

AFGHANISTAN

Recent developments

Table 1 2019

Population, million	38.0
GDP, current US\$ billion	19.3
GDP per capita, current US\$	507.1
Poverty headcount ratio ^a	54.5
School enrollment, primary (% gross) ^a	72.5
Life expectancy at birth, years ^b	64.5

Source: WDI, Macro Poverty Outlook, and official data.

Notes:

(a) Afghanistan Living Condition Survey (ALCS) (2016-2017).

(b) Most recent WDI value (2018).

Afghanistan experienced moderate growth in 2019 as the agricultural sector recovered from the impacts of drought. However, the economy is estimated to have contracted sharply in the first half of 2020 due to economic disruptions associated with nation-wide lockdowns, border closures, and declining remittance inflows. Medium-term prospects are subject to high levels of uncertainty, related to the COVID-19 pandemic, peace talks and future international security and aid support. Given the shock to the economy poverty is expected to increase in 2020.

After a relatively strong performance in 2019 (3.9 percent growth), the economy contracted in the first half of 2020. Over 2019, growth was mainly driven by recovery in the agriculture sector (17.5 percent) following drought in the previous year. This good performance, together with a moderate expansion of industry (4.8 percent), offset a decline in services (-1.4 percent). However, the economy contracted sharply in the first half of 2020, largely reflecting the impact of the COVID-19 crisis. Lockdowns hampered domestic production and consumption (especially in urban centers). Border closures disrupted exports and supply chains, and remittances declined significantly. While wheat production grew significantly, driven by favorable weather conditions, this was insufficient to offset the large negative impact of COVID-19 on other sectors of the economy.

Inflation was low in 2019 (averaging 2.3 percent) but it increased significantly in 2020. In March and April 2020, panic buying and import disruptions drove a significant spike in food prices and led the government to adopt administrative measures to prevent price gouging and distribute emergency wheat supplies. As a result, headline and food inflation have since declined, standing at 5.3 percent and 10 percent on average respectively, as of end June.

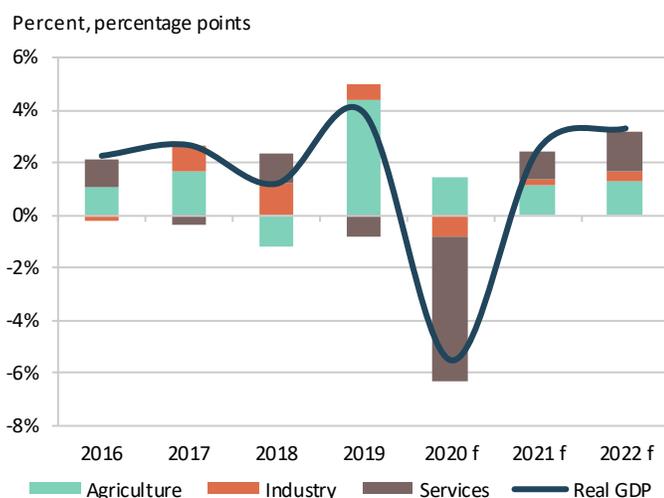
Afghanistan recorded a current account surplus in 2019 and in the first half of

2020. In 2019, the trade deficit narrowed to 30.4 percent of GDP (from 34.7 percent in 2018), as stronger domestic agricultural production drove a 7.1 percent drop in imports. With large grant inflows, the current account registered a small surplus of 0.6 percent of GDP in 2019. Over the first quarter of 2020 exports grew by 11 percent (year-on-year) reflecting the improved performance of air corridors, while weak domestic demand led to a 14 percent decline in imports. In the second quarter of 2020, both imports and exports fell precipitously given border closures and disruptions to trade and transportation, with greater absolute declines in imports driving an improvement in the trade and current account balances.

Fiscal imbalances that appeared in 2019 were aggravated in 2020. Domestic revenues reached a record high of 14.2 percent of GDP in 2019, largely driven by significant one-off revenues, including a transfer of operating profits from the central bank (Afs 24 million, equivalent to 1.6 percent of GDP). However, increased expenditures, mainly driven by salaries and wages, led to a deficit of 1.1 percent of GDP. With the onset of the COVID-19 crisis, weak economic activity, disruptions to trade and compliance, revenue performance deteriorated significantly and revenue estimates for 2020 were revised downward by over 30 percent (from Afs 209 to 144 billion) in the budget mid-year review. Total domestic revenue collection at end-June reached Afs 74.7 billion, 20 percent lower than the initial budget target.

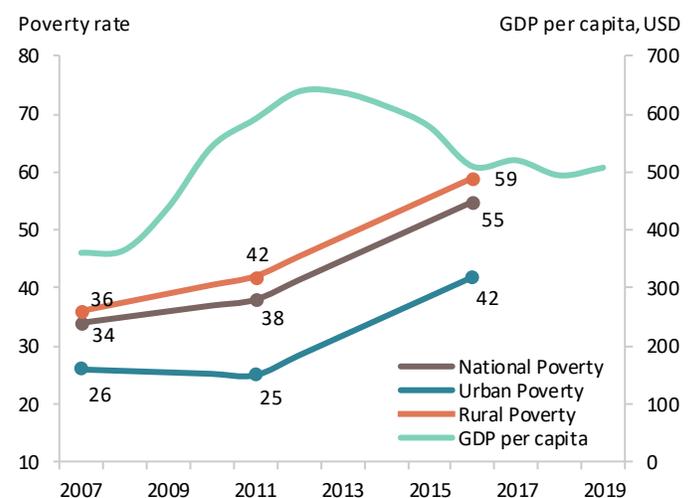
Poverty is believed to have worsened in 2019 surpassing 54.5 percent (in household

FIGURE 1 Afghanistan / Real GDP growth and contributions to real GDP growth



Sources: World Bank, Macroeconomics Trade and Investment Global Practice.

FIGURE 2 Afghanistan / Actual poverty rates and real GDP per capita



Sources: WDI, NSIA, Official data, and ALCS (2016-2017).

survey 2016-2017), amidst continued violence and political uncertainty. In the first half of 2020, with declining households incomes due to economic hardship, higher food prices due to COVID-19, a significant fall in remittances, and high returnee flows (mainly from Iran), poverty is estimated to have further increased.

Outlook

Real GDP is expected to contract by 5.5 percent in 2020, largely due to the impacts of the COVID-19 crisis. In following years, the pace of recovery is expected to be constrained in a context of continued insecurity, uncertainties regarding the outcome of planned peace talks, and questions about the level and duration of international security and aid support.

External balances are expected to improve in 2020, against a backdrop of declining trade activity. The trade deficit is projected to narrow to 26 percent of GDP down from 30.4 percent 2019. While exports are projected to fall by 24 percent, imports (that are significantly larger) are expected to decline by around 18 percent, reflecting border disruptions, depressed domestic demand, and lower global oil prices. With sustained foreign grants inflows, the current account

is expected to reach a surplus of 4.6 percent of GDP in 2020. However, it is projected to deteriorate over the medium term as grants decline, to a deficit of 2.2 percent of GDP by 2022.

With depressed revenues and higher expenditure needs, the fiscal deficit is projected to deepen to 3.4 percent of GDP in 2020. Over the medium-term, declining grants and overall growth weaknesses will constrain fiscal space, although the implementation of VAT in 2022 should provide a partial offset.

The economic contraction in 2020 is expected to have significant adverse social impacts. World Bank micro-simulations suggest that the combination of reduced incomes and higher prices could drive the poverty rate to as high as 72 percent, despite benefits from robust agricultural production to rural households. Over the medium term, the poverty outlook hinges on the pace of economic recovery and the continued provision of international aid and humanitarian support.

Risks and challenges

The main source of downside risk to the outlook stems from possible further adverse COVID-19 developments. Additional

sources of risk include further political instability, a deterioration of security conditions, uncertainties associated with the planned peace agreement with the Taliban, and precipitous reductions in aid flows. By contrast, on the upside, a sustainable and credible political settlement with the Taliban could help boost growth, confidence and private investment.

Given Afghanistan's declining revenues and constrained fiscal potential, public expenditures need to be carefully directed to protecting the vulnerable, limiting long-term economic damage, and establishing solid foundations for economic recovery. To support households, the government should prioritize: i) targeted social protection measures; and ii) ensuring the continued provision of basic services, especially healthcare. To support the private sector, priorities include: i) pursuing business regulatory reforms to facilitate new investment; ii) expanding access to credit; iii) ensuring the continued provision of basic infrastructure; and iv) avoiding accumulating arrears to private sector vendors. A clear commitment from international partners to continued grant support would help reduce uncertainty and improve confidence and investment, providing a vital underpinning for Afghanistan's recovery from the already-severe impacts of the COVID-19 crisis.

TABLE 2 Afghanistan / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2017	2018	2019	2020 e	2021 f	2022 f
Real GDP growth, at constant market prices	2.6	1.2	3.9	-5.5	2.5	3.3
Private Consumption	3.5	10.0	-2.0	-9.0	7.0	3.0
Government Consumption	3.3	-17.8	15.0	6.2	2.6	2.5
Gross Fixed Capital Investment	19.4	0.0	-15.3	-30.8	-3.6	4.1
Exports, Goods and Services	0.5	49.6	-6.3	-21.4	19.0	8.0
Imports, Goods and Services	9.8	13.1	-6.8	-16.3	13.0	3.0
Real GDP growth, at constant factor prices	2.3	1.2	4.4	-5.5	2.5	3.3
Agriculture	6.4	-4.4	17.5	5.0	3.5	4.0
Industry	9.2	11.1	4.8	-6.8	2.0	3.0
Services	-0.7	1.9	-1.4	-10.6	2.0	3.0
Inflation (Consumer Price Index)	5.0	0.6	2.3	5.0	4.2	4.5
Current Account Balance (% of GDP)	2.4	2.7	-0.1	4.6	-1.6	-2.2
Net Foreign Direct Investment (% of GDP)	0.2	0.5	0.0	0.0	0.0	0.1
Fiscal Balance (% of GDP)	-0.6	0.8	-1.1	-3.4	-2.2	-0.9
Debt (% of GDP)	6.6	5.8	6.6	8.6	9.6	9.6
Primary Balance (% of GDP)	-0.5	1.8	-0.4	-3.0	-2.2	-0.9

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices.
Notes: e = estimate, f = forecast.