Barriers to Afghanistan's critical private sector recovery

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Cover photo: Ingebjørg Kårstad/NRC. *A man gets bread from a local bakery in Khost. In Afghanistan today, bread is a synonym for survival.*

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TABLE OF CONTENTS

Glossary

CBR Correspondent Banking Relationships

CEO Chief Executive Officer

DAB Afghanistan Central Bank

EDD Enhanced Due Diligence

EO Executive Order

F4ID Fintech for International Development

FAO Food and Agricultural Organisation

FAQs Frequently Asked Questions

FTO Foreign Terrorist Organization

GDP Gross Domestic Product

GL General License

IMF International Monetary Fund

IRC International Rescue Committee

NGO Non-governmental organisations

NRCNorwegian Refugee Council

OFAC Office of Foreign Assets Control

SDGTSpecially Designated Global Terrorist

SWIFT Society for Worldwide Interbank Financial Telecommunication

TKB Transkapitalbank

UAE United Arab Emirates

UN United Nations

UNDP United Nations Development Programme

UNSCR United Nations Security Council Resolution

US United States

WFP World Food Programme

1 Executive Summary

Afghanistan has undergone a series of complex political, economic and social changes since the return to power of the Taliban in August 2021, whereby the plight of the Afghan people has deteriorated into an unprecedented humanitarian catastrophe. The Taliban's stance towards women, including restrictions on female education and bans on female aid workers, have posed additional challenges to the Afghan people and the country's economic prospects, as well as to international donors and aid organisations. Since the Taliban's resumption of power, international actors have pursued policies of political and economic isolation towards Afghanistan that have contributed to the current economic crisis and the populations' reliance on humaniatrian assistance. To date, most research and policy efforts have centred on the humanitarian catastrophe and the plight of women and girls. Less attention has been placed on constraints facing trade with Afghanistan, including those negatively impacting supply chains of essential goods that are neceassry to address the basic needs of Afghan people. This report seeks to fill a knowledge gap on some of the key challenges facing Afghan trade, especially relating to food and essential goods needed for basic survival. It is based on 25 anonymised interviews carried out in mid-2022 with a range of private sector, development and banking actors operating in, or with, Afghanistan. It explores challenges associated with international targeted sanctions; financial sector derisking; shifts in domestic regulations; implications of Russia's invasion of Ukraine in 2022; and wider trade and economic constraints. It also aims to showcase best-practice and coping strategies employed by the private sector operating in Afghanistan and generate a series of policy recommendations based on input from Afghan companies and those operating in the wider region.

Key findings:

1. Afghanistan should still be open for business despite sanctions

- The United Nations (UN) and United States (US) impose targeted sanctions on a set of individuals and entities in Afghanistan. These sanctions are not comprehensive in nature and do not apply to the entire country.
- The UN Security Council Resolution (UNSCR) 2615 of 2021 and the US General Licence (GL) 20 allow private sector actors operating in Afghanistan to engage in transfers of funds or assets to designated persons or entities if they relate to activities that support basic human needs in the country. This includes the processing and payment of funds and the provision of goods and services to support such activities.
- The UNSCR 2615 exemption and GL 20 have been fundamental and necessary for basic goods to be imported into Afghanistan, as they allow for the facilitation of the payments necessary to meet basic human needs.
- In spite of the US sanctions on a Russian bank (imposed in relation to the 2022 invasion of Ukraine), that acts as an intermediary for some Afghan trade, the US GL 28 and GL 28a allow the bank in question to continue serving as a correspondent for Afghan-related transactions until 23 January 2023.
- Financial transactions involving designated individuals that may be deemed to fall outside the scope of UNSCR 2615 and GL 20 continue to serve as constraints for firms operating in Afghanistan, particularly considering how subjectively such activities may be defined.

2. Financial sector derisking, and wider private sector overcompliance continues to represent a serious constraint in spite of sanctions' exemptions

- Differing interpretations of the regulations and exceptions mean firms engaging in food supply chains and related goods to and from Afghanistan say they need better guidance, capacity building and awareness-raising on what is permissible under UN and US sanctions regimes to forge greater confidence in, and appetite for, resumed trade with Afghanistan.
- Widespread misconceptions – particularly in Central Asia and the Middle East – hold that Afghanistan as a country is sanctioned. Banks and other firms in the region are not always aware of the humanitarian exemptions that allow for continued private sector activities in many areas.
- Correspondent banking relationships (CBRs) available to the Afghanistan financial sector are extremely limited due to perceived risks, the real costs and resourcing burden, and in some countries, ongoing confusion linked to sanctions compliance.

3. Accessing functioning banking channels presents a major challenge to most firms

- Firms dealing in the trade of essential goods to and from Afghanistan have struggled to access international banking services for cross-border payments since August 2021, due to numerous trade and economic constraints, including financial sector derisking.
- Some Afghan firms dealing in food and other essential goods lack capacity to meet stepped-up standards adopted by Afghan banks since 2021 regarding enhanced due diligence (EDD) checks. Other firms have suffered from a long waiting time of up to three months for compliance checks to be completed.
- Only Afghan firms able to access overseas bank accounts (typically through having offices in other countries, primarily in Turkey and the United Arab Emirates [UAE]) are typically able to settle international payments via the formal banking system. The same firms have struggled to open new bank accounts since August 2021.

4. *Hawala* – now the dominant form of international and domestic transfers for Afghanistan private sector actors – is not an accepted form of payment by most international firms

- *Hawala* is a legal and partially regulated form of money service business in Afghanistan and the neighbouring region, and widely used by humanitarian actors and businesses as a legitimate and effective payment mechanism of last resort.
- *Hawala* is mostly limited to domestic use in some parts of Africa, Asia and the Middle East, but generally cannot be used to pay suppliers elsewhere (for example, in North America or Europe).
- Since 2021, *hawala* has been subject to increased transaction costs, which appear to have negatively impacted smaller firms and women-owned businesses.

5. Alongside pre-existing multidimensional poverty, displacement, severe food insecurity and risks of human-driven environmental hazards, other exacerbating challenges include

- Loss of many women from the Afghanistan workforce.
- Restrictive domestic trade policies and financial controls.

- Absence of a fully functioning Afghan Central Bank (DAB) able to conduct monetary policy.
- Curtailed access to financial services and liquidity.
- Rising global food and energy prices, including in relation to the conflict in Ukraine, the 2022 blockade of Ukrainian ports, and protectionist policies on exports of food and fertilisers.
- Reduced airline freight capacity to and from Afghanistan since August 2021.
- Reduced contact with international partners through trade fairs.

Recommendations to international donor governments

1. **Establish a common understanding of the challenges facing the Afghanistan economy and the steps needed to stabilise it:** Major donor governments, international financial institutions, UN agencies and relevant regional actors should urgently convene, via a tabletop or scenario development exercise, to build a common analysis of the baseline status and functioning of the economy, and establish clear steps to address key challenges. Topics should include revenue collection and taxation; the role of the illicit, partially regulated and informal economies; drivers of the humanitarian crisis; and challenges faced by private actors in key sectors. This is a critical first step towards identifying and agreeing on a roadmap for the resumption of responsible levels of support to the Afghanistan economy.
2. **Raise awareness that sanctions do not apply to the whole of Afghanistan**. Support is needed from governments to ensure that firms and banks in Central Asia and the Middle East are aware of the existing range of sanction exemptions and safeguards that allow for continued trade, and how they apply to their operations. **Clearer sanctions guidance in areas where confusion persists would also assist the private sector, including on the full scope of activities permissible under the exemptions.**
3. **Secure mechanisms for providing technical assistance to the DAB:** Building the DAB's regulatory capacity and independence is a necessary step toward restoring the commercial banking sector and reconnecting the Afghan economy to the global economy. Technical assistance should draw on the expertise and experience of the International Monetary Funds (IMF) and World Bank in Afghanistan. Such assistance is essential to restoring and stabilising the economy as well as rebuilding confidence in the banking system. Furthermore, supporting the DAB to receive shipments of newly printed Afghani notes will be important for the Afghan economy.[1]
4. **Ensure resumption of one or more Afghanistan air corridors**: The former air corridor was a lifeline for hundreds of businesses in reaching customers and clients in India, Turkey, the UAE and elsewhere, according to interviewees. Creating a new air corridor will necessitate improvements to Afghanistan's air traffic control and airport access, including completion of outstanding contracts. Some cited the importance of including the UN in this process.
5. **Prioritise greater clarity of sanctions guidance in areas where confusion persists**. This should include basic human needs; ownership and control; and permitted mechanisms for the payment of taxes.
6. **Engage with correspondent banks** to encourage continued servicing of Afghanistan-related banking transactions as well as with the wider private sector to reduce over-compliance and the chilling effect.
7. **The Afghan Trust Fund should be urgently mobilised to stabilise the Afghan economy and provide support to the DAB.** The $3.5 billion of DAB's frozen foreign currency reserves that were transferred to a Trust Fund for the support of the Afghan people have a crucial role to play in supporting the return of a functioning Central Bank.
8. **Investment in and support of digital payment platforms,** including mobile money, should be prioritised to help facilitate domestic and cross-border transactions and to support the

increase of customers and outlets able to work with such technologies. This could include pilots, regulatory sandboxes and further research and capacity building across sectors.

9. **Provide support for Afghanistan firms to resume their presence at regional and global trade fairs:** The UN and other international organisations should continue to run and support international trade shows where Afghanistan firms can participate and showcase their work.
10. **Strengthen the purchasing power of the Afghan people.** Support a combination of cash for work; savings groups with developing loan funds and repayment schedules with flexible spending options; investment in livelihoods, and humanitarian support. This, in turn, will help foster private sector growth. Substantial development should be prioritised in areas such as water storage, renewable energy, road infrastructure and milling. Furthermore, poverty reduction should be addressed at the household level.

2 Introduction

As much of the world's attention has focused on mobilising a humanitarian response of sufficient speed and scale to meet Afghanistan's rapidly mounting needs since mid-2021, there is also a growing recognition of the vital need to support and revive the country's economic and trade activities in the face of a formidable set of challenges. Afghanistan has experienced a set of overlapping financial, fiscal, and trade crises[2] since the Taliban's resumption of power on 15 August 2021.[3] Development support and services ended abruptly at this time, due to the cessation of international aid that formerly contributed to 40 percent of the gross domestic product (GDP).[4] At the same time, the DAB lost access to over $7 billion of frozen foreign reserves, preventing the institution from executing its key functions related to the financial sector, monetary policy, and economic stabilisation. Since August 2021, the country's economy has suffered a severe decline, marked by a fragile and poorly functioning banking system, and hindered access to liquidity and physical bank notes.[5] The country is now facing an unprecedented humanitarian crisis. Although humanitarian assistance has increased since the Taliban's resumption of power, the reliance on humanitarian aid to meet the basic needs of the population is unsustainable without steps to address the wider economic crisis.

According to the United Nations Development Programme (UNDP), Afghanistan's real GDP decreased by 20 percent between 2021 to 2022, equating to a loss of $5 billion, which had taken almost ten years to generate.[6] As a consequence, per capita income declined by 14–28 percent and an estimated 700,000 jobs were lost during the same period.[7] The UN World Food Programme (WFP) reported that the proportion of households facing insufficient food consumption increased from 81 percent to 89 percent during this same period.[8] The country is "facing catastrophic famine or famine-like conditions," with 51 percent of the population relying on negative coping strategies to put food on the table.[9]

In addition, the global hike in food and fertiliser prices associated with Russia's war in Ukraine in February 2022 is understood by WFP to have added further pressure on Afghanistan.[10] The country is particularly vulnerable to shocks in the global supply chains of food[11] and other goods in light of its strong dependence on wheat[12] and other food imports from neighbouring countries for over half its food needs.[13] Furthermore, most value chains were supported by development agencies and non-governmental organisations (NGOs) in some way prior to August 2021, particularly those relating to the food and agriculture sectors. As such, current humanitarian assistance providing direct food support is thought by some to be having a negative impact on Afghan supply chains, by reducing small vendors' ability to sell food items that are now provided for free by humanitarian actors. Furthermore, this is also impacted by the country's food basket costs rising by 35 percent between August 2021 and August 2022.[14]

The World Bank notes some modest and fragile improvements, although adding that the country's financial sector crisis is still ongoing, including due to "major macroeconomic imbalances, the freezing of DAB's offshore assets [by the US Government and other governments, which have now been partially released into a new trust fund that can be used for economic stabilisation purposes], a breakdown of international correspondent banking channels, the collapse of domestic payment system's functionality and a "loss of public confidence" in the banking sector.[15] The World Bank also notes that while employment and demand for goods has improved somewhat since August 2021, current levels are well below those observed prior to August 2021.[16] Similarly, while liquidity has improved to a degree for some financial institutions – with some bank branches starting to reopen in some provinces of Afghanistan[17] – confidence in the banking sector remains low and access to credit and loans remains a major challenge.[18]

Despite efforts of various international organisations, governments, and trade bodies to support livelihoods and economic recovery in Afghanistan, a significant knowledge gap currently persists regarding the scale of the challenges faced by private sector actors. This is despite of the vital role they play alongside the work of humanitarian organisations in meeting Afghanistan's mounting food needs and contributing to economic resilience.[19] This study seeks to address this gap and provide the groundwork[20] for future research[21] in exploring challenges faced by firms engaged in the import or export of food and related goods or services to, or from, Afghanistan. It is based on 25 anonymised online and in-person interviews carried out between July-September 2022, with a range of private sector, development, and banking actors operating in, or with, Afghanistan.[22] The report explores a number of prominent economic and trade-related constraints as they relate to supply chains of food and other essential goods, including financial sector derisking, difficulties accessing functioning payment channels, wider private sector over-compliance, and domestic regulations. The report concludes with recommendations regarding actions that could help support the resumption and scaling up of trade, especially that which is most essential to the lives and livelihoods of the Afghan people.

Photo: Ingebjørg Kårstad/Norwegian Refugee Council. An empty food stall in the streets of Khost.

2 Targeted sanctions in place in Afghanistan

There are no country-based or comprehensive sanctions in place against Afghanistan. Instead, the UN and US impose targeted sanctions against a number of individuals and entities in the country, whose adoption long pre-dates the Taliban's return to de-facto control of the government in August 2021.[23] They include arms embargoes, travel bans on designated persons, asset freezes, and financial restrictions that prohibit making funds or assets available to designated persons or entities.

2.1 Private sector activities under UN sanctions

UN sanctions do not target the Taliban or the de facto authorities as a whole. Instead, the UN counterterrorism sanctions linked to the Taliban (S/RES/1988) involve a total and global asset freeze on 135 individuals and five entities (the Haqqani Network and four *hawala* agents). Additional measures are also in place in relation to Al-Qaida/ ISIL (S/RES/1267/2253), involving a total and global asset freeze on 12 individuals and 20 entities.[24] All member states of the UN are obliged to adopt these measures under Chapter 7 of the UN Charter. The de facto authorities that assumed position in 2021 include some 20 Taliban officials on the UN sanctions list. Under the UN humanitarian carveout (UNSCR 2516), funds or assets can be made available to designated individuals or entities, for the purpose of providing humanitarian assistance or conducting other activities in support of basic human needs. According to the resolution:

> *[H]umanitarian assistance and* ***other activities that support basic human needs*** *in Afghanistan are not a violation of paragraph 1 (a) of resolution 2255 (2015), and that the* ***processing and payment of funds, other financial assets or economic resources, and the provision of goods and services*** *necessary to ensure the timely delivery of such assistance or to support such activities are permitted, strongly encourages providers relying on this paragraph to use reasonable efforts to minimize the accrual of any benefits, whether as a result of direct provision or diversion, to individuals or entities designated on the 1988 Sanctions List, and further decides to review the implementation of this provision after a period of one year [empathsis added].*[25]

2.2 Private sector activities under US sanctions

The US has listed the Taliban as a Specially Designated Global Terrorist (SDGT) entity since 2002, pursuant to Executive Order (EO) 13224, as amended. The measures represent a de facto ban on most forms of contact with the group, and, by default, the de facto authorities. A set of GLs established by the US since September 2021 permit a range of activities and financial transactions, as described below. The US Department of the Treasury's Office of Foreign Assets Control (OFAC) imposes SDGT designations on financiers and facilitators of the Haqqani Network (pursuant to EO 13224) as well as designate the Haqqani Network as a whole as a Foreign Terrorist Organization (FTO) under Section 219 of the Immigration and Nationality Act. This signifies a block on their property and interests subject to the US jurisdiction, in addition to restrictions on US individuals and entities engaging in transactions with them. In addition to the measures described above, US sanctions apply to US Dollar transactions passing through the formal financial sector, as well as to US citizens working in foreign firms. OFAC issued several new general licences (GLs 14-21) in the second half of 2021 and early 2022, to facilitate humanitarian assistance to Afghanistan and limit the impact of sanctions on humanitarian action in accordance with UNSCR 2615. The GL 20 authorises commercial and financial transactions in Afghanistan, including with governing institutions, provided there are no transfers to listed Taliban individuals.[26]

The '50 percent ownership and control' rules, usually applicable to businesses, is a key legal issue which has created confusion in relation to state institutions which may be headed by a designated individual in Afghanistan. The private sector in Afghanistan, together with other relevant actors, such NGOs, has sought clear guidance from sanctioning authorities, according to interviews, on how to interpret these rules when applied to a scenario in which a SDGT and/or designated individual heads an entire state apparatus. To this end, OFAC FAQ 991 and 992 confirms that all commercial and financial transactions involving Afghanistan are authorised,[27] adding that OFAC does not view financial transfers to governing institutions as transfers to designated individuals who may lead those institutions. OFAC's FAQ 993, for example, clarifies that:

> *Generally speaking,* ***when a designated individual has a leadership role in a governing institution, the governing institution itself is not considered blocked****. Accordingly, engaging in a routine interaction with an agency in which a blocked individual is an official, but that does not involve the blocked individual in question, is not prohibited…GL 20 also* ***authorizes the payment of taxes, fees, or import duties, or the purchase of permits, licensing, or public utility services to blocked individuals that are in leadership roles of governing institutions*** *in Afghanistan, provided that such payments do not relate to luxury items or services [emphasis added].*[28]

It goes on to add:

> ***If [a] company needs to make a customs payment to a governing institution in Afghanistan led by a blocked individual, that is authorized.*** *Similarly, if [it] is signing a contract to provide services to or on behalf of that governing institution and the blocked individual appointed to lead that governing institution needs to sign the contract in their official capacity on behalf of the governing institution, that is authorized. However, if the blocked individual requests that funds be provided directly to them, other than for the purpose of effecting the payment of taxes, fees, or import duties, or the purchase or receipt of permits, licenses, or public utility services or financial transfers, that would not be authorized by GL 20 [emphasis added].*[29]

Also worthy of note, is that the following activities that could be carried out by private sector actors are covered under the exception and the US GLs, according to OFAC's FAQ 929:

> *For the purposes of Afghanistan-related GL 14, humanitarian assistance includes…the provision of healthcare and health-related services, protection and assistance for vulnerable or displaced populations…****the distribution of articles (such as food, clothing and medicine) intended to be used to relieve human suffering in Afghanistan****…Other activities that support basic human needs include activities to support non-commercial development projects in Afghanistan that primarily benefit poor or at-risk populations or otherwise relieve human suffering, including activities related to shelter and settlement assistance,* ***food security, livelihoods support****, water, sanitation, health, hygiene and COVID-19-related assistance, among others [emphasis added].*[30]

Also important to note for private sector actors is the following guidance in OFAC FAQ 958:

> *Other examples of engagement with the Taliban and the Haqqani Network that are authorised under GL 14 and GL 19 if they are ordinarily incident and necessary to activities authorized by these general licenses include: (i)* ***general coordination on delivery and provision of humanitarian aid or shipments****; (ii)* ***administrative issues involving importation of***

> ***goods****; (iii) attendance at donor coordination meetings; (iv) sharing descriptions of projects; (v) coordination with regard to travel or project locations; (vi) participation in technical working groups; and (vii) sharing of office space [emphasis added].*[31]

In addition, the OFAC FAQ 992 states that "transactions that are generally authorised by GL 20 [include] [c]ommercial transactions involving Afghanistan, including imports from Afghanistan, exports to Afghanistan and commercial transactions within or involving the geographical territory of Afghanistan."[32] It affirms that contact with designated entities or individuals is not prohibited.[33]

Photo: Ingebjørg Kårstad/Norwegian Refugee Council. A quiet grocery store in the city of Khost.

3 Sanctions-related challenges identified by Afghan private sector actors

Despite the issuing of the UN exemption and US GLs, that have been essential to facilitating the delivery of vital humanitarian aid, those consulted for this report highlighted the need to rectify misconceptions surrounding the sanctions in place in Afghanistan – from the local to regional and global levels. A number of key areas requiring further action were highlighted by interviewees, as described below.

3.1 Raising awareness that Afghanistan is ready for business

According to those consulted, a number of key companies and financial institutions, particularly in Central Asia and the Middle East, have adopted self-imposed bans on any form of trade with Afghanistan. This includes exclusion of Afghan firms from regional and international trade fairs, which formerly served as a source for new business and creation of useful networks. The chief executive officer (CEO) of one Afghanistan company said:

> *Nobody wants anything to do with Afghanistan right now and this hurts trade. International customers need to see us face-to-face so we can re-establish trust. Earlier trade fairs, such as Passage to Prosperity run by USAID, helped Afghanistan businesses tremendously. This could also allow women to remain involved in Afghanistan trade if the organisers insist on the presence of Afghanistan businesswomen.*

- CEO of an Afghanistan company

One firm highlighted the urgent need to raise awareness outside Afghanistan that existing sanctions do not prohibit trade with the country:

> *We need to educate companies and banks overseas that Afghanistan itself is not under sanctions. There is a real lack of understanding about this though – particularly among key sectors in our main export and import markets. Even when we show banks in Central Asia details of the sanction's UN exemption and the US general licenses, they still don't understand what is required of them. On the contrary, this seems to scare them off.*

- Executive of a large agricultural firm in Afghanistan

A senior Afghanistan banking representative also highlighted the need for change in this area to facilitate future banking transactions and Afghanistan trade:

Once overseas banks have a better understanding that trade can continue with Afghanistan and the situation is normalised, then 80 percent of our operations can continue.

– banking Executive in Afghanistan

3.2 Greater clarity on permissible contact with sanctioned persons

Another key area of concern according to private sector interviewees relates to difficulties understanding the full nature of permissible activities, particularly in relation to US sanctions. This was in spite of various rounds of guidance provided by OFAC in the form of FAQs. According to one lawyer, "Nobody in Afghanistan understands the US sanctions and it's hard to get guidance…You can send OFAC an inquiry about some project-specific activity, but they don't provide much information and what they do provide is very vague. The FAQs mostly provide similar information to the licences". He went on to say, "If we, as lawyers, struggle to understand the nature of permissible activities, what hope does a normal Afghan company have?". Another respondent highlighted the need for clearer guidance from the US.

The fact sheets issued by the United States aren't enough. The United States Chamber of Commerce also provided additional information, but this hasn't fully cleared up what can and can't be done. The problem is linked to the ambiguities around contact with the Taliban and Haqqani network.

– Executive of a food trading company in Afghanistan

3.3 Greater clarity on tax payments

Various interviewees raised concern over continued confusion relating to payment of taxes to government entities, in spite of some level of comfort provided through the exemptions and additional guidance. This includes in relation to what is permitted regarding payment mechanisms:

We understand now that GL 20 allows us to pay taxes to the Afghan authorities. But we still don't understand how we can do this if we can't access banking channels. Is it ok for us to use hawala from Turkey, for example? Or should we carry the cash into the country ourselves before paying the bill in person?

– businessperson based in Kabul

3.4 Increased domestic capacity on sanctions

The need for greater domestic support on sanctions compliance was also mentioned:

There has been no information coming from the new [de facto] Afghan authorities and no dissemination mechanism or provision of information on sanctions. There was no communication by the authorities on GL 20, for instance. The US Treasury, together with the US State Department, tried to create a communication channel with Afghan commercial banks. But the commercial banks could not communicate with foreign entities without DAB, so it didn't really go anywhere.

– Afghanistan bank representative

One Afghan banking representative added that “even the [de-facto] government doesn’t know a lot of the time what the sanctions involve, or what are the requirements”. Another interviewee argued for increased support on compliance requirements to help avoid confusion, and adapt to new due diligence frameworks:

> *The Afghan business community needs support to build capacity on sanctions as well as other regulations, such as anti-money laundering and countering the financing of terrorism regulations. There are all types of new due diligence requirements but widespread confusion as to how this affects them.*
>
> – Afghanistan financial specialist

Others noted that while a greater understanding of sanctions relating to Afghanistan was an important first step, other measures are urgently required to reduce international banking derisking behaviour.

4 Financial sector derisking

The process for both outgoing and incoming payments using the formal banking sector involving Afghanistan has become costlier, more challenging, and more time-consuming since August 2021, according to all interviewees consulted for this report.[34] As described below, financial sector derisking in the Afghanistan context is driven by various factors, according to consultations with the sector: :

- **Diminished risk appetite:** Reduced appetite among international financial institutions to transact with Afghan banks, due to real or perceived risks linked to sanctioned actors or other entities linked to the Taliban, including those in key positions at the DAB. Some highlighted that the humanitarian-related transactions under current exemptions and GLs do not cover the full panoply of trade-related activities and payments.
- **Resourcing burden:** Compliance costs related to factors such as due diligence and EDD checks by home and correspondent banks on individual clients; navigating the sanctions legislature, and liaising with additional government bodies, have increased significantly over the past year. One European bank relayed that it needed to use 40 to 50 staff members to service one financial transaction to Afghanistan.[35] Similarly, one executive of an Afghan bank mentioned having to double their compliance team to 80 staff members since August 2021. Another bank in Afghanistan cited the need to spend more money on the services of international lawyers to help them navigate the sanctions regimes and engaging more staff to help carry out compliance checks. The overall time and resources available to banks to undertake due diligence checks in relation to Afghanistan and elsewhere have been further constrained by the need to redirect capacity towards ensuring compliance with international sanctions on Russia.
- **Stricter compliance procedures adopted by Afghan banks**: Several businesses reported that some of the leading banks in Afghanistan now have a compliance threshold that has become too restrictive for many Afghan businesses. Others highlighted how Afghan banks are sometimes deciding not to service certain client transactions, due to these being deemed as not sufficiently 'humanitarian.' Some of the cited challenges with new due diligence checks were that the waiting time was too long; that it was too difficult to provide sufficient background information to the required standard; or that increased fees relating to international transfers had become prohibitively high.

This has impacted financial institutions that might otherwise provide services in a number of ways, including those below:

- **Decline in CBRs:** An acceleration in the decline of CBRs since August 2021. The situation was already poor before the Taliban returned to power, according to those familiar with the sector, with other CBRs ceasing immediately after the Taliban returned to de facto power. One CBR via Russia has been subject to increased derisking following Russia's war in Ukraine (described below).
- **Difficulties opening new bank accounts:** Reluctance among banks (particularly in Central Asia and the UAE) to open new accounts for Afghan businesses, even those with

overseas offices, due to wariness over any activities linked to the country and confusion over the scope of current sanctions in place.

- **Delays to, or refusal of, servicing of payments:** Reluctance among international banks to service transactions associated with Afghanistan was described by numerous interviewees, including Afghan banks. As illustrated by one interviewee:

There are big hurdles in supply chains because our foreign suppliers will not release our containers until we process their payments and this can be held up by the banks, sometimes for weeks or months on end.

– representative of an Afghan logistics company involved in food shipments into the country

- **Problems accessing Society for Worldwide Interbank Financial Telecommunication (SWIFT):** Access to the Brussels-based financial messaging platform, SWIFT, is not restricted through sanctions in Afghanistan, as in the cases of certain banks in Iran and Russia. Nevertheless, the service has not been available to most businesses in Afghanistan since August 2021, due to the reduced risk appetite of certain correspondent banks. Thus, many firms that formerly used SWIFT to transfer funds to external suppliers are now excluded from accessing formal banking services. Changes to SWIFT that took place in late 2022 through integration of ISO 20022, should permit more structures and transparent information to be shared in each transaction by home banks, according to one interview.[36] This in turn could lead to improved access to SWIFT in countries like Afghanistan.
- **Over-compliance in relation to sanctioned Russian intermediary banks**: While international sanctions have been imposed against Russian and Belarusian individuals and entities in relation to Russia's actions in Ukraine,[37] they do not target the Russian agricultural sector and do not include food or fertilisers.[38] Moreover, carveouts exist for trade in essential goods and humanitarian assistance, which seek to protect continued activities in these areas.[39] Since the onset of sanctions against some Russian banks and restrictions against their use of the SWIFT international payment system, at least one of the CBRs in Russia that played a role in transactions to and from Afghanistan has been sanctioned. While exemptions are in place that allow for the continued use of this bank (described below), some interviewees indicated that financial sector derisking has led to difficulties using the channel:

Some of the companies in Kazakhstan that were importing flour, beans and cooking oil from Afghan businesses in Mazar-e-Sharif have lost access to some of the Russian banks they were using before for the payments. Some of the fund transfers have been delayed or haven't been processed.

– Afghan banking executive

Transkapitalbank (TKB) is a Russian bank that specialises in correspondent services. Despite it being only Russia's 37th largest bank when ranked according to assets, it played a significant role in Afghanistan's banking transactions, including in relation to food imports and exports. Many food imports coming into Afghanistan from Kazakhstan, Tajikistan, and Uzbekistan were financially serviced by TKB, according to one interviewee. On 20 April 2022, TKB was designated as a sanctioned entity by OFAC pursuant to Russia-related EO 14024, which notes that the bank "offered services to several banks in Asia, including within China, and the Middle East, and suggested options to evade international sanctions."[40] Canada also imposed sanctions on the bank under its Special Economic Measures (Russia) Regulations.[41] After the announcement of the TKB sanctions, OFAC issued GL 28 and GL 28a that authorises Afghanistan-related transactions that make use of TKB as a correspondent for Afghanistan-related transactions until 23 January 2023:[42]

GL 28 also authorises US financial institutions to operate correspondent accounts on behalf of TKB, or any entity in which TKB owns, directly or indirectly, a 50 percent or greater interest, provided such accounts are used solely to effect transactions ultimately destined for or *originating from Afghanistan that are authorised by the GL. This means that US financial institutions are authorised to debit or credit correspondent accounts maintained for TKB, provided these debits or credits are for payments that are ultimately destined for or originating from Afghanistan.*

- US Department of the Treasury website, FAQs on Afghanistan-related sanctions[43]

Case study: Impact of inaccessible functioning banking channels

A technology company in Afghanistan, operating in the country for many years, was asked to supply technology equipment to a UN agency for a new project in Kabul in late 2021, as part of the humanitarian response in the country. Since the company was unable to access a functioning banking channel to make payments to suppliers located in North America (including through their lack of access to SWIFT), they were unable to import relevant supplies. Making the payments in *hawala* was not an option as the North American company did not accept this mode of payment. No other payment platforms were available to transfer funds. As such, the technology company was forced to turn down a major contract and lost out on a sizeable new source of recurring revenue. It was not clear whether the UN agency in question was able to secure a new technology supplier inside Afghanistan.

Collectively, these factors have limited the ability of food suppliers and other private sector companies to access financial services to continue operating at the same scale as the months preceding August 2021. These pressures are explained in more detail below.

4.1 Banks' risk mitigation strategies

Derisking strategies of international banks towards Afghanistan vary. Banks with US exposure have become particularly risk averse, according to sectoral consultations. Some interviewees mentioned the withdrawal of European banks, particularly those in Germany, since August 2021 as an additional challenge. A small number of banks retain an active role in servicing international transactions to Afghanistan,[44] though their availability can depend on the types of transactions involved and final customers within Afghanistan. An executive of one European bank noted that it had been able to resume Afghanistan transactions, and expressed positive views over sanctions clarity:

It was painful working on Afghanistan in mid to late 2021 in terms of the sanctions and [the slow pace of adoption of] exemptions, particularly needing to make sure there was clarity from regulators and government bodies. But once we understood from a risk perspective what was allowed and what wasn't, it was business as usual. The main problem in Afghanistan now is not risk or what is allowed, but liquidity.

– European banking executive involved in Afghanistan banking transactions

In some instances, derisking has led to complete blockage of banking services to certain Afghan firms and blocked access to assets in certain financial institutions. For example, a senior banking executive from a state-owned Afghan bank said that their $25 million bank account with a major US bank branch in Dubai has not been accessible since August 2021. In addition, their former correspondent bank was no longer replying to any communications. Some companies described diverted and delayed trade, as well as reduced profits in relation to difficulties accessing formal banking channels. In other instances, questions over permissibility of payments were resolved satisfactorily in the view of banking executives, whereby remaining constraints are more linked to the type of transaction or customer with which the bank is dealing. According to a number of interviews, some of the above challenges eased over the course of 2022, and some transactions have been facilitated through the UN exemption and US GLs.

Case study: Payment challenges facing an Afghanistan business

A company in Afghanistan that produces paper used by a range of sectors for packaging, including food exporters, formerly imported raw products from Europe, the US, as well as from elsewhere in the world. The company reports that it has been unable to make use of the formal banking sector for international payments since August 2021, and that the problem was particularly marked among European banks. This meant that supplies from former sources became unavailable. The company sourced alternative supplies from Pakistan, but had to wait three months to receive permission from a US bank that was involved in the transaction, via a leading Afghan bank. Aside from the need to secure new suppliers and the delays, suppliers were also subject to a 50 percent price increase due to higher export taxes imposed in Pakistan. According to a representative of the company, out of $100,000 relating to any one deal, the company needed to spend $4,000 to $5,000 in transactions costs in late 2022. This included border taxes and bank transaction fees, and marked a signifgant increase compared with transaction costs of approximately $2,000 before August 2021.

5 Trade challenges

Several trade-related challenges impose constraints on private sector operations in Afghanistan, in addition to those described above.

5.1 Supply chain constraints related to the war in Ukraine

The WFP detailed a steep rise in the global prices of fuel, fertiliser, and cereals linked to the conflict in Ukraine since February 2022.[45] They noted that 94 percent of its country offices have reported "rising food and nutrition needs due to the impact of the Ukraine crisis," with many populations around the world having to reduce their food intake due to soaring prices.[46] This has been driven by a number of factors linked to the war. First, grain planting in Ukraine in 2022 has been cut by half since the onset of the war.[47] Second, truck and rail transportation, that would have been used to transport food and related goods, has been diverted for military activities, according to some consultations. Third, Russia's blockade of the Black Sea coast – and of millions of tons of grain supplies in Ukrainian deep-water ports – has curtailed Ukraine's involvement in international maritime food trade.[48] Fourth, as noted by one Afghanistan businessperson, electricity costs have increased.

> *We import electricity from Tajikistan and Uzbekistan, but these supplies have been negatively impacted since the war in Ukraine. The same is true for fuel supplies. Prices are rising and supplies are down.*
>
> – Afghan businessperson working with a network of small enterprises across Afghanistan

On 27 July 2022, the UN and Turkey forged an agreement with Russia to unblock grain exports, as well as wider food products and fertilisers via the Black Sea. Alongside this, the UN Joint Coordination Centre Black Sea Grain Initiative was established, based in Istanbul, to monitor the implementation.[49] From August 2022 to February 2023, 17.8 million tonnes of grain and other food products have been exported under the Black Sea Grain Initiative to 43 countries, of which 105,900 metric tonnes were destined for Afghanistan.[50]

According to some respondents, moving goods and services across the region and within Afghanistan has become more challenging due to the war in Ukraine, despite relative improvements in the security situation and less active fighting than in the past.[51] Others, particularly exporters from Afghanistan, did not see a direct relationship between the war in Ukraine and their own operations:

> *The war hasn't been an issue at all for me and my company. The prices of wheat, corn and cooking oil have increased dramatically, though most of these commodities come via the aid community, so this helps absorb some of the price shocks.* – Afghanistan exporter of dried fruit and nuts

5.2 Restrictive regional trade policies to mitigate food shortages

While Russia and Ukraine are not significant trading partners for Afghanistan for food imports and exports, or that of related products (see Annex 1), the two countries play a critical role in global food supplies. Russia and Ukraine cumulatively accounted for some 30 percent of global wheat supplies and 70 percent of sunflower oil supplies, with Russia accounting for the largest portion of the world's fertiliser exports, making up around 15 percent of world supplies.[52] Afghanistan is particularly vulnerable to disturbances in these supplies given its position as one of the largest importers of flour in the world[53] and a major importer of other food items and related goods.

Russia's domestic ban on the export of food and fertilisers, enacted to stabilise domestic supplies and prices following its invasion of Ukraine,[54] is playing a major role in Central Asian economic crises and food shortages, according to some reports.[55] Countries such as India (the highest ranked exporter of food and second ranked exporter of food products to Afghanistan),[56] Indonesia and Malaysia have restricted exports of wheat, cooking oil and chicken to insulate their domestic markets. In addition, some 20 other countries have imposed various forms of export controls to mitigate impacts of rising food prices and dwindling supplies.[57] Kazakhstan, which is Afghanistan's second most important country for food imports according to the latest World Bank figures from 2019,[58] imposed a temporary quota on exports of wheat and wheat flour according to the Food and Agricultural Organization (FAO).[59] This had an important impact in Afghanistan, as Russian wheat was often mixed with wheat from Kazakhstan (and processed in Uzbekistan) for reasons of pricing and quality, as detailed below:

> *When the war in Ukraine started, Kazakh and Uzbek firms – who were purchasing directly from Russian suppliers – stopped exporting grain and other food items to us in Afghanistan to protect their own reserves. We had large pre-ordered supplies that were held up in Kazakhstan and we only got some released following the granting of exemptions from the Kazakh Government. We also had to get exemptions from Russia, but this took a long time – it was a very political process. In addition, prices would fluctuate a lot – they would give us prohibitively high quotes to deal with these fluctuations.*
>
> – Afghanistan grain importer

Furthermore, Pakistan,[60] which ranks as the number one food and food products exporter to Afghanistan,[61] has reportedly been hit hard by other countries' grain and vegetable oil restrictions.[62]

5.3 Domestic Afghanistan trade regulations

Domestic trade regulations in Afghanistan have increased under the new de facto Taliban authorities. These changes require Afghan companies to produce more formalised paperwork. Afghan firms describe the need for bolstered capacity to help them navigate these new requirements, which they report can be costly and time-consuming to obtain, sometimes taking weeks or months to be granted.[63] Furthermore, outgoing banking transactions are no longer permitted (at the time of writing in 2022) without the correct paperwork. A representative of one Afghan bank described new processes involved in payments for food imports:

> *If we wanted to import something before from China, we would just provide documentation to the bank and the bank would then transfer the required amount to the correspondent bank. Now the process is dependent on a DAB report and there are new restrictions on imports from China; only food is allowed through.*
>
> – Afghan banking executive

5.4 Reduced airline freight capacity

The sharp reduction in commercial flights in and out of the country since August 2021, that arose in part due to the lack of adequate security at Kabul Airport, has resulted in a dramatic decline in freight capacity[64] for goods being transported into Afghanistan via air. Furthermore, the Air Corridor Programme is no longer in operation.[65] This was a subsidised export initiative designed to facilitate the export of high value and perishable agriproducts, 80 percent of which was paid by exporters and 20 percent by donors. As a result of these logistical constraints, many suppliers have been forced to switch to road transportation. Some firms cited the lack of sufficient flights as a constraint in operating at scale or with appropriate speed.

According to one UN official involved in supply chains of essential goods to Afghanistan, the "cessation of commercial flights and a drop in freight capacity – coupled with funding challenges – [has meant that] exports of high value agricultural products have been immensely impacted". The situation was reportedly "manageable" at the time of writing but may become a problem in instances in which time-sensitive transportation is of the essence, such as for medicines and vaccines, according to the interviewee.[66]

Photo: Ingebjørg Kårstad/Norwegian Refugee Council. A few potatoes, onions, peppers, garlic cloves and a little flour – everything the Afghan family has in storage to make it through the day.

6 Afghanistan's economic challenges

A complex array of economic pressures present challenges for businesses in Afghanistan. This includes poor access to liquidity and physical bank notes; inflation and currency exchange rate fluctuations; restrictive or confusing domestic regulations; decreased purchasing power; and poor institutional capacity, including due to human flight from the country. Other challenges highlighted included:

- A number of domestic financial controls[67] imposed since August 2021 were described in interviews as having an impact on Afghanistan's private sector activities.
- Restrictions imposed by DAB (described above) currently prevent the transfer of funds from Afghanistan to other countries, except those permitted in relation to certain key areas (such as raw materials for the agricultural sector).[68] Transactions are governed via a strictly enforced list of permitted trade items.[69]
- Domestic controls on withdrawal limits from bank accounts – implemented to control inflation, prevent capital flight and in response to the 2021/2022 halt in printing of the Afghan local currency, which led to liquidity and solvency problems – prevented access by firms to sufficient quantities of cash.[70]
- Restrictions on the use of US dollars – enacted for similar reasons as those described above – pose problems for some firms. According to one Afghan company dealing in the import of essential goods, "a big problem is that international firms want to be paid in US dollars and will not accept the Afghan local currency".
- Some interviewees cited confusion over new Sharia banking laws, including policies on charging interest.

Reduced capacity in key institutions and firms, and loss of female workers

Public institutions, in areas such as agriculture and those providing support to businesses, have taken a severe hit since August 2021, according to consultations. The de facto ministries of Agriculture, Irrigation and Livestock, Mines and Petroleum and Industry and Commerce, which are spearheading the de facto authorities' economic recovery initiative, have approximately 48 percent fewer technical experts, according to UNDP.[71] Questions over the independence of DAB with its associated lack of a functioning monetary policy, pose concerns for foreign businesses operating in the country. This is coupled with the lack of international support to build its capacity or permit it to fulfil its functions.

Further damaging the Afghan economy is the fact that, since August 2021, the loss of many women from the Afghan workforce is thought to have equated to an immediate drop of $1 billion for Afghanistan's economy. The latter is compounded by the net outmigration of 1.4 million Afghans.[72]

6.1 Depressed purchasing power

UN schemes to release cash into the Afghan economy, such as the UN Humanitarian Financial Corridor, are thought by some to have increased the purchasing power of the Afghan people,[73] via the receipt of cash assistance provided by aid agencies. Others have argued that, in spite of the essential role it has played in the short term, the schemes do not serve the purpose of strengthening the economy as a whole or assisting businesses to grow because the private sector cannot directly access most schemes.[74] At the same time, while humanitarian assistance and some community-based development activities have been possible since August 2021, much of it has concentrated – understandably – at basic levels in attempts to meet survival-related needs and cannot serve to boost economic activities.[75] In this vein, aid agencies have made it clear that humanitarian assistance alone cannot replace a functioning economy. On 14 September 2022, the US and Swiss governments unveiled the Fund for the Afghan people with potential uses, such as paying for essential central banking services like SWIFT payments or banking sector liquidity support.[76]

6.2 Shortage of bank notes

Considering the liquidity crisis and difficulties accessing physical bank notes, vendors cannot make payments in many cases.[77] Poor banking functionality is eroding trust in the Afghan banking sector among private sector actors and discouraging firms and individuals from depositing cash, according to interviewees. This reduced depositor base, which fuels the banking sector's liquidity crisis, is exacerbated by the fact that many Afghani bank notes in circulation have deteriorated to such a state that they can no longer be used. This is given the production of Afghanis notes halted between August 2021 and October 2022, in light of regulatory concerns relating to continued working relations with DAB.[78] On 28 October 2022, DAB signed a deal with Polish Security Printing Works, which committed to the delivery of 380 million banknotes to Afghanistan within a month. This represented the first shipment of Afghani notes since 15 August 2021.[79] DAB was able to pay for the production of the bank notes via international banking system payments, after assurances were made from OFAC to the Polish printing company that they would not be prosecuted, allowing a transaction to take place with DAB.[80]

6.3 Staffing cuts and business closures

Afghan businesses have had to resort to various coping mechanisms to survive the past 18 months, while others have faced closure. This has included reduced investments via friends and family, staffing cuts and decreased staff salaries, particularly among medium and large firms.[81] One Afghan logistics company that imports food to the country mentioned the need to reduce their workforce by 25 percent. Whereas another Afghan firm working in the manufacturing sector noted that it has had to reduce the hours of its workforce by some 70 percent since August 2021. A different Afghan company in the services industry linked to the agri-food sectors relayed that since August 2021, they were forced to let go of over 50 percent of their staff. Another interviewee suggested that some 2,000 factories closed over the past year in Afghanistan due to the combined pressures on the sector. One food exporter described measures employed to keep afloat:

> *We were hoping to generate around $20 million this year, but so far, we haven't even reached half a million United States Dollars. We found a way to finance our operations via funding from friends and family. In return we give them 50 percent of the profit. It allows me to employ some staff in Kabul and keep the brand alive. But it's not sustainable.*
>
> – CEO of a dried fruit and nuts export firm in Kabul

An expert on Afghan supply chains of essential goods interviewed for this report explained that the panoply of pressures described above prevent localisation in terms of local manufacturing and capacity. In combination with a lack of specialised skills, international firms that would otherwise support local manufacturing and expertise in the country are unwilling to engage in business in Afghanistan.

Photo: Jim Huylebroek/Norwegian Refugee Council. An overview of Gullan refugee camp, Khost province

7 Afghan businesses' international transfers

Respondents identified four main methods that private sector actors have used to transfer money internationally in the absence of functioning formal banking channels including the use of overseas bank accounts avoiding Afghanistan; informal money transfer systems (e.g. *hawala*) and currency swaps (mapped below in Figure 1).

7.1 Overseas bank accounts avoiding Afghanistan

According to private sector actors consulted for this report, the only way that Afghan companies can transact at scale via formal banking channels is if they have access to foreign bank accounts – such as via overseas offices. This signifies that smaller companies without access to foreign accounts are forced to make use of informal or partially regulated value transfer systems, like *hawala* or barter systems. According to one Afghan businessman:

> *We have to use accounts in Dubai, but it has been a big challenge getting the banks there to understand that it's not Afghanistan that's sanctioned. It was really hard opening new bank accounts there too, as they were wary about the Afghan connection.*
>
> – Afghan businessperson

The representative of a major Afghan agricultural importer and exporter in Afghanistan noted that if companies mention Afghanistan in the payment instructions of international bank transactions, it will get blocked; even for food shipments via the United Nations.

7.2 Hawala

Hawala remains the main mode of transferring funds within the country for many Afghan businesses. Many businesses that formerly made active use of formal banking channels have increasingly had to turn to *hawala* to settle payments. Other studies have found that for international payments, some two-thirds of companies used *hawala* and only one-fifth used the formal banking sector, with the latter weighted more to larger firms in Kabul.[82] Some companies use *hawala* for everything from personal transactions and payroll, to sales of exports to customers, especially in certain countries in Central Asia and the Middle East, according to interviews. Nevertheless, *hawala* out-payments to international suppliers is not an option in most cases, as many international firms do not accept this mode of payment, particularly outside the Middle East and Asia,[83] as described by one interviewee:

> *When the Taliban came back into power, we couldn't access any of our funds in Afghanistan due to domestic restrictions and liquidity challenges. We had to switch to hawala for all our work inside the country and for some transactions with Uzbekistan. But [we could use these channels for] only up to around $100,000.*
>
> – Major Afghan agricultural importer and exporter

Such transfers have also been subject to an increase in fees since August 2021. One Afghan firm that imports a range of food items into the country described how fees had increased by 2 percent to 10 percent, depending on the type of transaction involved. As described by another exporter:

> *I can pay for many things via hawala but there are certain things where it's just not feasible. How can I pay for my Google for Business account, for example, where credit card payments to international companies are not an option right now in Afghanistan?*
>
> – Afghan exporter of dried fruit and nuts

7.3 Currency swaps

Since August 2021, a number of Afghanfirms have been making use of currency swaps inside and outside the country, in light of problems accessing national and international banking channels. These use similar, though typically distinct swaps, to those employed by NGOs and UN bodies. An example of the latter being the UN Humanitarian Exchange Facility, which to date has not been able to operate. Respondents noted that such mechanisms were not available to all businesses, however, particularly those that did not have good networks to companies overseas or access to foreign bank accounts. As such, this method of accessing physical cash did not represent a sustainable, scalable, or long-term solution.

Case study: Afghan firm's use of currency swaps

A medium-sized Afghan exporting company has engaged in parallel currency transfers with food companies in Uzbekistan and Afghanistan over the past year. Before August 2021, the company was able to make and receive banking payments to and from neighbouring countries, but this is no longer possible. To keep trading, the Afghan firm now ships their produce to Uzbekistan, where payment systems and banking channels continue to function normally. The company then sells and ships their Afghanistan-sourced produce from Uzbekistan to other countries using Uzbek banks and payment mechanisms. To get capital back into Afghanistan, they lend money to Uzbek food traders exporting goods into Afghanistan. The Uzbek food traders return the loan to the Afghan export company in Afghanistan, allowing the Afghan exporter to then pay for in-country salaries, production inputs and other investments.

7.4 Digital payments

Digital payment platforms represent an important potential means for businesses to transfer funds in Afghanistan, pending appropriate resourcing and support. Use of digital payment platforms and mobile money remain limited in Afghanistan, however, especially in rural areas, due to the absence of a functioning digital ecosystem in the country. Most local businesses and customers operate using only cash. Other challenges that have hindered earlier efforts to scale-up digital payment solutions in the country relate to insufficient digital infrastructure in certain areas (electricity, internet, banks, etc.) and cultural opposition. Nevertheless, its use has been growing since 2021, according to some reports.[84] Four mobile money platforms currently operate in the country, with a number of digital platforms growing in prominence. An example of the latter is HesabPay, hosted by Moore Afghanistan.[85] HesabPay is currently working with a USAID programme to expand their services to 2.5 million Afghans and 111,000 merchants (of which an estimated 11,000 will be able to transact internationally), according to its CEO.[86]

Case study: HesabPay (Moore Afghanistan)

Moore Afghanistan's HesabPay is a new platform expanding its services in Afghanistan. Able to work across all mobile phone networks, the platform offers a digital wallet using either a smartphone app or a QR code card for those without smartphones. The platform allows the transfer of funds, including internationally, between individuals, companies or official bodies and payment of electricity bills. It also offers users the ability to "cash out" through HesabPay agents. There are no fees for digital transfers, though fees may be incurred when bank or *hawala* transactions are involved.

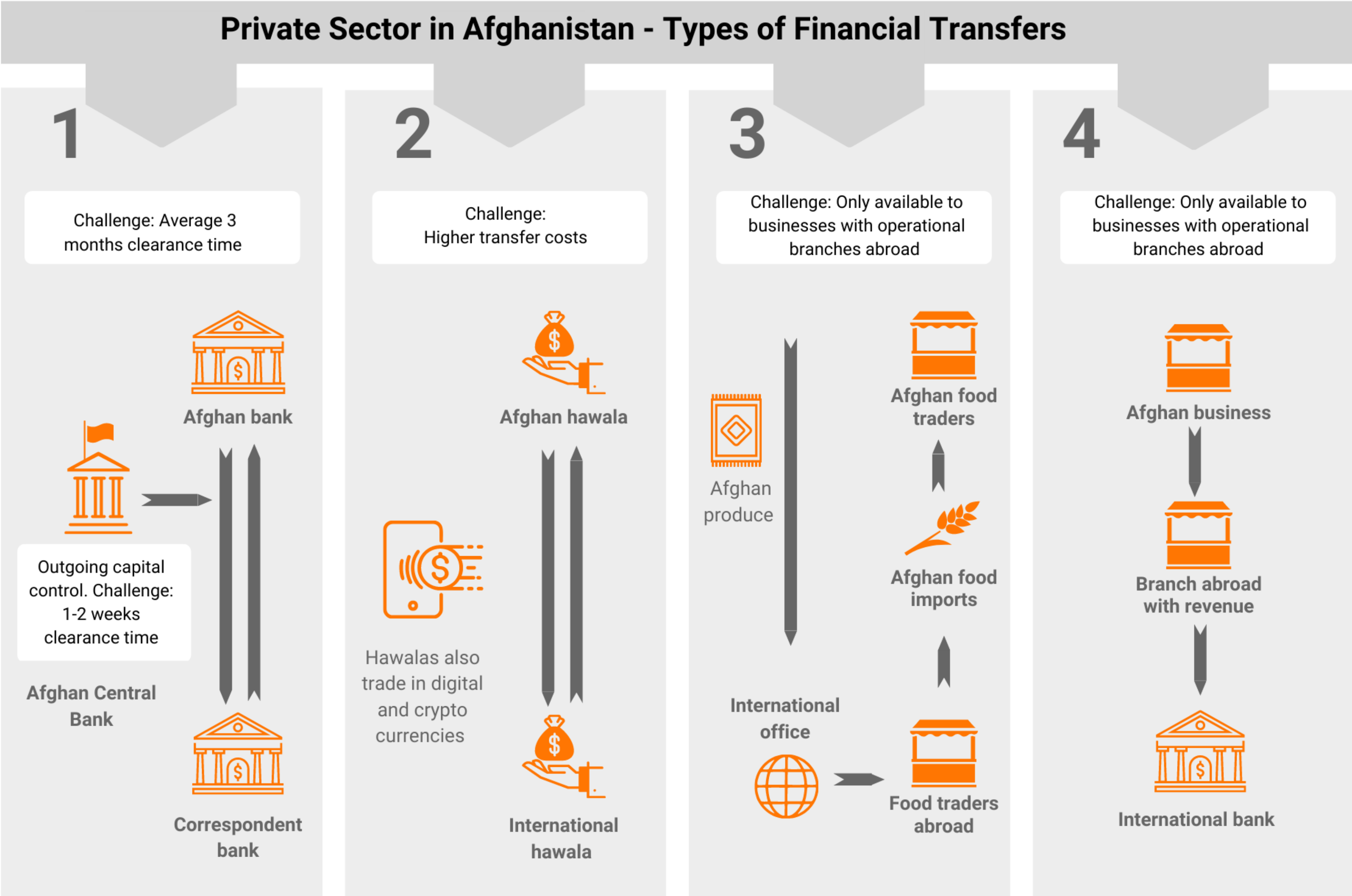
Another example of a digital platform is LOTUS20, hosted by Fintech for International Development (F4ID), which was borne out of a collaboration between Save the Children International, Standard Chartered Bank and Barclays Bank.[87]

Case study: LOTUS20 (F4ID)

LOTUS20 enables NGOs to pay small- and medium-sized local vendors to provide humanitarian assistance, including food items and other essential goods, to target households in need. Item prices are pre-agreed between the organisation and the local vendor on a rolling basis. Invoices are systematically generated on behalf of the vendor and promptly settled electronically by the NGO. F4ID holds that this approach helps stabilise purchasing power, reduces the demand for cash to buy essential goods, and helps provide certainty for both local trade and household needs. It operates over standard Android devices and is made available to NGOs and vendors in Afghanistan via the Google Play Store. Save the Children International conducted a small pilot in Afghanistan in June 2022 using LOTUS20. It employed local businesses to supply 63 tonnes of food to 600 target households in two provinces in one 24-hour period. Every transaction was digitally verified and timestamped, ensuring real-time distribution reports to the NGO and rapid payment to the local vendor. According to F4ID, the post-distribution monitoring report conducted by Save the Children after the pilot concluded that "90 percent of households using LOTUS20 agreed that the e-vouchers gave them more protection from local price volatility, meaning 75 percent preferred e-vouchers to cash assistance and 73 percent agreed it met their economic and nutritional needs".

A key problem at present is that most existing digital or mobile money platforms cannot be used to send funds out of Afghanistan, though they are reportedly playing a useful role in supporting some trade domestically. Continued international support of digital payment platforms was described as important and valuable by many, particularly in the hope that it could support a broader shift to digital banking, including among businesses. This could also bring about benefits for private sector resilience, financial inclusion, and accountability and transparency regarding payment pathways. Major international resourcing would be required to support this type of growth.

Figure 1: Financial flows for private sector firms and challenges in Afghanistan



8 Conclusion

The complex web of regulatory, economic, and financial constraints facing Afghanistan since 2021 continues to exert an insurmountable humanitarian impact on the Afghan people. In today's context, sharp economic contraction, and severe food insecurity present monumental challenges, including through hindering private sector activities and the ability of the Afghan economy to recover and strengthen. This report concludes that capacity building and awareness-raising is urgently warranted to reassure the international business community that Afghanistan should be open to business. The UN and US' targeted sanctions regimes are limited to a set of individuals and entities in Afghanistan and do not apply to the entire country.

UN and US exemptions allow private sector actors operating in Afghanistan to engage in transfers of funds or assets to designated persons or entities if they relate to activities that support basic human needs in the country. This includes the processing and payment of funds and the provision of goods and services to support such activities. These exemptions and GLs have played a vital role in supporting continued trade in, and with, the country. US GLs also allow for the continued use of some sanctioned Russian banks that act as correspondents in some Afghanistan trade.

However, financial transfers involving designated individuals and designated de facto authorities falling outside the scope of permissible humanitarian trade and activities supporting "basic human needs" can represent a constraint for businesses operating in Afghanistan, especially in relation to how such activities are defined and mechanisms for the payment of taxes. In addition, businesses engaging in the trade of essential goods to and from Afghanistan place significant value on clear guidance and capacity building on permissible activities under UN and US sanctions regimes to forge greater confidence in, and appetite for, resumed trade with Afghanistan. CBRs available to the Afghan financial sector are in serious decline due to perceived risks, costs, resourcing burdens and, in some countries, ongoing confusion linked to sanctions compliance.

A particular challenge faced by the majority of Afghan firms is access to functioning banking channels, which have become largely inaccessible for cross-border payments since August 2021, due to numerous trade and economic constraints, including financial sector derisking. Only Afghan firms able to access overseas bank accounts, through having offices in other countries, primarily in Turkey and the UAE, are typically able to settle international payments via the formal banking system. The same firms have struggled to open new bank accounts since August 2021. Moreover, some Afghan firms dealing in food and other essential goods lack the capacity to meet stepped-up standards adopted by Afghan banks since 2021 regarding increased compliance checks. Other firms have suffered from a long waiting time of up to three months for these procedures to be completed. As a consequence, *hawala* is now the dominant form of international and domestic transfers for Afghanistan's private sector actors, yet is not an accepted form of payment by most international companies. Since 2021, *hawala* has also been subject to increased transaction costs. Alongside pre-existing multidimensional poverty, displacement, severe food insecurity and risks of human-driven environmental hazards, other exacerbating factors include loss of many women from the Afghan workforce; restrictive domestic trade policies and financial controls; absence of a fully functioning Central Bank; curtailed access to financial services and liquidity. Reduced airline freight capacity to and from Afghanistan and reduced contact with international partners through trade fairs since August 2021 were also cited as causes for concern as these fairs have been a considerable source of new business deals. Global and regional impacts of Russia's 2022 war in Ukraine were also described as sources of additional pressure on the Afghanprivate sector, including in relation to elevated food and energy prices.[88] As a consequence of these multi-dimensional challenges, many traders and producers have no longer been able to import or export goods through their usual supply chains since August 2021, forcing them to find costlier trading partners from other countries and develop a set of other coping mechanisms.

Annex 1

Afghanistan's principal trade partners, according to most recent World Bank data, are as follows:

- **Food imports (2019)**: Pakistan, Kazakhstan, Malaysia, Uzbekistan, India, Turkey, Iran, Vietnam, Kenya and UAE.[89]
- **Food exports (2019)**: India, Pakistan, Turkey, China, Turkey, UAE, Iraq, Saudi Arabia.[90]
- **Food product imports (2022)**: Pakistan, India, Republic of Korea, UAE Turkey, Iran, US and Italy and China.[91]
- **Food product exports (2022)**: Pakistan, UAE, Turkmenistan, Tajikistan, Iran, Uzbekistan, United Kingdom, US, Turkey and Canada.[92]
- **Chemical fertilizer imports (2021):** Uzbekistan, Turkmenistan, Australia, Iran, Kazakhstan, China, Tunisia, Pakistan, Turkey, Russia.[93]

Endnotes

[1] The UN Assistance Mission in Afghanistan has the mandate to play a key role in coordinating dialogue and facilitating technical assistance between international financial institutions, Afghanistan financial institutions and the Taliban, without inferring recognition of the authorities.
[2] Afghanistan sits at the crossroads between Central Asia, South Asia and the Middle East and is one of the poorest countries in the world. It's 34 million people have suffered wars and conflicts over the past four decades.
[3] The country was already suffering from rising unemployment and widespread poverty and malnutrition in August 2021, linked to decades of war and conflict, climate change-related droughts, pre-existing financial sector derisking and the COVID-19 pandemic. In late 2021, approximately 19 million people in Afghanistan experienced high levels of acute food insecurity, representing an almost 30 percent increase from the same season the year before (Integrate Food Security Phase Classification, (2021), "Afghanistan", www.ipcinfo.org/fileadmin/user_upload/ipcinfo/docs/IPC_Afghanistan_AcuteFoodInsec_2021Oct2022Mar_report.pdf).
[4] UNDP (2022) "One Year in Review – Afghanistan Since August 2021," 5 October, www.undp.org/afghanistan/publications/one-year-review-afghanistan-august-2021
[5] Described in more detail in Erica Moret (2022) "Life and Death: NGO Access to Financial Services in Afghanistan," Norwegian Refugee Council, January, www.nrc.no/globalassets/pdf/reports/life-and-death/financial-access-in-afghanistan_nrc_jan-2022.pdf.
[6] UNDP (2022) "One Year in Review – Afghanistan Since August 2021," 5 October.
[7] UNDP (2022) "One Year in Review – Afghanistan Since August 2021," 5 October.
[8] WFP (2022) "One Year Since the Transition in Afghanistan: A Review of Monthly Remote Food Security Updates," August, https://reliefweb.int/report/afghanistan/one-year-transition-afghanistan-review-monthly-remote-food-security-updates-august-2022
[9] WFP (2022) "One Year Since the Transition in Afghanistan: A Review of Monthly Remote Food Security Updates," August.
[10] WFP (2022) "War in Ukraine drives Global Food Crisis," https://bit.ly/3nsc95e
[11] One interviewee, whose firm imports food to Afghanistan, noted that since August 2021, "flour prices increased by $108 per ton and vegetable oil increased by $300 per ton."
[12] Afghanistan now ranks among the world's largest importers of flour, according to the International Grain Council (for more details, see www.igc.int/en/default.aspx).
[13] In particular from Kazakhstan, Pakistan and Uzbekistan (Bloomberg, 2021, "Taliban Slash Import Duties on Food as More Afghans Go Hungry," 27 October, www.bloomberg.com/news/articles/2021-10-27/taliban-slash-import-duties-on-food-as-more-afghans-go-hungry).
[14] WFP (2022) "War in Ukraine drives Global Food Crisis," https://bit.ly/42Qzbmo
[15] Mohammad Sulaiman Akbari, Hikmatullah Fayez and Subika Farazi (2022) "Afghanistan Private Sector Rapid Survey: An Assessment of the Business Environment – Round 2," World Bank Group, September, https://thedocs.worldbank.org/en/doc/ced9ff1a094dd92886271f532f3c9754-0310062022/original/AFG-Private-Sector-Rapid-Survey-Report-Apr-2022-Final.pdf
[16] It predicts that "high prices and low purchasing power, combined with limited banking sector functionality and interrupted payment systems, will continue to pose challenges for businesses of all sizes." The report cites lack of consumer demand as the principal business constraint since November 2021. It notes that women-owned businesses have been particularly hard hit, resulting in revenue losses (Akbari *et al*, 2022).
[17] According to anonymous interviews with executives of Afghanistan banks throughout 2022.
[18] Furthermore, larger firms (which are most likely to make use of the formal banking sector) have been particularly impacted by problems in the banking system (Akbari *et al*, 2022).
[19] While an estimated 3,500 small enterprises were formerly functioning across many value chains in Afghanistan, for example, no exact figure currently exists on how many have ceased functioning.
[20] Carried out on a confidential basis between July and September 2022, as well as drawing from an earlier set of interviews carried out online with private sector actors in Afghanistan in early 2022, carried out by Erica Moret and Ellie Ward and commissioned by the Norwegian Refugee Council. It included consultations with a number of officials, experts (particularly on grain supplies and food markets) and financial sector representatives.
[21] Findings of a wider study coordinated by Erica Moret at the Geneva Graduate Institute entitled "When Money Can't Buy Food and Medicine: Banking Challenges in the International Trade of Vital Goods and their Humanitarian Impact in Sanctioned Jurisdictions," funded by Swiss Network for International Studies, helps to inform this study in terms of broader desk research and wider interviews on bottlenecks encountered in the supply chains of essential goods in relation to financial sector derisking.

[22] According to some interviewees, as much as 90 percent of Afghanistan's economy is in the informal and partially regulated sector. Statistics are approximate as the Afghanistan border in the trade for food commodities is particularly porous and import data is difficult to collect.
[23] Erica Moret and Karl Blanchet (2021) "Sanctions on Afghanistan: Why less is more," *The New Humanitarian*, 30 September, www.thenewhumanitarian.org/opinion/2021/9/30/sanctions-on-afghanistan-why-less-is-more.
[24] UNSC Consolidated List, www.un.org/securitycouncil/content/un-sc-consolidated-list.
[25] Available at: www.un.org/securitycouncil/content/sres26152021.
[26] For more details, see https://home.treasury.gov/system/files/126/ct_gl20.pdf.
[27] OFAC FAQ 991, https://home.treasury.gov/policy-issues/financial-sanctions/faqs/991 and OFAC FAQ 992, https://home.treasury.gov/policy-issues/financial-sanctions/faqs/992.
[28] United States Department of the Treasury (2022) "Frequently Asked Questions: Afghanistan-Related Sanctions," https://home.treasury.gov/policy-issues/financial-sanctions/faqs/993.
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[30] OFAC FAQ 929, https://home.treasury.gov/policy-issues/financial-sanctions/faqs/929.
[31] OFAC FAQ 958, https://home.treasury.gov/policy-issues/financial-sanctions/faqs/958.
[32] OFAC FAQ 992, https://home.treasury.gov/policy-issues/financial-sanctions/faqs/992.
[33] OFAC FAQ 992, https://home.treasury.gov/policy-issues/financial-sanctions/faqs/992.
[34] According to a World Bank survey, 33 percent of surveyed respondents encountered problems relating to outgoing payments and 21 percent with incoming payments (Akbari et al., 2022).
[35] Moret, Erica (2022) "Life and Death: NGO Access to Financial Services in Afghanistan," Norwegian Refugee Council, January, www.nrc.no/globalassets/pdf/reports/life-and-death/financial-access-in-afghanistan_nrc_jan-2022.pdf.
[36] For more information, see www.swift.com/standards/iso-20022.
[37] Which include restrictions against the financial and energy sectors, asset freezes, travel and visa bans and restrictions on dual-use technologies based on items listed in multilateral export control regimes.
[38] United States Department of the Treasury, OFAC (2022) "Russian Harmful Foreign Activities Sanctions Regulations 31 CFR part 587 General License No. 6B: Transactions Related to Agricultural Commodities, Medicine, Medical Devices, Replacement Parts and Components, or Software Updates, the Coronavirus Disease 2019 (COVID-19) Pandemic, or Clinical Trials," 14 July, https://home.treasury.gov/system/files/126/russia_gl6b.pdf; Ukraine GL 18 covers export to the "Covered Regions" referring to the so-called Donetsk People's Republic ("DNR") and Luhansk People's Republic ("LNR") regions of Ukraine) of agricultural commodities, medicine and medical devices and transactions related to the COVID-19 pandemic (https://home.treasury.gov/system/files/126/ukraine_gl18.pdf); see also later licencing updates and expanded guidance.
[39] United States Department of State (2022) "Joint Statement on Global Food Security," Office of the Spokesperson, 14 November, www.state.gov/joint-statement-on-global-food-security/.
[40] United States Department of Treasury (2022) "Afghanistan-Related Sanctions, Can U.S. persons continue to engage in Afghanistan-related transactions with TKB?" https://home.treasury.gov/policy-issues/financial-sanctions/faqs/1032.
[41] For more information: www.canada.ca/en/global-affairs/news/2022/02/canada-imposes-additional-economic-measures-on-russia-in-response-to-russias-attack-on-ukraine.html.
[42] On 17 October 2022, the extension of the exemption, GL 28a, was issued to be effective until 18 January 2022.
[43] See: https://home.treasury.gov/policy-issues/financial-sanctions/faqs/1032.
[44] Moret (2022).
[45] WFP (2022) "War in Ukraine drives Global Food Crisis."; WFP (2022) "Afghanistan Countrywide Monthly Market Price Bulletin Issue 23 (covering April 2022)," https://docs.wfp.org/api/documents/WFP-0000139383/download/.
[46] WFP (2022) "WFP Scales Up to Support the Most Vulnerable in Global Food Crisis," July, www.wfp.org/publications/wfp-scales-support-most-vulnerable-global-food-crisis.
[47] O'Donnell (2022).
[48] In goods such as cereals, vegetable oils and grain for animal feed production.
[49] United Nations (2022) "Black Sea Grain Initiative Joint Coordination Centre," www.un.org/en/black-sea-grain-initiative.
[50] United Nations (2022) "Black Sea Grain Initiative Joint Coordination Centre."
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[52] International Fund for Agricultural Development, (2022) "Impacts of Ukraine Conflict on Food Security Already Being Felt in the Near East North Africa Region and Will Quickly Spread, Warns IFAD," 17 March, www.ifad.org/en/web/latest/-/impacts-of-ukraine-conflict-on-food-security-already-being-felt-in-the-near-east-north-africa-region-and-will-quickly-spread-warns-ifad.
[53] *Miller Magazine* (2018) "Milling Potential in Afghanistan," 7 February, https://millermagazine.com/blog/milling-potential-in-afghanistan-2614.
[54] António Guterres, the UN Secretary-General, said in June 2022, "Without fertilizers, shortages will spread from corn and wheat to all staple crops, including rice, with a devastating impact on billions of people." Cited in

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[58] World Bank (2022) “Afghanistan Food Imports by Country and Region in $ Thousand 2019.”
[59] FAO (2022) “Kazakhstan to Introduce Temporary Quotas on Wheat and Wheat Flour Exports,” Food Price Monitoring and Analysis, 15 April, www.fao.org/giews/food-prices/food-policies/detail/en/c/1505413/.
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[61] World Bank (2022) “Afghanistan Food Imports by Country and Region in $ Thousand 2019.”
[62] Glauber et al. (2022).
[63] Before August 2021, Afghanistan companies could import goods from countries where strong and trusting business ties existed, such as China, India and Pakistan, without requiring formal purchase orders, according to interviews. Companies would formerly agree on deals via digital channels, then transfer funds through banking channels and receive goods through the Afghanistan customs office. This is no longer possible, according to some interviewees.
[64] Some domestic and international flights continue to operate but with large reductions in capacity. Two Afghanistan airlines (Kam Air and Ariana Afghan Airlines) fly to and from Doha, Dubai, Islamabad, Istanbul and Tehran from Kabul Airport. Iran's Mahan Air operates flights to Kabul. For further details, see: www.france24.com/en/live-news/20220429-deadlock-in-talks-to-run-afghan-airports-officials.
[65] Discussion with an executive of a large Afghanistan trading company in August 2022.
[66] One interviewee stated that the dry fruit exports sector in Afghanistan had suffered since August 2021 but had started to recover somewhat since flight connections with India restarted. One Afghanistan exporter of food products noted that they did not have permission to make use of Pakistani containers when transporting goods to India, serving as an additional constraint.
[67] Prior to August 2021, access to finance was very poor among small enterprises and remains this way, according to consultations. This includes limited access to loans and credit. Female run businesses reportedly face even greater challenges accessing finance, which has been exacerbated during the pandemic.
[68] On the process, a worker of one Afghanistan bank said “once our clients receive a green light then they can import food and medicines from Turkmenistan, Uzbekistan, Tajikistan and Kazakhstan. A whitelist is required for imports from other countries, however.” See www.aib.af/up_to_date_services_info for further details.
[69] For example, the trade in fresh fruit is less impacted as domestic production has continued but is more restrictive regarding clothing goods. Likewise, Afghanistan counts on a number of medicine production companies but not those producing raw materials.
[70] Businesses used to keep money in banks but since August 2021 they have faced major withdrawal restrictions, which has limited their willingness to keep using banking services. According to interviews, most businesses that were operating in the country’s business industrial park had to close as they could not operate on credit.
[71] UNDP (2022).
[72] UNDP (2022).
[73] The collapse of the development and social sector in Afghanistan has led to high unemployment, preventing the flow of cash into, and around, the country and resulting in a lack of demand due to low purchasing power, This, in turn, is reportedly having a negative impact on micro enterprises. Export sectors, particularly those relating to agriculture, are more directly impacted, but this has resulted in reduced production and, again, led to unemployment, thus reducing demand. The situation is exacerbated by high inflation rates. Furthermore, access to Afghanistan-produced inputs for all types of economic activity have become more expensive and harder to access due to price inflation and in relation to the closure of firms that formerly supplied inputs. In parallel, access to imported inputs has been curtailed through high prices, frequent closure of borders (including Pakistan) and payment difficulties as documented in Akbari et al. (2022).
[74] Sectors with large export markets face some of the biggest challenges (such as those exporting carpets and potatoes) as some neighbouring countries have closed their borders for trade.
[75] Some goods and commodities continue to flow from Pakistan. Food processing has reportedly not been impacted when the raw goods are available within Afghanistan.
[76] United States Institute of Peace (2022) “U.S. to Move Afghanistan’s Frozen Central Bank Reserves to New Swiss Fund,” 28 September, www.usip.org/publications/2022/09/us-move-afghanistans-frozen-central-bank-reserves-new-swiss-fund.

[77] A so-called liquidity trap continues to prevail (capital flight combined with the hoarding of cash).
[78] Moret (2022).
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[80] Greenfield, Charlotte (2022) "Afghan central bank gets fresh banknotes after U.S. helps clear payment," *Reuters*, 28 October, www.reuters.com/markets/asia/afghan-central-bank-gets-fresh-banknotes-after-us-helps-clear-payment-2022-11-09/.
[81] Akbari et al. (2022).
[82] Akbari et al. (2022).
[83] Afghanistan companies can sometimes receive payments in *hawala* from outside the country but not the other way around.
[84] Moret (2022).
[85] The card/app payment platform can work across all mobile phone networks and makes use of a digital wallet using either a smartphone app or a QR code card. It allows for the transfer of funds, including internationally, between companies, as well as individuals and official bodies. It also allows for payment of electricity bills. The company has reported that business registrations rose exponentially since the start of the crisis.
[86] Email consultation on 1 October 2022.
[87] The company that was born out of a collaboration between Save the Children International, Barclays and Standard Chartered launched a new e-voucher and payment platform in Afghanistan in 2022 that can be used by any NGO to provide access to goods and services from local suppliers and to monitor local supplies.
[88] The Taliban signed a provisional deal with Russia on 27 September 2022 to supply gasoline, diesel, gas and wheat to Afghanistan (Yawar, Mohammad Yunus and Greenfield, Charlotte, 2022, "Afghan Taliban Sign Deal for Russian Oil Products, Gas and Wheat," *Reuter*s, 28 September, www.reuters.com/markets/commodities/exclusive-afghan-taliban-sign-deal-russian-oil-products-gas-wheat-2022-09-27/).
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[90] World Bank (2022) "Afghanistan Food Exports by Country in $ Thousand 2019," https://wits.worldbank.org//CountryProfile/en/Country/AFG/Year/2019/TradeFlow/Export/Partner/ALL/Product/Food.
[91] World Bank (2022) "Afghanistan Food Products Imports by Country and Region in $ Thousand 2019," https://wits.worldbank.org//CountryProfile/en/Country/AFG/Year/2019/TradeFlow/Import/Partner/ALL/Product/16-24_FoodProd.
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