Economic Assistance in Conflict Zones

Lessons from Afghanistan

Ethan Kapstein and Kamna Kathuria

Abstract

The upcoming departure of NATO forces from Afghanistan highlights the question of whether that country will find lasting peace and prosperity without a significant foreign military presence. Has the international community been able to lay the foundations for a stable Afghanistan? Is the Afghan government now capable of formulating and implementing economic and security policies widely perceived as welfare-enhancing? Or will the country collapse into anarchy as Taliban and anti-Taliban forces struggle for power in the wake of the coming security vacuum?

This paper examines these questions through the lens of foreign-assistance policy. We argue that donors face a fundamental tension between the short-run demands of financing a war effort and the long-run demands of sustainable economic development. In short, this paper explores the question of whether or not foreign aid has helped to build state strength and legitimacy in Afghanistan, and not just bolster state capacity to fight a war.

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Center for Global Development
1800 Massachusetts Ave NW
Third Floor
Washington DC 20036
202-416-4000
www.cgdev.org

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Ethan B. Kapstein

The University of Texas at Austin

Georgetown University

Center for Global Development

ekapstein@cgdev.org

Brown University

kamna_kathuria@brown.edu

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Economic Assistance in Conflict Zones: Lessons from Afghanistan

The recent announcement that NATO troops would leave Afghanistan in 2014 brings into sharp relief the question of whether that country will be able to find lasting peace and prosperity in the absence of a significant foreign military presence. Has the international community been able to lay the foundation for a stable Afghanistan over the past decade of intensive counterinsurgency? Is the Afghan Government of now capable of formulating and implementing a set of economic and security policies that are widely perceived as welfare-enhancing? Has the state become a legitimate actor and the ultimate source of national political authority in the eyes of the Afghan people? Or will the country collapse into anarchy as Taliban and anti-Taliban forces continue to struggle for power in the wake of a coming security vacuum?

This paper examines these issues through the lens of foreign economic assistance. In particular, we ask what role international economic aid has played in Afghanistan during counterinsurgency operations and what role—if any—it can be expected to play following the departure of foreign troops. Has foreign aid helped prepare Afghanistan for a peaceful and prosperous future? Has it promoted the legitimacy of the state in the eyes of the Afghan people? Has it proved to be a "vital tool for promoting stability" as a U.S. Senate report recently proclaimed? (U.S. Senate, 2011, 1). Can aid flows somehow substitute for a foreign military presence in dampening the insurgency? Or, to the contrary, might assistance programs that are designed to promote economic activity instead embolden "rent-seeking" and predatory insurgents?

For those who are long-time students of foreign aid programs, these questions will seem eerily familiar. They were, for example, central to the preoccupations of American and Vietnamese policy-makers as the U.S. began to disengage from South Vietnam in the early 1970s (Dacy 1986). The appropriate role of foreign aid in wartime was debated by public officials and interested observers back then as it is now, while policy-makers and pundits alike raised similar kinds of issues. Should aid explicitly help to serve tactical military operations like gleaning information from the local population about insurgent whereabouts and activities? Should its primary emphasis be on budgetary support for security forces given the fiscal strains posed by wartime spending? Or should aid doggedly maintain a long-term, developmental focus, looking beyond the war toward post-conflict needs and requirements, and in so doing somehow extend the shadow of the future of the nation's economic agents? These questions have yet to be answered definitively despite the frequency with which they have been raised over the past fifty years.

This paper argues that the donor community faces a fundamental tension or dilemma between the short-run requirements of financing a war effort and the long-run demands of sustainable economic development. The search for a resolution to this dilemma is central to understanding how foreign assistance policy is shaped in conflict zones like Afghanistan. The extent to which the foreign aid community has succeeded in helping the Government of Afghanistan defeat the Taliban insurgents while preparing the country's economic future is the central issue that the paper examines, and we identify several major shortcomings and contradictions in donor policy that we believe ought to be addressed. In short, this paper explores the question of whether or not foreign aid has helped to build state *legitimacy* and *strength* in Afghanistan, and not just bolster state *capacity* to fight a war.

The paper is in four sections. Following this introduction, we briefly discuss the purposes of foreign assistance during a military conflict, drawing prominently from the case of Vietnam, which brings into sharp relief many of this paper's major themes. We then look specifically at aid flows to Afghanistan. Next, we discuss the possible evolution of foreign assistance as NATO troops depart, and what the aid community might do to prepare for the coming security gap. We conclude with some thoughts on future academic research along with lessons for the foreign assistance community as it contemplates how to operate most effectively in conflict zones.

Foreign Assistance at War

Foreign assistance has been used to advance many different objectives of donor nations since it became a major tool of foreign policy following the end of World War II (Pollard 1985; Ekbladh 2010). These objectives go by phrases that have now entered the lexicon of international economic relations, including such terms as "modernization," "economic development," "poverty reduction," "humanitarian aid," "inclusive growth," and, in the more specific case of conflict zones, "pacification" and "stabilization." Collectively they suggest the ability of foreign donors to shape in some decisive manner the fortunes of the recipient nation.

Common to all these diverse objectives a fundamental belief on the part of donor governments that recipient nations face a "budget gap," due to the lack of internal political and/or economic resources and capabilities needed to mobilize funds for needed investments in infrastructure and public goods. In the absence of foreign aid, recipient nations would face overwhelmingly difficult budgetary choices that could lead to such undesirable outcomes as high levels of inflation, widespread suffering or deprivation, political instability and, in the context of counterinsurgencies, the failure of the government to achieve victory. Less thought, it seems, has been given to the possibility that aid flows might actually prolong conflicts by providing the antagonists with external resources which, had they been denied, could have brought the warring parties together into negotiations more quickly (Gourevitch 2010; Eubank 2010).

During periods of extreme violence and military conflict, the budgetary challenges facing developing nations are, of course, greatly amplified. On the one hand, the rising costs of the conflict itself must be supported from existing government revenues; on the other, this must be done in circumstances that may well be straitened from a budgetary standpoint, as workers leave productive employment for military service, and as private investment is either crowded out by government spending or is redirected to military priorities. Furthermore, for reasons of political economy, governments may be particularly reluctant to enact such policies as tax hikes or the rationing of goods and services, since such policies would bring home the immediate costs of the war; as a consequence of the government's refusal or incapacity to confront its polity directly with ongoing war costs, inflationary pressures in the country are likely to rise.

This suggests that the most immediate objective of foreign assistance in conflict zones may be the straight-forward one of assisting the besieged government with the management of its wartime security and associated budgetary challenges, as opposed to serving predominantly as a vehicle for promoting long-term economic development, for example, through financing public goods like infrastructure and human capital creation. In fact, the short-run objective of supporting the defense-oriented budget might, ironically, undermine the developmental one in fundamental respects, as we will discuss in greater detail below. To put this somewhat differently, the relationship between the short-run fiscal demands of a conflict and the long-run requirements of sustained economic and political development could well be in tension. That this might be the case can be illustrated by an example from Vietnam among other cases; in later sections we will examine this tension in the specific case of Afghanistan.

During the Vietnam War, the weakness of the regime in Saigon—its lack of general legitimacy in the eyes of the people of South Vietnam—greatly constrained the range of economic policy options the government felt were available to it in meeting its wartime budgetary requirements (on Saigon's lack of popular legitimacy, see Lockhard 1994). In particular, the government in Saigon argued to American officials that the imposition of austerity measures and higher taxes to finance the war effort was out of the question from a political perspective, as these steps would further alienate an already restless population, fueling support for the Communist insurgency. Policy-makers in Washington and Saigon therefore came to agree that the primary role of U.S. foreign assistance must be to help the regime finance the war effort while ensuring that the South Vietnamese people continued to enjoy a rising standard of living, as measured by their ability to purchase a larger and more sophisticated basket of goods and services (Dacy 1986; Ekbladh 2010).

In many respects, the relationship between the governments of South Vietnam and the United States exemplifies the political economy theme of "the weak exploiting the strong," whereby one party's weakness in material capability is successfully used as a bargaining tool in its negotiations with its bigger partner (see Olson and Zeckhauser 1966, who built this model in the context of the NATO relationship between the United States and its smaller European allies). Simply stated, the United States came to adopt Saigon's self-assessment of its political weakness and lack of legitimacy in facing Vietnamese society, and by providing that regime with substantial budget support it basically engaged in what popular psychologists call "enabling" behavior; that is, it "enabled" the Vietnamese to avoid taking tough political and economic decisions such as the implementation of any austerity measures (which, ironically, could have strengthened the state in the eyes of its citizens; more on this below). As Dacy has put it, the Government of Vietnam (GVN) "could not reduce expenditures in a war situation, nor could it raise taxes, because that would cause political unrest. The only feasible solution was more aid…To the extent that building a record of solving one's own problems is important for self-sustained growth of a country, the approach used to fix aid levels for Vietnam was anti-developmental" (Dacy 1986, 32).

Beyond the decision by Washington and Saigon to "kick the can" of austerity down the road, there were additional economic problems associated with the foreign aid model adopted in Vietnam. Given the primacy accorded to fighting inflation while, at the same time, trying to raise the standard of living, Vietnam had to be open to imports of consumer goods from abroad (chiefly Japan); in the event, the country had little industry that could satisfy growing consumer needs and wants. These twin economic goals of low inflation and higher imports necessarily called for a strong or overvalued currency (the piaster), and indeed in 1960 the piaster was valued at $143, even though economists at the time estimated that it would have traded below $70 with a floating exchange rate (Luan and Banker 1966). In a similar vein, a recent report from the IMF suggests that the Afghani, too, is overvalued 20 percent over what it would be without foreign aid (IMF 2011).

In Vietnam, because of the overvalued piaster, imports were cheap, and local entrepreneurs were thus discouraged from making investments in industries that could compete against them; in the event, those with an entrepreneurial bent could make good money feeding off the U.S. presence. As early as 1966, Luan and Baker recognized the negative consequences, writing "Since exports have been low, the balance of trade shows a large deficit…" Indeed, the absence of productive entrepreneurial activity in conflict and post-conflict zones, due in part to the role of economic aid, is a theme that re-emerges throughout the foreign aid literature (see, for example, Eubank 2010).

This relationship is the oft-cited Dutch Disease in foreign aid literature. Rajan and Subramanian (2011), for example, found that aid inflows systematically decrease the recipient nation's competitiveness. Corden and Neary (1982) broke the short-term results of aid inflows into the resource movement effect and the spending effect. The first concludes that international aid, mainly funneled into non-tradable sectors, increases wages in these sectors and subsequently across the board. Higher wages reduce export profitability, leading to falling trade balance. Moreover, spending of these higher wages on non-traded goods hurts the real exchange rate, multiplying the negative effect on export sector profitability. Rajan and Subramanian (2011) analyzed empirical data and found evidence that the appreciation of the exchange rate is to blame for decreasing competitiveness.

Although the counter-factual of what Afghanistan's export sector would look like without international aid cannot be known, several studies indicate that the nation's competitiveness has declined as predicted. In the 1960s, according to the FAO, 48 percent of Afghan trade revenue stemmed from horticultural products such as apricots, melons, peaches and pistachios. Agriculture is now largely a subsistence sector, and many of these Afghan products have lost their place in the world economy (UN FAO). In fact, the growth of domestic output hardly kept up with population expansion. Even from 1961-1971, the GNP per capita in Afghanistan dropped from 5062 Afghani to 5028 due slow economic growth promulgated by the influx of foreign aid by the Soviets and Americans back then (Ford 139). Now, Afghanistan has lost much of its carpet sector to competitor nations, despite the fact that over one million Afghanis are still involved in the production chain of carpets (McCord 2007). Furthermore, a UN report on Drugs and Crime shows that the predicted trends held true in the early periods of international aid. Afghanistan's legal exports "decline[d] drastically in 2001" even as wages for casual labor increased by 69 percent in the first nine months of 2002 (UNODC 2003).

One further "anti-developmental" aspect of the U.S. aid program was its degree of interference in (or, to put it in other words, monitoring of) Vietnamese affairs. Since the United States was spending large sums in Vietnam, and since allegations of Saigon's corruption and incompetence were widely reported by the American press (and likely widely believed by the American public), U.S. officials decided that the regime's use of aid funds required significant oversight. This meant that American advisors, embedded within Vietnamese ministries, approved nearly all expenditures of funds that made use of American taxpayer dollars. As historian Craig Lockhard puts it, the Saigon government, became a mere tool "for ratifying, if not always carrying out, American directives" (Lockard 1994, 237). For his part, a policy analyst for the U.S. government who specialized in aid to Vietnam wrote in retrospect that "This system of aid administration made the Vietnamese more dependent on the Americans, and that could not possibly serve the cause of long-run development" (Dacy 1986, 36).

In Vietnam, then, the exigencies of war decisively shaped the U.S. foreign assistance program. Rather than focus on the country long-run political and economic development, Americans rushed in to fill Saigon's budget gap while trying to meet the demands of the citizenry for a higher standard of living. These policies, which also promoted an overvalued currency, weakened the government and country in important respects. They meant, for example, that imports would be favored over local production, and thus the country never developed much of an industrial class that could serve as a bulwark against Communism. The American demand for monitoring the regime's spending patterns also effectively neutered the government in the eyes of its own people. In short, in Vietnam, foreign aid failed to bolster state *strength and legitimacy*—the state's capacity to collect revenues, promote the rule of law, and monopolize the use of violence—though it did increase the state's *capability* to finance a war effort.

That failure to build state strength, in turn, undermined the South's long-run political stability and with it any belief in the country's economic future. To be sure, in conflict-ridden states, institutional and governance capacity is, almost by definition, weak. As a consequence, institutional development has been a chief concern of most foreign assistance programs to "fragile" governments. The OECD-DAC's "Principles for good international engagement in fragile states," adopted in 2007, calls upon to donors to "focus on State building as the central objective" of their foreign assistance programs. With specific reference to Afghanistan, in their 2010 London Communique the international community pledged "to make intensive efforts to ensure the Afghan Government is increasingly able to meet the needs of its people through developing its own institutions and resources." How best to advance that goal, however, remains one of the most challenging tasks facing both domestic political leaders and the international community that seeks to assist them.

The fact that donors can, if only inadvertently, undermine institutional capacity has been well-documented in the aid literature over the years. Given that aid-dependent countries are often flooded not just with funds but with projects and advisors, governments must spend much of their time catering to the needs of the foreign aid community rather than to the needs of their own people (Brautigam and Knack 2004). Further, as the World Bank has commented, "donors may fragment central capacity for policy formation, entering with ministries into bilateral deals on multiple projects without determining whether their cumulative effects are collectively sustainable or mutually consistent" (World Bank 1997, 84). Focusing on Africa, Brautigam and Knack (2004) find a robust statistical relationship between aid and deteriorating governance and higher aid levels and lower domestic tax revenue as a percentage of GDP. They suggest that donors focus on funneling aid through existing institutions, in order to avoid fragmenting the nation's capacity. In Afghanistan a large share of foreign aid continues to flow outside government channels, in part because of a lack of institutional capability (and thus a vicious circle is set into motion) and in part because of concerns with government corruption.

Bolstering this argument about the potentially perverse consequences of aid is an intriguing "counterfactual" case study conducted by Eubank on Somaliland, a country that was ineligible to receive foreign aid after seceding from Somalia in 1991, as the international community was intent on preserving the sanctity of that nation-state. Somaliland, like Afghanistan in 1992 when the Soviets exited, emerged from civil conflict and required tremendous rebuilding efforts. However, while Afghanistan has succumbed to further conflict and is characterized by a weak government, and chronic aid dependency, the widely supported Somaliland government provides security and stability to its citizens and has seen the peaceful transition of presidential power (even in face of a remarkably slim 80 vote margin!) It has accomplished all this with no foreign aid to the government (Eubanks 2010).

Eubank identifies three key reasons as to why Somaliland has emerged as a stable state "despite" an absence of official development assistance to support the new regime (Somaliland has received external funds in the form of remittances from expatriates). First, since the state did not receive outside financial support, the influence of the local business community, which was a major source of tax revenues increased. In particular, the business community used its influence by lobbying for the development and effective management of public goods like education. Second, had the transitional Somaliland governments received foreign assistance from external sources, they might have never engaged in peace talks, instead engaging in civil war. Gourevitch (2010) points out that the Biafran government was able to continue its war with Nigeria for at least an additional 18 months due to the (non-governmental) foreign aid flows it received from charities in the U.S. and Western Europe. Finally, and most important, because the government was dependent upon taxation for domestic revenues, it was also rendered politically dependent upon its constituents, who demanded policies that promoted peace and prosperity.

Can the Somaliland case be compared in any meaningful way to Afghanistan? To be sure, the "fixed effects" in each country case differ and these must be taken into account before drawing simple comparisons and lessons. Certain structural factors in Somaliland helped it to develop a reasonably capable and legitimate central government, including a lack of natural resources; some parity between the different groups that had been fighting; the shared commercial interests of a predominantly pastoral economy; and strong traditional institutions that were designed to promote negotiation and compromise among different social groups. Afghanistan's central geopolitical position, in contrast, has meant that it has rarely escaped the political machinations of both neighbors and more distant powers, which have supported various "sides" within the country at the expense of a strong state and national (as opposed to tribal) identity, and that is a major impediment to peace that has not yet been resolved.

Strengthening institutions in fragile states is evidently a complex task, and the Vietnam case among others suggests that the state's short-run exigencies may undermine the government's and donors' efforts at long-run institution-building. As a Brookings Institution report puts it in a review of such efforts, "It is no surprise…that institutional development is a strong focus of donors…in fragile states…However, given the political challenges that characterize most fragile countries, the causes of institutional weakness can be difficult to diagnose correctly, let alone to rectify. In countries where corruption is rampant, the entire integrity of the government's planning and budget process can be compromised…Donor efforts to support institutions in these environments often fail to achieve any traction" (Brookings Institution 2011, 11).

Further, the immediate pressures on the ground posed by humanitarian challenges may cause donors to do an "end-run" around state institutions. In Afghanistan, for example, the international community decided to sub-contract much of the country's health needs directly to non-governmental organizations (NGOs) rather than through the relevant health and rural ministries (Brookings Institution 2011, 12). While the Afghanistan Mortality Survey 2010 cites the results of these efforts as "stunning progress", the outsourcing of health programs has probably not improved the institutional capacity of the state. In the next section, we look at the allocation of foreign aid to Afghanistan and its effects on the legitimacy and strength of the Afghan government.

Still, there are signs of progress in building the Afghan state that deserve recognition. One proxy measure of the state's growing institutional capacity is the fact that domestic revenue as a percentage of GDP has increased from 3.2 percent in 2002 (World Bank 2005) to around 11 percent in 2011, with technical assistance from the IMF aiding the development of a more efficient taxation system (IMF 2012). From an historical perspective this is also a real achievement, since Afghanistan's domestic revenue as a percentage of GDP has traditionally been quite low, reflecting a weak state, never rising above 7 percent since 1929 (Riphenburg 2006). This rise in domestic revenues from taxation provides one promising signal among others (including the strengthening of the Afghan National Army), that real strides towards building a more capable state are being made.

Foreign Assistance to Afghanistan

The core objective of foreign aid to Afghanistan has been to serve a "stabilization" function in the face of an insurgency that has sought the overthrow of the regime of President Hamid Karzai and the withdrawal of the foreign troops which supported him. In this sense, aid has been actively shaped as a compliment to military action during the counterinsurgency campaign. Underlying these aid flows is a theory of counterinsurgency known as "winning hearts and minds" (WHAM).

The WHAM theory builds on the following assumptions: first, the population has grievances against the government; second, the insurgent exploits these grievances by suggesting it has a credible alternative; third, to the extent the population sympathizes with the insurgents, it will withhold information about his whereabouts and activities; fourth, counterinsurgents can only obtain information by "winning hearts and minds" and addressing grievances; fifth, to the extent that some of these grievances can be overcome with economic transfers, foreign aid can play a key role in supporting counterinsurgency strategy (on the economics of counterinsurgency in Afghanistan, see Kapstein 2012). As Savun and Hays put it, "Foreign aid can promote economic growth and development which reduces the level of grievances, mobilization and willingness of individuals to join" insurgent groups, or perhaps even to provide material support to such outfits. No less important, governments can also "use aid to finance repressive" counterinsurgency measures, which of course impose heavy costs on the state's treasury (Savun and Hays, 2011, 1).

Counterinsurgency campaigns are thus particularly complex and costly in that they require the application of both military power and economic resources to combat the insurgents. In this view, insurgents must live among the population and can only thrive much less survive with their support, whether tacit or explicit. Conversely, counterinsurgents can only win the war to the extent that they receive information flows from the noncombatants about the activities and movements of the insurgency. In short, "in as much as the government can secure the population and address popularly held grievances, the local beneficiaries of these efforts will reciprocate and reward it with their support" (Berman, Shapiro, Felter 2009, 4).

Central to a successful counterinsurgent campaign is therefore the effort to "address grievances." But what, in fact, are the grievances of the population? Are they economic or political in nature? Can economic assistance be used to positive effect to assuage political grievances, as counterinsurgency strategy seems to assume?

These questions were among those raised at a 2010 Wilton Park conference on Afghanistan. There, participants questioned whether such economic grievances as poverty and unemployment really played a significant role in shaping public support (or lack thereof) for the insurgency. At the same time, participants also expressed doubts about the extent to which the aid community's economic development programs in that country were providing a "stabilizing" function (Wilton Park 2010).

Indeed, a widely held view among the Afghan experts was that "the fundamental conflict drivers…are inherently political in nature, such as ethnic grievances and inter- and intra-tribal disputes." Further, "many Afghans believe the main cause of insecurity to be their government, which is perceived to be massively corrupt, predatory and unjust" (Wilton Park 2010). To those gathered at Wilton Park, it was by no means obvious that economic assistance could be used as an instrument for overcoming fundamentally political problems, such as the state's lack of legitimacy and the diffusion of political power. This impression was, ironically, bolstered by the Afghanistan Development Cooperation Report (DCR) of 2010, which baldly stated, "State building has not been the central objective [of foreign aid] in the past nine years" (43).

While this critique of the Afghan state and its foreign supporters may or may not be fair, any reasonable observer must admit that the donor community confronted a mammoth task when it entered the country following the overthrow of the Taliban regime in 2001. Even without the insurgency that erupted thereafter and the decade of severe military conflict that has followed, the challenge of rebuilding the country from its 2001 base would have proved overwhelming. As the Asian Development Bank (ADB) summarized the situation at the time of the Taliban's collapse, "War and civil conflict resulted in the deaths of over 1 million Afghans between 1978 and the end of 2001, with a further 1 million left orphaned or disabled. Up to one third of the population became refugees…most of Afghanistan's basic infrastructure was destroyed…The education of an entire generation of young Afghans was disrupted" (ADB 2008, 1).

The decade of warfare since 2001 has only compounded those problems. Many thousand more of Afghans have been killed and displaced, and public opinion surveys reveal widespread insecurity about the country's future (Kapstein 2012). Despite the billions spent in foreign assistance, "Some 12 million Afghans, or 42percent of the population, live below the poverty line, with incomes of about $14 per month per capita…life expectancy is under 45 years…over 20 percent of all Afghan children die before the age of five; half of Afghanistan's school-age children are not in school; 57 percent of the population is under 18…but with little hope of full-time employment…" (ADB 2008, 2).

So how have foreign assistance funds been allocated in Afghanistan, and how effective has that spending been in building up the Afghan state? A short-hand answer, to be developed in what follows, would be that funding has mainly gone to the Afghan military and to budgetary support of government operations, and that spending in some sectors has been more effective than in others, which is unsurprising in the face of what the relevant literature calls "aid heterogeneity" (on the heterogeneous effects of different types of aid spending see, for example, Asiedu and Nandwa 2007 and Mavrotas and Nunnenkamp 2007). Specifically, between 2001-2010, over fifty percent of all foreign assistance has been allocated to security in an effort to strengthen the Afghan National Army (ANA) and Police Force. In terms of economic development, Afghanistan's government has relied upon foreign aid for 100 percent of *its* development budget and 45 percent of its operating budget, resulting in an aid to GDP ratio of 71 percent and making it one of the most highly dependent nations in the world. Here it must be emphasized, however, that only 30 percent of the aid community's development funds are actually channeled through the government's core budget; the vast majority is, instead, administered as parallel projects by the donor nations or subcontractors. Since it is not funneled through the government, the nation is not training employees or creating institutions to manage the funds spent on the development of their nation and thereby contributing little to bolster institutional capacity (Islamic Republic 2010). The Somaliland and Vietnam cases illustrate how essential managing funds and budgets can be to strengthening state capacity. Table 1(end of document) provides an overview of foreign aid commitments to Afghanistan since 2002, while Table 2 provides a breakdown of aid spending by sector.

As Table 2 demonstrates, infrastructure has received the highest levels of investment from foreign donors after security, followed by agriculture and rural development. These three areas of spending (infrastructure, agriculture, and rural development) have all been touted as contributing to the counterinsurgency campaign, in particular through the mechanism of job creation. The United States in particular has emphasized the importance of "immediate job creation, particularly in the insurgency-plagued provinces of Helmand and Kandahar" (US Senate 2011, 20). In making this statement, the U.S. is explicitly making a causal connection between jobs (or the absence thereof) and support (or the lack thereof) for the government and counterinsurgency. The United Kingdom's Department for International Development also makes this connection, asserting that "Improved licit income opportunities and a growing economy will help weaken the appeal of an insurgency" (2011).

In an influential paper, however, Berman, Felter and Shapiro (2009) cast doubt on the purported causal connection between unemployment and popular support for insurgencies, and thus on the efficacy of this type of spending. They argue that "most aid spending by governments seeking to rebuild social and political order is based on an opportunity-cost theory of distracting potential recruits. The logic is that gainfully employed young men are less likely to participate in political violence, implying a positive correlation between unemployment and violence in places with active insurgencies. We test that prediction on insurgencies in Iraq and the Philippines… *Contrary to the opportunity-cost theory, we find a robust negative correlation between unemployment and attacks against government and allied forces and no* *significant relationship between unemployment and the rate of insurgent attacks that kill civilians"* (Berman, Felter and Shapiro 2009, italics added).

While job creation is undoubtedly one reason to invest in infrastructure, there are other important rationales, including the development of economic activity that could be stifled by the lack of transportation networks among other internal improvements. According to the World Bank, funding for roads was the single biggest foreign program in Afghanistan after security support; some $1.3 billion was devoted to road construction and rehabilitation. In many respects, this would seem to be a perfectly sensible use of aid funding. As the Bank writes, "Afghanistan is a landlocked country, and roads are the principal means for domestic and international transportation.… An effective, reliable, and modern road network can serve poverty reduction by supporting improved efficiency of agriculture and industries, facilitating cross-border trade, and contributing to economic integration of the region" (World Bank 2009, 75). It is significant here that the Bank highlights the role of roads in *poverty reduction*, suggesting that this developmental objective (poverty reduction has become *the* development objective of the international community since 2000 with the articulation of the Millennium Development Goals and its promise of reducing global poverty by fifty percent by 2015) is being pursued even in this war zone; whether that's appropriate is a question we'll take up below.

But the problem with this heavy focus on road construction, as the Bank points out, is that "The opportunities for corruption are great…in a situation lacking adequate institutional and human capacity and necessary public oversight and monitoring mechanisms." (World Bank 2009, 76). According to the 2010 Corruption Perception Index, Afghanistan is ranked as the second-most corrupt state after Somalia (Islamic Republic 2010). Further, at least in some cases, western contractors overseeing these projects have had no choice but the pay "powerful local figures" with "links to Afghanistan's insurgents" for security (New York Times, 1 May 2011).

This suggests more generally the hypothesis that rent-seekers and predators of all kinds will gravitate toward large infrastructure projects, making such projects targets of corruption and protection rackets, including those organized by the insurgents themselves (see Tanzi 1998; Crost, Felter and Johnston 2011). In the Helmand providence, aid was perceived as flowing to the group of tribes who had seized power in 2001. According to Fishstein and Wilder (2012), "The construction sector was generally described as the most corrupt, and evidence exists in some places it has become highly criminalized (45)." The result of aid flowing to concentrated groups with power rather than to the Afghan people more broadly has unsurprisingly made the population skeptical about the benefits of these aid flows. .

One alternative to big, national-level infrastructure projects would be support for small, local projects, like water wells and sanitation. To be sure, one could argue that such small-scale projects will also be captured by those local chiefs with power, extracting rents from the process. But the difference is that corruption of this nature is less likely to delegitimize the *national* government, and it's important to recall in this context that building the legitimacy of the Afghan government—its capacity to collect revenues, create the rule of law, and monopolize the use of violence—has been one of the cornerstones of America's war strategy (Jones 2010); without widespread, popular legitimacy, the Afghan government will have a much more difficult time retaining power and international support once the foreign troops depart. The National Solidarity Program (NSP) is often cited as providing support for this local model, through which community members become invested in supporting these small-scale projects. The Center for a New American Security even cites this program as the most successful project to date in creating ties between the people and the Afghan government, especially as project results are tangible and immediately useful (Roberts 2011). Indeed, in a study of small projects in Iraq, Berman, Felter and Shapiro (2008) find that they have a much stronger and positive effect on the local, tactical environment than large-scale development projects. Beath, Christia, and Enikolopov (2012) also find that, given a certain threshold level of security in an area, the NSP has been successful to some degree in improving security and the perceptions of people of their own well-being and towards the government. Larger scale development projects are rarely undertaken in areas with high security threats; thus, the scarcity of data makes it hard to estimate the effects of such projects on security levels.

To be sure, small-scale projects are not without their own set of drawbacks. USAID workers revealed that in order to finish projects by established deadlines, local infrastructure projects are often promoted in order to increase the "burn rate" of grant money. In one example, the American company PADCO, who won a $60 million grant from USAID, said that it tripled power in two Afghan provinces. But Afghan officials say that nobody in these areas had experienced any additional access to electricity. Small projects are perpetually under-staffed as well, particularly in regions with a poor security environment (Arnoldy 2010). Furthermore, high overhead costs, salaries for Western consultants, security arrangements for aid workers, and the network of subcontracting arrangements means that the percentage of aid that actually reaches Afghans "on the ground" is extremely low, making smaller projects extremely inefficient (Mullen 2009). Moreover, sub-contracted work generally leads to inflated costs as each firm along the chain takes a percentage of the money, forcing the lower organizations to work with significantly less money. As these firms economize on materials and costs to remain within the decreased budget, they produce low-quality output. Many Afghan respondents in fact understand the phenomenon of sub-contracting as a legal form of corruption (Fishstein and Wilder 2012).

The lesson that one can draw from investment in infrastructure, therefore, is that these types of large, "shovel ready" projects only makes sense in an institutional environment that has the capability to manage them in an effective manner. In Afghanistan, the areas that need the most infrastructure investment are often deemed too dangerous for donor activity, and project monitoring (including of western contractors) is often inadequate. Even with smaller projects, these concerns surface, although they may have less negative effects on the national government. Widespread corruption perpetrates the government and international aid's inefficacy in the minds of the citizens, as the general belief is that "the purpose of aid is personal enrichment" (Fishstein and Wilder 2012, 46).

On balance, then, there is probably no simple answer to the question of whether larger or smaller projects should be the focus of donor activity. Large-scale projects may be more efficient, but they may also have a higher susceptibility to large-scale corruption. Small-scale projects, in contrast, probably have the potential to make a deeper impact upon the hearts and the minds of people at a community level, but they are relatively costly and difficult to monitor.

We now briefly take up the issue of "poverty reduction" and its role in fragile states, and we recall that the World Bank cites poverty reduction as one rationale for infrastructure investment in Afghanistan. In this context, one question that arises is, what's the purported connection between poverty reduction and support for the counterinsurgency? As Djankov and Reynal-Querol write, "Progress in stopping war, civil conflict and violence - the argument goes - requires a reduction in poverty." They cite former German Chancellor Gerhard Schröder as an example, who stated in 2001: "reducing worldwide poverty is…essential to safeguarding peace and security."' Yet the authors go on to point out serious empirical limitations with such assertions. Most significant is the problem that war and poverty may be endogenous to one another, and when this possibility is taken into account, they find the statistical relationship between poverty reduction and conflict to be "spurious" (Djankov and Reynal-Querol 2008, 3). Poverty reduction might therefore be a laudable humanitarian goal, but its contribution to a counterinsurgency campaign is less obvious.

To summarize, foreign assistance has pursued multiple objectives in Afghanistan, but if one "follows the money" the focus has undoubtedly been on immediate security requirements and government budgetary support. The question this raises is whether funding these priorities alongside other, longer-term programs (e.g. investments in infrastructure, poverty reduction and so forth) have strengthened the legitimacy and authority of the Afghan state, or undermined it by fueling corruption and antagonizing important elements in civil society. The answer is probably "some of both," again reflecting the fact of aid heterogeneity—that some types of aid are more effective than others in developing institutional capacity. The issue that now arises is, how should the foreign assistance community prepare for the troop withdrawal from Afghanistan? How can the donor community best promote the country's chances for a peaceful and prosperous future?

What Should Be Done?

In preparing for its ultimate departure from Afghanistan, there is much the donor community could have done on the economic front but has thus far failed to implement. Now, with time pressing, the international community must prepare Afghanistan for a "soft landing." To be sure, the donors have sought to provide Kabul with reassurance that aid flows will continue for many years to come, but the killings in February 2012 of two Americans who were embedded in Afghan ministries—following the inadvertent burning of a box of Korans by U.S. soldiers—points to the fact that many Afghans resent the presence of foreign advisors. A number of actions must therefore be taken while the U.S. still has military forces and an active stake in the country.

To begin with, it is incredible that, after more than ten years of war, the U.S. has no trade agreement with Kabul. While a pact like a preferential trade agreement would undoubtedly be largely symbolic in nature, it nonetheless could motivate Afghan entrepreneurs to seek trade opportunities in the United States and Western Europe, especially if coupled with changes to the exchange rate. Instead, Afghan traders have looked closer to home, promoting cross-border flows with Iran and Pakistan, which can hardly be in NATO's strategic interest.. More unfortunate from a development standpoint, these flows consist largely of imports of food and consumer goods, since the U.S. has promoted a strong Afghan currency that makes it near impossible to produce such goods competitively within the country.

The lack of an export-oriented industry, in turn, means that Afghanistan lacks a strong and forward-looking entrepreneurial class which could have served as a foundation for an anti-Taliban society; again, the counterfactual case of Somaliland comes to mind. And this is an even greater loss when one recognizes the tremendous craftsmanship that Afghan society is capable of in such sectors as wood-working and glass-making. Interestingly, many of these same issues were present in Vietnam as the United States prepared to disengage from that country. At a time when aid flows are likely to decline, connecting "Afghanistan with regional and global markets by removing restrictions on trade" has become even more vital (World Bank 2011, 5; Eubank 2010).

Going forward, however, the problem facing Afghanistan will not be so much how to improve the aid that continues to flow, but instead how to cope with the fiscal calamity that could erupt as those flows decline. The World Bank, for example, anticipates an "enormous fiscal gap" as foreign soldiers and assistance workers withdraw and as aid levels decrease (World Bank 2011, 3). As in Vietnam, this means that the Government of Afghanistan could be called upon to introduce a severe austerity program just when it is most vulnerable. Unfortunately, the World Bank's plea that "reductions in international assistance are gradual, predictable, and orderly" may be at odds with domestic politics in the major donor countries, where other pressures and crises will surely redirect aid spending once the Afghanistan intervention recedes in memory (World Bank 2011). In this sense, the short-run political demands of *donor governments* are also in tension with the long-run developmental needs of recipient states.

Conclusions

The story of foreign assistance to Afghanistan is largely one of support to an ongoing military campaign. To be sure, schools and hospitals have been built, and government ministries created or revitalized. Elections have been held and the seedlings of democracy planted. Undoubtedly much has been done to improve the lives of the Afghan people, and that is no small accomplishment. But these schools and hospitals were often built without adequate funding for staff, and many have subsequently been closed or converted into storage units.

Furthermore, the distributive consequences of this good work are difficult to discern. According to the World Bank, poverty levels remain high, and it is quite possible that inequality has increased as a few "insiders" have profited from lucrative contracts associated with the foreign presence in the country. On the other hand, opportunities for women have undoubtedly increased and school enrollments are rising. These are encouraging signs in terms of an "inclusive growth" agenda (Ali and Zhuang 2007).

But there is no evidence that, despite these positive developments, aid has helped to ameliorate the social and political tensions that still divide the Afghan people and which undermine state authority. The Government of Afghanistan continues to have little popular legitimacy, as corruption—partly fueled by foreign aid—has undermined confidence in the country's leadership. Further, aid flows are widely perceived to have, ironically, "rewarded" the most unstable parts of the country in the South, while leaving the more secure regions bereft of external support; official data suggest that this perception is largely correct, in that most aid has in fact flowed to such regions as Kandahar and Helmand. Further, despite the billions spent on the security forces, there is little indication that the government in Kabul holds anything close to a monopoly over the use of violence. As a consequence, it is not apparent that aid has been viewed by the Afghan people as widely beneficial, or as acting as an inducement for good behavior on the part of political authorities.

Going forward, the challenge is to prepare Afghanistan for the probable loss of millions of dollars in military and assistance spending. That means that the government may need to pose austerity measures and shore up tax collection; in short, it means that the state will need to be strengthened, and quickly. Unfortunately, as Afghans foresee a time with less foreign inflows, those in authority may seek to "make hay while the sun shines," grabbing rents today that will not be available tomorrow, and in the process further undermining the state's legitimacy.

Our conclusion thus brings us back to the very beginning of this analysis. In fragile, conflict and post-conflict states, the government and donor community share the challenge of mustering the capability to fight an insurgency while building a bridge toward the future. Ironically, support for the immediate security task at hand may undermine these longer-run economic development efforts. This remains the unresolved tension that the donor community continues to face in Afghanistan and perhaps other conflict zones as well.

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Table 1: External Assistance to Afghanistan (US$ millions)

Table 1: External Assistance to Afghanistan

Figures in US$ Millions

Rank	Donor	2002-2013 Pledge	2002-2011 Com	2002-2010 Disb
1	United States of America	56,100	44,356	37,118
2	Japan	7,200	3,152	3,152
3	European Union/European Commission	3,068	2,883	2,594
4	Asian Development Bank	2,200	2,269	1,005
5	United Kingdom	2,897	2,222	2,222
6	World Bank	2,800	2,137	1,700
7	Germany	5,029	2,130	762
8	India	1,200	1,516	759
9	Canada	1,769	1,256	1,256
10	Netherlands	864	1,015	1,015
11	Norway	938	775	636
12	Australia	369	744	656
13	Italy	753	645	540
14	Sweden	515	635	635
15	United Nations	305	446	182
16	Denmark	533	438	438
17	Iran	673	399	377
18	France	134	323	174
19	Spain	308	220	194
20	Turkey	143	213	180
21	Finland	152	160	160
22	Russian Fed.	239	151	147
23	Agha Khan Development Network	190	140	140
24	Saudi Arabia	268	140	103
25	China	252	139	58
26	United Arab Emirates	97	134	117
27	Switzerland	197	118	102
28	South Korea	85	116	83
29	Czech Republic	0	108	102
30	Islamic Development Bank	87	70	17
31	Belgium	60	61	57
32	New Zealand	28	34	34
33	Ireland	29	22	21
34	Poland	7	22	20
35	Kuwait	70	19	19
36	Luxembourg	12	12	11
37	Lithuania	-	6	5
38	Hungary	1	6	5
39	Austria	14	5	5
40	Pakistan	289	5	-
41	Brunei	-	4	0
42	Greece	15	2	1
43	Singapore	-	2	2
44	Estonia	-	1	1
45	Portugal	2	1	0
46	Brazil	3	-	-
47	Croatia	2	-	-
48	Egypt	1	-	-
49	Malta	1	-	-
50	Oman	11	-	-
51	Qatar	30	-	-
52	Slovakia	5	-	-
53	Taiwan	33	-	-
54	Vietnam	3.46	-	-
	Total	89,982	69,248	56,803

Table 2: Breakdown of External Assistance to Afghanistan by Sector (2002-2011)

Figures in US$ Million

Rank / Development Partner	Infrastructure		Governance		Education		Health		Agri/Rural Dev.		Social Protect.		Private Sector Dev/Econ Dev		Security		Unclassified		Total Commitment	Total Disbursement
	COMT	DISB	COMT	DISB	COMT	DISB	COMT	DISB	COMT	DISB	COMT	DISB	COMT	DISB	COMT	DISB	COMT	DISB		
1 United States	3,615	2,558	2,345	1,172	734	522	675	538	4,452	3,377	418	390	820	512	28,850	26,050	2,447	2,000	44,357	37,118
2 Japan	371	371	303	303	134	134	225	225	202	202	559	559			954	954	404	404	3,152	3,152
3 European Union	149	141	518	493	13	12	201	169	513	417	826	721	66	55	486	482	111	104	2,882	2,594
4 Asian Dev. Bank	1,916	666	353	339	-	-	-	-	-	-	-	-	-	-	-	-	-	-	2,269	1,005
5 United Kingdom	479	479	476	476	186	186	183	183	275	275	228	228	35	35	358	358	-	-	2,221	2,221
6 World Bank	742	584	382	355	160	114	207	151	409	423	8	2	149	71	-	-	-	-	2,137	1,700
7 Germany	494	224	378	38	224	55	45	21	205	85	40	16	426	63	318	247		14	2,130	762
8 India	734	503	4	4	173	91	39	29	7	3	551	124	3	3			4	3	1,516	759
9 Canada	5	5	130	136	92	92	96	96	185	185	162	162	217	217	117	117	246	246	1,256	1,256
10 Netherlands	37	37	420	420	30	30	9	9	72	72	204	204	13	13	205	205	26	26	1,015	1,015
11 Norway	34	-	96	18	51	1	36	13	119	59	86	22	2	-	18	1	336	521	776	636
12 Australia	4	4	162	93	24	20	10	10	15	14	416	411	1	1	18	18	92	84	743	656
13 Italy	145	86	225	223	7	7	29	14	63	43	132	133	9	9	29	21	5	3	643	540
14 Sweden	27	27	256	256	137	137	34	34	2	2	149	149	9	9	21	21	-	-	635	635
15 United Nations	37	9	36	23	106	51	171	58	29	6	43	15	3	0.25	16	16	4	1	446	179
16 Denmark			61	61	92	74	10	10	70	70	20	20	9	5	15	13	161	185	438	438
17 Iran	202	180	10	10	33	33	6	6	11	10	16	16	3	3	8	8	111	111	399	377
18 France	17	11	36	29	55	42	50	34	94	64	41	33	10	3	20	16	-	-	323	174
19 Spain	36	36	26	26	8	8	11	11	54	54	9	9	-	-	1	1	76	50	220	194
20 Turkey	39	30	1	1	54	43	54	52	2	2	4	4	1	1	53	43	5	5	213	181
21 Finland	-	-	49	49	-	-	8	8	5	5	31	31	-	-	18	18	49	49	160	160
22 Russia	-	-	-	-	2	1	-	-	-	-	40	37	-	-	109	109	-	-	151	147
23 Saudi Arabia	30	-	45	45	17	0.29	2	2	-	-	51	51	-	-	0.01	0.01	-	-	145	98
24 AKDN	25	25	-	-	16	16	20	20	33	33	17	17	30	30	-	-	-	-	140	140
25 United Arab Em.	7	5	2	2	3	3	6	-	0.40	0.05	1	1	104	104	10	10	-	-	134	126
26 China	-	-	23	2	-	-	6	1	39	14			-	-	21	2	42	40	130	59
27 Switzerland	1	1	27	23	15	11	12	12	33	24	25	25			4	4	3	2	118	102
28 South Korea	4	4	14	11	18	17	54	29	5	5	2	-	-	-	5	5	14	14	116	85
29 Czech Republic	4	4	1	1	4	4	1	1	2	2	8	8			5	5	78	78	102	102
30 Islamic Dev. Bank	66	12	0.12	0.12	5	5	-	-	1	-	-	-	-	-	-	-	-	-	72	17
31 Belgium	1		15	12	1	1	6	6	13	8	21	20			5	4	1	6	63	58
32 Newzeland	7	7	6	6	5	5	2	2	3	3	-	-	-	-	3	3	7	7	34	34
33 Ireland	-	-	18	16	0.35	0.09	0.25	0.25	1	1	6	5	-	-	2	2	-	-	28	25
34 Poland	12	11	1	0.07	4	4	1	0.22	1	0.42	2	2	0.03	-	-	-	2	2	22	19
35 Kuwait	0.20	0.20	15	15	-	-	4	4	-	-	0.45	0.45	-	-	-	-	-	-	19	19
36 Luxembourg	-	-	9	8	1	1	-	-	-	-	2	2	-	-	0	0	-	-	13	11
37 Austria			1	1			0.06	0.06	2	2	2	2			2	2			6	6
39 Hungary	-	-	1	0.20	2	2	1	0.43	1	1	0.07	0.07	-	-	1	1	-	-	6	5
40 Lithuania	0.37	0.37	1	1	1	1	3	3	-	-	-	-	-	-	-	-	-	-	5	5
41 Pakistan	-	-	-	-	5	-	-	-	-	-	-	-	-	-	-	-	-	-	5	0
42 Brunei							3				0.44	0.44							4	0
43 Portugal	1	0.10	1.00	1	0	0.10	-	-	-	-	-	-	-	-	-	-	-	-	2	1
44 Greece	-	-	-	-	0.05	-	-	-	-	-	1	1	1	-	-	-	-	-	2	1
45 Singapore	-	-	-	-	-	-	1	1	1	1	-	-	-	-	-	-	-	-	2	2
46 Estonia			0.05	0.05	0.04	0.04	1	0.38							0	0.26			1	1
Total	9,241	6,020	6,452	4,669	2,415	1,724	2,220	1,750	6,998	5,442	4,122	3,399	1,911	1,133	31,670	28,735	4,221	3,955	69,250	56,812

1) Social protection includes humanitarian assistance.

Source: Islamic Republic of Afghanistan, Development Cooperation Report