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EVALUATION OF STRATEGIC MANAGEMENT ISSUES RELATED TO THE MICROFINANCE INDUSTRY AND SMALL AND MEDIUM ENTERPRISES IN AFGHANISTAN

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ABSTRACT

This article investigates the significance of strategic management at microfinance institutions and small and medium enterprises in Afghanistan. Despite the presence of numerous international and national donors and substantial sums of money funneled into the country, most participants of this industry are currently insolvent, and those who are not bankrupt are not financially self-sustainable. This study examines the historical progress and performance of microfinance industry in Afghanistan from 2002 to present time. We used mixed qualitative and quantitative methodology while collecting and evaluating the data, using face-to-face interview techniques on WhatsApp and other mobile messenger applications.

According to our findings and results, while the creation of the microfinance sector generated numerous new jobs for the economy, lack of accountability and leadership coupled with mismanagement of limited resources exasperated the current situation further. Attraction of more financial institutions and funds into the country, without a clear strategic plan and right management tools, created serious new problems in the areas of finance, social services, security, and human resources. We discovered serious issues such as lack of adequate internal control, adequate governance, absence of law enforcement and oversights, absence of credit bureaus, and lack of a national identification system.

Key Words: STRATEGIC MANAGEMENT, MICROFINANCE, ISLAMIC BANKING, SMEs

Jel Codes: M1, M16, M19, D12

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AFGAN MİKROFİNANS ENDÜSTİRİSİNDEKİ KÜÇÜK VE ORTA ÖLÇEKLİ KURUMLARDA STRATEJİK YÖNETİM EKSİKLİKLERİ VE ÇÖZÜM ÖNERİLERİ

ÖZET

Bu makale, Afganistan'daki mikro finans kuruluşlarının, küçük ve orta ölçekli işletmelerin stratejik yönetimini ve önemini analiz etmektedir. Birçok uluslararası ve ulusal bağışçıya ve büyük miktarda yapılan bağışlara rağmen, bu sektördeki oyuncuların çoğunluğu iflas etmiş ve hala kapanmamış olanlar ise finansal olarak kendi kendisini idare edebilir durumda değildir. Bu araştırma, 2002 yılından günümüze kadar mikro finans kurum ve kuruluşlarının gelişimini ve başarısızlıklarının nedenlerini incelemektedir. Bu çalışma için karışık kalitatife ve kantitatif metotlar kullanılmış, veri toplamalar WhatsApp gibi platformların kullanımı ile senkron bir şekilde çevrim içi yapılmıştır.

Araştırmamız sonucunda mikro finans sektörünün kurulması ve yaygınlaşması planlandığı gibi yeni iş olanakları yaratıp ekonomiyi canlandırırken, stratejik yönetim eksikliği, hesap verebilirliğin olmayışı ve kısıtlı fonların hileli bir şekilde dolandırılması finansal hizmetler sektörü ve birçok alanda kötü olan durumu daha da kötüleştirmiştir. Stratejik yönetim olmadan fazla fonu ülkeye çekmek ekonomik refah ve zenginlik getirmek yerine, finans, sosyal alanlar, güvenlik ve insan kaynakları alanlarında ciddi problemleri de beraberinde getirmiştir. Mülakatlarımızda ülkenin çok sayıda dolandırıcılık, iç kontrol eksikliği, doğru yönetim eksikliği, kanunların caydırıcılığının olmayışı, gözetim eksikliği, kredi bürolarının eksikliği ve ulusal kimlik sisteminin yokluğu gibi problemlerle boğuştuğu görülmüştür.

Anahtar Kelimeler: STRATEJİK YÖNETİM, MİKROFİNANS, KÜÇÜK VE ORTA ÖLÇEKLİ İŞLETMELER, KATILIM BANKACILIĞI

Jel Kodları: M1, M16, M19, D12

1. INTRODUCTION

Although historical record of microfinance goes back to the beginnings of money and commerce, it is a well-known truth that microfinance as we know it today began with the Grameen Bank's Grameen methodology, created by Muhammad Yunus in Bangladesh. The financial offerings were initially presented to female clients who were having difficulties accessing traditional banking institutions. The system used group lending methodologies, as well as cross-guarantees by group members to ensure creditworthiness of the applicants. Muhammad Yunus initially gave loans to 42 women to help them start their small businesses. Building on the success of these trials, the evolution of microfinance has occurred and the Grameen model adopted nationally and around the world by multiple different banks (BNP Paribas, 2017).

Microcredit, often known as microfinance, is a type of banking service that is generally supplied to low-income organizations or individuals who do not have access to financial services due to poor credit or low credit ratings. Microcredit, unlike other major loans, often runs from $100 to $25,000 with supplementary services such as microinsurance, savings accounts, digital/e-payments, and remittances available to these targeted demographics. According to the World Bank, more than half a million people benefit from microfinance services, most of them operating in developing nations. MFIs allow their customers to take out loans based on their requirements and repay them according to a pre-determined repayment schedule that includes interest, service fees, and other fees (Julia Kagan, 2021).

The United Nations (UN), designated 2005 as the International Year of Microcredit. By this time, the World Bank, and the Consultative Group to Assist the Poor (CGAP), had helped about 7000 MFIs and 16 million customers. Muhammad Yunus, the creator of Grameen Bank, was awarded a Nobel Prize in 2006 for his work in the microfinance sector. His effort has had a significant influence because he has enabled millions of individuals to obtain credit without having to put up any collateral. His concept has influenced a slew of other institutions throughout the world that provide similar services (Info, 2021).

According to historian Paul Thomas, who sheds light on the subject through trustworthy social and historical viewpoints, microcredit has been a natural cycle for a long time. Its use in Europe during the 18th and 21st centuries were compared by Thomas. N. Srinivasan, who traced the history of microcredit back to numerous religions, including Hinduism, which dates to the fourth century BC. In India, lending with interest is considered one of the 34 religious sins. Several religious books, including the Old Testament, Bible, and Holy Quran, all forbid lending with interest (Sam Mendelson, 2016).

In Europe, the first microfinance activity was recorded in 1720 in Ireland. The main goal of these credits was to provide low-interest loans for the poor segment of the society. Germany launched the world's largest microfinance system in 1778, with three major components: community-based savings, savings mobilization, and rural and urban loans. In 1778, the first Thrift Society’s establishment was formed followed by a communal savings scheme in 1801.

Microfinance was considered as a natural progression for SMEs and microcredit customers who had successfully grown their businesses. They had progressed to the Small and Medium Enterprises (SME) finance level, making them eligible for higher-value financing with various terms and conditions (Seibel, 2003).

Microcredit can have a big social and economic impact on people and communities. Microfinance has a long history in Asia, dating back thousands of years in various forms. In the mid-fifteenth century, Franciscan Catholic orders in Europe emphasized that the world is a small village. Bringing low-income and impoverished people together in their communities and engaging them in mutual economic and social developments to produces communal wealth. Germans were also compelled to establish similar cooperative lending and savings accounts in 1879. To reduce these loans' risks, they only permitted those who were employed to join these institutions, which is analogous to the contemporary credit union systems that operate today.

Researching how to reduce poverty in the mid-1800s, Lysander Spooner concentrated on the benefits of microfinance and small credit for farmers and small business owners. His approach was later credited for poverty reduction until the end of World War II. Like Spooner, Friedrich Wilhelm Raiffeisen and his Village Bank were regarded as cooperative banking pioneers. Between 1864 and 1901, Raiffeisen, as a German mayor and banker, gave over two million loans to underprivileged people, and eventually his Raiffeisen banking system was credited with Germany's extraordinary recovery from WWII's economic devastation. Raeiffeisen banking system was also used as a blueprint for the interest-free Islamic banking system in later years.

From 1900 until 1906, Marie-Clara Dorimène Roy Desjardins and her husband Alphonse Desjardins created an organization in Quebec, Canada, with the goal of providing microcredit loans for the poor and needy. They put their personal assets on the line to construct the organization, and they overcame two major obstacles, namely the establishment of the Caisses Popularizes Desjardins and the passage of microcredit legislation in the National Assembly of Québec. Similarly, Shore Bank was established in 1973 in Chicago, Illinois, with the mission of promoting community microfinance practices.

The European Commission defines SMEs as companies with fewer than 250 employees, a turnover of less than 50 million euros, and a balance sheet of less than 43 million euros. Micro, small, and medium firms are the three sorts of SMEs, as shown in table 1. According to the SME idea, an enterprise that is part of a group's SME status must be computed using data from the entire group's employees, turnover, and balance sheet, rather than only the data from the enterprise itself. The SME guideline specifies how much of the group's information can be utilized to determine whether a company is a small business. Unfortunately, statistical systems find it difficult to fully implement these rules. The financial sheet of an organization is not contained in structural business statistics or other project data sources. As a result, statistics frequently rely on size class information based purely on the number of people employed in the firms, rather than wage, turnover, or balance sheet data from peers. Because firms that are part of a domestic or global enterprise community may fulfill a different function than autonomous enterprises, this has statistical implications. This status, for example, has an impact on their ability to obtain financing, bargaining power, and potential to expand into foreign markets (European Commission, 2021).

Table 1: SME criteria as per European Commission

Description of Company	Number of Staff	Turnover	Balance Sheet
Micro Size Company	<10	≤ € 2,000,000	≤ € 2,000,000
Small Size company	< 50	≤ € 10,000,000	≤ € 10,000,000
Medium-sized	< 250	≤ € 50,000,000	≤ € 43,000,000

Source: Statistics on small and medium-sized enterprises - Statistics Explained (europa.eu)

Micro-SMEs must have fewer than ten employees, while small businesses must have between ten and fifty employees. Similarly, the average size of a medium-sized company's workforce is between 50 and 250 people. The micro-sized company's yearly turnover, or asset portion, is less than 2 million Euros, while the small-sized companies is 10 million Euros. The asset value for medium-sized businesses is estimated to range between 43 million and 50 million Euros.

Companies that pass these evaluation standards reap two major rewards. To begin, they must apply for and be accepted for the European Business Support program, which will provide them with funds for innovation, competitiveness, and research. Second, due to their EU administrative compliance status, they are eligible for a fee reduction (European Commission, 2012).

Conducting this research on Afghanistan was very difficult since it is an economically and politically fragile country with varied population demographics that has long relied on outside aid. The country has a 99 percent Muslim population, has been through several civil wars, and has recently had Russian and NATO military interventions in the country. Afghanistan's political, economic, and social stability has never been achieved since 2002. There aren't enough microfinance programs or organizations to meet demand. As a result, analyzing the difficulties of MFIs and SMEs and coming up with solutions is always a challenge.

Definition of MFI and SME

MFIs provide low-income and needy people and groups with microfinance loans or microcredits to help them become self-sufficient. The objective is to assist those individuals who are normally ineligible for any sort of credit using a loan structure and design. This would not only allow them to start their own enterprises, but it will also allow them to escape the poverty that they currently face (Financial Dictionary, 2021). The size of MFI loans vary by regions within a country, as do the eligibility criteria, which vary depending on the local population's income and economic circumstances.

The World Bank (WB) Group's major goal is to improve SMEs' access to capital by discovering innovative ways to tap into all available financial resources. Despite their small size and volume, SMEs play a critical role in the overall global economy. They outnumber big sized firms by a large proportion, employ more people, are more entrepreneurial, and contribute to new and innovative businesses.While there is no established procedure for identifying SMEs in the United States, the European Union (EU) has more specific definitions. The EU defines a small firm as one with less than 50 employees and a medium-sized business as one with fewer than 250 employees. In addition to small and mid-size firms, there exist micro-companies that employ less than ten people.

Between 2002 and 2012, SMEs were responsible for 77 percent of the new job growth in Canada. The United States had very similar rates. Between 1993 and 2011, SMEs created 64 percent of the net new jobs. For most of other industrialized countries, the situation was not any different. SMEs are vital to every country's economic well-being, both in terms of creating new jobs and generating tax revenues (Liberto, 2020).

Microfinance and SME History in Afghanistan

In Afghanistan, MFIs and SMEs have nearly two-decades of history. Most Afghan migrants residing in neighboring countries such as Iran and Pakistan returned to Afghanistan once the post-Taliban government was established in the early 2000s. The number of migrants returning home was extremely high, and the country's resources were insufficient to meet the demands of all the newcomers. For many of the newcomers who were unable to find work, starting a small business was the most popular answer or the alternative to finding jobs. That is why international donor groups have agreed to run and fund a variety of microcredit initiatives in Afghanistan. As time progressed, these tiny organizations matured into bigger microfinance organizations and banks. The Microfinance Investment Support Facility for Afghanistan (MISFA) was founded in 2003 in response to these developments. The MISFA's stated goals were to "coordinate and combine" competing donor goals (MISFA, 2019b).

MISFA formed Afghanistan Microfinance Association (AMA) in 2005, and it became operational in 2010 (Afghanistan Microfinance Association, 2021). Afghanistan Institute of Banking and Finance (AIBF) was established by the Central Bank of the country and began its operation in the same year (AIBF, 2010). Table 2 below lists all members of AMA.

Table 2: Members of AMA

S.#	Name of Organization	Sectors
1	The First MicroFinanceBank	Bank
2	Exchange Zone	Microfinance Institute
3	FINCA	Microfinance Institute
4	IIFC Group	Microfinance Institute
5	MUTAHID DFI	Microfinance Institute

6	OXUS Afghanistan	Microfinance Institute
7	ARFC	Finance Institute
8	AWC	Community-based Saving Promoting Institutions
9	Aga Khan Foundation (AKF)	Community-based Saving Promoting Institutions
10	HAND IN HAND AFGHANISTAN	Community-based Saving Promoting Institutions

Source: Afghanistan Microfinance Association

The following are the MFIs and banks that are currently participating in the Afghanistan market. The First Microfinance Bank was founded in 2003 with the help of Aga Khan Fund for Economic Development (AKFED), Kreditanstalt fur Wiederaufbau (KFW) and the International Finance Corporation (IFC). There are 32 branches and active work in 14 provinces. FMFB disbursed a total of AFN 9 billion in microfinance and AFN 61.7 million in SME loans. (FMFB Afghanistan, 2021). FINCA started its activity in 2003. Initially it worked in 11 provinces, but recently this number dropped to only 8 provinces. FINCA made cumulative loan disbursed of AFN 1.9 billion in microfinance and AFN 15 million in SME (FINCA Afghanistan, 2021). OXUS started its function in Afghanistan in 2007, which operated in 10 provinces until 2020. OXUS made disbursed AFN 2.2 billion in microfinance and AFN 9.7 million in SME loans. (Oxus Netowrk, 2021) MUTAHID merged six MFI such as MOFAD, MADRAC, PARWAZ, ARIANA, CHF, and WWI. MUTAHID disbursed the cumulative loan on microfinance is AFN 295 million and AFN 6 billion in SME (MUTAHID DFI, 2021).

The majority of MFI and SME loan products are based on loan sizes of less than $ 200 for ultra-poverty, $200-$5000 for microfinance, $5001-$200,000 for SME loans, and more than $200,000 for commercial loans. The flat interest rate scheme is utilized for short periods between six months and one year. When it comes to large loans, the loan system is depleted. which specify the loan product category as well as the interest rate (March, 2016).

List of Banks and MFIs Which are Closed Down or Merged with Others

Below is the list of banks and MFIs which are currently closed-down or merged with other institutions in Afghanistan.

Table 3: List of Closed MFIs and Banks

S.#	Name of MFI and Bank	Status
1	Afghanistan Microfinance Institution (AMFI)	Closed
2	Bangladesh Rural Advancement Committee (BRAC-Bank)	Closed
3	Child Fund Afghanistan (CFA)	Closed
4	Hope for Life	Closed
5	Sunduq (Khadamati Maali Sunduq)	Closed
6	World Council of Credit Unions (WOCCU)	Closed
7	Afghanistan Rural Microcredit Program (ARMP)	Merged with FMFB
8	Ariana Financial Service (AFS)	Merged with MUTAHID
9	Micro Finance Agency for Development (MoFAD)	Merged with MUTAHID
10	Microfinance Agency for Development and Rehabilitation of Afghan Communities (MADRAC)	Merged with MUTAHID
11	Parwaz Microfinance Institution	Merged with MUTAHID
12	Women for Women International (WWI)	Merged with MUTAHID

Source: Compiled by the Researcher

Key Indicators of Microfinance Organizations According to AMA

Table 4 below shows all the key indicators for banks, MFIs, and other community-based saving programs as shown in its December 2020 report.

Table 4: Saving by MSME Institutes

Institute Name	No of Province	No of Branches	No of MFI Staff	No of Loan Officer	No of Client	% of Women	No of Active Borrower	% of Women Borrowers
FINCA Afghanistan	10	19	322	130	21,872	56%	21,872	56%
IIFC Group	11	25	216	68	115,969	26%	13,769	20%
Mutahid DFI	6	8	236	112	14,397	37%	14,397	37%
OXUS Afghanistan	10	23	455	220	21,451	53%	21,451	53%
Sub-Total		***75***	***1,229***	***530***	***173,689***	***34%***	***71,489***	***44%***
FMFB Afghanistan	14	38	1,470	487	212,895	24%	50,145	24%
Sub-Total		***38***	***1,470***	***487***	***212,895***	***24%***	***50,145***	***24%***
Aga Khan Foundation	7	17	48	32	35,094	71%	4,815	73%
WEERDP	34	76	1,464	206	397,464	81%	93,953	84%
Hand in Hand Afghanistan	4	2	66	23	2,529	100%	522	100%
Sub-Total		***95***	***1,578***	***261***	***435,087***	***81%***	***99,290***	***83%***
Grand Total	**34**	**208**	**4,277**	**1,278**	**821,671**	**56%**	**220,924**	**57%**

Source: AMA Report

The final three organizations are not included in the microfinance category since their primary activity is with a community-based organization called Saving Promoting Institute, which operates in 34 Afghan regions. Banks and MFIs, on the other hand, operate in just 14 provinces: the capital and a center region, the North, Northeast, Eastern Part, and West Provinces (AMA, 2020).

Islamic Microfinance Products

While the Central Bank of Afghanistan gave the first Islamic bank license in 2018, several commercial banks and microfinance institutions were already offering Islamic banking products. Table 5 below lists the primary Islamic banking products available in the industry (Central Bank, 2018). Even though the banking industry offers a variety of Islamic banking products, Afghanistan lacks an Islamic banking and finance body to oversee their activities (Hamid, 2016).

Table 5: Primary Islamic Banking Products

S.#	Product Name (Meaning)	Description
1	Qard-Hasan (Benevolent/Interest-free loan)	It is interest-free but administrative costs, or another indirect cost might be added
2	Wadiah (savings and current accounts)	It is practiced same way as in conventional banks, but no return is guarantied. Instead, it can get unspecified added gift (Hadia or Hibah)
3	Modaraba (labor capital partnership)	It is based on Asset in one part and Liability in another party, the profit will be shared among them according to prior title deed
4	Bai-Istijrar (repeat purchases from a single seller)	This practice is for a customer who is loyal and continues to buy products from the same person.
5	Salam (Forward Sale)	Prepayment made to purchase products at a particular time. Mainly in agriculture to use in later seasons.
6	Musharaka (Partnership)	Based on the agreed ratio of profit and loss shared between parties.
7	Murabaha – Cost Plus Sale	This product is used for financing a fixed asset
8	Ijara – Islamic Lease	Products and goods are bought by Banks & MFIs, for leasing to the customers in an instalment schedule.
9	Istisna - Manufacturing contract	This type of product is used for manufacturing products, to receive a commission in advance or sale is finalized.
10	Mugharassaah (sharecropping)	Banks finance the farmer and then get their shares upon harvesting the goods.
11	Takaful (Insurance)	Insurance is required for the preservation of goods.

Source: Compiled by the author from websites of MFIs and banks

Difference Between MFI and SME

MFIs and SMEs do not operate under the same set of rules, which is why they are classified differently. Larger banks and companies can be found operating in this sector in wealthier and larger countries, however in underdeveloped countries like Afghanistan, there are only a few SMEs providing public services. While we see a lot of microfinance clients including general businesses, bakeries, and barbershops, we don't see any larger banks or corporations (Wala, 2021).

At first glance, and for some individuals, microcredit, microfinance, and SMEs may appear to be the same thing, but they are not, and there are several key differences between them. Individuals and organizations whose income is below average and who are occasionally unemployed are targeted for microcredit loans. Borrowers in this sector are not required to obtain collateral in situations such as the loan amount being below a specific threshold, despite their poor credit scores and high-risk levels. SME loans are for those individuals and companies who are in the process of raising their standard of living. They can considerably enhance their production and earnings by purchasing extra assets and machinery. These kinds of loans and funds also have a favorable effect on the unemployment rate. (Ashish M. Shaji, 2017)

2. LITERATURE REVIEW

For this study, the researcher investigated both directly and indirectly connected research publications on the issues of microfinance and SMEs for this study. The research focuses on the present COVID-19 epidemic, the microfinance sector in neighboring countries, microfinance and Islamic products, microfinance and SME, microfinance and social elements, and microfinance and SME in Afghanistan.

Zheng & Zhang conducted a research titled, "The Impact of COVID-19 on the Efficiency of Microfinance Institutes." They discovered that the COVID-19 pandemic had a significant detrimental influence on the social and financial realms during their research. It was extremely difficult to obtain money and access to capital. Demand and supply were out of whack. The social efficiency of microfinance was severely harmed. It was extremely difficult for low-income earners to keep up with their repayments. The performance of microfinance institutions deteriorated, while the Portfolio at Risk (PAR) skyrocketed. Microfinance institutions' downsizing has become a trend for them to continue functioning in the same market. Salaries, bonuses, allowances, and fixed and other variable expenditures were the key areas of reduction. They investigated several topics and discovered that COVID-19 had a beneficial impact on MFI demand in the field of social development (Zheng & Zhang, 2021).

Ariel Nabus Delfino authored a research article titled, “Impact Pathway Analysis and Sustainability Evaluation of Microfinance Projects in Goa, Camarines Sur, Philippines.” Project sustainability was assessed using both quantitative and qualitative techniques in this microfinance study. According to the findings of this study, microfinance initiatives saw a 9.8 percent increase in business profitability between 2010 and 2013. Six MFIs are identified in the study, with the goals of tracing paths, measuring performance indicators, performing activities with correspondence, and compiling results and impacts reports. The performance of MFIs was positively influenced by the awareness of household beneficiaries who were self-employed. The study also reveals that these industries face various concerns in terms of sociopolitical and economic reasons (Delfino, 2016).

Edaich and Smietanski authored a research article titled, “Islamic Microfinance Model and Hypothesis of Poverty Alleviation.” They concentrate on the use of microfinance and other Islamic banking features to alleviate poverty and enhance people's lives. The study focuses on Islamic microfinance programs, which in Islamic nations can be a superior alternative to traditional banking products. The investigation employed official data for their study which focused on the growth of microfinance in Indonesia as a case study. Saudi Arabia's Kafalah funds are also discussed in the report. In addition to Indonesia, the study looked at other Islamic countries' GDP growth rates as reported by the World Bank. Islamic microfinance might have a substantial impact on alleviation of poverty in Muslim countries. Due to a lack of governmental rules and regulations, microfinance and Islamic banking have limits as well. People become financially and socially weaker because of these inadequacies (Edaich & Śmietanski, 2020).

Ike Kusdyah Rachmawati, Agus Rahman Alamsyah and Eko Aristanto conducted a research on SMEs called, "Model of Accommodating Microfinance Institute for SMEs." MFIs, according to the report, are the intermediates who create beneficial settings for both the clients and the economy. If they work properly, they can contribute value to the economy. According to this study, even small firms can become the backbone of a country's economy. These tiny microfinance organizations, particularly those owned and controlled by female microfinance consumers, will have the ability to influence how large corporations function. Finally, these increased commercial activities will result in the creation of jobs and a reduction of unemployment. The fundamental goal of this article is to concentrate on long-term economic growth, the development of sustainable neighborhoods and districts, and the creation of more job possibilities. It also goes over the job functions of staff in MFIs and SMEs in great detail. In summary, the article examines all the MFIs' operational actions in depth for the reader (Ike Kusdyah Rachmawati, Agus Rahman Alamsyah, Eko Aristanto, 2019).

Javier Sierra, Victoria Muriel-Patino and Fernando Rodríguez-Lópeza conducted a research titled, "The Quest for the Evaluation of Microfinance Social Performance." The study demonstrates that different institutes and standards use financial performance to determine the social impact of microfinance. The methodologies that underpin the modifications are based on the rate at which existing operations are progressing. This paper employs a variety of evaluation techniques. MFIs were judged on five different social parameters, including their social mission, commercial success, and implementation. Although the SP14 assessment and performance method was utilized, which is the most often used method, the data on 195 types of microfinance social evaluations that have been deemed acceptable by stakeholders is not accurately calculated (Sierra et al., 2020).

Martin Greeley and Mohit Chaturvedi conducted a research titled “Microfinance in Afghanistan: A Baseline and Initial Impact Study for MISFA.” The relevance of the government and international donors working together to create MISFA as an organization in Afghanistan was the focus of this study. Poverty, migratory populations, rising inflation, the breakdown of the banking system, a short-term focus rather than long-term sustainability, and many other issues plague post-conflict civilizations. Each MFI has 30 clients in the data sample. Most of the data was gathered from 11 provinces, which account for 95% of MISFA's clients (Greeley & Chaturvedi, 2014).

3. METHODOLOGY

For this study, attempts were made to integrate both qualitative and quantitative methods, keeping in mind the importance of methodology. The qualitative data was gathered from both primary and secondary sources, including interviews. Quantitative data was gathered via publications, websites, periodicals, indexes, and other widely distributed documents.

Population and Sampling

Microfinance and SME in Afghanistan provided the sample used for the research. Top-level management, department heads, loan managers, loan officers and consumers were included in the interview group. A total of 50 individual were included in this batch. Former and current employees of MFIs and SMEs, as well as their clients took part in the interviews. Board Directors, Chief Executive Officers, Chief Operational Officers, Microfinance Directors, SME Directors, Risk Management

Directors, and Finance Managers were among the personnel. It's also worth remembering that this group contained both expatriate and local employees.

Scope and Limitations

The difficulty of accessing information is the most significant obstacle while conducting MFIs and SMEs research in Afghanistan, since many of these institutions operate in a highly secretive manner. In addition, the lack of technology and high internet costs made it difficult to obtain information from outside sources. We faced additional challenges in completing this study due to the absence of accurate and credible publication on this topic.

Research Design

Multiple individual and group interviews were undertaken to ensure the efficacy and accuracy of the data while attempting to answer the question of why microfinance and SMEs in Afghanistan are not self-sustaining, and why demand for MFI products has risen dramatically since the Taliban rule ended. These and other poll questions were posed to a diverse group of stakeholders who represent Microfinance in the marketplace. The research design not only included reviews of current performance indexes on the growth and performance of MFIs and SMEs published by independent international organizations and Afghan institutions, but also researched historical background and performance of MFIs and SMEs operating in the country.

The research is a cross-sectional study that investigates the availability of funds in the market based on MISFA's balance sheet and the individual SMEs' balance sheets. Questioners and interviews were used to investigate management deficiencies, the sector's capacity, quality control, and stakeholder relationships.

Scope of Studies

The study looked at the functions and performance of recent and currently operational MFIs and SMEs. The scope of this analysis includes 91 percent of Afghanistan's existing microfinance market share. The study also looked at microfinance programs and firms that have recently collapsed, gone bankrupt, or merged.

Research Methods

Two types of questionnaires were created for the study. Interviews were done using WhatsApp, Messenger, and other social media platforms, and they were shared with appropriate parties via email. The goal of the data gathering was to have a better understanding of MFI problems from various perspectives in order to conduct accurate analysis and make relevant recommendations.

The questionnaires were created and distributed to Microfinance Institute stakeholders. The interview questions and issues were diverse in nature. The interviews were performed with microfinance employees from various districts in Afghanistan. Climate, culture, sociology, and behavior are all varied in the areas where microfinance organizations operate. To reduce the effects of geographical and demographical factors, the data collection was spread out over a greater area.

Interviews were performed with around 50 MFI employees who were currently employed in the business or have previously worked employed for the firms. Interviews were performed with 20 microfinance customers and 15 SMEs customers to have better understanding of their perspectives and assess their satisfaction with MFI products. Ages, qualifications, business ranges, religion, and genders were all represented among the respondents. The purpose of the interview was to determine the volume, efficiency, and efficacy of the MFIs. Most of the interviews were conducted in a multiple language setting, taped and later translated into English.

Source of Data

Present and prior top management of MFIs, MISFA and other stakeholders, such as present and past clients who served by the industry, as well as the public, were the sources of data. Reports, publications, research articles, and annual financial reports were also gathered from the websites of MISFA, AMA, and MFIs.

Data Processing and Analyzation

The comprehensive and well-analyzed data aided in answering the research topic. The information was filtered, and the data was sorted to distill the desired responses. Sorting, categorization, data reduction, and summarization were among the procedures used. For data analysis, IBM's SPSS application was employed. Figures, tables, and graphs were used to present the results of the interviews and questionnaires.

Problems and Limitations

Some microfinance institutions, unfortunately, do not report their performance on their websites. Some of them describe their activities, but the researcher found the lack of precision to be a severe difficulty. Ex-employees of the organizations who are now employed by other firms were not interested in participating in the interviews. Another constraint was the difficulty of getting to and from Afghanistan, and the only method of contact with participants was via Skype, WhatsApp and Facebook Messenger. Contact with the participants required excessive amount of time due to Afghanistan's outdated infrastructure and internet connectivity. Participants’ location in different time zones created difficulties to contact them on appropriate times. Some interviewees withheld information while data collection due to fear of disclosing sensitive confidential information.

4. DATA ANALYSIS AND FINDINGS

Although there are multiple issues, only the most important obstacles and anomalies are highlighted in this section. These issues were discussed in depth during interviews with the top executives from MFIs and SMEs.

The most important issue addressed in this article is as follows:

Collateral

Microfinance institutions utilize original title deeds of land and houses as collateral for loans, and they restore them to the original owners till the loan is paid off. For all microfinance institutions, the method of putting liens as security for delinquent loans is the same. Due to the lack of a centralized agency to issue these titles deeds, clients who possess a single property may be able to get multiple microfinance entitlements or identification cards known as Tazkira.

According to statistics, these difficulties were quite prevalent until 2014, when the Afghan central bank began executing the Public Credit Database (PCD) program which was initiated in 2008. As a result, a considerable number of MFIs failed, went bankrupt, or merged with others during the 2002–2014 period.

Sharie, a government-registered; and Horofi, a written informal title are the two examples of title deeds that exists in Afghanistan. One of the most difficult aspects of title deeds is determining the worth of the land that is titled.

The court order has been amended to allow MFIs and banks to register collaterals. It takes two months to lodge a lien on a property's title deed. There is a 3% cost on the contract value and another 3% cost when the loan is paid off. The cost of transferring title deeds as security to banks is 6% of the property’s value, and another 6% is paid when the property is returned to the owner for a total of 12% cost.

Management Information System

MFIs and banks make significant investments in infrastructure for technology hardware and software. Since most of these firms are smaller and without large expense funds, they receive grant funding to purchase these software packages. As stated in the introduction section of this study, each firms’ culture was shaped and influenced by various international parent organizations, so most of these MIS do not meet their specific needs. During an interview with one of the CEOs who participated in the interview, it was mentioned that the AMA should serve as a link between donors and MFIs. This bridge will aid in the discovery of solutions and the acquisition of funds required to establish a solid management information system (Saba, 2019).

There have been 39 government and 128 private universities and institutes since the Taliban regime's inception until 2021. Most of these academic institutions have Information Technology departments. Unfortunately, none of these institutes has been able to create a local Management Information System that meets a high international standard (Ministry of Higher Education, 2021).

MISFA supported the establishment of a grant for some of the MFIs to purchase efficient and effective software for their MIS. The MIS purchased was dubbed Afghanistan's premier Microfinance core banking system. This software allowed FINCA MFI to carry out functions, conduct internal audits, and control and meet policies developed by the Global Corporate Audit (GCA) for reporting, auditing, and securing microfinance institutes in the country (MISFA, 2019b).

In MFIs, management information systems are one of the most expensive areas. For all MFIs, a lack of trained employees and the expensive cost of supporting them from outside is always a major barrier. Financial statistics from MFIs and banks indicate that a significant amount of money is invested in this area. Despite this, the government and local MFIs are unable to develop a MIS that meets the needs of Afghanistan's geography.

Client and Staff Behaviors

Human resources is concerned with both client and employee conduct. As a result, our research aims to shed light on this topic, since it is very important for the microfinance sector. Because microfinance clients have smaller salaries, they are always on the move and traveling. They are not devoted to keeping their commitments and honoring the agreements they have made with MFIs. SME clients are generally concentrated in urban regions due to the size of their loans and the value of their collateral. When it comes to staff behavior in the Microfinance and SME sectors, employees appear to be short-sighted. Most of the employees are looking for ways to get ahead in their careers. The norm has been for MFIs and SME sectors to make investment and lending choices based on emotions.

Due to decades of violence, it is impossible to compare Afghanistan's problems with those of any other country in the globe. The struggle has had a significant impact on the behavior of the average person, who is primarily concerned with short-term profits and hopes for a speedy recovery from financial hardship. Actions like these result in unethical behavior on part of both the client and the organization's staff. The following paragraphs expand on the common practices which was observed.

It was discovered that group loan products were being abused. These loans, for example, were made available to female clients, but these women were usually coerced by their male spouses to secure the loan and pass the proceeds on to them. As a result, loans were used for non-income generating activities, resulting in a high number of defaults.

Some MSME organization staff (primarily loan officers in collusion with their supervisors) also engaged in corrupt practices and obtained kickbacks on loans. Furthermore, some employees stooped to the level of issuing and repaying fictitious loans to themselves. It was discovered that they began the cycle with a low-interest loan, progressed to a high-interest loan, and then embezzled the entire amount, which amounted to $100,000 US dollars.

Client Identification Issues

Afghanistan was decades behind the global technological revolution, so national identification was primitive. There are still paper-based IDs in use, whereas other countries manage their citizens' data on computerized systems. The paper-based system, combined with high levels of corruption, has created a chaotic environment in Afghanistan, effectively paralyzing the financial services sector. Because of the system's flaws, microfinance clients can obtain multiple loans from multiple organizations by using multiple IDs. After stealing so much money from these MFIs, they default on their loans, causing millions of dollars in losses to their organizations. MISFA and international agencies did not put enough effort into this issue in the past to implement a biometrics system to close this loophole that allows massive fraud.

Clients of microfinance are typically low-income individuals who live in rented housing. Most clients move and change houses on a regular basis. It is difficult and time consuming to keep client records up to date. Most frauds are discovered when clients miss their loan payments and default on their loans. As a result, the organizations' PAR values rise as an indicator of ongoing fraud.

In 2014, the Afghan government approved Tazkira electronic identity cards, which include the ID card holder's name, language, mother's name, religion, and other information. Unfortunately, the implementation of electronic ID cards has been pushed back until 2020. Currently, the process of obtaining electronic ID cards is extremely slow. Afghanistan's Vice President expressed dissatisfaction with the delay in implementing the electronic Tazkira. The Afghan government took six years to launch the electronic ID card system, and still, it is not fully functional (BBC, 2021).

Afghanistan's Ministry of Interior has begun to issue electronic ID cards in Kabul and other major cities. It is hoped that this process will be completed across the country soon, and that everyone will have an ID card. The completion of the electronic ID project will eliminate duplicate applications and MFI fraud.

Security and Law Enforcement

According to several recent reports from international and national news outlets, Afghanistan is one of the world's most corrupt countries. The Daily Mail UK reported in 2008 that Afghanistan is the world's fourth most unstable country. (UK, 2008) This means that the stability of the government is dependent on law enforcement. In some key areas, the Afghan government has been unable to support and implement its own laws. Another report published in 2011 by the United Nations Assistance Mission in Afghanistan (UNAMA), states that Afghanistan failed to implement laws enacted in 2009 to prevent violence. In Afghanistan, the culture of silence among tribes is always questionable. Jerga is a gathering of tribal elders, and their decisions take precedence over constitutionally legislated laws in tribal rural areas (Huwaida, 2011). Afghanistan was named the most corrupt country in 2017 by Transparency International's annual corruption perception index. Corruption in government has a domino effect that affects every area, including most of MFI institutions (News, 2018).

The main problems in this area are a lack of security, corruption, a failure to enforce the law, and a lack of support from government institutions. This creates an environment devoid of law and order, in which the guilty get away with their crime and believe they have the freedom to continue their fraudulent activities. According to a study on the subject, submitting fraud complaint cases in Afghanistan is time consuming and complicated. It can take months, if not years, to see any results. On other occasions, the amount of fraudulent loans is usually insufficient to warrant prosecution by a lawyer. Initially, some MFIs referred their fraudulent cases to the legal system, but the outcomes were not favorable to MFIs. This has created an environment in which businesses are discouraged from seeking relief and assistance from government entities. Some of the Judges even advocate for the total prohibition of interest-based institutions in Afghanistan.

According to the MISFA's annual report on microfinance and MFI activities in 14 out of the 34 provinces, security is the number one concern to the industry (MISFA, 2019a).

High Cost of Finance

The majority of microfinance and SMEs secured loans with annual interest rates ranging from 20% to 40%. Many microfinance SMEs' clients couldn't afford this rate because they were already poor and struggling to make ends meet. Payment of such high interest rates had a negative impact on their profitability, and those who couldn't afford it went out of business or defaulted on their loans. These kinds of situations resulted in not only the loss of the business, but also the loss of jobs and the re-enslavement of their families. Because Afghanistan lacked a social welfare system, these clients' lives were made untenable. Expatriate employees were also able to secure high remuneration because their salaries included danger pay due to working in a risky country. Security, computer hardware and software, power, generator fuel, leasing charges, and expensive management compensation all add to the cost of operation, making self-sustainability unattainable.

Table 6 is an example of a microfinance Loan Officer's average performance calculation, which reflects the revenue creation of a Loan Officer for the Microfinance Institute. Although the direct cost of Loan Officers to the MFI is quite low, other essential factors such as indirect fund and support costs are very high. The performance of about 30% of Loan officers is listed below as a benchmark based on historical data from interviews.

Table 6: Average Calculation of MF Loan Officer Revenue

Average Loan size for a loan officer to match the equilibrium points		
Account Head	**Amount**	
Average Loan	104,000.00	
Average Number of Loan		160
Total Portfolio of Loan officer	16,640,000.00	
Average Interest rate 22%	3,660,800.00	

Average Expenditure of Loan Officer		
Account Head	**Monthly Amount**	**Annually Amount**
Salary	16,000.00	192,000.00
Transport	2,500.00	30,000.00
Medical	1,000.00	12,000.00
Field Allowance	8,000.00	96,000.00
Commission	25,000.00	300,000.00
Top Up Card	2,000.00	24,000.00
Eid Bonus Twice A Year		3,000.00

Total Direct Expenses	**657,000.00**
Profit/(Loss)	**3,003,800.00**
Provision Expenses 8%	1,331,200.00
Cost Of Fund Average 6.5%	1,081,600.00
Branch Cost 2%	332,800.00
Head Office Cost 1.5%	249,600.00
Profit/(Loss)	**8,600.00**

Source: Compiled from MFIs reports

Personal expenses, such as salaries and benefits for local and expat personnel in the microfinance business, appear to be very high, based on the above table from FMFB's financial reports. In comparison to overall sales, this number was 54 percent in 2020 and 46 percent in 2019. Communication expenses, insurance, office security, IT maintenance and support, travel and transportation, and generator fuel and maintenance are examples of operational costs incurred by this account head. Some of these operational expenses will account for 30% of total revenue in 2020 and 36% in 2019. In 2020, amortization and depreciation from assets were 11%, compared to 9% in 2019.

According to the data, Afghanistan's operational costs are quite expensive. MFIs take a long time to amortize and become self-sufficient in the market.

5. CONCLUSION AND RECOMMENDATIONS

The findings in this section discuss and emphasize the significant problems and challenges that microfinance and small businesses face today in Afghanistan. The historical evolution of MFIs and SMEs in the Afghan market from 2002 onwards is covered in the introduction section of this article. MFIs and SMEs offer variety of products, including Islamic financial products, which are currently available on the market. The number of successful MFIs now operating in Afghanistan, as well as the number of banks and MFIs that have collapsed or gone bankrupt owing to poor performance or insolvency, were also documented.

The researcher draws attention to serious and actual problems that MFIs face, for which answers are urgently needed at the national and, in some cases, worldwide levels. The research concludes that the microfinance and SME sectors are still not operational and self-sustaining after two decades of operation, based on the hypothesis and related research topics examined in this thesis work.

The topic of collateral, which is one of the most crucial challenges for the MFI and SME lending sectors, was examined. Several regulations have been altered during the last 40 years because of various legislations that have impacted the enforcement and quality of collateral, which are vital safeguards for lending and functioning financial institutions. Despite enacting over sixty different types of regulations and modifications over the previous forty years, meaningful answers to the sector's and society's social and moral concerns have yet to be found. As a result, the researcher's recommendations include that the Afghan government analyze them and try to build a system that improves the quality of the collateral so that financial institutions can rely on it (Temizkan & Yılmaz, 2020).

According to the findings, entrepreneur clients, MFI, micro, and SMEs staff behaviors are critical in protecting the assets used in lending procedures and limiting the portfolio at risk. The behavior of some clients and personnel has been explored in the interpretation section, and it has been seen that some individuals wish to achieve their goals by unethical shortcuts that are destructive to themselves and the financial institutions with which they interact. Clients and employees have orchestrated several frauds in the microfinance and SME sectors. These fraudulent practices were previously described as using distributed loans for non-business expenses such as wedding expenses, personal purchases, and other non-income generating activities. Fraudulent paperwork, fake IDs, and collusion with clients and senior staff to manufacture fake and unworthy loans are currently afflicting this industry and necessitating immediate answers.

Afghanistan still lacks proper security arrangements to ensure the protection of its population, and educated or more skilled persons who are constantly drawn to immigrate to other countries. As a result, brain drain, and the loss of qualified personnel is a major concern for Afghanistan. Hard-to-find monies are spent on training and capacity building for workers who will depart the organization and the nation in a few years. This sad spiral not only stymies the growth of a robust microfinance and SMEs sector, but it also encourages qualified persons to leave the nation. The establishment of law and order could help the microfinance and SME sectors grow in a variety of ways, because businesses can only thrive in supportive conditions, with security being one among them. Security has an impact on financial institution operations, from cash transfers between branches to enforcing laws against defaulting clients, fraudulent employees, and collateral seizure in the event of default. Due to ongoing governmental changes, Afghanistan's historical security structure has changed ten times in the last five decades. Exacerbating the problem is the Taliban's continued occupation of Afghanistan, and the failure of peace talks. If the Taliban takeover occurs again, interest-based banking and microfinance will be impossible to operate, since the Taliban's view of interest-based financing is exceedingly restrictive. It happened in the calm province of Bamiyan in the past, when religious leaders issued a Fatwa, and many microfinance and SMEs clients failed to return their loans (Yetgin, 2016).

According to the findings, one of the most serious problems that Afghanistan has in the twenty-first century is the lack of an effective customer identification system. Establishing an adequate electronic identification card system would benefit not only the microfinance and SMEs industries in terms of loss prevention, but also the country's social, demographic, and criminal management challenges.

Each regime in power in the country made minor revisions to the country's title and deeds laws to address the issue, but Tazkira, the country's title and deeds database and identity system, remains broken. The Ministry of the Interior recently released an electronic ID system that adds more information to the title ID, but it, too, need adjustments and usefulness. The system, which contained information on the ID owners' nationality, religion, ethnicity, and mother's name, required many years to install in one of the most conflict-ridden areas. The government unveiled the final version of the identity system in 2020 with high aspirations, but it is too early to judge how effective it would be, or how much the MFI will trust it.

For financial institutions, MIS and IT technology is a useful tool for analyzing, reporting, and interpreting data. After conducting numerous interviews and completing our research, we were able to confirm that most financial institutions in the country purchased their MIS and support from India due to its low cost, but that the systems and support they receive are still below industry standards in terms of actual hands-on support and training.

The high cost of borrowing is the final key factor examined in this study as to why MFIs and SMEs in Afghanistan cannot be self-sustaining. The high cost of funding is attributed to the greater operating costs of doing business in Afghanistan compared to other regions of the world, however this must be reduced to a manageable level. Only four of the fifteen MFIs and banks that have received licenses from the Afghan government in the last two decades are still active. Better management, internal controls, and employee devotion to their companies are the success elements at the backend of these four institutes.

Finally, MFIs will face additional hurdles and difficulties in the future because of the three major concerns now affecting Afghanistan. First, there is the long-term impact of the ongoing COVID-19 pandemic, which will limit MFI activities. Second, if the Taliban retakes power in the country, they may restrict traditional or interest-based loans, creating additional demand and opportunities for Islamic banking and interest-free goods. The third factor is Afghanistan's excessive reliance on foreign help. In many sectors, there will be no business left if the country's security deteriorates and civil wars erupts.

To summarize, the current state of MFI and SME in Afghanistan is alarming, and despite significant international investment over the previous two decades, little has been accomplished. Furthermore, the situation appears even bleaker, given that Afghanistan is currently undergoing another Taliban takeover, a potential civil war is brewing, a drought is expected, and financial instability is on the rise. Some of these MFIs start recovering only principal of loans which were disbursed. As a result, there is a greater need for strategic management tecknique s and added efforts to fix the ailing current microcredit, Islamic banking and MFIs in Afghanistan.

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