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DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
Washington, D.C. 20523

CAPITAL ASSISTANCE PAPER

Proposal and Recommendations
For the Review of the
Development Loan Committee

306-21-190-151

AFGHANISTAN - AGRICULTURAL INPUTS

AID-DLC/P-2118

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DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

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DISC/A-17-75

MEETING OF THE DEVELOPMENT LOAN STAFF COMMITTEE

Wednesday, June 25, 1975

New State - Room 3886 N.S.

2:30 P.M.

AGENDA

	<u>Amount</u>
1. Cameroon - Housing Investment Guaranty (AID-DLC/P-2116)	\$10.0 Million
2. Israel - Housing Investment Guaranty (AID-DLC/P-2117)	25.0 Million
3. Afghanistan - Agricultural Inputs	8.0 Million

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DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

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AID-DLC/P-2118

June 23, 1975

MEMORANDUM FOR THE DEVELOPMENT LOAN COMMITTEE

SUBJECT: Afghanistan - Agricultural Inputs

Attached for your review are the recommendations for authorization of a loan to the Republic of Afghanistan ("The Government") of not to exceed Eight Million United States Dollars (\$8,000,000) to assist in financing the United States dollar costs of procuring fertilizers.

This loan proposal is scheduled for consideration by the Development Loan Staff Committee on Wednesday, June 25, 1975; please note your concurrence or objection is requested at the meeting or by close of business on that date. If you are a voting member a poll sheet has been enclosed for your response.

Development Loan Committee
Office of Development Program
Review

Attachments:

Summary and Recommendations
Project Analysis
Annexes 1 - 11

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AFGHANISTAN - AGRICULTURE INPUTS

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8. Statutory Checklist
9. Project Agreement: Management Support for the Afghanistan Fertilizer Company
10. Agriculture Sector in Afghanistan
11. Appraisal of Afghan Fertilizer Company (AFC)

AFGHANISTAN - AGRICULTURAL INPUTS LOAN

Summary and Recommendations

1. Borrower: The Republic of Afghanistan.
2. Loan Amount: \$8,000,000 (Eight Million Dollars).
3. Loan Terms: 40 years maturity, including a 10-year grace period of repayment of principal with interest at two percent (2%) per annum during the grace period and three percent (3%) thereafter.
4. Description of Project: The purpose of this project is to insure the availability of fertilizer in all principal agriculture producing areas. The achievement of this purpose will measurably assist the Government of Afghanistan in meeting its goal of self-sufficiency in agriculture production, principally wheat. This project will also help strengthen the Afghanistan Fertilizer Company, whose formation was assisted by AID and presently is a recipient of AID grant-financed management assistance, by providing AFC with fertilizer material to market and distribute, thereby allowing AFC to expand its distribution area and retail outlets to service a larger number of farmers. The funds provided this loan will be used by the Government of Afghanistan to pay the costs of procuring, shipping, insuring and inspecting chemical fertilizers, primarily Diammonium Phosphate.
5. Executing Agency: The Afghan Fertilizer Company, a wholly owned Government Corporation.
6. Exim Bank Interest: The Export-Import Bank of the U.S. has indicated that it has no interest in financing this activity.
7. Mission's Views: The Mission endorses the proposed loan.
8. Statutory Criteria: All statutory criteria have been satisfied; see Annex 8.
9. Recommendation: Authorization of a loan in the amount of \$8,000,000 on the terms and conditions as stated in the Draft Loan Authorization attached as Annex 1.

10. Project Committee:

	<u>AID/W</u>	<u>USAID/Afghanistan</u>
Chairman :	Robert N. Bakley	John R. Wilson
Loan Officer :	Ted G. Lee	John Standish
Agriculture Economist:	John Balis	Raymond Hooker
Legal Advisor :	Jay A. Burgess	Gerald Zarr
Country Desk Officer :	Gladys Frazier	
Commodity Specialists:	Robert W. Wiley	
	Charles R. Jenkins	

I. INTRODUCTION

A. Application

1.01 The Government of the Republic of Afghanistan has requested a loan of \$8.0 million to finance the foreign exchange costs of procuring, shipping, insuring and inspecting chemical fertilizers, primarily di-ammonium phosphate (DAP). The proposed loan would finance approximately one year's supply (the spring and fall cropping seasons of calendar year 1976) of DAP. The purpose of the loan is to supply a major input-- fertilizer--to Afghanistan farmers which is critical to increasing crop yields and to assure availability of fertilizer supplies in all principal agriculture producing areas. The Government of the Republic of Afghanistan's application letter is attached as Annex 2.

B. Previous U.S. Assistance

1.02 Previous AID assistance directly related to fertilizer consists of two loans authorized in FY 1973 (306-H-017 and 017A) totaling \$19.5 million used (i) to purchase approximately 92,000 MT of fertilizer (50,000 MT of urea and 42,000 MT of DAP) and (ii) to pay for a nine-member management advisory team to assist in the creation of a company to import and distribute fertilizer in Afghanistan (AFC--the Afghanistan Fertilizer Company). As of March 31, 1975, all loan funds were either committed or reserved for commitment and the final shipment of fertilizer has been unloaded at Karachi port and is en route to Afghanistan. It is expected that Loan 017 funds will be fully disbursed by June 30, 1975, when the loan terminates.

1.03 To continue the momentum of AFC, AID approved a grant of \$816,000 in January 1975 to provide participant training to AFC employees and to continue the management advisory services, on a reduced scale, for up to two years. A one-year contract for the advisory services has been signed and the team is in place. Prior to the completion of the one-year contract, AID will undertake an in-depth evaluation of AFC. On the basis of this evaluation a decision will be made on whether to continue or terminate the assistance. The initial ProAg for AFC management services is attached as Annex 9.

1.04 As a result of the previous loan and the assistance provided to AFC, Afghanistan has tripled its use of fertilizer and has made substantial progress toward self-sufficiency in food production. There were no unmanageable problems encountered during the implementation of the project.

C. Other Donor Assistance

1.05 Many other donors have assisted Afghanistan agriculture over the past 20 years and most, or all, continue to do so. All activities and projects in the agriculture sector have at least an indirect effect on the

project to which this paper is addressed; however, three projects directly and most significantly affect this loan. They are:

(a) Mazar-i-Sharif Fertilizer Plant - This Russian-assisted urea plant was completed in October 1974. The plant is designed to produce 105,000 MT per year, but production to date is well below capacity. Assuming even moderate production, this plant will supply all of Afghanistan's urea needs for a number of years. Urea is sold at the plant gate to AFC at \$130 MT. While little is known of the plant's costs (capital, operating), this price should allow the factory to earn a reasonable return when operating at or near capacity.

(b) The First and Second IBRD Agriculture Credit Projects - The first project, signed on June 24, 1970, was a credit of \$5.0 million to support the Agricultural Development Bank's (AgBank) lending program to finance farmers' investments in farm mechanization, shallow-well pumps and improved small irrigation facilities. The project also aimed at institution building to enable the AgBank to better meet the farmers' credit needs. The second project, approved in April 1975, is a credit of \$14.0 million. The funds are to be used to (i) provide credit to 43,000 farmers investing in farm mechanization, on-farm development and modern farm inputs (fertilizer, pesticides and improved seeds); (ii) upgrade the AgBank's organization and staffing through the financing of field allowances for 54 additional staff, 30 fellowships, and equipment and vehicles to support the Bank's branches; and (iii) finance the building of 24 fertilizer warehouses of 55,000 MT total capacity throughout the country.

(c) Project on Agriculture Credit and Related Services through Cooperatives in Afghanistan (PACCA) - Phase I of this project was financed by the Swedish International Development Authority (SIDA) and implemented by FAO. The object of Phase I was (i) to increase farmers' income in certain pilot areas with particular emphasis on farmers with average or below average income and (ii) to support the Government's efforts to improve the organization of services for agricultural development. Phase II of PACCA, which is expected to start in 1975 (agreement between SIDA, FAO and GOA not yet signed), will (i) help organize and support the Ministry of Agriculture's newly created Department of Cooperative Development; (ii) assist the Department to run a training institute with a target of 456 trained in four years; and (iii) assist the Department in establishing about 214 primary multipurpose cooperatives and 14 cooperatives/unions in different provinces, and help the Department in providing the services (training, credit and marketing) and supervision needed by the cooperatives.

II. FERTILIZER USE AND NEEDS

A. Background

2.01 In 1967, a U.S. Agriculture Survey Team recommended that Afghanistan put primary emphasis on improving wheat production, with the objective of attaining self-sufficiency in foodgrains. The strategy recommended was in increased use of fertilizer and expanded use of new high-yielding varieties of wheat. Until 1971, however, fertilizer use was still almost nonexistent, supply was erratic and distribution poor. In 1971, after two consecutive drought years, the Government launched a major effort, concentrated mainly on wheat producing areas, and distributed about 21,500 MT of fertilizer to about 30,000 farmers in a period of less than three months.

2.02 Fertilizer use has now increased with approximately 63,000 MT sold in 1974/75, equivalent to a 29 percent a year growth rate over the past five years. Fertilizer use, however, is still extremely low with the current usage sufficient for only 5 to 8 percent of Afghanistan's irrigated cropland. Presently, 75 percent of the fertilizer is applied to wheat with the majority of the balance applied to sugar and cotton. Annex 10 provides an overview of the Afghanistan Agriculture Sector.

B. The Afghan Fertilizer Company

2.03 The increase in fertilizer usage throughout Afghanistan is largely attributable to the activities of the Afghan Fertilizer Company (AFC) which was chartered in October 1972 and became operational in January 1973. AFC's primary responsibilities are to:

- a. Purchase all chemical fertilizers produced in Afghanistan;
- b. Import those fertilizers not available domestically;
- c. Transport, store and distribute fertilizers to retailers throughout the country; and
- d. Set standards for the control and regulation of fertilizer storage, packing and sales.

USAID initiated its assistance to AFC by financing the services of a nine-man (U.S.) management team for the calendar years 1973 and 1974 under Loan No. 306-H-017. In August 1974, executive management of AFC passed into the hands of the Afghan staff and the U.S. Management team assumed an advisory role. In March 1975, a four-man advisory team was retained for a period of up to two years. USAID is financing the cost of the advisory team with grant funds.

2.04 AFC, as established, was to have been a self-sustaining enterprise-- that is, the company was expected to sell fertilizer at a price higher than its cost. Initially this happened. Fertilizer prices in 1971 were such that AFC could cover its costs and earn a small profit. But with fertilizer prices at their current levels, AFC loses on every sale and must receive continual payments from the Government to stay solvent.

C. Marketing and Distribution

2.05 At present AFC possesses 26,500 tons of warehouse capacity, the ownership of which was transferred to AFC by the Ministry of Agriculture and Irrigation shortly after AFC was established. Twenty-one thousand tons of this capacity is located in primary distribution centers and the remaining 5,500 tons in secondary distribution centers. In addition, 54,000 MT of capacity has been leased or borrowed from the Government and private agencies. Under the IBRD's Second Agriculture Credit Project, funds will be provided to AFC, through an equity investment by the AgBank, to construct an additional 55,000 MT of storage capacity in 24 locations: primary warehouses for 35,000 MT and secondary distribution warehouses for the remaining 20,000 MT. The additional storage capacity is estimated to cost \$1.4 million. Annex 6 shows the location of AFC's existing and proposed warehouses.

2.06 Until recently AFC sold fertilizer only to wholesalers, at a discount of 15 percent below the market price to farmers. Early in 1974, the Government directed that sales to wholesalers be discontinued and that AFC sell fertilizer directly to individual retailers. The rationale behind this move was that fertilizer is heavily subsidized and the Government wished to ensure that farmers, and not the relatively wealthy wholesalers, received the maximum benefit. Under the new system, retailers take ownership of fertilizer at the AFC warehouse and receive a discount of AF 20/bag (\$7.00/MT) below the price to the farmer. Retailers are licensed by AFC and are required to purchase their first fertilizer for cash. Subsequent purchases can either be made in cash or with AgBank credit coupons, received by the retailer from the farmer. At present AFC has licensed about 220 retailers and has plans to increase this to 400 in 1975/76. Annex 5, from the IBRD Second Agriculture Credit Project, show the flow of information, funds and fertilizer for cash and credit sales.

2.07 As previously stated, one of the constraints to development of the Agriculture Sector has been the limited availability of institutional credit to the farmer. To help alleviate this problem, the IBRD Second Agriculture Credit Project will provide \$14.0 million to assist AgBank in financing its lending program. Of this amount, \$6.7 million will be available for short-term lending for fertilizers, seeds and pesticides. These IBRD funds alone will provide sufficient credit for about 50 percent of one year's fertilizer sales. Also, historically the seven cotton ginning companies and the Afghan Sugar Mfg. Co. have provided funds to growers for seed, fertilizer and labor to farmers under contract.

D. Prices

2.08 Fertilizer prices to the farmer are fixed by the Government at \$160/MT for urea and \$179/MT for DAP. The fertilizer sold to the farmer in 1974 was purchased prior to the most recent rise in world prices (AFC uses a FIFO system of accounting). Based on the acquisition cost of this fertilizer, the 1974/75 subsidy to the farmer is estimated as follows:

TABLE 1

Fertilizer Subsidy
(1974/75)

	<u>DAP</u>	<u>UREA</u>
Fertilizer Cost		
Import Cost	\$ 205	\$ 171
AFC operating costs	23	23
Retailers' margin	<u>7</u>	<u>7</u>
Total cost	235	201
Sale price to farmer	<u>179</u>	<u>160</u>
Government subsidy per MT	56	41
Total sales 1974/75	<u>21,210</u> MT	<u>42,320</u> MT
Total Subsidy	<u>\$1,187,760</u>	<u>\$1,739,220</u>

2.09 The subsidy on urea should disappear as soon as imported stocks are depleted and AFC receives all its urea supplies from the Mazar-I-Sharif plant at \$130/MT. The subsidy on DAP will, however, increase as the world price has risen dramatically: the last DAP purchase (10,500 MT) by AFC was at \$478/MT CIF Karachi, and, although prices are now retreating, it is unlikely that prices will decrease to the current Afghanistan subsidized price.

2.10 Looking ahead to 1976/77, and assuming that: (i) all urea is produced at the Mazar-i-Sharif plant at \$130/MT; (ii) DAP costs level at \$300/MT CIF Karachi; (iii) AFC's operating costs hold at \$23/MT; and (iv) sales are as projected, the subsidy in 1976/77 will be as follows:

TABLE 2

Fertilizer Subsidy
(1976/77)

	<u>DAP (Imported)</u>	<u>UREA (Domestic)</u>
Fertilizer Cost		
Import CIF Karachi/Domestic cost	\$ 300.00	\$ 130.00
Inland transportation	30.00	-
AFC operating costs	23.00	23.00
Retailers' margin	<u>7.00</u>	<u>7.00</u>
 Total cost	 360.00	 160.00
Sale price to farmer	<u>179.00</u>	<u>160.00</u>
 Government subsidy per MT	 181.00	 -
 Total sales 1976/77	 <u>33,128 MT</u>	 <u>66,256 MT</u>
 Total subsidy	 <u>\$5,996,168.00</u>	 <u>\$</u>

E. Projections

2.11 Using the AFC fiscal year July 1/June 30 (i.e., two full planting seasons), in 1973/74 Afghanistan used approximately 50,000 MT of fertilizer (two-thirds of which was urea and one-third DAP)--up from 40,000 MT in 1972/73, representing an increase of 25 percent per annum. Sales have been projected by AFC, to continue increasing at this rate at least through 1976/77. Projections of sales, purchases and inventories for the period 1974/75 through 1976/77, assuming a 25 percent per annum growth rate are as follows:

TABLE 3

AFC Projections of Sales and Purchases as
of 1/12/75 Based on Application Mix
of Two Parts UREA and One Part DAP

	<u>Metric Tons of Product</u>		
	<u>1974/75</u>	<u>1975/76</u>	<u>1976/77</u>
Beginning Inventory			
UREA	86,220	53,800	33,775
DAP	<u>29,010</u>	<u>19,198</u>	<u>16,685</u>
Total	115,230	72,998	50,460
Purchases			
UREA (Mazar)	10,000	33,000	75,000
DAP	<u>11,398</u>	<u>24,000</u>	<u>38,000</u>
Total	21,398	57,000	113,000
Available for Sale			
UREA	96,220	86,800	108,775
DAP	<u>40,408</u>	<u>43,198</u>	<u>54,685</u>
Total	136,628	129,998	163,460
Sales			
UREA	42,420	53,025	66,256
DAP	<u>21,210</u>	<u>26,513</u>	<u>33,128</u>
Total	63,630	79,538	99,384
Ending Inventory			
UREA	53,800	33,775	42,519
DAP	<u>19,198</u>	<u>16,685</u>	<u>21,557</u>
Total	72,998	50,460	64,076

2.12 Results for the 1974/75 fiscal year are not yet available but indications are that sales will equal the 63,630 MT's projected. Assuming this is so, inventories on hand at June 30, 1975, will be 53,800 MT/urea and 19,198 MT/DAP (including the 10,500 MT now in transit from Karachi to Afghanistan). Sales for the fiscal year 1975/76 are projected to be 53,000 MT of urea and 26,500 MT of DAP. Assuming a reasonable, or safe, ending inventory equal to 50 percent of the succeeding years' needs (although the IBRD recommends 100 percent), purchases in FY 1975/76 will need to be 33,000 MT/urea and 24,000 MT/DAP.

2.13 Until 1974 Afghanistan imported all its fertilizer needs--primarily urea (46-0-0) and Diammonium Phosphate (DAP) (18-46-0). In 1974 the Russian-assisted Mazar-i-Sharif urea plant commenced production. This plant has a design capacity of 106,000 MT/Y and should satisfy Afghanistan's urea needs for the foreseeable future. Future imports, therefore, should be limited to phosphatic fertilizers (DAP or TSP). The following table shows fertilizer imports for the period 1966/67 - 1972/73:

TABLE 4

Fertilizer Imports

<u>Year</u>	<u>UREA</u>	<u>DAP</u>	<u>TSP</u>	<u>Total</u>
1966/67	5,700	-	3,300	9,000
1967/68	3,000	-	3,300	6,300
1968/69	19,000	6,600	4,000	29,600
1969/70	6,000	11,300	200	17,500
1970/71	10,000	4,700	-	14,700
1971/72	27,400	12,300	1,800	41,500
1972/73	26,000	7,000	-	33,000

F. Economics at the Farm Level

2.14 A number of fertilizer trials have taken place in Afghanistan, most of them in connection with improved varieties of wheat. The "Uniform Wheat Fertilizer Trials" were held in the nine main wheat growing locations in 1968 and 1969 using varying levels of urea and DAP. The rates of fertilizer recommended, as a result of these trials are 387 kg/ha (75 kg/jerib) composed of two-thirds urea and one-third DAP (or a compound mixture equal to 37-15-0). Fertilizer trials are continuing and there are indications that the percentage of nitrogen should be increased, especially for products other than wheat:

TABLE 5

Uniform Wheat Fertilizer Trials

<u>Fertilizer Application Urea-DAP Mix (kg/ha)</u>	<u>Wheat Output (kg/ha)</u>	<u>Average Output per Input (kg wheat/kg Fert)</u>	<u>Incremental Increase kg</u>	<u>Marginal Output-Input Ratio/a</u>
0	1,807	-	-	-
186	2,893	5.84	1,086	5.84
369	3,477	4.53	584	3.19
556	3,888	3.78	411	2.20

3.15 One method of measuring the attractiveness to farmers of fertilizer use is to calculate a benefit:cost ratio using the following formula:

$$\frac{\text{Value of increase on crop yield}}{\text{Cost of fertilizer}} = \text{B/C Ratio}$$

For the farmer to break even the ratio must exceed 1.0 since fertilizer use is accompanied by increases in other costs--improved seeds, higher labor, etc.,--and the farmer must cover the increased cost of inputs in those years when crop failures occur. There are no precise rules for determining the magnitude of the benefit:cost ratio needed before farmers will use fertilizer; nor the ratio needed to motivate farmers, who previously have not used fertilizer, to adopt the new practice. According to TVA, the ratio should be at least 3.0 in developed countries where farmers are accustomed to trying something new; and in developing countries, where farming practices may not have changed for a century or more, TVA recommends a higher ratio and states that benefits must be clearly discernible.

3.16 Using the normal and incremental yields obtained through the "Uniform Wheat Fertilizer Trials" and valuing wheat and fertilizer at current market prices in Afghanistan, the benefit:cost ratio is 4.11:

TABLE 6

Yield without fertilizer	1,807 kg/ha
Yield using fertilizer	2,893 kg/ha
Yield increase	1,086 kg/ha
Value of increase	\$ 126.98
Cost of fertilizer	30.88
Benefit:Cost ratio	4.11

The normal yields obtained in the "Trials" are somewhat higher than those obtained by the average farmer where yields are around 1.000 kg/ha. Using this average, and assuming the same yield with fertilizer (2,893 kg/ha), the benefit:cost ratio would increase 7.1. The benefit:cost ratio will continue to decrease as higher applications of fertilizer are used (the law of decreasing returns). For example, at 369 kg/ha and using the incremental increases obtained from the "Trials" the benefit:cost ratio decreases to 3.03.

III. THE LOAN

A. Purpose

3.01 The purpose of this project is to insure the availability of fertilizer in all principal agriculture producing areas. The achievement of this purpose will measurably assist the Government of Afghanistan in meeting its goal of self-sufficiency in agriculture production, principally wheat. This project will also help strengthen the Afghanistan Fertilizer Company, whose formation was assisted by AID and presently is a recipient of AID grant-financed management assistance, by providing AFC with fertilizer material to market and distribute, thereby allowing AFC to expand its distribution area and retail outlets to service a larger number of farmers. The funds provided this loan will be used by the Government of Afghanistan to pay the costs of procuring, shipping, insuring and inspecting chemical fertilizers, primarily Diammonium Phosphate.

3.02 As shown in Section II, Afghanistan uses two types of fertilizer: urea and DAP. With the completion of the Mazar-i-Sharif urea plant, only DAP will henceforth need to be imported. The requirement for imported DAP for the fiscal year July 1975 to June 1976 (the fall and spring planting seasons) is projected at 24,000 MT (see Para 2.11).

B. Costs

3.03 In November 1974, AFC procured 10,500 MT of DAP through an international tender. At that time, the lowest price offered was \$478/MT (CIF Karachi). In the past few months, however, prices have eased considerably and if AFC entered the DAP market today, it could expect to pay prices in the neighborhood of \$300/MT (CIF Karachi). At these prices the projected import requirement of 24,000 MT ranges in cost from \$7.2 million to \$11.5 million. For the purchase of fertilizer under this loan, AFC expects to "enter the market" in late summer or early fall. Industry sources expect fertilizer prices to then be at today's prices, or possibly even lower. The proposed loan of \$8.0 million should, therefore, be sufficient to finance 24,000 MT of DAP--one full year's needs.

C. Implementing Agency

3.04 The Afghan Fertilizer Company, assisted by Checchi and Company of Washington, D.C., under a grant-financed management advisory contract, will be responsible for all fertilizer procurement, i.e., contracts for product, vessels, insurance and inspection services. AFC will also be responsible for trans-shipment from Karachi (or other ports) to Afghanistan, warehousing, and distribution to retail outlets.

D. Procurement

3.05 The domestic (U.S.) supply of fertilizer has eased considerably and it is expected that ample quantities will be available for export throughout the remainder of 1975. Procurement under the proposed loan will therefore be restricted to U.S. source and origin and Code 941 countries and will be by competitive bidding.

E. Eligibility and Terminal Dates

3.06 The eligibility date for transactions under the loan will be concurrent with execution of the Loan Agreement which is estimated to be 60 days after execution of the Loan Agreement.

3.07 Procuring, shipping and transporting fertilizer to Afghanistan takes between 100 and 140 days, depending on the traffic at the port of Karachi and the availability of rail wagons. To ensure availability of the fertilizer in time for spring planting, fertilizer must be ordered by October 15, 1976. The Terminal Date for Requesting Letters of Commitment will therefore be April 30, 1976; and the Terminal Date for Disbursements will be October 31, 1976.

F. Host Country Contributions

3.08 Fertilizer sales in 1975/76 are projected at about 79,500 MT (53,000 MT of urea and 26,500 MT of DAP). The total cost of this fertilizer, using the Mazar-i-Sharif ex-plant cost of \$130/MT of urea and assuming \$300/MT of DAP, will be \$1.484 million of which the Government of Afghanistan will finance \$6,890 million or 46 percent. In addition, the Government will cover the cost of inland transportation and the operating losses of AFC. The host country's contribution will therefore exceed 25 percent of the project activity as required under Section 110(a) of the Foreign Assistance Act of 1961, as amended.

IV. BENEFITS AND JUSTIFICATION

A. Long-Term Objectives

4.01 One of the long-term objectives which we are pursuing in Afghanistan is to introduce technological change in farming. Without such change, farmers will not produce more and therefore be unable to earn (or at least eat) more. From our experience in South Asia, and from numerous studies, it is clear that the use of fertilizer, both on irrigated and on dry land, is one of the most important ingredients. Even where institutional credit and extension services are limited, as they were in India in the 1960's when fertilizer consumption rose dramatically, we have found that small as well as larger farmers are willing to adopt new farming methods and to use fertilizer. Lack of fertilizer, however, has been a critical constraint in Afghanistan and, at different times, in other countries. We can think of no more significant long-run change in rural Afghanistan than the spread of new agricultural technology of which the use of fertilizer is the most important ingredient.

B. Promoting Fertilizer Use

4.02 Starting in 1972, we helped to create the basic framework for a fertilizer marketing system. The formation of the Afghan Fertilizer Company (AFC) was assisted by an AID-financed management team which helped organize and manage the first systematic and effective fertilizer marketing system ever attempted in Afghanistan. The project was supported by a loan to provide management services and fertilizer for the system. Our objective was then, and still is, to link the development of that institution and the provision of fertilizer to assure that more fertilizer reaches a growing number of farmers. In part as a result of these efforts, fertilizer use rose from 21,000 tons in 1972 to 63,000 in 1974. AFC has expanded, and continues to expand, its warehousing capacity and its organization of private dealers. It will build 55,000 tons of additional storage capacity in 24 locations throughout the country, using funds made available by the IBRD. That will mean almost tripling the capacity of AFC owned storage. AFC is in the process to increase the number of its licensed dealers from 220 to 400. The proposed fertilizer loan is intended to further support the establishment and expansion of AFC's fertilizer distribution system, and will help to assure that an adequate supply of fertilizer flows through the expanded system. Obviously, we do not intend to become permanent suppliers of fertilizer for Afghanistan, and in fact this loan represents the last which we intend to make in connection with the innovations now under way. However, we believe that this additional increment of fertilizer will be supportive of these efforts and will help to institutionalize the expanded fertilizer network.

C. Agriculture Production

4.03 Afghanistan is just approaching self-sufficiency in food grain production and is below self-sufficiency in certain other food crops, particularly sugar. Increasing the land under irrigation and improving water management hold the most promise for increasing agriculture output; but it will be years before these improvements can make a significant contribution to increased production. In the short-term, Afghanistan will need to increase output on the land it now farms; this will require the use of more inputs, the most important of which is fertilizer.

4.04 The benefits from this loan will be increases in agricultural production, primarily food grains. Using an average incremental wheat output to fertilizer application ratio of 4.5, the incremental production of wheat realized with the fertilizer to be purchased under this loan would be 108,480 MT (24,000 MT of DAP times 4.5). Assuming imported wheat would cost Afghanistan \$200/MT, this increased domestic output will have a value of \$21,696,000. And, assuming the fertilizer to be imported under this loan costs \$7,200,000 (\$300/MT), a simple benefit:cost ratio of 3:1 and a foreign exchange saving of \$14,496,000 would result.

D. Employment

4.05 The project will generate substantial employment opportunities through increased agriculture production. We estimate that an increase of 108,480 MT of wheat would increase labor requirements, at the farm level, by 22,700 man-years. If part of the fertilizer is applied to crops other than wheat, for example cotton, the additional labor requirements would increase.

E. Institution Building

4.06 The Afghan Fertilizer Company will directly benefit from the project. The fertilizer purchased will allow AFC to expand its marketing and distribution system, thereby serving a larger number of farmers scattered throughout the country. This support, which will complement the technical assistance we are providing to AFC, is critical since Afghanistan's farmers traditionally distrust government in most forms and, to obtain the farmers' confidence, it must establish itself as a reliable supplier.

4.07 The AgBank will indirectly benefit from the project. AgBank plans to expand its short-term lending for fertilizer, seeds and pesticides from \$5.7 million annually to \$9.5 million annually; and to increase the number of farmers reached from 30,600 to 43,000. This project will provide part of the material the farmer purchases with his borrowed funds.

4.08 Finally, the project will complement the IBRD's Second Agriculture Credit Project. That project provides, inter-alia, (i) technical assistance to AgBank's staff, (ii) resources to support AgBank's lending program, and (iii) funds for the construction of an additional 55,000 MT of fertilizer storage capacity at 24 locations.

F. Target Group

4.09 We do not believe that a fertilizer distribution system can be established to serve small farmers exclusively. What we aim to achieve is that fertilizer is available to smaller as well as larger farmers. As we have learned elsewhere, when fertilizer is in short supply it tends to be available disproportionately to larger farmers. Here as elsewhere, increased fertilizer distribution which eliminates shortages is expected to flow disproportionately in favor of small farmers. Since the average holding of cultivated land is 3.5 ha in Afghanistan, a distribution system covering all parts of the country will bring fertilizer within the reach of the majority of small farmers, land-owners, tenants and sharecroppers alike. The new credit program mentioned above will support the broadened distribution system. Precise data on the distribution of fertilizer users by income, size of holdings and other social characteristics are not now available. However, data on beneficiaries of the credit program is being collected and AFC is already assembling similar data based on their sales records. Those data have so far not been consolidated, but a consolidation will be required under a covenant in the agreement for the proposed fertilizer loan.

G. Evaluation

4.10 The ProAg for the grant-financed AFC management assistance project provides for an in-depth evaluation of AFC during CY 1975/76. The evaluation will be made by a team which will include an outside consultant. The scope of the evaluation will be such that it will disclose AFC's success in marketing and distributing fertilizer including an identification of the beneficiaries. Also, AFC will report quarterly on (a) farm gate prices of basic farm commodities and purchase and sale prices of fertilizer; (b) subsidies per ton of fertilizer sold; and (c) fertilizer procurement procedures being employed (primarily for domestic procurement since AID regulations will be used for all procurement under this loan). Also, the IBRD requires Ag Bank to report quarterly on its activities including the number, size, location and repayment record of farmers receiving credit for fertilizer purchases. These reports will be shared with AID.

V. ISSUES AND COVENANTS

A. Fertilizer Projections

5.01 AFG projects (see paragraph 3.11) fertilizer sales to grow at a compound rate of 25 percent per annum, and that usage will continue in a ratio of two parts urea to one part DAP (a nutrient content of 37-15-0). If either of these assumptions change, it will affect projected DAP requirements.

5.02 While an increase of 25 percent per annum, on the surface, appears dramatic, considering Afghanistan's low use of fertilizer (63,000 MT) a growth even greater than 25 percent is certainly possible. On wheat alone, if the recommended dosage of 369 kg/ha was used on the irrigated acreage alone (1.2 million) the usage would be 464,400 (309,600/urea and 154,800/DAP). Also, some of the past constraints to the use of fertilizer, while not eliminated, have been reduced: institutional credit is now available in greater amounts than ever before, supply is in place, distribution has improved and more extension agents are carrying the message to the farmer.

5.03 Another factor which could upset sales projections, and the rate at which the fertilizer to be financed from this loan is used, is the mix between urea and DAP. Afghanistan presently uses a ratio of 2:1, urea:DAP. However, tests indicate that in certain wheat areas a mix of 3:1 is more desirable; and in test conducted in the Kunduz region on cotton by "Compagnie Française pour la Développement des Textiles," urea alone generated excellent yields. After considering these findings and studying the availability of domestic urea in excess of current demand, the Ministry of Agriculture is expected ultimately to recommend the 3:1 ratio on both wheat and cotton. If the mix were to be immediately changed to 3:1, Afghanistan's 1975/76 DAP requirement would be reduced from 24,000 MT to 16,000 MT. Change, however, is slow in Afghanistan and we expect that 1975/76 sales will be generally at a 2:1 mix as projected. We do expect that the ratio will change in the future as more trials are held and response ratios are quantified.

5.04 Regarding the projected sales growth of 25 percent, others, including the IBRD, believe that Afghanistan lacks the infrastructure and supporting facilities to achieve much more than a moderate increase quickly. For example, the ABRD projects fertilizer sales to increase at a compound rate of only 12 percent per annum. Probably, the truth lies somewhere in between. We believe, however, that supplies should be adequate to allow for the higher projected increase; or, put another way, we are persuaded that if we plan supplies for the lower growth rate, the lower projection will be a self-fulfilling prophecy.

B. Fertilizer Prices

5.05 The present fertilizer prices, to the farmer, are well below cost

and contain a heavy government subsidy. In 1974/75 the subsidy is estimated to amount to \$2.9 million (see para 3.08). It will increase to about \$9.0 million (or 4 percent of Afghanistan's budget) in 1975/76, when the recently purchased high cost fertilizer is sold to farmers, and will reduce to about \$6.0 million in 1976/77 when locally produced urea is substituted for imported urea (see para 3.09).

5.06 In reality, the subsidy is really geared to the consumer, primarily the urban consumer. Assuming this is necessary, and desirable, Afghanistan could accomplish the same result by allowing the prices of agriculture inputs and commodities to rise, purchase the commodities at the market price, and release the commodities to consumers at a subsidized price. The advantages of this would be that farmers' incomes would rise which should act as an incentive to increase agriculture production. The disadvantages are that it would require a large bureaucracy to manage (which is a weak suit in Afghanistan) and it is unlikely that the distribution would be on an equitable basis. For this loan we are not recommending any conditions or covenants related specifically to the subsidy problem. The entire problem will be covered in the evaluation of AFC to be held during FY 1975/76. At that time, and depending on factors existing at that time, we intend to discuss the problem with the Government.

C. AFC Financial Condition

5.07 A victim of the present fertilizer subsidy is AFC since it is they who purchase the fertilizer at the full market price and sell it at the subsidized price. In a sense, this hides the subsidy in the budget since it is show as a contribution to AFC (or the GOA can instruct AFC to borrow from the banking system). This system also hides the efficiency, or inefficiency, of AFC since it is not possible to tell, without a detailed examination, if AFC is losing money through sales or by poor management, or a combination of both. And obviously it is not a morale booster for AFC employees who don't want to work for a company that is always losing money. Another result is that AFC will never have surplus funds to pay for extension, or educative work, to convince more farmers to use fertilizer.

5.08 Considering the foregoing problem we are including a covenant in the Loan Agreement which will require the Government to present a plan to AID, within one year after execution of the Loan Agreement, which will ensure that AFC is a financially viable institution.

D. Conditions and Covenants

5.09 The Conditions Precedent to Disbursement will be:

- (a) Legal opinion;
- (b) Designation of Borrowers Authorized representative; and
- (c) Such other conditions as AID may require.

5.10 To ensure that the fertilizer purchased under this loan is procured and distributed in a timely and efficient manner and that the insti-

tutional structure of AFC is retained in form and substance acceptable to AID, the following covenants will be incorporated into the Loan Agreement, unless AID and the borrower otherwise agree:

(a) The Borrower shall, within twelve months from the date of the Agreement, submit a plan, satisfactory to AID, that will ensure the financial viability of AFC including, but not limited to, a two-year budget and source and applications of funds statement.

(b) The Borrower shall cause AFC to operate as an independent business entity and will permit AFC to manage its own activities, including the purchase of fertilizer from both domestic and foreign sources, arrange for transportation of fertilizer both within and without Afghanistan, operate its warehouses, and distribute fertilizer procured under this loan or any other financing sources to retailers and farmers.

(c) The Borrower shall provide all funds in addition to the loan needed for the purchase and transportation of fertilizer to be financed hereunder and, to the extent that existing funds and sales revenues are insufficient, the operating costs of AFC.

(d) The Borrower shall assure that the Agriculture Development Bank shall remain a shareholder of AFC.

5.11 Additionally, we believe that Government should continue its efforts in addressing Agriculture Policy and related matters. We therefore will include the following covenants in the Loan Agreement. The Implementation Letter will specify the frequency and detail of the reports required to comply with the covenants:

(a) The Borrower shall initiate new research to determine the optimum ratio and amounts of phosphatic to nitrogenous fertilizer, by crops and soil conditions.

(b) The Borrower shall continue to evaluate the amount of fertilizer subsidy paid and, as warranted, adjust the sales price of fertilizers to reflect the farmers ability to purchase and use appropriate amounts of such fertilizers.

(c) The Borrower shall, in conjunction with (b) above, review existing farmer credit systems for financing fertilizer procurement, and take actions designed to assure that maximum fertilizer usage is attained.

(d) The Borrower shall, instruct AFC and the AgBank to accumulate data which will identify the purchaser of fertilizer including size and tenancy of farmland, crops grown, location and source of financing.

(e) The Borrower shall cause AFC to adequately provide for the proper storage and timely distribution of an increasing supply of fertilizer so as to facilitate the flow of fertilizer to the majority of the farming population.

VI. ENVIRONMENTAL IMPACT

6.01 Di-ammonium phosphate will be the principal fertilizer imported under this loan. Afghanistan has a land area of 63 million ha, of which about 9 million are cultivated. The application of fertilizer will increase the yields per acre, which are among the lowest in the world. Thus, the use of fertilizer will have a significant beneficial effect in helping Afghanistan increase food production.

6.02 The potential adverse effects of fertilizers occur when nitrates and phosphates are released into surface and ground waters. There are no adverse effects on the soil or air from the use of these fertilizers.

6.03 In surface waters, such as lakes and other standing bodies of water, nitrates and phosphates contribute to the overgrowth of algae and other objectionable plant forms. This is a serious problem in lakes that are used for recreational purposes. The few lakes that are used for recreation in Afghanistan do not receive a significant runoff from cultivated land and therefore the use of fertilizers, at present and in the foreseeable future, will have no adverse effect on these waters.

6.04 In a few parts of the world, groundwaters containing high concentrations of nitrate have caused hemoglobinemia in infants. The United States Drinking Water Standards have therefore set a nitrate limit of 10 milligrams per liter. Data are not available on the nitrate content of drinking water in Afghanistan, nor is there any evidence of the incidence of hemoglobinemia. This condition, if it exists, is unlikely to be aggravated by the small amounts of fertilizer normally applied in Pakistan and by the even smaller amounts that would enter the groundwater.

6.05 We conclude, therefore, that the beneficial effects of importing and using fertilizer far outweigh any potential and unproved environmental effects.

VII. DEBT SERVICE CAPABILITY

7.01 As of March 1974 the GOA's foreign debt totaled \$719.9 million. the major creditors were the USSR (73.4 percent), the U.S. (12.4 percent) and the Federal Republic of Germany (9 percent).

7.02 Afghanistan export earnings have risen at better than 20 percent per annum during the past two years. Exports of fruits and nuts, which account for about 36 percent of total export earnings, are expected to continue to increase. Foreign exchange reserves (presently covering six months of imports) have been rising the past four years but are expected to drop this coming year mainly because of a drop in prices of cotton and karakul.

7.03 Over the past two years improved weather conditions and increased usage of agricultural inputs have resulted in a good wheat harvest, with 1973 and 1974 producing an overall surplus. With continued increase in agricultural inputs such as improved seed and fertilizer and GOA leadership interest in increasing irrigated agriculture, there is reason to believe agricultural production will continue to improve over the coming years.

7.04 Other positive signs in the economy are improved policies in some areas of agriculture including efforts to increase the use of fertilizer throughout the country, and the GOP efforts to promote, exports particularly to new markets in the oil rich countries such as Iran. The GOA is also making progress in increasing domestic revenues (31 percent increase over last year's collection) primarily through more strict enforcement of existing laws.

7.05 The performance of the past two years, and relatively good prospects for continued development, have given grounds for international agencies and bilateral donors (Iran) to provide concessional loans. There are reasonable prospects of this loan being within Afghanistan's ability to repay in the future.

ANNEX 1

AFGHANISTAN - AGRICULTURAL INPUTS LOAN

Capital Assistance Loan Authorization

Provided from: Development Loan Funds FAA 103
(Food and Nutrition)

Pursuant to the authority vested in the Administrator, Agency for International Development ("A.I.D.") by the Foreign Assistance Act of 1961, as amended, ("The Act") and the delegations of authority issued thereunder, I hereby authorize the establishment of a loan ("The Loan") pursuant to Part I, Chapter 1, Section 103, Food and Nutrition, and Part I, Chapter 2, Title 1, the Development Loan Fund, of said Act, to The Republic of Afghanistan ("The Government") of not to exceed Eight Million United States Dollars (\$8,000,000) to assist in financing the United States dollar costs of procuring fertilizers. This loan will be subject to the following terms and conditions:

1. Terms of Repayment and Interest Rate

The Government shall repay the Loan to A.I.D. in United States dollars, within forty (40) years from the date of the first disbursement under the Loan, including a grace period of not to exceed ten (10) years from said date. The Government shall pay to A.I.D. in United States dollars interest at the rate of two percent (2%) per annum during the grace period and three percent (3%) per annum thereafter on the outstanding disbursed balance of the Loan and any due unpaid interest.

2. Other Terms and Conditions

- a) Unless A.I.D. otherwise agrees in writing, commodities and related services financed under the Loan shall have their source and origin in the United States and countries included in A.I.D. Geographic Code 941.
- b) The Loan shall be subject to such other terms and conditions as A.I.D. may deem advisable.

Assistant Administrator for
Near East South Asia Bureau

Date

Ministry of Foreign Affairs

Note No. 8684/ 10989

Date: 20/11/53

Feb. 9, 1975

TO: Amembassy, Kabul

Presenting compliments, the Foreign Ministry note states:

"Enclosed please find Planning Minister's note dated Feb. 5th addressed to Mr. Brown, USAID Director in Kabul, requesting finance of the cost and transportation charges of 20,000 tons of diammonium phosphate.

Please forward the note to USAID office in Kabul, and inform us of the decision made by the relevant authorities of the friendly country.

Ministry of Foreign Affairs avails itself of this opportunity to renew the assurance of its highest consideration."

R. C. Mehra

MINISTRY OF PLANNING
SECRETARIAT

NO: _____
Date: Feb. 5, 1975
Ret: _____

REPUBLIC OF AFGHANISTAN
KABUL

Mr. Vincent W. Brown
Director
USAID
Kabul.

Dear Mr. Brown,

In recent years the use of chemical fertilizers in comparatively large volumes together with improved wheat seed has played a major role in increased food production and the results are very promising. The program of increased grain production has first priority with us. We have been relatively successful in implementing this program with the use of fertilizers and improved seeds and it is felt necessary to continue it.

Of the three major plant nutrients (N, P and K) nitrogen (N) is universally low in Afghan soils and it is proportionately the most limiting factor in food production. Phosphorus (P) is the next most limiting plant nutrient. While the role of potassium (K) in improving yield and crop quality has been established in sugar and starch producing plants, other crops seem to respond only marginally to applications of potash fertilizers necessitating further research.

There is some evidence that when phosphorus is added to medium and higher applications rates of nitrogen (according to the existing Extension Department recommendations) the extra yield due to application of phosphorus is quite high -- up to a ratio of 7 - 8 to 1. At a subsidized farmer price of afs. 9840/MT for diammonium phosphate (DAP), the purchase and application of DAP to moderate and higher application rates of Urea gives farmers, on the average, attractive

-2-

returns and consequently gives attractive returns to our economy as a whole when output is valued at world farm gate prices (for wheat this would be \$1200 \$150/MT). The role of phosphorus in substantially increasing yields of cotton, sugar beets and rice is also worth mentioning.

Based on ROA fundamental plans studies are underway to seek ways and means to reach and help the farmers who constitute the majority of our population. Some steps toward reaching this objective have already been taken. Expansion of AFC retail outlets to 400 in 1354, simplifying Af. Bank loan conditions to increase greater small farmer participation in fertilizer and seed credit programs, expansion of promotional programs to familiarize farmers with fertilizer use and passage of Cooperative Law are cited as good examples.

The current stock of urea in country plus the expected production of urea by the Mazar Plant will be more than enough to provide domestic nitrogen requirement for the year 1354. Future requirements of urea beyond 1354 will also be provided by the Mazar Plant facilities. The country's stock of DAP, however, will be exhausted after the fall of 1354 fertilizer campaign and hence it will be necessary to have new procurements.

The DAP requirement for the year 1355 which should be purchased in mid. 1354 is estimated to be about 33,000 MT. In order to partially satisfy the phosphorus requirement for 1353 the Government of the Republic of Afghanistan while presenting its compliments to the Government of the United States would like to formally request the consideration and provision of a loan to finance the importation of up to 20,000 MT of DAP (or an equivalent amount of TSP) plus shipping and Marine insurance charges to Karachi under the AID's most favorable concessionary terms. In order to strengthen AFC's financial status it will be greatly appreciated if a grant is also considered to finance forwarding and transportation charges from Karachi to Afghanistan borders.

-3-

Thanking you for your continued interest in our problems and timely assistance, I remain,

Sincerely,

Ali Ahmad Khoram
Minister of Planning

MINISTRY OF PLANNING
12 June 1975
No. 425

ANNEX 2
Page 5

REPUBLIC OF AFGHANISTAN
KABUL

Mr. Vincent W. Brown
Director,
USAID Mission for Afghanistan
Kabul

Dear Mr. Brown,

In my letter to you of February 5, 1975 we requested that U.S. Government consider providing the Government of Afghanistan a loan to finance the importation of up to 20,000 MT of D.A.P. (or an equivalent of amount T.S.P.) plus the usual shipping and marine insurance charges associated with such procurements.

We now understand that in current prices alone in the amount of \$8 million will enable us to purchase approximately 24,000 MT of D.A.P. against our 33,000 MT total estimated requirement for the year 1355. Accordingly we hereby request that your Government consider providing the GOA a loan of up to \$8 million which will be used to finance items mentioned above. We also wish to renew the request for the grant to finance forwarding inland transportation charges referred to in my earlier letter.

Thanking you for your continued interest in our problems and timely assistance, I remain,

Sincerely Yours,

ALI AHMAD KHORAM
MINISTER OF PLANNING

UNITED STATES OF AMERICA
AGENCY FOR INTERNATIONAL DEVELOPMENT

ANNEX 3

KABUL, AFGHANISTAN

هيئة انكشاف بين المللي اضلاع معجده امريكا
كابل افغانستان

OFFICE OF THE DIRECTOR

دفتر رئيس

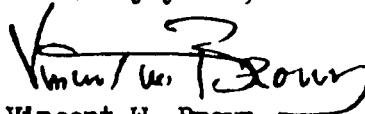
Mr. Robert H. Nooter
Assistant Administrator
Bureau for NESA
Agency for International Development
Washington, D.C. 20523

Dear Mr. Nooter:

As principal officer of the Agency for International Development in Afghanistan, it is my responsibility under Section 611(e) of the Foreign Assistance Act of 1961 as amended to certify as to the financial and human resource capability of Afghanistan to effectively maintain and utilize capital assistance projects estimated to cost in excess of \$1,000,000, taking into account among other things the maintenance and utilization of projects in such country previously financed or assisted by the United States.

Based on the structure and staffing of the Afghan Fertilizer Company (Government of Afghanistan Fertilizer Authority), its experience in procurement, warehousing and distribution of fertilizer, I hereby certify that Afghanistan has the capability effectively to utilize the fertilizer to be financed by the proposed \$8.0 million loan to the Government of Afghanistan.

Sincerely yours,



Vincent W. Brown
Director

UNITED STATES OF AMERICA
AGENCY FOR INTERNATIONAL DEVELOPMENT ANNEX 4

KABUL, AFGHANISTAN

هيئة انكشاف بين المللي اضلاع مسعده امريكا
كابل افغانستان

OFFICE OF THE DIRECTOR

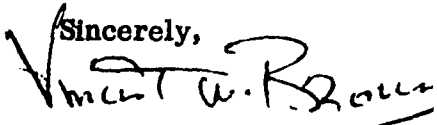
دھر ریس

Mr. Robert H. Nooter
Assistant Administrator
Bureau for NESA
Agency for International Development
Washington, D. C. 20523

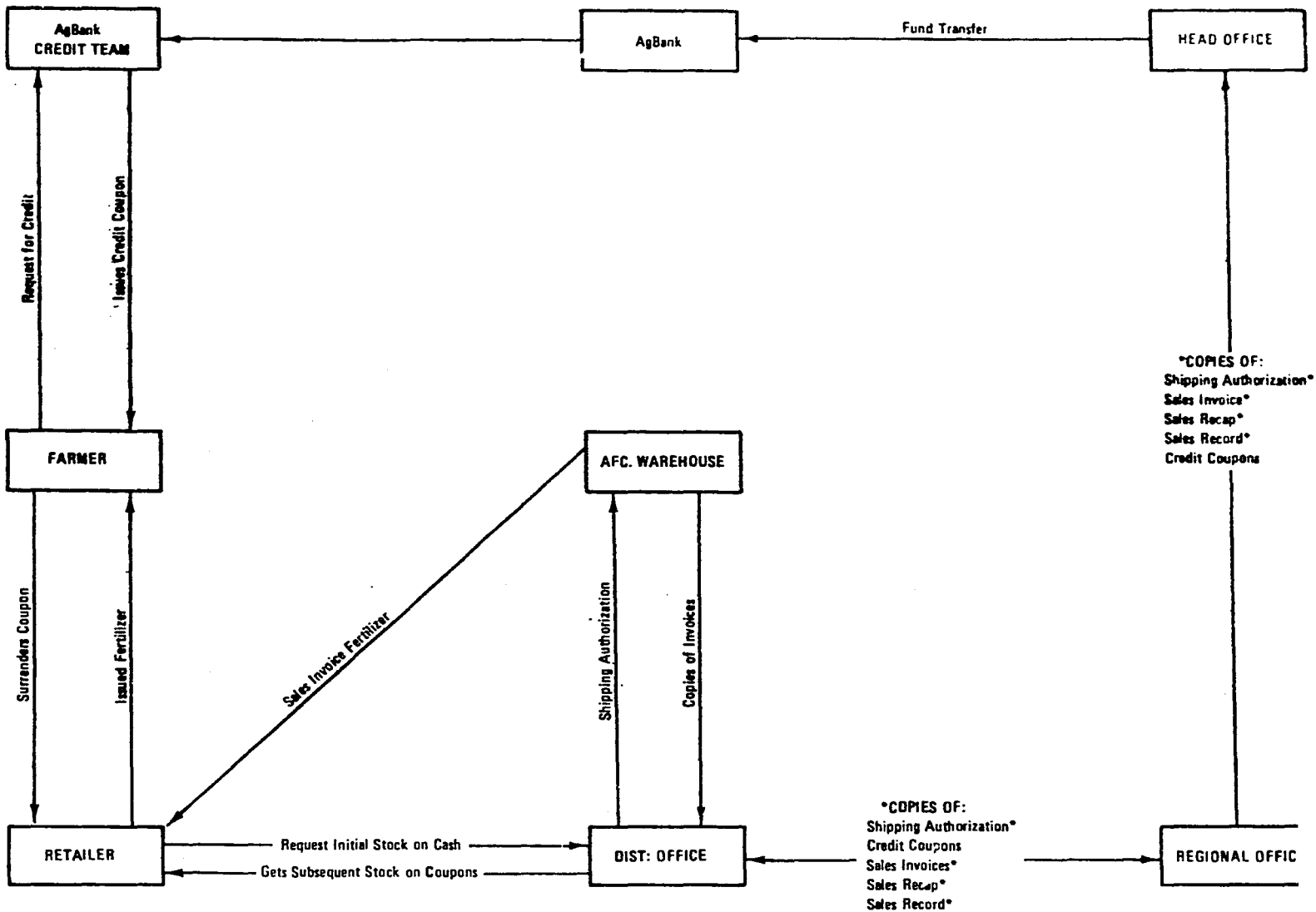
Dear Mr. Nooter:

As principal officer of the Agency for International Development in Afghanistan, it is my responsibility under Section 110 (a); 208 (e) of the Foreign Assistance Act of 1961 as amended, to certify that the Government of Afghanistan is prepared to provide at least twenty-five percent (25%) of the costs of the program, project or activity with respect to which the Loan is made.

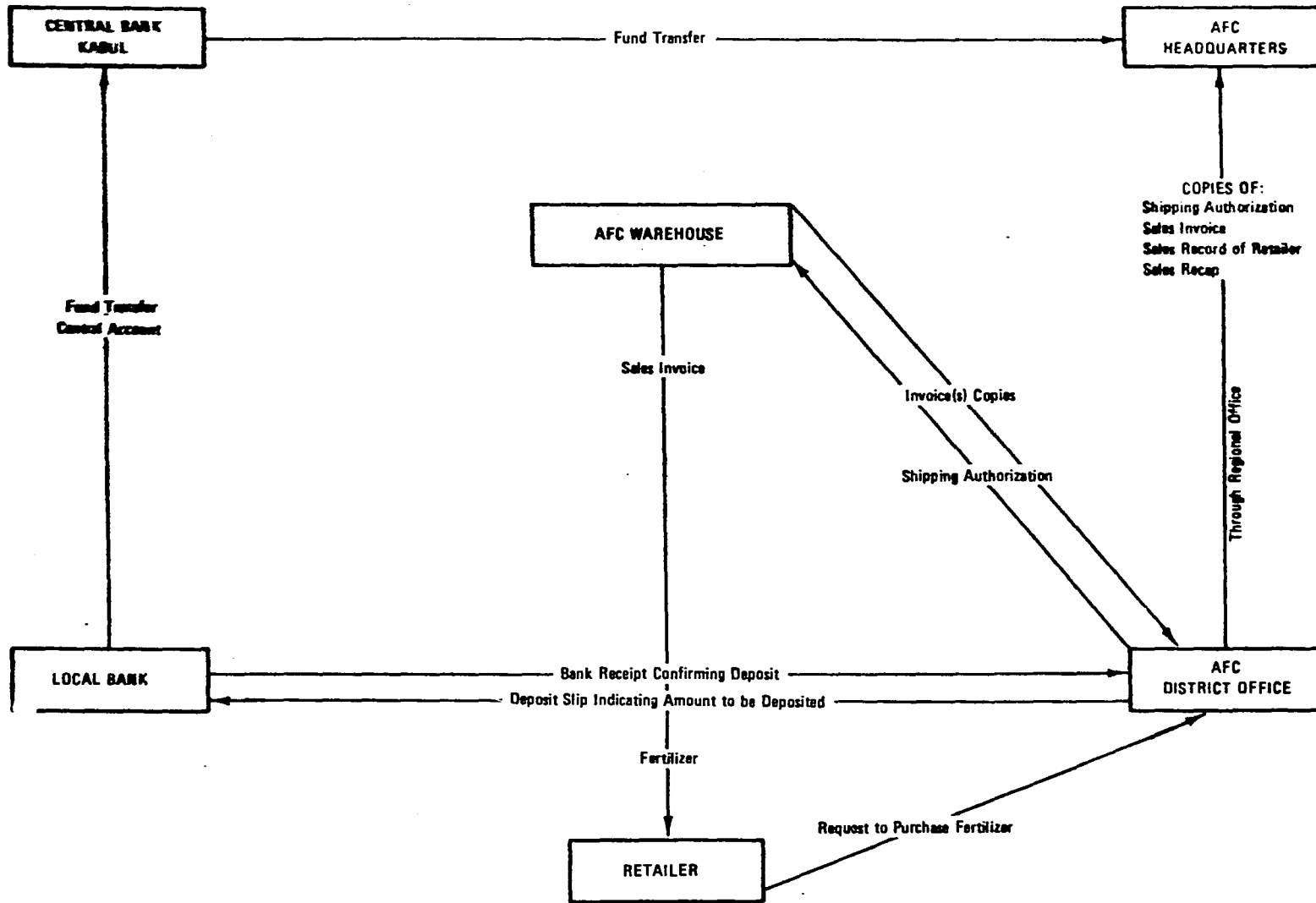
Based on verbal assurance from the Government of Afghanistan and verified by financial documentation supplied by the Afghan Fertilizer Company, it is apparent that the host country will have a large investment in the total project. During the three years of this project, the Government of Afghanistan and its sole agent the Afghan Fertilizer Company, will spend about \$18.0 million for fertilizer from its government operated Mazar-i-Sharif plant, \$6.0 million for distribution and credit costs and \$9.0 million to increase the availability of credit to farmers, for a total of about \$33.0 million. Based on this information, I hereby certify that more than twenty-five percent (25%) of the costs of the program to which this loan contributes will be met by the Government of Afghanistan.

Sincerely,

Vincent W. Brown
Director

APPRAISAL OF
 A SECOND AGRICULTURAL CREDIT PROJECT
 AFGHANISTAN
 AFGHANISTAN FERTILIZER COMPANY
 Fertilizer Sales on Credit
 Flow of Information, Funds, and Fertilizer



APPRAISAL OF
 A SECOND AGRICULTURAL CREDIT PROJECT
 AFGHANISTAN
 AFGHANISTAN FERTILIZER COMPANY
 Fertilizer Sales on Cash
 Flow of Information, Funds and Fertilizer



PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK

ANNEX 7

Page 1 of 2

Life of Project: 1975-1977
 Start Date: 1975
 Total US Funds: \$8.0 million
 Date Prepared: 6/1/75

Project Title & Number: AFGHANISTAN: Agriculture Inputs

*Grant assistance of \$366,000 previously auth. (306-11-199-143)

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
<p>Program or Sector Goal: The broader objective to which this project contributes:</p> <p><u>Sector Goal</u> Increase in production of principal agriculture crops through an accelerated use of fertilizer.</p> <p><u>Project Goal</u> A greater number of farmers using a greater amount of fertilizer</p>	<p>Measures of Goal Achievement:</p> <ul style="list-style-type: none"> -Annual agriculture production increases of 10% for wheat, 8% for cotton and 6% for sugar cane. -No wheat imports during years of normal weather. -Increase in fertilizer sales by 25% a year. -a 20% increase in number of farmers using fertilizer. 	<ul style="list-style-type: none"> - Ministry of Agriculture annual reports. - Food Procurement Departments annual reports. - AFC monthly reports. 	<p>Assumptions for achieving goal targets:</p> <ul style="list-style-type: none"> -There will not be a draught lasting two years or more. -Levels of precipitation are not less than 75%. -No disease or insect epidemic develops which reduces yields more than 5% below current yields.
<p>Project Purpose:</p> <p><u>GOA Project Purpose</u> Availability of fertilizer in all principal agriculture producing areas.</p> <p><u>AID Sub-Purpose</u> An effective organization for marketing and distributing fertilizer staffed by competent Afghanistan nationals.</p>	<p>Conditions that will indicate purpose has been achieved: End of project status.</p> <ul style="list-style-type: none"> -Warehouses are located in all principal agriculture producing areas. -Retail agents have increased from 220 to 400. -Adequate supplies of fertilizer exist at all warehouse and retail points. -Targets for distribution are met. -Distribution area has enlarged. -Afghanistan nationals in all key positions & have operated company effectively for one full year. 	<ul style="list-style-type: none"> - AFC monthly reports. - Intensive evaluation of AFC during the winter of 1975-76. - Continuous AID monitoring. 	<p>Assumptions for achieving purpose:</p> <ul style="list-style-type: none"> -Supplies of fertilizer, both imported and domestically produced are adequate to meet demand. -No bottlenecks occur in distribution system. -Warehouses are constructed. -Additional retail outlets established. -Management assistance, over past two years, has been effective.
<p>Outputs:</p> <p><u>AID</u></p> <ol style="list-style-type: none"> 1. Chemical fertilizers. 2. An efficient company, properly staffed for the marketing and distribution of chemical fertilizers. 3. Four trained middle-level managers. 4. New retail agents established to sell fertilizer. 	<p>Magnitude of Outputs:</p> <ol style="list-style-type: none"> 1. Approximately 24,000 MT of DAP. 2. One company. 3. Four employees. 4. Increase from 220 to 400 retailers. 	<ul style="list-style-type: none"> - AID and AFC reports. - Intensive evaluation of AFC. - AgBank quarterly reports. - AFC and AgBank audited financial statements. - IBRD evaluation of AgBank. 	<p>Assumptions for achieving outputs:</p> <ul style="list-style-type: none"> -IBRD loan is effective by August -GOA continuous to support AFC.
<p>Inputs:</p> <p><u>AID</u></p> <ol style="list-style-type: none"> 1. A dollar loan of \$8.0 million to be used to purchase chemical fertilizer. 2. Four man years of technical assistance 3. Participant training of four middle level managers. 	<p>Implementation Target (Type and Quantity)</p> <p><u>AID</u></p> <ol style="list-style-type: none"> 1. Fertilizer to be purchased in the late summer & early fall of 1975. 2. Initially for one year (CY 1975) with the provision of an extension 3. During calendar year 1975. 	<ul style="list-style-type: none"> - AID records. - AFC reports. - AgBank reports. - GOA fiscal data. 	<p>Assumptions for providing inputs:</p> <ul style="list-style-type: none"> -Necessary resources made available by AID, GOP and IBRD. -AgBank increases its effectiveness through technical assistance. -AFC can handle contracting and supervision of warehouse construction.

**PROJECT DESIGN SUMMARY
LOGICAL FRAMEWORK**

ANNEX 7

Page 2 of 2

Life of Project

From FY 1976 to FY 1

Total U.S. Funding \$8.0 million

Date Prepared 6/1/75

Project Title & Number: AFGHANISTAN: Agriculture Inputs (continued)

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
<p>Program or Sector Goal: The broader objective to which this project contributes:</p>	<p>Measures of Goal Achievement:</p>		<p>Assumptions for achieving goal target:</p> <ul style="list-style-type: none"> - Fertilizer/product relationship continues to be favorable. - Fertilizer is available in adequate quantities. - Credit constraint is reduced
<p>Project Purpose:</p>	<p>Conditions that will indicate purpose has been achieved: End of project status.</p>		<p>Assumptions for achieving purpose:</p>
<p>Outputs:</p> <p><u>GOA</u></p> <ol style="list-style-type: none"> 1. Adequate urea fertilizer to meet demand. 2. Adequate funds to ensure AFC and AgBank purposes are met. <p><u>IBRD</u></p> <ol style="list-style-type: none"> 1. A larger number of farmers purchasing fertilizer on credit. 2. An efficient, properly staffed Ag. Credit Bank. 3. Adequate warehouse facilities in new locations. 	<p>Magnitude of Outputs:</p> <ol style="list-style-type: none"> 1. 33,000 MT in FY 1976 and 75,000 MT in FY 1977. 2. Unknown at this time; magnitude depends on internal events (e.g. loan collections) which will occur next two years. <ol style="list-style-type: none"> 1. An increase from 33,000 to 43,000 farmers. 2. One bank with branches. 3. 55,000 MT in 24 locations. 		<p>Assumptions for achieving outputs:</p>
<p>Inputs:</p> <p><u>GOA</u></p> <ol style="list-style-type: none"> 1. Supply of fertilizer from the Russian-assisted urea fertilizer plant. 2. Budgetary support of AFC and AgBank. <p><u>IBRD</u></p> <ol style="list-style-type: none"> 1. Credit to farmers for purchase of fertilizer. 2. Technical assistance to AgBank. 3. Loan to AFC (through AgBank) for warehouse construction. 	<p>Implementation Target (Type and Quantity)</p> <p><u>GOA</u></p> <ol style="list-style-type: none"> 1. Continuous from 1975. 2. Continuous. <p><u>IBRD</u></p> <ol style="list-style-type: none"> 1. Over a 3½ year period commencing July 1975. 2. Through August 1978. 		<p>Assumptions for providing inputs:</p>

CHECKLIST OF STATUTORY CRITERIA

The following abbreviations are used:

FAA - Foreign Assistance Act of 1961, as amended.

FAA, 1973 - Foreign Assistance Act of 1973.

App. - Foreign Assistance and Related Programs Appropriation Act, 1974.

MMA - Merchant Marine Act of 1936, as amended.

BASIC AUTHORITY

1. FAA § 103; § 104; § 105;
§ 106; § 107. Is loan being made

- | | |
|--|--|
| a. for agriculture, rural development or nutrition; | Yes. The loan is being made to help Afghanistan improve agriculture, rural development and nutrition by financing fertilizer. It will contribute directly to increasing food grain yields. |
| b. for population planning or health; | No. |
| c. for education, public administration, or human resources development; | No. |
| d. to solve economic and social development problems in fields such as transportation, power, industry, urban development, and export development; | No. |
| e. in support of the general economy of the recipient country or for development programs conducted by private or international organizations. | No. |

COUNTRY PERFORMANCE

Progress Towards Country Goals

2. FAA §201 (b) (5), (7) & (8); § 208

A. Describe extent to which country is:

- | | |
|-----------------------------------|------------------------------------|
| (1) Making appropriate efforts to | (1) Rapid increase in agricultural |
|-----------------------------------|------------------------------------|

increase food production and improve means for food storage and distribution.

production is a top priority of the Afghan Government. This includes the introduction, extension and production of improved varieties of wheat and fertilizers in an effort to make the country self-sufficient in foodgrains. These efforts, coupled with favorable weather, led to a substantial increase in wheat production in 1973/74 after two years of serious shortage. With U.S. assistance, the GOA has been seeking to improve its fertilizer distribution system and fertilizer usage has steadily increased. The GOA has also utilized assistance of the U.S., the FRG and other donors in analyzing methods for supporting wheat stabilization programs and in increasing and improving good storage and distribution.

(2) Creating a favorable climate for foreign and domestic private enterprise and investment.

(2) Since the mid-1960's the development policy of Afghanistan has envisioned a mixed economy. Within this framework, the GOA has indicated that it allocates a significant role to private investment, particularly for small and medium enterprises. A Foreign and Domestic Private Investment Law, promulgated in 1967, has provided incentives to private investment and led to approval of over 350 small industries and the start-up of over 100 manufacturing operations in the past five years. A revised Investment Law has been promulgated in August 1974 with further incentives to private enterprise and investment.

(3) Increasing the public's role in the developmental process.

(3) The GOA has accorded high priority to the implementation of rural development programs designed to maximize benefits to the poorest segments of society and to utilize self-help efforts at the local level to the

greatest possible extent. Many small rural works projects, including feeder roads, bridges and irrigation ditches were constructed over the past few years and are actively under construction now. Broad popular participation in development has been enunciated as a basic goal.

(4) (a) Allocating available budgetary resources to development.

Afghanistan's budgetary resources are committed to social and economic development.

(b) Diverting such resources for unnecessary military expenditure (See also Item No. 20) and intervention in affairs of other free and independent nations.) (See also Item No. 11)

Afghan arms acquisition is motivated by desire for defensive capability and internal security. The Government professes no offensive intentions and has not carried out any such intentions.

(5) Making economic, social, and political reforms such as tax collection improvements and changes in land tenure arrangements, and making progress toward respect for the rule of law, freedom of expression and of the press, and recognizing the importance of individual freedom, initiative, and private enterprise.

(5) The creation of a Cadastral Survey Organization with earlier USAID assistance was designed to create the base for an agricultural tax. Concentration of land ownership and an extensive share-cropping pattern suggest that some form of land reform is desirable but there is no indication that such reform is presently contemplated by the Government. USAID is assisting in the improvement, standardization and rationalization of the tax collection system. At present freedom of the press is somewhat limited. As noted in paragraph (b) above, GOA policy envisions a significant role for private enterprise.

(6) Willing to contribute funds to the project of program.

(6) Afghanistan will provide the local currency resources required for implementation of the loan. The Government of Afghanistan will pay for all local distribution costs as well as providing approximately two-thirds of the country's fertilizer needs from its own plant. See also IV.F. of the Project Paper.

(7) Otherwise responding to the vital economic, political, and social concerns of its people, and demonstrating a clear determination to take effective self-help measures.

The Government of Afghanistan is responding to the vital economic, political and social concerns of its people. It has a firm determination to come to grips with the economic problems of the country.

B. Are above factors taken into account in the furnishing of the subject assistance?

B. Yes.

Treatment of U.S. Citizens and firms.

3. FAA § 620(c). If assistance is to a government, is the government liable as debtor or unconditional guarantor on any debt to a U.S. citizen for goods or services furnished or ordered where (a) such citizen has exhausted available legal remedies and (b) debt is not denied or contested by such government?

3. Afghanistan is not known to be in violation of this section.

4. FAA § 620(e) (1). If assistance is to a government, has it (including government agencies or subdivisions) taken any action which has the effect or nationalizing, expropriating, or otherwise seizing ownership or control of property of U.S. citizens or entities beneficially owned by them without taking steps to discharge its obligations toward such citizens or entities?

4. Afghanistan is not known to be in violation of this section.

5. FAA § 620(o); Fisherman's Protective Act § 5. If country has seized, or imposed any penalty or sanction against, any U.S. fishing vessel on account of its fishing activities in international waters,

5. Afghanistan has not taken such action.

a. has any deduction required by Fishermen's Protective Act been made?

b. has complete denial of assistance been considered by A.I.D. Administrator?

Relations with U.S. Government and Other Nations

- | | |
|--|---|
| 6. <u>FAA § 620(a)</u> . Does recipient country furnish assistance to Cuba or fail to take appropriate steps to prevent ships or aircraft under its flag from carrying cargoes to or from Cuba. | 6. We are not aware of any GOA non-compliance with this section. |
| 7. <u>FAA § 620(b)</u> . If assistance is to a government, has the Secretary of State determined that it is not controlled by the international Communist movement? | 7. The Secretary of State has determined that Afghanistan is not dominated or controlled by the international Communist movement. |
| 8. <u>FAA § 620(d)</u> . If assistance is for any productive enterprise which will compete in the United States with United States enterprise, is there an agreement by the recipient country to prevent export to the United States of more than 20% of the enterprise's annual production during the life of the loan? | 8. Not applicable. |
| 9. <u>FAA § 620(f)</u> . Is recipient country a Communist country? | 9. No. |
| 10. <u>FAA § 620(i)</u> . Is recipient country in any way involved in (a) subversion of, or military aggression against, the United States or any country receiving U.S. assistance, or (b) the planning of such subversion or aggression? | 10. No. |
| 11. <u>FAA § 620(j)</u> . Has the country permitted, or failed to take adequate measures to prevent, the damage or destruction, by mob action, of U.S. property? | 11. No. |
| 12. <u>FAA § 620(l)</u> . If the country has failed to institute the investment guaranty program for the specific risks of expropriation, in convertibility or confiscation, has the the A.I.D. administration within the past year considered denying assistance to such government for this reason? | 12. Afghanistan has instituted the investment guaranty program for the specific risks of expropriation, inconvertibility and war risks. |

13. FAA § 620(n). Does recipient country furnish goods to North Viet-Nam or permit ships or aircraft under its flag to carry cargoes to or from North Viet-Nam? 13. We are unaware of any GOA non-compliance with this section.
14. FAA § 620(q). Is the government of the recipient country in default on interest or principal of any A.I.D. loan to the country? 14. No.
15. FAA § 620(t). Has the country severed diplomatic relations with the United States? If so, have they been resumed and have new bilateral assistance agreements been negotiated and entered into since such resumption? 15. Afghanistan has not severed diplomatic relations with the United States.
16. FAA § 620(u). What is the payment status of the country's U.N. obligations? If the country is in arrears, were such arrearages taken into account by the A.I.D. Administrator in determining the current A.I.D. Operational Year Budget? 16. Afghanistan is not delinquent in any obligations to the United Nations.
17. FAA § 481. Has the government of recipient country failed to take adequate steps to prevent narcotic drugs and other controlled substances (as defined by the Comprehensive Drug Abuse Prevention and Control Act of 1970) produced or processed, in whole or in part, in such country, or transported through such country, from being sold illegally within the jurisdiction of such country to U.S. Government personnel or their dependents, or from entering the U.S. unlawfully? 17. No.
18. FAA § 659. If (a) military base is located in recipient country, and was constructed or is being maintained or operated with funds furnished by U.S., and (b) U.S. personnel carry out military operations from such base, has the President determined that the government of recipient country has authorized regular access to U.S. correspondents to such base? 18. There is no U.S. military base in Afghanistan.

Military Expenditures

19. FAA § 620(s). What percentage of country budget is for military expenditures? How much of foreign exchange resources spent on military equipment? How much spent for the purchase of sophisticated weapons systems? (Consideration of these points is to be coordinated with the Bureau for Program and Policy Coordination, Regional Coordinators and Military Assistance Staff (PPC/RC).)
19. Afghanistan's military budget appears to be about 30% of the total budget. The Soviet Union and other Eastern bloc countries are the principal suppliers of military equipment for the Afghan armed forces. This equipment is purchased on longterm credits at below "market prices". Some surface-to-air missiles, Mid 60's fighter bombers and guided anti-tank missiles are considered the sophisticated components of the Afghan military system. These weapons are available in limited quantities. Afghanistan is not known to be diverting development assistance to military expenditures. The Afghan military both air force and army, totals 84,000 men on active duty. The size of this force and its equipment are considered consistent with the country's defense and internal security needs.

CONDITIONS OF THE LOAN

General Soundness

20. FAA § 201(d). Information and conclusion on reasonableness and legality (under laws of country and the United States) of lending and relending terms of the loan.
20. The rate of interest is considered reasonable, and repayment of the loan with interest is within the financial capability of the borrower. Interest through the grace period will be at the rate of 2% per annum, and 3% thereafter. This rate is not higher than the applicable legal rate of interest in Afghanistan.
21. FAA § 201(b)(2); § 201(e). Information and conclusion on activity's economic and technical soundness. If loan is not made pursuant to a multilateral plan and the amount of the loan exceeds \$100,000, has country submitted to A.I.D. an application for such funds together with assurances to indicate that funds will be used in an economically and technically sound manner?
21. Yes, see Annex 2 of the Project Paper.

22. FAA § 201(b)(2). Information and conclusion on capacity of the country to repay the loan, including reasonableness of repayment prospects. 22. See sections III and V of the Project Paper.
23. FAA § 201(b)(1). Information and conclusion on availability of financing from other free-world sources, including private sources within the United States. 23. No other free-world sources, including private sources within the U.S., have indicated an interest in financing the loan.
24. FAA § 611(a)(1). Prior to signing of loan will there be (a) engineering, financial, and other plans necessary to carry out the assistance and (b) a reasonably firm estimate of the cost to the United States of the assistance? 24. (a) Financial and other plans necessary to carry out the assistance are completed (b) the cost of the assistance to the United States is limited to the amount of the loan.
25. FAA § 611(a)(2). If further legislative action is required within recipient country, what is basis for reasonable expectation that such action will be completed in time to permit orderly accomplishment of the purpose of the loan? 25. Further legislative action is not needed.
26. FAA § 611(e). If loan is for Capital Assistance, and all U.S. assistance to project now exceeds \$1 million, has Mission Director certified the country's capability effectively to maintain and utilize the project? 26. Yes. See Annex 4. of the Project Paper.

Loan's Relationship to Achievement of Country and Regional Goals

27. FAA § 207; § 113. Extent to which assistance reflects appropriate emphasis on: (a) encouraging development of democratic, economic, political and social institutions; (b) self-help in meeting the country's food needs; (c) improving availability of trained manpower in the country; (d) programs designed to meet the country's health needs; (e) other important areas of economic, political, and social development, including industry; free labor unions, cooperatives, and Voluntary Agencies; transportation and communication; planning and public administration; urban development, and modernization of existing laws; or (f) integrating women into the recipient country's national economy. 27. The loan has the indirect effect of encouraging institutional development for the distribution of agricultural inputs and rural development and contributes directly towards meeting Afghanistan's foodgrain needs. Furthermore, the AFC, as the sole fertilizer procurement and distribution agency of the GOA, was previously A.I.D. loan assisted and is now A.I.D. grant assisted in building its institutional capability. The loan has no direct impact on integrating women into the economy.

28. FAA § 209. Is project susceptible of execution as part of regional project? If so, why is project not so executed?
28. The loan is not directed at a regional problem. The U.S. is only one among a number of donors in Afghanistan. The Soviet Union, Germany, France, Peoples Republic of China, England, the United Nations, the World Bank, Asian Development Bank, and various voluntary agencies are important foreign assistance donors to Afghanistan.
29. FAA § 201(b)(4). Information and conclusion on activity's relationship to, and consistency with, other development activities, and its contribution to reliable long-range objectives.
29. The proposed loan would contribute to the development of the agriculture sector of the economy, a prime economic development objective of Afghanistan. It closely complements other developmental efforts underway in Afghanistan with U.S. and other donor assistance.
30. FAA § 201(b)(9). Information and conclusion on whether or not the activity to be financed will contribute to the achievement of self-sustaining growth.
30. Self-sufficiency in grain production is a major goal of Afghanistan and this project will definitely contribute toward the development of Afghanistan's rural economy and increased food production.
31. FAA § 209. Information and conclusion whether assistance will encourage regional development programs.
31. See above paragraph 28.
32. FAA § Section 111. Discuss the extent to which the loan will strengthen the participation of the urban and rural poor in their country's development, and will assist in the development of cooperatives which will enable and encourage greater numbers of poor people to help themselves toward a better life.
32. The institution of a farmers credit program for fertilizer procurement will enable and encourage a greater number of rural poor farmers to increase foodgrain yields and help themselves towards a better life.
33. FAA § 201(f). If this is a project loan, describe how such project will promote the country's economic development taking into account the country's human and material resource requirements and the relationship between ultimate objectives of the project and overall economic development
33. Incurred agricultural production is essential to Afghanistan's economic development. In order to increase production and good grain-yield per acre, increased quantities and timely availabilities of agricultural inputs such as fertilizer are required.

34. FAA § 281(a). Describe extent to which the loan will contribute to the objective of assuring maximum participation in the task of economic development on the part of the people of the country, through the encouragement of democratic, private, and local governmental institutions.
- 34.- Agricultural inputs are required for implementation of Afghanistan's agricultural and rural development strategy, since they facilitate obtaining increased food yields. Without adequate food levels participation of the rural population in democratic, private and local governmental institutions would be severely affected.
35. FAA § 281(b). Describe extent to which program recognizes the particular needs, desires, and capacities of the people of the country; utilizes the country's intellectual resources to encourage institutional development; and supports civic education and training in skills required for effective participation in governmental and political processes essential to self-government.
35. The loan recognizes the needs of the rural population and the desire for increased food production and incomes for producers, and their capacity to effectively utilize these inputs to achieve production and income goals. There is no direct effect on the use of the country's intellectual resources or on civic education and training in skills needed for increased civic participation.
36. FAA § 201(b)(3). In what ways does the activity give reasonable promise of contributing to the development of economic resources, or to the increase of productive capacities?
36. The application of fertilizer is designed to contribute to the maximum extent to the long-range economic development of Afghanistan.
37. FAA § 601(a). Information and conclusions whether loan will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition (c) encourage development and use of cooperatives, credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture, and commerce; and (f) strengthen free labor unions.
37. (a) in the first instance, trade would take place between the U.S. and Afghanistan since most purchases financed from the loan would have their source and origin in the U.S. In the longer term, the project may facilitate international trade by encouraging the import of other fertilizers and related agricultural inputs.
- (b) Increased private farm activity will be directly encouraged.
- (c) The loan will have no direct effect on the development and use of cooperatives, credit unions and savings and loan associations.
- (d) The loan would have no measurable effect on monopolistic practices.
- (e) Technical efficiency will be greatly improved through the existence of a reliable source of fertilizer.

(f) The loan will have no direct effect on the strengthening of free labor unions.

38. FAA § 619. If assistance is for newly independent country; is it furnished through multilateral organizations or plans to the maximum extent appropriate?

38. Not applicable.

Loan's Effect on U.S. and A.I.D. Program

39. FAA § 201(b)(6). Information and conclusion on possible effects of loan on U.S. economy, with special reference to areas of substantial labor surplus, and extent to which U.S. commodities and assistance are furnished in a manner consistent with improving the U.S. balance of payments position.

39. It is expected that most of the fertilizer will be purchased in the United States. Little, if any, adverse effect on the U.S. balance of payments is anticipated. No particular benefit to areas of labor surplus is anticipated. See also Section IV.D.

40. FAA § 202(a). Total amount of money under loan which is going directly to private enterprise, is going to intermediate credit institutions or other borrowers for use by private enterprise, is being used to finance imports from private sources, or is otherwise being used to finance procurements from private sources.

40. Loan proceeds are designated for procurement of fertilizer furnished by private sector sources.

41. FAA § 601(b). Information and conclusion on how the loan will encourage U.S. private trade and investment abroad and how it will encourage private U.S. participation in foreign assistance programs (including use of private trade channels and the services of U.S. private enterprise).

41. It is expected that most of the fertilizer will be furnished by United States private enterprise. The loan will make private investment in Afghanistan more attractive and feasible in the future in development of related agri-business.

42. FAA § 601(d). If a capital project, are engineering and professional services of U.S. firms and their affiliates used to the maximum extent consistent with the national interest?

42. Engineering and professional services will not be required under this loan. However, professional services are being provided under an A.I.D. grant project.

43. FAA § 602. Information and conclusion whether U.S. small business will participate equitably in the furnishing of goods and services financed by the loan
- 43.- Procurement procedures to be utilized under the loan will permit equitable participation of U.S. small business. Normal small business notification will be required in the implementation of the loan.
44. FAA § 620(h). Will the loan promote or assist the foreign aid projects or activities of the Communist-Bloc countries?
44. No.
45. FAA § 621. If Technical Assistance is financed by the loan, information and conclusion whether such assistance will be furnished to the fullest extent practicable as goods and professional and other services from private enterprise on a contract basis. If the facilities of other Federal agencies will be utilized, information and conclusion on whether they are particularly suitable, are not competitive with private enterprise, and can be made available without undue interference with domestic programs.
45. Technical assistance will not be provided under this loan nor will the facilities of other Federal agencies be utilized.

Loan's Compliance with Specific Requirements

46. FAA § 110(a) ; § 208(e). In what manner has or will the recipient country provide assurances that it will provide at least 25% of the costs of the program, project, or activity with respect to which the loan is to be made?
46. Considerably more than 25 percent of the costs of the program to which this loan contributes will be met by Afghanistan. USAID Director's certification is attached as Annex D. The GOA will provide assurance by signing a loan agreement with a provision contained therein that it will provide at least 25% of the cost of the program.

47. FAA §660. Will loan be used to finance police training or related program in recipient country? 47. No.
48. FAA § 114. Will loan be used to pay for performance of abortions or to motivate or coerce persons to practice abortions? 48. No.
49. FAA § 201(b). Is the country among the 20 countries in which development loan funds may be used to make loans in this fiscal year? 49. Yes.
50. FAA § 201(d). Is interest rate of loan at least 2% per annum during grace period and at least 3% per annum thereafter? 50. Yes.
51. FAA § 201(f). If this is a project loan, what provisions have been made for appropriate participation by the recipient country's private enterprise? 51. Afghan private enterprise retailers will be eligible to purchase and distribute the fertilizer.
52. FAA § 604(a). Will all commodity procurement financed under the loan be from the United States except as otherwise determined by the President? 52. Commodity procurement financed under this loan will be from the United States and countries included in A.I.D. Geographic Code 941.
53. FAA § 604(b). What provision is made to prevent financing commodity procurement in bulk at prices higher than adjusted U.S. market price? 53. The loan agreement will preclude such financing.

54. FAA § 604(d). If the cooperating country discriminates against U.S. marine insurance companies, will the loan agreement require that marine insurance be placed in the United States on commodities financed by the loan?
54. Yes, an appropriate provision will be included in the loan agreement
55. FAA § 604(e). If offshore procurement of agricultural commodity or product is to be financed, is there provision against such procurement when the domestic price of such commodity is less than parity?
55. All prices for agricultural input will be reviewed by the A.I.D. Commodity Management Division.
56. FAA § 604(f). If loan finances a commodity import program, will arrangements be made for supplier certification to A.I.D. and A.I.D. approval of commodity as eligible and suitable?
56. Yes.
57. FAA § 608(a). Information on measures to be taken to utilize U.S. Government excess personal property in lieu of the procurement of new items.
57. Not applicable.
58. FAA § 611(b), App. § 101. If loan finances water or water-related land resource construction project or program, is there a benefit-cost computation made, insofar as practicable, in accordance with the procedures set forth in the Memorandum of the President dated May 15, 1962?
58. Not applicable.
59. FAA § 611(c). If contracts for construction are to be financed, what provision will be made that they be let on a competitive basis to maximum extent practicable?
59. Not applicable.
60. FAA § 612(b); § 636(h). Describe steps taken to assure that, to the maximum extent possible, the country is contributing local currencies to meet the cost of contractual and other services, and foreign currencies
60. The GOA will pay for all local currency expenses of the project. All of the Loan proceeds will be expended on foreign exchange procurement. Afghanistan is not an excess currency country.

owned by the United States are utilized to meet the cost of contractual and other services.

61. Section 30 and 31 of PL 93-189 (FAA of 1973). Will any part of the loan be used to finance directly or indirectly military or paramilitary operations by the U.S. or by foreign forces in or over Laos, Cambodia, North Vietnam, South Vietnam, or Thailand? 61. No.
62. Section 37 of PL 93-189 (FAA of 1973); App. § 111. Will any part of this loan be used to aid or assist generally or in the reconstruction of North Vietnam? 62. No.
63. FAA § 612(d). Does the United States own excess foreign currency and, if so, what arrangements have been made for its release? 63. No. See paragraph 60 above.
64. FAA § 620(g). What provision is there against use of subject assistance to compensate owners for expropriated or nationalized property? 64. Neither this loan nor any previous assistance has been, or will be, used in this manner.
65. FAA § 620(k). If construction of productive enterprise, will aggregate value of assistance to be furnished by the United States exceed \$100 million? 65. Not applicable.
66. FAA § 636(i). Will any loan funds be used to finance purchase, long-term lease, or exchange of motor vehicle manufactured outside the United States, or any guaranty of such a transaction? 66. No such use is contemplated.
67. App. § 103. Will any loan funds be used to pay pensions, etc., for military personnel? 67. No.
68. App. § 105. If loan is for capital project, is there provision for A.I.D. approval of all contractors and contract terms? 68. There will be a provision providing that procurement contract terms and conditions are subject to A.I.D. approval.

69. App. § 107. Will any loan funds be used to pay UN assessments?
69. No. Use of loan funds for any purpose unrelated to the project will not be permitted under the loan agreement.
70. App. § 108. Compliance with regulations on employment of U.S. and local personnel. (A.I.D. Regulation 7).
70. Not applicable.
71. App. § 110. Will any of loan funds be used to carry out provisions of FAA § 209(d)?
71. No.
72. App. § 112. Will any of the funds appropriated or local currencies generated as a result of AID assistance be used for support of police or prison construction and administration in South Vietnam or for support of police training of South Vietnamese?
72. No.
73. App. § 113. Describe how the Committee on Appropriations of the Senate and House have been or will be notified concerning the activity, program, project, country, or other operation to be financed by the Loan.
73. The loan is included in the FY 1975 OYB which has been presented to Congress. Formal notification will be given to Congress in compliance with this provision.
74. App. § 601. Will any loan funds be used for publicity or propaganda purposes within the United States not authorized by Congress?
74. No.
75. App. § 604. Will any of the funds appropriated for this project be used to furnish petroleum fuels produced in the continental United States to Southeast Asia for use by non-U.S. nationals?
75. No.
76. MMA § 901.b; FAA § 640C.
(a) Compliance with requirement that at least 50 per centum of the gross tonnage of commodities (computed separately for dry bulk
76. Provisions will be included in Loan Agreement for complying with this section.

carriers, dry cargo liners, and tankers) financed with funds made available under this loan shall be transported on privately owned U.S.-flag commercial vessels to the extent that such vessels are available at fair and reasonable rates.

PROJECT AGREEMENT

BETWEEN THE DEPARTMENT OF STATE, AGENCY FOR INTERNATIONAL DEVELOPMENT (AID),
AN AGENCY OF THE GOVERNMENT OF THE UNITED STATES OF AMERICA, AND
Ministry of Agriculture and Irrigation

MINISTRY OF THE GOVERNMENT OF Afghanistan

The undersigned parties hereby mutually agree to carry out a project in accordance with the terms set forth herein and the terms set forth in any annexes attached hereto, as checked below.

1. PROJECT/ACTIVITY NO.
306-11-199-143

PAGE 1 OF 18

2. AGREEMENT NO.
AFC #1

3. ORIGINAL OF
REVISION NO. _____

4. PROJECT/ACTIVITY TITLE

AFC Management Support

PROJECT DESCRIPTION ANNEX FOREIGN CURRENCY STANDARD PROVISIONS ANNEX

STANDARD PROVISIONS ANNEX SPECIAL LOAN PROVISIONS ANNEX

This Project Agreement is further subject to the terms of the following agreement between the two governments, as modified and supplemented:

GENERAL AGREEMENT FOR TECHNICAL COOPERATION

DATE **2/7/51**

5. PROJECT DESCRIPTION AND EXPLANATION

(See Annex A attached.)

ECONOMIC COOPERATION AGREEMENT

DATE **6/23/56**

6. AID APPROPRIATION SYMBOL

72-11X1023

7. AID ELEMENT SYMBOL

402-50-306-00-39-31

(other) **TC Program Agreement as amended**

DATE **6/30/53**

8. AID FINANCING DOLLARS LOCAL CURRENCY

PREVIOUS TOTAL (A)

INCREASE (B)

DECREASE (C)

TOTAL TO DATE (D)

(a) Total

\$366,633

\$366,633

(b) Contract Services

\$324,633

\$324,633

(c) Commodities

(d) ~~XXXXXX~~ Participants

\$42,000

\$42,000

9. COOPERATING AGENCY FINANCING - DOLLAR EQUIVALENT

(a) Total

(b) Technical and other Services

(c) Commodities

(d) Other Costs

10. SPECIAL PROVISIONS (See Additional Cooperation Steps if Necessary)

"The Cooperating Government agency agrees to execute an assignment to AID, upon request, of any cause of action which may accrue to the Cooperating Government agency in connection with or arising out of a contractor's performance or breach of performance on any contract financed in whole or in part out of funds provided by the United States Government under this Agreement."

11. DATE OF ORIGINAL AGREEMENT
April 8, 1975

12. DATE OF THIS REVISION

13. ESTIMATED FINAL CONTRIBUTION DATE
April 8, 1978

14. FOR THE COOPERATING GOVERNMENT OR AGENCY

15. FOR THE AGENCY FOR INTERNATIONAL DEVELOPMENT

SIGNATURE:

DR. Zarif Salam, President of AEO

SIGNATURE:

Director, USAID/A, Kabul

DATE:

306-11-199-143

FX

Investment

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ANNEX A
PROJECT AGREEMENT: MANAGEMENT SUPPORT FOR THE AFGHAN
FERTILIZER COMPANY
Project Number: 306-11-199-143

INTRODUCTION

Agriculture is by far the most important industry in Afghanistan. More than eighty percent of the people are directly engaged in agriculture and most of the rest are involved in activities ancillary to it. Almost all of the exports of the country are based upon either livestock or crops and almost every person maintains a linkage with his village, his family and his farm. While Afghanistan is not a heavily populated country, the pressure on the arable, irrigable land, is relatively heavy. Also, much of the land that is irrigable is of relatively poor quality or the supply of water is not assured or is intermittent. Because of the low rainfall, dryland production is low with native grass and wheat being the only crops grown to an appreciable extent. At the present time about half of the land planted to wheat is dryland but this area produces only twenty percent of the total crop. Yields in Afghanistan are generally low, averaging, in the case of wheat, something over one ton per hectare on irrigated land. This is partially because of the insecure water supply, and partially because of the low soil fertility and the poor technology used by farmers.

The Government of Afghanistan has been aware of this situation for many years and, starting over 20 years ago, began taking steps to correct the situation. A Ministry of Agriculture was formed, research, extension, plant protection and other activities were started and fertilizer was introduced. Sales were slow however and, as a result of the two drought years of 1970/1971 and the resulting food shortages lasting up to June of 1972, the Government decided it had to take action to increase fertilizer availability and use. Therefore, the Afghan Fertilizer Company (AFC) was established in 1972 to be responsible as the sole agency for procuring fertilizers and distributing them in all parts of the country. Since then, the Republic of Afghanistan, because of the drastic increases in the prices of fuel, fertilizer and freight accompanied by worldwide shortages of cereals has decided that it is imperative that the AFC improve its own efficiency and that farmers all over the country have fertilizer readily available to them at prices and on terms which they can afford.

A. ACTIVITY TARGETS

The ultimate goal of this project is to increase the level of agricultural production and productivity in Afghanistan. It has been agreed by both the Government of the Republic of Afghanistan and most donor agencies that, given reasonably good

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weather and an adequate supply of fertilizer, the country could be self-sufficient in cereals. Experience the last two years indicates that this is true. With A.I.D. and other donor assistance over the last twenty years, a relatively large number of people have been trained in various aspects of agriculture and, with the help of American technicians, Afghan research officers have developed and/or adapted a number of varieties of wheat found to be fertilizer and water responsive under Afghan conditions. It has also been demonstrated that, by adding fertilizer to the mix of water, land and local industriousness, enough wheat could be produced to feed the country.

The specific purpose of this project is to help make improvements in the operation of the AFC so that it will be modernized and made more efficient in the procurement and distribution of fertilizer to all farmers. The Agricultural Development Bank, which is assisted by the IBRD, has recently initiated a farmer credit program jointly with the AFC to help the smaller farmer purchase fertilizer. However, if major benefits to the investments already made in fertilizer in the country are to be realized, and if the industry is to grow at the projected rates, the management of the AFC -- the sole distributing agency -- must be further improved and modernized.

The project is designed to furnish all assistance to the AFC in those areas of management most needing improvement:

1. General Management
2. Financial Management
3. Marketing
4. Supply and Distribution

B. COURSE OF ACTION

The Government of Afghanistan and USAID agree that the project will consist of the following:

1. Technical Advisors and Consultants. Four full time experts who will work within the AFC as advisors, assistants, and planners as required to:

- (a) improve the day-to-day operational efficiency of the AFC;
- (b) train their counterparts in modern business administration;

AND IDENTIFY THE RESPECTIVE DESCRIPTION)

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- (c) develop transportation, storage and financial and stock (inventory) control systems adapted to conditions found in Afghanistan;
- (d) help ensure that adequate quantities of fertilizer are available on time in all parts of the country;
- (e) prepare plans for improved service, expanded business activities, and rational growth of the organization;
- (f) write manuals of instruction and procedures on various phases of the AFC's activities to enable the organization to standardize business methods and increase operational efficiency;
- (g) make senior managers acquainted with the world fertilizer industry so that they can make the proper decisions quickly and confidently, and in order that the AFC can adjust rapidly to changing world fertilizer situations;
- (h) perform various special duties as assigned by the President or Vice-President of the AFC.

Specific job descriptions for each of the technicians are outlined in a letter from the AFC to USAID Director Brown which is attached as Annex B.

1. Briefly, each man will be assigned as follows:

- (a) The Chief Advisor will be officed next to the President of the AFC and will assist him in the day-to-day management of the company. He will provide advice on all aspects of management, on the procurement from both domestic and international sources, project development and planning, and on public relations.
- (b) The Financial Advisor will work with the Financial General Director of the AFC and the Executive Committee. He will provide advice, on a daily basis, develop financial procedures which may be adapted by the AFC and assist and train his counterparts in all aspects of accounting, financial control, budgeting, auditing, and other aspects of financial management including credit and the AFC's relationships with the Agricultural Development Bank and other credit institutions.
- (c) The Marketing Advisor will work with the General Director of Marketing of AFC and the Executive Committee. He will advise on a daily basis and develop sound marketing procedures for the AFC. He will

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also conduct dealer training and servicing programs and will assist with all other aspects of retailing, retailer relationships, sales promotion and forecasting, development of new markets, packaging, and other actions as necessary to make sure that farmers in Afghanistan have fertilizer readily at hand.

- (d) The Supply and Distribution Advisor will work with the General Director of Supply and Distribution and the Executive Committee. He will advise on and develop sound procedures for transportation, warehousing, inventory control, product allocations, and supply and demand forecasting. He will be required to travel with his counterparts to the Karachi Port and elsewhere as necessary to assist in off-shore fertilizer transportation and storage. In addition, short-time consultants will likely be required to assist in some aspects of the AFC operation such as foreign procurement, inventory control, prices and subsidies, auditing, etc., and will be provided as needed and as agreed upon by the USAID and the Government of Afghanistan.

2. Participants. Up to four (4) middle level officers of the AFC are to be sent abroad for specialized, non degree training of one year's duration in various aspects of business administration with particular reference to the fertilizer industry. It is expected that one or two of these officers may participate in an agricultural marketing program in the U.S. and that two or more may take courses in accounting, supervision, personnel administration, etc., in Iran, Lebanon, India, Turkey, or some other nearby country.

3. Progress to Date. The Government of the Republic of Afghanistan has been importing fertilizer by direct purchase and under loans and grants since the early 60's. Consumption has always been low and in 1970/1971 farmers used only 13,000 tons. Because of the serious food shortage in the country, Afghanistan's Cabinet decided in 1971 to conduct an extraordinary campaign to import and distribute fertilizer. In order to meet the situation, a country-wide program was conducted that fall under which the Agricultural Development Bank assisted the Ministry of Agriculture and Irrigation in making arrangements for group credit, and fertilizer was distributed from warehouses and the tail gates of trucks on a crash campaign basis. The army, several different departments of the Government, and the Extension Service of the Ministry of Agriculture and Irrigation, which for the purpose had been transferred to the Prime Ministry, took part in the program. This campaign was, relatively speaking, very successful with fertilizer consumption jumping from the 13,000 tons of the previous year to about 44,000 tons.

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Credit collections from this effort a year later were fair and a decision was made to continue the program in the Fall of 1972. This time the cooperation among the departments of the Government was not forthcoming at the same level as had been the case in 1971 and sales fell slightly to about 38,000 tons. During and at the conclusion of the 1972 campaign, all segments of the Government agreed that some different kind of distribution system had to be developed to impart and distribute fertilizer in Afghanistan.

The Government then approached USAID/Afghanistan and asked it to consider a loan with which to purchase fertilizer and to establish a distribution system in the country. This distribution system was to be organized as a joint stock company to be owned primarily by the Agricultural Bank (Ag Bank). In November, 1972 a loan agreement was signed providing \$16.5 million which was increased by \$3.0 million on June 23, 1973 to a total of \$19.5 million. The Government of Afghanistan authorized the AFC to negotiate with a number of firms to supply management assistance. A contract was arranged with the Cecchi Company of Washington, D. C., to supply 18 man-years of service over a two-year period. The team arrived to start work January 15, 1973.

The AFC, with the help of the expatriate team, developed a distribution system making use of private sector wholesalers. Several large commercial firms joined the company and handled the distribution of fertilizer through their own retail stores. During the course of the first year, these private wholesalers operated through about 300 retail stores to distribute 44,000 tons of fertilizer.

Upon the formation of the Republic in July, the new Government decided that a private sector distribution system was too expensive to be supported by the country, and that fertilizer distribution down to the retailers could be handled more economically by the AFC itself functioning as a government corporation. In August of 1974, the Government decided also that the Afghan counterparts of the expatriate management team had advanced enough that they should take over the management of the AFC with the management team shifting to an advisory role. The wholesalers were reimbursed for their stocks and participating certificates, and all connections with them were severed. Since that time, the AFC has established dealers on its own behalf, and distributed fertilizer as widely as possible. At the present time they have about 300 retailers which sold about 63,000 M. T. of fertilizer this past year. The AFC staff still requires considerable guidance in general management, financial management, marketing and fertilizer procurement and distribution.

While the senior officers of the AFC, for the most part, have worked with their counterparts for a year and a half or more and have had some experience as government administrators, they are not yet fully familiar with the modern business techniques introduced by the former management team. This has been recognized by

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the new Afghan management of the AFC and as a result, the Government on October 23, 1974, asked USAID/Afghanistan to supply the services of four technicians in the areas of: (1) general management; (2) financial management; (3) marketing; and (4) supply and distribution for a period of one year. This same request also suggested that "preference should be given to present team members currently serving in Afghanistan".

In a letter, dated 18 November 1974, the Executive Committee of the AFC (concurrent in by the Minister of Agriculture and Irrigation) outlined in considerable detail the tasks to be assigned to each member of the team and the steps the AFC is prepared to take to make full use of the skills and abilities of the individual advisors. (See Annex B). It is recognized that this list of tasks is too broad to be accomplished within the period of this project agreement and it will be necessary to establish priorities among them in order to have the team focus on the most important and immediate tasks.

4. Evaluation. All issues concerning project design, implementation, and progress made toward the objectives of this project will be jointly discussed by the AFC, the Ministry of Agriculture and Irrigation, the Ag Bank and USAID.

- (a) First Year Evaluation. In addition, this project will undergo an in-depth evaluation by representatives of the Ministry of Agriculture and Irrigation, the AFC, Ag Bank and USAID prior to the end of the first year of grant funding. The results of the evaluation will be published in the form of a report and will be used by the Government of Afghanistan and USAID to determine whether or not to continue the project beyond the first year.

To facilitate this evaluation the AFC will prepare within 60 days of the signing of this agreement specific work plans and objectives for itself and the advisory team individually and collectively against which the performance of the contractor, his expatriate team, and the AFC may be evaluated. These work plans should include a specific time frame within which the tasks and objectives would be accomplished.

- (b) Quarterly Evaluation. In addition, to ensure that institution building aspects of the AFC are progressing in accordance with established goals of the project, an on-site joint AFC,

Contractor and A. I. D. evaluation of project accomplishment will be made quarterly, or oftener if desired by either party. (This evaluation will not be held during the quarter in which the in-depth evaluation mentioned above is held.)

If it is determined during the evaluation that the goals and targets specified in the contract are not being fully met, any identified impediments along with recommended corrective action will be incorporated into a quarterly assessment report. Dissenting views and recommendations will be noted and become part of the report. The report as a management tool will be presented to and reviewed with the Supreme Council of the AFC as soon as possible following the close of the quarter.

The contractor, with the approval and assistance of AFC and A. I. D., will prepare the agenda of subjects to be jointly reviewed for each evaluation and will also prepare the quarterly assessment report.

5. U. S. Contributions.

(a) Advisors. During the time period covered by this agreement, advisors will be provided, full time, in the following fields:

1. General Management (Chief Advisor)
2. Financial
3. Marketing
4. Supply and Distribution

In addition up to two man-months of short-term consultants' time will be made available in disciplines needed by the AFC and as agreed to by the Government of the Republic of Afghanistan and USAID; two man months for procurement services and one man month of Home Office support.

(b) Participants. Funds are provided for up to four participants who will be programmed by USAID. The training program will be non-degree and will not exceed one year each and will be conducted in the U. S., Iran, Lebanon, India, Turkey or elsewhere in disciplines appropriate to the needs of the AFC.

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- (o) Support. The U. S. will supply all support services except for those specified in Para 6 below at the same level as is provided other USAID contract employees.

6. Government of Afghanistan/AFC Contributions.

- (a) Senior officers of the AFC will be provided as counterparts to the U. S. advisors.
- (b) Suitably qualified middle level officers will be selected by the AFC with concurrence of USAID for participant training.
- (c) The AFC will supply to the advisory team the services of one full-time secretary able to work in the English language and type at a rate of 40 words per minute, or better.
- (d) The AFC will provide vehicles for the team to be used for home to office and office to home transportation on a daily basis and other official business transportation within Afghanistan.
- (e) The AFC will provide and maintain household furnishings at the same level as supplied in the previous contract (AFC-Checchi).
- (f) The AFC will make allocations of funds with which to purchase essential commodities and materials for training purposes.
- (g) The AFC will provide administrative support for the foreign advisors and their project activities. This is to include, but is not limited to, office space and equipment; transportation in country; office supplies, procurement of necessary road passes, permits and visas, customs clearances for commodities, and translation services.
- (h) The AFC/Government of the Republic of Afghanistan will promote a free exchange of information between the AFC - Contractor - Ag Bank - USAID - MAI on all matters affecting the progress of the project and the physical and mental well-being of the contract employees.
- (i) Trust Funds administered by USAID/Afghanistan are to cover participant travel costs on Ariana Afghan Airlines' segment of international travel. Trust Funds as available will also be used to pay for U. S. Contractor support.

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- (j) The AFC and the Government of the Republic of Afghanistan will use its best efforts to make fertilizer available to meet the needs of the farmers and at prices to make the AFC a successful organization.
- (k) Credit to promote fertilizer purchases by farmers will be made available in adequate quantities and on favorable terms.
- (l) In view of the very high prices of phosphatic fertilizers and the low price of locally produced urea, the AFC will arrange with the MAI for research to be conducted to determine the optimum amounts and proportions of N:P to be used on each major crop on which fertilizer is applied.
- (m) The Government of the Republic of Afghanistan will provide at least twenty-five (25%) percent of the costs of the entire program with respect to which the assistance obligated by this agreement is to be provided.

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ANNEX B

November 18, 1974

Copy

Mr. Vincent W. Brown
 Director
 U. S. Agency for International Development
 Kabul, Afghanistan

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Dear Mr. Brown:

at the request of the Afghan Management of the Afghan Fertilizer Company, a formal letter was transmitted to you by the Ministry of Planning requesting a grant-in-aid to cover the cost of a four-member team of advisors to assist the Afghan management of the Afghan Fertilizer Company for a period of one year. We refer to memo number 226 dated October 23, 1974, on the signature of Mr. A. Aziz Feroz, Deputy Minister of Planning, listing the four general areas, namely Finance, Marketing, Supply and Distribution, and General Management.

Further to this referenced memo, we wish to amplify in more specific terms as to how the Afghan Management anticipates utilizing the services and knowledge of the four advisors. As stated in the referenced Ministry of Planning memo, we wish to emphasize that the current advisory team, former management team, possesses the experience, knowledge and expertise required to best carry forward the needs and services required to insure the continued success of the short and long range plans and programs of AFC. New or outside advisors would require many months of orientation and observation before being able to make the maximum contribution to the management needs of AFC. We fully expect and plan to utilize the knowledge and services of these advisors, if approved by the Republic Government of Afghanistan and USAID, in a most active day-to-day basis and further will advise and consult with them on all activities and decision-making processes in the overall management of AFC. They will not be observed as an active element in the management processes and forward planning of AFC.

The Afghan Management of AFC is mindful that AFC was started in late 1972 through a \$19.5 million USAID loan to pay for fertilizer imports and for the nine-member management team. We are also mindful of the Pakistan \$5.15 million as an off-setting grant to defray most of the dollar costs of the management team. Without the above funding and management assistance, the success in establishing a viable company such as AFC, would probably have not been possible. This request for four advisors will, if approved by the Republic Government of Afghanistan and USAID, help insure the continued success and growth of AFC.

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In each of the categories mentioned above, we shall attempt to amplify and outline in more specific terms as to how and when the services of the respective advisors shall and will be utilized.

I. FINANCE

We would like to utilize the services of a financial advisor to not only carry forward those financial and accounting functions and procedures currently implemented but to further refine such functions and procedures and to develop and assist in implementing new concepts. The following are areas where we believe further or continuing assistance is needed in an advisory capacity:

- A. Development of a basic training program covering all the fundamental inputs required in the scheme of AFC's financial and accounting operations, among which are:
1. Development of detailed guidelines to be followed by all staff and line personnel in the preparation of financial or operational budgets. Each input will be fully defined and procedures outlined in a clear and concise manner. Seminars will be held when and where necessary to familiarize all interested personnel at the Kabul headquarters and regional levels.
 2. Further improvements and procedures in fertilizer sales, invoicing, documentation, etc., will be analyzed and all necessary improvements and procedures for implementation of such improvements, changes and the like will be implemented at all levels within the Company.
 3. Procedures and necessary forms will be developed and implemented to gain a better knowledge of actual sales by provinces, subdivisions, regional and nationally. Such data is needed to improve further AFC's distribution system and gain greater efficiency.
 4. Further improvements need to be made in respect to devising systems and procedures for comparing and analyzing actual or current expenditures with budgeted forecasts. Such data needs to be more current in order to be able to take active and timely measures where necessary.
 5. Development and refinement of accounting procedures and further implementing of uniform procedures throughout the AFC organization, particularly at provincial levels.
 6. Assist management in all other financial or fiscal matters pertaining to banking procedures, procurement, letters of credit, bank transfers, and related fiscal transactions.

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7. Development and improvement of auditing procedures for regional operational controls.
8. Development and implementation of a simplified computer system for financial and accounting departments.

II. MARKETING

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The expatriate marketing advisor and regional managers during the approximately two years of management of AFC have developed two distinct marketing or sales systems, namely an initial system utilizing a limited number of national or regional wholesalers and more recently a system of independent and private retailers. The wholesaler and their retailer system has been replaced with a proper channel of fertilizer distribution. In spite of this change, AFC marketing has been able to maintain good continuity in distribution and sales of fertilizer to all areas of consumption throughout Afghanistan. This is to develop a more efficient distribution and sales system. AFC can and will maintain product control from the production point or procurement to the final distribution point before consumption by the farmers.

The following projects should be developed and implemented during the period of the advisory team's contract. The marketing advisor will direct his efforts and activities toward the following projects.

- A. Further development of training programs and procedures for operational improvements in the following areas:
 1. Sales Forecasting - In light of the new national organization, it is necessary to devise more precise and specific procedures for forecasting actual and factual sales rates and trends. A step-by-step system, detailing the various inputs will be developed for use at the district, regional and for national summaries. This system or procedure for forecasting will be uniform for all areas and all personnel charged with forecasting responsibilities. Seminars or meetings will be scheduled to explain and implement these procedures at regional and national levels.
 2. A sales and technical training program will be developed for AFC marketing personnel and also for the retailers. The AFC sales training program will embody the basic marketing, sales and technical features applicable to a marketing staff. The retailer sales and technical programs shall emphasize proper retailer store operations, procedures and technical data on proper fertilizer recommendations, use and cultural practices.

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3. A retailer performance and evaluation procedure will be developed for implementation at the regional levels. Such is necessary in order to properly make an evaluation of dealer performances and to improve the overall dealer distribution system.
4. A complete analysis of marketing short term and long term manpower requirements by manpower classification will be made for management guidance and personnel action plans.
5. A personal evaluation system and guidelines for performance will be developed in coordination with AFC's personnel department. This system will aid management in evaluating existing marketing/other personnel and serve as a standard for selection, promoting and elimination of poor performers. Timely and routine guidelines will be suggested or outlined for implementation of the evaluation.
6. An analysis of fertilizer consumption or use by specific crops as a percent, by tons, by province, by product, and nationally will be implemented. This will serve as a guide in allocating and directing marketing efforts for maximum effectiveness.
7. Other projects as outlined in the current Marketing Director's Report, entitled "Agricultural Marketing Survey and Action Plan for Use of AFC Marketing Personnel" will be implemented as time permits.
8. Many years of experience in international fertilizer trading, marketing and procurement rests within the current expatriate marketing adviser. A procurement procedure has been prepared for use of the Afghan management; however, experience must be gained by "doing". In light of this, it is logical that this experience should be applied in assisting and teaching the Afghan procurement personnel in all matters pertaining to fertilizer procurements, when AFC feels this need is necessary. This would require extensive travel which might/could be a part of the ADD grant.
9. A comprehensive study of past and current fertilizer "credit" programs will be made with specific recommendations to the proper governmental authorities on changes which AFC feels will improve upon the effectiveness of such programs.

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10. The marketing department will expand upon fertilizer demonstrational and advertising programs for the immediate future. The advisory contribution can be very significant in the development, implementation and evaluation of such programs.
11. The World Bank has indicated an interest in funding suitable agricultural input marketing programs in Afghanistan. The marketing advisor and the Afghan Manager will follow up and consult with the proper World Bank personnel and assist in the development of whatever projects show merit or appear to offer a material contribution to Afghan agricultural development.
12. The marketing advisor will assist in a feasibility study to further determine the advisability of AFC's establishing a nation-wide distribution and sales organization for a complete list of farm chemicals, spray equipment and related farm input items such as improved seed varieties, etc.

III. SUPPLY AND DISTRIBUTION

The Supply and Distribution Department has implemented a very efficient warehousing and distribution system for AFC. In spite of what has been accomplished, much remains that can or should be done in the interest of improving operational efficiency and reduction of storage and transportation costs. At the present time, AFC controlled, leased, owned or rented storage is in place to serve all regions.

In addition to warehouses, logistical procedures and requirements are well defined for the movement of fertilizer through the Port of Karachi and onward to Afghanistan by inland rail and truck transport. Procedures for reception at Karachi and onward movement have been well defined and implemented; the Afghan staff can handle such functions; however, a knowledgeable advisor would be most helpful in assisting and further training of Afghan personnel on anticipated future shipments over the next twelve-month period. Situations arise which require expertise not fully gained by the Afghan staff.

The following programs, plans, etc., should be implemented during the forthcoming twelve-month period to further aid and assist the supply and distribution department of AFC.

1. A much needed project in detailed procedures to assist the Afghan staff in making the most comprehensive determination of when, where, what quantities of product, types of products and related information to ship or inventory at each central warehouse location of AFC.

Such a plan or program will be developed in detail in cooperation and coordination with the marketing department. Anticipated or forecasted sales must serve as a basis for an orderly and logical supply base.

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2. A formal and comprehensive warehousing and transportation refresher training program will be expanded to include all current and changing requirements to better serve AFC's expanding number of selected outlets.
3. With the current on-stream status of the Mazar urea plant, additional and new procedures for reception and shipment of urea from this plant must be formulated and implemented. Logistics and transportation present a new and unusual set of circumstances that must be solved and implemented within a short period of time.
4. A comprehensive evaluation of existing warehouses as to location, size, suitable construction, etc., will be made. This study will not only serve the best interests and efficient operation of AFC's distribution requirements but also serve as a sound basis for making specific recommendations to the World Bank, who is currently interested in evaluating the need for and possible timing of fertilizer warehouse construction in Afghanistan. Warehouse construction of up to, say, 50/60,000 metric tons capacity may be needed to replace existing storage which is leased, out of proper location etc. Advisory services for such a construction program would be extremely desirable from the Afghan point of view.
5. At the current time all fertilizers are transported by the General Transport Company of AFC. A study should be made to determine the feasibility and economic advantage of moving at least a part of this large tonnage by AFC owned or leased trucks, or trucks from other organizations.
6. A feasibility study should be made in cooperation and in coordination with the Mazar urea plant to determine the best and most suitable bags to be used for packaging urea. A small bag manufacturing and labeling facility for manufacturing of bags from reliable finished bag materials should be evaluated. Substantial cost savings may be effected.

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V. GENERAL MANAGEMENT

It is imperative that AFC continue to use the most modern, effective and very best general management procedures in general acceptance by world industrial and management groups. It is recognized that modern accepted management practices must always be tailored and adapted to fit local situations and needs but never ignored or changed to the point where the organization and management structure becomes ineffective or loses the ability to perform all required operational and planning functions. We believe the advisory group can continue to make a significant contribution to existing management systems as well as initiate new systems to fill the short and long term requirements of AFC.

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ANNEX 9 (7-71) (NARRATIVE DESCRIPTION)

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The following areas should be addressed by an advisory group from either a short term, long term or a combination point of view.

1. Office management and administrative procedures should be evaluated in light of current practices and operations. All necessary changes, additions, and the like should be recommended and implemented where such can make a material contribution to the effectiveness of AFC's home and regional office operations.
2. In order for AFC to grow and make a significant contribution to the well being of the people of Afghanistan, it must continue to grow, expand and develop new lines of endeavor. In order to do this, definitive plans and programs must be initiated, evaluated, recommended and implemented by AFC Management in coordination with other governmental agencies. Areas that should be addressed first could be farm implement imports and/or production, all applicable and needed agricultural chemicals, food processing plants, export capabilities of various agricultural products and other projects directly related to the agricultural infrastructure of Afghanistan. Such studies will be contingent upon availability of personnel, funding, and a will to move forward in a positive manner.
3. General management should also be directed toward those things which can be done to foster and develop sound and meaningful cooperative relations and projects with all Ministries of the Afghan Government. An advisor could make a worthwhile contribution in continuing or implementing such functions and activities.
4. Feasibility studies for additional fertilizer facilities should be initiated and carried forward at an early date. Some outside assistance could possibly be a consideration of a future grant from USAID, UN or other direct governmental grant. If such funding is necessary, the advisor could recommend to AFC and assist in locating such available funds and willing donors.
5. Act as overall coordinator of the advisory team and offer all necessary advice to the Executive Board of AFC.

The Afghan Management of AFC in cooperation with the advisory team will review the projects and programs suggested above and place an order of priority and schedule a completion date for such projects. Such a schedule will indicate or show the month and/or quarter for completion. The AFC Management and advisors will review such programs with USAID, giving complete details of such programs, action taken and the results obtained or anticipated results of those projects which cannot be completed during the time interval of the advisory contract.

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Over the period of the advisory contract, AFC's Executive Committee, President and two Vice Presidents, plus the various departmental managers, regional managers, or other management personnel pledge to consult with and apprise the advisory team members on a day-to-day basis of all operational, decision-making and other matters related to the functioning of AFC. Timely group meetings will be scheduled, preferably every two weeks, between the Executive Committee and the Advisory Team to fully apprise the team of current happenings, plans, programs, etc. and to solicit appropriate advice.

The Executive Committee of AFC is prepared to schedule an early meeting with USAID/Kabul to further discuss this proposal and indicate or make suggestions in respect to the advisory teams. Since the expatriate team members are in general making preliminary plans to depart from Afghanistan, it is extremely important to move forward to a final decision within the shortest period of time.

Sincerely,

Dr. Zarif Saleem
President (now in the USA)

Mr. Mohammed Aslam Helaly/S
Commercial Vice-President

Mr. Mohammed Naim/S
Financial and Administrative Vice-President

(This report has been reviewed by the Minister of Agriculture and Irrigation, and a Committee made up of Mr. Noory, President of Research and Mr. Anam, President of Forestry)

Mohd. Aslam Helaly/S
Mohd. Naim/S

A. General

Afghanistan, a completely landlocked country, covers an area of about 63 million hectares (ha), of which 13 million ha are arable. About 5 million ha are cultivated each year. Half of the cultivated land is classified as irrigable; however, due to insufficient water, only 1.2 million ha receive adequate irrigation; the remaining 1.3 million ha are under fallow or insufficiently irrigated during the summer. Food grains (wheat, barley, rice and corn) account for about 70 percent of cropped area with the balance planted to cotton, sugar beet, oilseeds, fruits and vegetables.

Estimates of population range between 10 and 18 million. The annual growth rate is slightly over 2 percent. About 85 percent live in rural areas, mostly in villages scattered throughout the mountains and desert; 2 million are nomads. Because of particularly difficult communication conditions, the rural population is too far from the urban areas to actively participate in the market economy. An estimated two-thirds of agricultural production does not enter the monetary economy. More than 80 percent of the people are directly engaged in agriculture and most of the rest are involved in activities ancillary to it.

According to the 1969 preliminary census, the average size of farm holdings is 3.5 ha of cultivated land. Land ownership distribution is, however, uneven. In some areas farmers own most of their farmed land, while in other regions a high proportion of the cultivated land is owned by a relatively small number of large

landholders. Estimates indicate that there are at least 1.5 million agriculture households with six or seven persons each, but a large number own either no land or less than 0.5 ha.

Many farms are sharecropped. Generally, if the tenant provides inputs (fertilizer, seed, draft animals or other implements), his share of the crop varies between 40 and 60 percent depending on the amount of input provided. Under a sharecropping arrangement of 50 percent, the tenant finds enough incentive to use fertilizer; however, this incentive is often limited by the tenant's cash on hand to make the required investments. Another arrangement under the sharecropping system is when the landlord provides all the inputs. In this case the tenant's share is from 16 to 25 percent.

There is considerable seasonal under-employment among agriculture workers. The degree of under-employment depends heavily on the size, cropping pattern and livestock program of the farm. While under-employment is predominant on farms of less than 10 ha, larger farms frequently find themselves short of labor.

Hired labor is mainly paid by the day with wages (including meals provided by the farmer) varying between AF/S 50/day (\$.91) up to AF/S 120/day (\$2.18) during peak labor periods, such as weeding and harvesting time. A substantial proportion of the farmwork, such as wheat harvesting or cotton picking, is done on a piece basis with wages paid in kind. There are few employment alternatives outside the agriculture sector; however, many small landholders have the opportunity for seasonal work on larger farms.

Farmers owning tractors or oxen perform "custom work" on other farms to increase their income.

B. Production and Prices

The following table shows the production of Afghanistan's principal crops for the period 1969-70 to 1974-75:

TABLE 1

Estimated Production of Principal Crops
(in thousands of metric tons)
(year ended March 20)

	<u>1968/69</u>	<u>1969/70</u>	<u>1970/71</u>	<u>1971/72</u>	<u>1972/73</u>	<u>1973/74</u>	<u>1974/75</u> ^{1/}
<u>Food Grains</u>							
Wheat	2,354	2,454	2,081	1,915	2,450	2,750	2,867
Barley	361	365	340	295	350	360	360
Corn	773	785	667	670	720	760	760
Rice	402	407	366	350	400	420	420
<u>Industrial Crops</u>							
Cotton (unginned)	71	85	76	63	58	105	105
Sugar beets	62	68	62	60	63	60	60
Sugar cane	57	60	55	50	55	60	60
Oilseeds	36	37	35	28	34	38	38
<u>Fruits & Vegetables</u>							
Fruits	834	842	809	750	820	840	840
Vegetables	654	671	626	650	658	680	680

1/ Preliminary

Reliable agriculture statistics are still in the process of being developed and production estimates for major crops are subject to wide margins of error. However, the trends in crop output are supported by available precipitation and price data.

The dependence of the agriculture sector on weather conditions was dramatically illustrated in the past five years. A two-year period of severe drought (1970/71 and 1971/72) caused a sharp decline in production while the favorable weather conditions (above normal precipitation and heavy winter snows) in 1972/73 and 1973/74 resulted in substantial recovery in 1972/73 and in record crops in 1973/74.

Wheat is by far the principal crop with approximately 60 percent of the cultivated land planted to it annually. It is grown in all 28 provinces and by almost all farmers. Approximately 64 percent is produced in the 10 cotton growing provinces. Wheat absorbs about 40 percent of consumers' total expenditures for food and accounts for about 60 percent of the annual cereal production. About two-thirds of the total wheat production is consumed in the area where it is produced. On this basis, traditional average annual production has been estimated at 2.4 million MT. Droughts (three of ten years) reduce this figure by about 260,000 MT/year, while favorable weather (two out of ten years) increases it by about 190,000 MT.

About 1.4 million ha of irrigated wheat and about 1.2 million ha of dry land wheat are cropped annually. Irrigated wheat with an average yield of 1.3 ton/ha (under traditional methods) constitutes about 77 percent of total wheat production; dry land wheat with an average yield of about 0.5 tons/ha accounts for about 23 percent. Yields of irrigated wheat on demonstration plots and selected farmers' fields have reached 5.0 tons/ha.

In 1973/74 wheat production reached a new record level of 2.75 million tons, an increase of about 13 percent over the peak level reached in 1972/73. This level of production was roughly equivalent to self-sufficiency and, if sustained, should eliminate the need for foodgrain imports. Statistics from the Ministry of Commerce indicate that imports, in the 10-year period 1964/65 to 1973/74, averaged about 110,000 MT with a peak of 217,000 MT in 1971/72 and a low of 40,000 MT in 1968/69. The Food Procurement Department (FPD) of the Ministry of Finance is responsible for importing, storing and distributing imported wheat and has storage facilities throughout the country with a total capacity of 279,000 MT.

FPD is also responsible for stabilizing internal wheat prices through domestic purchases and sales of wheat; but its efforts in this area have been minimal and internal wheat prices have fluctuated in accordance with production. The following table shows FPD carryover inventories and procurements during the period 1964/65 to 1972/73.

TABLE 2

Food Procurement Department
Wheat Inventories, Purchases, Imports and Distribution, 1964/65-1972/73

<u>Year</u>	<u>Beginning Inventory</u>	<u>Purchases</u>		<u>Total Supply</u>	<u>Distribution</u>
		<u>Domestic</u>	<u>Imported</u>		
1964/65	1,825	4,880	80,000	85,705	111,681
1965/66	10,024	2,934	150,000	162,958	138,500
1966/67	72,158	2,32	20,000	94,480	75,826
1967/68	18,660	8,000	123,500	150,160	80,200
1968/69	69,960	27,000	74,000	170,960	72,000
1969/70	98,960	32,000	80,030	210,990	61,738
1970/71	129,252	--	59,600	188,852	89,553
1971/72	99,299	--	226,868	326,167	204,207
1972/73	121,960	15,000	187,604	324,564	NA

Using the estimate of one million tons of domestic product traded in a normal season and adding the 110,000 tons average imports, FPD has been responsible for between 7 and 20 percent of the national cash wheat sales and from 0 to 8 percent of domestic wheat purchases.

The Afghanistan price for wheat during the decade ending 1973 averaged \$89 MT which was generally higher than world prices which were between \$64 to \$71 MT. The most recently quoted bazaar (retail) price of wheat is \$116 MT which is the same price the FPD is prepared to pay to farmers. At this price, Afghanistan wheat prices are below the world market price, which is currently quoted at \$135 ton FOB U.S. Gulf ports.

Cotton, the main cash and export crop, has been grown in Afghanistan for about 35 years. Most cotton (about 90 percent) is processed through seven ginning companies which have a total installed capacity well in excess of the amount processed. In 1972/73 production on 50,000 ha yielded 58,000 MT, and in 1973/74 production on 74,000 ha was 105,000 MT. Between 1972 and 1974 the average yield increased from 1.2 MT/ha to 1.5 MT/ha; with the best cotton fields yielding over 4.5 MT/ha. The increase is attributed to favorable weather and increased use of fertilizer.

Between 1970/71 and 1972/73, the domestic textile industry processed 8,000 to 9,000 MT of ginned cotton and is expected to increase to 13,500 MT in 1974/75; the remainder is exported. Exports over the past ten years have been as follows:

TABLE 3

Exports of Cotton

<u>Year</u>	<u>Tons</u>	<u>Year</u>	<u>Tons</u>
1964/65	21,000	1969/70	7,700
1965/66	15,900	1970/71	13,400
1966/67	16,700	1971/72	20,700
1967/68	10,700	1972/73	15,600
1968/69	7,600	1973/74	9,800

Exports have varied substantially from year to year due both to changes in production and to stock carryovers. Cotton from one year's harvest is partly exported in that year and partly in the next one.

2.16 The price at which cotton is bought from the farmers is controlled and prices for the 1974/75 harvest are as follows:

TABLE 4

First Quality	AF 15.3/kg or \$278/MT
Second Quality	AF 14.1/kg or \$256/MT
Third Quality	AF 13.0/kg or \$236/MT

The current prices of wheat (\$116 MT) and cotton (\$278 MT) corresponds to a wheat:cotton price ratio of 1:2.2. A balanced ratio, under Afghanistan costs and yields, is thought to be about 1:2 ratio (historically the ratio has been about 1:1.25). At these prices it is anticipated that a number of farmers (presumably the larger ones who do not need to plant a high percentage of wheat for family consumption) will switch from wheat to cotton. Raising the farmgate price to about \$130 MT would bring the ratio in balance.

C. Organization and Supporting Services

The Ministry of Agriculture (MAI) has primary responsibility for agriculture in Afghanistan. MAI is organized into departments representing the different subsectors of agriculture (extension,

irrigation, plant protection, livestock and research) and into Regional Authorities in charge of specific projects.

Research activities are normally the responsibility of MAI's Research and Soil Department. More than 20 stations in about eight agricultural regions carry out seed selection programs for cereals, feed crops, oil seed, rice, cotton, sugar beets and horticultural crops. Research activity, however, is seriously hindered by a shortage of qualified staff, lack of equipment and budgetary constraints.

The number of extension agents has expanded rapidly over the past few years from only 300 agents in 1970 to about 3,000 agents by 1973. Most of those recruited, however, have been young and without experience. In the last 18 months the staff has been reduced to eliminate some of the most poorly qualified agents. The need for in-service training is great, but little is being done on a national or regional basis to help the remaining agents to upgrade themselves.

Agriculture training is being conducted on two levels--at secondary schools and at the University of Kabul. Three secondary schools, with a total enrollment of about 700 students, graduate a total of about 300 a year; but the annual demand for these graduates is about 5,000. The University of Kabul's Faculty of Agriculture graduates about 200 students each year. The study program requires four years with specialization in the third and fourth years.

Most of the credit in the Afghanistan economy is provided by non-institutional sources such as money bazaars and private lenders; banks provide agriculture credit to only 3 to 4 percent of the farmers. Money bazaars provide strictly short-term loans while banks and other institutions extend medium and long-term financing as well.

Of the six banks in Afghanistan (three commercial and three specialized), only the Agriculture Development Bank (AgBank) directly services agriculture. It was established in 1954; but because of poor management, unrealistically low interest rates, nonexistent collection records, etc., by 1969 it had dissipated all its capital and in a practical sense had ceased operations. In 1970 the World Bank and UNDP assisted in the reorganization of the AgBank, and it now shows signs of being an effective source of institutional credit. (The World Bank has just authorized its second credit to AgBank--see paragraph 1.05.)

Under new policies now in effect, lending activities, which were largely confined to farm mechanization prior to 1970 now include much broader types of agriculture lending; and lending terms and conditions are related to the particular items being financed. Following are AgBank terms now in effect for some selected items:

TABLE 5

<u>Loan Type</u>	<u>Percent of Investment Financed</u>	<u>Term (Years)</u>	<u>Grace Period</u>	<u>Interest Rate</u>
Tractors	80	5	-	8
Sprayers	100	2	-	10
Water Pump	80	6	-	8
Fertilizer	100	1	-	10
Surface Irrigation	80	7	2	8

Loan disbursement and collection rates have also increased significantly since the 1970 reorganization. Disbursements in 1974 were 30,969 loans totaling \$7.2 million compared with 44 loans totaling \$47,000 in 1970. The collection rate of loan principal on loans made since 1970 has been 92 percent.

Lending activities in 1974 primarily involved short-term

production loans (78 percent of total disbursements). Specifically, \$4.6 million for fertilizer and seed was disbursed to 30,689 farmers and \$1.1 million for fertilizer was disbursed to seven cotton companies. Most beneficiaries were small holders or sharecroppers farming about 3.5 ha of irrigated land. Over the next three years AgBank plans to increase its lending program for fertilizer, seeds and pesticides to \$9.5 million annually and to reach a minimum of 43,000 farmers.

One of the most important contributions made by the AgBank was the introduction of new security requirements in February 1974. Under these requirements, loans not exceeding \$181 can be secured by a promissory note signed by the borrower and one guarantor; loans between \$181 and \$454 by a promissory note in the same form but with two guarantors; and loans between \$454 and \$1,818 by a promissory note, with one guarantor, which is registered with the Directorate of Registration of Documents.

D. Constraints to Agricultural Development

The major constraints to agricultural development in Afghanistan are (in descending order of importance) limited irrigation and water supply; inadequate supply and distribution of agriculture inputs; inadequate management of resources; weak extension services; limited availability of institutional credit; and shortage of farm labor and power during certain seasons. None of these restraints will be overcome, or corrected, in the short run, but efforts are being made to limit the problems. This loan, coupled with the assistance we have provided to the Afghanistan Fertilizer Company, will allow for an adequate supply of fertilizer given current usage and will improve its marketing and distribution.

APPRAISAL OF
A SECOND AGRICULTURAL CREDIT PROJECT
AFGHANISTAN

Afghan Fertilizer Company

A. Background

Fertilizer Use in Afghanistan

1. Very little fertilizer has been used in the past in Afghanistan. Imports for 1966/67-1973/74 were as follows:

<u>Year</u>	<u>Urea</u>	<u>D.A.P.</u>	<u>Superphosphate</u>	<u>Total</u>
	-----tons-----			
1966/67	5,700	--	3,300	9,000
1967/68	3,000	--	3,300	6,300
1968/69	19,000	6,600	4,000	29,600
1969/70	6,000	11,300	200	17,500
1970/71	10,000	4,700	--	14,700
1971/72	27,400	12,300	1,800	41,500
1972/73	26,000	7,000	--	33,000
1973/74	49,700	32,200	--	81,900

Source: MAI and AFC.

The higher import figures in the last three years resulted from the Government's drive to launch a fertilizer import program in order to help alleviate the serious food shortages, particularly of wheat, incurred in the early 1970's. USAID is supporting this program by a long-term loan of US\$19.5 million on soft terms to the Government of Afghanistan for the importation of fertilizer. Of this amount, US\$5.4 million (Af 294 million) remains to be withdrawn. Purchases of fertilizer by farmers have grown roughly parallel with imports, and in 1973/74 were approximately 48,000 tons.

History and Objectives of the Afghan Fertilizer Company

2. Following USAID support for fertilizer importation, the Afghan Fertilizer Company (AFC) was established by Government in October 1973. AFC is a joint stock company, but with all its shares owned by AgBank. According to its recent charter, the objectives of AFC are:

- (a) procurement and importation of chemical fertilizers from abroad or procurement from domestic sources;
- (b) transport of chemical fertilizers to selected outlets within the country, and their storage and distribution;
- (c) the setting of standards for controlling and regulating storage and packing, and sale of chemical fertilizers.

B. Organization and Management

3. AFC's main governing body is the Supreme Council, which comprises the Ministers of Agriculture (chairperson), Finance, Planning, Mines and Industry, and Commerce; the President of AgBank; and the Managing President of AFC. The legal position and role of the Council have been modeled on those of the Supreme Council of AgBank (Annex 4).

4. AFC's main office is in Kabul. For the purposes of sales the country is divided into four regions (see map), each having a regional manager. Each office has four main divisions: Sales, Personnel and Credit, Finance, and Supply and Distribution. Nine key positions in AFC were filled by consultants from Checchi and Company (a US firm) until September 1974, when executive management passed into the hands of Afghan staff with the Checchi consultants being retained as advisers, at least until January 1975. With the change in marketing structure from wholesale to retail and the resulting increase in AFC's supervision responsibilities, the mission feels that it would be desirable for the advisers to remain longer in order to facilitate the smoothest possible changeover. The Government has indicated that an extension of the advisers' contract would most likely be sought.

C. Physical Resources and Operations

5. At present, AFC has the use of 26,500 tons of warehouse capacity, which are still owned by the Ministry of Agriculture. It has been agreed that these warehouses will become the property of AFC, either as a grant or against additional shares issued by AFC to Government. Twenty-one thousand tons of this capacity is located in primary distribution centers and the remaining 5,500 tons in secondary distribution centers. In addition, 54,000 tons of capacity has been leased or borrowed, of which about one-third is on loan from other Government agencies and two-thirds rented from the private sector. Historically, leased facilities have been inexpensive, averaging about a dollar per ton per year. However, with the expansion of crop production, particularly wheat and cotton, it is anticipated that warehouse storage will become more difficult to obtain.

6. Typically, warehouses used by AFC are small and poorly designed for handling fertilizer. In some areas fertilizer is being stored outdoors due to lack of suitably located storages. With present procurement problems AFC's peak fertilizer inventory is expected to comprise at least one full year's sales. With the very high cost of fertilizer (landed cost of DAP is now around US\$550 and urea US\$440 per ton), availability of good storage is particularly important to minimize product deterioration, facilitate maximum control of inventory, and reduce inventory losses. Thus AFC's proposed program of constructing purpose-built fertilizer stores is justified and will form an integral part of the improved fertilizer distribution system to be funded under the project.

Retailers

7. Until recently, AFC sold fertilizer only to wholesalers, at a discount of 15% below the price to the farmer. Some of this discount was passed on to retailers, but it is widely reported that the retail margins under the wholesale/retail system averaged only about 2%. Early in 1974, Government decided that wholesalers were to be abolished and that AFC would provide fertilizer directly to individual retailers. The rationale behind this move was that fertilizer is heavily subsidized and Government wished to ensure that the benefits passed to farmers and not to the relatively wealthy wholesalers. Despite opposition from AFC and USAID, which foresaw substantially increased management problems as a result of this move, the wholesalers have now been abolished. Preliminary budgets (see para 26) indicate that some savings may result from this decision, but overall, effective management of AFC will be more difficult to achieve.

8. Under the new system, retailers take ownership of fertilizer at the AFC warehouse and receive a discount of Af 20/bag below the farmers' price. In addition, a transport allowance of Af 2/ton-km is made and deducted from the invoice. Present fertilizer prices to the farmers are fixed at Af 440/50 kg bag for urea (US\$160/ton) and Af 492/50 kg bag for DAP (US\$179/ton). On this basis, the retailers' margin is 4 to 5%.

9. Retailers are licensed and are required to purchase their first loads of fertilizer for cash. Subsequent loads can either be exchanged for credit coupons given by the farmers to the retailer (see flow charts attached) or bought for cash, ^{1/} with the proceeds from cash sales. These retailers are screened by the Sales Division of AFC and selected on the basis of availability of sufficient storage space to operate effectively.

^{1/} Over the project period, about 70% of fertilizer sales would be for coupons and 30% for cash. Wide variations are expected between individual retailers.

10. With about 220 retailers selling an estimated 53,000 tons of fertilizer in 1974, the average retailer will need to handle 250 tons of fertilizer during the year. That is, he may need to turn over inventory 25 to 30 times, assuming that initial cash availability is sufficient to purchase only one 8 to 10 tons/load (approximately Af 80,000). In view of the seasonality of demand, most retailers would probably sell about 60% of their annual stock in a single 4-week period. Thus, on the basis of a one-load inventory holding, the average retailer would need to turn over total inventory every two days during the peak period. It is doubtful whether procedures will be sufficiently well organized for this to be practicable, particularly in situations where the retailer is far from the warehouse. Consequently, once the creditworthiness and integrity of a retailer has been established, it is recommended that part of his fertilizer requirement should be made available on a consignment or credit basis during the peak season. This would allow his average inventory to be higher, and reduce the number of trips he has to make to AgBank and the AFC warehouse.

Procurement

11. Since its establishment through August 1974, AFC has procured about 82,000 tons of imported fertilizer. Most fertilizer procurements by AFC have been made according to international bidding procedures of USAID. Fertilizer is procured in bulk lots of 5,000 to 30,000 tons after advertising internationally from Washington, D.C. The source and origin of fertilizer procurement is restricted to countries included in Code 941 of USAID. There are no legal guidelines for procurement of USAID recycled funds. However, until now those funds have only been used for meeting transport costs. In addition to AFC's procurements, Government has procured fertilizer through (a) bilateral agreements in bulk lots of 5,000 to 10,000 tons from the USSR, the Federal Republic of Germany and Kuwait; and (b) since October 1974 from the Mazar-i-Sharif plant. This fertilizer has been made available to AFC partly as grant, partly as loan.

Transportation

12. Apart from vehicles for personnel, including motorcycles for regional sales staff, AFC does not own transportation but hires trucks from private operators through the Afghanistan Transport Company and pays national transportation rates, normally AF 2/ton-km. Transportation from AFC warehouses to retailer is organized by the retailer, and an allowance of AF 2/ton-km is made for this purpose.

13. Imported fertilizer from Europe generally goes by rail through Russia to the border; and from the US by ship to Karachi and thence by rail to Peshawar and Chaman and by road into Afghanistan. Total cost of shipment, etc., from Karachi to AFC warehouses averages US\$30/ton.

C. Financial Resources

14. The audited balance sheet of AFC at August 22, 1973 and an unaudited balance sheet at June 21, 1974 are shown in Table 1. The main sources of AFC finance are the long-term loan for US\$19.5 million from USAID, of which US\$14.15 million has been drawn down, and the Government's contribution. This latter source of funds comprises an estimate of the valuation of fertilizer (Af 357 million) taken over from the Government. An exact valuation has not yet been agreed between Government and AFC. When this is agreed, shares will be issued against it, and in addition the value of the Government warehouses taken over will appear under AFC's fixed assets, and a corresponding figure as shares on the liability side of the balance sheet. At present, AFC is highly liquid, with current assets of US\$22.41 million of which only US\$12.13 million are actually tied up in fertilizer stocks. This position, however, must be viewed against the rapid rise in fertilizer prices. Between January 1973 and September 1974 prices averaged US\$171 for urea, but these prices have now more than doubled.

15. The main current assets besides inventory are deposits with AgBank. The accounts receivable at AgBank are a legacy of the 1973 policy whereby AFC provided 75% of credit to farmers and received only 25% of fertilizer sales as cash. As of March 21, 1974, deposits with AgBank amounted to Af 419 million. With the increase in world fertilizer prices, AFC will require most of its funds for international procurement and will not continue with this arrangement (paras 27 and 28).

16. The substantial accounts receivable figure of US\$2.5 million in June 1974 includes fertilizer (of which an estimated 8,000 tons are still unused) supplied by AFC to the cotton and sugar companies, which AFC has considered as outright sales, but which the companies have considered as goods on consignment.

17. The net Government subsidy ^{1/} shown in the balance sheet is essentially subsidy paid before it has fallen due. It is the difference between subsidy disbursements by Government and the operating losses incurred. In the longer run this figure would be zero, since Government would simply provide cash resources to cover AFC's operating losses.

18. Operating in its present fashion, therefore, but assuming that the need to finance 75% of farmers' fertilizer purchase is abandoned, AFC has total capital of approximately Af 1.6 billion, including Af 294 million (US\$5.35 million) to be withdrawn from USAID loan which can be used for procuring fertilizer.

^{1/} See para 21.

19. Government has agreed, as part of the terms of the USAID loans, to underwrite AFC's losses in its first few years of operation. Government's initial payments amount to AF 489.9 million (US\$8.9 million) which is being disbursed between January 1, 1973 and August 30, 1975. Government subsidies due on fertilizer being sold at present are estimated 1/ as follows:

	<u>DAP</u>	<u>Urea</u>
	----US\$ per ton----	
<u>Fertilizer Costs</u>		
Import Cost	205	171
AFC Operating Costs	23	23
Retailers' Margin	<u>7</u>	<u>7</u>
<u>Total Cost of Fertilizer Import and Distribution</u>	235	201
Sale Price to Farmers	<u>179</u>	<u>160</u>
Government Subsidy	<u>56</u>	<u>41</u>

20. AFC takes inventories on a "first in first out" (FIFO) basis. This means that losses are incurred only after the actual use of fertilizer is below its cost.

21. On the basis of current (September 1974) fertilizer import prices and 1974 sale prices to farmers, which Government has promised to maintain, the level of subsidy required to offset losses would be approximately two-thirds the total cost of import and distribution. The subsidy required on urea will depend upon the fertilizer amounts to be provided by the Mazar-i-Sharif plant.

D. Analysis of Performance

Procurement

22. Procurements have been substantially in excess of sales and under normal trading conditions would have been considered excessive. In the present price circumstances, however, this excess has been beneficial since AFC now holds substantial stocks of fertilizer purchased for less than half their present replacement value. In future, if holding costs are to be minimized, it will be necessary to make more accurate forecasts of seasonal

1/ Using historic rates of exchange for purchases but current rates for other costs and sales.

sales and to take these forecasts into account when procuring fertilizer. In a country such as Afghanistan where the total level of fertilizer use is only a very small percentage of the potential level, sales are extremely difficult to predict. In order to ensure availability of supplies, it is suggested that fertilizer be procured such that the total expected annual sales are in stock prior to the autumn selling season. By following this policy, autumn sales could be substantially above the expected level yet still be provided for by scheduling forward the fertilizer which otherwise would have been sold in spring. Additional procurement for spring requirements would then need to be made during the winter. Using this policy, peak stocks of fertilizer should not exceed the subsequent year's estimated sales and maximum inventory would be in AFC warehouses at the end of July.

Storage

23. Although the condition of some of the storage facilities is far from optimal, AFC appears to have done extremely well in keeping physical inventory losses to 1% of stock. Stores inspected by the mission appeared to be well organized and maintained. However, as a result of AFC's shortage of purpose-designed storage, some fertilizer stored outdoors appeared in danger of deterioration and there was evidence of split bags due to storing to excessive heights. Considering the expected growth of the fertilizer program and the general shortage of proper storage space, there is a need for purpose-designed storage facilities. Without these facilities inventory losses could be expected to increase substantially.

Sales

24. Sales of fertilizer have been running below the AFC budgeted level. However, this is partly a function of Government credit and distribution policy. The mission estimates that provided present fertilizer price policies are followed, physical fertilizer sales would grow at a compound rate of about 10-15% per year, although the proportion of fertilizer sold on credit will probably decline. Currently, fertilizer prices in Pakistan (roughly equivalent to AF 415 per bag) are slightly below wholesale prices in Afghanistan and it is possible some Pakistan fertilizer will pass illegally into the country and thus reduce AFC's fertilizer sales.

Operating Cost

25. Table 2 shows AFC's operating cost during the 10 months to June 1974 and a budget for the 7 months August 1974-March 1975. The increase from US\$7.3/ton in the previous period to a budget of US\$18.5/ton (excluding depreciation, contractors' expenses, and interest charges), largely stems from the fact that in the second period AFC will be fulfilling the primary wholesaling function. The wholesalers' commission will be saved, but additional costs of transport from AFC stores to retail shops will need to be allowed for. Comparison between the actual costs of the 10 months to June 1974 and the budgeted costs for the 7 months to March 1975 cannot be precisely drawn; however, the figures do indicate a potential saving from the abolition of wholesalers, as follows:

	<u>System with</u> <u>Wholesalers</u>	<u>AFC Direct to</u> <u>Retailers</u>
	-----US\$/ton-----	
<u>Cost of Distribution</u>		
AFC Operating Costs /a	7.3 /b	18.5 /c
Wholesale Margin)	
) 25.6	-
Retail Margin)	7.3 /d
Transport Allowance	-	<u>0-3.0</u>
Total Costs	32.9	25.8-28.8

/a Including depreciation, consultants' expenses, and interest charges.

/b Based on 10 months to June 1974.

/c Based on 7 months to March 1975.

/d 15% of contemporary prices.

26. The overall cost of running AFC appears reasonable in relation to the tonnage of fertilizer distributed.

E. Future Development

Projections of Procurement, Sales, and Cash Flows

27. AFC's projected cash flow (Table 6) has been derived from projected fertilizer sales and prices and from AFC's income statement (Tables 3-5). Fertilizer distribution is projected to increase by 10% annually to 85,000 tons in 1978/79. The highest level of annual cash expenditure on imports is expected to occur in 1975/76 and to peak at about Af 1.5 billion. It will decrease slightly thereafter, due to falling fertilizer prices. Government subsidies are based on annual operating losses as shown in the income statement and will be disbursed to AFC in the subsequent fiscal year. In making these projections, it is also assumed that about Af 82 million of additional fixed capital, mainly for new headquarters, to be expensed in 1974/75 and 1975/76 would have to be covered by the available funds. The financial requirements for the proposed warehouses would be covered by funds from IDA and the Government and therefore are not shown in the cash flow.

28. The projected cash flow shows that AFC's available financial resources would be completely depleted by 1975/76. AFC has to withdraw Af 312 million of its AgBank deposits in 1974/75 and the remainder (Af 107) in 1975/76. The remaining balance of USAID loan (Af 294 million) has also to be fully utilized in 1975/76. In addition to the subsidies from the Government, AFC would still need about Af 700 million to sustain the envisaged programs. Due to the expected decline in the procurement cost of fertilizer and the lagging of the subsidies, most of the additional financial requirements could be repaid by 1978/79.

Expansion of Warehouse Capacity

29. The mission estimates that fertilizer imports will average 85,000 tons annually by 1978/79. Since AFC owns only 26,500 tons of warehouse storage, AFC has prepared proposals for the expansion of this capacity by 55,000 tons (Appendix A). If this proposed expansion program is successful, total AFC storage capacity will be sufficient to handle most of its imports on its own premises by 1978/79. Principally, AFC's proposals concentrate on providing 35,000 additional tons of primary warehouses and 20,000 tons of secondary distribution warehouses (in 1,000 and 2,500 ton buildings to give between 1,000 and 5,000 tons per location). The secondary warehouses will largely replace facilities which previously had been provided by wholesalers. AFC's proposal to own its storage facilities is justified, because it will allow AFC to reduce its loss percentage from what it would otherwise have been and to streamline its labor force and transportation. If the fertilizer program is to be successful it will be vitally important that shipments in and out of store can be affected as quickly as possible during the time of peak fertilizer demand. The benefits from getting fertilizer to the retailers on time rather than slightly late are enormous.

30. Direct savings from replacing rented warehouses with purpose-built facilities are difficult to estimate precisely. However, the amount saved annually by replacing three small rented facilities with a purpose-built 1,000 ton facility might be as follows:

Estimated Savings from Constructing a 1,000 Ton Warehouse

	<u>US\$</u>
2 night watchers /a	960
Rental Charge Saved /b	1,000
Reductions in Expected Loss from 1-1/2% to 1%	<u>2,350</u>
Total	<u>4,310</u>

/a Number of guards reduced from 3 to 1. US\$40/person/month including overtime, etc.

/b Based on AFC figures of US\$1/ton/year.

Carefully chosen site may also reduce average hauling distance by US\$36/km.

31. In addition to the benefits derived from owning storage, the other main advantage of AFC's proposed construction will be that it will return storage presently used by AFC to the general market, thus providing additional capacity for the storage of wheat and cotton. It is expected that both of these crops will be substantially expanded as a result of the project, but no specific storage components for them have been included.

Diversification of AFC

32. AFC has prepared tentative proposals to provide for using the organization as a basis for expanding agricultural input facilities in Afghanistan. AFC already acts as a distributor of wheat seed for the Ministry of Agriculture through its system of retailers, and it is expected that it will be used as a distribution organization for agricultural chemicals and possibly for agricultural equipment. The new warehouses which AFC plans to have constructed would be of a general purpose design and so would be suitable for storage of items other than fertilizer if required.