Islamic microfinance gains popularity in war-torn Afghanistan

After spending several years in Iran as a refugee struggling to make a living working in a beauty parlour, Shooperi Sharif never imagined that one day she would have a business of her very own.

Sharif and her family fled Afghanistan during the Taliban regime in 1996. In 2002, shortly after their downfall, the family returned to Kabul.

With war-shattered Afghanistan lacking basic infrastructure and institutions – including schools, Sharif began teaching school-aged children in her home.

Last year, the 34-year old mother of three took a microfinance loan from the Foundation for International Community Assistance (FINCA) to expand her school.

After successfully paying off her loan, Sharif's loan officer encouraged her to use the skills she learned in Iran and open a beauty parlour in her neighbourhood, something which would have been inconceivable under the Taliban.

Sharif immediately saw it as a good opportunity. While many schools have reopened in her neighbourhood, there were not so many beauty parlours.

“I had never taken a loan before; it gave me a lot of confidence to see that I could borrow money in my own name and pay it back. In Iran, as an Afghan, I would never have had an opportunity like this,” she says.

Sharif is one of thousands of Afghans who refuse to take interest-bearing loans. Trying to cater to potential clients such as Sharif, FINCA in 2006 became the first microfinance institution (MFI) in Afghanistan to offer non-interest bearing Murabaha Islamic loans (contracts where sellers declare their cost and profit).

Following the guidelines of Murabaha lending, she went along with her loan officer to buy items such as tables, mirrors and chairs for the parlour. The goods were sold to Sharif at a two per cent mark up which she is paying back in monthly installments.

Paul Robinson, FINCA’s country director in Afghanistan, says not only are the products better received than conventional forms of lending, the Murabaha practice is also better for business.

“The advantage of Murabaha loans is that 100 per cent of the money goes into the business. When you do small business lending at Bank of America for instance and you are a small business, as a banker, I would give you a cheque with the name of the store, rather than giving the borrower cash to make sure all the money goes into the business,” Robinson says.

FINCA began its operations in Afghanistan in 2004. Two years later, following market demand, they switched their products to the Murabaha practice.

One borrower, Gul Khana, has felt the benefits of a Murabaha loan first hand. A widowed mother of four, the 37-year old was one of FINCA's first clients in 2004, using the money to open a bakery in Kabul.
"Now that all the money I am borrowing goes into business supplies, I earn more. Before, when I would receive cash directly, there was always some of the money that I would use to purchase other things not relating to my business," she explains.

Providing Shariah-compliant loans has made it possible for FINCA to expand in areas of Afghanistan where other MFIs have been turned away for charging interest.

There are currently 14 microfinance institutions in Afghanistan that are supported by the Microfinance Investment and Support Facility, Afghanistan (MISFA) – a multi-donor venture established in 2003.

With just over 400,000 borrowers in Afghanistan, the popularity of Islamic loans has enabled FINCA to become Afghanistan's fastest-growing and second-largest MFI with nearly 60,000 clients.

“Many NGOs (non-governmental organisations) are coming to me and asking how we are working in such volatile regions as Kunar and Langahar province in eastern Afghanistan. FINCA is able to do so, because we hire local people to work there that the community knows and trust. You have to learn from the local people and develop a delivery mechanism that goes with the values and norms,” Robinson explains.

“Islamic products are not that difficult to develop. Here, in the developing phases, you have to understand the needs of the clients and build delivery systems people are comfortable with,” Robinson adds.

FINCA employee Zul-fi-Qar Mandozai, who previously worked for a rival MFI, says that from his experience working in the central province of Kapisa, clients are more comfortable with Islamic-compliant products.

“At the previous organisation I worked for, so many villagers refused to take the loans because they charged interest,” he says.

Joyce Lehman, a microfinance program officer for the Gates Foundation, agrees that more Shariah-compliant products need to be offered. Lehman previously worked as chief of party for Agriculture Rural Investment and Enterprise Strengthening (ARIES), the United States Agency for International Development-funded rural finance projects in Afghanistan and as MISFA’s chief operating officer.

“Out in the field, MFIs are losing clients to other organisations that provide Shariah loans and it’s that type of market competition that is making MFIs look into providing Shariah products,” she says.

Commercial banks that are offering small- and medium-sized enterprise loans are also finding a strong demand for Shariah-compliant products as they expand in Afghanistan.

“ARIES is encouraging commercial banks to lend to SMEs by training staff and providing capital if needed. In the south and east of the country especially, many banks are finding potential borrowers to not be interested because the loans aren’t Shariah-compliant,” says Lehman.

With Afghanistan’s financial system being just four years old, switching to a Shariah-compliant system is too difficult a task to fathom for many banks.

MISFA is currently working with ShoreBank International on a project providing technical assistant to commercial banks providing SME loans.

“In the context of Afghanistan, in my view, developing Shariah-compliant products are critical. We have received some resistance from pockets here and there, but nothing that would derail the whole sector. However that doesn’t mean we should be complacent. We are bringing people from the Middle East where there is good experience in Islamic banking products to do some training here,” says MISFA’s managing director Amjad Arbab.

Recently, the Afghan Research and Evaluation Unit (AREU) released a study on microfinance funded by the UK’s Department for International Development (DFID). In the report ‘*Microcredit, Informal Credit and Rural Livelihoods: A Village Case Study in Kabul Province*’, researchers Erna Andersen and Paula Kantor found that communities were often divided on their views on interest-bearing loans.

On one of the MFIs examined, the researchers wrote: “For a programme seeking to expand its client base in order to achieve operational sustainability in a Muslim environment, more direct attention to ensuring all staff explain programme costs and charges would be seemingly important.”

Andersen and Kantor found that in this particular community, many problems arose from local religious leaders disapproving of interest-bearing loans.

There is little doubt that as the financial sector expands in Afghanistan, both commercial banks and MFIs will have to follow the lead of FINCA and provide more Islamic lending products. As the pioneer organisation in providing such services, FINCA has proved that such a task is not so daunting.

http://executive.education.insead.edu/social-entrepreneurship
INSEAD Social Entrepreneurship Programme

Find article at
https://knowledge.insead.edu/responsibility/islamic-microfinance-gains-popularity-war-torn-afghanistan