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## The financial scandal that broke Afghanistan's Kabul Bank

By Jon Boone

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**Nearly \$1bn has disappeared from Kabul Bank in mysterious insider loans. The scandal has pushed Afghanistan's tiny economy to the brink of ruin – and yet no one has been charged. Jon Boone follows the cash trail.**

As he saunters into the shisha bar atop one of Kabul's most exclusive hotels, the man accused of rivalling only the Taliban in terms of the damage he has done to Afghanistan does not seem particularly haunted by his actions. Nor does he seem worried that he might have to answer for his role in what is, in relative terms given Afghanistan's tiny economy, the biggest bank collapse in history.

Khalilullah Ferozi, supposedly under house arrest, settles into a seat and orders a shisha and several plates of rice and kebab. On his wrist sits a diamond-studded watch. As he talks, getting animated, a steady spray of half-masticated kebab flies across the table.

Ferozi, a pillar of the Afghan business establishment, lost his job as chief executive of Kabul Bank last year after the Afghan Central Bank belatedly realised he had been in effect running it, along with the bank's former chairman, Sherkhan Farnood, as a giant pyramid scheme. Yet none of the other well-heeled diners at the shisha bar, largely members of Afghanistan's post-2001 nouveau riche, bat an eyelid. Nobody seems disturbed by the presence of a man who helped drain the savings of thousands of depositors totalling \$579m (£359m) in a binge of insider lending by the bank's politically powerful shareholders. Because there was never any obligation

to pay any interest on these "loans", the total unaccounted sum is \$910m. In a country where GDP is just \$12bn, that is an extraordinary figure.

The fallout has been immensely damaging as Afghanistan heads towards 2014, when the foreign presence in the country is to be dramatically reduced. One of the world's poorest nations, Afghanistan has to finance a \$820m bailout of the bank and the ministry of finance is ramping up its tax collection efforts to pay for it. Public confidence in the banking system, non-existent under the Taliban, has been shattered – 24,000 safes were sold during the run on the bank last summer, as people hoarded cash at home. Of all the problems in Afghanistan the role of people close to the president, Hamid Karzai, in the scandal has soured support for the war in the US Congress. Foreign donors are refusing to make aid payments until the mess is cleared up to the satisfaction of the International Monetary Fund. If a deal isn't reached soon, the Afghan government will, within a month or so, struggle to pay civil servant salaries.

Yet Ferozi seems genuinely perplexed by all the fuss, bemused by the idea that the bank should be constrained by banking laws designed to stop irresponsible lending. To his mind the bank's strategy made perfect business sense. Through the floor-to-ceiling windows that line the restaurant he points to some of his excellent investments around the city. Over there, the Gulbahar Centre, a giant building of shops and unfinished apartments. "We invested \$35m in that and it is now worth \$350m," he claims. "The money is not lost, it is sitting right in front of you!"

Had he got his way he would have added an even more grandiose monument to the Kabul skyline: a multi-million dollar Kabul Bank headquarters with three office towers encased in bulletproof glass, three underground garages, a waterfall and a rotating restaurant on the top floor.

He despatches a suited minion to retrieve a March 2010 letter which, he says, shows how well the Americans thought Kabul Bank was being run. The letter from the assistant US treasury secretary is actually a diplomatically worded reminder of the need for "complete compliance with Afghan law by financial institutions". Those charged with cleaning up the mess are far less optimistic that the missing money will be recovered. With shareholders accused of deliberately hiding the scale of their withdrawals, often made in the names of fake companies or other people, including domestic servants, experts believe it would take a miracle to recover half the money. So far just \$61m has been recovered.

Massoud Ghazi, a 33-year-old Central Bank official, was put in charge of the broken bank earlier this year after the government took it over and stripped the shareholders of their rights. Now, as CEO of a reborn "New Kabul Bank", he knows more about the mess Ferozi and Farnood left behind than almost anyone else. An inquiry found that 207 borrowers took out undocumented loans. "The management claimed they were profitable, but if you did the correct calculation you see they lost money for three years," he says. "That was because they took the money and then made no repayment of the principal or any interest payments." In other words, they were not really loans at all.

## Dodgy dealings in Dubai

The most notorious of Kabul Bank's "investments" are in Dubai, where Ferozi says \$160m was spent on 35 luxury villas on the Palm Jumeirah, the artificial sand banks that jut out in "fronds" into the Arabian Sea. Many of the houses were registered in Farnood's name and handed out to bank shareholders. I visited house No1 on Frond O – a huge five-bedroom "Riviera"-style mansion occupied by Ferozi. Others owned by the bank showed every sign of occupation – pools were full of water, and cushioned garden furniture was set up in the sticky summer heat.

It was in these houses that Afghan MPs were entertained with drink and "Russian girls", according to one Afghan intelligence official, who says the bank deliberately sought to compromise the politically powerful.

Ferozi frankly admits that millions of dollars were lost on these villas after Dubai's real estate bubble burst in 2008. He firmly pins the blame on Farnood (who promised to answer my questions by email, but never did), saying most of the disastrous lending, particularly in Dubai, happened before he became CEO.

Less well known is Business Bay, perhaps Dubai's most catastrophic property development, where property developers and speculators flipped off-plan properties during the Emirate's real estate bubble. What was meant to be home to 240 towers is now a ghostly wasteland of half-finished buildings. On the edge of this empty quarter are two massive holes in the ground – the planned sites for 20-storey apartment complexes. Victims of the real estate crash, they will almost certainly never be built, according to a British property expert who shows me around. They are literally money pits for Afghan money: each swallowed almost \$20m of Kabul Bank money, according to Ferozi.

The wreckage of Kabul Bank is also visible on the edge of the runway at Dubai airport, where a Pamir Airways jet has been stranded ever since the carrier was shut down by Afghan authorities for flouting safety rules. The five planes were bought by Farnood in 2009 for \$54m – apparently after no discussion with Ferozi – in blatant disregard for the country's banking laws that bans direct investment in non-banking companies.

Last year one of Pamir's ancient Antonov planes, later discovered to be flying under fake documentation, came down in the mountains of Afghanistan, killing all on board. During the disaster I met Ferozi, still CEO of Kabul Bank, at the airport. He was sporting bizarre dyed blond hair (in the winter he roamed town in full-length fur coats) and in a remarkable display of his unorthodox business skills he managed to re-write the rules of plane-crash public relations. Rather than promising an investigation, he hosted a press conference where some of the wives of the passengers, who had been promised handsome compensation, told the media that Pamir was blameless and that Nato air-traffic controllers were responsible.

## Financial novices

Some say the collapse of Kabul Bank was only to be expected given the backgrounds of the men who ran it. Both Ferozi and Farnood spent time in Moscow in the 1980s, running businesses that

occasionally ran afoul of the criminal underworld. Farnood used to run hawalas, the regulation-free money exchange systems found all over South Asia. Ferozi says he was a small-time trader exporting goods from Russia to Afghanistan. Nothing fancy: flour, cooking oil and water pumps. And yet he was put in charge of Afghanistan's largest commercial bank, a decision approved by the Central Bank governor Abdul Qadeer Fitrat.

Despite being novices in the world of legitimate finance, they knew that a pyramid scheme, with so much money being taken out of the top, desperately needed to attract new people to deposit money at the bottom to preserve the bank's liquidity. This they did by running ethically questionable and expensive-to-run "fortune" lottery accounts that attracted customers with the chance of a cash prize. Such accounts have since been banned.

But salvation came when the government gave Kabul Bank responsibility for handling the payroll accounts of all the country's civil servants, soldiers and policemen, guaranteeing regular infusions of cash. The deal was all the sweeter, Ferozi says, because he would usually lend the money straight back to the Central Bank on time deposit accounts at interest rates of up to 10% – meaning the government was paying interest on its own money.

By his own admission, the key to this contract was the currying of favour with Karzai's family. In one of Kabul Bank's most outrageous loans, it gave \$22m to Mahmoud Karzai, one of the president's brothers, and a former restaurant owner from Maryland. Karzai used the interest-free loan to buy a share in the bank itself. Thus did the president's brother become the third biggest shareholder in the country's biggest bank without spending a penny of his own money.

Then there was the \$4m in bank money for Karzai's 2009 re-election campaign. "We didn't give [the \$4m] for free," Ferozi tells me. "For that we got 430,000 government accounts and from those accounts the bank made a profit of \$4m a month. If we had not done it, other banks were ready to give \$20m to get the accounts."

At the time, such practices were common knowledge in Kabul but nobody could prove it. I first learned about the corruption one evening three years ago in the garden of Ashraf Ghani, a former finance minister who was considering running for president against Hamid Karzai. The former World Bank technocrat outlined precisely the insider lending and the systematic flouting of the banking law. The only way it made any sense to his famously logical mind was that the management must be deliberately conspiring to destroy the bank and, calculating that it was far too big to fail, would force the Americans into a quiet bailout. (Others doubt this level of sophistication – Ghazi, the new CEO of Kabul Bank, believes that shareholders helped themselves to cash "because they saw everyone else doing it".)

### Cover-ups and corruption

I spent weeks trying to prove even a fraction of what Ghani told me. Fitrat, the diminutive Central Bank governor, said he had ordered an investigation that showed Kabul Bank was in rude health. He pointed out that the bank's external auditors had also found nothing. That was because they were taking the bank's numbers at face value. We now know these numbers were, according to Ghazi, meaningless, as the bank's management simply entered fake information into

the internal audit system. For example, loans that had existed for more than 180 days without any repayments being made should have been recorded as "lost". Instead, they were shown to be fine. A secret ledger of the actual state of the bank was kept by Farnood, Ghazi says.

Despite such outright cheating there was one group of people who might have been expected to know that things were not as they seemed: western consultants on six-figure salaries paid by the US government. Working for a company called BearingPoint, which has since been bought up by Deloitte, they were embedded inside government departments where they were supposed to raise standards among their Afghan colleagues. According to a damning recent report by the US government's inspector general that was briefly leaked on the internet, these consultants saw ample "red flags" but failed to raise the alarm. These included death threats made by the management of Kabul Bank against an expat adviser who was part of an inspection team from the Central Bank.

In 2009 I was shown an email from one consultant who tried to blow the whistle. Writing to the Central Bank's board, he claimed he was sacked after daring to raise concerns that people in the financial oversight department were being paid to turn a blind eye to the affairs of Kabul Bank.

Firat denied the allegations to me, saying the consultant had been fired because of poor work and for "creating ethnic discord" within the bank. The consultant was banned by BearingPoint from raising his concerns with anyone outside the Central Bank – including the US government that paid his salary or, as I discovered, with the media. When I phoned him at the time at his home in California he initially seemed happy to talk, but when I made an appointment to call him back, he never picked up.

### Ethnic divisions

There were other factors at work that stopped the truth about Kabul Bank from coming out, principally the problem of an ethnic Pashtun having to keep the Tajiks, the country's second biggest ethnic group, happy. Despite having some Pashtun shareholders, Kabul Bank was a cornerstone of the Tajik establishment of northern Afghanistan, with close ties to top warlords, including Marshal Fahim, whom Karzai chose – to the consternation of the UN – to be his vice-president in 2009.

Fahim's brother and family received at least \$78m in Kabul Bank loans, according to figures provided by Ghazi. According to a US official, Fahim vowed, during the fight to prevent the bank being taken over by the government, never to allow it be "taken over by the Pashtuns".

Ghazi now works out of the wood-panelled office once occupied by Ferozi. On the wall there is still a portrait of Ahmed Shah Massoud, a guerilla commander who resisted the Taliban and is a hero to the Tajiks. He recalls that when his colleagues from the Central Bank tried to investigate Kabul Bank, they were warned: "We can take you to the north of the country and maybe something will happen to you there that you can't control."

Ferozi, for his part, says the bank purge has been orchestrated by Pakistan's Inter-Services Intelligence agency, which has traditionally supported the Pashtun Taliban against Tajiks and

Uzbeks. "Because the CEO and other top members of the bank came from the north, the government of Pakistan felt threatened and feared the northerners would use the bank to have great influence on the politics of Afghanistan," he says. He promises to publish a book detailing his claims.

With such blatant playing of the ethnic card at a time of growing Tajik concern that Karzai might cut a "deal" with the Taliban, there are doubts over whether the people involved in this epic raid on the taxpayers of one of the world's poorest countries will be brought to book.

Finance minister Omar Zakhilwal assured me it is all in the hands of the attorney general, but he enjoys little confidence and is viewed as politically tainted after abandoning a fraud inquiry into one of Karzai's key aides last year. Fitrat wants a "special court" of handpicked judges deemed reasonably clean and versed in financial law.

Another problem is the fear that Farnood possesses compromising information about the involvement of some of the most important people in the government in the Kabul Bank affair. "What they are saying is they have a little black book so you better not push too hard," one western official closely involved in the issue says.

Afghan officials say the shareholders are lying about how much money they took out of the bank, in the hope of holding on to some of it – for example, Farnood says he only spent \$17m of Kabul Bank's money on Gulbahar, although Ferozi cheerfully tells me it was \$35m. Three weeks ago, Karzai summoned the shareholders and disgraced managers and begged them to hand over the money. In a sign that he would like to avoid the political fallout of prosecutions, he gave them one last chance to hand over the cash voluntarily.

But a full-blown inquiry is vital, not least because the law of the United Arab Emirates makes it impossible to seize any assets in Dubai until proper criminal procedures have begun. Also, the IMF is unlikely to declare the country "investment worthy" without a commitment to lock people up.

"They should all go to jail immediately," Ghazi tells me, with a look of bafflement that these men had not been jailed months ago.

A \$10m forensic audit, partly paid for by the UK's Department for International Development, should help with asset recovery and prosecutions, but there is a long way to go yet. Ferozi, pulling on his shisha pipe, believes nobody should go to prison. The government should retrieve the cash by selling off the assets, he recommends. "After that we can discuss the matter of prosecutions," he says with a smile.