



Empty Hat: Foreign Investors Shun Karzai's Afghanistan

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No major foreign equity investment in either the goods or the resources-producing sectors in Afghanistan has been made, notwithstanding Karzai's frantic travels abroad seeking to woo investors. This contrasts sharply with Afghanistan under the Taliban [1996-2001] when both the giant U.S. oil firm, UNOCAL, committed to building a trans-country gas pipeline and a private New Jersey-based enterprise, Telephone Systems International Inc., secured a license from the Taliban to set up an integrated, high-tech communications network costing \$240 mn.¹ The Taliban for all their faults, were able to put in place a degree of political stability and the means to enforce contracts - after all, in one year they reduced poppy cultivation to next to nothing. Under the "non failed state" of Karzai, on the other hand, poppy production has soared. Afghanistan's share of the world heroin market rose from 12% in 2001, to 76% by 2003.²

To-date, direct investment has involved two cell phone companies, two air express services, three hotels, four [minor] airlines establishing links with Kabul, a Chinese importing agency, and private individuals in some restaurants [e.g., B's Place set up by an Australian³ and the new Thai restaurant], bars [e.g., the British-owned Irish Club but recently forced to close⁴], and the like. Mini-skirted waitresses [replaced in April 2003 by dresses slit to the thigh⁵] served Tsing Tao beer to customers

eating barbequed pork at the Chinese Restaurant in Kabul, opened in November 2002.⁶ World Airways and Swiss Skies secured a \$ 102 mn 2 1/2 year contract for bi-weekly flights between Dulles airport and Kabul, explicitly targeting the large NGO and governmental communities in Washington and Geneva as passengers.⁷ The British Standard Chartered submitted a request for a license to operate a full-line commercial bank branch in Kabul, as did the state-owned National Bank of Pakistan.⁸ An American investor from Florida, Stephen King, is reported to have purchased the defunct state-owned, large German-built Gulbahar cotton textile enterprise.⁹ Another American investor - Marc Seidner's Permanente Corp. - has joined with Afghan Americans in a proposed vast \$ 2 bn farming and forestry project in Afghanistan, which

"over the next decade...can transform vast dust-blown wastelands into rich forests, chicken and turkey farms and fruit and nut orchards that could generate about \$ 6 bn a year."¹⁰

Minor investments from neighboring Iran and Pakistan have been made. Equity investments by Afghan expatriates have occurred given their superior knowledge about the country, a better understanding of risks involved and expectations of benefits in addition to the immediate return on investment.



No manufacturing, no mining and *no gas pipeline* deals have been consummated.¹¹

A prospective private equity investor will examine the risk-return trade-off, being able to have equity contracts enforced, and have the ability to withdraw their stake quickly. If an institutional structure does not exist which protects the equity investor or the long-term investors, investments simply will not be forthcoming. Other factors raise the cost of conducting business in Afghanistan, including endemic corruption, bureaucratic red tape, absence of banking and legal infrastructure, etc.¹² No risk-averse foreign investor will contemplate putting in hundreds of millions of dollars to build a gas pipeline through Herat, Helmand and Kandahar provinces linking gas supplies in Turkmenistan with Pakistan. Nor will a capitalist investor spend the millions of dollars necessary to build infrastructure and develop the isolated Ainak copper deposits in Logar province.¹³

On September 1, 2003, Taliban rebels attacked security positions guarding reconstruction of the Kabul to Kandahar highway, killing at least seven Afghan police and employees of the Louis Berger Group.¹⁴

The United States government operates an investment insurance facility called O.P.I.C. which has offered a \$40 mn insurance coverage to Hyatt International for a planned deluxe, 205-room hotel to be built, not surprisingly, opposite the U.S. Embassy.¹⁵ OPIC also provided a loan to The Berkeley Group/World Airways.¹⁶ On June 16, 2003, Afghanistan joined the World Bank's Multilateral Investment Guarantee Agency [MIGA] which provided political risk insurance for investments [against exporting profits,

expropriation, breach of contract, damage from war and civil disturbance].¹⁷ Both these schemes in effect socialize the risk of private direct foreign investment in Afghanistan.

The investments which have occurred [see **Table 1** below] have been in services provision, largely in the ISAF-protected Kabul. The cell phone companies operate equipment in a half dozen major cities. Cell phone companies have small capital investments consisting mostly of towers and personnel. An Internet cafe has been set up in Kabul's Intercontinental Hotel by AWCC. Two minor-league, charter airlines have established weekly service to Kabul: World Airways/Swiss Skies from Washington and Germany's L.T.U. from Dusseldorf. But, the weekly LTU flight has been condemned by a German pilots' group as being reckless and dangerous given mines next to Kabul runways and possible anti-aircraft rockets.¹⁸ Azerbaijan's state-run AZAL has three flights a week joining Kabul with Baku. Iran's private airline, Mayan, began flying the Teheran-Kabul stretch twice a week with an Airbus, in May 2002. The ground fire hitting an Ariana Airlines Boeing 727 taking off on July 26, 2003, from Kabul might even discontinue those connections. As with the two express delivery companies, these stakes represent minor investment exposure within Afghanistan itself. DHL leases an old Russian Antonov-12 to fly between Kabul and Bahrain, DHL's Middle Eastern hub. A total of about \$ 120 mn has been invested, but fully 88% of that is made up of the two investments by cell phone consortia, or 75% comes from just one source, the Aga Khan Fund.



At the handover of the ISAF command to NATO in Kabul, on August 11th, Karzai [again] distinguished himself in imagery rather than substance. He proclaimed

"today we have a truly international city. Today we have a city where people can come and invest... we have in this city a Thai restaurant... we have restaurants from India and China..."¹⁹

Yes, an international army is in Kabul without which Karzi would long be history. And yes, foreign investors have established a few restaurants, but this is a far cry from what Karzai's commerce minister, Sayed Kazemi had suggested in April when he mentioned that foreign investors were preparing to pour billions of dollars into the country. The first Chinese restaurant, The Golden Lotus, opened in Kabul in the 70's.

On the other hand, foreign aid grant disbursements to Afghanistan totaled \$ 1'836 mn [January 2002 – March 2003], which when set in relation to the country's G.D.P. estimated at \$ 4'400 mn for 2002 by the Asian Development Bank, *yields a very high ratio of 42%*.

What also clearly emerges is that the direct investments which have been made do not require long-term capital commitments and can be quickly withdraw if necessary. Not until some semblance of stability and predictability exist in Afghanistan will foreign investment commit. Most importantly and most egregiously missing in Karzai's Afghanistan, is a legal system to enforce contracts.

In addition, the investments made *cater exclusively to the urban upper middle classes* [both the huge foreign expatriate community, the returned Afghan exiles, and the Karzai bureaucrats] and do little to garner mass support and political

stability. The average wage in Kabul is \$ 1/day. AWCC's low-end, hand-held Nokia model sells for \$ 290 and a Motorola set goes for \$ 350.²⁰ One hour at the new Internet cafe costs \$5. Round-trip Teheran-Kabul on Mahan Airlines costs \$330. Business class round-trip Dulles-Kabul, will cost \$7'500. This says much about the role of foreign investment in Afghan "reconstruction." As I and others pointed out long ago, foreign investors in non-extractive activities *do not develop markets, they follow markets and they tend to produce complicated products in complicated ways in order to appropriate scarcity rents*.²¹ Given the income distribution, the endemic poverty in Afghanistan and the high-risk environment, no rational investor will gamble asset exposure in Karzai's Afghanistan.

Too risky to commit to.

Table 1. Direct Foreign Investment in Karzai's Afghanistan

Afghan Wireless Communication Co. (AWCC)	5/2002 (1998)	\$ 50 mn	A wireless cell phone GSM network, opened in Kabul (April 2002) and 4 other cities. AWCC's major supplier is WorldCom	A joint venture between Afghan expat, Ehsan Bayat's TSI Int'l [NY] and Karzai gov't [@ 20%]
DHL Worldwide Express	3/2002	?	Air express service between Kabul-Bahrain, with a chartered AN-12, having an 18-ton cap.	DHL @ 100%. DHL had serviced Afghanistan up until 1987
Mahan Airlines (Iran)	5/2002	?	Air service twice weekly Teheran-Kabul with an Airbus	Mahan Airlines is a private Iranian firm
FedEx	11/2002	?	Air express delivery to Kabul and ground transport in Kabul	FedEx with Afghan Express Ltd.
Intercontinental Kabul Hotel	2002	\$ 8 mn	Renovation of major old 200-room U.S. hotel	15 yr. lease by Dubai's Al Yaqoub Group. Owner of the InterCon is now Six Continents Hotel chain
An Indian company	9/2002	\$.25 mn	Manufacture industrial gases	Announced as a joint venture
Azerbaijan Airlines (AZAL) air lines	1/2003	?	Three times a week by Azerbaijan's state airline between Kabul and Baku	100% owned by AZAL, flying one Boeing 727-200
Aga Khan Fund for Economic Development	2003	\$ 25 mn	Renovate/expand old Kabul Hotel into 5-star facility, Kabul Serena	100% @ Agha Khan. Construction started
Hyatt Regency Kabul	planned	\$ 40 mn	Build a 5-star hotel, 205 room hotel, opposite U.S. Embassy	Still under planning by Hyatt, 3 Turkish construction firms and the Afghanistan Reconstruction Co.
Standard Chartered Bank	Planned 2003	\$ 1.5 mn	To set up a commercial bank branch in Kabul, license pending	100% @ British parent bank which

				has a strong regional presence
China Merchandise Trade Center Ltd.	7/2003	\$ 1.2 mn	Trade firm marketing imported Chinese products in Kabul	100% Chinese owned
World Airways Inc.-The Berkeley Group and Swiss Skies	7/2003	\$ 2.1 mn OPIC loan	Bi-weekly air service by MD-11 between Dulles Washington-Geneva-Kabul.	Swiss Skies is owned by The Berkeley Group, Wash.D.C., and contracted with World to run the air service. Waleed Youssel is CEO of Swiss Skies.
An int'l consortium, Telecom Dev. Co. Afghanistan, launches new service called Roshan	7/2003	\$ 55 mn	A second cell phone network in 6 cities- Kabul, Herat, Kandahar, Mazar, Kunduz, Jalalabad	Aga Khan Fund (51%), Monaco Telecom Int'l (35%), MCT (9%), and Alcatel (5%)
Luftransport-Unternehmen (L.T.U.)	8/2003		Weekly air service between Dusseldorf-Kabul with Airbus 330	100% @ German parent airline company
The Chinese Restaurant	11/2002	\$.16 mn	A Chinese restaurant in Kabul	75% @ Mr. Wong Wentian and 25% @ gov't
Three companies	2002-3		A brake-making co., mineral water and herbal medicines firms	Chinese capital
A Florida investor, Stephen King	7/2003	\$ 2.5mn ²²	Bought the large Gulbahar cotton textile complex	100% @ U.S. investor



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¹ for details on the UNOCAL deal, see Ahmed Rashid, Taliban: Militant Islam, Oil, and Fundamentalism in Central Asia [New Haven: Yale University Press, 2001] and also Adam Tarok, "The Politics of the Pipeline: the Iran and Afghanistan Conflict," Third World Quarterly 20,4 [1999]: 801-820. On the



telecommunications deal, see Simon Romero, "Afghan Phone Links Are an American Legacy," New York Times [November 12, 2001]

² "Afghanistan is Biggest Illicit Drug Source: U.M.," Dawn [June 26, 2003]

³ Todd Pitman, "Kabul Adds Western Style at a Price," Washington Post [November 26, 2002]

⁴ "Threats Close Kabul's Irish Bar," BBC News [April 26, 2003] at 15:28 GMT

⁵ Hamida Ghafour, "Anarchy, Ambition Collide in Kabul," Globe and Mail [August 12, 2003]

⁶ "Chinese Mini-Skirted Revolution Hits Post-Taliban Afgha," Sydney Morning Herald [December 17, 2002]

⁷ Joe Sharkey, "Getting to Kabul Could Be All the Fun," New York Times [June 3, 2003] and "World Airways Gets \$102 mn Contract for Afghanistan Service," Atlanta Business Chronicle [May 1, 2003]. The Washington Dulles airport to Kabul link, was created by "Swiss Skies" in June 2003. But in fact, the major mover is a Waleed Youssef, air transportation engineer, air consultant, and partner in the Washington-D.C.-based consultancy, The Berkeley Group. Youssef is CEO of Swiss Skies. Swiss Skies is owned 76% by American investors - the other 24% is unknown. In 2002, the Berkeley Group had secured a consulting contract from the U.S. Government's Trade and Development Authority to analyze civil aviation in Afghanistan. The report was completed by Waleed Youssef and published in November 2002. Swiss Skies has contracted with World Airways to run the bi-weekly air service using MD-11s between Dulles and Kabul with a stopover in Geneva. Youssef is an enthusiast of airport privatization with much international airport consulting experience.

⁸ Mike Patterson, "Standard Chartered Step Marks Revival of Afghan Banking," Agence France-Presse [June 29, 2003 at 7:33 AM PDT]

⁹ "Afghanistan's \$ 30 Billion Investment Aim Starts at Textile Mill," Bloomberg.com [August 5, 2003], at: <http://quote.bloomberg.com/apps/news?pid=nifea&sid=aPms4VlaAFK8>

¹⁰ Paul Watson, "Afghan Aid Faces Hurdles," Los Angeles Times (September 1, 2003). In this article, Watson notes that Seidner has never managed an agricultural mega-project.

¹¹ for a glimpse into official "hype" regarding reconstruction, see <http://www.export.gov/afghanistan/commercial/sectors/transportation.html>

¹² see Danesh Kerokhel, "Investment Turn-Off," Institute for War and Peace Reporting [June 30, 2002]

¹³ where in fall 2001 300 Al Qaeda Arab fighters had set up camp.

¹⁴ "Attack on Road Construction Team Kills Six," IRIN News [September 1, 2003]

¹⁵ "OPIC Agreement Marks Start of Hotel Project in Afghanistan," OPIC Press release [June 9, 2003]

¹⁶ "American Small Business To Open Direct Air Link to Kabul," U.S. Department of State International Information Programs [June 27, 2003]

¹⁷ "Afghanistan Joins Agency to Provide Risk Insurance for Investors," Agence France-Presse [July 4, 2003 at 5:40 AM PDT]

¹⁸ "German Airline Criticized for Kabul Flights," DW - Deutsche Welle [September 1, 2003]

¹⁹ "ISAF Peace Contribution Drawing Business to Afghanistan: Karzai," Agence France-Presse [August 11, 2003]

²⁰ Diana Muriel, "Afghan Telecom Risk Paying Off," CNN.com/Business [October 28, 2002]

²¹ see Marc W. Herold, "An Analysis of the Historical Determinants of United States Investment in Latin American Manufacturing" [Berkeley, CA.: unpublished Ph.D dissertation in Economics, University of California, 1979], 680 pp. The appropriability theory of the multinational corporation was developed by Stephen P. Magee, see for example "Multinational Corporations, the Industry Technology Cycle and Development," Journal of World Trade Law 11 [1977]: 297-321.

²² from <http://www.austecprecision.com/Afghanistan2003.html>