Research Article

WTO Accession of Afghanistan: Costs, Benefits and Post-accession Challenges

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Abstract

This article undertakes a cost and benefit analysis of Afghanistan's accession to World Trade Organization (WTO) while attempting to shed light on the post-accession challenges. For the empirical part of our analysis, we have applied the WITS/SMART model to assess the implication of WTO membership. The partial equilibrium model embedded in World Integrated Trade Solution (WITS) allows users to estimate the impact of tariff reductions on trade flows, tariff revenue, and consumer surplus for a single market at a time. Tariff cut is an independent variable, and government revenue, trade creation, consumer welfare and general welfare of the economy are the other variables. The results show that Afghanistan consumers stand to benefit from tariff reforms with overall positive welfare gains to the economy. However, a reduction in tariff will lead to a fall in government revenue and a substantial increase in imports which may raise some concerns over the negative trade balance. The last section of the article studies the post-accession challenges of WTO accession with a special focus on developmental, institutional, legal and environmental challenges. Our analysis based on the sectoral mix of Afghanistan's economy suggests that producers will lose out. Findings of this study support the argument to maintain maximum policy space for Afghanistan for its long-term development need purposes.

JEL: F13

Keywords

Liberalization, WTO accession, Afghanistan, WITS/SMART model, trade

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Introduction

Having completed the bulk of the accession formalities,[1] Afghanistan is scheduled to become the 35th least developed country (LDC)[2] member of the World Trade Organization (WTO). Afghanistan is a landlocked country, but strategically located at the heart of the Silk Road,[3] which even today can serve as the 'trade and transit hub' of Central Asia and South Asia.[4] It is believed that sustainable economic growth through attracting significant trade and investment cannot be achieved without broader integration into the world economy. Afghanistan National Development Strategy (ANDS) explicitly recognizes the role of trade for economic development and highlights Afghanistan's integration into the world economy as one of the key development goals for which membership to WTO is an essential step (GoIRA, 2008). Economic growth and poverty reduction are the core objectives of ANDS,[5] which place greater emphasis on a free market and private sector-led economy.

Almost all trading partners of Afghanistan at South Asian Association for Regional Cooperation (SAARC), Central Asia and West Asia are either WTO members or are in the process of accession. Therefore, WTO membership gives Afghanistan a broader chance for fair trade through a dispute settlement mechanism at WTO (MoCI, 2012). However, WTO accession requires extensive reforms to adjust to its rules and regulations to be compatible with the multilateral trade regime under the WTO. These compliance requirements themselves pose a real challenge to an LDC like Afghanistan. Keeping in view the development objectives of the Afghan Government, this article undertakes the cost–benefit analysis of Afghanistan's accession to WTO and assesses the challenges for post accession. The objective is to identify key sectors of the economy where policy space needs to be preserved to address future development challenges. Furthermore, the study provides an ex-ante and ex-post assessment of Afghanistan's accession to WTO. Cost and benefit analysis in this study is a pre-accession stimulation, while in a separate section we study the post-accession challenges.

The study is structured as follows. The second section of the article presents an overview of the trade and economic profile of Afghanistan. The third section briefly presents the WTO accession process of Afghanistan, while the fourth section is devoted to the empirical part of the study by undertaking the simulation of costs and benefits of WTO accession in terms of the consumer and welfare gain and implication on government revenue. This will allow us to identify sensitive sectors of the economy. In the fifth section, the post-accession challenges are briefly discussed. Finally, the sixth section concludes the article.

Economic and Trade Profile of Afghanistan

Afghanistan Economy: A General Overview

Afghanistan is a landlocked, war-torn and aid-dependent economy. The total area of the country is 652,864 km^2 and the population is approximately 30 million out

Table 1. Structure of Afghanistan Economy for the Year 2012

Indicator	Value (%)
Population (million)	29.82
GDP (US$ billion)	20.5
GDP per capita (US$)	687
GDP growth (%)	14.40
Inflation (%)	7.20
Imports of goods and services as percentage of GDP (%)	39.20
Exports as percentage of GDP (%)	5.50
Current account deficit (US$ billion)	7.5
Services as percentage of GDP (%)	53.5
Trade in services (%)	25.90
Agriculture value added as percentage of GDP (%)	24.60
Industry as a percentage of GDP (2011) (%)	22.50

Source: World Bank (2013).

of which 78 per cent is living in the rural areas (AISA, 2013). It is primarily an agrarian economy (75 per cent of the population; World Bank, 2013). For details of the economic structure, see Table 1. The per capita GDP of the country amounted to US$ 687 in 2012 with a staggering economic growth of 14.4 per cent. Real GDP growth for the same period was 9.2 per cent and the inflation rate was 6.4 per cent (CSO, 2013). In 2012, agriculture contributed 24.6 per cent to the GDP. Industry is at a very primary stage of development and more or less run at a small scale. The industrial produce of the country includes textiles, soap, furniture, shoes, fertilizers, leather, non-alcoholic drinks, cement, carpet and natural gas. The industrial products of the country are mainly meant for the domestic consumption and do not have much contribution to the foreign exchange earning of the country. Measures like Human Development Index (HDI) place Afghanistan at a very low level of human development when measured by health, education and living standards. These measures reflect the results of decades of conflict, which has destroyed much of the agricultural and industrial capacity of the country. Even after several years of economic growth since international forces intervened and toppled the government in 2001, estimates place 42 per cent of the population below the national poverty line.

Exports and Imports

As in 2011, the export–import ratio of the country was 20 per cent (World Bank, 2012). The larger portion of exports of the country consists of dried fruits, saffron, fresh fruits, rags, leather and precious stones to the target markets, such as Pakistan, India, United Arab Emirates, Kazakhstan, Uzbekistan and some other countries. Import portfolio of the country includes almost everything from food to industrial products, automobiles, heavy machines and energy. Since its establishment in 2002, the Government of Afghanistan has understood the importance of trade with its neighbours and has tried to integrate with them through membership in regional organizations like SAARC to which Afghanistan became a member in the year 2007 and Shanghai Cooperation Organization (SCO) in which Afghanistan is an observer since 2012.

The major trade partners are those which are the members of regional organizations, such as SAARC and SCO with whom Afghanistan is already a trade partner, and have agreed on minimum tariffs. Yet, it has not been able to capture a significant share in the regional organizations as markets for its exports. SAARC member states have signed the South Asian Free Trade Area (SAFTA) according to which the non-least developed contracting states (NLDCS), such as India, Pakistan and Sri Lanka and the other five least developed contracting states (LDCS) including Afghanistan would bring down their tariffs to 20 per cent and 30 per cent, respectively.[6] In addition to this, Afghanistan has signed preferential trade agreement (PTA) with India, according to which it has agreed to reduce its tariffs for some necessary goods, such as tea, medicines, sugar and cement imported from India.

The total value of exports of the country amounted to 370 million dollars in 2012 with a meagre share of 0.03 per cent of world exports. Eighty-six per cent of total exports earnings were from agricultural products, while 14 per cent were from manufactured commodities. Pakistan, India, Iran, Saudi Arabia, Russia and the European Union are the major export destinations of the country (Figure 1). Afghanistan is a net importer sourcing almost everything from abroad, from heavy machinery, automobiles and technology to textiles and food. The major supplying countries are Pakistan, China, Japan, Iran, India, European Union and some other countries (Figure 2).

SAARC countries alone make up 60 per cent of the export markets for Afghanistan,[7] and Afghanistan imports 30 per cent of its requirements from SAARC countries. The Afghanistan–SAARC trade intensity index has declined, but the trade growth has had fluctuations.

The export–import gap in Afghanistan is always very huge. The data for exports and imports are available for the years 2007–2012. Figure 3 depicts this gap.

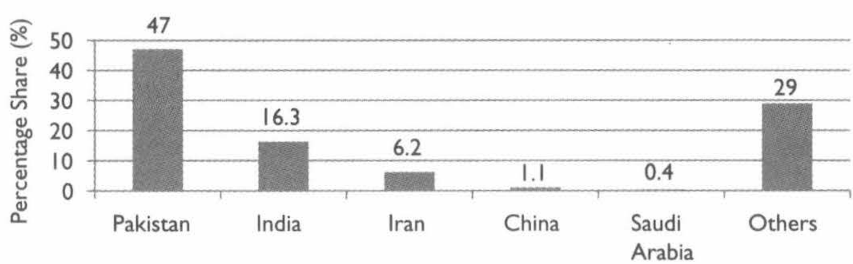

Figure 1. Export Desitnations of Afghanistan for the Year 2012

Source: WTO (2012), CSO (2013).

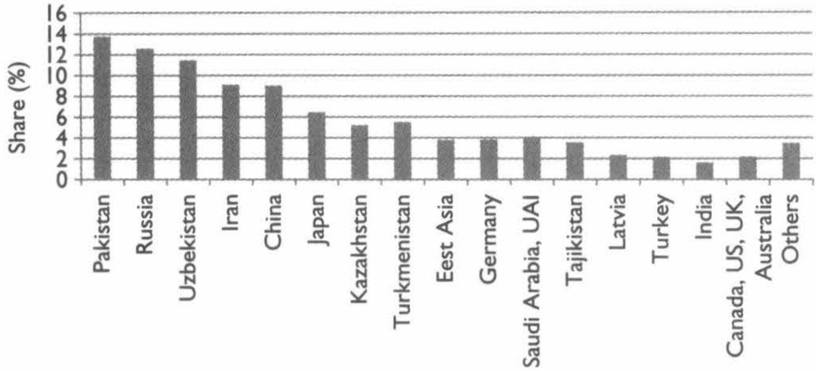

Figure 2. Major Suppliers to Afghanistan

Source: WTO (2012), CSO (2013).

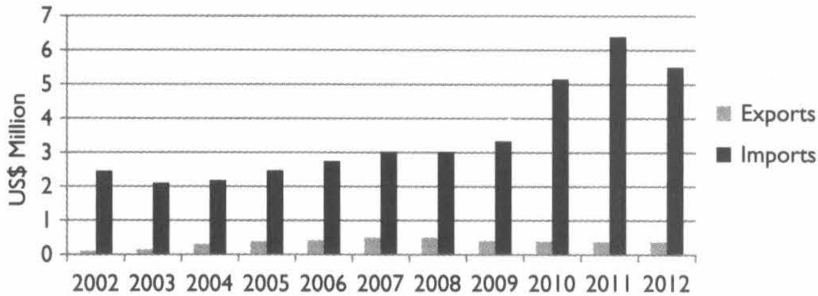

Figure 3. Exports and Imports of Afghanistan

Source: CSO, 2012.

The export–import ratio has always been much below 20 per cent. For instance, in the year 2002, when the country was just recovering from conflict and the foreign aid started flowing to the country, the ratio was approximately 4 per cent, and it kept on increasing normally till 2008, when the ratio was 18 per cent. Later on it started declining and reaches 6.8 per cent in 2012.

The export growth rate of the country has not been so fascinating as well. If we take 2002 as the base year for the country's export performance, again the data show that this growth has been smooth till 2008 (4 per cent growth in comparison to 2002) and then goes through a steady decline to 2 per cent in 2012. The average growth rate of exports for this period is approximately 2.78 per cent per year. One of the fundamental reasons for exports lagging behind imports is the fact that the country heavily relies on the foreign aid and aid-funded projects that constitute the major portion of imports, such as machinery and oil. The fiscal gap in 2007–2008 was 70 per cent, which reduced to 34 per cent in 2012 and has been financed by aid throughout.

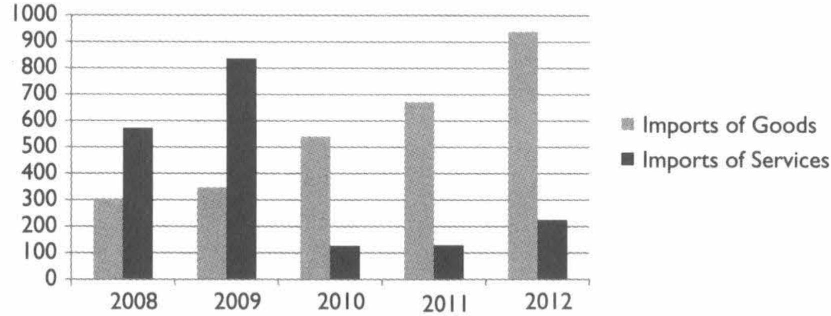

Figure 4. Imports of Goods and Services (Value in US$ 100 Million)

Source: World Bank, 2013.

Imports of goods and services in Afghanistan change depending on the circumstances. For instance, till 2008, due to the lack of capacity, the country had to avail of foreign consultancy services in all walks of public management, and, therefore, the share of services is more than that of goods, while later on services imports declined and goods imports increased (Figure 4). However, the investment in services is one of the potential sectors to grow far better and attract foreign direct investment more than the production sector in case Afghanistan accesses to WTO and reduces its charges for the foreign businesses in services.

Tariff Profile of Afghanistan

Since the inception of the post-Taliban regime in Afghanistan, in order to maintain the prices at an affordable level to the consumers, without regard to the current account deficit, the Government of Afghanistan has maintained the tariff level to the minimum possible. The tariff structure maintained by the Afghanistan National Tariff Schedule (ANTS) is based on a harmonized commodity description and coding system[8] and the tariff rates consist of 14 tariff bands which range from 0 to 50 per cent (Table 2).

Table 2. Tariff Structure of Afghanistan in the Year 2012

Serial No.	Tariff Band (%)	No. of Tariff Lines	Share in Total
1	0	27	0.503
2	1	83	1.545
3	2.5	1,510	28.114
4	3.5	10	0.186
5	5	2,255	41.985
6	8	28	0.521
7	10	1,123	20.909

(Table 2 Continued)

(Table 2 Continued)

Serial No.	Tariff Band (%)	No. of Tariff Lines	Share in Total
8	12	4	0.074
9	16	207	3.854
10	20	21	0.391
11	25	38	0.708
12	35	4	0.074
13	40	9	0.168
14	50	4	0.074
15	Prohibited	48	0.894
	Total	5471	100

Source: WTO Working Party Report, 2012.

Prohibited goods include those goods which are illegal as per the constitution of the country, such as alcoholic drinks, pork, illegal drugsand so on. Vehicles and salt are the commodities with highest tariff band (35 per cent–50 per cent), followed by furniture, fruits, nuts, processed marbles and carpets (25 per cent). Apart from tariff regulations, tax rate ranging from 2 per cent to 3 per cent is also levied on all imports.

Currently, the tariff structure provided for in the legal documents includes the following provisions:

- Ad valorem tariffs (presently applied);
- Specific duties, calculated and charged as fixed amount per quantity;
- A combination of ad valorem tariffs and specific tariff rates and
- Preferential tariff rates (only for some goods imported from India in line with the Indo-Afghan PTA).

Customs valuation is done on the basis of Article VII of General Agreement on Tariffs and Trade (GATT). Valuation is based on the transaction value of the goods subject to adjustments due to the inclusion of the cost insurance and freight charges. There are no VAT and excise duty applicable at the customs stations. Afghanistan's tariff is one of the lowest among LDCs for most of the commodities (World Bank, 2010). The tariff structure is slightly progressive, and richer groups tend to pay higher duties for their imports, according to household consumption data for a basket of basic goods from the 2008 National Risk Vulnerability Assessment.[9]

Afghanistan's Tariff in Comparison to Other LDCs

Although Afghanistan is not yet a member of WTO, the applied tariffs of the country are still lower than many of the LDCs. This is evident from Figure 5

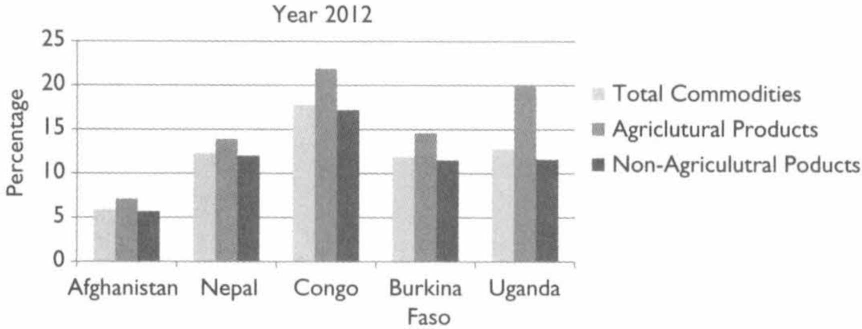

Figure 5. Comparison of Simple Average MFN Rate between Five LDCs
Source: WTO, 2013.

which compares the simple average most favoured nation (MFN) rates of a few selected LDCs. Among the five LDC members of WTO, Afghanistan has the least tariffs both for agricultural products and non-agricultural products. In the year 2012, the MFN rate applied was below 5 per cent which covered 73.8 per cent of the non-agricultural imports and 60.2 per cent of the agriculture imports, while 15.6 per cent of the agriculture imports and 2.7 per cent of the non-agriculture imports were tariff between 15 per cent and 25 per cent. Maximum tariff for the same year was applied for transport equipment at the rate of 50 per cent.

In the following section, we briefly discuss Afghanistan's accession process to WTO.

Afghanistan's Accession Process to WTO

Afghanistan applied for WTO accession in 2004 for the following objectives[10]:

1. Secure stable and non-discriminatory access for Afghan exports
2. Control over unfair treatment of Afghanistan's goods and services in foreign markets
3. Secure non-discriminatory transit for Afghanistan's exports
4. Modernization of the economy
5. Enhance economic growth and development
6. Increase fiscal revenue
7. Good governance, enhancement of the rule of law and transparency in the system

The accession process has been very slow and sluggish. However, as it can be observed from Table 3, Afghanistan has made significant progress beginning

Table 3. WTO Accession Process of Afghanistan

1.	**Application received**	21 November 2004
2.	**Working party established**	13 December 2004
3.	**Memorandum of Foreign Trade Regime (MFTR) submitted**	31 March 2009
4.	**Replies to the questions raised**	26 July 2010
5.	**Meetings of the working party**	31 January 2011 18 June 2012 7 December 2012 25 July 2013
6.	**Other documentation**	
	(a) Additional questions & replies	19 November 2012 31 October 2012 10 April 2013 7 June 2013 27 June 2013 2 July 2013
	(b) Information on agriculture (WT/ACC/4)	29 October 2012
	(c) Information on services (WT/ACC/5)	
	(d) SPS/TBT checklists (WT/ACC/8)	6 February 2012 (SPS) 26 April 2012 (TBT) 7 June 2012 (SPS)
	(e) TRIPS checklist (WT/ACC/9)	28 October 2011 19 November 2012
	(f) Legislative action plan	28 October 2011 6 June 2012 5 December 2012 15 July 2013
7.	**Market Access Negotiations**	
	Goods offer	
	(a) initial	14 November 2012
	(b) latest	
	Services offer	
	(a) initial	13 June 2012
	(b) latest	
8.	**Factual summary**	3 May 2012
9.	**Elements of a draft working party report**	9 November 2012 14 November 2012
	Draft working party report	24 June 2013

Source: WTO website http://www.wto.org/english/thewto_e/acc_e/a1_afghanistan_e.htm from 2009 completing bulk of accession negotiation both in multilateral and bilateral tracks.

Afghanistan launched service negotiations in June 2011, and submitted the goods offer during the first week of October 2012 in order to start bilateral negotiations on goods at the end of 2012 (WTO, 2013). At the fourth meeting of the working party on 25 July 2013, WTO members commended Afghanistan for its strong commitment matched by its technical inputs to advance its WTO accession negotiations to closure (WTO, 2013). At the agriculture plurilateral negotiations on 25 July, chaired by the WTO Secretariat, members welcomed Afghanistan's commitment to bind export subsidies at zero and also welcomed the fact that its domestic support was concentrated in the 'Green Box' (i.e., domestic support for agriculture that is allowed without limits because it does not distort trade, or at most, causes minimal distortion; WTO, 2013).

Cost–Benefit Analysis

Costs and Benefits of Afghanistan's Accession to WTO

According to one study, net benefits from accession seem strictly positive (Anderson, 1998). This strong assertion on the net benefit of WTO accession implies that whatever the cost might be, the positive effect thereof can generate sufficient welfare for the economy. This notion of cost–benefit disregards the sectoral mix of the economy, and believes that as long as the loss of one sector is more than compensated by gain in the other sectors, the economy is at a better position and there is a Pareto improvement. Institutional reform after WTO accession is another very important factor for the economic growth of a country.[11] Institutional and legal framework adjustment to WTO prescription is an impetus to economic efficiency, growth and enhanced welfare.

Studies on LDCs are not as optimistic on the positive impact of WTO accession as the above findings. The benefits from WTO membership in terms of improved market access for traditional exports are likely to be limited for vulnerable economies and developing countries. However, by submitting a wide range of trade-related policies to international scrutiny and by entering into binding commitments on the conduct of these policies, reform-oriented governments in these economies can make it more likely that their reforms will be successful (Langhammer & Lücke, 2001).

WTO promotes trade liberalization and free trade. Trade liberalization has been beneficial for many countries, but the gains from liberalizing reaming of protection may be outweighed by the costs. Tariff revenue losses even outweighed by gain in other areas are very significant. Total tariff losses for developing countries under the non-agriculture market access (NAMA)[12] could be US$ 63.4 billion or almost four times the benefit. Countries in Sub-Saharan Africa and Middle East, and Bangladesh with large informal economies and where tariff revenues are important for government revenues are predicted to be net losers in terms of benefits. They will also suffer even larger losses in tariff revenues (Gallagher & Kumar, 2006).

Here, we attempt to shed some light on the costs and benefits of WTO accession for Afghanistan. The result of the study will guide policy-makers to identify the most sensitive sectors of the economy, in which sector policy space is required to address future development goals. Afghanistan as an LDC and landlocked country (LLC) can benefit from integration to the global economy through WTO membership significantly. The country is one of the important producers of dry fruits[13] and carpet[14] in the world, whereas the WTO membership provides greater opportunities to exploit the vast potential in the international markets and emerge as a major player in these two commodities. Similarly, cheap raw material and labour, untapped resources like iron, copper, coal and host of other mineral resources can change the development trajectory of the country attracting much needed investment (FDI), which is encouraged and facilitated by WTO regulations. Furthermore, Afghanistan is an important tourist destination and WTO regulations on services[15] can help the country to enhance this business at the regional and international levels.

While the benefits of trade liberalization are of paramount importance, the cost is nonetheless critical for any country, especially for vulnerable economies. Import liberalization through tariff cuts for a small country like Afghanistan may bring down the prices by the amount of tariff cuts, increase the imports and decrease the government revenue from tariffs. The general welfare of the economy, which is a combination of consumer surplus, producer surplus and government surplus (government revenue), depending on the effect of tariff cuts for different countries, may be either negative or positive. According to the theory, the consumer surplus is positive due to cheaper prices of commodities. The producer surplus can take either positive or negative sign. If the producer is competitive and benefits from cheap imported raw material that would enable her to increase sales at a lower price both at the domestic and international markets, it may gain from liberalization. But, if the firm uses domestic raw material and produces for the domestic market, liberalization may be detrimental to it. Therefore, an industry in the country may lose or gain from the trade, depending on their competitive position. In case of Afghanistan, since industries are at their primitive stage, import liberalization may affect them negatively. Government revenue, on the other hand, may increase due to increased imports or can fall due to reduced tariffs.

Although Afghanistan's current applied tariff rates are very low[16] and the country as an LDC may not be required to undertake further commitment to reduce its current MFN applied tariff rates, still it has to bind its tariffs at certain rates. Now which products are to bind at a higher rate and which ones to a lower rate so that the average will comply with the WTO stipulations? In order to maintain the maximum policy freedom, Afghanistan has to have a clear idea of the cost and benefits corresponding to each commodity or group of products. The country needs to maintain certain policy freedom suitable to its long-term development goals.

Methodology

An ex-ante analysis of the cost and benefits of a policy change is cumbersome task, and one such model which can capture all variables and establishes relationship between all factors concerned is general equilibrium analysis. But, this undertaking on one hand requires a lot of data for every variable, while on the other hand, there is no customized tool to calculate this model. Exhaustive quantitative measurement of the expected benefits and costs is beyond the scope of this study. However in a similar study, the Asian Development Bank[17] has used the partial equilibrium model to assess the welfare and revenue implication of SAFTA. Otheino and Shaniyekwa (2011) have used the same model to assess the effect of tariff reduction[18] on trade, welfare and revenue of Uganda.[19] Following the same methods used in similar studies, we undertake a partial equilibrium analysis of tariff cuts.

The independent variable in this study is tariff cuts and dependent variables are trade creation, government revenue, consumer surplus and welfare. There are various tools to run partial equilibrium analysis, among which we use the World Bank/United Nations Conference on Trade and Development (UNCTAD) SMART stimulation model that is a suitable tool to assess the costs and benefits of accession to WTO. This model was developed by James and Olarreaga (2005) and operationalized by the World Bank.[20] The impact of reducing tariffs on the basis of this model is given in Figure 6.

Applying SMART Stimulation for Afghanistan and Analysis of the Results

We use the COMTRADE and TRAINS data to run the stimulation. In our model, we consider the products from Nomenclature HS2 which includes 97 chapters across industries and sectors.

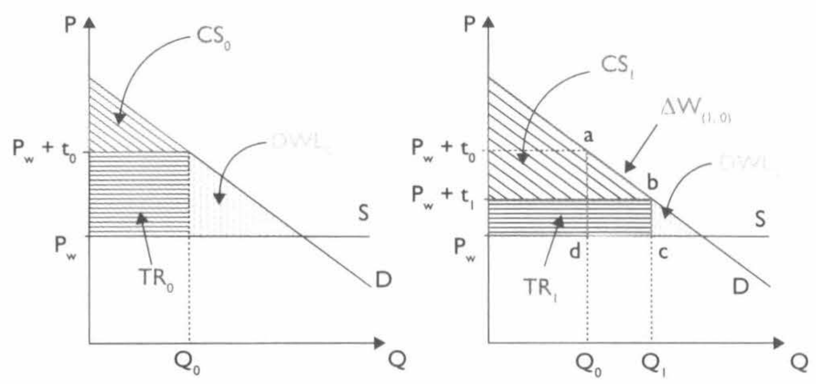

Figure 6. Impact of Reducing Tariffs

Source: WITS/SMART User Manual, Smart Framewor, p. 171.

Table 4. Top 25 Products with Greatest Trade Effect (Value in US$ Million)

Rank	HS Code	At 10% Tariff Cut	At 5% Tariff Cut
1	87	39.70	19.85
2	11	35.49	17.75
3	12	23.71	11.85
4	27	10.97	5.49
5	85	2.83	1.41
6	84	1.91	0.96
7	93	1.84	0.92
8	86	1.82	0.91
9	7	1.81	0.90
10	4	1.79	0.90
11	10	1.61	0.80
12	90	1.49	0.00
13	16	1.49	0.74
14	25	1.44	0.72
15	57	1.38	0.69
16	39	1.37	0.68
17	24	1.36	0.68
18	72	0.98	0.49
19	44	0.95	0.48
20	8	0.91	0.12
21	73	0.77	0.39
22	63	0.72	0.36
23	88	0.65	0.32
24	18	0.64	0.10
25	34	0.57	0.28
Total of 97 chapters		145.01	89.81
Total of top 25 items		137.64	67.51
Percentage in total		94.92	75.17

Source: Author's calculation of the model from COMTRAD.

Table 5. Top 25 Products with Greatest Revenue Effect (Value in US$ Million)

Rank	HS Code	At 10% Tariff Cut	At 5% Tariff Cut
1	87	–3.79	–1.88
2	11	–3.73	–1.84
3	12	–3.16	–1.50

(Table 5 Continued)

(Table 5 Continued)

Rank	HS Code	At 10% Tariff Cut	At 5% Tariff Cut
4	27	–2.68	–1.34
5	85	–2.19	–1.09
6	84	–1.70	–0.85
7	93	–1.41	–0.70
8	86	–0.88	–0.44
9	7	–0.87	–0.44
10	4	–0.83	–0.42
11	10	–0.79	–0.39
12	90	–0.70	–0.35
13	16	–0.67	–0.01
14	25	–0.65	–0.32
15	57	–0.61	–0.30
16	39	–0.51	–0.10
17	24	–0.49	–0.01
18	72	–0.47	–0.02
19	44	–0.42	–0.21
20	8	–0.39	–0.19
21	73	–0.38	–0.15
22	63	–0.35	–0.17
23	88	–0.35	–0.17
24	18	–0.22	–0.11
25	34	–0.22	–0.10
Total of 97 chapters		–31.15	–15.27
Total effect of top 25 chapters		–28.25	–12.99
Percentage in total		90.70	85.09

Source: Author's calculation of the model from COMTRAD.

Table 6. Top 25 Products with Greatest Consumer Surplus Effect (Value in US$ Million)

Rank	Product Code	At 10% Tariff Cut	At 5% Tariff Cut
1	87	3.15	1.62
2	11	1.57	0.81
3	12	0.98	0.50
4	27	0.65	0.33
5	85	0.24	0.12
6	84	0.21	0.11

(Table 6 Continued)

(Table 6 Continued)

Rank	Product Code	At 10% Tariff Cut	At 5% Tariff Cut
7	93	0.17	0.09
8	86	0.16	0.08
9	7	0.15	0.08
10	4	0.13	0.07
11	10	0.12	0.06
12	90	0.10	0.05
13	16	0.10	0.05
14	25	0.09	0.01
15	57	0.08	0.04
16	39	0.08	0.04
17	24	0.06	0.03
18	72	0.06	0.03
19	44	0.06	0.03
20	8	0.05	0.02
21	73	0.04	0.02
22	63	0.04	0.00
23	88	0.04	0.01
24	18	0.03	0.00
25	34	0.03	0.02
Total effect of 97 Chapters		8.80	5.34
Total of Top 25 Items		8.38	4.21
Percentage in Total		95.1620714	78.89283802

Source: Author's calculation of the model from COMTRAD.

Table 7. Top 25 Products with Greatest Welfare Effect (Value in US$ Million)

Rank	HS Code	At 10% Tariff Cut	At 5% Tariff Cut
1	87	10.638	5.459
2	11	2.121	1.089
3	12	1.686	0.865
4	27	0.944	0.484
5	85	0.291	0.149
6	84	0.220	0.113
7	93	0.203	0.010
8	86	0.194	0.099
9	7	0.174	0.089

(Table 7 Continued)

(Table 7 Continued)

Rank	HS Code	At 10% Tariff Cut	At 5% Tariff Cut
10	4	0.161	0.083
11	10	0.138	0.071
12	90	0.130	0.067
13	16	0.128	0.066
14	25	0.118	0.060
15	57	0.106	0.054
16	39	0.091	0.047
17	24	0.078	0.040
18	72	0.069	0.010
19	44	0.063	0.032
20	8	0.056	0.029
21	73	0.053	0.027
22	63	0.047	0.024
23	88	0.045	0.002
24	18	0.043	0.022
25	34	0.035	0.000
Total effect of 97 Chapters		18.27	10.14
Total of Top 28 Items		17.79	8.99
Percentage in total		97.38327782	88.66513246

Source: Author's calculation of the model from COMTRAD.

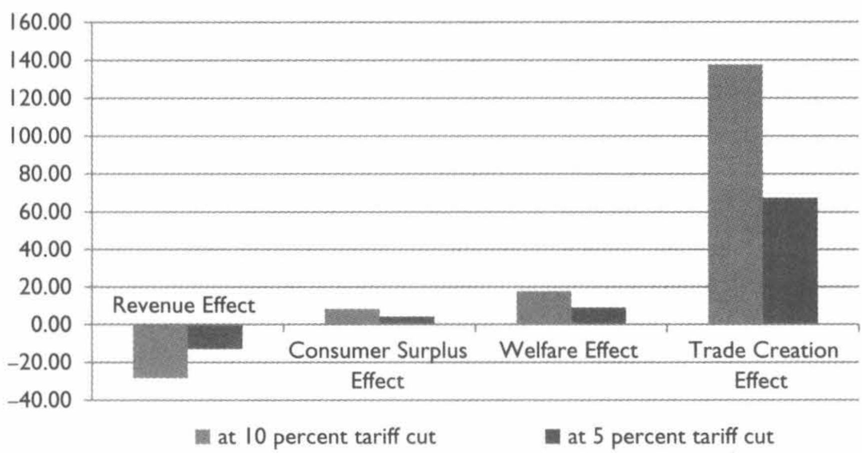

Figure 7. Partial Equilibrium Results of Top 25 Tariff Schedules (Value in US$ Million)

Source: Results of the model. Author's calculation from COMTRAD.

Table 8. Comparative Costs and Benefits of Tariff Cut (Value in US$ Million)

Effect of Tariff Cut	At 10% Tariff Cut	At 5% Tariff Cut
Revenue Effect	–28.25	–13.00
Consumer Surplus Effect	8.38	4.21
Welfare Effect	17.79	8.99
Trade Creation Effect	137.64	67.52

Source: Author's calculation from COMTRAD.

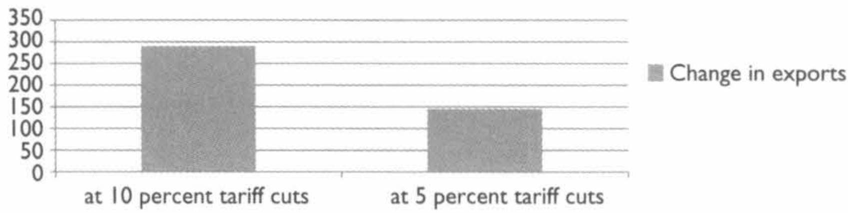

Figure 8. Change in Exports Revenue of Afghanistan's Trading Partners (Value in US$ Million)

Source: Author's calculation of the model from COMTRAD.

Post-accession Challenges

Development Challenges: Support to Agriculture and Infant Industries

Our empirical analysis in the previous section highlights the expected benefits and costs in terms of consumer welfare, efficiency and revenue. Consistent with the theory, our results show that at 10 per cent and 5 per cent tariff cuts, consumers will gain, government revenue will fall and imports will increase. But the SMART stimulation does not incorporate producers in the calculation of cost and benefits, while the theory suggests that small farmers lose as a result of trade liberalization (Reddy, 2007). However, our motivation is to assess the cost and benefits of accession, but our results except for the revenue loss do not explain other implications on the economy. An important aspect of development in all schools of thoughts is economic growth. GDP growth is a necessary condition for development. Therefore, for an economy to grow, it has to produce more goods and services, export more and gain more market share in the global markets. Neoliberals take this point as ransom and argue that increased market share can be obtained by uninterrupted market forces and liberalization of the economy. This is exactly what WTO also promotes: in order to have growth we need to produce more; production requires larger market (demand) and this can be attained through international trade and trade can grow in a free trade regime, which brings efficiency in international allocation of resources. This regime is facilitated by WTO agreements. The acceding member has to harmonize its national laws with the WTO trade laws and abide by MFN treatment of all WTO members with whom the country has signed MFN agreement. This implies that the country loses policy space for its national development strategies with WTO accession.

Here, we first look at the story of the production sector in Afghanistan and assess how it will likely be in the post accession; secondly, we will highlight the necessity of maintaining broader and more nationally favourable policy space in support of production sector for long-term development purposes.

Agriculture is the most important production sector of Afghan economy (20 per cent of GDP, 2013). Due to its significance, the Government of Afghanistan has announced that agriculture and industry are the top priority investment sectors in the country (Government of Afghanistan, 2013). Incentives are given in terms of tax exemption, land acquisition, licence provision and export facilitation for domestic and international investors to commit their capital for production (AISA, 2013). On the other hand, liberal import policies have been adopted to support consumers (MoCI, 2012). Because of predominance of wheat in agriculture and historical importance and potential growth of textile, two representatives from agriculture and industry, the potential effect of liberalization on domestic producers is in these two sectors.

Wheat

Wheat is an important food staple in Afghanistan and almost all farmers allocate a part of their land (70 per cent of cropped area) or a season of production for wheat cultivation either for household consumption or for commercial purpose. In 1978, Afghanistan was self-sufficient in food production for its 14 million people (AREU, 2011), but nearly two decades of war damaged or destroyed irrigation canals and storage and market infrastructure, severely decreasing the productive capacity of the wheat sub sector. Consecutive years of drought further constrained agricultural production. Furthermore, numerous policies and programmes on wheat within the region create significant obstacles and disincentives to investment. For example, a few mills that have been established in Afghanistan with the help of foreign assistance have difficulty competing with Pakistani mills that receive subsidized credit and other forms of assistance.

In 2003, the total quantity of domestically produced wheat that was marketed may have amounted to 25 per cent of the country's production (Chabot & Dorosh, 2007). According to Persaud, recent trends in Afghanistan's limited available data are consistent with an own-price elasticity of 0.20, that is, a 1 per cent increase in the real price of wheat is associated with a 0.20 per cent increase in wheat area in the following year, everything else remaining the same. Hence, from these findings, one can infer that there is likely a relationship between prices and production of wheat.

United States Agency for International Development report (USAID, May 2007) concludes that continuous inflow of wheat to Afghan markets is important for food security and price stability, but it does not address the impact of extended wheat imports on the local wheat production. Afghan flour producers face challenges of inadequate domestic supplies of wheat and competition from imported flour (flour can be proxy for wheat), much of it from neighbouring country Pakistan, where wheat producers and flour millers benefit from government's support. Efforts to support Afghanistan's wheat production by increasing border protections would lead to higher prices that harm consumers. Similarly, efforts to boost domestic production of wheat for milling through import policies would require a difficulttoenforce combination of flour and wheat tariffs or other restrictions that would also impose costs on consumers. Hence, according to the report, free trade, entailing unhindered wheat imports, may lead to stronger growth in domestic wheat production and consumption, with relatively small losses in farm production.

In 2005, the government decided to encourage agriculture as per ANDS development goal and resorted to tariff and non-tariffbarriers. Still, tariff rates for food items have been 3.5 per cent only. Afghanistan's trade policies have played a limited role in protecting domestic wheat producers. In thecase of wheat, Afghanistan's import policies have been relatively liberal, where the government has not established countervailing policies to Pakistan's[21] domestic grain market interventions.

Furthermore, as the country was proceeding to its negotiations for WTO accession, it was encouraged to further lift all non-tariff barriers, lower tariffs and make its trade laws consistent with WTO rules.

Textile

Textile industry has long roots in history and culture of the country for which the country was the silk trade route connecting east and west. In the 1980s, during the Soviet regime, the country was producing 350,000 m of processed cotton per year, while in the year 2013, the cotton production in the country amounted to 36,300 m only (AISA, 2013). Historically, cotton and textile industries, which consist of both private and public firms, have been predominant in four major cities of the country, namely Gulbahar Textile Plant in north of Kabul, Kandahar Cotton Textile Enterprise, Herat Textile Project and Balkh Cotton Textile Enterprise. Currently, 66 per cent of total textile production is sold at the domestic markets, 27 per cent at the national markets and 7 per cent is exported to other countries. While cheap labour, cheap raw material and growing domestic demand are the promising factors for the growth of this sector; low productivity, lack of efficiency, tendency towards export of raw materials and lack of modern technologies are the key challenges. In pursuance of WTO accession of Afghanistan, tariff rates have been kept as low as 2.5 per cent.

Commitment to WTO agreements will further leave the domestic small-scale producers vulnerable against international cheap imports. Long-term industrial development in the country not only requires strong initial support of the government in establishing domestic firms, but also constant protection from more efficient foreign companies. A loss of policy with WTO accession makes it impossible for the country to align its development goals with liberal policies.

Hence, for the reason argued above, both agriculture and industry require government support and protection against foreign imports.

Institutional Challenges

WTO accession is not merely an end in itself; rather it is the beginning of a process of reforms and adjustments. Benefits from membership to the WTO can be feasible only if competent institutions are in place to enable an economy utilize its advantages for economic growth. Institutions for this matter include both public and private stakeholders who are involved in an interdisciplinary task for the economic performance of a country (San José, 2007). The efforts of AISA have been tremendous in terms of supporting the private sector and establishment of industrial parks. Afghanistan has modified major laws, institutions and legal frameworks for compliance purposes. However, existing institutions are not enough for availing the benefits from free trade under the WTO-based trading system. Institutional capacity is one of the major concerns for all LDCs and Afghanistan in particular. Afghanistan in order to protect its interest in the international trade under WTO regime needs to increase the capacity of its institutions for strong position in negotiating terms of trade and dispute resolution with the trading partners. Furthermore, WTO agreements are highly technical legal text, which require specialized understanding of terms on jargons, contexts and cases. Afghanistan needs to train highly competent human resources in international trade and trade lawyers, who shall translate and interpret the text to the concerned authorities. Hence, identification of possible areas for trade-related capacity building areas is the main objective.

Complex Interdisciplinary Relations

Decision-making in Afghanistan is a slow and tidy process. In order to enforce an international commitment in the legislation, even an action plan should go through various rigorous processes which sometimes takes years.[22] This issue remains a challenge in the post- accession as well. Each LDC is given a transition period to reform the remaining laws to conform to WTO regulations. Any delay in such decisions brings negative consequences to the country. Therefore, the decision-making should become localized and subject-specific.

Human Resources Capacity Building

WTO negotiations, dispute settlement and continuous development and reformation of laws require the engagement of highly specialized and expert professionals in various areas, such as law, economics, international trade and so on. Attaining long-term development goals requires a holistic approach to human capital development, which would encompass acquisition of knowledge and skills in science and technology alongside practical entrepreneurial capabilities (GoIRA, 2008). Currently, mission of human resources development is coordinated by the Human Resources Development Board, which includes harmonization of strategic plans of sectoral ministries and donors. However, such efforts should be strengthened so that a generation of highly specialized human capital takes over the decision-making and economic planning in the country. Policy-makers, advisors and executives in various government bodies, especially those which concern the management of international trade, should be capable enough to understand and implement reformed laws and develop action plans, which are in conformity with international commitments on one hand, and sustainable development path on the other. Research and Development in various scientific and social issues in Afghanistan is a rare phenomenon. Research is the intellectual eye for every development project. But, think tanks and research organizations in Afghanistan are at very primitive stage of department. Training institutions need to be established at various levels of the stakeholders dealing with trade. For this purpose, the country can apply for WTO/UNCTAD technical assistance to train experts and researchers on international trade. Researchers and students from Afghanistan should be admitted to WTO University and other international universities, which specialize in international trade and trade law.

Business Capacity

Public and private business is at the core of every economic planning. An export-led growth under the WTO regime requires standard products and services for international markets. Given the state of technology and capacity in Afghanistan, fulfilling such standard is a challenging task before the government and private sector of the country. The country can benefit from the fruits of free international trade under WTO regime only if it can competently align its exports to accepted international standards.

These challenges can be addressed through technical assistance by redeveloped members of WTO. WTO membership provides Afghanistan an opportunity to modernize her institutional systems for improving safety and quality of goods and services through capacity building programmes of UNCTAD, WTO, UNESCAP and other development organizations and partner countries. To boost up exports, the country can seek aid for trade facility. However, both at pre-accession and post-accession negotiations, the country should consider maintaining maximum policy space for the protection of its sensitive sectors.

Legal Challenges

If there is anything which will create trust for business to flourish in support of institutions, that is none other than legal framework. WTO's emphasis on legal reforms to make the business and trade laws consistent with WTO regulations is of paramount importance. Perhaps, the existing legal gaps have delayed Afghanistan's accession (WTO, 2013). At present, 22 laws are yet to be endorsed by Afghanistan Parliament to make all legislations in conformity with the WTO requirements. Afghanistan has been given a transitional period of three years to enforce the legal reforms in respect of these.

These legislations include law on plant protection and quarantine, regulations on customs valuation, patents law and law on foreign trade in goods.[23] WTO trade regime works in full compliance with legal and institutional framework of member countries.After accession, the legal reforms may continue to be a challenge for Afghanistan.

Environmental Challenges

In thirst of growth and short-term development of infrastructure, it so happens that an unsustainable development path may be adopted, in which the property rights to domestic and international firms are bestowed, and they in pursuit of their personal interest voraciously extract resources that contribute to resource depletion and environmental degradation. Afghanistan in terms of its resources is the best FDI destination, which, on one hand, is beneficial to the economy from employment and GDP growth perspective, and, on the other, given the institutional and legal weaknesses in Afghanistan, privatization of water, soil, mineral resources, flora and fauna of the country, can lead to an extremely challenging environmental issues both from pollution generation and scarce resource exploitation. Evidence of deforestation and pollution in countries like India, Nepal, Indonesia and South Africa highlights this danger for any other country pushing FDI, which is facilitated by WTO commitments. Currently, the National Environmental Protection Agency (NEPA) is the only organization which works for environmental sustainability in the country. It should be noticed that multinational corporations in pursuit of minimized cost choose developing countries and LDCs for the purpose of production and resource extraction. Therefore, Afghanistan should establish competent legal and institutional frameworks to address the challenge posed against environment by economic growth. Sanitary and phytosanitary (SPS) measures is the agreement under WTO, which allows members to take necessary measures to protect human and animal lives in their territory (WTO, 2014). Under this agreement, Afghan authorities can establish laws to safeguard necessary environmental challenges.

Recommendations for Capacity Building to Deal with Challenges

Based on the analysis presented in this article, the following recommendations are suggested for policy purposes:

- Trade as an instrument of development is mainstreamed in the ANDS, and WTO accession is therefore considered an important step towards attaining this goal. However, despite emphasis on central role of trade in economic development, operational objectives and action plans for trade are yet missing. Strategies and plans relevant to trade either does not exist or if exist, are in the form of various sectoral strategies, such as Ministry of Commerce and Industries (MoCI) strategy, private sector development strategy, export promotion policy, industrial policy, etc. These strategies need to be integrated in one single trade development strategy document, encompassing all trade-related priorities across different government departments.

- The diagnostic trade integration study (DTIS) and action matrix still do not reflect the Afghan Government trade strategy. Rather, Afghanistan was accepted as a beneficiary country to the European Investment Fund (EIF)[24] process in 2008 by the EIF Board.[25] Afghanistan needs to fully prioritize its needs to get full access to EIF. Furthermore, since EIF is one of the programmes that can be designed under DTIS and action matrix, the need for such a study is crucial to provide intellectual input based on concrete empirical and contextual studies. The study can be undertaken by engaging a large number of stakeholders in government, private sector, academia and development community with the purpose of understanding the country context, critical issues affecting the development of the private sector and trade in Afghanistan, which would provide ongoing and planned programmes an analytical work, and seek relevant inputs regarding potential areas to cover in the report. In such a study, prioritization in the following areas is recommended:

    1. Building productive capacity through the support of private and public sector to enhance their competitiveness, export diversification and value chains.
    2. Building economic infrastructure, such as transport facilities, cross-border infrastructure, power, raw material, springhouses, etc.
    3. Enhance the activities of complementary services, such as credit facilities, insurance and consultancies.
    4. Trade policy and regulations: Trade facilitation and trade policy analysis, negotiations and implementation.

    Currently, the operational strategy in Afghanistan has prioritized infrastructure within the annual budget as prescribed by the ANDS. However, in the meantime, the other priority areas should be focused upon as well and presented in DTIS to get aid for trade facilities from donors and development organizations. To prepare concise and justifiable financial needs in DTIS, Afghan Government should engage in bilateral and multilateral dialogue with the donor community, private sector, civil society and other major stakeholders, both region-wide and internationally. International Monetary Fund, World Bank, UNCTAD and some development organizations, such as USAID, Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ), Japan International Cooperation Agency and donor countries, which are currently involved in multi-pronged development activities in Afghanistan, should be discussed with to formulate a financial need for the priority areas.
- Major development projects in Afghanistan in the last 13 years have been engineered and run by the donor party, which has created multiplicity in the system and has not attained the would-be capacity despite huge amount of funds. Trade is one of the important development goals, which attract

financial support from the international community. Trade strategies should be coordinated, monitored and evaluated by the Government of Afghanistan under the leadership of MoCI. In other words, trade development, prioritization and implementations should be an Afghan-initiated and Afghan-led process, rather than multiple donors operating independently. A national committee comprising of various stakeholders inside the government to oversee and coordinate trade-related activities may be established to direct the international funds based on the priority areas. Moreover, the Afghan Government should establish a mechanism to discuss the impact of trade-related programmes with the donors and other stakeholders.

- Though MoCI, Afghanistan develops and strategizes trade policies; formulation of action plans and legal proposals specifically for WTO requirements bring in various stakeholders of the economy, which make the process longer than it should be. To address this challenge, various agencies and ministries should be brought together in a single platform to decide on trade-related issues and oversee the performance.
- For a successful aid for trade programme implementation, the Government of Afghanistan needs to first include it as its top agenda, and secondly, develop a monitoring and evaluation mechanism to assess and oversee the performance of various donors and players who are engaged in the process of trade facilitation in Afghanistan. And later, the entire aid for trade programme should be designed and implemented by the government, rather than individual players.

Conclusion

Consistent with the theory, our ex-ante cost–benefit analysis results show that WTO accession and undertaking further tariff cuts will have a negative impact on the revenue, a positive impact on the consumers and the welfare gain, which signals positive efficiency improvement. However, the model does not allow for the assessment of the production sector of the economy, and hence, an important sector remains out of the purview of the simulation. One can infer that due to the lack of competence and efficiency in the domestic production, the sensitive production sectors of the country will lose in the competition. Our analysis started with a clear assumption that Afghanistan's tariff schedules are already consistent with the WTO prescription and may not be required to undertake further commitments with regard to tariff cuts, but a 10 per cent and 5 per cent tariff cut stimulation can be used as a proxy to project the extent of the effect, which in turn helps to identify the sensitive sectors of the economy and negotiate for maintaining the least possible binding and highest possible tariff rates. Policy space concept allows for an LDC to preserve some freedom, which would facilitate division of policies with regard to long-term development goals. Agriculture, textile, cement and services are among important sectors of the economy, which require due consideration. Further research can be undertaken on trade in each commodity with specific countries to assess the trade potential of Afghanistan by applying other general equilibrium models.

The real challenges start after accession. Afghanistan should create necessary capacity to enable it to integrate with the competitive world economy as a competent trading partner, which will meet all international quality requirements and standards. This can happen only if the country establishes capable institutions to manage its trade and investment in a rule-based trading system. Legal framework remains a challenge which will take long parliamentary engagements in the country.

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Notes

1. The fourth meeting of the working party was held on 25 July 2013 in which Afghanistan was urged to resolve outstanding technical issues, enact the few outstanding draft laws and conclude remaining bilateral negotiations to ensure that it remains on track to complete its accession process at the Ninth Ministerial Conference (MC9) in Bali.
2. There are 44 countries recognized as LDCs by the UN, of which 34 countries are members of WTO. Eight LDCs including Afghanistan, Bhutan, Comoros, Equatorial Guinea, Ethiopia, Liberia, Sao Tome & Principe and Sudan are currently negotiating for WTO membership. Yemen is the recent LDC member of WTO.
3. The Silk Road was a network of trade routes that linked cities, trading posts, hostels and caravan-watering places. It was most active from about 300 BC to 200 AD and extended between the Eastern Roman frontier in the Middle East and the Chinese frontier, with other paths going north through Afghanistan from the Indian Ocean to the Siberian Steppe.
4. Afghanistan's presentation to WTO, 2012.
5. For details, the reader can refer to ANDS Preamble.
6. Article 7 of the SAFTA Agreement.
7. See ADB database, http://www.adb.org/countries/afghanistan/main.
8. HS refers to Harmonized System of coding for products in 2012. It is the nomenclature developed by the World Customs Organization for customs tariffs and international trade statistics to organize products through hierarchical categories.
9. See http://cso.gov.af/en/page/1726
10. These objectives have been highlighted in Afghanistan's first application and reiterated in various presentations made by Afghan delegates.
11. See http://mission-afghanistan.ch/Mission/index.php/economic/unctad.
12. NAMA refers to all products not covered by the agreement on agriculture. In other words, in practice, it includes manufacturing products, fuels and mining products, fish and fish products and forestry products. They are sometimes referred to as industrial products or manufactured goods. See http://www.wto.org/english/tratop_e/markacc_e/nama_negotiations_e.htm.

13. Before 1980, over 60 per cent of global dried fruits were supplied from Afghanistan. For more information, refer to USDA report, *Afghanistan's Dried Fruit Market Regains Strength*.
14. In 1975, up to 35 per cent of employed population in selected provinces was engaged in carpet weaving (Baqi, 2005), and currently, over one million Afghan population is engaged in carpet industry (McCord, 2007).
15. Refer to WTO General Agreement on Trade and Services.
16. Working Party on the accession of the Islamic Republic of Afghanistan, 29 October 2013.
17. Quantification of befits from Economic Cooperation in South Asia, 2008.
18. Tariff reduction was imposed on what the author calls category B goods such as agricultural products, processed food, textile, plastic products, iron and steel products, detergent, building materials and tobacco.
19. Trade Revenue and Welfare Effects of East African Community Customs Union Principle of Asymmetry on Uganda, 2011.
20. The details of the model can be accessed from World Bank official website https://wits.worldbank.org/
21. Pakistan and Kazakhstan are the largest exporters of wheat to Afghanistan.
22. Based on an interview between author and Baraimal Jerian at MoCI.
23. Refer to WT/ACC/AFG/9/Rev.2.
24. See http://www.wto.org/english/tratop_e/devel_e/a4t_e/enhance_if_e.htm.
25. The first EIF awareness workshop was held in MoCI in May 2008. As an outcome of this workshop, the National Steering Committee chaired by the Deputy Minister for Trade, National Focal Point and the Donor Facilitator were appointed by MoCI. Afghanistan is still waiting for the EIF Board to assist with the establishment of the national implementing unit in order to start the process.

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