



ARIES

Agriculture, Rural Investment
and Enterprise Strengthening
Program in Afghanistan

WOCCU-IIFC
Program Brief No. 1



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The Financial Integration, Economic Leveraging, Broad-Based Dissemination Leader with Associates (FIELD-Support LWA)

The ARIES Program is a sub-award under the FIELD-Support Leader with Associates (LWA) cooperative agreement — a single, 5-year award created to both advance the state-of-the-practice in microenterprise development and microfinance as well as assist USAID missions and other operating units to design and implement innovative, integrated, market-based approaches to sustainable economic growth with poverty reduction.

Through sector assessments, program design, technical evaluations, and implementation of multi-year projects, FIELD-Support allows USAID Missions and other operating units to pursue their strategic objectives to:

- Strengthen livelihoods and food security for marginalized groups, youth, women and other vulnerable populations such as people affected by HIV/AIDS and natural disasters;
- Foster enterprise development, job creation and broad-based economic recovery in conflict and post-conflict situations as well as other fragile environments;
- Extend the reach of microfinance and develop more inclusive financial systems;
- Upgrade and improve the competitiveness of value chains in which microenterprises participate; and
- Facilitate institutional strengthening and policy reform for broad-based economic growth.

WOCCU–IIFC Program Brief

The following is one in a series of briefs highlighting the experiences and lessons learned under the USAID Agriculture, Rural Investment and Enterprise Strengthening (ARIES) Program. A \$100 million, three-year initiative, ARIES aims to create a strong private sector foundation for a sustainable, market-driven rural finance system in Afghanistan. ARIES targets USAID's Alternative Development Program (ADP) regions in the east, south and north of Afghanistan, as well as Herat Province in the west.

ARIES is managed by the Academy for Educational Development (AED) in partnership with ACDI/VOCA, the World Council of Credit Unions (WOCCU), the Microfinance Investment Support Facility for Afghanistan (MISFA), FINCA and ShoreBank International (SBI). Each partner focuses upon a different component of the financial landscape, from household micro-loans of less than \$200 to loans of over \$1 million to larger scale Small and Medium Enterprises (SMEs). In addition, WOCCU's affiliate in Afghanistan also offers savings services to members.



Activity Profile

Goal: The objective of the ARIES partnership with WOCCU is to support the growth of the microfinance sector by expanding WOCCU's network in the Program's targeted regions. Specific targets set for WOCCU for the end of the ARIES Program include expansion through creation of 18 new Islamic Investment and Finance Cooperatives (IIFCs); and the disbursement of a cumulative total of 36,700 loans worth US \$21.2 million.

Implementing Partners: ARIES' sole implementing partner for the expansion of the IIFC network is WOCCU.

Funding Level: ARIES initiated its partnership with WOCCU through a US \$21.4 million grant in 2006. As one of MISFA's microfinance partners, WOCCU also receives grants and loan capital from MISFA, as well as earmarked funding from CIDA, DFID, and NOVIB, to support its other, non-ARIES IIFCs.

Role within ARIES: The WOCCU/IIFCs offer individual and group loans, as well as savings products, from under US \$200 to \$5,000. Within the overall scale of ARIES' partners' financing, this is in the upper range of microloan sizes, as ARIES' other microfinance partners provide loans of \$100 to \$2,000, and its SME partners offer loans from \$3,000 to over \$1 million.

Overview

WOCCU, a US-based international trade association and credit union development agency, operates in 97 countries with the goal of promoting access to affordable financial services to underserved communities through the development of credit unions that are owned, controlled and operated by their members.

WOCCU began its operations in Afghanistan in 2004 with a one-year, US \$1 million grant from MISFA to develop Afghanistan's first network of credit unions. Though the credit union concept of cooperative ownership is largely in line with *Sharia* (Qur'anic law) as it is interpreted in Afghanistan, WOCCU re-labeled its credit unions in Afghanistan "Islamic Investment and Financial Cooperatives" (IIFCs) to avoid the use of the word "credit," which is often associated with interest prohibited according to a strict interpretation *Sharia*. With

ARIES support, WOCCU has been expanding its network of IIFCs in the USAID's target ADP areas in the east, north and south regions since 2007; as of September 2009, 27 IIFCs and points of service were supported by ARIES.

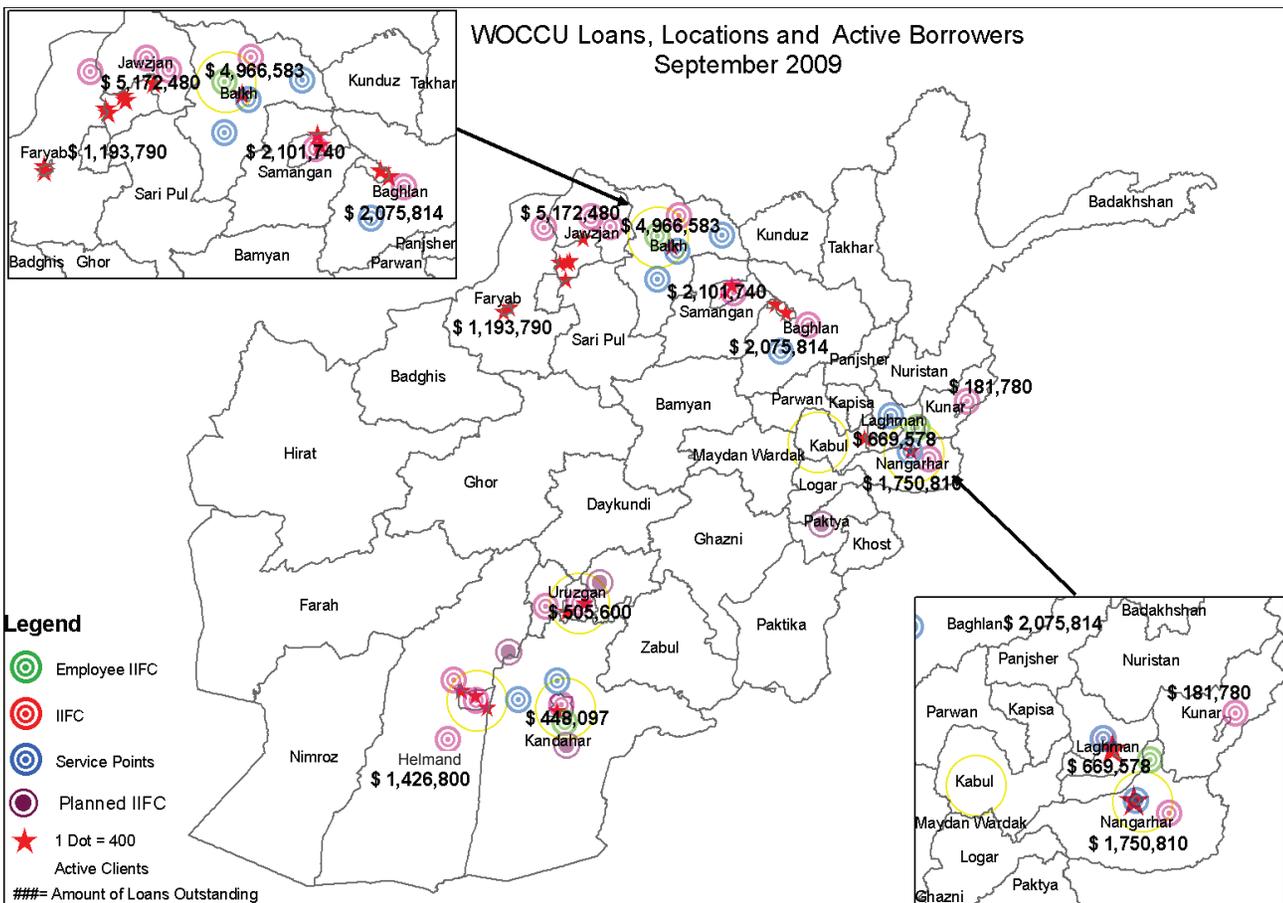
Each IIFC is a community-based entity that offers a broad range of financial services. While most microfinance providers offer credit only, the IIFCs also provide access to savings accounts, even to low-income depositors. As shareholders, not just clients, IIFC members elect their own Boards of Directors and help determine how IIFC funds will be used in their communities. The institutions thus serve as vehicles for developing civic participation and democratic processes.

To ensure local acceptance of the program, WOCCU provides grants to its IIFCs for community-articulated development projects or "CDPs," such as refurbishment of a mosque, for example. The WOCCU grant is described to the community as a type of *zakat*, or almsgiving, as prescribed in the Qur'an. In addition to contributing to community development, the CDPs play an important role in developing local infrastructure, and building positive relations with the public.

WOCCU intends for its IIFCs to become permanent and sustainable financial institutions, able to cover all operational costs with revenues. To achieve this, WOCCU is currently developing a national IIFC apex organization, the Afghanistan Investment and Banking Association, which will provide long-term, post-project oversight and capacity building for the IIFCs. As there is no regulatory framework for credit unions in Afghanistan currently, the apex will play an important oversight and support function that should help the IIFC's integration into the country's financial sector over the long term.

Operations: WOCCU's IIFC network has experienced significant growth since the inception of its partnership with ARIES. Twenty-five new IIFCs and points of service were established and the number of IIFC members increased from 8,498 in 2007 to 41,324 in 2009.

As demonstrated in the chart below, WOCCU's growth has been driven primarily by expansion of its loan portfolio, which grew from just over US \$2 million at YE2007 to more than \$4 million by YE2008. Over the same period, deposits grew from US \$470,000 at YE2007 to \$870,000 at YE2008. Growth of WOCCU loan portfolio is somewhat constrained by the limited amount of deposits its low-income clients are able to make.



Critical to growth was ARIES support for a restructuring of the IIFC governance model to include community shura boards of directors, which include religious leaders, to act as the local counsel for all loan decisions. The ARIES grant also allowed WOCCU to increase its level of technical advice and oversight in the field. Following recommendations resulting from a 2007 internal donor audit, ARIES supported WOCCU's establishment and maintenance of a more efficient loan tracking and reporting management information system. As a result, WOCCU is currently installing an updated version of MICRO-BANKER software for its portfolio management in all of its branches.

Areas of Operation

The administrative headquarters for WOCCU's Afghanistan operations is in Kabul. WOCCU's ARIES-supported IIFCs are active in 11 provinces across the ADP regions, as illustrated in Table 1 below.

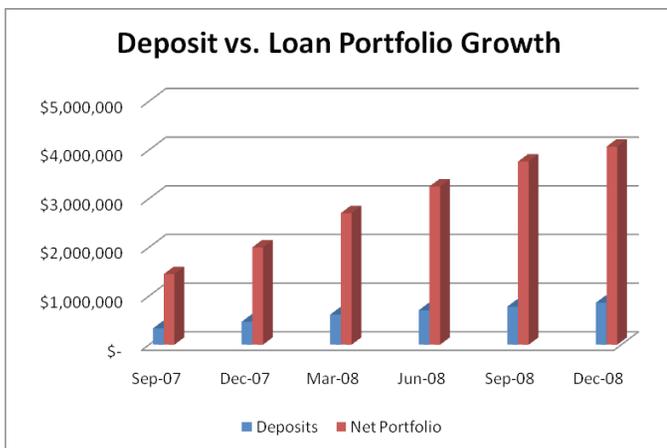


Table 1: WOCCU IIFC Locations as of YE2008

Region	Province	IIFC
North	Balkh	Balkh IIFC
		Balkh Employee IIFC
	Jawzjan	Jawzjan IIFC
		Aqcha IIFC
	Faryab	Andkhyo IIFC
Samangan	Samangan IIFC	
East	Baghlan	Baghlan IIFC
	Nangarhar	Nangarhar IIFC
	Laghman	Laghman IIFC
	Kunar	Kunar IIFC
South	Kandahar	Kandahar IIFC
	Helmand	Helmand IIFC
	Uruzgan	Uruzgan IIFC
Deh-Rawod IIFC		

Financial products

To meet the needs of its target clients, WOCCU has worked with IIFCs and local stakeholders to develop a portfolio of financial services that includes both savings and loan products.

Savings Products

- **Current accounts.** This product offers no return to the depositors. IIFC current accounts are essentially a safekeeping, or *al-wadiah* arrangement in which depositors may withdraw their funds at any time.
- **Investment accounts.** This product is based on the *mudaraba* principle, in which the financier (i.e. WOCCU) absorbs all risk, but shares returns with the client through a pre-arranged contract. Similar to certificates of deposit, IIFC investment accounts are term deposit accounts that may not be withdrawn before maturity.
- **Savings accounts.** These products (see Table 2, below) are designed to encourage asset accumulation by matching deposits with funds from WOCCU's USAID/ARIES grant. The Individual Development Account (IDA) is intended for women, students and other low-income earners. Business Individual Development Ac-

counts (BDA) are intended for individual members who have demonstrated earning potential, including private or public sector employees, and entrepreneurs. Only individuals with BDA accounts are eligible for loans.

Loan Products

- **Individual Productive Loan.** Loan terms range between six to nine months and rely on payroll deduction to ensure repayment (with maximum loan sizes equal to 50% of the employee's annual salary). These loans support a variety of sectors and purposes with 40% going to trade, 38% to agriculture, 14% to services, 5% to other sectors, and 3% to consumption.
- **Group Productive Loan.** Loans generally have terms of six to nine months, with some longer terms available. All support agricultural investments.

Both individual and group loans (see Table 3, following page) are based on *murabaha* transaction (a pre-approved and mutually agreed upon sale contract that explicitly itemizes the sale of a commodity for cash plus a markup, including administrative costs associated with the transaction) and therefore comply with *Sharia* law, with the pre-agreed mark-up resulting in an

Table 2. Savings Products

Savings Product Name	Current Account	Investment Account	Savings Accounts		
			Individual Savings	Individual Development Account ("IDA")	Business Development Accounts
Group Size	Individual	Individual	Individual Savings	Individual Development Account ("IDA")	Business Development Accounts
Client Focus				Women, students, other low income earners	Individuals who may be either public or private sector employees
Minimum Amount				400 Afs/ US \$8	First year deposits may be up to a maximum of 10,000 Afs/ US \$200 Second year deposits may be up to a maximum of 15,000 Afs/ US \$300
Maximum Amount				2,500 Afs/ US \$50	15,000 Afs/ US \$300
Terms		Term deposits		Funds must be deposited for a two year period	Funds must be deposited for a two year period
Return	None	Ranges from 3%-7.5% depending on IIFC	Depends on IIFC, usually 3% - 5%	Initial deposit amount is matched by IIFC grant	Initial deposit amount is matched by IIFC grant

Table 3. Loan Products

Loan Product Name	Cooperative Group Loan	Business Loan – LoC
Group Size	5-10; groups may be either male or female	Individuals and groups
Client Focus	Home-based women and family businesses, males are farmers	Individuals are usually traders or employees of private or public sector
Maximum Agreement Amount	250,000 afs/ US \$5000	For employees, up to 50% of annual salary
Loan Terms	6–9 months	6–9 months
Pricing/Mark-up (all flat rates)	2% monthly	2% monthly

effective rate of 2% flat monthly. Approximately 46% of both individual and group loans range from US \$200–\$500, 32% of loans \$501–\$1,000 and 17% \$1,001–\$10,000.

Eligibility requirements for an individual loan include being 18–60 years of age; demonstrating permanent residency in the area in which the IIFC is located; and demonstrating income from a job, business, or productive skill. For both individual and group loans, the applicant must deposit at least 20% of the loan amount into their account. The loan also requires at least one guarantor, such as a member of the local *shura* council.

Performance

As of September 2009, WOCCU had established 27 out of ARIES' target number of 29 IIFCs and points of service. The ARIES-supported IIFCs have disbursed 32,463 loans worth a cumulative amount of more than US \$20.4 million since 2007. The majority of loans fall within the \$200-\$500 range. There are currently 10,498 active borrowers, over 14% of whom (1,534) are female.

WOCCU's portfolio quality in Afghanistan as measured by portfolio at risk over 30 days past due (PAR₃₀) has been good, with an overall PAR₃₀ of 10% as of the end of September, 2009. Only one of its IIFCs located in Nangarhar Province suffers from serious portfolio quality problems. Upon identifying the problem, WOCCU took immediate action, working with the local police to convey to the community that repayment is expected. The IIFC's PAR₃₀ stands at 33.3% as of September 2009.

Two of the northern region IIFCs in Balkh and Jawzjan have already achieved operational self-sufficiency and no longer require direct grant support. When factoring in the costs of WOCCU's head office in Kabul, however, its IIFC network remains below 50% operationally self-sufficient.

Achievements

- As of September 2009, the IIFCs had 41,324 clients nationally
- Over 31,400 jobs have been created or sustained through the IIFCs with ARIES funding
- The IIFCs have established financial cooperatives in Balkh and in Kandahar for Afghanistan's government public service employees
- As of September 2009, WOCCU has completed or is implementing over 30 community development projects through its IIFCs. These have proved to be effective in expanding outreach and building local support
- Through consultation with local councils of *shuras*, WOCCU has developed customized, *Sharia*-compliant products appropriate for Afghanistan

Challenges, Adjustments and Lessons Learned

For all of the ARIES partners project goals have remained the same while the strategy for achieving them has evolved. WOCCU, like the other partners, has faced unforeseen obstacles. The following points illustrate these challenges, how the project has adjusted, and the lessons learned for others working in similar contexts.

Challenge: *Lack of public awareness of the credit union concept and its ability to comply with Islamic principles. Based upon the principles of risk sharing and equity, the IIFCs are broadly Sharia-compliant (congruent with Qur'anic law) as interpreted in Afghanistan. Concepts of shareholding and shared risks in investment are commonly understood in local agricultural and trading, they are far less so in Afghanistan's financial sector.¹*

¹ It is not surprising that the registration of the IIFCs took two years to achieve, as GoA officials were unclear under which ministry they should be placed. All of the other MISFA MFIs, for example, are registered with AISA; the IIFCs were finally registered with the Dept of Cooperatives, Ministry of Agriculture.



Adjustment: WOCCU uses a variety of strategies to introduce itself, including completion of community development projects, and engagement of the shura in governance and financing decisions. In promoting its concept, WOCCU used terminology that was more familiar to Afghans than “credit unions,” referring to units as “financial cooperatives” and comparing its Sharia-compliant products to those of other existing microfinance institutions.

Lessons learned: Consult with local community members to determine public awareness and perceptions of proposed products before offering them on a large scale. Adapt products to respond to local needs and concerns, and explain products in terms that are culturally appropriate and locally comprehensible.

Challenge: Security concerns constrain project implementation. Contrary to initial expectations, security in Afghanistan, especially in the rural areas, has continued to deteriorate since ARIES launched in 2006. This real-

ity has increased costs and limited technical assistance support for the field operations.

Adjustment: WOCCU's security protocol was reviewed and revised; expatriate staff members are now permitted only very restricted movement. In response national staff has had to take on increased management responsibilities. Additionally, WOCCU has worked closely with the provincial reconstruction teams (PRTs) to expand outreach in the south, and will now work only in those areas which the Afghanistan National Army and ISAF forces have secured.

Lessons learned: Flexibility, creativity and contingency planning are key to ensuring continued progress in conflict-affected environments. Partnerships and collaboration with local security forces can help to mitigate security concerns. If proper efforts are made to build local ownership and capacity, progress can continue in a conflict environment.

- **Challenge:** Limited human resource capacity. Identifying, training and retaining staff involves higher costs and more time than originally anticipated. It is necessary that staff be fully conversant with the IIFC products and services for the program to be sustainable after WOCCU's expatriate technical advisors are withdrawn.
- **Adjustment:** Due to the high costs of sending field staff to Kabul for MISFA and other trainings, WOCCU has relied more on "on the job" training and mentoring to build staff capacity.
- **Lessons learned:** A long-term commitment and investment in staff training and professional development is key for outreach and sustainability.
- **Challenge:** Local demand for WOCCU's savings and lending products and services to be Sharia compliant.
- **Adjustment:** WOCCU consults with communities prior to outreach and customizes its conventional savings and lending products to ensure Sharia compliance. To ensure rapid community acceptance of the IIFCs, WOCCU obtains letters from the local shura council, which includes religious authorities, stating that its activities are Sharia-compliant.
- **Lessons learned:** Prior to broad public outreach, consult with members of the local community to determine what types of financial products and services are appropriate and acceptable, and customize them accordingly. Where appropriate, engage local religious leaders in this process to ensure your interpretations are accurate.
- **Challenge:** Reaching and retaining female clients in a socially conservative environment, in which men and women are separated in the public sphere.
- **Adjustment:** WOCCU employs female loan and outreach officers and cashiers specifically to serve female

clients, and has established women-only sections in its branches. There is no differentiation of savings and loan procedures for males and females, but groups and meetings are segregated by gender. Moreover, as female borrowers often share their loans with male relatives in family enterprises, WOCCU permits women clients to use their loans as "family loans."

- **Lessons learned:** Specialized operations, products, and distribution mechanisms may be required to reach and retain certain target groups like women. In Afghanistan, adaptations were needed to comply with local culture and to gain acceptance by both male and female members of society.

Moving Forward

WOCCU's goals for its IIFCs are outreach, "Afghanization," and sustainability, including the establishment of 29 IIFCs by the end of the ARIES program in December 2009. WOCCU will continue its CDPs and local capacity building efforts, while decreasing the number of and reliance on expatriate advisors.

WOCCU will also expand its Sharia-compliant equipment leasing, and is exploring other new products such as micro-life and medical insurance ("MEDMAP"), which it will soon pilot in Helmand.

Another priority for WOCCU is the launching of a financial cooperative network for the Afghan National Army. Negotiations began at the end of 2007 and are still ongoing.

Finally, WOCCU will continue to develop and initiate a national credit union apex organization, the Afghanistan Investment and Banking Association, which will provide oversight and technical advice to the IIFCs after the exit of WOCCU and its technical advisors.

The World Council of Credit Unions (WOCCU) is the global trade association and development agency for credit unions that promotes the sustainable development of credit unions and other financial cooperatives around the world to empower people through access to high quality financial services. WOCCU supports the global credit union system and works with international organizations and governments to improve legislation and regulation.

www.woccu.org

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