

SIGAR

**Special Inspector General for
Afghanistan Reconstruction**

OFFICE OF SPECIAL PROJECTS

**KABUL CARPET EXPORT CENTER: PROGRESS
MADE TOWARD SELF SUFFICIENCY BUT
CRITICAL SALES, REVENUE AND JOB CREATION
TARGETS HAVE NOT BEEN MET**



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The Honorable John Barsa
Acting Administrator
U.S. Agency for International Development

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Mission Director for Afghanistan
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Developing the Afghan economy is a significant focus of the U.S. reconstruction mission in Afghanistan. In support of that mission, the United States Agency for International Development (USAID) initiated the Afghanistan Job Creation Program. The Program provides grants to help develop different sectors of the Afghan economy. To develop the carpet industry, USAID awarded a \$9.4 million grant to the Charleston, SC based Impact Carpet Associates LLC (ICA) to establish the Kabul Carpet Export Center (KCEC).

The purpose of the KCEC project is to develop a self-sufficient Afghan company to connect Afghanistan's carpet manufacturers with international buyers. During the course of the five-year award 2018-2023, the project receives \$9.4 million in USAID funding for the first three years, with two years of additional technical guidance provided by USAID. According to the grant agreement, KCEC is required to facilitate all steps of the sales process, such as connecting international buyers with Afghan carpet weavers, providing financing services to carpet makers for the purchase of raw materials, and handling quality control and export processes. In addition, ICA is required to establish a fully operational carpet export center and meet sales, revenue and job creation targets. SIGAR initiated this review to determine what progress has been made toward establishing a fully operational KCEC and specifically, whether sales, revenue, and job creation targets were being met.

ICA successfully met most benchmarks associated with establishing the Kabul Carpet Export Center. Specifically, ICA registered KCEC as a local company in Afghanistan, developed work and monitoring & evaluation plans, conducted a baseline stakeholder survey and established product tracking capabilities. However, ICA has not developed a secure e-commerce capability on its website, which limits buyer's ability to initiate orders online, and they have not engaged with the Afghan government to address burdensome airfreight policies as agreed to in the grant agreement. In addition, ICA's efforts to develop a financing program to help weavers finance raw material purchases did not adequately consider Afghans' refusal to accept interest bearing loans because of religious beliefs. This oversight undermined a key goal of the project, to provide Afghan carpet manufacturers the capital that would help free them from reliance on Pakistani middle men.

In addition, KCEC has not achieved its sales, revenue and job creation targets. Despite receiving a six-month extension (from May 31, 2019 to November 30, 2019), the KCEC could not meet its first year targets of \$714,286 in sales, \$48,000 in revenue and the creation of 5,715 new jobs.¹ The second year target is to double sales and revenue, and create an additional 5,715 new jobs. As of April 1, 2020, KCEC has reported that it has generated \$717,030 in sales, \$41,836 in revenue and created 8,825 new jobs. With 3 months until the end of the second year (extended to June 30, 2020) and the COVID19 worldwide pandemic causing trade shows to be cancelled, there is little chance to achieve these targets, thereby placing KCEC's ability to become self-sufficient by June 5, 2021 in jeopardy.

To improve KCEC's chances for greater self-sufficiency as a viable commercial enterprise, we recommend that the USAID Mission Director or his designee (1) direct ICA to immediately update KCEC's current website to include an HTTPS security protocol and a comprehensive and secure public e-commerce capability for all current and potential clients; (2) in conjunction with ICA, establish new targets for performance and job

¹ According to the grant agreement, KCEC's revenue will come from the fee it charges carpet makers for any of its services, while sales is the total cost of all carpets exported out of Kabul Airport using KCEC services.



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creation and assess KCEC ability to achieve financial self-sufficiency by June 2021. The assessment should include a reevaluation of KCEC's marketing, sales, and operational strategies; and (3) reassess the financing program and consider setting up a system that conforms to prevailing lending norms of the Afghan carpet industry.

We provided a draft copy of this report to USAID on July 20, 2020. We received comments from USAID on August 10, 2020. USAID agreed with SIGAR's first two recommendations on enhancing KCEC's website security protocols, establishing e-commerce capabilities, setting new performance and job targets, and reevaluating KCEC's sales and marketing strategies to achieve self-sufficiency. USAID reported that, prior to issuing their agency response, they issued a modification to the grant that canceled KCEC's loan portfolio and reprogrammed the funds to provide financial assistance to carpet weavers and traders, fund more training sessions for the Afghan carpet industry stakeholders and sponsor new tradeshow. Therefore, the third recommendation in the draft report, which recommended that USAID reassess the financing program and consider setting up a system that conforms to prevailing lending norms of the Afghan carpet industry, was closed as implemented and removed from this report. USAID's comments are reproduced in appendix I.

We conducted this review in Washington, D.C., in accordance with the *Quality Standards for Inspection and Evaluation January 2012*, Council of the Inspectors General on Integrity and Efficiency. SIGAR performed this work under the authority of Public Law No. 110-181, as amended, and the Inspector General Act of 1978, as amended. Should you or your staff have any questions about this project, please contact Mr. Benjamin Piccolo, Director of Special Projects, at (703) 545-2192 or benjamin.j.piccolo.civ@mail.mil.

Sincerely,

A handwritten signature in black ink, appearing to read "John F. Sopko".

John F. Sopko
Special Inspector General
for Afghanistan Reconstruction

Afghanistan's handmade carpets are known worldwide for beauty and durability. In 2018, carpet sales accounted for 2.5% of the country's total exports.² Decades of instability and its effect on the Afghan economy has resulted in Pakistan receiving many of the benefits of the Afghan carpet industry. Pakistani companies created a sales strategy that uses the skills of the Afghan weavers in Pakistani refugee camps by providing them the yarn for the rug on credit, and later finishing and packaging the rugs for export with the label "Made in Pakistan". The relationship continues to flourish even after millions of Afghan refugees (among them carpet weavers) returned to Afghanistan after 2001, when the United States-led coalition forces toppled the Taliban regime. The need for capital to buy wool, a dearth of the skills needed for proper packaging, excessive customs red tape, and a disconnect between Afghan manufacturers and the global carpet industry are critical factors that keep Afghan carpet manufacturers tied to the Pakistani wholesalers.

Developing the Afghan economy continues to be a primary focus for the U.S. government and the U.S. Agency for International Development (USAID). As part of its efforts to develop the Afghan economy and spur job creation under the Afghanistan Job Creation Program (AJCP), USAID has awarded a grant to establish the Kabul Carpet Export Center (KCEC).³ The stated goal for the KCEC project is that it will "place the theory and practice of the Pakistani rug making and distribution model directly into the hands of the Afghan carpet trade participants themselves, thereby creating a true 'Made in Afghanistan' product," and creating thousands of jobs.⁴

The objectives of SIGAR's review are to determine whether (1) a fully operational KCEC was established, and (2) sales, revenue and job creation targets were achieved.⁵ To answer these two objectives, we reviewed the documentation the implementing partner—Impact Carpet Associates LLC—submitted to USAID as support for achieving key milestones and sales, revenue and job creation targets. We also interviewed representatives of USAID; and the sub-awardee responsible for KCEC's day-to-day operations, the Oxus Group. Through the interviews SIGAR clarified grant documents, requested more information from stakeholders, and attempted to establish a better understanding of the day-to-day operations of KCEC and the challenges it faces in creating a self-sufficient carpet export center.

Background

USAID initiated the Afghanistan Job Creation Program (AJCP) in June 2017 to generate revenue and sustainable jobs by supporting Afghanistan's value-chain development – industries with growth potential to identify and help create competitive opportunities, and to help Afghan businesses increase exports. The program funds multiple awards, with the value of individual grants ranging from \$2 million to \$10 million. On June 6, 2018, USAID awarded Impact Carpets Associates LLC (ICA) a firm-fixed grant of \$9.4 million to establish the Kabul Carpet Export Center.

The KCEC, registered as an Afghan company, was established to assist Afghan carpet makers by helping solve three major problems facing the indigenous carpet industry: (1) burdensome processes to airfreight carpets from Afghanistan, (2) a lack of access to export financing, and (3) the absence of a direct linkage and web-based market for overseas wholesale buyers. It also acts as an intermediary between international buyers and sellers (i.e. carpet manufacturers) until the end-product is inspected, packaged, and shipped to its final destination from the Kabul Airport.

² United Nations Statistics Division, "2018 International Trade Statistics Yearbook," ST/ESA/STAT/SER.G/67 (Vol. I), 2018, p. 32.

³ The AJCP is a USAID initiative intended to fund up to 12 awards for projects set to be implemented by 2022. The main objectives of AJCP are 1) to generate revenue and sustainable jobs by supporting value chain development and 2) to support trade promotion and facilitate Afghan businesses in increasing exports. The AJCP provides prospective applicants with a fair opportunity to develop and submit competitive applications to USAID for review and potential funding.

⁴ USAID, Establishing Kabul Carpet Export Center, 720-306-18-FA-00006, awarded to Impact Carpet Associates LLC, June 6, 2018, p. 28.

⁵ According to the grant agreement, KCEC's revenue will come from the fee it charges carpet makers for any of its services, while sales is the total cost of all carpets exported out of Kabul Airport using KCEC services.

ICA, a U.S. based firm, is responsible for establishing the Kabul Carpet Export Center, administering the award, and ensuring any use of the award’s funding is consistent with underlying agreements, program objectives, and the terms and conditions of the award. ICA has subcontracted with a number of companies to assist in the implementation of the award. These companies and their responsibilities under the contract are outlined in Table 1.

Table 1: KCEC’s Original Prime and Sub-Awardees

Firm	Status	Role
Prime Awardee		
Impact Carpets Associates, LLC (ICA)	Prime Awardee US Small Business	<ul style="list-style-type: none"> Overall project management compliance, quality control, and client communication Monitoring and Evaluation
Sub-Awardees & Vendors		
The Oxus Group (OXUS)	Lead Sub-Awardee US Small Business with Afghan Subsidiary	<ul style="list-style-type: none"> Day-to-day project delivery All Afghan project personnel
Afghan Growth Finance (AFG)	Afghan Business	<ul style="list-style-type: none"> Responsible for vetting carpet makers Making loans and managing repayment to small carpet makers Ensure collection of fees for KCEC
Afghan Rug and Carpet Center (ARCC) ¹	Afghan Business	<ul style="list-style-type: none"> Warehousing and related equipment
Emerging Consulting, LLC (EC)	US Small Business with Afghan Subsidiary	<ul style="list-style-type: none"> Financial management and reporting Compliance with USAID grant agreement terms
Paxton International	US Business	<ul style="list-style-type: none"> Shipping between KCEC and Kabul Airport including export formalities

¹ Afghan Rug and Carpet Center (ARCC) was the sub-awardee responsible for handling all warehousing and equipment needs, but in July 2019 Oxus Group absorbed these tasks too. ICA told SIGAR ARCC did not attend meetings or partake in the business per the contractual requirements, thus it decided to let ARCC go and handed over its tasks to Oxus Group.

Source: USAID, Establishing Kabul Carpet Export Center, 720-306-18-FA-00006, awarded to Impact Carpet Associates LLC, June 6, 2018, p. 44.

According to the grant agreement, in its first year of performance KCEC is required to generate \$714,286 in sales and create 5,715 new jobs (4,351 weavers, 1,364 support jobs). In its second year of performance KCEC is required to generate \$1,428,571 in sales, and create another 5,715 new jobs (4,351 weavers, 1,364 support jobs). In its last year of USAID funding, KCEC is required to produce an additional 34,286 jobs and increase its yearly sales to \$5,741,286.

By the end of the program’s three years of USAID funding, KCEC is expected to generate \$7.98 million in sales and create more than 45,000 new jobs. By the end of the program’s five-year strategy, KCEC is projected to have \$23.5 million in sales and create 68,572 jobs. KCEC charges a fee of 7% of the final export’s cost for its services and is required to generate \$48,000 in fees from operations in its first year, followed by \$96,000 and \$384,000 in its second and third years of operation respectively. The program’s targets for job creation, export sales, and revenue are summarized in Table 2.

Table 2: KCEC Targets for Job Creation, Export Sales, and Revenue

New Jobs	USAID Funded Project Years			Post-USAID Funding	
	Year 1	Year 2	Year 3	Year 4	Year 5
Weaving	4,351	4,351	26,104	8,701	8,701
Support	1,364	1,364	8,182	2,727	2,727
Total Number of Jobs	5,715	5,715	34,286	11,428	11,428
Export sales	\$714,286	\$1,428,571	\$5,714,286	\$7,142,857	\$8,571,429
KCEC Revenue ²	\$48,000	\$96,000	\$384,000	\$480,000	\$580,000

² The fee revenue target that KCEC is assessed against is the award listed goal, minus a 4% business tax (i.e. the contract lists slightly bigger targets for years 1-5 with goals of \$50,000; \$100,000, \$400,000; \$500,000, and \$600,000 respectively).

Source: Kabul Carpet Export Center

The grant is structured with ICA receiving direct USAID funding for the first three years of the program, with continued USAID supervision and technical guidance provided in the fourth and fifth years. The project has 38

milestones over the course of its three-year lifecycle from June 6, 2018 to June 5, 2021. The twenty-six milestones of the first two years, (14 for the first year, and 12 for the second year) focus on getting the KCEC up and running, establishing relations with carpet makers as well as potential clients abroad, and meeting initial sales, revenue, and job creation targets. See appendix II for a listing of the milestones.

As of June 1, 2020, USAID has disbursed \$4.66 million to ICA in connection with the program successfully meeting milestones. The milestones included the establishment of a fully operational export center, setting up a loan financing program, training Afghan carpet manufacturers, and attending trade shows with a goal of achieving sales, revenue, and job creation targets. The USAID funded period of the award is broken into three “project years” signifying different stages of the project, with KCEC established and beginning operations in project year one (originally June 6, 2018 to May 31, 2019), expanding KCEC operations during project year two (originally May 31, 2019 to May 31, 2020), and KCEC becoming financially independent by the end of project year three (originally May 31, 2020 to April 30, 2021). The original agreement has been modified to adjust the deadlines for achieving project year one sales, revenue and job creation targets from May 31, 2019 to November 31, 2019 and year two sales, revenue and job creation targets were moved from May 31, 2020 to June 30, 2020.

Despite Meeting Several Milestones, KCEC is not Fully Operational

The grant agreement required ICA to establish a fully operational KCEC by December 15, 2018. Actions required for KCEC to become fully operational included (1) registering KCEC as a local company in Afghanistan, (2) developing work plan, public relations plan, and monitoring and evaluation plans, (3) conducting a baseline stakeholder survey,⁶ (4) developing e-commerce capabilities, (5) establishing product tracking capabilities via a barcode system. In addition, the grant stipulated that ICA would work with the Afghan government to streamline export regulations.

Several positive steps have been taken to launch KCEC, and SIGAR found that ICA met 4 of the 6 requirements of the grant agreement. For example, in 2018 ICA created and registered KCEC as an Afghan company, securing a business license from the Ministry of Commerce and Industries. In conjunction with their registration, ICA opened a KCEC office in Kabul and developed a barcode system that would provide a tracking functionality. KCEC also conducted a baseline stakeholder survey to identify perceptions, priorities and areas for improvement in the Afghan carpet sector as determined by industry experts, manufacturers and other stakeholders. This information was collected in order to further guide the activity of KCEC to ensure the program’s maximum positive impact. Additionally, ICA submitted to USAD documents related to marketing, loan management, carpet exports, and reporting requirements as well as its monitoring and evaluation plan. Meeting these requirements were important steps towards establishing the foundation of the KCEC program. The completion of these milestone requirements largely fulfilled the goal of establishing the KCEC, however, the goal of achieving full KCEC operationally has not been met. To date, ICA has not integrated e-commerce capabilities into its website, nor has it engaged with the Afghan government to advocate for the streamlining of export regulations—two milestones required to achieve fully operational status.

KCEC has not developed a Secure Website with e-Commerce Capabilities

In accordance with the grant agreement, KCEC was required to develop a website with capabilities that will give international buyers “the ability to order direct[ly] from Afghan carpet producers.” The current website does not have this capability. The KCEC website handles all information traffic over an unsecured HTTP network protocol. We tested the KCEC website using each of the four major internet browsers (representing

⁶ A baseline stakeholder survey is meant to identify perceptions, priorities and areas for improvement in the Afghan carpet sector as determined by industry experts, manufacturers and other stakeholders.

over 85% of all web searches) and each browser flags a warning to the site visitor that the website is not secured and could put their information at risk.

The KCEC website also does not have e-commerce capabilities that allow individual consumers to purchase a carpet directly through the website, nor can a prospective client initiate an order online. KCEC representatives told SIGAR that its first year sales approach was primarily to work with wholesalers in North America and Europe, as opposed to selling directly to retailers or consumers. To date all sales have occurred either at trade shows, or via direct outreach by KCEC staff to international wholesalers, many of which ICA had pre-existing business relationships. The KCEC representative told us that after the first year the project expanded its strategy to sell directly to retailers and individual consumers.

Business closures related to the 2020 pandemic have already resulted in the cancelation of two trade shows that KCEC planned to attend. Other trade shows are likely to be cancelled. This necessitates that KCEC find new methods for maintaining current clients and attracting new ones. KCEC representatives told us in May 2020 that they have recently started trying to develop an e-commerce site. However, according to the representatives, its development too has been stalled due to the pandemic. As of June 1, 2020 retailers and consumers were still unable to order carpets online.

ICA has not Engaged the Afghan Government to Simplify Export Procedures

One of the objectives of the KCEC project is to help resolve the burdensome processes to airfreight carpets from Afghanistan. For example, a single carpet must receive a separate export certificate from three different Afghan government agencies prior to shipment. As stated in the grant award, each carpet must undergo multiple inspections, leaving the carpet dirty, damaged, or poorly re-wrapped before it's loaded onto a plane for shipment. The grant agreement states that in order to address the burdensome airfreight policies complicating carpet exports out of Afghanistan, KCEC will assist all relevant Afghan government authorities "to help develop expedited export clearance procedures that eliminate situations where carpets get damaged. KCEC will engage all [Government of Afghanistan] parties that have jurisdiction over carpets to provide assistance."⁷ While ICA had agreed that KCEC will engage in policy advocacy per the grant agreement, its representatives told SIGAR it has made no progress nor taken any action to work with the Afghan government to address to streamline Afghan export laws or policies. A USAID official told SIGAR that KCEC is not in a position to make or influence export policies of the Afghan government but did not explain why policy advocacy is in the performance work statement.

KCEC Has Missed Sales, Revenue, and Job Creation Targets by Wide Margins in Its First Two Years of Operation

According to the grant agreement, the primary objective of the KCEC project was to establish a self-sustaining carpet export center by June 2021 that's capable of linking international buyers with Afghan carpet manufacturers, which would in turn create jobs. However, the KCEC has fallen short of meeting its first year targets for sales and revenue with no indication that it can achieve its second year targets, which places its prime goal of self-sufficiency in jeopardy. The grant funded participation in trade shows to assist carpet manufacturers to develop relationships with international buyers. The grant also incorporated a manufacturer financing program that was intended to serve as a sustainable source of up-front funds for weavers to buy the raw materials and reserve time on rented equipment such as looms. This financing was intended to sever the ties that held manufacturers to Pakistani financiers, and enable Afghan weavers to sell their carpets through the KCEC.

⁷ USAID, Modification Number P002, 720-306-18-FA-00006, awarded to Impact Carpet Associates LLC, July 25, 2019, p. 11.

During its first year, KCEC's target for sales and revenue were \$714,286 and \$48,000 respectively, with sales and revenue targets doubling in the second year to \$1,428,571 and \$96,000. However, due to KCEC's slow start, the agreement was modified on July 25, 2019 to extend the year one deadline to the end of November 2019, giving KCEC an additional 6 months to achieve its first year targets. The second year target was also extended from May 31, to June 30, 2020. However, as of April 1, 2020, KCEC had generated \$717,030 in sales and collected \$41,836 in revenue. Over half of these sales occurred at trade shows – an avenue that will likely become increasingly limited in light of the COVID19 pandemic and the high cost of attendance once USAID funding concludes.

Trade Show Attendance did not Generate Expected Sales

To achieve sales and revenue targets, the grant identified 11 trade shows that KCEC representatives attended to develop relationships with international buyers and to sign sales contracts. ICA received a total of \$1,491,500 from USAID to cover the costs of KCEC personnel and affiliated carpet makers attending these shows. ICA data indicates that on average, KCEC sent four staff members and paid for nine affiliated Afghan carpet makers to set up booths. After each trade show, ICA was required to submit a report documenting KCEC's activities, including KCEC participants, prospective buyers and "after event actions planned."⁸ Of the 11 trade shows attended by the KCEC team, 5 shows with a total average cost of \$677,955 did not result in any sales or Memorandums of Understanding being signed with international carpet buyers. Direct sales occurred at only two of the eleven trade shows, yielding \$418,245 in sales. Table 3 summarizes KCEC's sales activities at the eleven trade shows attended as of December 31, 2019.

Table 3: KCEC Sales Activities at Trade Shows

Name of Carpet Show	Date(s) of Carpet Show	Sales Activities Conducted at the Show
New York Rug Show	August 25-28, 2018	No MOUs, Purchase Orders, Or Sales Occurred
Istanbul Carpet Week	August 23-27, 2018	Four Letters of Intent signed between KCEC and interested buyers indicating the clients' interests in using KCEC to purchase Afghan carpets
Americas Mart Atlanta Area Rug Show	January 8-15, 2019	No MOUs, Purchase Orders, Or Sales Occurred
DOMOTEX, Hannover	January 11-14, 2019	Three MOUs signed between KCEC and potential clients interested in using KCEC to purchase Afghan carpets
DOMOTEX USA, Atlanta	February 28-March 2, 2019	Two MOUs signed between KCEC and potential clients interested in using KCEC to purchase Afghan carpets
DOMOTEX, Shanghai	March 26-28, 2019	No MOUs, Purchase Orders, Or Sales Occurred
The High Point Market, North Carolina	April 6-9, 2019	No MOUs, Purchase Orders, or sales occurred, however, samples purchased and potential retailers informally (not in writing) expressed desires to use KCEC in the future
USAID Afghan Treasures in Italy Luxury Show, Milan	June 26-27, 2019	No MOUs, Purchase Orders, Or Sales Occurred
New York Rug Show	September 7-10, 2019	Four MOUs signed between KCEC and potential clients. An additional Letter of Intent signed between KCEC and an interested buyer indicating plans to use KCEC in the future to buy Afghan carpets. This client, and other two carpet wholesalers, also made direct purchases at the trade show totaling \$100,245.
Afghan Artisan Rug Pop-up, New York	October 31-November 3, 2019	KCEC facilitated \$318,072 in carpet sales at the pop-up Afghan carpet market
3rd Annual Passage to Prosperity, New Delhi	September 24-26, 2019	Five MOUs signed between KCEC and potential clients interested in using KCEC to purchase Afghan carpets

Source: SIGAR Analysis of Kabul Carpet Export Center Documents

⁸ "After event actions planned" outlined the steps KCEC staff would take to build on the relationships they developed at trade shows, and the staff member assigned to implement specific follow-up actions by a determined deadline.

Potential Change to Fee Structure Could Further Undermine KCEC's Prospects for Greater Self-Sufficiency

KCEC's proposed changes to the fees it charges for its services may further limit its ability to achieve self-sufficiency. KCEC earns its revenue by charging a fee for its services which includes handling orders received by KCEC from international buyers, performing quality control, and packing, shipping and exporting the carpets. Initially, KCEC planned to charge a flat fee for each carpet sale it facilitated, equal to 7 percent of the final sale price of the carpet. KCEC struggled to recruit manufacturers interested in KCEC's services at the 7 percent service fee, and as a result only earned \$41,836 in revenue as of April 1, 2020, leaving KCEC short of its year one target and will require KCEC to earn an additional \$102,164 over the subsequent three months to meet its year two target by the end of June 2020.

KCEC reported to USAID that "following the actual implementation of the activity it has been understood that KCEC cannot charge 7% for all types of exports."⁹ In an effort to incentivize more clients, KCEC has proposed to USAID a variable fee structure where the percent fee KCEC earns is based on the scale of services it provides for a specific sale. This change to KCEC's fee structure is still pending USAID approval.

As stated in the grant agreement, the benefit of using KCEC is that it's a "one-stop shop" for international buyers to purchase from Afghan manufacturers. One of KCEC's primary roles is to ensure consistency, with buyers receiving products that were evaluated for quality control and properly packaged. KCEC's involvement throughout the process, instead of "a la carte" option, is intended to increase consumer confidence in the Afghan carpet sector, a lack of which has been highlighted as a major issue by both ICA and USAID. The services that would be offered at various fee rates are summarized in Table 4.

Table 4: Proposed KCEC Service Fee Structure

Services Provided by KCEC	Percentage of Final Export Price
"Full Service"- KCEC facilitates and receives the carpet order from an international buyer, coordinates the order with an Afghan manufacturer, implements KCEC quality control procedures and inspections, packages the carpets for safe transport, and handles the export (including customs procedures) and shipping of the carpet.	7%
KCEC handles the carpet's shipment, including packaging, export and country clearance.	3%
KCEC provides ONE of the following services:	
a) Customs clearance and carpet shipment	1%
b) Packaging and shipment	
KCEC charges no fee for sample carpet shipping or carpets destined for exhibitions and shows.	0%

Source: Kabul Carpet Export Center

KCEC Has Not Met Job Creation Targets and Methodology Is Flawed

KCEC's target was to create 4,351 new weaving jobs in each of the first two years of the project. USAID extended the deadline for meeting the first and second year targets from May 31, 2019 and May 31, 2020, to November 30, 2019 and June 30, 2020. As of April 1, 2020, KCEC reported that it created 8,825 new jobs. The current methodology for measuring the number of new jobs created, uses a formula based on volume of exports, with every 1.5 square meters of carpet shipped creating 0.67 weaving jobs and .21 support jobs (such as sheep herding or wool washing) per square meter of carpet shipped. This measure of KCEC's job creation is in reality another measure of export volume, rather than measuring the number of actual new jobs created. This metric does not accurately measure the program's success in achieving a key goal, and heavily overestimates KCEC's progress toward achieving year one and two job creation targets. To count the number of actual new jobs created under the KCEC program, SIGAR analyzed KCEC records and found that it had actually created 2,414 new weaver jobs as of April 1, 2020 compared to the almost 9,000 weaving jobs reported based on the methodology in the grant agreement. KCEC representatives told SIGAR that they

⁹ Kabul Carpet Export Center, "Realignment the target calculation of the KCEC Indicator #10 'Amount of revenue generated from KCEC Fees-based,'" (memo to file, KCEC), Adobe Portable Document Format.

recognized that the award's initial metric for calculating job creation was not representative of the actual jobs created, therefore it kept additional records to better measure the total number of new jobs created. KCEC has proposed using records of individual weavers to calculate job creation figures instead of the formula-based metric. This revision is included in a revised monitoring and evaluation plan that is pending USAID's approval.

KCEC's Loan Financing Program Has Been Unsuccessful

Currently Pakistani marketing companies commission Afghan weavers and traders to produce carpets at prices that fail to yield significant profits for the weavers. In addition, these large companies often make "arbitrary deductions" which the Afghans involved in the process have "no way to dispute or rectify," resulting in the Afghan members of the value chain receiving far less than expected.¹⁰ The carpets sold by these large companies are eventually labeled as "Made in Pakistan," further undercutting the Afghan carpet industry.¹¹ With KCEC directly providing Afghan carpet manufacturers with financing services, Afghan manufacturers would be both "more assured of [the] return on their work" and more likely to see increased profits. Meanwhile, the broader Afghan carpet sector could begin reclaiming its stake in the international carpet industry by producing a truly "Made in Afghanistan" product.

To this end, ICA subcontracted with Afghan Growth Finance (AGF), to handle the financing service KCEC offers carpet manufacturers. The organization Afghan Growth Finance was renamed AGF Advisors, LLC on July 25, 2019. The target for project year one was for AGF Advisors to issue \$243,409 in loans. According to the grant, manufacturers could obtain a loan through AGF Advisors for up to 35% of the total cost of a carpet sold through KCEC in order to purchase needed materials and reserve loom space. Accordingly, AGF Advisors would charge the manufacturer a "market rate" for its services, and KCEC would pay AGF Advisors an additional fee, equal to 15% of the amount it loaned the manufacturer. However, the program has met significant pushback/resistance from Afghan manufacturers as a result of their refusal to accept interest-bearing loans. Under the Islamic jurisprudence (Sharia), which governs all Afghan laws, charging interest is forbidden – a concept ICA and USAID did not take into consideration when designing the program.

In its annual performance report to USAID, KCEC also reported that carpet manufacturers expressed an aversion to utilizing the KCEC loan because of the high interest rate (7%) and their reluctance to accept such loans given religious restrictions against interest.

In the summer of 2019, KCEC revised its loan program.¹² The new program still did not attract the interest of Afghan manufacturers and did not result in any loans. The lack of success in achieving milestones related to KCEC's financing services indicate KCEC is struggling to achieve a key project goal -- providing Afghan carpet manufacturers the capital that has long tied them to the Pakistani middle men. In April 2020, KCEC informed SIGAR of its request to eliminate the loan financing component of the award and instead the funds would be reallocated to provide grants to a select number of carpet manufacturers who are producing new jobs within the industry, and the remaining funds would go toward expanding training and trade show opportunities. However, USAID officials told SIGAR that providing manufacturers grants to purchase materials was unsustainable because the USAID funding for grants is temporary, meanwhile loans were envisioned as a long term funding-solution for the Afghan carpet manufacturing industry.

¹⁰ USAID, Modification Number P002, 720-306-18-FA-00006, awarded to Impact Carpet Associates LLC, July 25, 2019, p. 10.

¹¹ USAID, Modification Number P002, 720-306-18-FA-00006, awarded to Impact Carpet Associates LLC, July 25, 2019, p. 7.

¹² Under the new loan program, KCEC offered manufacturers the option of having KCEC purchase the needed raw materials from a third party (worth up to 35% of the carpet), instead of offering weavers loans to purchase the materials themselves. However, this approach also failed to appeal to weavers. Many purchased the majority of their materials before they were commissioned to make the carpets (the point at which KCEC funding was available). Additionally, many manufacturers still refused to offer collateral or accept interest that would allow KCEC to ensure the carpet was made and sold; allowing KCEC to receive a return on its investment.

Conclusion

KCEC has struggled to achieve sales and revenue targets which in turn is limiting job growth and the ability of KCEC to become self-sufficient. The current strategy is unlikely to generate the sales and revenue needed to sustain operations after USAID funding ceases in June 2021. The cost to attend trade shows and the inability of the KCEC website to receive and process online orders is limiting the KCEC's growth potential, and the lack of a financing mechanism that is acceptable to Afghan carpet manufacturers is limiting the ability of the Afghan carpet industry to free itself from reliance on Pakistani middlemen. KCEC needs a secure e-commerce capability in order to retain its current customers and to allow new customers to purchase carpets. Additionally, the current pandemic is going to further limit KCEC's growth potential and therefore, KCEC will not likely be able to sustain itself without continued funding. Going forward USAID and ICA will need a plan that considers the current limitations and what additional actions are needed, to include what financing mechanism is needed to assist carpet manufacturers and for KCEC to achieve self-sufficiency.

Recommendations

To improve KCEC's ability to become a self-sufficient commercial enterprise, we recommend that the Mission Director for Afghanistan, USAID:

1. Direct ICA to immediately update KCEC's current website to include an HTTPS security protocol and a comprehensive and secure public e-commerce capability for all current and potential clients.
2. In conjunction with ICA, establish new targets for performance and job creation and assess KCEC ability to achieve financial self-sufficiency by June 2021. The assessment should include a reevaluation of KCEC's marketing, sales, and operational strategies.

Agency Comments and SIGAR's Evaluation

USAID concurred with SIGAR's first two recommendations to work with KCEC to increase its website's security protocols, and upgrade its capabilities for potential online sales, and to revise KCEC's monitoring and evaluation plans reflecting SIGAR's recommendations by December 31, 2020. USAID took action to implement the third recommendation in the draft report which was to reassess the financing program and consider setting up a system that conforms to prevailing lending norms of the Afghan carpet industry. In their agency response on August 10, 2020, USAID stated they issued a modification to the grant that canceled KCEC's loan portfolio and reprogrammed the funds to provide financial assistance to carpet weavers and traders, fund more training sessions for the Afghan carpet industry stakeholders, and sponsor new tradeshow. As a result, we considered the recommendation implemented and closed, and removed the recommendation from the final report,

APPENDIX I – USAID Comments on Draft Report



USAID | AFGHANISTAN

FROM THE AMERICAN PEOPLE

MEMORANDUM

August 10, 2020

TO: John F. Sopko, Special Inspector General for Afghanistan Reconstruction (SIGAR)

FROM: Peter Natiello, Mission Director, USAID/Afghanistan

SUBJECT: Mission Response to draft SIGAR Special Project Report titled: "Progress made toward self sufficiency but critical sales, revenue, and job creation targets have not been met" (SIGAR-20-XX-SP)

REF: SIGAR Transmittal Email dated July 20, 2020

USAID would like to thank SIGAR for the opportunity to comment on the draft "Progress made toward self sufficiency but critical sales, revenue and job creation targets have not been met" report.

Developing the Afghan economy continues to be a primary focus for the U.S. government and the U.S. Agency for International Development (USAID). As part of its efforts to develop the Afghan economy and spur job creation under the Afghanistan Job Creation Program (AJCP), USAID awarded a grant to establish the Kabul Carpet Export Center (KCEC). USAID initiated the Afghanistan Job Creation Program (AJCP) in June 2017 to generate revenue and sustainable jobs by supporting Afghanistan's value-chain development industries with growth potential to identify and help create competitive opportunities, and to help Afghan businesses increase exports. The program funds multiple grant awards, with the value of individual grants ranging from \$2 million to \$10 million. On June 6, 2018, USAID awarded Impact Carpets Associates, LLC (ICA) a firm-fixed grant of \$9.4 million to establish the Kabul Carpet Export Center.

USAID acknowledges SIGAR's findings that ICA successfully met most, but not all, benchmarks associated with establishing the KCEC. Specifically, ICA registered KCEC as a local company in Afghanistan, developed work plans,

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monitoring and evaluation plans, conducted a baseline stakeholder survey, and established product tracking systems.

In the draft report SIGAR also states that ICA has not developed a secure e-commerce platform on its website, which limits online purchasing capabilities. Additionally, ICA has not engaged with the Afghan government to address burdensome airfreight policies as contained in the grant agreement.

KCEC sales, revenue, and job creation targets are not yet achieved. Despite receiving a six-month agreement extension (from May 31, 2019 to November 30, 2019), the KCEC could not meet its first year targets of \$714,286 in sales, \$48,000 in revenue and the creation of 5,715 new jobs. The second year target is to double sales and revenue, and create an additional 5,715 new jobs. As of April 1, 2020, KCEC reported \$717,030 in sales generation, \$41,836 in revenue, and 8,825 new jobs created. With three months until the end of the second year (extended to June 30, 2020) and the COVID-19 worldwide pandemic causing trade shows to be cancelled, there is little chance to achieve these targets, thereby placing KCEC's ability to become self-sufficient by June 5, 2021 in jeopardy.

To improve KCEC's ability to become a self-sufficient commercial enterprise, SIGAR recommends that the USAID/Afghanistan Mission Director:

- 1. Direct ICA to immediately update KCEC's current website to include an HTTPS security protocol and a comprehensive and secure public e-commerce capability for all current and potential clients.*

USAID/Afghanistan concurs, and will work with KCEC to upgrade the current KCEC website with proper security protocol and e-commerce potential for online sales. KCEC should be able to complete the task by December 31, 2020.

- 2. In conjunction with ICA, establish new targets for performance and job creation and assess KCEC ability to achieve financial self-sufficiency by June 2021. The assessment should include a reevaluation of KCEC's marketing, sales, and operational strategies.*

USAID/Afghanistan concurs, and will work with KCEC to revise the M&E plan reflecting SIGAR and USAID recommendation. USAID will make sure to complete the task by December 31, 2020.

3. Reassess the financing program and consider setting up a system that conforms to prevailing lending norms of the Afghan carpet industry.

USAID/Afghanistan canceled the loan portfolio under the KCEC activity through attached Modification (MoD) 3, which was signed and executed on August 3, 2020. Based on this action, USAID requests closure of Recommendation 3.

cc: Elizabeth A. Chambers, Controller, USAID/Afghanistan
U.S. Embassy/Kabul
OAPA Audit
Paul Bruning, Director Office of Economic Growth,
USAID/Afghanistan

APPENDIX II – KCEC Milestones through December 31, 2019

Number	Milestone [†]	Means of Verification/Deliverables Required from ICA	Required Completion Date
1.1	Task 1: KCEC Project Offices Opened	Copies of signed contracts for key personnel and Afghan Growth Finance (AGF) personnel appointed. Confirmation of Kabul office set up signed by AOR following office visit. Confirmation of Charleston office opened by video file tour office and meeting with staff.	7/15/2018
1.2	Task 2: KCEC registered as local company in Afghanistan Task 3: Approved KCEC Work Plan and M&E Plan	Copies of registration documents for Kabul Carpet Export Center (KCEC). Confirmation of AOR approval of Year 1 Work Plan. Confirmation of AOR approval of final monitoring and evaluation plan for project.	8/31/2018
1.3	Task 4: Website launched Task 5: Baseline Stakeholder Survey Task 6: Public Relations Plan Complete	AOR confirmation of successful launch of KCEC website with functional links and customer/seller interface verified by AOR as functional. Screenshots of each page of the website, as well as screenshots of 5 sellers and 5 buyers confirmed to be registered on the site. Report on KCEC baseline stakeholder (potential customers, producers, employees) survey. Document detailing public relations and advertising campaign to advise international buyers and carpet makers in Afghanistan of KCEC submitted to AOR and confirmed as received.	9/15/2018
1.4	Task 7: Initial KCEC loan funds established with Afghan Growth Finance	A copy of sub-award agreement signed between ICA and Afghan Growth Finance (AGF). Standard operating procedures for KCEC loan funds established with AGF to contain routines for KCEC and AGF to establish detail requirements and procedures for issuing export finance. To include outreach approach to attract borrowers.	11/25/2018
1.5	Task 8: KCEC attends New York Rug Show	Report on the New York Rug Show including objectives, activities and after event actions planned. Trade show verification of attendance and result reports on no less than 5 sales consultations, including: Name of show, location and dates of the event. List of participating KCEC personnel and carpet traders. Report on 5 specific new or prospective buyers and copies of any memoranda of understanding or purchase orders. Photo confirmation of KCEC personnel and carpet traders attending trade show.	10/20/2018
1.6	Task 9: Inauguration of KCEC facility in Kabul Task 10: Pilot program to initiate air freight shipments to KCEC customers initiated	Copy of full production Staffing and Training Plan. Visit of USAID AOR to facility for a launch event, or video of event, and report to AOR. Copies of Policies/Procedures and Communications materials for Air Freight Pilot Program Accepted by AOR. Documentation provided to AOR for KCEC use of Kabul Air Bridge by 5 sellers who have not yet used the air bridge to ship carpets, but who intend to air freight orders with KCEC.	11/15/2018
1.7	Task 11: Training materials for Afghan carpet business owners on KCEC developed Task 12: Complete 10 Afghan carpet business owners training	Training materials for 10 Afghan carpet business owners provided to AOR before training. Attendance lists, photos, and training questionnaires from training of 10 Afghan carpet business owners.	11/30/2018
1.8	Task 13: KCEC fully operational Task 14: KCEC attends Istanbul Carpet Week	AOR confirmation that KCEC is operating, including barcode scan system to enter and initiate the full process of order placement, export financing and production tracking is operational, as demonstrated during site visit, or by video and report to AOR. Report on the Istanbul Carpet Week including objectives, activities and after event actions planned. Trade show verification of attendance and result reports on no less than 5 sales consultations, including: Name of show, location and dates of the event. List of participating KCEC personnel and carpet traders. Report on 5 specific new or prospective buyers and copies of any memoranda of understanding or purchase orders. Photo confirmation of KCEC personnel and carpet traders attending trade show.	12/15/2018
1.9	Task 15: Complete 10 KCEC sales meetings Task 16: Train 10 Afghan carpet trade business owners	Copies of email marketing communications and list of 10 international buyers and 20 Afghan carpet sellers contacted via campaign provided to AOR. Minutes including participant attendance of 10 sales meetings with potential buyers, 5 in USA and 5 in Europe. Attendance lists, photos, and training questionnaires from training of 10 Afghan carpet business owners.	12/31/2018
1.10	Task 17: KCEC exhibits at January Atlanta International Rug Show Task 18: KCEC exhibits at Domotex, Hannover, Germany	Report on the Atlanta Rug Show including objectives, activities and after event actions planned. Trade show verification of attendance and result reports on no less than 5 sales consultations, including: Name of show, location and dates of the event. List of participating KCEC personnel and carpet traders. Report on 5 specific new or prospective buyers and copies of any memoranda of understanding or purchase orders. Photo confirmation of KCEC personnel and carpet traders attending trade show. Report on the Hannover Domotex Show including objectives, activities and after event actions planned. Trade show verification of attendance and result reports on no less than 10 sales consultations, including: Name of show, location and dates of the event. List of participating KCEC personnel and carpet traders. Report on 10 specific new or prospective buyers and copies of any memoranda of understanding or purchase orders. Photo confirmation of KCEC personnel and carpet traders attending trade show.	1/31/2019

Continued

Number	Milestone ¹	Means of Verification/Deliverables Required from ICA	Required Completion Date
1.11	Task 19: KCEC exhibits at inaugural Domotex Atlanta	Report on the Atlanta Domotex Show including objectives, activities and after event actions planned. Trade show verification of attendance and result reports on no less than 10 sales consultations, including: Name of show, location and dates of the event. List of participating KCEC personnel and carpet traders. Report on 10 specific new or prospective buyers and copies of any memoranda of understanding or purchase orders. Photo confirmation of KCEC personnel and carpet traders attending trade show.	2/28/2019
1.12	Task 20: KCEC Fee Revenues meet 80% of Year 1 target Task 21: KCEC registration of 10 International Customers and 10 Afghan sellers	KCEC fee revenues represent 80% of annual sales forecast for Year 1. Sales and Production report sent to AOR. Documentation on 10 international customers and 10 Afghan carpet sellers registered with KCEC.	9/30/2019
1.13	Task 22: Conduct 4 regional training sessions for carpet traders Task 23: KCEC exhibits at Domotex Shanghai, China	Attendance lists, photos, and training questionnaires from training from regional trainings provided to Kabul Carpet Association, the Afghanistan Carpet Exporters Guild and sub-associations in Mazar-e Sharif, and Herat. Report on the Shanghai Domotex Show including objectives, activities and after event actions planned. Trade show verification of attendance and result reports on no less than 10 sales consultations, including: Name of show, location and dates of the event. List of participating KCEC personnel and carpet traders. Report on 10 specific new or prospective buyers and copies of any memoranda of understanding or purchase orders. Photo confirmation of KCEC personnel and carpet traders attending trade show.	4/30/2019
1.14	Task 24: KCEC meets Year 1 targets for square meters of carpets exported to generate \$714,286 Task 25: KCEC meets Year 1 new job creation forecast of 5,714 jobs	AOR confirms receipt of annual report containing the requirements listed in appropriate Section of the award. Financial statements verifying target for Year 1 carpet sales. – KCEC registered firm job creation reports. – KCEC registered firm staff tax reports. – Freight forwarding receipts verifying target for square meters of carpets shipped. Report provided to AOR for confirmation of 5,714 new jobs created, based on jobs per square meter of carpets shipped by KCEC and equaling 100% of Year 1 revenues. Report describing how Success Stories have been directed at international buyers and to Afghan ministries and agencies.	11/31/2019
2.1	Task 26: KCEC exhibits at High Point Market	Report on the High Point Show including objectives, activities and after event actions planned. Trade show verification of attendance and result reports on no less than 10 sales consultations, including: Name of show, location and dates of the event. List of participating KCEC personnel and carpet traders. Report on 10 definitive buyers and copies of five memoranda of understanding. Photo confirmation of KCEC personnel and carpet traders attending trade show.	5/31/2019
2.2	Task 27: Second installment and expansion of KCEC loan facility with Afghan Growth Finance	80% of first installment lend to carpet sector, Report on the status of loans issued and outstanding including amount and number of loans issued under KCEC. Draft "Success Stories" booklet showcasing borrowers and their businesses.	12/31/2019
2.3	Task 28: KCEC exhibits at Afghan Treasures in Italy Luxury Show Task 29: Train 40 20 new Afghan carpet business owners. (10 moved from 2.1)	Report on the Afghan Treasures in Italy Luxury Show, including: objectives, activities and after event actions planned. Event verification of attendance and result reports on no less than 5 sales consultations, including: Name of show, location and dates of the event. List of participating KCEC personnel and carpet traders. Photo confirmation of KCEC personnel and carpet traders attending trade show. Attendance lists, photos, and training questionnaires from training of 20 new Afghan carpet business owners.	7/30/2019
2.4	Task 30: KCEC exhibits at New York Rug Show	Report on the New York Rug Show including objectives, activities and after event actions planned. Trade show verification of attendance and result reports on no less than 5 sales consultations, including: Name of show, location and dates of the event. List of participating KCEC personnel and carpet traders. Report on 5 definitive buyers and copies of five memoranda of understanding, and \$100,000 sales or purchase orders. Photo confirmation of KCEC personnel and carpet traders attending trade show.	9/30/2019
2.5	Task 31: KCEC completes first full fiscal year Task 32: KCEC stages the Afghan Rug Roadshow in New York City Task 33: KCEC attends the Passage to Prosperity (P2P3) in New Delhi India	Fiscal 2019 annual performance report on KCEC progress, loans to carpet makers, sales/export figures, international network growth and new job creation. Report on the Week Afghan Rug Roadshow in New York City including objectives, activities and after event actions planned. Report on 5 definitive buyers, and \$100,000 sales or purchase orders. New Delhi P2P3 event verification of attendance and activity report including name of event, list of participating KCEC personnel. Photo confirmation of KCEC participating personnel and potential customers attending event. Report on 5 definitive buyers and copies of 5 memoranda of understanding, or purchase orders.	10/31/2019

¹ For clarity, SIGAR has assigned a "task number" to each individual activity to be completed under the milestones.

Source: USAID, Modification Number P002, 720-306-18-FA-00006, awarded to Impact Carpet Associates LLC, July 25, 2019.

This project was conducted
under project code SP-232

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The mission of the Special Inspector General for Afghanistan Reconstruction (SIGAR) is to enhance oversight of programs for the reconstruction of Afghanistan by conducting independent and objective audits, inspections, and investigations on the use of taxpayer dollars and related funds. SIGAR works to provide accurate and balanced information, evaluations, analysis, and recommendations to help the U.S. Congress, U.S. agencies, and other decision-makers to make informed oversight, policy, and funding decisions to:

- improve effectiveness of the overall reconstruction strategy and its component programs;
- improve management and accountability over funds administered by U.S. and Afghan agencies and their contractors;
- improve contracting and contract management processes;
- prevent fraud, waste, and abuse; and
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