



Afghanistan Under Transition: Assessing India's Economic Engagement

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Introduction

In the midst of changing global and regional political dynamics, President of Afghanistan Hamid Karzai visited India in mid-November 2012 to discuss the evolving scenario in his country and the South Asian region, and seek cooperation on critical issues of security, capacity building, regional trade and investment. Afghanistan is passing through twin transitions in 2014; transfer of security from International Security Assistance Force (ISAF) to Afghan national forces and transition of political leadership in Kabul, since President Karzai will complete two terms, the maximum allowed under the country's constitution.

In recent times, India has increased its footprint in Afghanistan and has actively pursued reconstruction and development, capacity building, and training of Afghan security forces. In the wake of political and security transitions in Afghanistan, the visit of President Karzai to India in mid-November holds immense value for New Delhi's future engagements with Kabul. India has keen interest in the Afghan mining sector and has signed an agreement with Kabul to explore the Hajigak mine in 2011. Afghanistan is also crucial for India's trade and energy linkages with Central Asian Republics (CARs); recently, New Delhi has signed the Turkmenistan-

Afghanistan-Pakistan-India (TAPI) gas pipeline project.¹ During his visit, President Karzai explicitly pressed for increased Indian investments in his country, especially in mining and industrial sectors. However, India Inc. appears to be cautious given the looming sense of uncertainty and security dilemma in Afghanistan. India's worries stem from the complex regional geopolitical dynamics, unclear political future scenario, and social fragility in Afghanistan.

In this backdrop, this Paper aims to assess India's engagement in Afghanistan in the future, particularly investment and trade opportunities in the mining sector and the prospects of TAPI gas pipeline project.

India-Afghanistan Economic Engagement and Future Prospects

Though security concerns are crucial in India's policy towards Afghanistan, New Delhi and Kabul have been exploring opportunities for greater bilateral economic cooperation for mutual benefit. India and Afghanistan are strategic partners but their economic relations have been limited. The total bilateral trade accounted for US \$ 639 million i.e. 0.08 per cent of India's total trade in 2011-12.² In general, the bilateral trade comprises export of agro and horticulture products to India; and machinery, medicines, textiles and animal products etc. to Afghanistan.³ On the other hand, India is a major trade partner of Afghanistan; more than 20 per cent of its total exports i.e. US \$128 million, go to India.⁴

Trade between India and Afghanistan has been hampered because there is no direct connectivity between the two countries and Afghanistan is a landlocked country. Both countries need a third party to carry out trade exchanges. In this regard, India and Afghanistan need to explore the potential of Iranian port of Chabahar to help expand trade and transit opportunities and provide alternative transport routes for the prosperity and development. During the Non-Aligned Movement (NAM) Summit in August 2012 at Tehran, a tripartite agreement between India, Iran and Afghanistan officials was successfully concluded and it was decided to set up a joint working group to boost trade and transit through Chabahar to Afghanistan and Central Asia.⁵

Newly discovered mineral resources have been considered major sources of attraction for business opportunities in Afghanistan. It has been estimated that the country has untapped mineral wealth of more than US \$3 trillion, including huge reserves of oil, gas, copper, iron, gold and rare earth minerals like lithium and niobium.⁶ Afghanistan's iron ore deposits are estimated to be worth US \$ 421 billion; copper deposits worth about US \$274 billion; niobium worth US \$81 billion; cobalt worth US \$51 billion and gold deposits are estimated to be worth US \$25 billion.⁷ The US Geological Survey estimates 36.5 trillion cubic feet of natural gas in the northern region of Afghanistan. Oil reserves of the country are estimated to be around 3.6 billion barrels.⁸

Considering the huge deposits of mineral resources in Afghanistan, cooperation in this area holds immense potential for both India and Afghanistan. India is of the view that mining sector and infrastructure development may be the key areas of private investment as Indian companies have indicated to invest up to US \$ 10 billion in the mining, steel plant and related infrastructure in Afghanistan. Indian companies were granted Hajigak bids to mine four blocks of an estimated reserve of 2 billion tonnes of iron ore.⁹ Indian companies have also shown interest in Afghanistan's petroleum blocks and copper ore mines.¹⁰ Afghanistan's mineral resources can be transported to India. There is an agreement between Pakistan and Afghanistan signed in 2010¹¹ on the 'one way supply' of Afghan goods to India via Pakistan.¹² Indian help in reviving Afghan manufacturing industries such as cement, oil, gas, and in services i.e. hotels, banking, and communications would also be important. Indian entrepreneurs should take advantage of the low tax regime in Afghanistan.¹³ Besides, the government of Afghanistan has also announced policy measures to attract investments from abroad, including from India.

Afghanistan has reformed its policies and regulations to attract investments in the country's mining and infrastructure sectors. It has also undertaken initiatives to remove the existing physical infrastructure bottlenecks. The Constitution of Afghanistan (2004) and the Afghan Investment Law (2005) assure foreign investors of complete safeguards for their investments, including 100 per cent ownership and no restrictions on repatriation of capital and revenue.¹⁴ Afghanistan is also improving governance because it still ranks low in the 'Worldwide Governance Indicators' report on the issues of voice and accountability, political stability and absence of violence, government effectiveness, regulatory quality, rule of law, and control of

corruption.¹⁵ It ranks 180 out of 182 countries, third from the bottom on the Transparency International Corruption Perceptions Index 2011.¹⁶ Kabul has also launched a number of initiatives to develop infrastructure in the country, such as the National and Regional Resource Corridors Programme (NRRCP) formulated under the Infrastructure Development Cluster. These programmes are an integrated economic initiative that link existing and planned infrastructure projects with corridors of high export potential from extractive industries.¹⁷ Afghanistan is also attempting to increase its linkages with neighboring countries, including Tajikistan, Turkmenistan and Uzbekistan. A modern transportation network that links Afghanistan with its neighbours would spur long-term growth in the region.¹⁸

In this backdrop, to realize their full potentials and increase prospects of economic engagement, India and Afghanistan have concluded four agreements on cooperation in the relevant areas, including small development projects, fertilizer sector and mineral resources, during the visit of the President Karzai to New Delhi.¹⁹

TAPI Pipeline – Regional Energy Game Changer: A SWOT Analysis

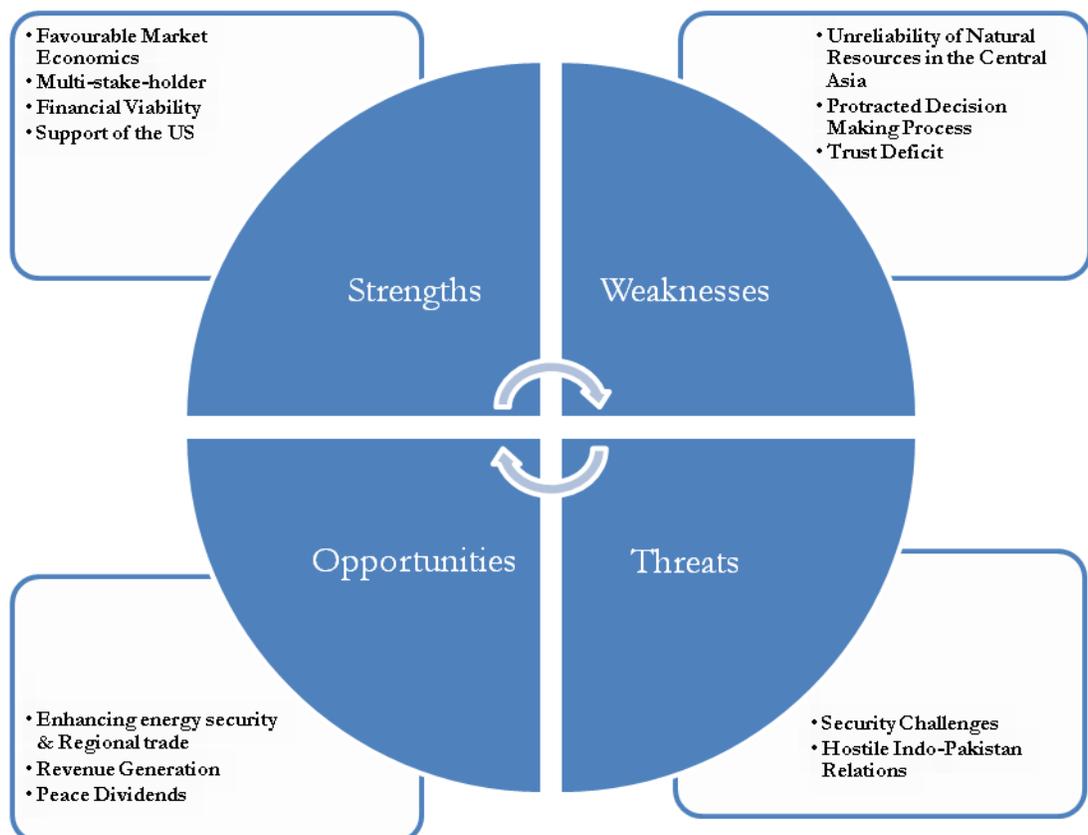
At the regional level, India and Afghanistan are participating in an important energy project. Turkmenistan, Afghanistan, Pakistan and India are planning to build TAPI gas pipeline. This pipeline has been conceptualized to enhance regional energy cooperation. The 1,680 km long TAPI pipeline would cost US \$7.6 billion and connect vast energy resources of Central Asia with the biggest energy markets of South Asia. The participating countries have signed the ‘gas sale purchase agreement’ for the pipeline on 23 May 2012.²⁰ Turkmenistan will supply 90 million metric standard cubic metres per day (mmscmd) of natural gas per day, with India and Pakistan getting 38 mmscmd each and 14 mmscmd to be received by Afghanistan. If operational, the pipeline would transform Afghanistan into an ‘energy bridge’ between Central Asia and South Asia and generate revenue through transit fees as well as employment opportunities. For Afghanistan, the stakes in the pipeline are high and a critical analysis merits attention.

Natural gas is considered as the fuel of the 21st century. Considering the potential of enhancing energy security, business, energy transportation, revenue and employment generation etc., the pipeline appears to be a ‘win-win’ scenario for each country. Even the US, which is a major player in the region, has welcomed the move – as opposed to Iran-Pakistan-India (IPI) pipeline – and described it as a ‘very positive step forward’. The US State Department stated that

the pipeline was a perfect example of energy diversification and energy integration.²¹ However, the current security scenario is quite complicated. Several non-state actors, such as terrorist groups in Pakistan and Afghanistan, and Baloch separatists etc., have the potential to disrupt the dream of gas supply from Central Asia to South Asia.

The SWOT (strengths, weaknesses, opportunities and threats) analysis of TAPI project illustrates that the pipeline is crucial not only for enhancing energy security and regional trade but also in promoting peace and economic development in the region. However, several areas of concern loom large over the project that have the potential to spoil the ‘cherished dream’ of regional countries.

Figure 1: SWOT Analysis of TAPI



Source: Prepared by authors

TAPI project’s major Strengths include favourable market economics; flow of energy from a surplus region to an energy deficient region; multi-stakeholder engagement i.e. four participating countries; and involvement of international financial institutions such as Asian

Development Bank (ADB). Involvement of several stakeholders would enhance the risk-sharing capacity. Greater economic dependency may reduce the scope for adversarial political and strategic decisions. Considering the geopolitical and geo-economic conditions in the region, the US's positive stand on the pipeline is a favourable development. The US's views are accommodated in Pakistan and Afghanistan's foreign policy and economic establishments; hence, its support would boost the chances for the success of this project. The involvement of multilateral financial institutions will also ensure financial transparency and viability of the project.

If we analyse the Weaknesses of the project, it becomes clear that there are many areas of concerns. It is unclear whether Turkmenistan can pump enough gas to feed TAPI. Ashgabat has multiple commitments to meet gas supplies to Iran, China and Russia. It is in this context that the TAPI stakeholders had sought independent verification of country's gas reserves. Alternative source of gas supply to India and Pakistan in the form of Iran-Pakistan-India (IPI) pipeline is available and the cost-benefit analysis indicates that the delivery of gas to India through TAPI pipeline seems costlier than IPI. Due to the involvement of different stakeholders, decision-making would be protracted, ultimately affecting the project. No single partner may be capable of providing security to the entire project. There is a trust deficit among project's stakeholders e.g. between India/Pakistan and Afghanistan/Pakistan. Lack of mutual trust between the two largest stakeholders – India and Pakistan – will always loom large over the project.

However, the pipeline holds immense Opportunities for the region. Apart from access to untapped natural gas of CARs to India and diversifying India's energy basket, the pipeline has the potential to become a mainstay for the regional energy trade. If it succeeds, it will build confidence among regional players to further explore possibilities of trade and investment and promote peace and development in the region. It can be a 'game changer'. The expected benefits can facilitate in deepening economic cooperation and greater mutual understanding. In the larger context of regional trade, TAPI can usher further initiatives. For example, presently Afghanistan has low trade linkages with other countries in the region, but it is estimated that its participation in South Asian Free Trade Area (SAFTA) would result in trade gains of up to US \$2 billion to the region with as much as US \$606 million accruing to Afghanistan.²² The pipeline is expected to generate revenues for both Afghanistan and Pakistan. In the wake of NATO drawdown and

subsequent contraction of financial aid, transit revenue from TAPI can be particularly helpful for the Afghan government.

The pipeline also faces Threats in term of security and political instability in the region. The pipeline will pass through Afghanistan and Pakistan that are unstable and prone to attacks by extremist elements. The Afghan government claims that the security transition is ‘very good’²³ for Afghanistan but skepticism over security is rising. Military withdrawal may lead to power struggle and the possibility of continued armed violence. Fierce competition for political power in Kabul and in the provinces may continue and even intensify in the near future. The prospect of renewed civil war cannot be discounted.²⁴ High costs incurred in securing the pipeline may render the project financially unviable. It can also deter investors from investing in high-risk zones. Though in recent times India and Pakistan have shown flexibility towards each other, their hostile relations have always been an impediment for the growth of regional trade and connectivity. India’s growing engagement in Afghanistan is not taken positively by Pakistan.

Conclusion

Today, Afghanistan stands at the crossroads. The country has not yet stabilized, security transition is in the process, and political transition is also due next year. International support for the democratization process in the country has been gradually increasing; however, political and social fragility remains a major concern.

India’s approach seems to be cautiously optimistic towards Afghanistan. However, Kabul will remain high on the priorities of Indian foreign policy agenda not only for security but also for natural resources and regional trade as well as connectivity with Central Asia, which is considered as India’s ‘extended neighbourhood’. New Delhi’s economic engagement with Kabul will depend on security scenario in Afghanistan in the aftermath of ISAF drawdown in 2014.

The current political and economic conditions in Afghanistan appear favourable for Indian businessmen. President Karzai has promised a ‘red-carpet’ welcome for Indian business community in Afghanistan. The promise needs to be translated into action on the ground. Afghanistan needs to undertake measures to improve governance and enhance security in order to boost investment prospects in the country. The Afghan government should promote transparency in all business deals it enters into with foreign and domestic companies. To

optimize the investment benefits, including TAPI and mining projects, legal framework should be amply complemented by security and effective governance.

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