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The World Bank

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Report No. 115097-AF

INTERNATIONAL DEVELOPMENT ASSOCIATION

PROGRAM DOCUMENT FOR A PROPOSED DEVELOPMENT POLICY GRANT

IN THE AMOUNT OF SDR 73 MILLION
(US$100 MILLION EQUIVALENT)

TO

THE ISLAMIC REPUBLIC OF AFGHANISTAN

FOR THE

INCLUSIVE GROWTH DEVELOPMENT POLICY OPERATION

May 15, 2017

Macroeconomic and Fiscal Management Global Practice
South Asia Region

Islamic Republic of Afghanistan
GOVERNMENT FISCAL YEAR
December 22 – December 21

CURRENCY EQUIVALENTS
(Exchange Rate Effective as of April, 2017)
Currency Unit
US$1.00 = AF67

ABBREVIATIONS AND ACRONYMS

ACBR	Afghanistan Central Business Registry
ACCA	Association of Chartered Certified Accountants
ACCA	Association of Certified Chartered Accountants
AF	Afghanis (Currency)
AFMIS	Afghanistan Financial Management Information System
Aftel	Afghanistan Telecom
AISA	Afghanistan Investment Support Agency
ALCS	Afghanistan Living Conditions Survey
ANPDF	Afghanistan National Development Policy Framework
ARAZI	Afghanistan Land Authority
ARTF	Afghanistan Reconstruction Trust Fund
ARTF IP	Afghanistan Reconstruction Trust Fund Incentive Program
ASA	Advisory Services and Analytics
ASIL	Adam Smith International Limited
ATRA	Afghanistan Telecom Regulatory Agency
BRT	Business Receipts Tax
CPF	Country Partnership Framework
CSO	Civil Society Organization
DAB	Da Afghanistan Bank
DABS	National Electricity Utility of Afghanistan
DiREC	Displacement and Return Executive Committee
DPO	Development Policy Operation
ECF	Extended Credit Facility
FPIP	Fiscal Performance Improvement Plan
GDP	Gross Domestic Product
GoIRA	Government of Islamic Republic of Afghanistan
HIPC	Heavily Indebted Poor Countries
IAS	International Accounting Standards
ICT	Information and Communication Technologies
IDA	International Development Association
IDP	Internally Displaced People
IFC	International Finance Corporation
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IPM	Integrated Pest Management
ISA	Investment Support Agency
MAIL	Ministry of Agriculture, Irrigation and Livestock
MCIT	Ministry of Communication and Information Technology

MOCI	Ministry of Commerce and Industry
MOE	Ministry of Education
MOF	Ministry of Finance
MTEF	Medium-Term Expenditure Framework
NATO	North Atlantic Treaty Organization
NEPA	National Environment Protection Agency
NPP	National Priority Program
NRM	Natural Resource Management
NRVA	National Risk and Vulnerability Assessment
PEFA	Public Expenditure and Financial Accountability
PFM	Public Financial Management
PFMR	Public Financial Management Reform
PFMRII	Second Public Financial Management Reform Project
PMP	Pest Management Plan
PPP	Public Private Partnership
SDR	Special Drawing Rights
SESA	Strategic Environmental and Social Assessment
SIA	Strategic Impact Assessment
UNAMA	United Nations Assistance Mission in Afghanistan
UNDP	United Nations Development Programme
USAID	United States Agency for International Development
USIP	United States Institute of Peace

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ISLAMIC REPUBLIC OF AFGHANISTAN

INCLUSIVE GROWTH DEVELOMENT POLICY OPERATION

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SUMMARY OF PROPOSED DEVELOPMENT POLICY GRANT AND PROGRAM

ISLAMIC REPUBLIC OF AFGHANISTAN
INCLUSIVE GROWTH DEVELOPMENT POLICY OPERATION

<table>
<tr><td>Borrower</td><td>Government of the Islamic Republic of Afghanistan</td></tr>
<tr><td>Implementation Agency</td><td>Ministry of Finance</td></tr>
<tr><td>Financing Data</td><td>IDA Grant: SDR 73 million (US$100 million equivalent)</td></tr>
<tr><td>Operation Type</td><td>Standalone Development Policy Operation</td></tr>
<tr><td>Pillars of the Operation
And Program
Development Objective(s)</td><td>The development objectives and pillars of the operation are: i) enhance the policy framework to expand access to economic opportunities for the vulnerable; and ii) strengthen the policy and regulatory framework for private sector development.</td></tr>
<tr><td>Result Indicators</td><td>
<table>
<tr><th>Indicator</th><th>Baseline</th><th>Target</th></tr>
<tr><td>• Border(s) issuing returnee certification.</td><td>1</td><td>4</td></tr>
<tr><td>• Landholders currently without formal land ownership records granted formal ownership under the new land management law.</td><td>0</td><td>500</td></tr>
<tr><td>• Gender disaggregated land records available under the ARAZI digital registration system.</td><td>No</td><td>Yes</td></tr>
<tr><td>• Share of land acquisitions for which there is media notice at least 6 months in advance of acquisition and social impact assessment is carried out.</td><td>0%</td><td>100%</td></tr>
<tr><td>• Registered non-bank electronic money institutions.</td><td>0</td><td>3</td></tr>
<tr><td>• Share of PPP transactions with invitations for expressions of interest published on PPP website.</td><td>0%</td><td>100%</td></tr>
<tr><td>• Percentage of fiber-optic network (by value of investment) under Aftel management</td><td>100%</td><td><80%</td></tr>
<tr><td>• Days taken to renew a business license.</td><td>120</td><td>25</td></tr>
<tr><td>• Afghan national and resident accountants with accredited under the Accountancy Law</td><td>~20</td><td>100</td></tr>
</table>
</td></tr>
<tr><td>Overall risk rating</td><td>High</td></tr>
<tr><td>Climate and Disaster Risks</td><td>(i) Are there short and long term climate and disaster risks relevant to the operation (as identified as part of the SORT environmental and social risk rating)? No
If yes, (ii) summarize briefly these risks in the risk section and what resilience measures may help address them? N/A</td></tr>
<tr><td>Operation ID</td><td>P160544</td></tr>
</table>

IDA PROGRAM DOCUMENT FOR A
PROPOSED DEVELOPMENT POLICY GRANT
TO THE ISLAMIC REPUBLIC OF AFGHANISTAN

1. INTRODUCTION AND COUNTRY CONTEXT

1. **The proposed standalone operation will provide US$100 million of IDA grants in support of reforms organized under two pillars**: i) enhance the policy framework to expand access to economic opportunities for the vulnerable; and ii) strengthen the policy and regulatory framework for private sector development. Resources provided through the standalone operation will help Government meet its development objectives as articulated in the new Afghanistan National Peace and Development Framework (ANPDF).

2. **Afghanistan is a deeply fragile and conflict affected state. It has been in almost constant conflict for over 35 years with no durable political settlement established.** This has had a destabilizing effect on social cohesion, exacerbating ethnic divisions and weakening government institutions and rule of law. GDP per-capita is among the lowest in the world, poverty is deep and widespread, and social indicators are still at very low levels. Given this context, the proposed operation is intended to support achievable and important reforms within a difficult reform context. Supported reforms will allow progress against, but cannot on their own resolve deep and long-running problems of fragility and aid dependence.

3. **Following a sustained period of impressive development progress after the fall of the Taliban, Afghanistan is currently undergoing a difficult adjustment.** With an influx of aid since 2002, Afghanistan sustained rapid economic growth and improvements against important social indicators for more than a decade. Annual growth averaged 9.4 percent between 2003 and 2012. Since the drawdown of international security forces in 2012, however, economic and social progress has substantially slowed. Aid flows decreased from around 75 percent of GDP in 2012 to 45 percent of GDP in 2015 (with the number of NATO troops declining from more than 130,000 in 2011, to around 15,000 by end-2014). Reduced aid and security presence led to a rapid weakening of demand, especially in construction and other service sectors, with follow-on impacts across the economy. Impacts were magnified by a disruptive and prolonged political transition following the disputed outcome of the 2014 election. Internal divisions within the National Unity Government slowed vital reforms and delayed the appointment of key officials, undermining policy certainty. Security has also deteriorated. There were around 3,500 conflict related civilian deaths and nearly 8,000 injuries in 2016, the highest on record. Reflecting falling confidence, annual firm registrations have declined by more than half since 2012 while unemployment has increased (from 13.5 percent in 2008 to 22.6 percent in 2014). With slowing economic activity, fiscal revenues declined from 11.6 percent of GDP in 2011 to 8.7 percent of GDP in 2014, before recovering slightly to 10.7 percent of GDP in 2016. The deteriorating security situation has also led to reversals and increasing disparities in access to services.

4. **Disparities in access to economic opportunities are both eroding recent gains against social indicators and contributing to fragility pressures.** Afghanistan currently faces a humanitarian crisis arising from large numbers of return migrants (approximately 800,000 in 2016) and a large and growing internally displaced population (1.2 million). Displaced populations require both immediate humanitarian assistance and support for longer-term reintegration, including access to services and economic opportunities.

Unmanaged and rapid urbanization is driving rapid growth of informal settlements, and risks overwhelming urban services. Despite rapid economic growth since 2001, poverty has remained stubbornly high, with the poverty rate increasing from 36 percent in 2012 to 39 percent in 2014. Increases in poverty have been concentrated in geographically and economically isolated regions – especially the Southwest. This period has also seen growing inequality, with real per capita consumption declining by 2 percent for the poorest 20 percent of the population, little change for the bottom 40 percent, and the richest 20 percent experiencing a 9 percent increase. There are also important disparities between rural and urban areas, with poverty rates about 16 percentage points higher in rural areas. Recent evidence from household surveys suggests that access to services is declining among the poor.

Figure 1: Poverty headcount ratio

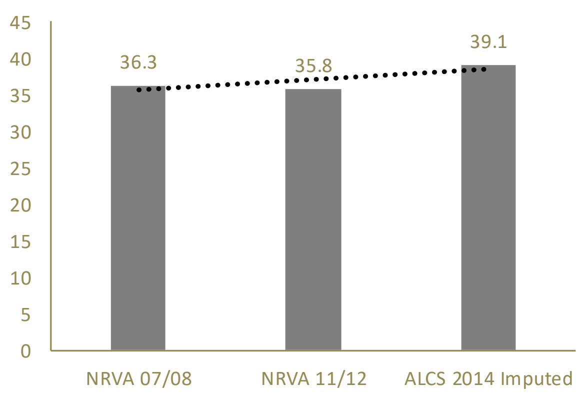
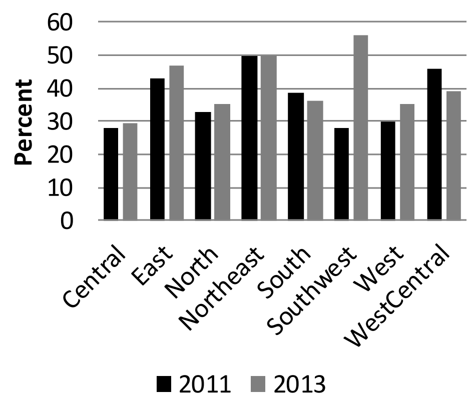


Figure 2: Poverty headcount ratio by region



5. **Private sector development is vital for Afghanistan's economic future.** With an undiversified productive base, the economy remains reliant on aid. The private sector is extremely narrow, with employment concentrated in low-productivity agriculture. Investment since 2001 has focused around the aid-driven contract economy. Private sector development is constrained by weak institutions, inadequate infrastructure, widespread corruption, and a difficult business environment (Afghanistan was ranked 183rd of 190 countries in the 2017 Doing Business Survey). Limited private sector activity presents important threats to macroeconomic stability over the medium-term, in the context of continued declines in aid. Foreign grants currently finance more than two-thirds of budget expenditure and substantial off-budget security needs. A large trade deficit, equal to around 38 percent of GDP in 2016, is also financed almost entirely by aid inflows. With aid expected to decline from around 46 percent of GDP in 2017 to 20 percent of GDP by 2030, and in the context of a rapidly growing population, new sources of growth, employment, revenues, and exports are desperately needed.

6. **The proposed operation complements the Afghanistan Reconstruction Trust Fund Recurrent Cost Window Incentive Program (IP).** The IP is the major channel for multi-donor policy-based recurrent cost support to the Government of Afghanistan, providing approximately US$400 million per year. Four prior actions (both land actions, electronic money regulation, and business license reforms) supported by the IP are also supported by this operation, mobilizing additional resources behind high-priority reforms. Four prior actions supported by the proposed operation are additional to those supported by the IP, either because: i) new windows of opportunity for reform have emerged since IP triggers were agreed; or ii)

reforms are beyond the scope of the IPs relatively narrow focus on fiscal management, civil service, and PFM.

7. **The choice of a standalone operation reflects elevated risks and intentions to move towards new modalities of budget support.** Given fluidity of the political and security situation, a programmatic series of Development Policy Operations was not considered appropriate at this time. Short-term political and security risks are elevated. Ongoing external security and civilian support was confirmed at the 2016 Warsaw NATO conference and the Brussels Conference on Afghanistan, but some uncertainties regarding external assistance remain given the fluid international environment and local security conditions. Further, the World Bank is considering options for regularizing the IP and consolidating the program with future IDA development policy operations. There is a current window of opportunity for reshaping Bank engagement through the IP, with the current IP program expiring in 2017.

2. MACROECONOMIC POLICY FRAMEWORK

2.1. RECENT ECONOMIC DEVELOPMENTS

8. **Afghanistan's recovery from the 2014 drawdown of international assistance has been slow.** Afghanistan sustained rapid growth between 2002 and 2014 driven by inflows of international assistance and associated expansion of the service sector and strong agricultural output. Real GDP growth slowed to 1.3 percent in 2014 and 0.8 percent in 2015, reflecting declining public sector spending, recovering only slightly to an estimated 1.2 percent in 2016. Continued slow growth reflects the impact of weak confidence on investment in the context of insecurity and political instability. Agriculture output is estimated to have declined by 0.5 percent in 2016, due to unfavorable weather conditions, curtailing consumption of the majority of Afghans dependent on agricultural income. Service and industry sectors recorded modest growth of 1.4 percent and 2 percent respectively.

9. **Afghanistan remains heavily aid dependent.** Aid flows to Afghanistan were equal to around 46 percent of GDP in 2016, financing a large share of both total civilian and security expenditures (85 percent and 75 percent, respectively). On-budget grants of around 16 percent of GDP finance nearly two-thirds of total budget expenditure of which is about 27 percent of GDP. High security expenditures (around 25 percent of GDP in 2016, including off-budget security costs) drive Afghanistan's overall high levels of public expenditure (56 percent of GDP in 2016). Government revenue-financed expenditures on security are equal to more than a third of total revenues, leaving revenues equal to only around 6.4 percent of GDP to finance non-security expenditure needs.

10. **Revenue policies have helped manage the impact of the drawdown of international security forces.** Domestic revenues fell to 8.7 percent of GDP in 2014 from a peak of 11.6 percent in 2011, as a result of economic slowdown and deteriorating governance in the context of political uncertainty around upcoming elections and the uncertain political impacts of the international security drawdown. Revenues recovered in subsequent years, however, due to a range of policy measures, including: i) rollout of the SIGTAS electronic tax system; ii) increased risk-based compliance measures in customs; iii) efforts to recover arrears, iv) an increase in the business receipts tax rate from 2 percent to 4 percent; and v)

introduction of a 10-percent telecommunications tax on mobile phone top-ups.[1] Improved revenue performance has continued into 2016, with revenues up 15 percent compared to the previous year. Customs duties, however, recorded no growth, likely due to weakening imports.

11. **Pressures are building on the expenditure side.** On-budget security expenditure has increased from 10 percent of GDP in 2012 to 11.1 percent of GDP in 2016, as government forces have taken on increasing responsibilities and insurgent activities have intensified. The share of the budget dedicated to (on budget) security expenditure has increased from 25 percent of total expenditures in 2006 to about 41 percent in 2016, and domestic revenues are now adequate to finance only two-thirds of civilian expenditures. Slight growth of on-budget non-security expenditure (around 1 percent of GDP since 2012) has been driven by increased operating and maintenance costs, as government takes control of donor-built assets, and a changing civil service salary structure. Despite pressures, the Government has run a largely balanced budget (including on-budget grants). The 2016 deficit was equal to only 0.2 percent of GDP and was financed from cash reserves and concessional borrowing. On-budget capital expenditure increased slightly from 3 percent of GDP in 2014 to 4.4 percent of GDP in 2016.

12. **Large security expenditure needs limit resources for other sectors that are vital for development. Security currently consumes around 40 percent of the budget. Infrastructure, education, and agriculture and rural development only received respectively 20 percent, 13 percent and 7 percent of the budget allocation in 2016. Health only received 6 percent of the total budget but the health system builds on a decentralized NGO delivery system, which is mostly externally financed by donor grants. Budget execution rates, however, remain low. The execution rate for the development budget was 54** percent in 2016, with poor execution driven by weaknesses in project selection and management, and delays in procurement. All budget documentation is available to the public and published online within a few days of submission to the National Assembly. In-year execution reports and end-year financial statements are also available.

[1] Af 14.5 billion of non-tax collections in 2016 were once-off including: i) the transfer of DAB profits; and ii) transfers from Kabul Bank and SOEs. However, there is robust underlying revenue growth estimated at around 4 per cent.

Figure 3: Contributions to growth by sector

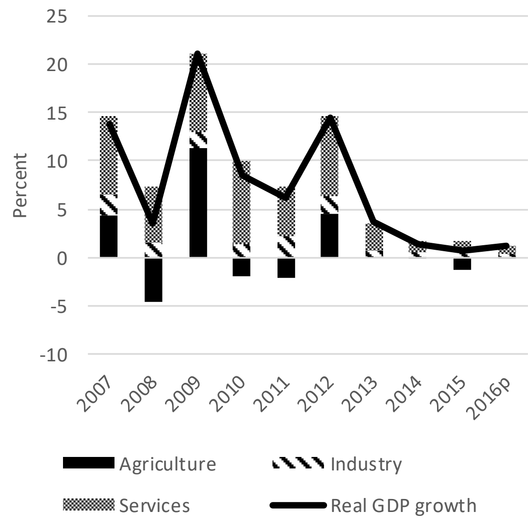
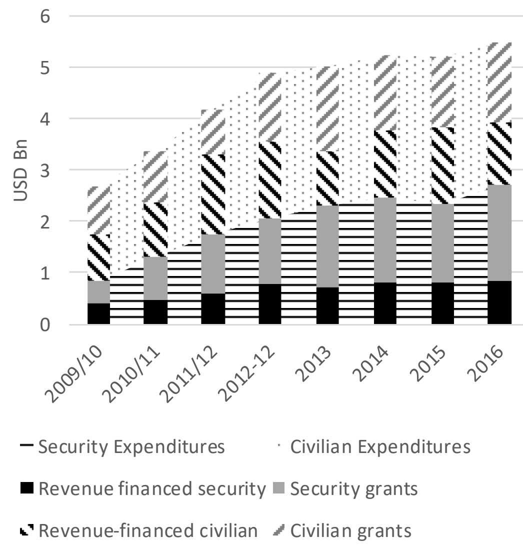


Figure 4: Expenditure and Revenues



13. **Inflation was negative in 2015 but picked up in 2016.** Inflation has remained moderate since the 2008 global food price surge (averaging around 6 percent per annum). After declining by 1.5 percent (period average) in 2015, driven by the fall in global commodity prices and weak domestic demand, prices increased by 4.4 percent in 2016. The increase was driven primarily by depreciation and food supply constraints associated with unfavorable weather conditions. High levels of dollarization and a narrow financial sector weaken monetary transmission channels. Reserve money is the nominal anchor. Inflationary pressures are strongly linked to import prices, reflecting the large import bill.

14. **The external reserve position is comfortable.** Exports (primarily dried fruits, nuts, and textiles) continue to grow, but slowly and from a very low base (around 6 percent of GDP in 2016). Imports have declined with reduced aid inflows, but remain at around 40 percent of GDP, reflecting Afghanistan's undiversified economy. Due to aid inflows, the current account remains in surplus (4.4 percent of GDP in 2016) and foreign exchange reserves remain at comfortable levels (9 months of prospective imports). The value of the Afghani depreciated by 10 percent against the US dollar during 2016 (period average) driven mostly by declining private foreign exchange inflows and slowing foreign direct investment.

15. **Afghanistan's financial sector remains underdeveloped and vulnerable.** Confidence in the banking sector is yet to fully recover from the Kabul Bank crisis of 2010, during which massive fraud led to a run on Afghanistan's largest Bank, necessitating a government bail-out and undermining confidence in the sector. Profitability of private banks remains marginal. Average return on assets across the banking sector was negative up until the end of 2015 but turned positive in 2016, while non-performing loans were equal to 10.8 percent of total gross loans at end-2016. Of three state-owned banks, only one is currently profitable, although the other two broke even in 2016. While banks are highly liquid, credit growth is sluggish due to risk aversion in the context of increasing insecurity and political uncertainty, relatively heavy collateral requirements, and a generally underdeveloped financial sector. Credit to the private sector expanded only by 6 percent in 2015 and 5 percent in 2016, which barely offset a 6.6 percent contraction in 2014. Only 10 percent of adults, one-third of informal firms, and two-thirds of formal firms have access to a bank account. Only around 2 percent of firms use bank loans to finance investment.

Government has recently committed to several measures to address financial sector weaknesses, including under the IMF Extended Credit Facility program. Efforts are underway to complete resolution of the 2010 Kabul Bank Crisis and revitalize the financial sector. Government is planning to transfer funds to the Kabul Bank Receivership to clear outstanding obligations, which will contribute to elimination of the Central Bank's continued lender-of-last resort exposure.[2] Government has also recently recapitalized the New Kabul Bank, allowing it to transition from a temporary bridge bank to an adequately capitalized and deposit-oriented institution. With World Bank support, Government is also progressing a program of regulatory, institutional, capacity-building, and infrastructure initiatives to expand access to finance.

Table 1: Central Government Operations

	2013	2014	2015	2016e	2017p	2018p	2019p
	In percent GDP, unless otherwise indicated						
Total revenues	25.5	24.4	25.2	26.7	28.2	28.5	28.9
Domestic revenues	9.7	8.7	10.2	10.7	11.0	11.2	11.6
Direct taxes	4.6	4.5	4.9	5.2	5.2	4.9	3.9
Indirect taxes	2.5	2.3	2.5	2.5	2.6	2.7	2.7
Nontax revenues	2.5	1.9	2.7	3.1	3.2	3.6	4.1
Donor grants	15.8	15.7	15.0	15.9	17.2	17.3	17.3
Security	7.7	8.2	7.9	8.7	9.8	9.9	9.9
Civilian	8.1	7.5	7.1	7.2	7.4	7.4	7.4
Total expenditures	25.3	26.2	26.5	26.9	28.2	29.4	29.7
Security	11.3	12.2	12.0	11.1	11.4	11.8	12.0
Civilian	13.9	14.0	14.5	15.8	16.8	17.6	17.7
Wages and salaries	4.2	4.6	4.5	4.5	4.6	4.7	4.8
Operations and maintenance	5.1	4.6	4.5	5.2	5.5	5.8	6.0
Capital expenditures	3.6	3.0	3.9	4.4	4.9	5.3	5.0
Social transfers	0.9	1.7	1.6	1.7	1.7	1.8	1.8
Interest payment	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Overall balance	0.2	-1.8	-1.3	-0.2	0.0	-0.9	-0.8
Overall balance excluding grants	-15.6	-17.5	-16.4	-16.1	-17.2	-18.2	-18.1
Borrowing	0.1	0.2	0.1	0.1	0.1	0.6	0.0
Change in Government deposits	-0.3	1.6	1.2	0.1	-0.1	0.3	0.8

Source: Bank staff estimates

[2] MoF underwrote DAB's lender-of-last resort liability to Kabul Bank with a promissory note. Around US$343 million remains to be paid.

Table 2: Selected Economic Indicators

	2012	2013	2014	2015	2016e	2017p	2018p	2019p
Real economy								
Nominal GDP (billion Af) /1	1,061	1,133	1,151	1,205	1,313	1,433	1,566	1,695
Nominal GDP (billion US$) /1	20.5	20.5	20.0	19.6	19.4	20.7	22.2	23.6
GDP per capita (US$)	691	666	634	604	580	606	635	660
Population (million)	29.7	30.7	31.6	32.5	33.4	34.2	34.9	35.7
Real GDP growth /1	14.4	2.0	1.3	0.8	1.2	2.4	3.4	3.1
Prices								
CPI inflation (period average)	7.2	7.7	4.6	(1.5)	4.4	6.0	5.0	5.0
Fiscal								
Total Revenue and Grants	69.8	68.4	60.6	55.1	56.4	54.1	52.2	50.8
Domestic revenues	10.3	9.7	8.7	10.2	10.7	11.0	11.2	11.6
Grants	59.2	58.6	51.8	44.9	45.6	43.1	41.0	39.2
Security grants	37.1	34.2	29.3	21.9	23.0	23.4	22.4	21.8
On-budget	6.3	7.7	8.2	7.9	8.7	9.8	9.9	9.9
Off-budget	30.8	26.5	21.1	14.0	14.3	13.6	12.5	11.3
Civilian grants	22.1	24.4	22.5	22.9	22.6	19.7	18.6	17.4
On-budget	6.5	6.7	7.3	7.0	7.2	7.4	7.4	7.4
Off-budget	15.7	17.8	15.1	15.9	15.4	12.1	10.7	9.4
Total Expenditures	70.3	69.5	62.4	56.4	56.3	55.8	56.7	56.5
Security spending	40.9	37.8	33.3	26.0	25.2	26.9	28.4	29.5
Off-budget security	30.8	26.5	21.1	14.0	14.1	15.5	16.6	17.5
On-budget security	10.0	11.3	12.2	12.0	11.1	11.4	11.8	12.0
Civilian spending	29.4	31.7	29.1	30.4	31.2	28.9	28.3	27.1
Off-budget civilian	15.7	17.8	15.1	15.9	15.4	12.1	10.7	9.4
On-budget civilian	13.7	13.9	14.0	14.5	15.8	16.8	17.6	17.7
Budget deficit	-0.8	-1.2	-1.9	-1.4	-0.2	0.0	-0.9	-0.8
Budget deficit excl. grants	-13.5	-15.6	-17.5	-16.4	-16.1	-17.2	-18.2	-18.1
External Sector								
Exports of goods (million US$) /2	640	729	783	667	687	769	888	1059
Imports of goods (million US$) /3	10,054	9,244	8,711	7,867	7,986	8,262	8,566	9,310
Trade balance	-45.8	-41.6	-39.6	-36.7	-37.7	-36.2	-34.6	-35.1
Net current transfers	52.0	49.0	47.5	41.7	39.0	34.4	31.4	29.9
Current account balance	6.2	7.4	8.0	5.0	4.4	3.4	1.0	-1.0
Gross foreign exchange reserves (million. US$)	6,771	7,447	7,360	6,864	7,255	7,500	7,600	7,700
Gross foreign exch. res. (months of imports)	7.2	7.8	9.8	9.0	10.9	10.9	10.6	9.9
External debt	6.6	6.7	6.5	6.3	6.4	6.4	6.1	5.9
Exchange rate (AFN/USD, period average)	51.7	55.4	57.4	61.4	67.9	..	..	..
Monetary								
Broad money (M2)	32.0	33.0	34.9	34.4	34.7	35.0	35.2	35.4
Total deposits	17.6	17.6	17.7	17.5	17.7	17.9	18.4	19.5
Credit to private sector, commercial banks	4.1	4.2	3.8	3.9	3.5	3.8	4.4	4.6

1/ National Accounts data exclude opium value added.
2/ Exclude sales of goods to nonresidents in the country.
3/ Include estimated unofficial trade or smuggling.

Source: Bank staff estimates.

2.2. MACROECONOMIC OUTLOOK AND DEBT SUSTAINABILITY

16. **Growth prospects are limited in the short-run.** Growth is projected to pick up slightly to 2.4 percent in 2017, increasing to 3.4 percent in 2018. Slow growth in 2017 reflects weak confidence amid a deteriorating security environment, and expected poor agricultural performance. Slightly stronger growth in out-years is predicated on improvements in security, political stability, reform progress, and continued high levels of aid. The poverty rate is expected to remain high due to weak labor demand and security-related constraints to service delivery, despite some offsetting positive impacts from improvements to the performance of the agriculture sector and lower food prices.

17. **The fiscal outlook is challenging, and outcomes are sensitive to the level and modality of aid commitments.** The 1396 Budget is expected to balance and will see an increase in expenditures of around 1.2 percent of GDP, driven by increased on-budget civilian expenditures. Increased expenditures will be financed by a combination of increased on-budget grants and increased tax revenues, reflecting ongoing improvements in compliance. Expenditures are expected to further increase to 29.7 percent of GDP by 2019, with security spending previously undertaken directly by international partners being moved on budget. Growing non-security expenditure reflects maintenance of current service levels to a growing population, essential infrastructure, and necessary maintenance of aid-financed assets recently transferred to government ownership. If government can sustain recent improvements in compliance and administration, domestic revenues are projected to increase from 10.7 percent of GDP in 2016 to 11.6 percent by 2019. Fiscal sustainability analysis undertaken by the World Bank suggests that non-security aid commitments will be sufficient to meet growing expenditure needs, but only if these resources are tightly aligned with government priorities and with a growing proportion delivered through the budget. At current expected aid levels there is very limited fiscal space over coming years for programs to stimulate aggregate demand and spur increased growth.

18. **Prices are expected to remain stable and the current account to remain in surplus.** Inflation is expected to remain at around 5 percent and within the Central Bank's target range. The current account surplus is expected to turn to a deficit of around 1 percent of GDP by 2019, driven by declining aid. Credit to the private sector is expected to grow modestly. Impacts of slow growth and weak confidence will continue to constrain credit growth, despite efforts to support financial inclusion and improve financial sector corporate governance.

19. **Macroeconomic policies and priorities are appropriate to the challenging context.** The authorities have demonstrated capacity to respond appropriately to macroeconomic shocks. Policies during the drawdown of international security forces maintained price stability, with expenditure controls and revenue policy and administrative measures implemented to maintain deficits within sustainable levels. Government is currently working closely with the World Bank to improve alignment between the budget expenditures and policy priorities established in the Afghanistan National Peace and Development Framework (ANPDF) as well as improving the selection, assessment, and execution of development projects through strengthening systems for Public Investment Management (PIM). The new Fiscal Performance Improvement Program, implemented with World Bank support, is intended to further reinforce Afghanistan's resilience to shocks through strengthening a broad range of PFM functions, including revenue administration, procurement, audit, and core treasury functions. A stronger PFM system is also considered a perquisite for moving more aid on budget.

20. **Conditional on continued reform progress and realization of expected aid levels, Afghanistan's macroeconomic framework is adequate for the operation, but exposed to substantial downside risks.** Small deficits (after grants) are projected over 2018-2019, conditional on an increase in the proportion of aid delivered on-budget from 33 percent in 2015 to 44 percent by 2019.[3] This change is in line with current plans of development partners. Under any scenario, Afghanistan will rely on elevated levels of external assistance until at least 2030. Main macroeconomic risks now include: i) a premature withdrawal of aid, which would undermine fiscal sustainability and force difficult adjustments on the expenditure side; ii) further deterioration in the security environment, which would undermine confidence and further slow growth; and iii) political instability which would have highly unpredictable impacts on the security situation, business confidence, and external support. Continued progress with strengthening governance, improving revenue policies and administration, and establishing a conducive environment for private sector growth underpin longer-term sustainability. Mobilization of required aid will continue to depend on adequate performance in implementing required structural reforms under the Self-Reliance through Mutual Accountability Framework.

21. **Structural transformation is required for long-term macroeconomic sustainability.** With an average annual population growth rate of 3 percent and an estimated 400,000 individuals entering the labor market each year, much higher growth rates are required to improve per capita incomes and provide quality employment opportunities for the expanding workforce. New sources of growth are needed to support government revenues in the context of expected normalization of aid levels over the longer-term, and generate foreign exchange with which to finance Afghanistan's large import bill. Recent World Bank analysis suggests that, even under optimal revenue policy and administrative settings, the upper-bound revenue potential is equal to only around 17 percent of GDP due to the undiversified economy and continued heavy reliance on subsistence agriculture. This contrasts with expenditure needs expected to remain above 35 percent of GDP until 2030. Given low levels of human capital, substantial infrastructure deficits, and weak institutions, opportunities for structural transformation are limited in the short-term but – over the longer term – Afghanistan has substantial potential in agriculture, extractives, and through leveraging its geographical location through energy and ICT connectivity.

22. **Afghanistan is at high risk of debt distress under the World Bank/IMF Debt Sustainability Framework.** The most recent World Bank/IMF debt sustainability analysis was published in July, 2016. Afghanistan is classified at high risk of debt distress despite very low levels of public debt (7 percent of GDP), all of which is external and comprises mostly of highly concessional debt to multilaterals. The "high" risk rating is driven by the inclusion of a customized "low grant" scenario which illustrates the sensitivity of Afghanistan's debt sustainability to the continued availability of external grants. While there are no breaches of any policy thresholds under the baseline, the customized scenario shows significant and sustained breaches of the PV-of-debt-to-exports ratio (more than 150 percent by 2030) and a marginal breach of the PV-of-debt-to-GDP ratio towards the end of the forecast period. The customized scenario is predicated on a change in the financing mix, with 15 percent of grants (included under the baseline) replaced by external borrowing from 2019. The customized scenario illustrates that, despite low levels of debt and no breaches of thresholds under the baseline, Afghanistan's external debt sustainability remains subject to substantial downside risks, including aid shortfalls, the fragile security situation, political uncertainty, domestic revenue shortfalls, and exchange rate depreciation.

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[3] Small deficits include limited concessional borrowing for infrastructure projects (around 0.1 percent of GDP per year).

Figure 5: PV of debt-to-GDP ratio

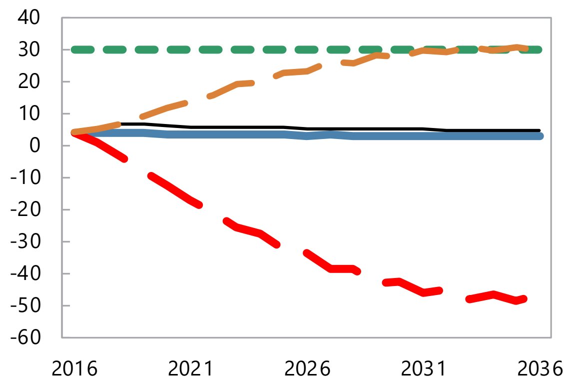
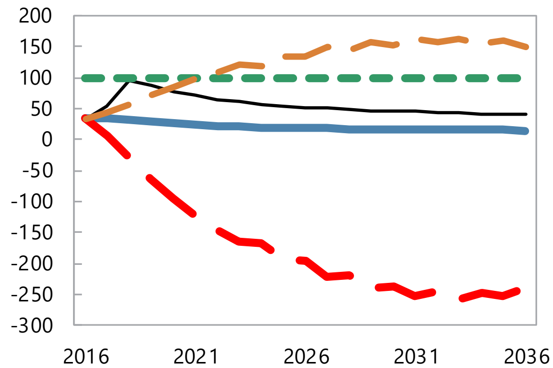


Figure 6: PV of debt-to-exports ratio



2.3. IMF RELATIONS

23. **Afghanistan's macroeconomic policies are supported by the IMF under an extended credit facility program.** Afghanistan agreed a US$44.9 million three-year Extended Credit Facility (ECF) program with the IMF in July, 2016. The first program review will be considered by the IMF Board in May, 2017. The program aims to consolidate recent gains in macroeconomic management and structural reform and catalyze donor support. In relation to fiscal management, the program supports tax administration and policy reforms, improvements to budget formation and execution, and strengthened cash controls and commitment management. In relation to financial sector, the program supports improvements to the central bank's regulatory and supervisory framework. The program also supports resolution of Kabul Bank crisis legacies (as discussed above), new anti-corruption measures, and further reforms to the AML/CFT framework. IMF and IDA staff are collaborating closely, and reforms supported by the proposed operation are aligned with and complementary to those supported by the IMF program.

3. THE GOVERNMENT'S PROGRAM

24. **Strategic vision.** The strategic vision of the government is outlined in the document "Towards Self-Reliance: Commitments to Reform and Renewed Partnership" presented at the London Afghanistan Conference in December 2014, and the recently circulated draft National Peace and Development Framework (ANPDF). This vision is based on greater government ownership of the development process, a more equal government-donor partnership, and a greater proportion of aid provided as discretionary budget assistance. The main instruments for implementation of the strategy are the national budget and 12 National Priority Programs (NPPs).[4] The main priorities identified in the ANPDF are: i) improving

[4] These are: (i) National Infrastructure and Connectivity program; (ii) Citizen Charter program; (iii) Rural Development; (iv) National Economic Empowerment; (v) Justice Sector Reform; (vi) Effective governance program; (vii) Private sector development (banking reform, small and medium enterprises, investment climate, trade and informal sector); (viii) human capital development; (ix) Urban development program; (x) Revenue enhancement program (tax and non-tax revenue); (xi) Comprehensive agricultural development program; and (xii) National Mineral and resource development program.

governance and state effectiveness through public sector reform, rooting out corruption and strengthening subnational governance; ii) building social capital and nation building through reforming the justice sector and building national identity; iii) economic growth and job creation through a comprehensive agriculture development program, private sector–led development program, mineral and resource development, and energy and infrastructure development as well as promoting regional integration, improving human resource skills, and urban development; and iv) poverty reduction and social inclusion through improving the quality of health and education programs, implementing the Citizens Charter program, and national gender strategy, including the women's economic empowerment national program. The ANPDF also emphasizes the need to support returnees and the internally displaced through approaches that realize their potential human capital contribution and respect their civil, economic, social, and political rights.

4. THE PROPOSED OPERATION

4.1. LINK TO GOVERNMENT PROGRAM AND OPERATION DESCRIPTION

25. **The proposed standalone development policy operation supports reforms intended to contribute** to the development objectives of the new ANPDF. Policy reforms supported by the proposed operation will contribute to priorities i) and iii) of the ANPDF, and are aligned with National Priority Programs. The two pillars of the proposed operation are:

- **Pillar one: enhance the policy framework to expand access to economic opportunities for the vulnerable.** Reforms under the first pillar are intended to broaden access to economic opportunities to excluded populations in Afghanistan, including returnees, the internally displaced, the rural poor, and newly urbanizing populations. Reforms include: i) adoption of a policy guiding response to the current Internally Displaced Person (IDP) and returnee crisis; ii) reforms to the legal governance framework for land management and public land acquisition; and iii) establishment of a regulatory framework to support financial inclusion through e-money.
- **Pillar two: strengthen the policy and regulatory framework for private sector development.** Reforms under the second pillar will contribute to improvements in policy conditions for private sector investment, supporting job-creation, growth, and increased revenues over time. Reforms include: i) the adoption of a policy governing public-private partnerships; ii) reforms to allow private investment in new telecommunication technologies; iii) reforms to the business licensing process; and iv) the establishment of a legal framework for accounting practice and the accountancy profession.

26. **The operation design reflects lessons learned from previous development policy operations in Afghanistan.** Previous experience has demonstrated that: i) DPOs can provide an effective means of focusing government policy attention and capacity on vital reforms even in contexts of elevated risk and uncertainty; ii) standalone operations may be an appropriate response to elevated political risk and have achieved satisfactory results through strategically focusing on important reforms that can be implemented over the short-term (programmatic operations supporting sequential reforms have sometimes been adversely affected by realization of political risks and changes in government priorities); iii) reform progress is heavily dependent on avoiding overly-ambitious and complex reform programs and ensuring availability of technical assistance to reform implementation, given thin capacity within government; and iv) government ownership of the reform agenda is vital.

27. **Supported reforms are aligned with ongoing technical assistance and other engagements.** The World Bank has been working closely with Government on the policy response to the current IDP/returnee crisis, including through the Citizen's Charter program. World Bank technical reviews have informed revisions to Land Management and Land Acquisition Laws and implementation support will be provided through new recipient-executed technical assistance engagement. World Bank technical assistance has informed the development of the PPP policy and a new operation is being developed to support implementation. Tax and telecommunication reforms were supported by USAID in close collaboration with World Bank teams. The accountancy law was developed with technical assistance support provided by USAID and under the World Bank PFMRII project. The proposed operation is complementary to, and supports selected reforms supported by, the ARTF Recurrent Cost Window Incentive Program and the World Bank's broader engagement in Afghanistan (See Box 1).

Box 1: Complementarity of Bank engagement with the proposed DPG

The proposed operation is supported by a range of activities within the broader engagement of the World Bank in Afghanistan.

Land governance reforms: The World Bank is planning a TECHNICAL ASSISTANCE FOR AFGHANISTAN INDEPENDENT LAND AUTHORITY (ARAZI) project which will aim at strengthening ARAZI's capacity to implement the two laws supported by this operation. The ongoing Urban Development Support projects provides assistance ARAZI, MUDH, IDLG and the five participating municipalities to better address this fast growing demand for land administration support. ARAZI is also receiving substantive support through other partners and has been systematically partnering with institutions such as UN-Habitat and the Turkish Land Administration Agency to develop systems for the allocation of occupancy certificates and prepare a five-year strategic development plan.

IDP and Returnees: The Government and development partners are coordination their response to the surge in IDP and returnee's through the Displacement and Return Executive Committee (DiREC). The World Bank co-chairs the technical working group on Finance, together with the Ministry of Finance. In terms of direct assistance, the World Bank supports additional financing to the Citizens' Charter Afghanistan Program (CCAP) to assist host communities for returnees. This intervention is expected to be followed by a larger stand-alone regional operation to address medium-term reintegration into the communities. In addition, the World Bank is conducting analytical work on forced displacement through analysis of the socio-economic profile of returnees, internally displaced persons and host communities, a representative tracking survey of returns and geospatial data.

ICT, Financial Inclusion, PPP and Business Licensing: A wide range of World Bank Group technical assistance activities will support the implementation of the other reforms under this operation including through the on-going Afghanistan Business Licensing Project (IFC Advisory), the Afghanistan ICT Sector Development Project (P121755), the upcoming Access to Finance Project as well as the planned PPP project.

Policy dialogue: Relevant policy dialogue is structured around the ARTF Incentive Program (IP), the preparation of the upcoming development policy operation, and supervision of the proposed operation. The IP was established in 2008 to support a policy reform agenda under the Afghanistan Reconstruction Trust Fund (ARTF) Recurrent Cost Window. Since then the IP has provided a vital foundation for policy dialogue, and has proven a successful vehicle for supporting reforms and their implementation. IP funds are from ARTF (which does not include IDA) resources and can be used to flexibly finance recurrent, civilian public expenditures. Generally, the IP is defined as a 3-year program and consists of three components that determine disbursements: (i) the Revenue Matching Grant, through which recurrent cost support is provided on the basis of achievement of revenue mobilization targets; (ii) the Structural Reform Scheme, through which recurrent cost support is mobilized against the achievement of structural reform actions; and (iii) the Operations and Maintenance Facility (launched in 2013), through which additional resources are provided against marginal increases in government allocations to operations and maintenance. The Ministry of Finance is the main implementation partner of the

IP and coordinates the cooperation with participating Ministries. The World Bank, in collaboration with ARTF donors, provides technical support to the implementation of reforms under the IP. An independent "monitoring agent" audits expenditures financed through the IP to ensure that resources are used only for eligible items. The IP has achieved significant success in supporting government's reform agenda, with the flexibility of the instrument well-suited to fragile contexts where reform trajectories are seldom linear or predictable.

Reforms currently being pursued under the IP cover a range of policy areas, including revenue and tax administration and policy reform, land governance reforms, pension reform, PFM reform, and sub-national fiscal relations. The proposed operation is complementary to the IP. In turn, the IP will continue to support the policy dialogue of these reforms throughout the implementation of the reforms.

4.2. PRIOR ACTIONS, RESULTS AND ANALYTICAL UNDERPINNINGS

Pillar 1: Enhance the policy framework to expand access to economic opportunities for the vulnerable

Prior Action #1: *The Recipient's Cabinet has approved a cross-government policy framework guiding a coherent policy response to the current displacement and returnee crisis*

28. **Afghanistan is facing a crisis arising from influx of returning migrants and growing internal displacement.** In response to civil conflict and repression, millions of Afghans left Afghanistan between 1979 and the fall of the Taliban. Since 2001, refugees have steadily been returning and an estimated 20 percent of Afghanistan's population are now returnees. The pace of returnee arrivals has increased over the past year due to changes of policies in regional and international migrant destination countries, particularly Pakistan, with increasing numbers of involuntary migrants. Nearly a million returnees are estimated to have arrived in Afghanistan in 2016, mostly from Pakistan and Iran, and the number of returnees is expected to increase to as many as 1.7 million during 2017. Reflecting widespread conflict, an estimated 1.2 million Afghans are currently internally displaced. 33 out of 34 Provinces are producing Internally Displaced People (IDPs), but most displacement is occurring in areas most effected by conflict, especially in the Southern region. All Provinces are now hosting displaced populations.

29. **The pace and extent of influx presents important short- and long-term challenges.** First and foremost, Government is dealing with immediate humanitarian challenges as it seeks to support and coordinate with development partners to meet the immediate needs of mobile populations. Risks to security and development outcomes are also apparent. Previous evidence has shown that regions experiencing the greatest influx of returnees experience heightened conflict pressures. Evidence is also clear that displaced populations are more likely to be unemployed and underemployed, and less likely to have children enrolled in school. Evidence also suggests that communities hosting IDPs and returnees may be reaching their limits in terms of absorptive capacity, with the incidence of secondary displacement steadily increasing. The incidence of internal displacement among refugees returning in 2013 is twice as high as compared to in 2002, despite the fact that returnee numbers were 50 times greater in 2002.

30. **In the absence of a unified policy, risks accompanying displacement are elevated.** The logistical, administrative, and coordination challenges associated with returnee influx and internal displacement are daunting. The WBG and other donor agencies are working with government in responding to the current crisis. The WBG is mainstreaming IDP and returnee response into ongoing Bank projects, including service provision to internally displaced and returnee populations through education and health sector engagements, and providing new employment opportunities through labor intensive public works under transport sector engagements. Through the Citizens' Charter program, the World Bank is providing additional resources for basic services to those communities most impacted by an influx of returnees and

IDPs. World Bank analytical work is also providing a vital foundation for the design of broader policy and programming responses.[5] While there has been substantial investment in coordination, some important issues have arisen regarding the alignment of approaches to registration of returnees, packages of assistance, and access to services, with no unified policy guiding the actions of multiple international and government agencies. The absence of a single database recording returnees is inhibiting data collection and targeting of assistance. Unevenness in packages of financial assistance to returnees is leading to equity concerns. Exclusion of returnees and the internally displaced from social services due to lack of documentation presents challenges to reintegration, human capital development, and longer-term outcomes. Absence of economic opportunities for returnees threatens increased poverty and hardship. Returnee influx and internal displacement in the context of current weaknesses in land administration increases risks of disputes and conflict. Conflict risks could be magnified in the absence of an overarching policy framework, as inequitable treatment of different groups resulting from fragmentation in response may lead to grievance or perceptions of deliberate favoritism.

31. **The Policy Framework for Returnees and IDPs will guide a coherent response across government agencies and the international community.** As a prior action for the proposed operation, the High Council on Refugees – chaired by the President – has approved an overarching policy to guide a coordinated government response. The Policy Framework constitutes a clear statement of overarching Government policy to guide the action of all development partners and government agencies. The Policy Framework recognizes the constitutional rights of returnees and IDPs as citizens of Afghanistan. It is based on core principles of voluntariness for all IDPs and returnees, with no measure under the policy involving any type of coercion and all measures intended to support the dignity and rights of displaced populations. The Policy Framework includes the following policy principles: i) ensuring a single policy framework will govern humanitarian and development assistance for returnees and IDPs; ii) establishing 100 per cent registration for all undocumented returnees arriving through major border points with Pakistan and Iran; iii) provision of identity documentation will be prioritized to facilitate access to basic services; iv) facilitation services will be provided to those who are willing to move their businesses to or reestablish their businesses in Afghanistan; v) a "whole of community" approach will be followed wherever possible, ensuring hosts are eligible for humanitarian and development assistance so as to avoid the emergence of conflicts or contestation between displaced groups and host communities; vi) financial packages provided by national and international agencies and foreign governments will be reviewed to ensure sustainability and harmonization to avoid inequities in treatment; vii) access to land will be prioritized following identification of suitable sites and broader improvements in security of tenure through legal reforms (see prior action ii); and viii) settlers will be assisted to join local representative bodies to ensure representation of their concerns and needs.

32. **The Policy Framework also establishes a governance mechanism to ensure coordinated implementation.** The Cabinet and Council of Ministers manage overall implementation of the policy, but have formally delegated various implementation responsibilities to sub-committees in order to facilitate timely decision-making and reduce the administrative and decision-making burden on Cabinet. These delegated sub-committees have the authority to coordinate action of government agencies and donors and provide information and advice to Cabinet relevant to their respective areas. A sub-committee of the Council of Ministers leads at the policy level, supported by and providing guidance to a Displacement and

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[5] World Bank and UNHCR (2016) "Fragility and Population Movement in Afghanistan" available at: http://documents.worldbank.org/curated/en/315481475557449283/pdf/108733-REVISED-PUBLIC-WB-UNHCR-policy-brief-FINAL.pdf.

Returnees Executive Committee comprising senior officials from relevant government and development partner agencies. The Executive Committee is supported, in turn, by three working groups providing policy advice, coordination, and oversight support and comprised of representatives from relevant government and development partner agencies (a policy support group will provide policy analysis and advice, a technical support group will provide support and coordination of implementation, and financing support group will identify and help meet resourcing needs). This structure will ensure that the Policy Framework can guide all relevant decisions while facilitating information flows from across government and development partners to the policy level. Government is now also working on an Implementation Plan, drawing on input from various committees, to ensure that the principles embedded in the Policy Framework are effectively translated into coordinated action.

33. **Results and results indicator.** Overall, this action will ensure a coordinated response to the current IDP and returnee crisis and implementation of specific measures to improve access to services and provision of vital support to effected communities. An important expected result will be establishment of information systems for recording returnee flows and the issuance of identification documentation to migrant populations to facilitate access to services. Recording of returnee flows and issuance of certification provides a vital foundation for both ensuring that returnees can access services and that an evidence base is generated through which broader outcomes can be tracked over time. At the baseline for the operation, certifications were being issued only at the Torkham crossing, which was used by only around 60 percent of returnees. Increasing the number of border crossing at which certifications are issued will allow the vast majority of returnees to be issued with certifications (estimated at more than 80 percent). The relevant results indicator is: *The number of border crossings at which returnee certificates are issued increases from 1 in mid-2016 to 4 by end-2018.*

Prior Action #2: *The Recipient's Cabinet has approved and submitted to the National Assembly a Land Management Law intended to improve security of tenure for the various categories of land users and provide more accessible procedures for formal titles to be issued, including to communities and investors.*

34. **The WBG has been working in close partnership with Government to improve land governance in Afghanistan for over a decade**. The World Bank has provided technical assistance to the land management agency and supported policy reforms under a previous Development Policy Operation, through investment projects, and through the ARTF Incentive Program. Specifically, the Government has been working with the World Bank and other development partners since 2007 to: i) strengthen the institutional framework for land management through strengthening the mandate of the independent land management authority (ARAZI); ii) develop and publish a land management policy outlining key principles and objectives to drive future reforms, with an emphasis on tenurial security and an end to land-grabbing; iii) build institutional capacity within ARAZI through international technical assistance support; and iv) build the analytical basis for improving the legal framework for land management, including through several assessments of existing laws, development of new legislation, and development partner-supported expert technical reviews of draft legislation (see Annex 6). A recent Land Governance Assessment undertaken by the WBG has identified substantial ongoing weaknesses in the current institutional arrangements for land management that can only be addressed through substantial legislative reform.

35. **Analytical work has demonstrated that the current legal framework is inadequate to protect tenurial security and facilitate efficient use.**[6] Absence of an institutional and legal framework providing clarity and protection of property rights is an important driver of land-related conflict. Only around 30 percent of urban properties and 10 percent of rural properties have been registered by official institutions. The existing legal framework provides inadequate recognition of land rights for those without formal documentation, with land ownership defaulting to the state when land ownership cannot be proved. Even for land that has been registered, the existing legal framework, set out in the Land Management Law of 2008, does not provide a clear classification of land types and land uses, leading to a lack of clear property rights, impeding investment and transactions, and generating scope for dispute. Property owners are responsible for surveying their own land. Registering ownership is burdensome, requiring documentation that is seldom available to landowners. This requirement has particularly negative consequences for women, who are less likely to possess formal documentation (only 2 percent of Afghan women currently hold formal ownership of land). The existing legal framework has also facilitated "land grabbing" due to failure to criminalize the practice and by failing to provide clear property rights to those without formal documentation. Registration relies on the overloaded and often corrupt court system, which has caused major delays and imposed high costs.

36. **Conflict and contestation over land arises in relation to intra- and inter-communal disputes over agricultural land, disputes over customary land rights, growing informal settlements, and a history of land-grabbing by powerful individuals.** Survey evidence suggests increasing concern regarding land disputes since 2002, with 50 percent of respondents to one survey citing land disputes as a major source of insecurity.[7] Almost 240,000 hectares of state lands have been expropriated by political and economic elites since the fall of the Taliban. Agricultural development and rangeland rehabilitation is constrained by a lack of clear tenure rights, with negative impacts for the 50 percent of households (and 80 percent of the poor) who rely on income from agriculture.

37. **Land administration represents an opportunity and a risk in the context of current demographic changes.** The current IDP and returnee crisis is increasing risks related to inadequate land management, with population influx to both urban and rural areas placing pressure on land and potentially driving conflict – especially in the context of already-rapid urbanization (the urban population is growing at 5.2 percent per year). The capacity of returnees and urban arrivals to successfully access land for occupation and livelihoods will influence whether their potential economic contributions of newly-settled populations can be realized and the extent to which conflict and fragility risks will eventuate.

38. **Once fully implemented the Land Management Law will help strengthen property rights, especially for disadvantaged groups.** The proposed operation will support the approval by Cabinet and submission to the National Assembly of a revised Land Management Law. The law has been developed with extensive stakeholder engagement, is consistent with international good practice, and has been subject to several social impact assessments.[8] The law will substantially strengthen tenurial rights, especially for those currently lacking formal ownership. The law will provide a vital foundation for the ongoing Land Occupancy Certificate process through which IDPs, returnees, and newly-urbanized

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[6] World Bank (2013) Land Governance Assessment Framework Afghanistan: Final report. World Bank, Kabul; Gatson, E. and L. Dang (2015) Addressing land conflict in Afghanistan, United States Institute of Peace, Washington DC.

[7] Waldman, M. (2008) 'Community Peacebuilding in Afghanistan: The Case for a National Strategy', Oxfam International Report, 8, 9.

[8] Reshdya, S. (2017) "Comparative Analysis of the New Land Management Law of Afghanistan (2017)", World Bank, Kabul.

populations are provided with certified land rights over land that they are occupying. The new law will also strengthen the land rights of women. Key changes introduced by the law include:

i. A formal process for land survey and registration will be established with a comprehensive dispute resolution mechanism in place. Rather than land-owners being responsible for registering ownership through the court system, the land administration agency (ARAZI) will be responsible for surveying land and determining and recording ownership.
ii. Requirements for establishing ownership will be simplified to allow recognition of a broader range of documents and for this process to be overseen by ARAZI rather than the courts. ARAZI will be able to convert Sharia documents, state decrees, tax payment documents, water rights documents, and customary deeds into official ownership documents.
iii. Formal rights will be granted to those without any form of documentation who can demonstrate occupancy for at least 35 years. Land Occupancy Certificates – currently being issued to urban squatters including IDPs and returnees who do not possess documentary evidence of ownership and do not meet minimum time requirements to acquire land rights through occupation – will also be recognized under the law.
iv. Under the new legal framework marriage certificates will be recognized as evidence of ownership, increasing opportunities for women to obtain formal land ownership rights when land is included as part of the dower.
v. Types of land, ownership, and use rights will be clearly demarcated. By clearly demarcating land on the basis of its ownership and use, the potential for competing and uncertain property rights can be avoided.
vi. An effective framework for addressing land-grabbing will be established, with land grabbing defined and criminalized within the law. ARAZI is provided with an explicit mandate to identify illegitimately expropriated land and refer land grabbers for criminal prosecution.

39. **Fully implementing the new legal regime for land management will take time and involve risk.** Experience with land administration reform from other fragile states highlights potential challenges of implementation, including political opposition, manipulation of new laws and administrative processes by vested interests, and limited resources and capacity to enforce formal frameworks. These experiences are particularly relevant in Afghanistan, where government capacity and resources are stretched and state authority remains contested in some areas. These risks cannot be completely avoided, but new land legislation can be expected to deliver benefits over time for several reasons: i) the National Unity Government is strongly committed to reforming land administration and the law enjoys political support at the highest levels; ii) the new land administration agency (ARAZI) has strong technical capacity and ownership over the new law; iii) the new law will help address existing administrative constraints to land administration by transferring responsibility for establishing land property rights from the over-loaded court system to ARAZI. ARAZI has undertaken a governance vulnerability assessment for the new law, and alongside proposed legal reforms, ARAZI will establish a grievance redress system, including a complaints hotline, to mitigate any risks that new systems will be subject to abuse or elite capture. The grievance redress unit will have the mandate to investigate reported abuses and corruption in land administration, transactions, or public acquisition. A full discussion of risks and mitigation related to this action is presented in Annex 5.

40. **Results and results indicator:** Overall, changes to land management represent a substantial improvement on the status quo of inconsistent and ambiguous frameworks that deny tenurial security to many Afghans, especially the vulnerable. Over time and subject to effective implementation the new framework will help address constraints to economic participation facing economically disadvantaged

groups in both urban and rural areas. The results indicators for this action are: i) n*umber of landholders currently without formal land ownership records provided with formal ownership through the administrative processes established under the new land management law increases from zero to 500 by 2018; and ii) gender disaggregated records of land ownership are available under the ARAZI digital registration system.*

Prior Action #3: *The Recipient's Cabinet has approved and submitted to the National Assembly a Land Acquisition Law intended to ensure fairness and efficiency in the acquisition of land for public purposes.*

41. **Current laws relating to public land acquisition undermine tenurial security.** The existing legal framework for public land acquisition – as established in the Land Expropriation Law of 2000 – contributes further to uncertain property rights. The current law does not require those using land that is publicly acquired to be provided with compensation unless they possess formal records of ownership (70 percent of urban and rural landholders lack such documentation). The purposes for which land can be expropriated are not clearly explained, with the current law listing various types of project for which land could be acquired rather than the principles on which public expropriation would be justified. The law specifies that compensation must be paid by the state, but the scope of compensation is limited, and the law does not provide for compensation to those who may obtain beneficial use of the land without ownership. Compensation is to be paid on the basis of land quality and location, rather than taking into account other determinants of land value. Further, the law does not lay out any clear process for land acquisition or establish any appeal or dispute process, leaving full discretion with the Council of Ministers. Weaknesses in the current framework allow unjust evictions to occur, compensation to be insufficient, and local dissatisfaction to rise.

42. **The Recipient's Cabinet has approved and submitted to the National Assembly a Land Acquisition Law intended to help resolve problems with the current legal framework.** The Land Acquisition Law will address key weaknesses in the existing legal framework, protecting the rights of land-owners while also allowing for necessary public developments. The law has been reviewed by World Bank experts in the area of land management and is considered consistent with international good practices in regards to: i) establishing requirements to compensate affected populations; ii) mandating social and environmental impact assessments; and iii) achieving important improvements in transparency through publication of all land acquisitions. Key changes introduced by the law include: i) providing definitional and conceptually-based (rather than project-type) clarity regarding legitimate purposes of land acquisition; ii) establishing a clear and fair process for acquisition, with the role of relevant agencies and actors clearly determined, and the establishment of an appeals process; iii) establishing best-practice requirements for determining land values and required compensation; iv) ensuring needs-based acquisition, where land can only be acquired when in the interests of public welfare, and ensuring that acquired land can only be used for the purposes for which it was acquired; and v) introducing provisions on resettlement and rehabilitation, with provisions to protect food-security of any affected communities and recognizing rights of vulnerable occupants lacking formal ownership.

43. **Results and result indicator:** Through establishing sound processes for public land acquisition, government will be able to undertake necessary public works while protecting property rights and ensuring transparency and management of social risks. Under the new law: i) all land acquisitions will be publicized 6 months prior to acquisition to allow sufficient time for public consultation (including information regarding land to be acquired, the purpose of acquisition, and processes for objection and dispute); ii) social impact assessments will be carried out; and iii) compensation will be provided to

affected populations. The relevant results indicator is: *the proportion of land acquisitions for which public notice is provided through media at least 6 months in advance of acquisition and social impact analysis is carried out increases from zero percent to 100 percent by 2018.*

Prior Action #4: *The Recipient's Central Bank has issued and published new regulations governing Electronic Money Institutions supporting development of e-money systems and expanded access to financial services.*

44. **Lack of access to financial services is an important constraint to growth and poverty reduction in Afghanistan.** Only 10 percent of adults in Afghanistan have access to a transaction account, and only 4 percent use formal financial sector to save. Rural populations and other vulnerable groups are less likely to have access to financial services. Constraints to access to finance also have negative impacts on women, with women less likely than men to have access to financial services. Access is constrained by poor transport infrastructure and insecurity. Lack of consumer confidence is also an important factor given critical weaknesses in the legal and regulatory framework. Less than 1 in 20 firms in Afghanistan has a line of credit or a loan from a financial institution and less than 2 percent of firms reported having applied for a loan the previous year. Two thirds of informal firms and one-third of formal firms do not hold a bank account.

45. **Benefits of increased access to financial services are likely to be substantial in Afghanistan.** Increased access to financial services helps households and firms finance investments and manage shocks through access to credit and savings. Recent household surveys show households in Afghanistan are more likely to experience negative shocks than any other country in the world, with 88 percent of households experiencing at least one shock in 2013/14 and a larger proportion in insecure areas. More than a third of all households, and about half of households in the lowest wealth quintile use harmful coping strategies when impacted by negative shocks, suggesting that the risks faced by households – and especially poor households – are translating into reduced investment in human and physical capital, with potentially negative long-run consequences for growth and development. Evidence also shows that firms are heavily exposed to risks in Afghanistan, especially risks associated with fragility (15.5 percent of firms report crime-related losses, higher than any other country in South Asia).

46. **Government has recognized the importance of improving access to finance to support growth and poverty reduction and help firms and households manage fragility-related risks.** Government, with World Bank support, has established a taskforce to develop a National Financial Inclusion Strategy to address a broad range of constraints to financial inclusion, including regulatory, policy, capacity, and infrastructure constraints. Facilitating use of electronic money will be an important component of this strategy, given the potentially transformative role of electronic money systems in expanding access to financial services in the context of widespread insecurity and geographical constraints to the spread of conventional financial infrastructure. As a vital step, Afghanistan's Central Bank has issued and published regulations governing Electronic Money Institutions. The regulations provide a basic framework for an electronic money system by allowing non-bank institutions (e.g. telecom operators) to issue e-money and through systems that are compatible with and integrated into the overall payment system. The regulations also safeguard users against potential risks by requiring: i) non-bank institutions to legally ring-fence customer funds from those associated with other business areas through the establishment of a dedicated subsidiary firm; and ii) electronic money institutions to insure the aggregated funds of the customers under Afghanistan Deposit Insurance.

47. **Results and results indicators.** Establishment of an appropriately-regulated electronic-money system will lead to the entry of electronic-money institutions and, over time, improvements in access to financial services. The relevant results indicator is: *The number of registered non-bank electronic money institutions increases from zero in mid-2016 to three by 2018.*

Pillar II: Strengthen the policy and regulatory framework for private sector development

Prior Action #5: *The Recipient's Cabinet has approved a PPP policy and approved and submitted to the National Assembly a PPP law, establishing a policy and legal framework for PPPs.*

48. **PPP transactions present substantial risks to Government, given Afghanistan's limited experience to date, uneven capacity, and possibilities of negative political economy influence on transaction and contract design and implementation.** Government has previously received a large number of unsolicited PPP offers from the private sector. International experience of PPPs in fragile contexts highlights fiscal and other risks in the absence of adequate legal and policy frameworks, where transactions have often led to: i) inappropriate allocation of risks to Government due to inadequate technical capacity to design PPP agreements; ii) politicization and corruption due to inadequate transparency and contestability; and iii) inadequate concerns for environmental and social outcomes due to uncoordinated contracting without reference to broader regulatory frameworks.

49. **The Government of Afghanistan is aware of these risks and is responding appropriately.** The private sector and Government have both identified the need to develop a legal and policy framework for PPPs to help appropriately manage associated risks. Government is now working to establish a best practice governance and legal framework for PPPs including through a PPP policy and a new PPP Law. A new Central PPP Authority has already been established at general directorate level within the Ministry of Finance, reporting directly to the Minister, which has driven development of the PPP policy and will continue to play a strong analytical and technical role in vetting PPPs, ensuring fiscal and other risks are appropriately managed, and that required processes are complied with. Development partners, including through the Public-Private Infrastructure Advisory Facility, are playing a strong role in supporting the new policy and legal framework and building required capacity within the Ministry of Finance.

50. **The PPP Policy and Law establish a sound PPP governance framework.** The new PPP policy and law: i) define PPP transactions and the reasons for which they may be pursued; ii) establish key principles for PPPs, including value for money, appropriate allocation of risk, affordability and protection of users, transparency, competition, consultation, and environmental and social responsibility; iii) establish the institutional framework for PPPs, including the allocation of responsibilities to Cabinet, the Central PPP Authority, the PPP advisory committee, and different government agencies; and iv) establish and describe the process for PPP procurement. The PPP Law will create a specific regulatory and institutional framework for the development, procurement, approval and award of PPPs separate to traditional Government procurement, as set out in the Procurement Law and procedures issued under that law. The PPP policy and law specifically ensure that any potential PPPs will be assessed in terms of environment and social impacts and that approved PPPs are compliant with relevant regulations and safeguards.

51. **Results and results indicator:** Adoption of the PPP policy and law is expected to ensure risks associated with PPP transactions (including environmental, social, and fiduciary risks) are appropriately managed. Under the new framework, all PPP opportunities will be publicized, including bid conditions and pre-determined evaluation criteria, to enhance contestability and transparency. The relevant results

indicator is: *Proportion of PPP transactions for which invitations for expressions of interest are published on PPP unit website increases from 0 percent to 100 percent by 2018.*

Prior Action #6: *The Recipient's High Economic Council has approved an Open Access and Competitive Provisioning policy, allowing mobile network operators to invest in national and metropolitan fiber-optic networks, and the policy has been published on an official government website.*

52. **The telecommunications sector is one of Afghanistan's largest and most dynamic economic sectors.** Government is firmly committed to market-based policies in the telecommunications sector. There are five private sector providers, and vigorous competition has driven improvements in technology, service quality and access. 66 percent of all households now own at least one mobile phone while the number of GSM broadband subscribers has increased from almost zero to 1.9 million between 2012 and 2015.

53. **Lack of investment in fiber-optic technologies has become a binding constraint to broader development of the information and telecommunication sector.** For several years, the Ministry of Communication and Information Technology (MCIT), through the Afghanistan Telecommunications Regulatory Authority (ATRA) has pursued a market-based approach to adopting new technologies and expanding access. Private operators have open access to the Afghanistan Telecom (Aftel) fiber-optic network on an "even playing field" basis. Aftel, however, maintains exclusive ownership and management of the fiber-optic network and private firms are currently unable to invest in their own fiber-optic networks. Despite robust growth for more than a decade, investment, expansion, and availability of new technologies in the information and communication technology sector is now being constrained by the current monopoly on physical investment. In addition to investment, the sector needs capable and accountable service providers. Private investment in the sector may offer scope for service improvements, with international experience showing that, when properly regulated, private sector owned and operated networks provide better secure service, to larger segments of the population, at a better price than state enterprises. Private investors have signaled their willingness to immediately invest if existing regulatory constraints can be overcome. Overall, the current monopoly on fiber-optic network is constraining broader development and continued private investment in a sector with proven potential for growth even in the context of continued insecurity.

54. **Policy changes are required to allow private investment in fiber-optics.** The proposed operation will support approval of a new Open Access and Competitive Provisioning policy by the High Economic Council (Cabinet-level and highest necessary level of endorsement). This policy provides private businesses with the right to build, own, and operate active and passive network infrastructure and ensures transparent, non-discriminatory access, facilitating effective competition at the wholesale and retail level. The policy will provide the legal framework governing ICT Providers' access to basic passive and basic active infrastructure and will govern all government policies and actions relating to authorizing existing and future ICT providers to build, locate, own, and operate networks, including international gateways and internet exchange points.

55. **Results and results indicators:** The adoption of the Open Access and Competitive Provisioning Policy is expected to mobilize new private investment in fiber-optic technology. The relevant results indicator is: *Percentage of fiber-optic network (by value of investment) under management of the state utility (Aftel) decreases from 100 percent to 80 percent by 2018.*

Prior Action #7: *The Recipient's Ministry of Commerce has unified processes for investment licensing and business registration within the new Afghanistan Central Business Registry.*

56. **Afghanistan's private sector has suffered under a cumbersome and complex business licensing and registration regime.** All businesses were required to acquire either a trader's license from Ministry of Commerce and Industry (MoCI) or an investment license from the Afghan Investment Support Agency (AISA), in addition to sector-specific licenses from relevant ministries. Fees and license durations differed across business and license type, creating confusion for firms, with many licenses valid for only one year. Renewing a license frequently took up to 3 months.

57. **Government has recognized the need to streamline business licensing processes.** Government has recently ordered the merger of AISA and the Afghan Central Business Registry (ACBR) of MoCI. Under the relevant Presidential Decree, AISA will be abolished, with its staff and assets moved to MoCI's ACBR. ACBR will take on a one stop shop function for business licensing and taxes, and has already established a premises in Kabul where firms can acquire licenses and pay taxes at a single location. Additional one-stop shops are now being rolled out to provincial capitals, substantially reducing costs for firms that previously had to travel to Kabul to acquire licenses.

58. **As a prior action for this operation, investment licenses previously issued by AISA and trade licenses issued by the Ministry of Commerce have been unified into a single business license.** Fees for the license have been unified at Af18,000 for sole proprietors and Af30,000 for companies. Under new streamlined processes, the time taken to register a business and acquire a first-time license has been reduced to one day.

59. **Results and results indicators:** Reforms to business license processes are expected to reduce the costs and time taken to start a business and meet ongoing regulatory compliance costs. The relevant results indicator is: *Average number of days taken to renew a business license declines from 120 days in mid-2016 to 25 days by 2018.*

Prior Action #8: *The Recipient's Cabinet has approved and submitted to the National Assembly a new Accountancy Law to establish the legislative basis for a regulated accounting profession in Afghanistan.*

60. **Afghanistan currently lacks an adequate legislative and regulatory framework to ensure accuracy in financial reporting.** The current legal framework does not establish any uniform reporting standards. There is no professional association or regulatory body to ensure that those undertaking accountancy functions have adequate capacity and skills and comply with international standards. Audit Practices may register for business activity with the Afghanistan Investment Support Agency (AISA) but this body is not required to screen applicants with respect to professional qualification or competencies, nor does it perform post registration regulation. There are approximately 20 internationally qualified accountants in the entire country, the majority of which are not Afghan nationals.

61. **The absence of a regulated accountancy framework and profession in Afghanistan is constraining private sector development through several channels.** Firstly, an inadequate policy and regulatory framework undermines transparency in financial reporting, which impedes investment. Domestic and international investors do not have the information required to make investment decisions, increasing the costs of acquiring required information or the risks associated with investing in the absence of full information. Secondly, absence of adequate accounting practices and standards is impeding development of Afghanistan's financial sector, due to increased information problems and risks facing

banks and other financial institutions. Thirdly, the absence of a domestic accountancy profession increases costs for businesses undertaking international transactions or investments, who must acquire accountancy services from overseas to meet standard reporting and audit requirements. Fourthly, the absence of qualified accountants and accounting standards generates additional opportunities for corruption in both the private and public sectors, with implications for investor perceptions, government service delivery, and costs of doing business. Finally, the inability of firms to generate reliable, standardized financial data regarding their own operations presents a constraint to business operations and management.

62. **Cabinet has approved a new Accountancy Law, providing the foundation for improved accountancy practices and financial transparency.** The proposed operation will support submission to the National Assembly of the Accountancy Law. The law will, among other things: i) stipulate Afghanistan's accounting and auditing framework (IFRS and IAS); ii) prescribe the lead time required to progress from partial to full IFRS compliance; iii) prescribe the entity group that must comply with the IFRS framework as well as the group who must be subject to Statutory Audit; iv) prescribe the required accounting records to be maintained and filing dates; v) define the accounting and auditing regulation process; vi) recognize an Institute of Accountants and Auditors as industry regulator; vii) prescribe the requirements for qualification and licensing of Auditors; viii) prescribe penal provisions for non-compliance with the law; viii) Prescribe the duties and responsibilities of the institute of accountants and auditors; and ix) prescribe the composition of the founding council of the institute and the subsequent election and composition of the permanent council when the establishment of the institute has been successfully achieved. Alongside the new law, an accounting regulatory authority will be established to regulate the accounting and auditing professional in accordance with the new law. The authority will be designed as a private sector, self-regulating, and independent professional organization under the coordination of the Ministry of Finance, and designed to qualify for membership in the International Federation of Accountants. A school of accounting will also be established to build the stock of qualified Afghan accountants meeting international certification standards. The institute will assist with curriculum reform in national and private universities by creating curriculum and education delivery. Curriculum will be based on the Association of Chartered Certified Accountants (ACCA) with specialized education in Afghan law and taxation.

63. **Results and results indicator:** Through its implementation, the Accountancy Law will help address important constraints to private sector development through establishment of an adequate legal and regulatory framework for accountancy and audit in Afghanistan. The relevant results indicator is: *The number of accountants with accreditations recognized under the Accountancy Law increases from <20 to at least 100 by 2018.*

64. **Recent analysis undertaken by the World Bank Group, the Government, and other development partners has informed the content and selection of prior actions for this operation.** The following table shows analytical work relevant to each of the prior actions.

Table 3: Analytical Underpinnings

Prior Action	**Analytical Underpinnings**
Pillar 1: Enhance the policy framework to expand access to economic opportunities for the vulnerable	
Prior Action #1: The Recipient's Cabinet has approved a cross-government policy framework	The Policy Framework reflects findings from a range of analytical work including: i) joint UNHCR and World Bank

guiding a coherent policy response to the current displacement and returnee crisis.	work identifying the magnitude and development consequences of current displacement; ii) Norwegian Refugee Council analytical work highlighting problems with current identification and registration arrangements; and iii) USIP and Bank-commissioned analytical work demonstrating the need for reform of land administration to enable effective returnee and IDP settlement.
Prior Action #2 and Prior Action #3: The Recipient's Cabinet has approved and submitted to the National Assembly: i) a Land Management Law intended to improve security of tenure for the various categories of land users and provides more accessible procedures for formal titles to be issued, including to communities and investors; and ii) a Land Acquisition Law intended to ensure fairness and efficiency in the acquisition of land for public purposes.	World Bank conducted: i) two social assessments including a stakeholder analysis and livelihood assessments, and ii) several reviews of existing and draft revised laws highlighted the need for reforms to ensure tenure security and certainty of property rights while highlighting requirements for improved land acquisition processes. A World Bank supported land governance assessment and UNAMA analysis identified weaknesses in the current land administration system, including the scope of land-grabbing and options for addressing this practice. Recent USIP analysis has highlighted land issues as a driver of conflict.
Prior Action #4: The Recipient's Central Bank has issued and published new regulations governing Electronic Money Institutions supporting development of e-money systems and expanded access to financial services.	Recent analytical work under the 'Navigating Risks and Uncertainty' program has highlighted access to finance constraints. The World Bank is supporting development of the Financial Inclusion Strategy and has been providing technical assistance to Da Afghanistan Bank on e-money and payment systems reform.
Pillar 2: Strengthen the policy and regulatory framework for private sector development	
Prior Action #5: The Recipient's Cabinet has approved a PPP policy and approved and submitted to the National Assembly a PPP law, establishing a policy and legal framework for PPPs.	A PPIAF assessment identified gaps in the existing policy and regulatory framework for PPPs, and informed development of the PPP policy.
Prior Action #6: The Recipient's High Economic Council has approved and published an open access and competitive provisioning policy, allowing mobile network operators to invest in national and metropolitan fiber-optic networks, and the policy has been published on an official government website.	A World Bank policy note highlighted benefits from and options for adoption of open access. USAID has supported MCIT in developing the open access policy and the World Bank provided comments on the final document.
Prior Action #7: The Recipient's Ministry of Commerce has unified processes for investment licensing and business registration within the new Afghanistan Central Business Registry.	The World Bank Group has provided extensive technical assistance to business licensing reform. Reforms build on an extensive base of analytical assessments of business constraints which highlighted licensing as a key constraint.
Prior Action #8: The Recipient's Cabinet has approved and submitted to the National Assembly a new Accountancy Law to establish the legislative basis for a regulated accounting profession in Afghanistan.	World Bank policy engagement under the PFMRII project has been instrumental in identifying benefits from and need for a comprehensive accountancy legal and regulatory framework. USAID has provided additional support on developing the accountancy law.

4.3. LINK TO CPF AND OTHER BANK OPERATIONS

65. **The proposed operation is fully consistent with the priorities and approach established in the World Bank's Country Partnership Framework for Afghanistan (FY2017-FY2020) No. 109589-AF which was approved at the Board on October 27, 2016.** Building on a Systematic Country Diagnostic completed in 2016, the CPF is structured around three pillars: i) building strong and accountable institutions; ii) supporting inclusive growth; and iii) social inclusion. Reforms supported under both pillars of the proposed operation directly contribute to all three pillars of the CPF, through an emphasis on institutional, legal, and regulatory reforms that both expand access to economic opportunities to disadvantaged groups and support private sector development. Actions to improve the business environment are also complementary to ongoing IFC and MIGA activities intended to mitigate risks faced by private sector investors in fragile contexts through risk sharing and guarantee facilities.

4.4. CONSULTATIONS, COLLABORATION WITH DEVELOPMENT PARTNERS

66. **The Government has designed its reform agenda through a consultative process.** Government's national development strategy was informed by consultation with civil society groups and the private sector. Specific reforms supported by this operation were also informed by detailed consultation during policy development processes. Consultation on reforms to land administration has been ongoing for several years with ARAZI organizing a large number of public consultations across the country, including civil society organizations, the private sector, and the general public (see Annex 6). The PPP policy and legal reforms were informed by extensive consultation with private sector, civil society, and NGOs.

67. **The team worked closely with development partners in the development of this operation.** Donor aid coordination in Afghanistan is strong and frequent. Policy reforms and technical assistance efforts are coordinated on different donor-government platforms, among others the Joint Coordination Monitoring Board (JCMB), head of agency meetings, the ARTF strategy working group and other technical working groups. During the preparation phase of this operation, discussions have been held with the IMF, EU, DFID, ADB, and other bilateral donors. Overall strategic coordination on outcomes and reform priorities has been supported through the ARTF IP technical working group, which is monitoring implementation of the IP triggers and supporting the country's high-level structural reform priorities. The World Bank team is also closely cooperating with the IMF and coordinating policy advisory activities.

5. OTHER DESIGN AND APPRAISAL ISSUES

5.1. POVERTY AND SOCIAL IMPACT

68. **Policy actions supported by the operation are expected to have significant positive poverty and social effects over the longer-term.** Poverty and social impacts have been assessed based on: i) recent

World Bank analytical work regarding IDP and returnee demographics and living conditions;[9] ii) governance and policy assessments of land in Afghanistan;[10] and iii) a series of recent poverty and social impact assessments of land laws, including several commissioned specifically for this operation.[11] No policy actions supported by the operation are expected to have significant negative poverty and social effects.

69. **The adoption of a policy guiding response to the current IDP and returnee crisis is likely to have significant positive poverty and social effects.** Recent World Bank analysis shows many of the internally displaced and returnees are highly vulnerable, particularly in terms of accessing services and engaging in vulnerable forms of employment (such as being unemployed and/or underemployed). This analysis shows that most migrants are currently involuntary and a large proportion are undocumented and therefore face constraints to accessing services. Many returnees and IDPs have few assets and no source of income. Positive social and poverty effects are expected through: i) improved access to services as a result of improved documentation for currently undocumented displaced populations (IDPs and undocumented returnees); ii) improved data collection to target humanitarian and development interventions at communities most affected by the influx of displaced populations; iii) representation of IDPs and returnee populations within community governance mechanisms; and iv) cash grants to communities to generate income opportunities. The Policy Framework is not expected to have negative social and poverty effects. Principles of voluntariness are embodied in the framework, ensuring that government policies avoid coercion or duress in treatment of IDPs and returnees. The use of a 'whole of community' approach will ensure that differential treatment between returnees and host populations is avoided, mitigating any risk of grievance and conflict pressures. While the policy has no explicit gender focus, gender impacts will be tracked as part of the monitoring efforts by Government and Development partners and reported to the Displacement and Return Executive Committee (DiREC).

70. **Reforms to land management are expected to have significant positive poverty and social effects over time.** Reforms to land administration are intended to address key weaknesses in land governance identified through extensive analytical work conducted by the Government, the World Bank, and other development partners. The land laws have been developed in response to reviews of existing laws carried out by Government and the World Bank experts on land management. New laws are consistent with international good practice and well-suited to the fragility context, especially in terms of the inclusion of grievance redress and dispute resolution mechanisms and emphasis on transparency. The

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[9] World Bank and UNHCR (2016) "Fragility and Population Movement in Afghanistan" available at: http://documents.worldbank.org/curated/en/315481475557449283/pdf/108733-REVISED-PUBLIC-WB-UNHCR-policy-brief-FINAL.pdf

[10] World Bank (2013) Land Governance Assessment Framework Afghanistan: Final report. World Bank, Kabul.

[11] Wily, L. (2008) The Land Management Law 2008: Social Assessment, World Bank, Kabul; Wily, L. (2013) A Social Analysis of Land Expropriation Law of Afghanistan, World Bank, Kabul; Upadyay, S. (2015) Assessment of Proposed Changes to the Land Management Law of Afghanistan (2012), World Bank, Kabul; Upadyay, S. (2015) The Proposed Amendments To The Land Acquisition Law Of Afghanistan, 2014: Does it secure private investment and ensure tenurial security?, World Bank, Kabul; Reshdya, S. (2017) Comparative Analysis of The New Land Management Law of Afghanistan With the Previous Land Management Law 2008, World Bank, Kabul; Reshdya, S. (2017) Comparative Analysis of the land Acquisition law 2017 with the Land Acquisition law 2009, World Bank, Kabul.

most recent analysis of the new land management law concluded that the law was "very comprehensive and responsive to the need of land management system and institutions in Afghanistan".[12] The World Bank will provide continued support to all aspects of implementation, including grievance redress mechanisms, through investment project support to ARAZI. The new legal framework will strengthen land rights and over time mitigate land-related disputes and help rectify land-grabbing. Reviews of the Land Management Law and Land Acquisition Law undertaken in preparation of this operation demonstrate likely positive impacts through several channels, including: i) agricultural investment and productivity is expected to benefit from strengthened tenurial security, with 80 percent of the poor relying on agriculture for income; ii) increased opportunities to register land is likely to increase security and opportunities for economic participation for those occupying informal settlements; and iii) public land acquisition processes are less likely to impose costs on the poor, with social impact assessment now required as part of the public land acquisition process and compensation required for affected persons.[13] Reforms to land administration are also expected to benefit women, with traditional marriage certificates now recognized as valid legal documents for land ownership, allowing establishment of women's property rights if land was part of the dower. This specifically would strengthen and protect women's claim to land rights and increase the proportion of women with formal land ownership.

71. **Benefits of reforming land administration will depend on effective implementation.** International experience with reforming land administration in fragile states highlights important distributional risks arising from implementation of new legal frameworks.[14] Firstly, formal titling processes may enable expropriation, with state institutions and vested interests being empowered to claim and illegitimate land rights. Secondly, formal land titling processes may fuel corruption, if governance is weak within new institutions established to manage disputes. Thirdly, new processes may lead to frustration if processes for processing land transactions and resolving disputes are slow or viewed as unfair. Finally, much land in Afghanistan is under poppy cultivation or under the control of armed opposition groups, and new frameworks may not be implementable in such conditions. Such risks are mitigated by both the contents of the land laws and World Bank support provided to implementation through an Investment Project. Firstly, the reforms are explicitly intended to reduce reliance on an overloaded and sometimes corrupt court system, with administrative responsibilities transferred to a relatively high-capacity agency that enjoys strong ownership over the supported legal reforms and high-level political support. Secondly, the new legal framework is explicitly intended to address "land grabbing" through defining and criminalizing the practice in law, and avoiding any provisions that would legitimize previous land-grabbing. Thirdly, the framework establishes an administrative dispute resolution process and increases transparency in regards to processes for public land acquisition. Finally, the new Land Acquisition Law specifically introduces social impact assessment requirements to ensure threats to livelihoods associated with land acquisition are recognized and managed. The World Bank will support ARAZI in implementation of the new legal framework, providing capacity building and institutional strengthening under a dedicated project, with an explicit focus on ensuring pro-poor and gender-sensitive outcomes from new legislative arrangements.

72. **The Accountancy Law, electronic money regulations, telecommunications reforms, and business licensing process reforms are not expected to have significant direct effects on poverty.** These reforms are expected to reduce costs and risks of doing business, contributing positively to growth and

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[12] Reshdya, S. (2017) "Comparative Analysis of the New Land Management Law of Afghanistan (2017). World Bank, Kabul.
[13] Reshdya, S. (2017) "Comparative Analysis of The New Land Management Law of Afghanistan (2017)". World Bank, Kabul.
[14] For examples see: Unruh, J. and R. Williams (2013) 'Land and Post-Conflict Peace-Building', Routledge, New York.

employment outcomes over time. Over time, electronic-money regulations may support poverty reduction through improved access to financial services. The Accountancy Law may bring additional benefits through reducing corruption, which international research has shown to have disproportionate negative impacts on the poor.

5.2. ENVIRONMENTAL ASPECTS

73. **Actions supported by this operation are not expected to have significant effects on the environment, forests, or other natural resources.** Reforms to land management are expected to facilitate investment and development, including of agricultural land. But at the same time, security of property rights may increase incentives for sustainable land management on behalf of land owners in some cases. To mitigate potential environmental effects such as depletion and pollution of groundwater and other natural resources, the new Land Acquisition Law (2017) introduces resettlement, rehabilitation and livelihoods restoration measures, including the requirement to prepare Strategic Impact Assessment (SIA). The new law also requires public consultation and disclosure of information in cases of land acquisition for public purposes. A new Pesticide Law has been approved by Parliament (respective regulations are forthcoming). The Ministry of Agriculture Irrigation and Livestock (MAIL) has developed a Pest Management Plan (PMP) and Integrated Pest Management (IPM) approach.

74. **A basic legal framework is in place in Afghanistan to safeguard against potential environmental effects of new public and private sector investments**. The PPP policy and law – by providing greater certainty to investors – may facilitate additional investments that have environmental effects. At the same time, the new PPP policy and law directly mandate an environmental and social impact assessment (ESIA) of for all large PPP projects. The legal framework requires environmental impact assessments and public consultation for projects, policies, and plans for which substantial environmental effects are anticipated. These aspects are being reinforced by the new ESIA regulation recently approved by the Cabinet. [Note: ensure all highlighted acronyms included in list.]

75. **The Government has stepped up efforts to improve natural resource and environment management, with support from the World Bank and other development partners.** Capacity building and technical assistance is needed [15] to enable NEPA to properly implement the ESIA Regulation. Recently, the Government adopted the Natural Resource Management Strategy, which gives priority to using forests, pastures, and other natural assets sustainably, and requested Bank support with its implementation. This is a key step to address the possible environmental effects of the of the land management reforms. The Bank is currently providing technical assistance under the Capacity

[15] Shortcomings were identified by the Strategic Environmental and Social Assessment (SESA) prepared with Bank support as part of the Sustainable Development of Natural Resources Project II (P118925) in 2013. Phillips, D. and Hooge, L. Strategic Environmental and Social Assessment for the Extractives Industry Sector in Afghanistan (SESA --EI). Final Version. November, 2013. Adam Smith International Limited (ASIL).

Development for Natural Resource Management - ASA to assess the capacity to sustainably manage natural resources, and support the implementation of an action plan.[16]

5.3. PFM, DISBURSEMENT AND AUDITING ASPECTS

76. **The Public Financial Management System is considered adequate for the purposes of this operation and is the focus of ongoing reform effort.** The 2013 Afghanistan Public Expenditure and Financial Accountability (PEFA) assessment indicates that financial resources of the government sector are, by and large, tracked and reported within a budget which has contributed to aggregate fiscal discipline. The expenditures and financial position of the GoIRA are reported regularly in an understandable format and the National Assembly reviews the fiscal reports of the executive. GoIRA's commitments to financial transparency and accountability has supported mobilization of high levels of external support for both the recurrent and development budgets. Strengthening of the public financial management system is ongoing under the Public Financial Management Roadmap II, an inaugural 5-year rolling plan, and a detailed Rolling Fiscal Performance Improvement Plan (FPIP). These documents outline a number of high level objectives and targets to improve budget reliability, efficiency and effectiveness of government procurement systems, cash management, and monitoring and accountability systems.

77. **The fiduciary risk is substantial mostly as a result of the volatile nature and the fragile country environment but also due to some instances of ineligible expenditure and concerns related to capacity challenges**. The fiduciary risks are mitigated by the self-reinforcing actions committed to under the FPIP, the ARTF Incentive Program, and the Second Public Financial Management Reform Project (PFMR II?). The actions include (i) strengthening the budget in driving effective delivery of key priority outcomes; (ii) improving budget execution, and (iii) strengthening accountability and transparency.

78. **The IMF completed its most recent safeguards assessment of Da Afghanistan Bank (DAB) in December 2017.** It found that DAB had strengthened some elements of its safeguards framework since the previous assessment (2008), but an effective internal audit mechanism had not been established. The assessment made recommendations to address the risks emerging from the Kabul Bank fraud, including related to central bank autonomy and recapitalization. Since that time, some of the 2011 safeguards recommendations have been implemented, albeit with delay. Amending the law has been difficult, however, and the recommendation concerning the DAB's legal structure remains outstanding. DAB has continued to publish on its website DAB's financial statements audited by an international audit firm.

79. **Funds flow and disbursement arrangements.** A foreign currency account in dollars will be established at DAB. This will form part of the country's official foreign exchange reserves. Upon notification by IDA of grant effectiveness, and with the submission by the recipient of a withdrawal application, the proceeds of the grant will be deposited by IDA into the GoIRA dollar account in DAB. Given

[16] This ASA will help assess technical and institutional capacity of key institutions involved in implementation of the NRM Strategy, with the focus on forests, forests landscapes, and rangelands. The intermediate aims of this activity are to: (i) assess the available capacity to support the implementation of the newly adopted Natural Resources Management Strategy of key institutions involved in NRM, including Ministry of Agriculture, Irrigation and Livestock (MAIL), particularly its NRM department, at the national and provincial levels; National Environmental Protection Agency (NEPA); local governments (district councils, municipalities, village committees); and relevant CSOs; and(ii) identify key needs and provide recommendations, including with respect to specific capacity to step-up access to Climate finance.

that foreign exchange transactions are easier to trace than local currency expenditure, the Bank will require, a dedicated government account in Afghani in DAB for the budgeted expenditures only. An amount equivalent to the grant proceeds will be credited within five working days of receipt of funds from IDA, to the dedicated GoIRA Afghani account in DAB to finance budgeted expenditures. The proceeds of the grant cannot be used for ineligible expenditures (i.e., to finance goods and services from IDA's standard negative list as reflected in the financing agreement). If the proceeds of the grant are used for ineligible expenditures, IDA will require the GoIRA to refund the amount directly to IDA. Amounts refunded to IDA shall be cancelled. The receipt of the grants proceeds would be promptly accounted for in the government's budget system; transactions and balances of the government account will be fully incorporated into the government's accounting records and financial statements, via the AFMIS.

80. **Within 30 days of receipt of the grant, the government will provide to IDA:** (a) a written confirmation that this transfer has been completed; (b) any other relevant information relating to these matter, including the exchange rate of the conversion from US dollars to Af Afghanis; and (c) any other information that IDA may reasonably request. Disbursements will not be linked to specific purchases and no procurement requirements will be necessary. The financing agreement gives IDA the right to require the recipient to audit the foreign currency deposit account and the dedicated GoIRA account in Afghanis through agreed terms of reference. IDA may also request audits of the foreign currency deposit account prior to its closure in accordance with the financing agreement.

5.4. MONITORING, EVALUATION AND ACCOUNTABILITY

81. **The Ministry of Finance is the delegated implementing agency and will be responsible for the overall monitoring and evaluation of the program.** MOF has previous experience with monitoring results of World Bank DPO and will work closely with specific agencies with key policy responsibilities under the program, including: ARAZI, the PPP unit within the Ministry of Finance, the High Council on Migration, and the Afghanistan Telecommunications Regulatory Authority. Results indicators for the program have been selected on the basis of data availability constraints and generally rely on currently-available data sources. Tracking the results indicator related to registration of land under the new legislative framework will depend upon the establishment of new systems within ARAZI, to which the World Bank is planning a program of dedicated technical assistance support.

82. **Grievance Redress.** Communities and individuals who believe that they are adversely affected by specific country policies supported as prior actions or tranche release conditions under a World Bank Development Policy Operation may submit complaints to the responsible country authorities, appropriate local/national grievance redress mechanisms, or the WB's Grievance Redress Service (GRS). The GRS ensures that complaints received are promptly reviewed in order to address pertinent concerns. Affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, as a result of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the World Bank's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the World Bank's corporate Grievance Redress Service (GRS), please visit http://www.worldbank.org/GRS. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

6. SUMMARY OF RISKS AND MITIGATION

83. **The overall risk rating for the operation is high.** Risks in four areas are most pronounced and could potentially jeopardize the achievement of program outcomes. These risk areas, discussed below, are: i) political and governance risks; ii) macroeconomic risks; iii) institutional capacity for implementation and sustainability risks; and iv) security risks. Risks specific to the reforms in land governance are discussed in Annex 5.

84. **Political and governance risks:** There are multiple sources of political and governance risk in Afghanistan. Power-sharing arrangements under the National Unity Government are a continued source of tension and potential future instability. Divisions within the government have previously led to long delays in filling senior civil servant posts, with less suitable candidates often selected on the basis of acceptability to both parties. The existence of parallel bureaucracies under both leaders exacerbates coordination problems and leads to contestation and bargaining over decisions made at every level. Current political arrangements and the possibility of a change of government pose risks to program development objectives in terms of potential political disruptions delaying reform implementation, or potential changes in the level of political support for reforms. Reforms to land administration may pose a challenge to powerful vested interests, posing challenges to effective implementation. These risks have been managed by ensuring broad support for planned reforms and the provision of adequate implementation support through technical assistance engagements to maintain momentum and ensure the availability of required capacity. Ongoing policy dialog under the Incentive Program and an Investment Project will support policy commitment and momentum and implementation of the land administration reforms. The establishment of enhanced public consultation and grievance redress systems under supported reforms to land administration will help minimize the likelihood of vested interests slowing or distorting implementation.

85. **Macroeconomic risks:** Afghanistan’s macroeconomic outlook is subject to substantial risks. Afghanistan remains heavily reliant on aid, and any reduction in security and civilian support below expected levels would place pressure on fiscal sustainability and service delivery. Access to continued external support is most likely to be sustained at expected levels if progress can be sustained against key structural reforms. Successful implementation of the supported program of reforms will therefore, itself, help mitigate this risk along with continued World Bank policy dialog on fiscal management and structural reforms under the ARTF IP. Deterioration of the security situation could lead to increased expenditure pressures and lower revenues as confidence and growth decline, undermining outcomes that involve increased investment and government administrative functions. This risk has been somewhat mitigated through selection of prior actions and development program objectives that are robust to some level of ongoing conflict. Macroeconomic risks are further exacerbated by weaknesses in the financial sector including potential fiscal risks arising from state-owned banks and outstanding financial obligations on government arising from the Kabul bank crisis. These risks are partly mitigated through planned World Bank technical assistance to reform of state-owned banks and reforms for the resolution of the Kabul Bank obligations under the IMF ECF program.

86. **Institutional capacity for implementation and sustainability:** The public sector in Afghanistan is characterized by highly uneven and thinly spread technical capacity. The context of long-term aid dependency had left some agencies and reform processes heavily dependent on international technical assistance, and vulnerable to associated delays, discontinuities, and coordination problems. Coordination problems and capacity constraints have been exacerbated by parallel bureaucracy and contestation over appointments under the National Unity Government. Lack of capacity is a particular constrain in the

Ministry of Justice, with a lack of technical skills in the ministry weakening the legislative review process, causing delays and sometimes unexpected changes to legislation that are inconsistent with policy goals. To mitigate these risks, all policy reforms are being supported by technical assistance from the World Bank Group or other development partners. In addition, Bank experts, including land management specialists, will conduct close supervision and monitoring of the results. Policy reforms under the operation have also been selected on the basis of adequate existing capacity and leadership.

87. **Security risks:** Continued insurgent activity represents another source of risk to achievement of program outcomes. Deterioration in the security situation could divert government capacity and policy attention from supported reforms, impede the provision of technical assistance, disrupt monitoring arrangements, or undermine the expected impact of supported reforms. These risks are somewhat mitigated through the program's focus on a small number of policy actions that have been selected on the basis of their likely positive impact even in the context of ongoing conflict. Previous experience has shown that the Bank can successfully monitor and support implementation of reform programs even with a limited in-country presence.

88. **In addition, risks in several areas are rated substantial, including:**

89. **Technical design**: many reforms supported by this operation can be considered new and complex in Afghanistan's operational environment. While all reforms are underpinned by significant analysis, the learning curve for the institutions implementing the reforms will be steep. To mitigate these risks, all policy reforms are being supported by technical assistance from the World Bank Group or other development partners. Based on lessons learned from operating in Afghanistan's fragile environment, the World Bank country team pays attention to adaptive designs in technical assistance projects in order to be able to flexibly respond to shifting parameters.

90. **Fiduciary Risks**. Fiduciary risks are substantial despite good progress in most phases of budget operations. Previous DPO and investment operations (e.g., Public Financial Management Reform Project II) have helped to put in place adequate processes and practices for financial management, procurement and control. Afghanistan has a relatively strong public finance capacity track record as witnessed by the 2013 PEFA and other relevant PFM indicators. However, fiduciary risks remain high due to low compliance with PFM rules and limited internal and external controls. For the most part risk mitigation relies on the self-reinforcing actions committed to under the Government's Fiscal Performance Improvement Plan, the ARTF Incentive Program, the IMF Extended Credit Facility and the Second Public Financial Management Reform Project, and its follow-on operation, the planned Fiscal Performance Support Project. The ARTF Incentive Program (IP), in particular, focuses heavily on the timely implementation of PFM measures across the whole range of the PFM cycle.

91. **Social and Environmental risks**: As discussed in paragraphs 73 - 75, environmental risks deriving from the reforms are not expected to be significant and are indirect in nature. However, the operation could potentially carry risks for social livelihoods. Most of them related to the implementation of the land-governance related laws and the IDP and Returnee policy framework. As mentioned above, risks will be mitigated by continued engagement through technical assistance, analytical services as well as structured policy dialogue through the ARTF IP. Moreover, the legislations supported by this operation have been designed to specifically include provisions that improve social and environmental safeguards and address stresses produced by the reforms. Other risk mitigation measures are discussed in paragraphs 68 – 72 and further elaborated in Annex 5.

92. **Stakeholder risks**: The main stakeholder risk to the operation is potentially a lack of awareness of how the reforms supported by this operation strengthens property rights, especially of the vulnerable population. Moreover, elites negatively affected by the provisions in the land related laws could exercise undue influence on decision-makers in the government and parliament, undermining the effective implementation of the reforms. Through a range of technical assistance activities but also through its broader engagement, and throughout the implementation of the reforms, the World Bank stands ready to assist Government in conducting informed discussions on these issues, carrying out adequate consultations with the affected social groups, the private sector and civil society, and in identifying risks and mitigation measures. This will also involve assistance with media strategies and campaigns to ensure that Afghan citizens and investors are made aware of the rights extended to them through the changes in the different legislations.

93. **Budget:** In light of Afghanistan's aid dependency, continued donor support will be crucial for balancing the budget. At the Warsaw and Brussels conference in 2016, international partners committed to providing military and civilian support to Afghanistan through 2020. However, in return the Afghan government committed to, among other things, strengthening governance, reducing corruption and improving gender equity and increasing fiscal revenue. A possible risk is that donor support wanes if the government reneges on these commitments. The proposed operation itself contributes positively to mitigating this risk by supporting the government in meeting the some of the Brussels commitments (e.g. on land governance).

Risk Categories	**Rating**
1. Political and governance	High
2. Macroeconomic	High
3. Sector strategies and policies	Moderate
4. Technical design of project or program	Substantial
5. Institutional capacity for implementation and sustainability	High
6. Fiduciary	Substantial
7. Environment and social	Substantial
8. Stakeholders	Substantial
9. Security risks	High
Overall	High

ANNEX 1: POLICY AND RESULTS MATRIX

Pillar	Prior Action	Result	Baseline	Target
Enhance the policy framework to expand access to economic opportunities for the vulnerable	The Recipient's Cabinet has approved a cross-government policy framework guiding a coherent policy response to the current displacement and returnee crisis.	Number of border crossings at which returnee certifications are issued.	1	4
	The Recipient's Cabinet has approved and submitted to the National Assembly a Land Management Law intended to improve security of tenure for the various categories of land users and provides more accessible procedures for formal titles to be issued.	Number of landholders currently without formal land ownership records provided with formal ownership through the administrative processes established under the new land management law.	0	500
		Gender disaggregated records of land ownership are available under the ARAZI digital registration system.	No	Yes
	The Recipient's Cabinet has approved and submitted to the National Assembly a Land Acquisition Law intended to ensure fairness and efficiency in the acquisition of land for public purposes.	The proportion of land acquisitions for which public notice is provided through media at least 6 months in advance of acquisition and social impact assessment is carried out.	0%	100%
	The Recipient's Central Bank has issued and published new regulations governing Electronic Money Institutions supporting development of e-money systems and expanded access to financial services.	Number of registered non-bank electronic money institutions.	0	3
Strengthen the policy and regulatory framework for private sector development	The Recipient's Cabinet has approved a PPP policy and approved and submitted to the National Assembly a PPP law, establishing a policy and legal framework for PPPs.	Proportion of PPP transactions for which invitations for expressions of interest are published on PPP unit website.	0%	100%
	The Recipient's High Economic Council has approved an open access and competitive provisioning policy, allowing mobile network operators to invest in national and metropolitan fiber-optic networks, and the policy has been published on an official government website.	Percentage of fiber-optic network (by value of investment) under management of the state utility (Aftel)	100%	<80%
	The Recipient's Ministry of Commerce has unified processes for investment licensing and business registration within the new Afghanistan Central Business Registry.	Average number of days taken to renew a business license.	120	25
	The Recipient's Cabinet has approved and submitted to the National Assembly a new Accountancy Law to establish the legislative basis for a regulated accounting profession in Afghanistan.	Number of Afghan national and resident accountants with accreditations recognized under the Accountancy Law	~20	100

ANNEX 2: LETTER OF DEVELOPMENT POLICY

جمهوری اســلامی افغانستان
وزارت مالیه

د افغانستان اسلامی جمهوریت
دمالیی وزارت

Islamic Republic of Afghanistan
Ministry of Finance
Chief of Staff
ریاست دفتر

Number: 2017-05-06-01
Date: May 6, 2017

Mr. Jim Yong Kim
President
The World Bank Group
1818 H street, NW Washington DC, 20433
USA

RE: Inclusive Growth Development Policy Operation

Dear President Kim:

This letter lays out key elements of the Islamic Republic of Afghanistan's economic policy and institutional reform program. The Government of Afghanistan requests assistance from the World Bank Group in the form of a development policy operation to support priority reforms under this program. Afghanistan has made huge strides in the past 16 years. Core democratic and government institutions have been established, macroeconomic stability has been maintained, and access to services has expanded substantially.

The formation of the National Unity Government opened a new chapter of reforms in general and in the economic sector in particular. Afghanistan achieved 27 out of 30 of the reform benchmarks under Realizing Self-Reliance through Mutual Accountability Framework for 2015-2016. The other remaining 3 were also achieved, albeit with a delay. An IMF staff monitored program (SMP) was successfully completed and a subsequent extended credit facility (ECF) focusing on macroeconomic reforms is currently being implemented. A special Anti-Corruption Justice Center with a dedicated major crimes unit was established.

Following a range of tax policy and administration reforms, revenue collection from normal streams increased by 16 percent in 2016 (and 25 percent when one-offs are included), surpassing the IMF target of 7 percent. This followed an impressive 22 percent increase of the 2015. As a share of the GDP, revenue has increased from a low of 8.7 percent in 2014 to nearly 1 1 percent in 2016. This is a notable achievement, considering the increasingly challenging environment.

آمریت تحریرات، ریاست دفتر ، وزارت مالیه ، شماره تماس :۰۲۰۲۱۰۰۳۸۷، ۰۲۰۲۱۰۲۸۳۷
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Despite the progress outlined above, important challenges still remain. Since the drawdown of international security forces in 2014, growth rates have slowed substantially, security challenges have increased and investment has declined increasing unemployment and poverty rates. Challenges have been exacerbated by the ongoing returnee and internal displacement crisis, with large numbers of Afghans requiring resettlement after returning from overseas or fleeing domestic conflicts. With aid flows expected to decline over coming years, it will be vital for new sources of growth to be mobilized and new investment facilitated.

In this context, the Government of Afghanistan is committed to further reforms to increase investment, generate adequate jobs for the young and growing population, and create new opportunities for excluded and vulnerable populations, including the displaced. A comprehensive strategy for achieving peace, and economic and social development is presented in the new Afghanistan National Peace and Development Framework (ANPDF). We are requesting World Bank support to vital institutional and policy reforms that underpin the new ANPDF priorities. These reforms are organized under two pillars: i) enhancing the policy framework to expand access to opportunities for the vulnerable; and ii) strengthening the policy framework for private sector development.

Enhancing the policy framework to expand access to opportunities for the vulnerable

The Government of Afghanistan is fully committed to ensuring a better future for Afghans including the 1.2 million internally displaced people and more than one million Afghans that returned to Afghanistan in 2016. Substantial efforts have been taken over the past year to provide immediate assistance to returnees and IDPs, including initiatives to provide immediate humanitarian and financial relief. Cabinet has recently approved a policy framework for IDPs and returnees that will ensure sustainable reintegration of displaced populations, addressing issues of equity, access to services, and access to land. The policy also establishes governance mechanisms for a coordinated whole-of-government policy response to the current crisis, under the ultimate leadership of the Cabinet and Council of Ministers.

Under this pillar, Cabinet has also recently approved important improvements to the legal framework for land management. The new Land Management Law is ratified through Presidential Decree which will establish an administrative system of land management in Afghanistan, facilitating access to secure land rights for all Afghans while reducing reliance on the over-burdened court system. The new Land Acquisition Law will substantially overhaul the framework for public land acquisition, introducing a range of important protections for landowners and occupants while still facilitating land acquisition for vital public purposes. Together, these laws will facilitate investment and private sector activity through the strengthening of property rights while explicitly enhancing protections against land-grabbing available to the vulnerable.

Finally, we are working to develop a financial inclusion strategy to expand access to financial services to many more Afghan households and firms.

As a key step towards this goal, Da Afghanistan Bank has issued regulations governing electronic money institutions laying the foundations for technology driven expansions in access to financial services, especially for those living in insecure and remote areas.

Strengthen the policy framework for private sector development

The ANPDF places high priority on private investment as the core driver of job creation. Government recognizes that private sector activity will play a vital role in driving growth and revenues in the context of lower aid inflows.

Accordingly, the High Economic Council recently approved a new Open Access and Competitive Provisioning Policy for fiber-optic telecommunications technology. This policy will address an immediate constraint to private investment in the sector and establish the foundations for new investment, increased competition, and improved access to fiber-optic services.

Cabinet also recently approved a new policy and legal framework for Public-Private Partnerships (PPPs) in Afghanistan. PPPs provide opportunities for mobilizing private capital in vital sectors in Afghanistan. International experience, however, has demonstrated the importance of an adequate policy and legal framework to manage risks to government and provide necessary certainty to investors. Among other things, the new PPP policy and law will ensure transparency and contestability in PPP contracts while also establishing requirements for the identification and management of any environmental risks.

In order to improve the business regulatory environment and reduce compliance costs facing firms, we have made important administrative changes to our business licensing regime. The Afghanistan Investment Support Agency has been merged into the Ministry of Commerce and Industry, allowing for important streamlining of business license processes. These changes are expected to reduce the time and costs associated with business licensing.

Finally, a new Income Tax Law is approved by Cabinet and Accountancy Law is ratified through Presidential Decree, which establishes a legal framework for accountancy services and the development of accounting capacity in Afghanistan. Over time, this is expected to facilitate investment, support financial sector development, reduce costs of accessing accounting capacity, and reduce opportunities for corruption.

Government is well aware of the potential environmental impacts of the above reforms, including intensified land use and pollution through new investment following improvements to the business environment. Reflecting this, Government will continue to strengthen the regulatory framework for environmental protection, including implementing new regulations for strengthened environment and social impact assessment processes and implementation of a new natural resources management strategy under the Ministry of Agriculture, Irrigation, and Livestock (MAIL).

Overall, Government is strongly committed to the ambitious program of reforms supported by this operation. We look forwards to working with the World Bank on our ongoing economic reform agenda over years to come.

I take this opportunity to thank the Word Bank Group for its continued support to Afghanistan.

Sincerely,

Eklil Hakimi

Eklil Hakimi
Minister

ANNEX 3: FUND RELATIONS

Islamic Republic of Afghanistan - Assessment Letter for the World Bank

This letter reflects our preliminary assessment of Afghanistan's macroeconomic conditions and policies based on the Request for a Three-Year Arrangement Under the Extended Credit Facility (ECF Arrangement—July 20, 2016) and developments since then. A press release was published on July 20, 2016 (No. 16/348), and the Staff Report was published on July 20, 2016 (No. 16/252). A mission to conduct the First Review under the ECF Arrangement took place February 23–March 4, 2017, during which a staff-level agreement on the completion of the review was reached. A press release was issued after the mission. The agreement is subject to approval by IMF management and Executive Board, which is tentatively scheduled to consider the review on May 10, 2017.

Recent Developments, Outlook, and Risks

1. **Afghanistan continues to face difficult economic challenges.** The country is undergoing a challenging political, security, and economic transition. Continued insecurity, political uncertainty, weak institutions, and corruption are salient factors preventing robust and inclusive economic growth. Against this background and following the sizeable international troop reduction starting in 2013, real GDP growth has declined substantially in recent years.

2. **Growth has remained low in 2016, with the security situation deteriorating.** There have been several high profile insurgent attacks and civilian casualties reached a record level. An additional destabilizing force is the large returning refugee influx from Pakistan and, to a smaller extent, Iran and Europe, although the influx may entail a short term boost to private consumption. Constrained by weak confidence, growth remains low, estimated at 2 percent in 2016, a modest acceleration from 0.8 percent in 2015, reflecting improved agricultural output. Inflation moderated in the second half of 2016 and reached 4.1 percent y/y in February partly reflecting an easing in food prices. A small overall fiscal surplus (including grants) of 0.1 percent GDP was recorded in 2016, in part owing to a 15.4 percent increase in domestic revenues, well above the ECF arrangement target. The strong revenue performance was driven by enforcement efforts, and buoyant sales tax and non-tax revenue. Trade and current account deficits (before grants) remain very large, but gross international reserves cover eleven months of imports.

3. **Donor support is strong**. As demonstrated by the successful Warsaw and Brussels meetings last year, the international community continues to stand behind Afghanistan as it struggles with its transition. At the Brussels conference, donors pledged $15.2 billion in development assistance, which surpassed most analysts' expectations.

4. **A modest pickup in growth is expected in 2017 and the medium term.** The baseline envisages growth of 3 percent in 2017, and a gradual increase to 5–6 percent over the medium term predicated on improvements in security and political stability, implementation of reforms, and a continued high level of aid. Over time, extractive industries and regional trade and infrastructure integration could support growth and job creation.

5. **Risks to macroeconomic outlook.** The outlook is subject to significant risks. If security conditions worsen, aid falls short, or reforms stall, growth would be lower with attendant effects on

unemployment and poverty. On the upside, lasting peace with insurgents would improve the medium-term trajectory by boosting private sector confidence and facilitating a growth-supportive shift in public spending from security to development.

Policy Implementation under the ECF Arrangement

6. **Performance under the program has been satisfactory.** Following the recent review mission, staff assessed that all end-December 2016 performance criteria and indicative targets have been met, with a sizeable over-performance on the domestic revenue and net international reserves targets.

7. **Structural reforms have proceeded, but there have been delays in some areas.** Out of five structural benchmarks covered by the first review, two were not implemented in full: the criminalization of corruption has become part of a draft consolidated penal code, which is likely to be passed by presidential decree in the next four months; and the 2017 budget, while in line with the macroeconomic framework, did not specify the transfer to be made to the Kabul Bank Receivership in line with the benchmark requirements; the latter is expected to be corrected with a mid-year revision to the budget.

8. **Going forward, the main policy priorities include:**

- *Maintaining a balanced and sustainable fiscal position*. With sluggish growth, disruptions in trade with the main trading partner (Pakistan), and considering the uncertain impact of WTO accession, there are downside risks to revenues, while the security challenges and the influx of returning refugees—along with rising numbers of internally displaced people fleeing violence—put pressure on budgetary and off-budgetary (donor-financed) spending. While the scope for raising revenue intake through tax policy measures is limited, there is still a room for improving revenue collection efficiency, while ensuring that the conduct of revenue collection is even-handed and does not harm economic activity. Over time, efforts to shift public spending towards productive investments in human and physical capital will need to accompany the revenue raising efforts.

- *Strengthening financial stability*. DAB's legal, regulatory and supervisory frameworks require bolstering to address issues of central bank mandate, institutional and personal autonomy, DAB profit distribution and recapitalization, foreign reserves management, the lender of last resort function and financial stability. Amending the DAB law has proven a challenge, and, as a result, the 2011 Safeguards Assessment recommendation concerning DAB's legal structure remains outstanding; an amendment process in consultation with the IMF Legal Department is underway. The authorities also need to continue with overcoming the legacy of the Kabul Bank collapse by restoring DAB's balance sheet. In addition, developing a strategy for state-owned commercial banks (in cooperation with the World Bank) is essential.

- *Strengthening economic governance and the business climate*. While there has been progress in strengthening the institutional set up to combat corruption, some legislative measures (e.g., asset declarations, and the criminalization of corruption) still need to be finalized. The next step is implementation. With regard to the business climate, Afghanistan has major gaps to close especially with regard to the regulatory burden and the quality of infrastructure. Reforms in this area are essential if the government's development strategy—as outlined in "Afghanistan's National Peace and Development Framework"—is to succeed.

Relations with the Fund

9. After the successful completion of the Staff Monitored Program in 2016, Afghanistan requested a financial arrangement with the Fund. On July 20, 2016, the Executive Board of the International Monetary Fund approved a three-year SDR 32.4 million (about US$ 45 million, 10 percent of quota) arrangement under the Extended Credit Facility. The authorities' program sets out a structural reform agenda that focuses on institution building, fiscal and financial reforms, and measures to combat corruption to lay the foundations for scaled up private sector development and job creation. It aims to preserve macro-financial stability by implementing prudent fiscal, monetary, and financial policies, and by maintaining external buffers and a flexible exchange rate regime. Most recently, staff-level agreement on the completion of the first review was reached in early March, with the Executive Board discussion tentatively scheduled for May 10, 2017. Completion of the review would release a disbursement of SDR 4.5 million (about US$ 6.1 million). The last Article IV consultation was concluded in November 2015, and the next such consultation is expected in November 2017.

Table 1. Islamic Republic of Afghanistan: Selected Economic Indicators, 2013–17

(Quota: SDR 323.8 million)

(Population: approx. 33.4 million)

(Per capita GDP: approx. US$615; 2015)

(Poverty rate: 35.8 percent; 2011)

(Main exports: opium, US$2.7 billion; carpets, US$83.4 million; 2014)

	2013	2014	2015	2016	2017
				Prel./Est.	Proj.
Output and prices 1/					
Real GDP	3.9	1.3	0.8	2.0	3.0
Nominal GDP (in billions of Afghanis)	1,117	1,168	1,204	1,282	1,399
Nominal GDP (in billions of U.S. dollars)	20.2	20.4	19.7	18.9	20.5
Consumer prices (period average)	7.4	4.7	-1.5	4.4	6.0
Food7.6	7.7	-1.9	5.7	…	
Non-food	7.2	1.4	-1.2	3.2	…
Consumer prices (end of period)	7.2	1.5	1.1	4.6	7.2
Investment and savings					
Gross domestic investment	23.1	17.6	18.6	18.7	18.5
Of which: Private	6.6	5.9	5.8	5.4	6.4
Gross national savings	23.4	23.4	21.5	25.8	23.3
Of which: Private	7.6	13.4	10.1	12.4	10.7
Public finances (central government)					
Domestic revenues and grants	24.3	24.0	25.0	26.9	26.3
Domestic revenues	9.8	8.6	10.2	11.0	10.9
On-budget grants (excl. donors' direct spending outside the budget)	14.6	15.4	14.9	15.9	15.4
Expenditures	25.0	25.7	26.4	26.7	25.8
Operating 2/	17.8	19.5	19.6	19.4	18.1
Development	7.2	6.2	6.9	7.3	7.7
Operating balance (excluding grants) 3/	-8.0	-10.9	-9.4	-8.4	-7.2
Overall balance (including grants)	-0.6	-1.7	-1.4	0.1	0.5
Public debt 4/ 5/	9.5	8.8	9.3	8.3	7.6
Monetary sector					
Reserve money	12.4	36.5	2.3	11.8	10.3
Currency in circulation	12.5	16.7	2.6	10.6	10.5
Broad money	9.4	8.6	3.2	9.6	8.2
Interest rate, 28-day capital note (in percent)	3.4	3.6	3.5	3.0	…
External sector 1/					
Exports of goods (in millions of U.S. dollars)	507	643	580	618	708
Exports of goods (annual percentage change)	6.6	26.8	-9.8	6.6	14.6
Imports of goods (in millions of U.S. dollars)	8,057	6,497	7,034	6,151	6,510
Imports of goods (annual percentage change)	5.6	-19.4	8.3	-12.5	5.8
Merchandise trade balance	-37.4	-28.8	-32.8	-29.3	-28.3
Current account balance					
Excluding official transfers	-43.4	-32.2	-35.3	-32.2	-30.9
Including official transfers	0.3	5.8	2.9	7.1	4.8
Foreign direct investment	0.4	0.2	0.9	0.4	1.1
Total external debt 4/	6.9	6.5	7.0	6.5	6.6
Gross international reserves (in millions of U.S. dollars)	6,873	7,311	6,808	7,332	7,534
Import coverage of reserves 6/	9.8	10.2	11.0	11.1	11.0
Exchange rate (average, Afghanis per U.S. dollar)	55.4	57.4	61.1	67.9	…
Real exchange rate (average, percentage change) 7/	-2.7	-0.6	-7.7	-7.1	…

Sources: Afghan authorities, United Nations Office on Drugs and Crime, WITS database, and IMF staff estimates and projections.

1/ Excluding the narcotics economy.

2/ Comprising mainly current spending.

3/ Defined as domestic revenues minus operating expenditures.

4/ Public sector only. Incorporates committed but not yet delivered debt relief. Debt relief recorded fully at time of commitment.

5/ Public debt (including 2016 program number) was revised to include promissory note issued by MoF to settle DAB's Kabul bank exposure.

6/ In months of next year's import of goods and services.

7/ CPI-based, vis-a-vis the U.S. dollar.

ANNEX 4: ENVIRONMENT AND POVERTY/SOCIAL ANALYSIS TABLE

Prior actions	Significant positive or negative environment effects	Significant poverty, social or distributional effects positive or negative
Pillar 1: Enhance the policy framework to expand access to economic opportunities for the vulnerable		
Prior action #1 The Recipient's Cabinet has approved a cross-government policy framework guiding a coherent policy response to the current displacement and returnee crisis.	No likely significant negative or positive effects.	Potential positive effect due to improved access to services, support, and economic opportunities, for returnees and displaced
Prior action #2 The Recipient's Cabinet has approved and submitted to the National Assembly a Land Management Law intended to improve security of tenure for the various categories of land users and provide more accessible procedures for formal titles to be issued, including to communities and investors.	Potential positive and negative effects. Strengthening of land property rights will improve incentives for sustainable management. Increased land use for agriculture and other purposes may lead to pollution and pressure on water resources, depending on the scale and type of new investment.	Potential positive effect. Strengthened property rights will enable investment, benefiting the majority of Afghanistan's population that currently lack formal land rights and depend upon agricultural production.
Prior Action #3 The Recipient's Cabinet has approved and submitted to the National Assembly a Land Acquisition Law intended to ensure fairness and efficiency in the acquisition of land for public purposes.	Potential positive effect. Inclusion of environmental impact statement and public consultation requirements for public land acquisition will help ensure effective management of environmental impacts.	Potential positive effect. Improved compensation requirements and introduction of grievance mechanisms will provide better protection to vulnerable and their continued access to livelihoods
Prior Action #4 The Recipient's Central Bank has issued and published new regulations governing Electronic Money Institutions supporting development of e-money systems and expanded access to financial services.	No likely significant negative or positive effects.	No likely significant negative or positive effects.
Pillar 2: Strengthen the policy and regulatory framework for private sector development		
Prior action #5 The Recipient's Cabinet has approved a PPP policy and approved and submitted to the National Assembly a PPP law, establishing a policy and legal framework for PPPs.	Potential positive and negative effects. New PPP investments due to increased investor certainty may have environmental impacts. However, the new legal and regulatory framework introduces strengthened environmental protections,	No likely significant negative or positive effects.

Prior action #6 The Recipient's High Economic Council has approved an open access and competitive provisioning policy, allowing mobile network operators to invest in national and metropolitan fiber-optic networks, and the policy has been published on an official government website.	No likely significant negative or positive effects.	No likely significant negative or positive effects.
Prior action #7 The Recipient's Ministry of Commerce has unified processes for investment licensing and business registration within the new Afghanistan Central Business Registry.	No likely significant negative or positive effects.	No likely significant negative or positive effects.
Prior action #8 The Recipient's Cabinet has approved and submitted to the National Assembly a new Accountancy Law to establish the legislative basis for a regulated accounting profession in Afghanistan.	No likely significant negative or positive effects.	No likely significant negative or positive effects.

ANNEX 5: RISKS AND MITIGATION FOR LAND ADMINISTRATION REFORMS

1. Weaknesses in Afghanistan's land governance environment are a major source of conflict and poverty. Recent analytical work, including a World Bank Land Governance Assessment shows that out-dated systems, overlapping responsibilities, lack of capacity at local levels, conflicting systems for land ownership, and uncertain or incomplete legal frameworks, compounded by decades of conflict and widespread displacement, have created weak property rights, inequitable distribution, and widespread land-related conflict.[17] Data on existing land-holdings is inadequate, but recent evidence suggests that a large proportion of the rural population are landless.[18] Land holdings are extremely inequitable. Some customary practices limit women's land ownership (only one percent of land is owned by female-headed households, although 56 percent of female-headed households own land) and inheritance rights of women have been weakened by the failure of the existing legal framework to recognize sharia documents, including informal marriage certificates, as evidence of ownership.[19] Seventy percent of all murders and violent crimes in Afghanistan are the result of land disputes.[20] Reflecting the high costs of establishing land rights through the corruption-prone judicial system, only 20 percent of land is formally titled.[21] The situation is exacerbated by the prevalence of illegal crops, particularly opium, which makes land titling and the development of a modern cadaster extremely challenging.

2. Powerful vested interests have taken advantage of weak systems for recording land property rights to illegitimately acquire large amount of valuable land. The land authority has received complaints that 1.5 million jireebs of land has been usurped over the past decade, equal to 15 percent of all arable land.[22] Much of the land that has been illegitimately appropriated has been developed by powerful interests. Distribution of public land, only permitted through Presidential decree under the 2008 Land Management Law has in fact been undertaken by a range of uncoordinated subnational institutions, through processes involving corruption and patronage.[23] Land-grabbing is not criminalized under current legal framework, with relevant provisions vaguely worded and unenforceable. Consequently, there have been no known indictments or convictions for land grabbing. Current land acquisition law only requires the minority of landholders with documentation to be compensated when their land is needed for public investment purposes. The absence of clear legal guidance permits unjust evictions to occur, compensation to be insufficient, and local dissatisfaction to rise.[24] Resolution of disputes is lengthy; even small-scale land acquisition cases have exceeded 120 weeks in recent years.

3. The World Bank and other development partners have been closely involved with land governance reform in Afghanistan. Reforms to land administration are being pursued under the 2007 National Land Policy. The World Bank and other development partners have been supporting implementation of this policy through a range of engagements. These include: i) World Bank

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[17] World Bank (2013) Land Governance Assessment Framework Afghanistan: Final report. World Bank, Kabul.
[18] Pain, A. and D. Huot (2017) 'Afghanistan's "surplus" rural population' Secure Livelihoods Research Consortium Briefing Paper 24, SLRC, London.
[19] Education and Training Center for Poor Women and Girls of Afghanistan (2013) 'Women's land ownership in Afghanistan' USAID, Kabul.
[20] Ibid.
[21] Gatson, E. and L. Dang (2015) Addressing land conflict in Afghanistan, United States Institute of Peace, Washington DC.
[22] United National Assistance Mission to Afghanistan (2014) 'The stolen lands of Afghanistan and its people: the legal framework', UNAMA, Kabul.
[23] United Nations Assistance Mission to Afghanistan (2014) 'The stolen lands of Afghanistan and its people: the state land distribution system', UNAMA, Kabul.
[24] Wily, L. (2013) A Social Analysis of Land Expropriation Law of Afghanistan, World Bank, Kabul.

development policy support and USAID technical assistance support to the establishment and institutional strengthening of a new land management authority (ARAZI); ii) commissioning of an application of the World Bank Land Government Assessment Framework to identify weaknesses in the existing institutional and legal arrangements and provide recommendations for priority reforms; iii) commissioning technical reviews of previous draft versions of the new ARAZI Law and Land Acquisition Laws to inform subsequent legislative revisions and improvement; iv) supporting various steps in the policy formulation process through the multi-donor ARTF Incentive Program, including institutional reforms within ARAZI and development of new land legislation; and v) undertaking assessments of both the draft ARAZI Law and Land Management Law as recently approved by Cabinet to ensure that new legislation addresses identified weaknesses and gaps.

4. Assessments of new land laws undertaken for the purposes of this operation demonstrate that legislative changes will explicitly address many of the weaknesses identified through application of the World Bank land governance assessment. Recommendations made under this framework and addressed through the new ARAZI Law and Land Acquisition Law supported by the proposed operation include: i) recognition of a wider range of documentation to register public land; ii) establishment of an administrative land registration system, separate from the courts; iii) criminalization of land-grabbing through new legislative provisions; iv) establishing a definition of public interest in cases of public land acquisition; v) introduction of legal provisions ensuring fair and just compensation; vi) establishment of a centralized database for registering land titles; and vii) establishment of dispute resolution processes within ARAZI.

5. ARAZI's has developed technical capacity to manage these legislative reforms. Since its establishment, ARAZI's technical capacities have quickly developed. The number of staff has increased from 900 in 2013, to 1900 in 2016, while increased budgetary allocations have supported the development of systems and infrastructure. Development of institutional capacities has reflected international assistance, including through UN-HABITAT and the Turkish Land Administration Agency. ARAZI's recent work has demonstrated the substantial progress achieved, including contributions to implementation of the City for All (CFA) Program, under which ARAZI has surveyed 200,000 properties, with Occupancy Certificates prepared for issuance.

6. Reforms enjoy political support at the highest levels. Strategic leadership for planned reforms is being provided through the High Council for Land and Water. The High Council is chaired by the President, and includes all Cabinet members, the Head of ARAZI, other senior agency heads, and various advisors. ARAZI reports directly to the President.

7. Important risks remain. Given Afghanistan's overall weak governance environment, negative social and governance outcomes from poor implementation of the new legal framework remains a possibility. Table 5 presents a number of these risks. However, risks are mitigated both through the content of the new laws and accompanying implementation support measures. The World Bank is preparing an investment project to provide technical assistance to ARAZI for all aspects of implementation, including training of staff, institutional strengthening, and establishment of electronic systems. This project will be explicitly intended to ensure pro-poor and positive gender outcomes under the new legal framework. Further steps in policy processes, such as passage of laws and key implementation milestones, will be supported through various multi-donor policy-based engagements, including the ARTF Incentive Program, other development partner budget support arrangements, and potential new World Bank policy based budget support instruments. The Land Clearance process established under the Land Management Law further mitigates risks by requiring a Land Clearance

Commission to undertake site visits and public consultation when verifying land ownership under the Land Management Law. The membership of the Land Clearance Commission is established under the law, along with key requirements Land Clearance processes.

8. Risks will be closely monitored and mitigation measures will be implemented as necessary, through an Investment Project. During the preparation of the new World Bank Technical Assistance to ARAZI project, an initial baseline social assessment will be undertaken. The project will include an independent mid-term and end of project social impact assessments. The ARAZI stakeholder advisory forum, co-chaired by the CEO of ARAZI and USAID will continue to monitor the impacts and progress of implementation of both the LML and the LAL as well as the proposed alternative land dispute resolution law. The investment project will include an independent mid-term and end of project social impact assessments. The Bank is a key member of the stakeholder forum and collaborates with other partners including UN Habitat and FAO, which are also monitoring the status and impact of relevant laws in cooperation with urban community development committees and local mosques. Under the investment project to ARAZI, this approach would be adopted for both rural and urban pilot areas.

9. Overall, benefits of the supported legislative reforms to land administration justify risks. Improved land governance is vital: i) for development of agriculture, which will remain central to poverty reduction and growth; ii) to safeguard the property rights of vulnerable groups who have suffered from land-grabbing and have insufficient protection under existing laws; and iii) to address conflict and crime arising from the current inadequate land governance framework. Evidence from other low income countries shows that land tenure reform can bring benefits to poor households through improved land use even under difficult institutional conditions.[25] Central risks inherent in any land governance reform process can be managed. Key risks and mitigations are shown in the table below.

Table 3: Reforms to the legal framework for land - risks and mitigation

Risk	Mitigation
Land legislation submitted to Cabinet not passed into law or substantially altered prior to parliamentary approval by the National Assembly or Wolesi Jirga	The new legal framework for land has strong support at the highest levels of Government. New land laws will be presented to the National Assembly in the form of legislative decree, with the National Assembly required to consider the law in its entirety without the opportunity to revise specific provisions. While the rejection of the law remains a possibility, there has been no significant track record of rejected laws by the National Assembly. ARAZI is working actively on socializing the land governance reforms with the members of the National Assembly.
Ineffective implementation of new administrative system for land registration due to capacity and institutional constraints.	The World Bank is preparing an investment project to provide substantial capacity building and institutional support to ARAZI in implementing the new legal framework. This project will seek to ensure pro-poor outcomes under the new legislative framework. This project will incorporate the good international practices as well as technical experience from the ARAZI-Turkish land agency

[25] K. Deininger, D. Ali, S.T. Holden, J. Zevenbergen (2008) 'Rural land certification in Ethiopia: process, initial impact, and implications for the other African countries' World Development, 36 (10), pp. 1786–1812; S.T. Holden, K. Deininger, H. Ghebru (2009) 'Impacts of low-cost land certification on investment and productivity' American Journal of Agricultural Economics, 91 (2), pp. 359–373; S.T. Holden, H. Ghebru (2013) 'Household welfare effects of low-cost land certification in Ethiopia' S.T. Holden, K. Otsuka, K. Deininger (Eds.), Land Tenure Reforms in Asia and Africa: Impacts on Poverty and Natural Resource Management, Palgrave Macmillan, London & New York, pp. 137–161.

	partnership funded by the Turkish International Development Agency and also build upon the UN Habitat supported City for All Project being implemented with ARAZI, MUDH/ILDG.
Formalization of illegitimately acquired land.	Legislation has been designed explicitly to avoid the risk of formalizing recent illegitimate land acquisition, with landholders required to provide documentation of ownership or demonstrate occupation for a period preceding recent land-grabbing. The new legislative framework will support ongoing Government-led processes to identify and resolve instances of land-grabbing. ARAZI has a very reliable list of almost all of the estimated 16000 land grabbers throughout the country. Further, ARAZI has largely identified much of the grabbed lands, which includes those large tracts of rural lands under opium cultivation. In addition, there are 355 Shahrak or small towns both official and informal that have land ownership problems. ARAZI has blacklisted all of the lands identified as having been grabbed, and as such will continue to preclude the grabbers from securing any formal rights over these lands. The Land Management Law has very strict provisions for confirming the rights of land to occupants, including through claims of adverse possession. Moreover, the new law requires claimants to produce documentation and witness evidence of possession and occupation and also prove uninterrupted peaceful occupation for not less than 35 years. As such, these measures will mitigate most illegal claims.
Reduced tenure security for those without formal documentation.	Tenurial security will be strengthened for many of those currently lacking formal land rights through allowing the acceptance of a broader range of documentation, including customary documents, for registration of ownership. ARAZI is currently implementing the City for All program through which households in informal urban settlements are being provided with Land Occupancy Certificates (OC) conveying formal land rights. This project has already surveyed/registered 200,000 land parcels, with only 500 parcels remaining unresolved. The target is to issue 750,000 OC over urban areas before 2019.
Corruption in processes for land registration or vested interests influencing payments for land acquisition.	Corruption and pressure from vested interests in administrative systems is possible, but an important goal of the reforms is to move to an administrative system of land registration, thereby avoiding the court system which has previously been subject to widespread corrupt practices. New grievance processes within ARAZI and transparency provisions under the Land Acquisition Law should reduce scope for corruption. The land clearance process included in legislation is sufficiently robust to prevent compensation being paid to those with illegitimately acquired land.
Widespread illicit cultivation for opium production may deter participation in or generate resistance to land registration.	ARAZI intends to survey and register all land irrespective of use. In the event of opposition or disruption in areas where opium is cultivated, surveying and registration could be restricted to other areas without significantly undermining benefits of the reform. Opium cultivation lands, which are under control of powerful individuals, have been identified and blacklisted by ARAZI. They will have no rights conferred.
Reputational risks to World Bank arising from potential negative social or poverty effects.	Government is strongly committed to land administration reforms supported by the operation and welcomes World Bank support. Risks must be considered against benefits of lending substantive support to Government in one of its highest priority reform areas.

ANNEX 6: SUMMARY OF RECENT WORLD BANK LAND ENGAGEMENTS

Dates	Account of Engagement	Supporting WB Documents
2006-2007	**Analytical work leading to National Land Policy 2007**. In the context of increased government investment in infrastructure and concerns regarding both the time taken for land acquisition and short-comings in associated safeguards, World Bank prepared and consulted widely on an analytical report on land acquisition issues. This work ultimately supported a new Land Policy (2007) and informed subsequent efforts to revise the Land Expropriation Law (LEL).	World Bank (2007): Land Acquisition in Afghanistan. Report
2008-2010	**Attempts to reform land acquisition law.** Technical assistance by USAID and DFID supported the establishment of ARAZI as a department under the Ministry of Agriculture and irrigation. WB dialogue on the LEL continued but progress was hampered by ARAZI's limited mandate and ambiguity over land-related institutional responsibilities of other Ministries and agencies.	World Bank (2009). Comparative analysis Afghan Law and Practice on land acquisition/resettlement and WB OP.4.12. Paper.
2011-2013	**Preparation of "Promoting Economic Growth and Fiscal Sustainability" DPG Series.** In the context of growing interest in mining development in Afghanistan, land governance reform received renewed attention. Reflecting government commitment to improving land governance, Government and the Bank agreed to the inclusion of a range of land-related institutional and legal reforms in a new DPG Series. Institutional reforms within ARAZI progressed quickly. ARAZI was granted status as an independent agency, receiving formal custodianship over the LEL, LML, and the cadaster. As part of the DPG PSIA, two social impact assessments of the existing land governance laws were prepared to inform the legal drafting process and identify opportunities to address social, poverty and fragility dimensions of land governance reforms. With World Bank support, ARAZI initiated a land governance assessment framework (LGAF) which provided the analytical foundation for the preparation of a new Government-executed IPF. Through the WB executed Resource Corridor TA initiative, the World Bank also assisted ARAZI with the preparation of 5 year strategic and operational plan, including a clearly defined Governance structure and human resource plan. Cabinet approval of both were included as triggers for the second DPG in the series. Implementation of the series was disrupted by the contested presidential election and subsequent formation of the National Unity Government. The LEL and LML were not approved within planned timeframes and the second operation of the program was ultimately cancelled. Political commitment to land governance reforms remained strong, however, and Government sought to include approval of the new laws as prior actions under the ARTF Incentive Program.	World Bank (2011): Land Registration Process in Balkh. Report World Bank (2013): Protecting Peoples' Interests? A Social Analysis of Land Expropriation Law of Afghanistan. TA Report World Bank (2013): The Afghanistan Land Management Law, 2008. Social Impact Assessment. TA Report. World Bank (2012 and 2013): LEL and LML assessments of proposed changes.
2014-2015	**Afghanistan Resource Corridor Project PRGF**: Under this project, the World Bank continued to support ARAZI, with: i) legislative revisions to the Land Management Law (LML) and the Land Expropriation Law (LEL),	ARCP (2015): Annual Report

	ii) drafting procedure on effective land use to protect public land, mitigate land grabbing, and increase national revenue through proper and effective use of land; iii) preparation of a comprehensive capacity building plan; iv) technical assistance for developing a 5 year preventive strategy for land grabbing, approved by the High Council of Land and Water; v) technical assistance in drafting land dispute resolution regulation; and vi) preparation and approval of a restitution policy for grabbed lands approved by Council Ministers.	World Bank (2015): Afghanistan Land Governance Assessment ARAZI (2014): 5 year Strategic and Operational Plan.
2016-2017	**Preparation of "Inclusive Growth" Development Policy Grant:** Reflecting strong commitment to reform of land laws by the National Unity Government and H.E. President Ashraf Ghani, the LEL and LML were included in the new Mutual Accountability Framework. In order to provide additional support to approval of the new laws in the context of a mounting returnee and refugee crisis, Government agreed with the Bank to include approval of the LEL and LML as prior actions for the proposed Inclusive Growth Development Policy Grant. Work is now ongoing to support implementation of the new laws. Partly in response to the returnee and IDP crisis, new regulations are being prepared to recognize the occupancy rights of poor households in informal settlements under the new law. The World Bank is preparing a major project to support implementation of the new laws and is already supporting ARAZI with establishing grievance redress mechanisms, including hotlines, public information systems, and citizen feedback mechanisms.	World Bank (2017): Assessment of changes in Cabinet-approved LEL and LML