and for promoting enterprise development and off-farm employment (Chapter 4). The complementary role of further investments in rural infrastructure is examined in Chapter 5, and measures for strengthening governance are analysed in Chapter 6. In Chapter 7 issues that cut across all counter narcotics efforts are examined. A final chapter looks at implementation, and at issues of prioritization, synergies and phasing (Chapter 8).