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## Compounding Uncertainty in Afghanistan Economic Consequences of Delay in Signing the Bilateral Security Agreement

### Summary

- The still unsigned Bilateral Security Agreement (BSA) between Afghanistan and the United States provides the legal basis for continuing U.S. military presence in Afghanistan.
- In addition to its substantive importance, the BSA is also a confidence-building mechanism. The delay in putting it in place is compounding uncertainty and further diminishing economic confidence during Afghanistan's already challenging and uncertain transition.
- Afghans' responses include, among others, hedging behavior (legal and illegal), personal decisions on whether to come back to or stay in Afghanistan, delays in investments, incipient job losses, declining demand for goods and services and real estate prices, and farmers planting more opium poppy.
- Most of these effects would appear to be reversible if the BSA is signed soon, but the longer the uncertainty persists, the greater the risk that they become increasingly difficult, even impossible, to undo.
- The BSA delay also increases Afghanistan's vulnerability to other risks and shocks. For example, any problems during the election process, or adverse security developments, may be magnified and feed on each other, potentially leading to a downward spiral in confidence and outcomes, whereas having the BSA in place would provide a better anchor for navigating transition challenges.

“The delay in signing the BSA undermines confidence in the future international engagement with associated economic implications and negative consequences for Afghanistan's financial outlook.”

### The BSA as a Confidence-Building Measure

Afghanistan faces numerous challenges and risks during its ongoing political, security and economic transitions. These include upcoming presidential and provincial council elections in April 2014 as well as parliamentary elections in 2015; political developments after elections; departure of most international combat troops and performance of Afghan National Security Forces (ANSF); evolution of the insurgency and prospects for reconciliation; declining international financial support; actions by neighboring countries; and others. Some challenges and risks have an immutable component (e.g., Afghanistan's geographical location), whereas others are amenable to policy decisions and risk mitigation measures.

The BSA provides the legal basis for continuing U.S. military presence in Afghanistan, which in turn would enable an equivalent NATO security agreement that would allow some NATO member states also to maintain a limited troop presence. The BSA is widely seen to be extremely important for the further development of (and continuing international support for) ANSF, as well as more

generally providing a foundation for continuing international engagement and aid to the country. Those opposed to signing the BSA in the immediate future depict it as an issue of national sovereignty and try to mobilize support for their viewpoint, especially in rural areas, by emphasizing this aspect and at least implicitly drawing on anti-foreign sentiment.<sup>1</sup>

This Peace Brief focuses not on the substance of the BSA, but rather on the BSA as an anchor for domestic economic confidence and stability during Afghanistan's transition. The delay in signing the BSA undermines confidence in the future international engagement with associated economic implications and negative consequences for Afghanistan's financial outlook.

## Economic Implications of Delay

In December and January, USIP staff conducted 29 key informant interviews in Laghman, Nangarhar, Kabul and Herat provinces. While qualitative and far from comprehensive, these interviews shed light on how Afghans perceive the delay in signing the BSA and its economic implications.<sup>2</sup>

Although one respondent suggested that complete withdrawal of foreign troops (in the absence of the BSA) would facilitate peace and thereby help the Afghan economy, the bulk of the interviews highlight that continuing uncertainty over the BSA is having negative economic repercussions. These include, among others, short-termism and hedging behavior that can take a variety of forms—legal and illegal; declines in demand for goods and services; various economic decisions put on hold; falling land and real estate prices; uncertainty over jobs; caution on investments and slowdown in construction activities; foregoing education to meet short-term economic needs; and some people beginning to consider moving or staying away from Afghanistan. Most of these issues are just starting to take hold and could be reversed if the BSA is put in effect soon. However, many respondents expect the adverse economic effects to progressively worsen the longer the uncertainty over the BSA persists. A former policeman in Laghman summed up: "By not signing the BSA, President Karzai has attacked the Afghan economy, not the U.S., because if it is signed four months later it won't have any impact on the U.S., but it will have a big impact on our economy in that time."

At the extreme, hedging can involve outright theft. In Kabul, finance officers and those with access to international organizations' funds and government bank accounts have been withdrawing cash and disappearing at a greater rate than usual. Reportedly two international aid and development organizations recently lost more than \$100,000 in this way, one U.N. agency \$400,000, and the Ministry of Finance at least Afs 350,000. At the macro level, the Afs 14 billion (11 percent) shortfall in government budget revenue in 2013 as compared to the original target<sup>3</sup> has been attributed at least in part to worsening corruption. Uncertainty and short-time horizons breed these kinds of behaviors.

A variety of legal hedging also is underway. Some who rely on government and aid-dependent salaries are cutting expenditures. In Laghman, government teachers reportedly are saving a greater share of their paychecks or have stopped purchasing on credit. This is beginning to ripple through local economies in the provinces, leading to declining imports, especially of luxury goods but also of staples like rice. Interviewees said that larger scale automobile importers and small business owners alike are importing fewer goods.

Farmers are also beginning to take measures to insure themselves from future shocks. In Nangarhar, interviewees said that farmers planted more opium poppy in late 2013 than any time in the last half decade or so. As one NGO worker whose family also owns a farm stated: "Everyone keeps opium seeds in their house as insurance and it is just a matter of planting them."

The second-order effect on security was explained in this way by one interviewee: “Families in the east always used to make sure at least one of their boys went into the national army, if for no other reason than to draw a steady paycheck. Right now they are rethinking this livelihood strategy, and fewer families are sending their sons to the government.” The recent failure of the government to pay police in many provinces is not helping matters.<sup>4</sup> Some families are choosing instead to arm themselves. A small arms dealer in Jalalabad city said he is moving more Kalashnikovs and handguns than “anytime since the fall of the Taliban.” He noted that the price of AK47s and pistols increased by about \$100 just a week after the late-November national Jirga (at which President Karzai announced he would not be signing the BSA until after the presidential election).

A government engineer in Nangarhar reported that until mid-2013 the province had around 4,000 ongoing infrastructure projects, whereas today there are only about 800. For years traders and investors in Nangarhar had been waiting for the Mahipar and Naghlu dams to come online and provide reliable and cheaper electricity to the Jalalabad area. Both have been producing electricity since October but investment has not increased, with the delay in the BSA the most commonly cited reason. NGO employees in Jalalabad stated that “before this BSA controversy, we were not bidding on any projects less than \$50,000, but now we will bid on anything for \$20,000 just to keep our offices open. Some NGOs have closed their offices due to not being able to cover staff costs and are now waiting at home.”

At the other end of the spectrum from infrastructure investments, a rickshaw driver in Herat city said: “Right now no passengers want to use this old rickshaw because of how bad it sounds! I have the money to trade it in for a new one, but I am waiting to see if the U.S. decides to leave the country or not. Right now I need to save this money to support my family.” When asked what he would do if the BSA is not signed and the U.S. pulls out, he said his most likely option would be moving to neighboring Iran.

Although there does not seem to have been a large outflow of economic migrants yet, returns of long-term Afghan refugees living in places like Peshawar (in neighboring Pakistan) appear to have slowed. One interviewee in Laghman said that his brother had come from Pakistan in November but returned to his family and residence there after finding no work. A provincial judge in Nangarhar said that although he could save a considerable amount of money in weekly travel costs by relocating his family back to Afghanistan, he will continue to make the cross-border commute because he would feel vulnerable without refuge in Pakistan.

Fluctuations in real estate prices in Kabul due to BSA uncertainty have been reported,<sup>5</sup> but outside the capital land prices also have been dropping fast. A biswa (approximately 100 square meters) of undeveloped residential property in Jalalabad city reportedly dropped from a pre-Jirga price of US\$6,000 to \$3,000 a week later. Though it would seem to be a buyer’s market, both buyers and sellers appear to be in a holding pattern at the moment—the latter reluctant to sell in the event that the BSA is signed soon, the former feeling that if the zero-option becomes a reality prices will only decline further.

And some may be giving up longer-term ambitions due to the uncertainty. A Laghman University student said: “My family and I have lost hope. I belong to a very poor family and had to borrow money to study, and my plan was to repay the money and to start supporting my family. I studied in order to be employed with an international organization and earn a good salary. If the BSA is not signed, then I will have to leave the university and take whatever job I can find.”

## ABOUT THIS BRIEF

William A. Byrd, a senior expert at the U.S. Institute of Peace (USIP), has published extensively on Afghanistan's economy and other topics. Casey Garret Johnson is a Kabul-based USIP senior program officer, who has published on Afghan local politics, tribal relations and the insurgency. Sanaullah Tasal is a Kabul-based USIP program officer, who has published on issues of religion, peacebuilding and security in Afghanistan. Additional reporting was contributed by Farid Bayat, Kabul-based USIP researcher. This paper forms part of ongoing research on economic aspects of Afghanistan's transition. The views expressed in this brief do not necessarily reflect the views of the U.S. Institute of Peace, which does not take policy positions.

## Conclusions

While the BSA cannot be seen in isolation from other factors influencing the transition and affecting confidence, it is significant. The failure to sign it so far is by all indications having a damaging impact by further diminishing confidence in an already uncertain environment. This paper has focused on the problematic economic consequences, but there are also important security, political and international implications. While most of the delay's adverse economic effects would appear to be reversible if the BSA is signed soon, the longer the uncertainty persists the greater the risk that they become increasingly difficult, even impossible to undo. Moreover, the BSA delay compounds uncertainty and increases Afghanistan's vulnerability to other risks and shocks. For example, without the BSA, problems during the election process, or adverse security developments in coming months, may be magnified and feed on each other, potentially leading to a downward spiral in confidence and outcomes. Having the BSA in place would provide a better anchor for navigating the unavoidable challenges.

## Notes

1. Pro-BSA advertisements, which often feature economic arguments, have been targeted by opponents, which suggests that they do not want the BSA defined as an economic issue (see [http://www.reuters.com/article/2014/01/22/us-afghanistan-us-advertising-idUSBREA0L00T20140122?utm\\_source=Sailthru&utm\\_medium=email&utm\\_term=\\*Situation%20Report&utm\\_campaign=SITREP%20JAN%2023%202014](http://www.reuters.com/article/2014/01/22/us-afghanistan-us-advertising-idUSBREA0L00T20140122?utm_source=Sailthru&utm_medium=email&utm_term=*Situation%20Report&utm_campaign=SITREP%20JAN%2023%202014)).
2. There are also international economic and other ramifications that may be associated with the BSA delay, which are not discussed in this paper.
3. As reported by Tolo News (<http://www.tolonews.com/en/business/13470-government-revenues-miss-fiscal-year-target>).
4. Many we spoke with attributed the delay in police salaries to the BSA controversy, whereas in fact it was due to parliamentary delays in passing the annual budget.
5. See *Wall Street Journal* (<http://online.wsj.com/news/articles/SB10001424052702304355104579234161225965976>).



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