

POLICY BRIEF

WHAT DOES IT MEAN TO TAKE CONTEXT SERIOUSLY FOR ENGAGING IN MARKETS?

Lessons from Afghanistan

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Why it matters

Throughout 2001–2021, many millions of dollars were spent on an economic transformation of Afghanistan that never happened. Investment was based on an implicit theory of how markets worked and how markets could drive the economy: those assumptions were false. Economic and agricultural development policy can't work without understanding how Afghan markets work.

What aid programmers got wrong

Interventions focused on the supply-side, on investing in infrastructure, on training and on promoting value chains. It was assumed this would smooth access to markets and give producers better prices.

It was also assumed that rural Afghans seek to maximise income. Better market prices for agricultural produce would encourage more investment in agriculture and lead to higher productivity. This would result in higher incomes and economic growth.

What was wrong with the assumptions?

Price competition does not drive markets in Afghanistan, which have a long history. Traders at all levels compete for 'market power'. Profit on trade comes from the application of market power to dictate more profitable terms. This includes leveraging political connections to avoid taxes or to create new taxes for competitors; and using farmers' need for credit to lock them into contracts where farmers are forced to sell produce back to the traders at a disadvantageous price. There is no such thing as 'the price' of any good in markets in Afghanistan. There are different prices, with different conditions for different people.

Markets are sources of opportunity – and risk. The rural poor have limited ability to take risk, so they make decisions that are less profitable to increase the security of their survival. Better market opportunities alone cannot set them free to be entrepreneurs.

Policy implications: getting it right

- There is no blueprint for market interventions in Afghanistan, but there are smarter ways of engaging with the context that will give a much better chance of getting it right.

- Profit in the market comes from market power, not just trade – the ability to manipulate markets, to access credit, etc. There is good, clear literature on power in markets in Afghanistan, which should be read and discussed by all those engaging in market interventions.
- Those with market power have successfully resisted attempts to make markets more ‘free’. Aid programmers should not intervene until they understand how their intervention might also be derailed and what they can do about it.
- Market interventions cannot deliver economic transformation because asset-poor households are not driven only by market opportunities. They often choose low-risk activities with lower returns. Interventions should focus on reducing the risks of more profitable choices at local level.
- Realism is needed in designing market interventions and agricultural development programmes. Progress is possible, but it will be slow and local.

Why context matters

Much of the investment for the attempted economic transformation of Afghanistan in 2001–2021 relied on a theory of how markets would work in the country that was never made explicit. It is likely that this is because market theories are so engrained in thinking in some sectors that they are seen as economic laws of cause and effect, akin almost to laws of physics; it was perhaps not even realised that these are actually social theories about how people and institutions might behave in reaction to certain interventions. Had it been recognised that an implicit social theory was being used, more attention might have been given to its plausibility in Afghanistan. The investment of billions of dollars failed to achieve significant change, and this is largely because so little attention was given to how markets actually worked in Afghanistan, and how they were likely to react to the proposed interventions.

The conceptual framework behind the description, planning and promotion of agricultural commodity markets was a simple abstract model of supply and demand. Price competition was assumed, so that prices were driven by supply and demand; and price signals, in turn, drove investment decisions and ensured a distribution of benefits to producers, workers and consumers. Interventions for market support focused on the supply side, investing in infrastructure, training for producers and promoting value chains within a light regulatory framework. If challenges faced in bringing products to market could be smoothed away, it was assumed that this would unlock the advancement of entrepreneurial activity. The entrepreneurial spirit was assumed to exist, because, again, it was not appreciated that unscrutinised social theories were implicitly being advanced about what actually drives decision-making and economic behaviour of different people. The

planning and design of investment ignored the social institutions that underpin and regulate real markets in Afghanistan and the ways in which these structured markets and shaped exchange relations.

What is Afghanistan’s market context?

Western-led market development efforts did not enter virgin terrain. Afghanistan has long been part of transnational trading networks and integrated into regional markets to both the north and south through cash, credit and debt relations. But the simple act of trading is not necessarily evidence of price competition driven by supply and demand. Afghanistan’s market structures then, as now, can be characterised as more predatory, rent-seeking and patronage-based than open and competitive. Profit is made by being able to maintain one’s position in the market, through trade or arbitrage, and it does not have to depend on transforming production. In some ways, markets behave more like those where there are cartels or monopolies at some point of the chain, licit or illicit, including in markets such as oil and gas, markets dominated by technology giants and organised crime. Traders who benefit from their place in such markets have tended to resist the integration of markets that introduce competitive imperatives.

Afghan commodity markets are a mix of informal, formal, illicit and aid-driven elements. Key actors straddle the political and economic ‘marketplaces’, using their position in one marketplace to strengthen their position in the other. Even at the microlevel, hierarchical social relations and informal regulatory practices structure the flows of commodities, labour and money (through informal credit relations). These social and power relations determine the distributional outcomes for the various actors engaged in the market. (This is perhaps

a major difference between Afghan markets and two of the examples given of non-competitive markets in other economies. Domination in the oil and gas markets and in markets dominated by tech giants is played out in economic and political spheres: of the three examples given above, only organised crime compares to Afghan markets in that it tends to include embedded *social* relations in its rules.)

If this is understood, then it is more obvious that farmers in Afghanistan were not simply entrepreneurs-in-waiting, an assumption that *had* to be true if the planned agricultural and economic transformations were to take place. Markets are not just a source of opportunity, but also one of the greatest sources of risk for farmers. Markets cannot be free, and prices cannot be set solely by supply and demand, if producers are so often locked into exploitative economic relationships, often through informal credit relations. Such relations mean that farmers are often not free to sell their labour or their produce where they wish, but instead are forced to sell them where they have debts or dependent relations of other kinds – at prices set by the patron. Afghan farmers did indeed engage in markets in 2001–2021, but their primary inclination was to secure their subsistence needs, not to risk those in to order to maximise potential profits. With few assets and a limited buffer against price fluctuation, many poor households will often choose low-risk activities even though these have lower returns.¹

Understanding how markets work

Mainstream economic theory often measures market performance by price correlation across markets. High price integration is a key indicator that markets are functioning efficiently and competitively.² Field observations in commodity markets in Afghanistan point to very high daily levels of price volatility (Minoia and Pain, 2017). There is no ‘price’ set by simple supply and demand, because traders can manipulate prices. Prices do not only vary from day to day, but also from client to client, because the price depends on who you are. This of course makes market price analysis very difficult, and research into the poultry market in Nangarhar found prices were simply impossible to track, partly because of the secrecy involved (Pain et al., 2022). The term ‘mafia’ is often used to describe the powerful market traders there who control and manipulate prices through anticompetitive informal agreements, backed by political connections which in turn limit competition between traders. They can ensure that very few small traders can ever become big traders.

Other mechanisms also limit free price setting (i.e., only by supply and demand). Almost all farmers depend on access to informal credit to acquire inputs. The grower or producer is required to sell back the product to the credit giver at a pre-set price in what is termed an interlocking contract. The trader profits on both transactions. This phenomenon is pervasive in Afghanistan. Farmers are thus tied into both input and output markets on disadvantageous terms, enforcing unequal access to markets.

Ethnic identity and geography set the scope of trade for any individual trader. The more powerful traders are connected to the provincial political elite and their networks and so have broader opportunities. There are close relationships between the economic and political marketplaces, consistent with the ‘mafia’ characterisation of key market traders. Powerful actors hold prominent positions in both spheres and use them to further their interests. For example, big onion traders in Afghanistan used political connections to evade cross-border taxes and checks (both formal and informal) which their competitors cannot avoid, consolidating their dominant market position. Key traders in the poultry trade operated in a similar manner, with respect to both feed and other inputs.

Rural and urban labour markets are also governed by personal rather than impersonal relationships, because they are a part of the social relationship and thus reflect social inequalities. Wages – often paid in-kind – are determined by custom more than by supply and demand, and they are segmented by gender, age, locality. Dependent relationships arise in part because most rural labour markets are oversupplied. There is no need for employers to compete on price. Those selling labour require goodwill to be hired even at exploitative rates. The one exception observed in Afghanistan is the labour market for harvesting opium, where the skills required, the importance of timing and the altitudinal spread of harvest dates dramatically tripled labour wage rates and increased the number of working days. No other crop will have those multiplier effects.

What does ‘taking context seriously’ mean when engaging in markets?

The picture of market functioning presented here comes from knowledge that had already been documented at the time investments in markets were made. If what was known about markets was not taken seriously, that

1 An attraction of opium poppy cultivation is that it is a relatively low-risk crop in a high-risk environment, given the market support it has provided through credit and farm gate purchase.

2 High integration means that price movements in any one market are similar to those in other markets.

cannot be because the information wasn't there. There are deeper reasons why context gets ignored, which are discussed in the companion paper in this series, 'Ten traps to avoid if aid programming is serious about engaging with context: lessons from Afghanistan' (Levine and Pain, 2024).

It is necessary to appreciate the entrenched set of unequal power relations that have shaped market activity. Those with power fight to hold on to their power, because that is the source of their profits. Understanding how this can play out should inform how interventions for market development are designed, including their horizons and ambitions. External market reforms are unlikely to lead to the rapid transformation of the economy.

Interventions cannot look simply to support farmers to sell to the market. The structures of markets have to be engaged with. Approaches need to incorporate an understanding of how and where profits are currently extracted – e.g., through market manipulation and socially regulated access to credit. Understanding how benefits of trade are currently distributed makes it clear that growth in agricultural production alone will not easily translate into poverty reduction.

The starting point for planning cannot be a theoretical economic analysis of the marketplace, i.e., a market following free market principles. The starting point must be the poor rural household itself. The risks they face in relation to markets and market prices give them good grounds for limiting their engagement in markets. Interventions and policy design must look at the different uncertainties that these households face and seek to

reduce them. The rural poor often have to sacrifice the future to guarantee the present, so measures must offer benefits that are felt quickly.

Risks vary from place to place and from household to household. To understand people's specific risks and what could be done to reduce them, 'participation' and 'consultation' must avoid the standard formulaic exercises. A more gradualist approach could allow local markets to 'thicken' locally over time, rather than focusing on grander efforts at the national level.

However, such measures do not address the politically saturated nature of markets and the broader nature of the risk environment. There needs to be greater realism as to the extent to which market interventions can bring about systemic and broader-scale changes to widen the benefits of market growth. There are fundamental challenges of interventions 'coming to scale' and the mid-level programmes that donor support can do little to address.

Arguments for realistic expectations can be unwelcome on every level. In Afghanistan, there was a political demand to remake society and the economy – and a demand to use huge volumes of aid in order to achieve this. Instead of a genuinely plausible pathway to change, there is a drive instead for a pseudo-plausible narrative that promises success. This is driven by the needs of every actor, from political elites in both donor and recipient countries, to the agencies seeking funds and local actors. The call to take context seriously is akin to a counter-revolutionary narrative. Combating this demand to promise quick success is a political challenge, not a technical one.³

3 See the companion paper (Levine and Pain, 2024) for further discussion on the political reasons for excluding contextual understanding in decision-making.

References

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Additional reading

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About this series

This paper is based on a briefing note written for the United Kingdom's Foreign, Commonwealth and Development Office (FCDO), and this version is published with their permission. It is one of series of five papers designed to help decision-makers to integrate a better understanding of Afghanistan into their work. The other papers in the series cover Community Development Councils, rural differentiation, informal credit and post-harvest storage and processing.

Based on the analysis of these five papers, an overview paper examines why it has proved so hard for aid actors to take context seriously (Levine and Pain, 2024). It identifies 'Ten traps to avoid if aid programming is serious about engaging with context: lessons from Afghanistan'. Although based on a study of the failure to take context seriously in Afghanistan, the paper is written to be of wider relevance.

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