

**CZECH UNIVERSITY OF LIFE SCIENCES PRAGUE**

**Faculty of Tropical AgriSciences**



Czech University of Life Sciences Prague

**Faculty of Tropical  
AgriSciences**

**Islamic Microfinance in Afghanistan**

**Diploma Thesis**

**Supervisor:**

Dipl.-Kfm. Tomáš Hes, Ph.D.

**Author:**

Shamshad Zadran

# CZECH UNIVERSITY OF LIFE SCIENCES PRAGUE

Department of Economics and Development

Faculty of Tropical AgriSciences

## DIPLOMA THESIS ASSIGNMENT

Bc. Shamshad Zadran

Sustainable Rural Development in the Tropics and Subtropics

Thesis title

**Islamic microfinance in Afghanistan**

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### Objectives of thesis

My aim is to analyse the state and demand of of microfinance in Afghanistan, to research and find out if the people of Afghanistan prefer Islamic or conventional Microfinance for their small, medium enterprise small farm and local production.

### Methodology

Literature review part will focus mainly analyses of the role and principle of Islamic and conventional microfinance description and interpretation . Study and research of the current situation for microfinance related to household, small businesses, and to find out the area for usage of Islamic microfinance in small farms, agricultural activities and handkerchief and carpets production. Experimental part will include market research based on observation and secondary data acquisition of microfinance institutions, statistical data acquired from electronic questionnaire and interviews with local population in different provinces in Afghanistan in rural and urban areas. Analysis of the data will be done in IBM SPSS Statistics software.

**The proposed extent of the thesis**

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**Keywords**

poverty alleviation, principles of microfinance, principles of Islamic finance, Shari ah law, SMEs in Afghanistan

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**Recommended information sources**

## Literature

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**The Diploma Thesis Supervisor**

Dipl.-Kfm. Tomáš Hes, Ph.D.

Electronic approval: 30. 6. 2014

**Ing. Vladimír Verner, Ph.D.**

Head of department

Electronic approval: 9. 3. 2015

**doc. Ing. Jan Banout, Ph.D.**

Dean

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## Declaration

I declare that I have worked on my diploma thesis titled "Islamic Microfinance in Afghanistan" by myself and I have used secondary data from sources mentioned at the end of the thesis and primary data was collect through questionnaire in Kabul Afghanistan (August-September) 2014.

Signature... 

In Prague 23.04.2015

Shamshad Zadran

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# List of Abbreviations

AFS	Ariana Financial Services
AKAM	Aga Khan Agency for Microfinance
AMFI	Afghanistan Microfinance Institution
ARMP	Afghanistan Rural Microcredit Programme
BRAC	Bangladesh Rehabilitation Assistance Committee
CFA	Child Fund Afghanistan
FMFBA	The First MicroFinance Bank Afghanistan
FINCA	The Foundation for International Community Assistance
HFL	Hope for Life
MADRAC	Microfinance Agency for Development and Rehabilitation of Afghan
MISFA	Microfinance INVESTMENTSupport Facility for Afghanistan
MOFAD	Micro Finance Agency for Development
Muthahid DIF	Mutahid Development Finance Institution
WOCCU	World Council of Credit Unions
WWI	Women for Women International

## Glossary of Arabic terms

Akhuwat	Brotherhood.
Awqaf	Plural of waqf. For meaning, see below.
Bai salam	A sale in which payment is made in advance by the buyer and the delivery of the goods is deferred by the seller.
Gharar	Literally, it means deception, danger, risk and uncertainty.
Halal	Things or activities permitted by the Shariah.
Ijara	Leasing. Sale of usufruct of an asset. The lessor retains the ownership of the asset with all the rights and the responsibilities that go with ownership.
Istisna	Refers to a contract whereby a manufacturer (contractor) agrees to produce (build) and deliver in the future
Kafala	A contract whereby a person accepts to guarantee or take responsibility for a liability or duty of another person.
Mudaraba	A contract between two parties, capital owner(s) or financiers (called rabb al-mal) and an investment manager (called mudarib). Profit is distributed between the two parties in accordance with the ratio upon which they agree at the time of the contract. Financial loss is borne only by the financier(s). The entrepreneur's loss lies in not getting any reward for his services.
Mudarib	An investment manager in a mudaraba contract.
Murabaha	An investment manager in a mudaraba contract. Murabaha Sale at a specified profit margin. The term, however, is now used to refer to a sale agreement whereby the seller purchases the goods desired by the buyer and sells them at an agreed marked-up price, the payment being settled within an agreed time frame, either in installments or in a lump sum. The seller bears the risk for the goods until they have been delivered to the buyer. Murabaha is also referred to as bay muajjal.
Musharaka	Partnership. A musharaka contract is similar to a mudaraba contract, the difference being that in the former both the partners participate in the management and the provision of capital, and share in the profit and loss. Profits are distributed between the partners in accordance with the ratios initially set, whereas loss is distributed in proportion to each one's share in the capital.
Qard Hasan	A loan extended without interest or any other compensation from the borrower. The lender expects a reward only from God.
Quran	The Holy Book of Muslims, consisting of the revelations made by God to the Prophet Muhammad (peace be upon him). The Quran lays down the fundamentals of the Islamic
Rabb al-Mal	Capital owner (financier) in a mudaraba contract.
Riba	Literally, it means increase or addition or growth. Technically it refers to the 'premium' that must be paid by the borrower to the lender along with the principal amount as a condition for the loan or an extension in

	its maturity. Interest as commonly known today is regarded by a predominant majority of fuqaha to be equivalent to riba.
Sadaqah	An act of charity.
Salam	The short form of bai al salam.
Shariah	Refers to the corpus of Islamic law based on Divine guidance as given by the Quran and the sunnah and embodies all aspects of the Islamic faith, including beliefs and practices.
Takaful	An alternative for the contemporary insurance contract. A group of persons agree to share certain risk (for example, damage by fire) by collecting a specified sum from each. In case of loss to anyone of the group, the loss is met from the collected funds.
Wakala	Contract of agency. In this contract, one person appoints someone else to perform a certain task on his behalf, usually against a fixed fee.
Waqf	(Usually charitable cash donation)
Zakah	The amount payable by a Muslim on his net worth as a part of his religious obligations, mainly for the benefit of the poor and the needy. It is an obligatory duty on every adult Muslim who owns more than a threshold wealth.

*(Obaidullah M. 2008).*



## **Abstrakt**

Tato práce se zabývá základní znalostí mikrofinancí zaměřenou na islámskou společnost v Afganistánu. Důkaz z Kábulu, který je aplikován na základě informací získaných průzkumem v srpnu 2014 a který ověřuje růst úrovně chudoby a nedostatek přístupu k financování. Konvenční mikrofinanční program je často odmítnutý muslimskou společností z důvodu náboženského vyznání. K úspěchu snižování chudoby je potřeba alternativní vzor vztahující se k vyznání islámu a kultury. Diplomová práce klade důraz na růst poptávky po islámské mikrofinanci v Afganistánu, který je bezúrokovým základem s nástroji řídicími se právem šaría. Smlouva o vlastním kapitálu je financována formou spolupráce dvou či více organizací nebo podniků.

## **Abstract**

This thesis explains the basic knowledge of a microfinance program targeted Islamic societies in Afghanistan evidence from Kabul, which is studied by survey in August 2014. This proves rising levels of poverty and lack of financial access. Conventional microfinance programs often denied by Muslim due to their religious believe. For poverty reduction scheme to succeed in Islamic countries there is need for an alternative model related to Islamic beliefs and cultures. The paper insists that there is high demand for Islamic microfinance in Afghanistan, which is free interest basis with tools of Shariah-compliant systems of microcredit; Partnership contract of equity financing joint venture

## Contents

<b>Abstract</b> .....	8
<b>List of figures</b> .....	12
Introduction.....	13
Country Background.....	14
1. Literature Review of Microfinance Institutions.....	16
1.1 Microfinance.....	16
1.2 History of microfinance.....	16
1.3 Objectives of the Year of Microcredit 2005.....	17
1.4 Current global microfinance situation.....	20
1.5 Problem of microfinance In Islamic countries.....	20
1.6 Islamic Microfinance.....	21
1.7 Concept of Islamic microfinance.....	22
1.8 Haram (Forbidden) Activity in Islamic Finance.....	22
a) Riba (interest).....	22
b) Gharar (uncertainty).....	22
c) Gambling (Al-maisir).....	23
d) Haram (Forbidden) Investment.....	23
1.9 Zakat (Islamic Tax for poor people).....	23
1.10 Current Islamic finance.....	25
1.11 Advantages of Islamic microfinance.....	26
1.12 Disadvantages of Islamic microfinance.....	26
1.13 Islamic Microfinance Products.....	26
a) Musharaka (Joint Enterprise Contract).....	26
b) Murabahah (Cost plus mark-up).....	27
c) Takaful (Insurance).....	27

d) Bai Salam (payment in advance) .....	28
e) Istisna'a (Sale) .....	28
f) Wakala (AGENCY) .....	28
g) Kafalah (Guarantee).....	28
f) Waqf.....	28
1.14 differences between Islamic and conventional Financial system .....	29
2. Objectives of this study.....	30
Main Objective.....	30
Specific Objective .....	30
3. Microfinance in Afghanistan .....	31
3.1 Informal economy of Afghanistan .....	31
3.2 Microfinance institutions (MFIs) in Afghanistan .....	31
3.3 Afghanistan new Banking Law .....	33
4. Methodology and Data Collection Techniques.....	35
4.1 Comparision and the main difference between IMFI and CMFI.....	35
4.2 Data Collection Techniques .....	35
a) Secondary Data .....	35
b) Sampling of area .....	36
c) Collecting Primary Data .....	37
d) Statical Ggraphs and Pie Charts.....	38
e) SWOT Analysis about IMFIs .....	38
f) Internal Factor Evaluation Matrix IMFIs .....	38
g) External Factor Evaluation Matrix of IMFIs .....	38
5. Result and Discussion .....	39
5.1 Result of primary data.....	39
5.2 Summary of Questionnaire .....	49

5.3 SWOT Analysis about Microfinance in Afghanistan ..... 50

5.4 Internal Factor Evaluation Matrix ..... 51

5.5 External Factor Evaluation Matrix ..... 52

5.6 SWOT Analysis Summary ..... 52

6. Conclusion and Recommendations ..... 55

    6.1 Recommendations ..... 56

7. References ..... 57

## List of Tables

Table 1: Institutions Offering Islamic Microfinance Products by worldwide region.	25
Table 2 Outreach Data of MISFA Partners	32
Table 3 Secondary collected data about MFIs and their clients	33
Table 4 Gender of the respondents	39
Table 5 Information about age of respondents	39
Table 6 Marital status	39
Table 7 Number of children	40
Table 8 SWOT analysis about IMFIs in Afghanistan	50
Table 9 IFE Matrix	51
Table 10 EFE Matrix	52

## List of figures

Figure 1: Fund from Waqif/Muzakki (Donor)	24
Figure 2 Profit and loss sharing	27
Figure 3 Map of Kabul province the targeted research area	36
Figure 4 Family member	40
Figure 5 Education level	41
Figure 6 monthly income	41
Figure 7 Occupation	42
Figure 8 bank account	42
Figure 9 Usage of microcredit	43
Figure 10 Credit is used in institutions	43
Figure 11 Access to credit	44
Figure 12 Demand for loan	44
Figure 13 Purpose of getting loan	45
Figure 14 Religious importance	45
Figure 15 Prevention by Ulama	46
Figure 16 Decision of loan	47
Figure 17 Opinion about shariah compliants products	47
Figure 18 Preference of institutions	48
Figure 19 Changing of MFIs in case of cheap interest rate	48

## Introduction

Inequalities in the world increasing and it creates problem between societies and within societies. Poverty the lack of (Education, Health, Food, Clean water and Safety Sanitation) and financial inclusion finally inability to participation equally in society and political decision, this all factors together increase the chance conflict and instable political situations, which is nowadays main problem in most of developing countries.

Serageldin (1997) sees the inequalities in the world that *“The top 20 % of the world population consumes 83 % of the world’s income, while the remaining 80 % live on 17 %, and the bottom 20 % live on 1.4 %. These gaps have been growing. In the 47 “least developed” countries of the world, 10 percent of the world’s population subsists on less than 0.5 percent of the world’s income. Some 40,000 people die from hunger related causes every day. One billion people live on less than a dollar day”*.

Chen and Ravallion (2008) defines the international poverty line is \$1.25 a day for 2005, research was held on 15 countries (Malawi, Mali, Sierra Leone, Ethiopia, Niger, Uganda, Rwanda, Gambia, Guinea-Bissau, Tanzania, Chad, Mozambique, Tajikistan, Nepal and Ghana).

Microfinance is not always tool for development it could be anti-developmental tool. Bateman (2013) wrote about South Africa that from 1994 to 2003 income of employment dropped by more than 11 % per year because of informal microenterprises, and the community was forced to sell their household assets to repay their loan.

Obaidullah (2008) estimated that there are more than 600 million poor in the world’s 10 Islamic countries. According to World Bank (2013) Afghanistan with population about 30.5 million and at national poverty line rate is about 36 % (2011).

According to Yunus (1999) microfinance is providing access to credit for the poor. Credit would create economic power that would generate into social power, lifting the poor out of poverty.

Johnson and Rogaly (1997) give an example that in Viet Nam after microcredit about 97% of the daughters of the borrowers attend school compared with 73% of daughters of non-borrowers.

Singh (2013) mentioned that there are two types of microfinance institutions in Islamic countries Islamic and conventional microfinance to serve Muslim population which is more than 72 percent do not use conventional financial services due to religious believes.

*“After decades of war and political instability, Afghanistan remains one of the poorest countries in the world” (Central Statistics Organization, 2014).* There is no study available about Afghanistan poor people to explain that why the poor people do not use microcredit fully, but it is heard that the religious believes and Islamic leader creates barrier to utilize credit with fix interest rate. This study is focused on opinion of inhabitants in Kabul, Afghanistan in rural and urban area through a structured questionnaire to find out the opinion of Afghans about demand for microfinance, and as well as to survey if the poor people prefer Islamic or conventional microfinance.

## Country Background

Afghanistan is one of the poorest landlocked country links with Central Asia, South Asia north and west of Pakistan, east of Iran, and south of Turkmenistan, Uzbekistan, Tajikistan and also share small border in the northeastern with Chania. Afghanistan affected by a conflict that has start in 1979, for almost 4 decades (KAKAR, M. Hassan, 1997).

Estimates of current population is about 30.5 million, GDP \$20.3 billion, GDP growth 1.9%, Inflation 7.6% (2013, World Bank). 2 but some people believe that the population of Afghanistan is more than 40 million as Abdul Rahim Ayubi member of Afghan parliament said in debits in Tolo TV in 2014, that the population of Afghanistan is more than 40 million.

About 75% of the population is living in rural area. Agriculture has been the support of Afghanistan's economy, working as much as 80 percent of the workforce and providing at least half of the gross domestic product (GDP). Because of the poor quality of most agricultural land, subsistence agriculture predominates. In 2008 the six most populated

cities were Jalalabad, Herat, Kandahar, Mazar-e Sharif, Konduz and the capital city Kabul (Library of Congress, 2008). 3 According to CIA Fact book Afghanistan about 23.5% of total population living in urban area and it was estimated (2010-15.) that urbanization rate will change annual about 4.41% (CIA, 2014).

According to National Risk and Vulnerability Assessment the population of Afghanistan below the poverty line in is 36 percent, almost 9 million Afghans are not able to meet their basic needs. (NRVA) shows that poverty has not changed since 2007 Poverty in Afghanistan stays higher among the Kuchi (nomadic) people are most vulnerable with absolute poverty rates about 53.8 percent, in rural area people are living with poverty rates about 36 percent and urban area people are living with poverty rate of 28.9 percent (NRVA 2011-12).

Unemployed rate of Afghanistan is about 53% one of the highest in the region (MLSAMD, 2011). Each year about 400,000 new entrants into labor force which increase unemployment rate (World Bank, 2014).



# 1. Literature Review of Microfinance Institutions

## 1.1 Microfinance

Microfinance is very small loans for poor borrowers with little or no collateral, it is a facilities of financial services and a movement for households with low-income to have permanent chance and access to financial services activities to generate income, build assets, stabilize consumption, and protect against risks as well (Microfinance Gateway. 2015).

According CGAP's view "*the goal of microfinance is to build a world in which as many poor and near-poor households as possible have permanent access to an appropriate range of high-quality financial services.*" Service quality meaning offering a suitable all variety of financial products such as (loans, savings insurance and remittances) that are the real needs of poor households (Christen R.P, Rosenberg R, Jayadeva V. 2004). Microfinance Serve, SME, Poor Farmers, Persons engaged in off-farm activities, Fishermen, Poultry rearing, Livestock farming and Women.

## 1.2 History of microfinance

The history of microfinance started in the middle of the 19<sup>th</sup> century when the theorist Lysander Spooner was writing over the advantages from little credits to farmers and entrepreneurs as a way of how the people get profit. Shore bank was the first community and microfinance development bank started in in Chicago in 1974. An economical historian Timothy Guinnane from Yale has been doing some study on Friedrich Wilhelm Raiffeisen's village bank movement in Germany which was founded in 1864 an by the year 1901 the bank had achieved 2million village farmers. Today the World Bank evaluates that around 7000 microfinance institutions worldwide serve more than 16 million people. CGAP experts estimated that around 500 million families benefits from these little loans making new business realizable (*Microfinanceinfo, 2015*)

Nowadays use of microfinance has started in the 1970s when organizations, such as Grameen Bank of Bangladesh with the microfinance settler Mohammad Yunus. Rowland

mention about the success of the Grameen Bank (which currently supports over 7 million substandard women in Bangladesh) has motivated the planet (Rowland R, 2014).

The year 2005 was declared as the International year of Microcredit by The Economic and Social Council of the United Nations in a call for the building and financial sector to “fuel” the strong entrepreneurial spirit of the poor worldwide. As the United Nations General Assembly proclaimed on 29 December 2003 that 2005 is the International Year of Microcredit and they recognized microcredit’s contribution to poverty alleviation,

On the resolution’s significance, the Secretary General Kofi Annan said: *“The International Year of Microcredit 2005 underscores the importance of microfinance as an integral part of our collective effort to meet the Millennium Development Goals. Sustainable access to microfinance helps alleviate poverty by generating income, creating jobs, allowing children to go to school, enabling families to obtain health care, and empowering people to make the choices that best serve their needs. The stark reality is that most poor people in the world still lack access to sustainable financial services, whether it is savings, credit or insurance. The great challenge before us is to address the constraints that exclude people from full participation in the financial sector. The International Year of Microcredit offers a pivotal opportunity for the international community to engage in a shared commitment to meet this challenge. Together, we can and must build inclusive financial sectors that help people improve their lives”* (UNGA 2003).

### 1.3 Objectives of the Year of Microcredit 2005

- a) By assessing and support the contribution of microcredit and microfinance to achieving the (MDGs).
- b) Increase the public’s awareness, understanding and role for them to eradication poverty through microcredit and microfinance.
- c) Promote in poverty including financial systems to stimulate a sustainable building and government to take action for collective strategies.
- d) Support sustainable access by increasing the capacity of microcredit and microfinance service providers, enabling them to be more effective and efficient at addressing the needs of poor people; and by strengthening the capacity of donors

d) Create a sustainable system for supporting access to financial services in effective and efficient way to identify the needs of poor people.

e) Encourage strategic partnerships by supporting new innovation and partnerships to construct and increase the outreach and triumph of microfinance for everyone (*UNGA, 2003*).

In 2004, the Consultative Group to Assist the Poor (CGAP) built a listing of 11 main principles of microfinance

1) The poor need a variety of financial services, not just loans.

Just like everybody else, poor inhabitants need also needs financial services not just loan and credit. Credit schemes are useful for helping poor businesses to generate income, but these is not enough still need other financial services, such as savings, cash transfers, insurance and cash transfers.

2) Microfinance is a powerful instrument against poverty.

Microfinance is a good tool to fight poverty, through microfinance, the poor have possibilities to sustainable financial services which allow the poor people to grow profits, construct assets, improve their standard of living, and reduce their vulnerability to external factors. Microfinance enables poor households to move from daily survival to the future plans.

3) Microfinance means building financial systems that serve the poor.

Poor inhabitants contain the large majority of the population in most of developing countries. To reach the goals of MF, it should become a basic part of the financial sector.

4) Financial sustainability is necessary to reach significant numbers of poor people. The ability of MFIs is to cover operational costs enables large numbers of the poor to access their services. Sustainability therefore results in further provision of services, as well as reduced transaction costs, better products. Providing better products and services that meet customers' needs, and searching new ways to achieve the unbanked poor.

5) Microfinance is about building permanent local financial institutions.

Constructing financial rules for the poor means constructing sound domestic financial intermediaries that can offer financial services to poor inhabitants on a long-time basis

Depending on funding from governments and donors—including government-financed development banks—will gradually minimize as local financial institutions and private capital businesses mature.

6) Microcredit is not always the answer.

Microcredit is not convenient for everybody, Small grants, infrastructure improvement, employment and training, educating and skillfull programs. Other non-financial services also have the potential to combat poverty.

7) Interest rate ceilings can damage poor people's acces to financial services. Serving many small loans is more costly than a few large loans. Unless micro-lenders can charge interest rates that are well up the average bank loan rates. Interest rate increasing enables MFIs to cover their operational costs, but many negatively affect on the ability of the poor to generate incomeand it reduce access to financial services.

8) The government's role is as an enabler, not as a direct provider of financial services. Governmental play a significant role in setting a sustainable policy that encourages the progress of financial services while securing poor people's savings services, and more meaningful than providing their own lending systems.

9) Donor subsidies should complement, not compete with private sector capital. Donors should use convenient grant, loans, and equity tools on a short-term basis to build institutional capacity and develop supporting infrastructure, as well as support experimental services and products to design and the implementation of projects. To be effective donor subsidies may be used to reach remote or sparsely populated areas.

10) The lack of institutional and human capacity is the key constraint. Microfinance combines banking with social goals, and capacity needs to be built at all levels. Most investements of both private and public should focus on capacity building.

11) The importance of financial and outreach transparency. Bank supervisors and regulators, donors, investors, and clients of MFIs require convenient, standardized, and comparable information on their financial and social performance (CGAP, 2004).

Microfinance is not always helpful and it could be disaster as Bateman has written that in 1997-2003 microcredit has been a disaster for the poorest in South Africa.

Microfinance is not always tool for development it could be anti-developmental tool. Because, it exists only on paper to support the poorest people by small, medium enterprise, but in practice is increasingly all about supporting consumption and spending

In South Africa majority of microloan's holder have been forced to repay their microloan even by selling off their household assets, many of them have been forced by borrowing from friends and family and relatives, many of the poorest individuals have been forced to repay their microloan by selling off their household equipment, sometime the poor have

been taking out new microloans to repay the old ones, the main causes was in self-employment income decrease dramatically more than 11 percent per annum between 1997-2003 (Bateman M, 2013).

## 1.4 Current global microfinance situation

Microfinance has constructed a hard track record as a critical instrument in the fight against poverty. The rapid rise of the industry in the last 15 years has achieved around 130 million customers according to recent surveys. Yet microfinance still achieves less than 20 percent of its potential business among the globe's three or more billions of poor (International Finance Corporation, 2015). While almost 8 % of the world's poor now use microfinance, the fact rests that 92 % of the. World poverty still lack access to financial services (Atikus Insurance, 2014). Microfinance goes on to develop with USD 81.5 billion in loans granted all over the world and a 5% grow in the number of clients in 2012. (JAKUBOWICZ J. 2014). Increase in all areas, with Latin America (24%) and East Asia/Pacific (23%) posting the most powerful growth, and mild growth in South Asia (12%), Africa (12%), and Europe/Central Asia (10%) (Micro Rate, 2013). South Asia conducts the market with the highest number of borrowers (52%), and also the largest number of women (92%) and borrowers from rural areas (80%). Of the highest 100 institutions, 43 are in South Asia and account for nearly 48% of world borrowers. (Micro Rate, 2013). The IMF predicts all world areas to perform better in 2014 than in 2013. A return to increase in the Eurozone is largely anticipated and outer regions – i.e. Eastern Europe, North Africa (MENA). And the Middle east – are predicted to increase at a quicker rate. According to the new IMF forecasts, emerging and developing economies are expected to increase more than 5% next year (moderately more than in each of the last two years), with developing Asia and Sub-Saharan Africa conducting the way (responsAbility, 2014).

## 1.5 Problem of microfinance In Islamic countries

Around 72 percent of habitants living in Muslim states do not use conventional financial services. (Singh S, 2013). High poverty, unemployment, and insufficient financial access in Muslim states carry on to great request for microfinance. While conventional microfinance has successfully achieved high numbers of poor people in Muslim states (mainly

Bangladesh and Indonesia), there is proof to suggest that there are large potential of customers of microfinance that refuse products that do not comply with Islamic laws.

International finance corporation (IFC) commissioned market studies show that in Algeria and Jordan, around 20% of the poor cite religious matters for not seeking conventional microfinance, while in Syria and Yemen; this number reaches to 40%. In a 2008 CGAP poll, local practitioners and key informants suggested similar request trends in Afghanistan ,Pakistan ,Indonesia, and the Palestinian areas, and also in Muslim majority territories of Philippines ,India, Brunei ,Cambodia ,Sri Lanka. Overall, it is estimated that about 2/3 of the microfinance market in the Muslim countries either insists on, or prefers Islamic financing. Islamic microfinance provides an alternative paradigm for millions of poor people who are at the moment not served by conventional microfinance. In order to offer access to sustainable services on scale, it is obligatory for the industry to adopt innovative practices and prove that these models operate. To this end, the industry demands deeper market poll and a comprehensive initiative to construct the capacity of players in the micro, miso and macro levels, in order to support in developing and implementing appropriate market models (Karim N, Mohammed Khale, 2011).

## 1.6 Islamic Microfinance

There are two types of microfinance institution in the Islamic countries in the world, the conventional microfinance and Islamic microfinance (Microfinance Gateway, 2015). Islamic and conventional microfinance both have a social goal to fight poverty, support entrepreneurship, but Islamic microfinance mixes both Islamic and conventional microfinance finance and the Islamic finance is the financial system which is based on Islamic law called Sharia (Clarke M, 2013). Islamic Microfinance relates to a system of localized finance plans set up as an alternative source of funds for little, low-income customers in Islamic countries. Typically clients of Islamic microfinance have small or no collateral, as they do not owns useful assets, and therefore excluded from other manner of financing, including Islamic bank financing. Thus, Islamic microfinance gives an aim of accessing funds for those clients who do not accept other form of finance and they are still seeking Islamic way of life (Bloomsbury Publishing, 2010).

## 1.7 Concept of Islamic microfinance

- Islamic finance contains risk sharing between all groups in a transaction.
- It is obligatory for financial transactions to be asset backed; therefore they are connected with real assets instead of financial speculation.
- There must be a clear contract about the sold product between the merchant and the buyer.
- Islam bans all economic actions that are morally and socially damaging such as business that involves with alcohol, prostitution and gambling.
- Financial risk must stay solely with the lender/owner of the capital not with the director or agent who operates with the capital.
- Any predetermined interest rate is banned.
- It is not allowed to sell what a person does not own, thus short trade is not permitted in Islam (Clarke M, 2013)

## 1.8 Haram (Forbidden) Activity in Islamic Finance

The main issue in is that Muslim must not involve in some activity which is Haram (forbidden) in Quran and therefore IFIs provide products and services which is not Haram. List of some and some of Haram (Forbidden) in the Islamic law (sharia).

### a) Riba (interest)

*"Riba` is a loan with the condition that the borrower will return to the lender more than and better than the quantity borrowed."(Blackbunker, 2010)*

### b) Gharar (uncertainty)

Gharar: is in uncertainty business activity which means that something we are going to buy or sell about which we do not have complete information and knowledge. It's similar to gambling and create problem among people after purchase of it and therefore it is forbidden in Islamic financial system (*Obaidullah M. 2008*).

c) Gambling (Al-maisir)

Invest in, online lotteries, lotto draws, casinos and betting transactions is forbidden (Haram) in Sharia (Islamic law).

d) Haram (Forbidden) Investment

in the industry which produces: Alcoholic drink, drugs, Tobacco and Pork are forbidden. Investing in the industries which distribute pornography include Magazines, Audio, Videos, Cinema, TV, Theatre, Websites, and all other methods of distributing pornography.

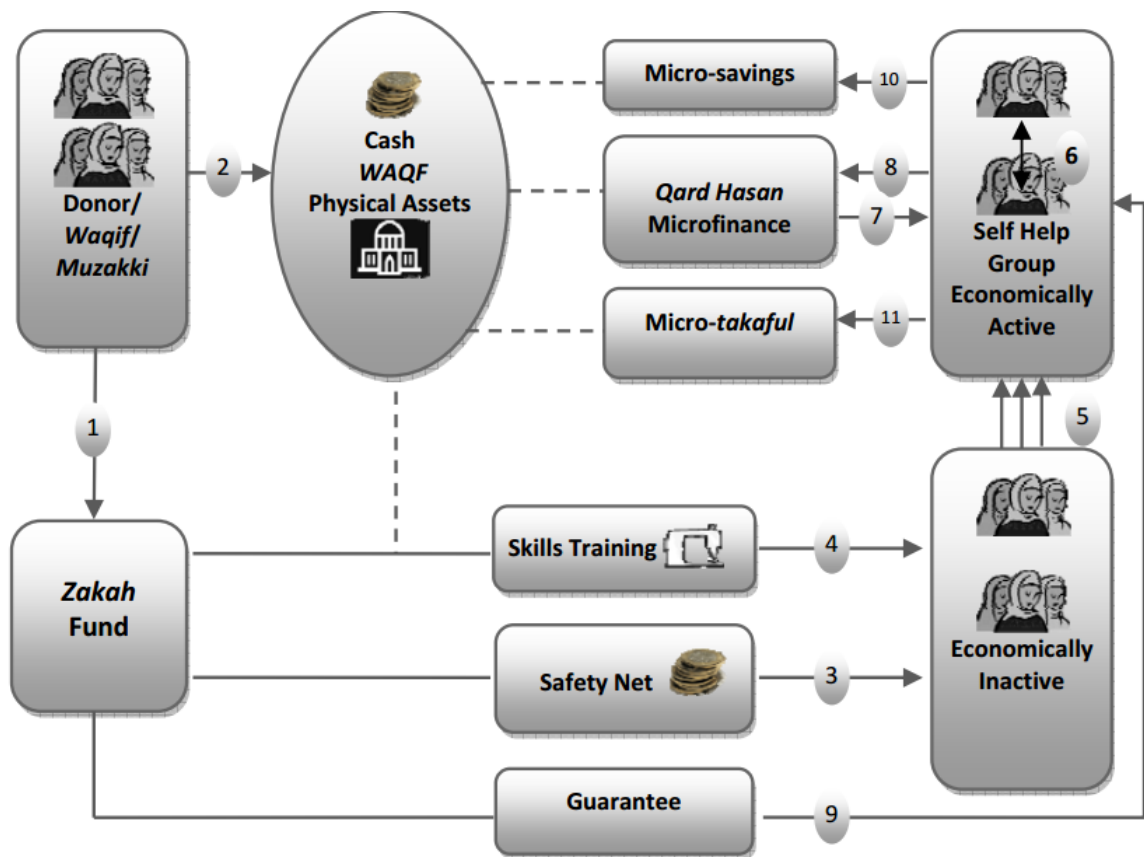
## 1.9 Zakat (Islamic Tax for poor people)

Is the fourth pillar of Islam and it is promote because of justice related to the distribution of wealth. Every Muslim must pay 2.5% of savings as zakat who meets certain criteria regarding the accumulation of wealth, which is distributed to people in need, to avoid poverty from the society (Zulfiqar M. 2014).



IFIs deal with Zakat in time if the clients are not able to repay their debt there is some other way of dealing with this issue as in figure 1.

Figure 1: Fund from Waqif/Muzakki (Donor)



(Mohammed Obaidullah, 2008)

1. Islamic Microfinance Institution (IMFIs) or Program makes a Zakat
2. Waqf works as physical assets as well as monetary assets. The physical assets are used to help skills training and education. The monetary assets may work as a form of cash waqf, or as normal Sadaqa;
3. Program carefully relates the poorest of the poor and the impoverished that are not economically active and conducts a part of Zakat Fund towards meeting their main necessities as a promise, trying to provide a safety;
4. Program provides skills training to not economically active, using community-held physical assets under waqf;
5. Beneficiaries graduate with managerial skills;
6. Beneficiaries are divided into groups with mutual guarantee under the kafala;

7. Financing is handed on the principle of Qard Hassan to the group; also to individuals backed by promise under kafala;
8. Members pay back and in turn, are handed more reached levels of financing;
9. Added guarantee against failure by the group is handed by the Zakat Fund and actual failure accounts are paid off with zakat funds
10. Members are supported to save under convenient microwaving's schemes;
11. Members are supported to form a Takaful Fund to hand micro-insurance against sudden risks and without certainties causing in illness, loss of livelihood etc. (Mohammed Obaidullah, 2008).

## 1.10 Current Islamic finance

is a fast growing industry with more than one thousand Islamic finance institutions with total assets more than \$1.3 trillion, the development of Islamic microfinance has been much less procreative. Offering of the Islamic microfinance products has been doubled in number by service providers since 2006, but the number of clients served by Islamic microfinance products represent less than 1 percent compare to conventional microfinance. (El-Zoghbi and Tarazi 2013).

According to the 2013 CGAP focus note, there are 255 microfinance institutions which provide Sharia-compliant products worldwide in five regions

**Table 1:** Institutions Offering Islamic Microfinance Products by worldwide region.

Institutions	<i>Frequency</i>	<i>Percentage</i>
East Asia and Pacific	164	64
Middle East and North Africa	72	28
South Asia	12	5
Sub-Saharan Africa	4	2
Europe and Central Asia	3	1
<i>Total</i>	255	100

Source: CGAP Focus Note 84, March 2013.

## 1.11 Advantages of Islamic microfinance

Able to play a significant role in aiding to address poverty in some parts of the Muslim country. -contracts can be worked independently or combined, providing greater flexibility to their usage.

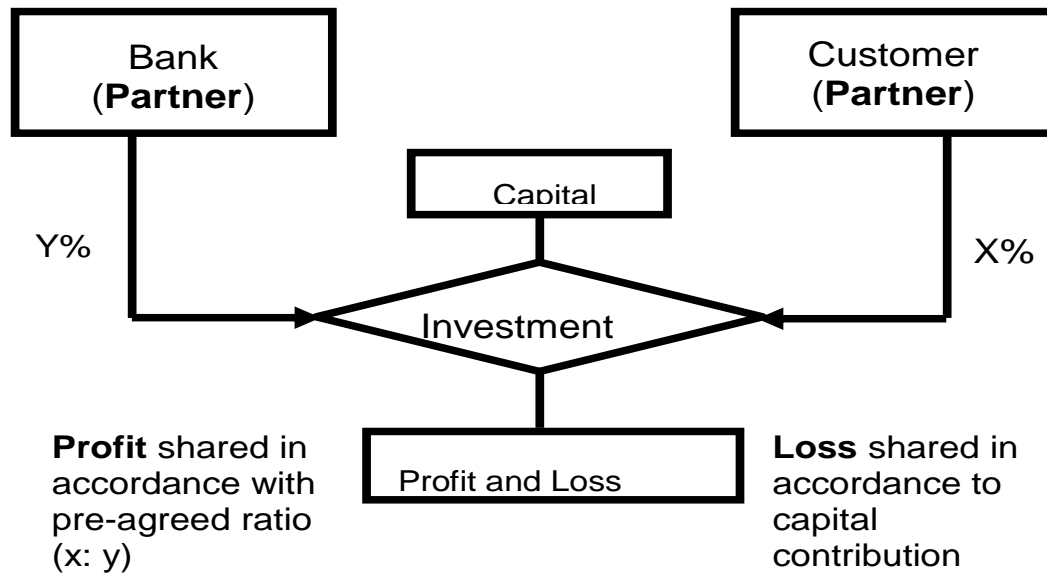
## 1.12 Disadvantages of Islamic microfinance

In general is seen as more a social help system created on charitable basics rather than a business like other manners of microfinance, Islamic microfinance needs help to assure its sustainability. This help contains some way of ongoing grant, usually from a government or nongovernment organization, such as waqf endowment (Bloomsbury Publishing, 2010).

## 1.13 Islamic Microfinance Products

### a) Musharaka (Joint Enterprise Contract)

Contracts are agreed between two partners one may be the IFI and Musharik (partner), profit is determined between the IFI and partner. Losses are according to the basic capital invested by each partner in the beginning of contracts sign (Usmani T, 2004)



Own source inspiration (Bank al Islam)

Figure 2 Profit and loss sharing

b) Murabahah (Cost plus mark-up)

Murabahah a particular sale of commodity by IFIs with cost-plus mark-up, it is actually resale to the clients, it means an (IFIs or IMIs) buy some commodity pointed by client and resale it with a high price to the client for future periodic repayment (International Fund for Agricultural Development, 2014).

c) Takaful (Insurance)

“Takaful is a mutual assistance scheme. It is an agreement which participants agree to contribute into a fund which will later be used to help each other in times of need based” (Takaful-Malaysia. 2015).

22 The Ijara contract is similar to a normal lease in which the owner of property rents or leases his property or goods to a lessee for specified periods for a periodic fee.

d) Bai Salam (payment in advance)

Is a kind of a particular sale of commodity that will be delivered in a specific date in future to the buyer, but the price is paid in advance to seller. Islamic banks also provide capital to farmers who will cultivated and produce specific crop. When it is delivered, the bank can sell through a subsidiary agricultural unit, in order to make profit.

e) Istisna'a (Sale)

Is a special kind of sale contract in which the commodity are sold before produce or available in the time of selling or at the time of contract signed, but the price of commodity is paid in advance at the time of contract signed. In this kind of contract the seller make promises in the time of contract that he/she will manufacturer or produce the commodity needs by buyer according to the ordered Item in contract. It is similar to „Salam sale“, but especially for commodity of manufactures and constructors (Kettell B, 2011)

f) Wakala (AGENCY)

A contract in which one person appoints another person to act as an agent on their behalf in a transaction

g) Kafalah (Guarantee)

Agreement to pay debt of another who defaults in Islamic financing. (*Obaidullah M. 2008*).

f) Waqf

The cash waqf (plural: awqaf) was a trust fund set up with money to support services to mankind in the name of Allah. These donations were allowed by the Ottoman courts in the early 15th century and by the end of the 16th century, they had reportedly become very popular all over Anatolia and the European areas of the empire (*Çizakça M, 1996*).

Qard al Hassan is an interest-free loan used to bridge short-term financing gaps. The principal amount of the loan is repaid by the borrower without interest

Qard al Hassan is designed for people in need and the only type of loan in Islamic finance (*International Fund for Agricultural Development, 2014*).

## 1.14 differences between Islamic and conventional Financial system

Source: (Ahmad, A.U.F 2010), (Abdullah D. V, Chee, K. 2013).

<b>Conventional Financial Institutions</b>	<b>Islamic Financial Institution</b>
Money is a product besides medium of Exchange and store of value. Conventional system is operating according to man-made law there is no religion principles, and regulation.	Real Asset is a product. Money is just a Medium of exchange. Islamic system operating according to Islamic law (Sharia), origin of Sharia is Quran and Sunnah.
Main investment products are accepting deposit and providing of loan	Main investment product is (Musharaka, Mudaraba, and Murabaha) all of these products are in mode of profit and risk sharing.
The main purpose is maximizing just profit.	Purpose is maximizing profit, Islamic discipline and welfare of society.
Do not pay zakat, but may pay tax to state.	Main and social responsibility is collecting and distributing of zakat.
Earning and making revenue through paying and charging fix interest to the deposits and customer loans, may compound rate of interest in case of defaulters	Make profit through the concept of profit-loss sharing. In Islamic law paying or receiving of interest for deposit and loans is forbidden no compound rate of interest from the defaulters.
No effort to ensure growth with equity.	Aim is to ensure growth with equity.
Borrowing from the money market is relatively easier due to paying fix rate of interest.	Borrowing of money from the money market is comparatively difficult due not paying fix rate of interest.
Main target group is women	Main target group is women family
Source of funds usually from international donors, saving for customers Relation to its clients is as creditors and debtors.	Source of funds usually from religious donations from zakat and waqf Relation to its clients is as investors, trader and partners
Provider of loans to all kinds of business such as casinos, gambling, alcohol, pornography, etc.	Not lending to businesses, such as those based on gambling, drugs, pornography, alcohol, etc.

## 2. Objectives of this study

### Main Objective

Main objective of this study was to find out demand for Micro-finance in Kabul Afghanistan, in both rural and urban area as well as the preference of the people about the two types of (Islamic and conventional) microfinance institutions, which one they chose for their business activity.

### Specific Objective

- (i) Find out total number of clients who used micrfinance services in Afghainstan
- (ii) The specific objective was to examine if the local people had access to any types of credit and microfinance in Kabul, Afghanistan
- (iii) Assess the issue of fix interest rate that is charging for cash which was widely dicussed in most of Islamic countries.

## 3. Microfinance in Afghanistan

### 3.1 Informal economy of Afghanistan

The World Bank estimates that around 80% and 90% of the economy in Afghanistan happens in the informal sector, and almost all credit and other financial transactions are still followed through the informal sector. Four types of agricultural credit plans for little and poor farmers are popular in Afghanistan. Anawat is a system containing short selling of commodities for cash loans, which is sometimes used by shopkeepers. Commodity credit is the delayed payment for goods paid from shopkeepers and traders. The third and most frequent form of credit is from kinship group sources and family. The fourth is Salaam which is the most largely used by the trade of opium. It contains the progressive sale of produce at arranged prices, frequently before the season of planting but also later on in the crop season. In Afghanistan Microfinance institutions use their informal credit provision knowledge to create improving products to meet local request. The biggest informal sector system in Afghanistan is Hawala, and while it is not the largest provider of agriculture credit to little farmers, the Hawala “money transforming system” which is important for the economic life of the state and in the opium business (Rasmussen, 2005).

### 3.2 Microfinance institutions (MFIs) in Afghanistan

Microfinance in Afghanistan provides microcredit/loan only for income-generating activities not any self consumption purposes. Some MFIs ask their clients to have at least six months of experience in their business activity and the size of a loan does not exceed \$50,000 for small enterprises and. In total there are nine MFIs in Afghanistan which operate in some provinces. Organization called Microfinance Investment Support Facility for Afghanistan (MISFA) provides funds to seven of these MFIs (AISA, 2012). According to Hussein (2009) in Afghanistan there were 3 MFIs in 2003 and at the end of 2008 it has expanded to 15 MFIs, and the average size of clients loan is between \$100-\$600. The microfinance market was evaluated at over 360,000 clients, which is only 18 percent of the evaluated 2.6 million houses living under the poverty line in Afghanistan (AKAM, 2012). Bahram Barziin (the director of MISFA) an interview in 2013 said “We



*believe that microfinance services have a positive impact on the lives of the Afghan people. A study conducted by MISFA a few years ago concluded that each microfinance loan will create 1.5 jobs in Afghanistan” (Shafaie Z, 2014).*

In general most of the MFIs are available only in the capital of Afghanistan in Kabul city and in the north provinces of Afghanistan as well as some of them operating in central provinces, in the east and south of Afghanistan there is almost zero MFIs. There is a table available in appendix which shows all provinces of Afghanistan and MFIs availability with the number of borrower and the percentage of women clients.

In this following table is the outreach data about MISFA partners in Afghanistan  
 Outreach Data of MISFA Partners in Afghanistan

**Table 2 Outreach Data of MISFA Partners**

Outreach - Overall	FMFB	FINCA	HFL	MUTAHID	OXUS	Total
Provinces	14	8	1	6	10	14
Districts	80	1	0	0	3	83
Active Clients	115,866	29,636	2,870	11,869	11,749	171,985
Active Borrowers	52,118	29,635	2,870	11,869	11,749	108,241
No. Of Loans disbursed Cumulative	399,896	306,606	30,663	25,580	97,874	860,619
Amount of Loans disbursed \$ Cumulative	640,671,964	125,600,666	12,365,538	16,114,003	71,546,996	866,299,167
No. Of Loans Outstanding	52,118	29,635	2,870	11,869	11,749	108,241
Gross Loan Outstanding \$	63,225,551	14,451,946	1,719,932	6,017,469	9,030,054	94,444,951
Women Clients	23,304	23,038	1,464	2,939	3,402	54,147
Women as % Total Clients	20,10	77,7	51	24,8	29	31,5

Source: (MISFA, 2015), [www.misfa.org.af](http://www.misfa.org.af).

There are 15 microfinance institutions in Afghanistan, in which 4 are Islamic and 11 are conventional.

**Table 3 Secondary collected data about MFIs and their clients**

Institution	Type	Year of Establis	No. of active borrowers	Gross loan portfolio (US\$)	Average Loan Amount (US\$)
FMFBA	CMF	2003	466	\$5,900,000	972
OXUS	IMF	2007	11,439	\$8,733,859	261
DFI	IMF	2011	5,503	\$2,200,000	
AFS (MC)	CMF	2002	6,003	\$3,362,738	315
AMFI	CMF	2004	1,405	\$230,242	196
ARMP	CMF	2002	21,905	\$15,280,822	701
BRAC	CMF	2002	116,707	\$16,420,273	195
CFA	CMF	2005	6,817	\$1,530,560	167
FINCA	IMF	2004	29,047	\$13,847,175	138
MADRAC	IMF	2005	780	\$220,120	150
MOFAD	CMF	2008	936	\$239,330	202
PARWAZ	CMF	2002	2,887	\$415,691	161
SUNDUQ	CMF	2005	7,772	\$1,269,929	142
WOCCU	CMF	2007	16,432	\$12,959,125	530
(WWI)	CMF	2004	7,224	\$2,540,013	133

(Source: <http://www.mixmarket.org>)

### 3.3 Afghanistan new Banking Law

Reuters - Afghanistan could have a new banking law confirmed by government in a few months including provisions for Islamic contracts, which may support to attract hundreds of thousands of people into the formal financial sector. About nine out of 10 households in the majority of Muslim country of 30 million keep distance and finally they reject interest-based finance for religious reasons. The central bank, Da Afghanistan Bank (DAB), is finalizing a regulatory framework for Islamic banking which will be completed by the time the new law is confirmed, Akhond Jan Rustaqi, acting deputy director general of Islamic banking at DAB, told Reuters. At present, Islamic banking contracts are offered by a many

lenders through Islamic windows, but there is no standalone Islamic lender. As of last June, Afghan banks held \$813 million in outstanding loans, and \$4.2 billion in assets according to the World Bank. Banks with Islamic windows include Afghan United Bank, Ghazanfar Bank and state-owned New Kabul Bank. Last year Afghanistan International Bank launched an Islamic window (Al Sayegh H. and Vizcaino B., 2015).

## 4. Methodology and Data Collection Techniques

The thesis aims to investigate the MFI demand in Afghanistan and preference among the two types of MFIs in Kabul, Afghanistan, that which one is more acceptable for the local people.

To achieve the goals we used these following methods.

- Comparison and the main difference between IMFIs and CMFI
- Data Collection Techniques
- Secondary and Primary data
- Sampling of area and respondents.
- Observation of active respondents at work places
- Semi structured Questionnaire and Interview
- Statistical Graphs and charts which explain whole percentage of the data
- SWOT Analysis about IMFIs of Afghanistan
- Internal Factor Evaluation Matrix IMFIs
- External Factor Evaluation Matrix of IMFIs

### 4.1 Comparison and the main difference between IMFIs and CMFI

The basic comparison and the differences between IMFIs and CMFIs were represented in the tables for better comprehension of the similarity and differences among these two types of Microfinance Institutions.

### 4.2 Data Collection Techniques

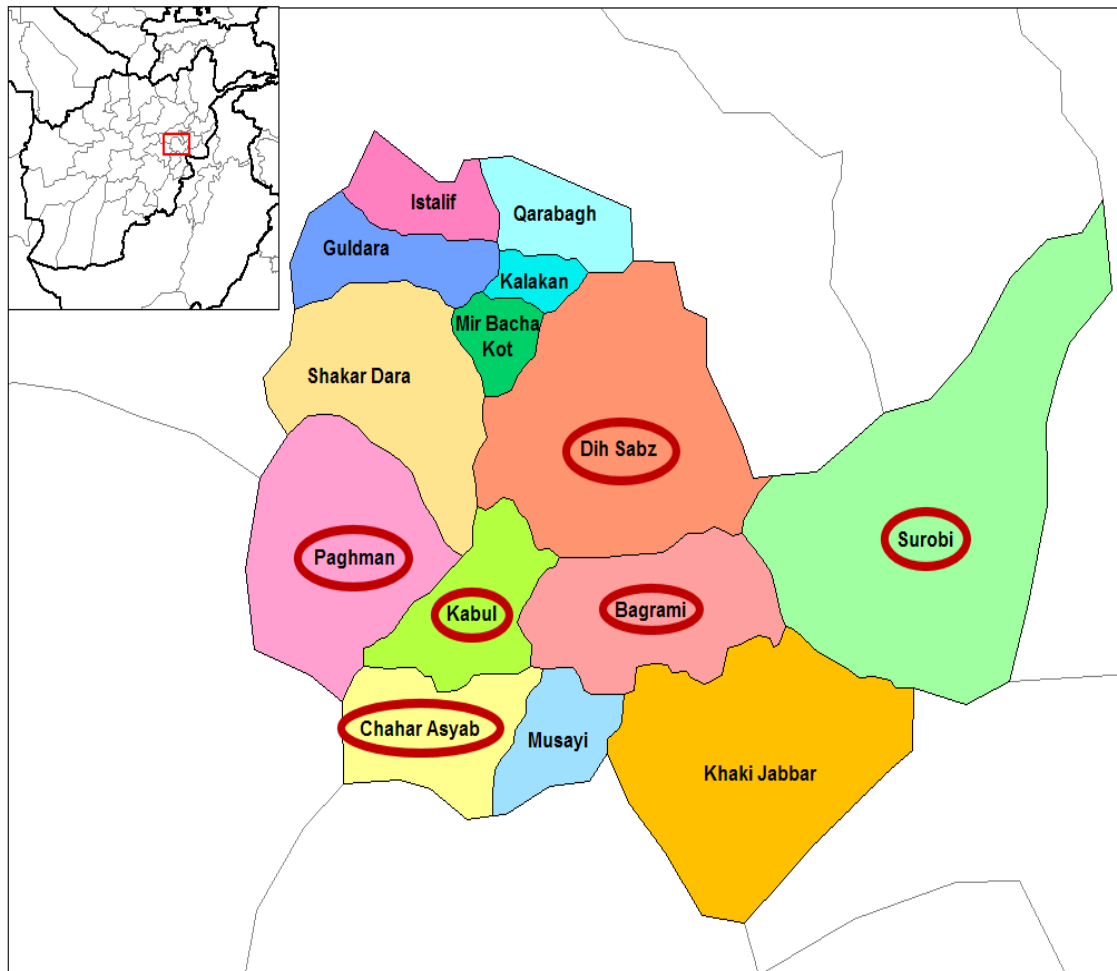
#### a) Secondary Data

Secondary data was collected from websites of financial institutions in Afghanistan which represented the active borrowers related to different locations with the percentage of active women clients. *It was mentioned in Table 2 and 3*

b) Sampling of area

Data was collected from (August–September) 2014 in rural and urban area in the province of Kabul Afghanistan. Cluster sampling methods was used for data collecting, Kabul province was divided in 5 districts (Dih Sabz, Surobi, Bagrami, Paghman and Chahar Asyab), and Kabul city which is pointed in the map of Kabul province. Where the people of five districts are living in rural area, but the Kabul city as an urban area and it is the capital of Afghanistan with almost 3 million populations.

Figure 3 Map of Kabul province the targeted research area



### c) Collecting Primary Data

Our target group was local inhabitants (Farmer/ shepherd, craftsman and Small Medium Enterprises) were asked by questionnaire and observed in their work places questionnaire were started with demographic, Economic, Usage of credits, basic information about religion and preference of MFIs. As majority of the respondents were illiterate therefore questionnaire was filled with the help of surveyor in interview with the local people. There were 20 questions and 194 respondents below you can see the research questions.

#### **NO. Demographic Information**

- 1 Gender
- 2 Age
- 3 Marital Status
- 4 Number of Children
- 5 Number Family Members
- 6 Education Level

#### **NO. Economic Information**

- 7 How much is your monthly income?
- 8 What is your Occupation?
- 9 Do you have bank account?

#### **NO. Usage of Credit**

- 10 Have you ever used MF?
- 11 From which MFIs you used Microcredit?
- 12 Do you have access to credit now?
- 13 Do you need credit?
- 14 For what purpose will you use MF?

#### **NO. Religious Information.**

- 15 Is religion important part of your life?
- 16 Does your religious leader prevent from loan with fixed interest rate?
- 17 If your religious leader prevents you from loan with fixed interest rate, what is your decision will you use it or not?

#### **NO Preference of Microfinance Institutions**

- 18 If any MFIs will be available will you use its Services?
- 19 Which MFI do you prefer? IMFI or CMFI

20 If CMFI is cheaper than IMFI which institution would you utilize?

#### d) Statistical Graphs and Pie Charts

Statistical bar graphs and pie charts are best used for categorizing and explaining data as a whole percentage. Our research was based on above mentioned survey with socio-economic information and analysed with statistical bar graphs and pie charts.

#### e) SWOT Analysis about IMFIs

SWOT analysis is a method to analyze competitive position of IMFIs. It assesses both internal and external aspects of business.

Each letter in the word SWOT represents one strong word: S = strengths, W = weaknesses, O = opportunities, T = threats.

Strengths and weaknesses in the SWOT matrix are internal factors, Opportunities and Threats are external factors that affect the business.

Weakness and Threats are Negative Factors  
Strengths and Opportunity are Positive Factors

SW: According to industries Strengths managers plan to reduce Weakness of their industry.

OT: According to Opportunities managers make best decision to compact future external Threats.

#### f) Internal Factor Evaluation Matrix IMFIs

Internal Factor Evaluation (IFE) matrix is a strategic management tool for evaluating major strengths and weaknesses in functional areas of a business.

#### g) External Factor Evaluation Matrix of IMFIs

External Factor Evaluation (EFE) matrix is a strategic-management method often used to visualize the opportunities and threats that a company is facing in business activity. Concerned external factors are social, economic, political, legal, etc.

## 5. Result and Discussion

### 5.1 Result of primary data

#### 1. Gender of the respondents

**Table 4 Gender of the respondents**

<b>Gender</b>	<b>Frequency</b>	<b>Percent (%)</b>
<i>Male</i>	<i>163</i>	<i>84</i>
<i>Female</i>	<i>31</i>	<i>16</i>
<i>Total</i>	<i>194</i>	<i>100</i>

Afghanistan's tradition and Islamic rule does not allow men to interview women in rural area but it is easier to interview women in urban area, in this research was asked women in the capital city Kabul.

#### 2. Information about age of respondents.

**Table 5 Information about age of respondents.**

<b>Age range</b>	<b>Frequency</b>	<b>Percent (%)</b>
18-25	29	15
26-30	43	22
31-40	69	36
41-50	33	17
>50	20	10
Total	194	100

Age category of respondents start from 18 up to 50 and more than 50 years.

The majority of the respondents age category is between 25-40 year.

#### 3. Table shows Marital status of respondents in Kabul province

**Table 6 Marital status**

<b>Marital Status</b>	<b>Frequency</b>	<b>Percent (%)</b>
Married	157	81
Single	37	19
Total	194	100



Marital status percentage of respondents estimates that more than 81% of the clients in Kabul province are married and they have family, it shows that MFIs in Afghanistan deal with families.

4. Table shows respondents children numbers.

**Table 7 Number of children**

Number of Children	Frequency	Percent (%)
0	48	25
1	23	12
2	30	15
3	40	21
4	39	20
>5	14	7
Total	194	100

Estimated average number of children in a family according to this study is 3, but in Afghanistan exists parents with high number of children up to 7, according to World Bank data fertility rate total (births per woman) is 4.9 children.

5. How many member are there in your family?

**Figure 4 Family member**

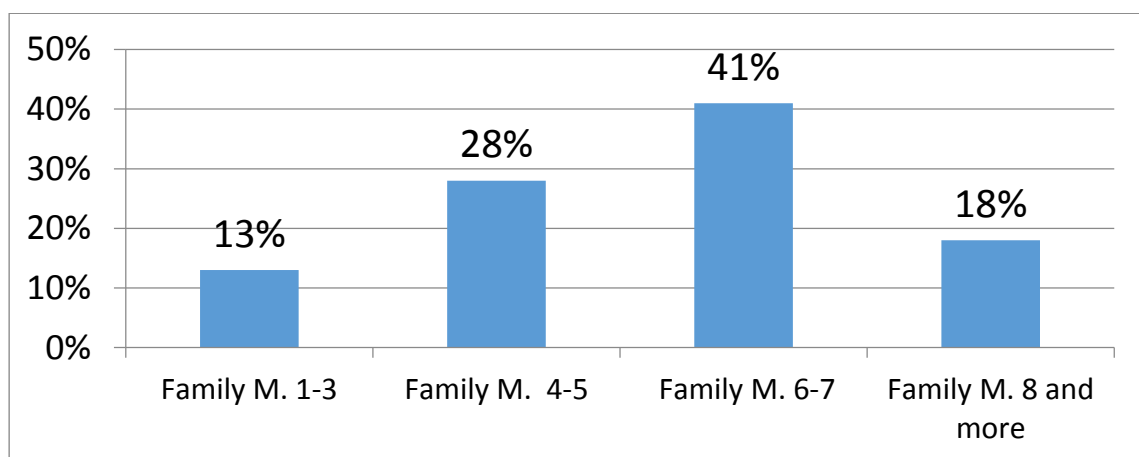
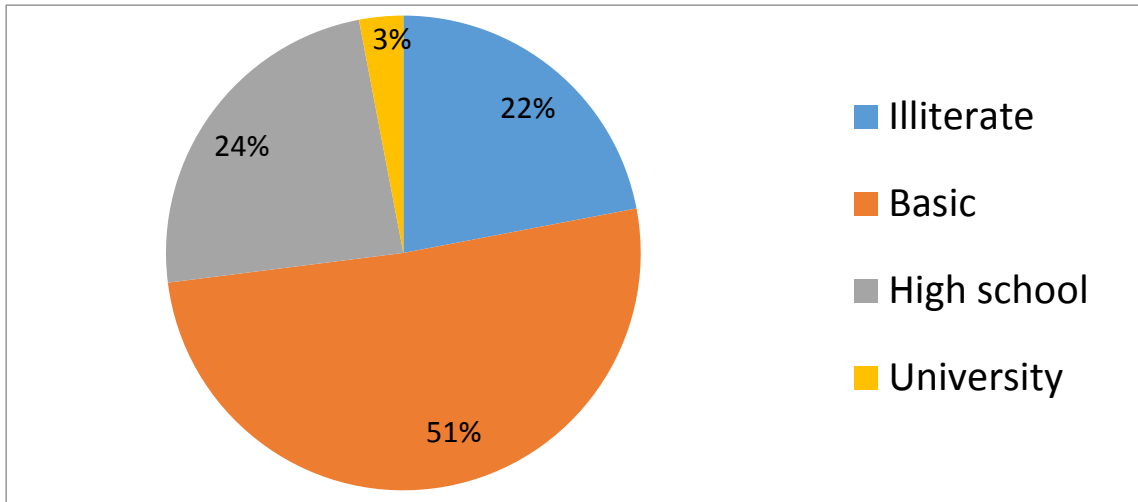


Figure 4 shows that majority of family in Kabul, Afghanistan has member between 4-7 and a family could be a as group guarantee to MFIs where poor family do not have collateral.

## 6. Education level of respondents

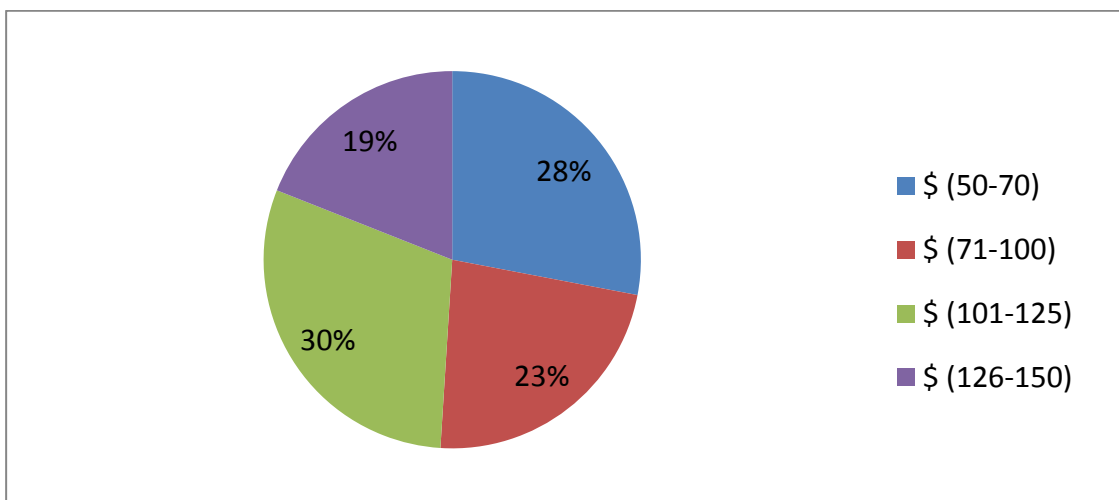
Figure 5 Education level



Majority of the clients have just basic education, it shows that poor people in Afghanistan has low access to education or if they have access to education they do not send their children to school because of poverty. Their children also have to work in farm, agriculture, household etc.

## 7. How much is your monthly income?

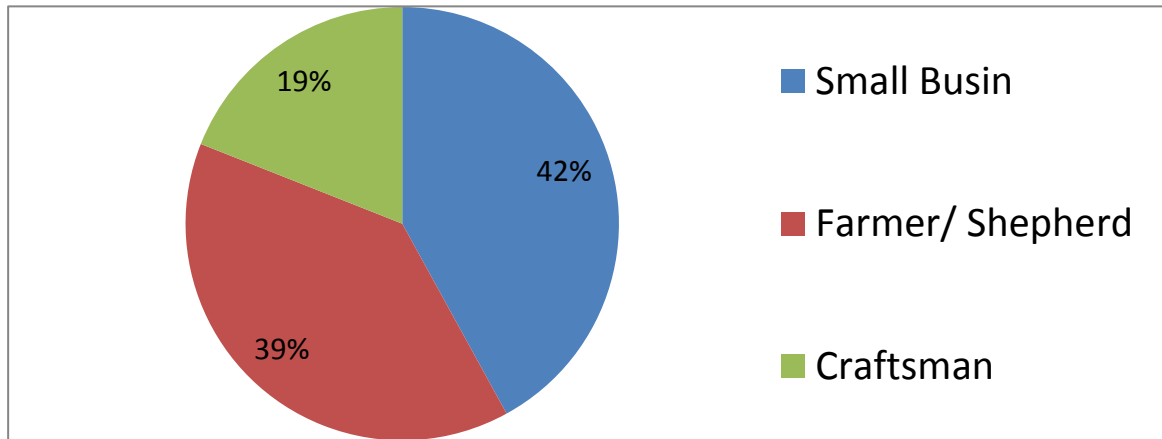
Figure 6 monthly income



The average monthly income of respondents is US\$ 95.

8. What is your occupation?

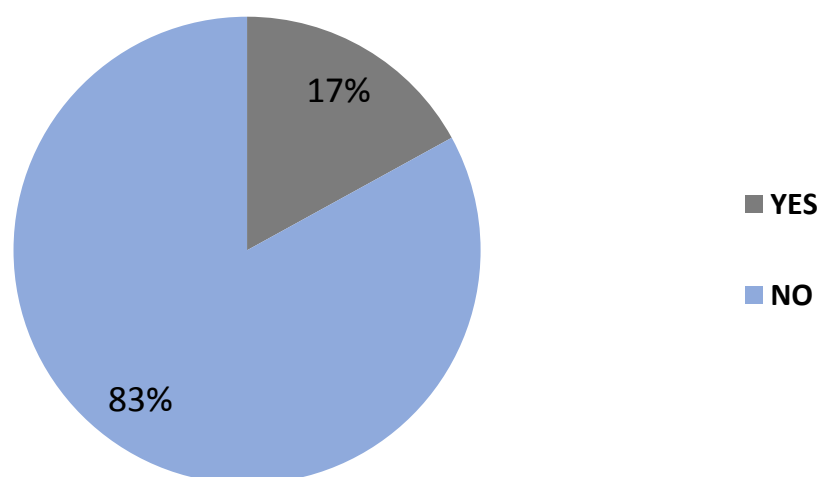
Figure 7 Occupation



Majority of the respondents' occupation is small business, it shows that the clients want to use credit to improve their existing businesses, but in rural area people use credit for agriculture and livestock, most of the women use credit for manufacture of carpet. In general we can say that people in Afghanistan use credit for income generating.

9. Do you have any bank account?

Figure 8 bank account

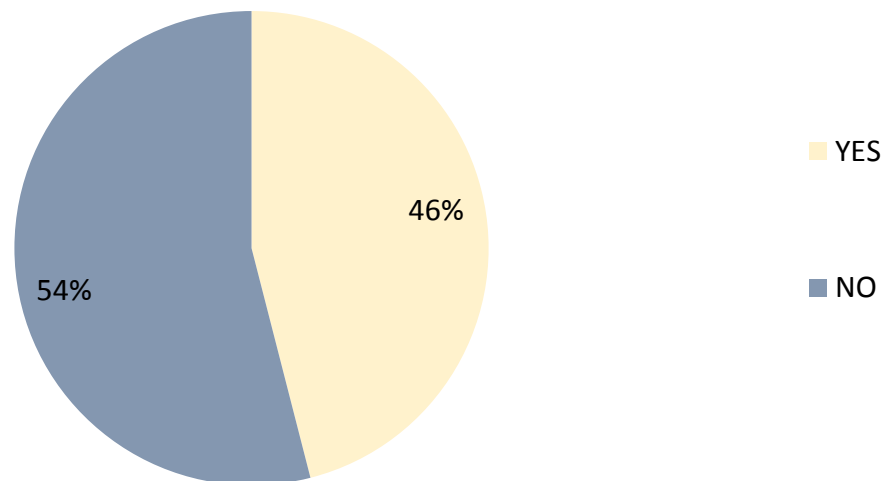


In most of developing countries poor people do not have access to bank account, this number increases in Islamic countries because of religious belief, that in sharia (Islamic law) fix interest rate is Haram (forbidden) which is usual in conventional banking system.

That population of Afghanistan is Muslim and that is the reason why the respondents do not have bank account, and there is a good segment for Islamic banking system as well as for Islamic microfinance.

10. Have you ever used small loan/microcredit for your economic activity?

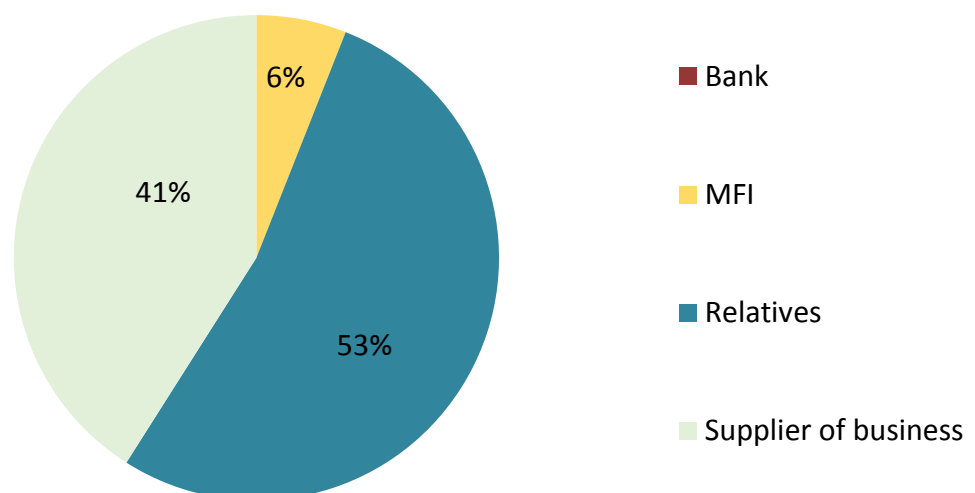
Figure 9 Usage of microcredit



It shows that almost every second person used credit in their life period and they are familiar with using loan from different sources.

11. If you used credit/loan, from which institution you got the credit/loan?

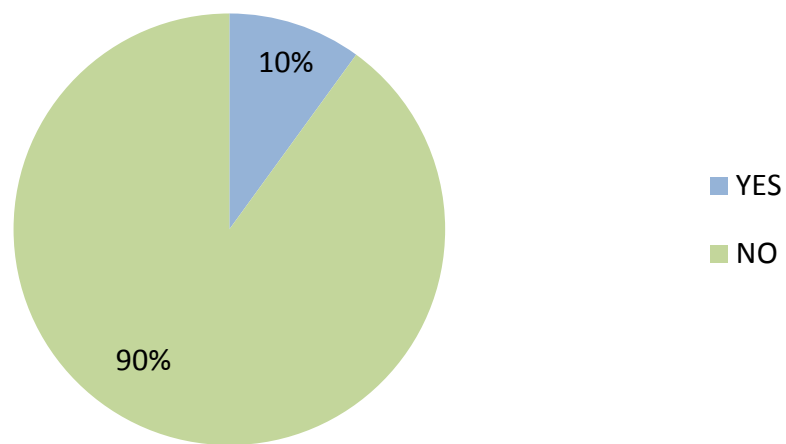
Figure 10 Credit is used in institutions



None of the respondents used loan from bank. Just 6 % of the poor people have used loan/credit from MFIs it shows that in Afghanistan there is low accessibility to get credit from MFIs. Majority of people get benefit from own relatives and the active people in SME gets support from their business supplier.

12. Do you have access or opportunity to get loan/credit from any MFIs for your business activity?

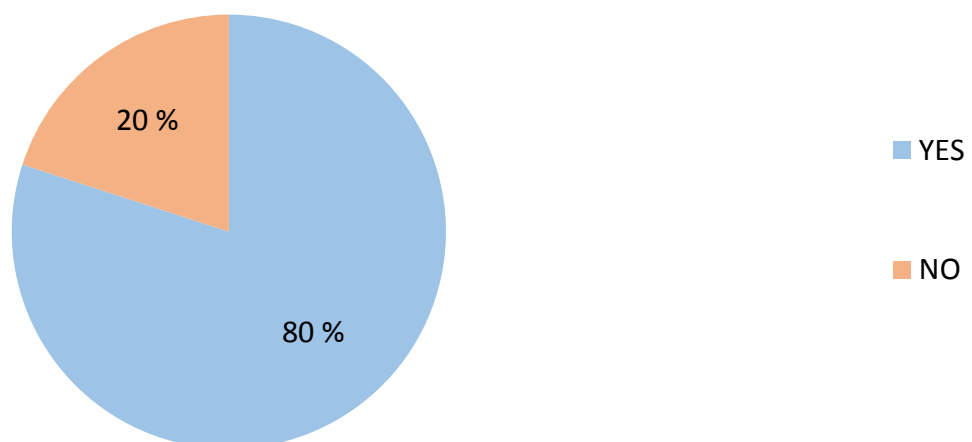
Figure 11 Access to credit



It shows that MFIs are not available for poor people in all parts of Kabul, and the access to credit is difficult to start or improve existing business.

13. Do you need to get small loan/microcredit to start or improve your business activity?

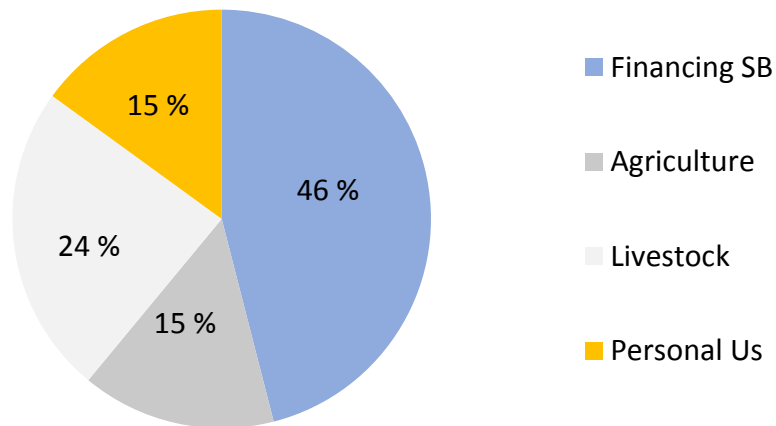
Figure 12 Demand for loan



There is huge demand for credit in Kabul; poor people are suffering from poverty because of high rate of unemployment therefore the local people of Kabul wants to start their own business activity for income generating.

14. If you will get small loan/microcredit for which purpose will you use it?

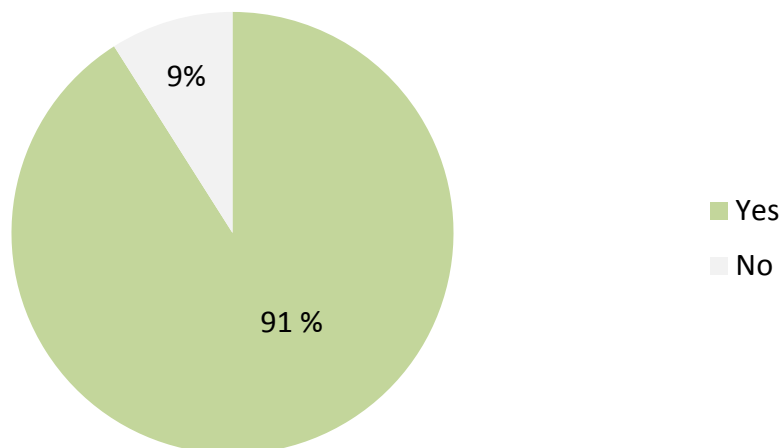
Figure 13 Purpose of getting loan



Majority of Kabul population is active in small businesses, while questions were asked the surveyor observed the respondents activity in rural area most people need credit for small business, but in rural area people needs credit for agriculture and livestock activity. Some people need credit for personal use also but in Afghanistan it is hard to get loan from any financial institution because institutions do not trust the clients if they do not have any business activity.

15. Does your religion create important part of your life?

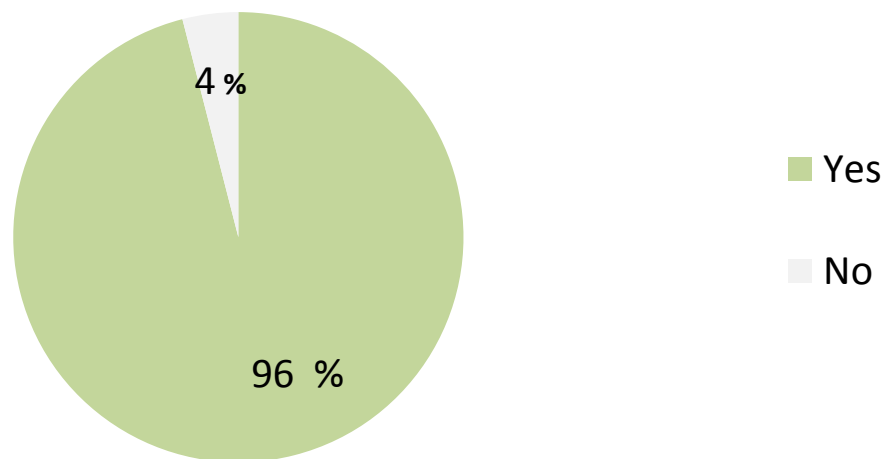
Figure 14 Religious importance



Afghanistan is an Islamic country and 99% of the population is Muslim and the religion is significant part of their life.

16. Does your religious leader prevent you from taking microcredit or small loan which charge fix interest rate?

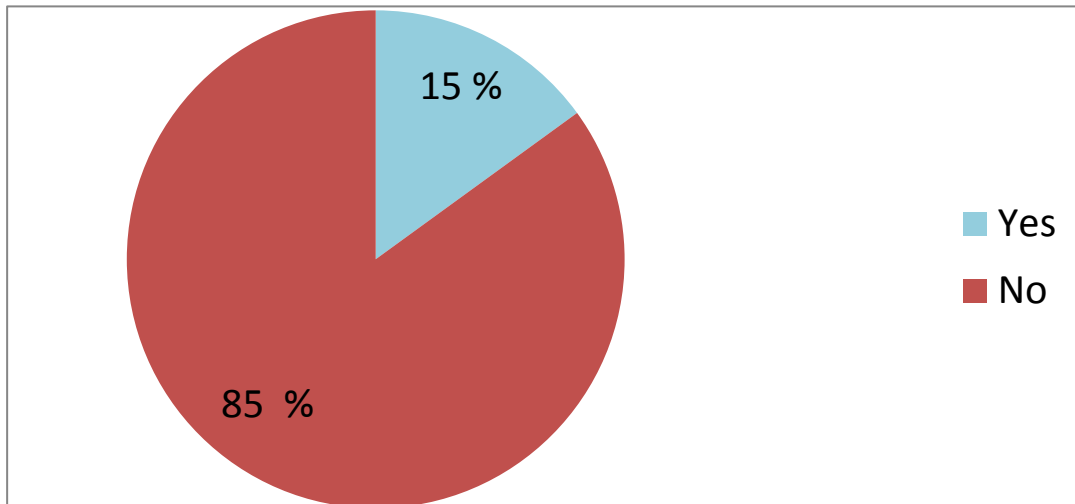
Figure 15 Prevention by Ulama



The majority of the Muslim in Afghanistan follows the Islamic law in all aspect of life, but in case they do not follow the rule of Islamic finance in economic activity, the religious leader often prevents them from non Islamic financial activity wich charge fix interest rate for cash.

17. If the religious leader prevents you from loan with fix interest rate from MFIs, what is your your decision would you take the loan with fix interest rate?

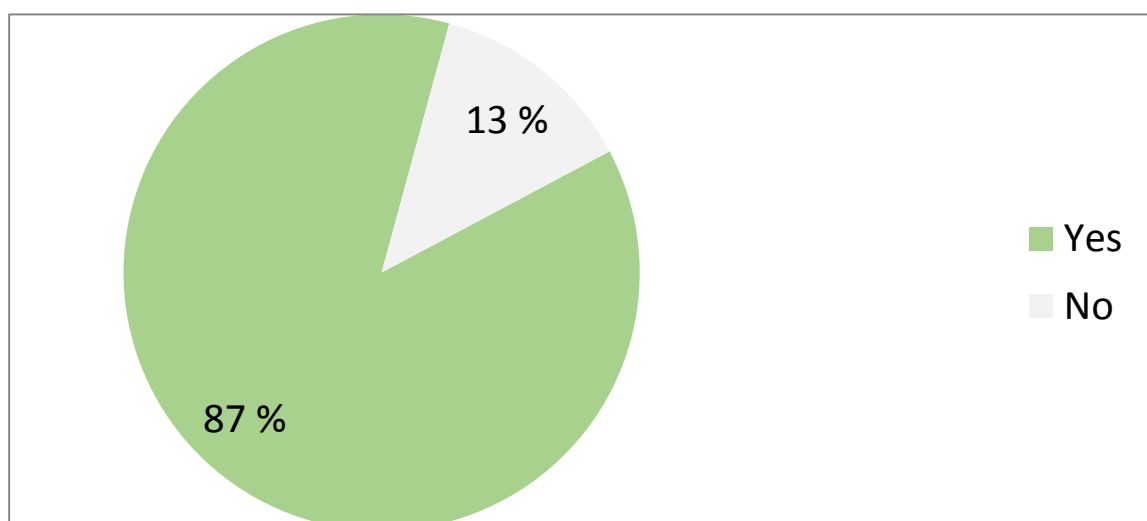
Figure 16 Decision of loan



The majority of the Muslim in Afghanistan respects the religious leader's words, and the role of religious leader is important in Afghan society and the local people can not go against the decision of religious leader and they have to respect it even they do not like it.

18. If there will be any institution available such as IMFIs which provides loan/microcredit according to your religious and sharia (Islamic law), will you use the products and services?

Figure 17 Opinion about shariah compliants products

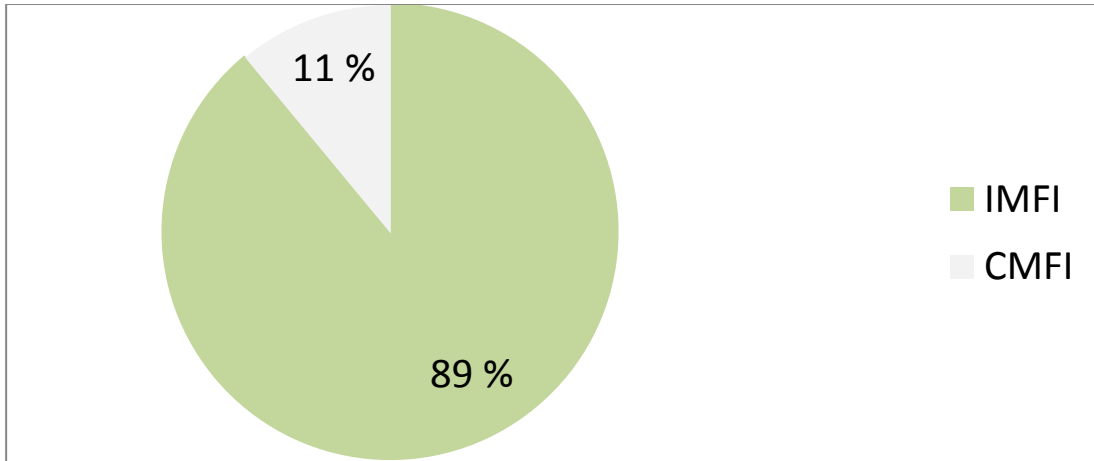




In condition of availability of IMFIs about 87 % of respondents said yes they need and they will use IMFIs products and services.

19. CMFIs charge fix interest, provide cash in hand, but IMFIs use partnership and some other products with Islamic law, which institution do you prefer to get loan/microcredit?

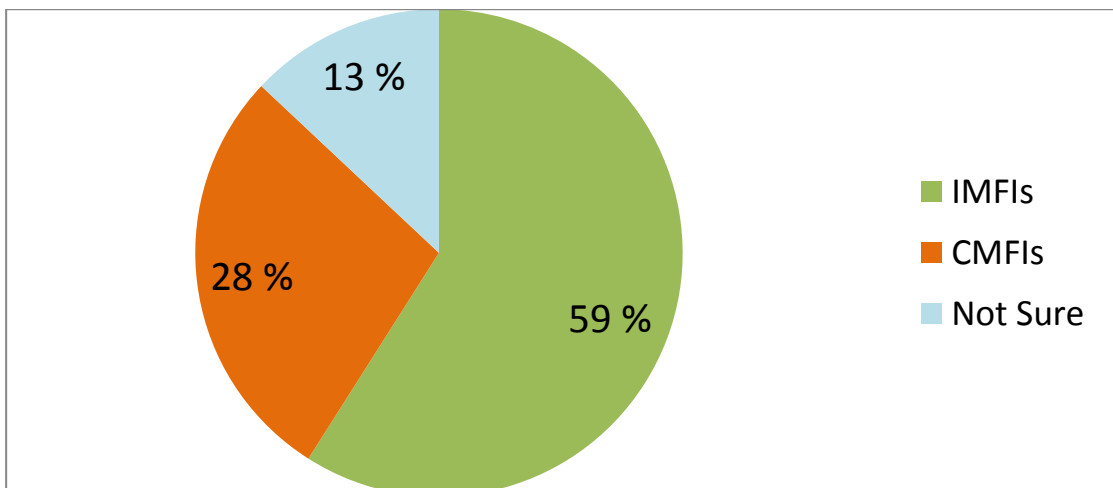
Figure 18 Preference of institutions



In the final dissension when the respondents were asked about preference about Islamic and conventional MFI, most of them said they prefer IMFIs for their income generating activity.

20. If CMFIs were cheaper than Islamic MFIs, which institution would you utilize?

Figure 19 Changing of MFIs in case of cheap interest rate



Even though CMFIs provide products and services cheaper than IMFIs, still majority wanted to use IMFIs, but in this situation the respondents' utilization increased from 11 to 28 percent for CMFIs, and almost 2.5 time increase was seen in respondent's changed opinion from IMFIs to CMFIs.

## 5.2 Summary of Questionnaire

The research and analyze and evidences suggesting that in Kabul Afghanistan there is a huge demand for microfinance, but religious value makes barrier to conventional microfinance. The opinion of religious leader has important rule in Afghan society even in socio-economic activity. Ulama (religious leader) suggest clients not to utilize loan with fix interest rate for cash, because it is Haram (forbidden) in Sharia (Islamic law). The Ulama suggest clients to avail loan from different available financing schemes which is compatible in Islamic law. That is why majority of client's decision in Afghanistan influence by religious value. The examination of the client's perception toward Islamic Microfinance products and services is preferred by majority of the clients in Kabul Afghanistan compare to conventional microfinance. About 89 percent of the client preferred Islamic microfinance and 11 percent want to use conventional microfinance.

The statistical evidence explains that majority of respondent will not go against religious value even though conventional microfinance is cheaper than Islamic microfinance still about 59 percent will utilize Islamic microfinance products and services.

### 5.3 SWOT Analysis about Microfinance in Afghanistan

There are 4 IMFIs in Afghanistan which provide Sharia compliant products and services this SWOT Analyze Islamic microfinance in Afghanistan in general the internal factor Strengths, Weaknesses, and external factor Opportunities and Threats are observed and studied according to situation in 2014 is presented in the table below.

**Table 8 SWOT analysis about IMFIs in Afghanistan**

<b>Internal</b>	
<b>Strengths</b>	<b>Weaknesses</b>
<ol style="list-style-type: none"> <li>1. Provide interest free Shariah-compliant products and services.</li> <li>2. The religious believes make the IMFIs to appeal rich Muslim for donation such as (Zakat, Sadaqa (charity), Waqf and Qard Hassan).</li> <li>3. The IMFIs use all types of charity to help non active clients with skills, training, education and kafala (guarantee) for clients.</li> <li>4. Loyal employee because of religious believes</li> <li>5. Good Reputation and Image worldwide</li> </ol>	<ol style="list-style-type: none"> <li>1. It is harder to become a borrower and get loan from IMFIs.</li> <li>2. Lack of standardized products and services.</li> <li>3. Lack of trained worker because IMFIs are recently established in the world as well as in Afghanistan.</li> <li>4. Some products are not truly accepted by religious leaders.</li> <li>5. Limited Access to International Found.</li> <li>6. Little Diversification Products</li> </ol>
<b>External</b>	
<b>Opportunities</b>	<b>Threats</b>
<ol style="list-style-type: none"> <li>1. The Muslim population is growing in the world which increase the market for IMFIs worldwide as well as in Afghanistan.</li> <li>2. Growing of local and international market by increasing awareness about Islamic financial services.</li> <li>3. High demand for Shariah-compliant products and services are significantly high in Afghanistan.</li> <li>4. Support from the DAB</li> <li>5. Support from Ulama Shora (Scholar Council).</li> <li>6. Potential of cross boarder trade</li> </ol>	<ol style="list-style-type: none"> <li>1. Competition of CMFIs will enter to the IMFIs' Market by establishment of Islamic windows and providing both types of Islamic and Conventional Microfinance services.</li> <li>2. False propaganda from competitors that IMFIs are just by name IMFIs but does not offer Halal (permitted) products and services.</li> <li>3. False rumour that IMFIs, finance Islamic terrorist organisations.</li> <li>4. High Rate of Inflation.</li> <li>5. Non stable political situation.</li> <li>6. Government regulation</li> </ol>

## 5.4 Internal Factor Evaluation Matrix

Table 9 IFE Matrix

IFE Matrix (Internal Factor Evaluation) about Afghanistan IMFI			
Internal Strengths	Weight	Rating	Weighted Score
1. Shariah-Compliant Products and Service	15 %	4	0.60
2. Donation from Charity (Zakat, Sadaqa, Waqf and QH)	15 %	4	0.60
3. Usage Charity for Clients Skills.	10 %	3	0.45
4. Loyal Employee	10 %	3	0.30
5. Good Reputation and Image	5 %	3	0.15
Internal Weakness			
1. Difficulty of get loan from IMFIs.	10 %	2	0.20
2. Lack of standardized services.	7 %	2	0.14
3. Lack of trained worker.	5 %	1	0.05
4. Limited acceptance of products	5 %	2	0.10
5. Limited Access to Found.	7 %	2	0.14
6. Little Diversification.	6 %	1	0.6
Total Weighted Score	100 %		2.79
Major weaknesses (1) Minor strength (3) Major weaknesses (2) Major strength (4)			

According to IFE Matrix if the total weighted scores below 2.5 point means internally weak business, and scores above 2.5 indicate a strong internal position. In our IFE Matrix the total weighted scores are 2.79 shows that Islamic Microfinance in Afghanistan has internally strong position.

## 5.5 External Factor Evaluation Matrix

External Factor Evaluation (EFE) matrix is a strategic-management method often used to visualize the opportunities and threats that a company is facing in business activity. Concerned external factors are social, economic, political, legal, etc.

**Table 10 EFE Matrix**

EFE Matrix (External Factor Evaluation) of IMFIs about Afghanistan			
<b>External opportunities</b>	<b>Weight %</b>	<b>Rating</b>	<b>Weighted Score</b>
1. Increase Market for IMFIs	14 %	4	0.56
2. Increasing Awareness about IMFIs	12 %	3	0.36
3. Demand for IMFIs products	13 %	4	0.52
4. Support from DAB (De, Afghanistan Bank)	10 %	3	0.3
5. Legal support from Shora Ulama (Scholar Council).	7 %	4	0.28
6. High potential of cross boarder trade	8 %	3	0.24
<b>External Threats</b>			
1. CMFIs Entering to the IMFIs' Market.	4 %	2	0.08
2. False Propaganda of Competitors.	4 %	2	0.08
3. High Rate of Inflation	5 %	1	0.05
4. Non stable political situation.	10 %	2	0.2
5. False rumour thta finance terrorisem	7 %	2	0.14
6. Government regulation	6 %	1	0.06
<b>Total Weighted Score</b>		4	2.87
Major weaknesses (1) Minor strength (3) Major weaknesses (2) Major strength (4)			

The total weighted score can range from a low of 1.0 to a high of 4.0. The average score you can possibly get is 2.5. EFE Matrix the total weighted scores scale are below 2.5 point indicate external weak business. Scores significantly above 2.5 indicate a strong external position.

## 5.6 SWOT Analysis Summary

By Strengths, weakness could be reduced. With opportunity, threats could be reduced

In our IFE Matrix the total weighted scores are 2.79 shows that Islamic Microfinance in Afghanistan has internally strong position to avoid internal weaknesses.

In our EFE Matrix the total weighted scores are 2.87 which show that the Islamic Microfinance in Afghanistan has external strong position and the business has the ability to respond to external Threats factors.

## 5.7 Discussion

Our studies in Kabul province found out that there is huge demand for Microfinance, and people preferred Islamic Microfinance over conventional Microfinance.

There was no study and research available from Kabul Afghanistan about people opinion according to preference of conventional or Islamic microfinance, but it was always heard from Ulama (Religious leader) that conventional financial institutions which charge fix rate of interest is Haram (prohibited) in Sharia (Islamic law). In several other studies revealed and estimated that 2/3 of Muslim population in Islamic countries insists on Islamic financial products and services (Karim and Khaled, 2011).

In Afghanistan our research found out that the only reason for preferring Islamic Microfinance was the religion and Ulama's prevention from CMFIs. But it in case of Abbas, Dzuljastri and Norma (2014) found out in their research that in Pakistan more likely people preferred islamic microfinance over conventional not only based on religious reasons, but also the quality of services and products in terms of low transaction costs are the reasons why people prefer Islamic Microfinance. We can see in two neighbour countries Afghanistan and Pakistan that people prefer Islamic microfinance with different reasons it is because of the different culture and ethicks. Still in some countire as (Honohon (2007) estimated that 72 % of people living in Muslim-majority countries do not use formal financial services (Karim, Tarazi, and Reille, 2008).

Still preference does not mean that Muslim people are not using conventional microfinance products, they do use it as you can see in Table (...) that in Afghanistan out 15 microfinance institutions 11 are conventional and 4 are Islamic.

The research and analyze and evidences suggesting that in Kabul Afghanistan there is a huge demand for microfinance, but religious value makes barrier to conventional microfinance. The opinion of religious leader has important rule in Afghan society even in socio-economic activity. Ulama (rileigious leader) suggest clients not to utilize loan with fix interest rate for cash, because it is Haram (forbbiden) in Sharia (Islamic law). The Ulama

suggest clients to avail loan from different available financing schemes which is compatible in Islamic law. That is why majority of client's decision in Afghanistan influence by religious value. The examination of the client's perception toward Islamic Microfinance products and services is prefer by majority of the clients in Kabul Afghanistan compare to conventional microfinance. About 89 percent of the client preferred Islamic microfinance and 11 percent want to use conventional microfinance.

The statistical evidence explains that majority of respondent will not go against religious value even though conventional microfinance is cheaper than Islamic microfinance still about 59 percent will utilize Islamic microfinance products and services.

## 6. Conclusion and Recommendations

Islamic and conventional microfinance both have same goal to fight poverty, but Islamic Microfinance provides an alternative for millions of poor people who are at the moment not served by conventional microfinance. In order to offer access to sustainable products and services for poor people in Islamic countries it is important for donore and financial institution to adopt innovative practice models such as Islamic Microfinance.

It was found in this study that majority of the Afghan people prefer Islamic Microfinancefor. For better operating it is necessary to provide each nation and country with services related to their culture, believe and other traditional accepted values. The religion of Islam play an important role in socio-economic activity of all Afghans as it was studeud in this research, it should be respected. Nowadays in Afghanistan every single decision of the Afghan society is made by Ulama (religious leader), it may have positive or negative affect on Afghan peoples' life but to avoid conflect and misunderstanding all donors, governmental and non governmental organization should take it in account that not to cross the border of culture and relious value.



## 6.1 Recommendations

The lender through the Islamic Microfinance Institutions have chance of supervision on their client's business activity and they can generate even more and reduce risk of lost in their invested capital. The Islamic microfinance has better condition for lender and borrower that the investor has control on his own negotiated profit and loss contracts with clients. Also it has good opportunities for clients that the investor recommends and assesses the clients' business activity which is adjusted time to time to improve.

Research needed to evaluate which institutions serve better IMFIs or CMFIs.

Research is needed to study the implementation of Islamic Microfinance in Afghanistan; to find out is practically possible for local and international companies to invest on IMFIs.

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