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RURAL FINANCE COOPERATIVE DEVELOPMENT (RUFCOD):

ANNUAL PERFORMANCE MONITORING REPORT

DECEMBER 5, 2009 – DECEMBER 4, 2010

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November 2010: Farmer members of Baraki Barak IIFC plowing their fields in preparation for wheat cultivation after receiving *Sharia*-compliant financing from the IIFC in Logar province.

Table of Contents

Abbreviations and Acronyms..... **5**

I. INTRODUCTION..... 6

A. **Overview of RUFCOD**..... 6

B. **Background – IIFC Industry in Afghanistan**..... 7

II. RUFCOD ACCOMPLISHMENTS AND IMPACT..... **7**

A. RUFCOD Progress towards its Objectives..... **8**

B. RUFCOD Countrywide Indicators..... **10**

C. RUFCOD PMP Summary Table..... **18**

D. Key Achievements..... **20**

III. KEY ACTIVITIES PLANNED FOR 2011..... **21**

IV. CRITICAL ASSUMPTIONS..... **23**

V. CONCLUSION..... **26**

A. Challenges, Corrective Actions Taken, Lessons Learned and Recommendations..... **26**

ANNEX I..... **29**

Table of IIFC Locations..... 29

Table of POS Locations..... 30

Abbreviations and Acronyms

AoO	Area of Operation
AREDP	Afghanistan Rural Enterprise Development
ARIES	Agriculture, Rural Investment & Enterprise Strengthening
BOD	Board of Directors
COP	Chief of Party
DAB	Da Afghanistan Bank
DQA	Data Quality Analysis
FAF	Foreign Assistance Framework
F Indicator	Foreign Assistance Indicator (defined by Washington for worldwide reporting)
FY	Fiscal Year
GIRoA	Government of Islamic Republic of Afghanistan
GDP	Gross Domestic Product
ICT	Information and Communication Technology
IIFC	Islamic Investment and Finance Cooperative
IIFC Group	Afghanistan Islamic Investment and Finance Cooperative Group
IPTT	Indicator Performance Tracking Table
KBSS	Kabul Balkh Safety and Security (Company)
MAIL	Ministry of Agriculture, Irrigation and Livestock
M&E	Monitoring and Evaluation
MFI	Microfinance institution
MISFA	Microfinance Investment Support Facility for Afghanistan
MSME	Micro, Small and Medium Enterprises
MOU	Memorandum of Understanding
MRR	Microenterprise Results Reporting
MRRD	Ministry of Rural Rehabilitation and Development
PAR	Portfolio at Risk
PEARLS	WOCCU's Financial Performance Monitoring system
PI	Performance Indicator
PIRS	Performance Indicator Reference Sheet
POS	Point of Service
RCE	Regional Command East
RCN	Regional Command North
RCS	Regional Command South
RUFCOD	Rural Finance Cooperative Development
SCF	*Sharia*-Compliant Financing
SME	Small Medium Enterprise
TA	Technical Assistance
USAID	United States Agency for International Development
USG	United States Government
WOCCU	World Council of Credit Unions

I. INTRODUCTION

A. Overview of RUFCOD

With a total value of $60.5 million and duration of three years (2009–2012), Rural Finance and Cooperative Development (RUFCOD) is one of USAID's largest rural development projects in Afghanistan. RUFCOD aims to increase access to financial services primarily in southern and eastern Afghanistan with an emphasis on providing *Sharia*-compliant financial services to small and medium-scale business owners, farmers, low and medium income households and women. The World Council of Credit Unions (WOCCU) is USAID's implementing partner for the RUFCOD project and will provide oversight and management of the project including project reporting (programmatic and financial), communication, coordination and the overall leadership of the project operations.

The purpose of RUFCOD is to complete the establishment of and provide the necessary technical assistance to the national apex entity – the IIFC Group – which will expand the outreach of Islamic Investment and Finance Cooperatives (IIFCs), regulate, supervise, monitor and provide technical assistance to the IIFCs so that they become vibrant, profitable and fully sustainable financial institutions.

The RUFCOD Technical Approach is built around two key results:

1. **Enhanced outreach of retail rural finance cooperative institutions**
   Working with existing and new IIFCs to expand the delivery of financial services to priority geographic areas and increase the disbursement of loans to underserved small businesses, farmers, low and middle income households and women. It will also include mobilizing savings and share investments from the same client group, as well as developing new and more appropriate financial products and services, and using new delivery mechanisms and approaches.

2. **Enhanced capacity of rural finance and cooperative support and infrastructure**
   Establishing a fully sustainable cooperative apex institution, the IIFC Group that will:
   a. Provide external oversight and supervision of the individual IIFCs;
   b. Provide IIFCs with training and technical support to enhance staff and leadership skills and improve the operating performance of the cooperatives, and
   c. Provide the IIFCs with access to external capital and increase the volume of lending for agriculture and small businesses in rural communities.

According to the Strategic Plan of USAID Afghanistan, the primary goal of the mission is to support the rapid transition of Afghanistan to a more stable and productive state through the promotion of democracy, rule of law and sustainable economic and social development. To reach this goal, USAID Afghanistan designed the following three interlinked strategic objectives the achievement of which will contribute towards the mission's primary goal in Afghanistan:

1. A thriving licit economy led by the private sector

2. A democratic Government with broad citizen participation

3. A better educated and healthier population

Each of the above three strategic objectives has intermediate results against which the achievement of the strategic objectives can be measured. RUFCOD was designed to contribute towards USAID Afghanistan's goal through serving strategic objective of *thriving licit economy led by the private sector* consistent with its intermediate result *accelerated growth in the rural economy*. To this end, RUFCOD has set the five key objectives that are elaborated in section *II.A RUFCOD progress towards its objectives* of the report.

B. Background – IIFC Industry in Afghanistan

With funds from USAID's ARIES program (2006-2009) and MISFA (2004 – 2009), WOCCU established an extensive network of financial cooperative totaling 27 IIFCs and points of service (POSs) that provided more than $22.9 million in loans and created 53,718 jobs for Afghanistan's population in rural and urban communities in the North, South and Eastern provinces before RUFCOD was awarded in December 2009.

The Islamic cooperative model being used in Afghanistan was developed over a period of years and designed to make the Islamic Investment and Finance Cooperatives (IIFCs) more acceptable to the local populace, and particularly to the more conservative rural communities in the East and South. WOCCU consulted with Islamic scholars (*muftis*) and local *mullahs* in modifying its traditional credit union development methodology for application in Afghanistan. WOCCU obtained *Fatwas* (decrees by local *muftis*, or religious leaders) approving the credit products of the IIFCs. These religious endorsements helped attract members to the cooperatives. The IIFCs are the first fully *Sharia* -compliant financial institutions in rural Afghanistan. The mutual ownership and shared risk of cooperative members is in line with Islamic values, and that aspect has enabled the IIFCs to attract new members.

WOCCU has also tested and proven the effectiveness of a new leadership model that includes local tribal leaders (tribal or village council of elders) on the IIFC boards of directors. The participation of the boards in loan approvals taps traditional social networks where social pressure compels repayment of obligations.

II. RUFCOD ACCOMPLISHMENTS AND IMPACT

In its first year of operations (December 5th, 2009- December 4 th, 2010), significant progress was made on all fronts of the project despite the worsening security situation in the southern and eastern areas where RUFCOD's operations are mostly focused. Below is a brief explanation of RUFCOD's progress towards the achievement of its objectives and the first year targets.

A. RUFCOD progress towards its objectives

The following are the project objectives specified in the project's year one work plan. The attainment of these objectives has a direct impact on the project's ability to support the intermediate result for USAID's activity objective in Afghanistan: accelerated growth in the rural economy. RUFCOD has made considerable progress towards the achievement of these objectives in its first year of operations as noted below.

1. Expand access to finance (credit) for primary inputs and equipment for farmers

   The IIFCs disbursed 8,952 agricultural *sharia*-compliant financing (SCF) loans (worth above $6.9 million) to their members across the IIFC network this year [1]alone increasing the total agricultural loan disbursements to 23,363 SFC loans totaling above $15.4 million. The cumulative agricultural SCF loan disbursements represent 39% of the total loan disbursements as of the end of November 2010.

2. Wherever feasible, increase the use of modern technology combined with traditional systems to give rural areas broader access to basic financial services

   The project procured the necessary computers and the related tools and equipment including the MicroBanker software, a management information system designed and customized for the use of IIFCs. This year, 26 of the 30 IIFCs used the computerized system to record their day-to-day transactions and generate the financial and programmatic reports. Technical employees of the IIFCs who are responsible to use the system are being trained by the IIFC Group staff on regular basis and technical assistance is being provided to them to further improve their knowledge and practical skills.

   However, based on an assessment, it was concluded that the demand for the use of M-Paisa in areas where IIFCs are operating is considerably low and the estimated cost of it is significantly high. Therefore, RUFCOD did not recommend the IIFCs to use M-Paisa in providing *Sharia* compliant financing to their members. M-paisa is a new innovative lending or money transfer system run through personal cell phones and provided by the telecommunication companies in Afghanistan.

3. Increase membership and promote new IIFCs in RUFCOD project's Area of Operation (AoO)

   Fourteen new IIFCs and three POSs were established in various provinces of Regional Command South (RCS), Regional Command East (RCE) and Regional Command North (RCN) this year alone. 15,958 new members were added to the 30 IIFCs operating in the project's AoO bringing the total membership to 62,201 as of the end of November 2010.

4. Bring all IIFCs under a national organization – the IIFC Group – that will provide supervision, technical assistance and loan capital to the IIFCs

[1] The term *this year* refers to the first year of RUFCOD operations: December 5, 2009 – December 4, 2010

The IIFC Group was successfully registered as a corporation in the Afghanistan Investment Support Agency (AISA), an entity related to Government of Islamic Republic of Afghanistan (GIRoA). The IIFC Group also formed its nine-member board of directors representing a mix of Afghan intellectuals, representatives of Afghanistan's international chamber of commerce, an Islamic scholar and IIFCs' prominent *Shura* board members. It is worthwhile to note that there is one female member on the IIFC Group's board of directors representing IIFCs in the north.

The organization is fully staffed and most of the key operational policies such as HR, finance, IT and others have been approved by the board and are now being applied. The IIFC Group conducted a number of field visits to the IIFCs in some of the high risk areas like Helmand, Kandahar and Uruzgan to closely monitor the operations of the IIFCs there and provide necessary technical assistance to them including hands-on training and guidance.

5. Cooperate with other USAID projects, coalition development platforms and GIRoA programs to create unity and coherence of effort, maximize the leveraging of resources and minimize duplication and waste of effort.

The IIFC Group signed a cooperation agreement with a USAID funded project, *Agricultural Credit Enhancement or ACE* through which $3 million will be invested in credit in the IIFCs only operating in the North. These funds are designated solely for agricultural loans to be provided by the IIFCs to their members. The first disbursement under this agreement is expected to be made in the next coming weeks. In the meantime, RUFCOD is also in the process of reaching a formal agreement with another USAID supported project, called *Afghanistan Stabilization Initiative (ASI)* to support the lending operations of the IIFCs in the South.

'Welthungerhilfe' is a Dutch NGO providing agricultural services in Jawzjan province. It intends to disburse a certain amount of money to the residents of the 15 villages in Jawzjan province. RUFCOD staff members had initial discussions with the NGO to encourage them to invest their funds through Jawzjan and Aqcha IIFCs to offer *Sharia*-compliant financial services to farmers. As a result, a memorandum of understanding was drafted between the Welthungerilfe and Aqcha and Jawzjan IIFCs, outlining how the NGO will invest funds through the two IIFCs to provide *Sharia*-compliant loans to farmers of the above 15 villages in Jawzjan province. This Memorandum of Understanding is expected to be formally signed and enacted in the near future.

Agriteam Canada is a Canadian NGO supporting a vocational training center which enhances carpentry skills and teaches tailoring to its 50 members in Dand district of Kandahar province. The project staff have partnered with Agriteam Canada wherein an agreement was reached that the NGO will ask and encourage its members to join Dand IIFC in order to obtain *Sharia*-compliant financial services needed to support their businesses.

Additionally, the RUFCOD staff held a couple of meetings with the representatives of Afghanistan Rural Enterprises Development Program (AREDP) – a government led

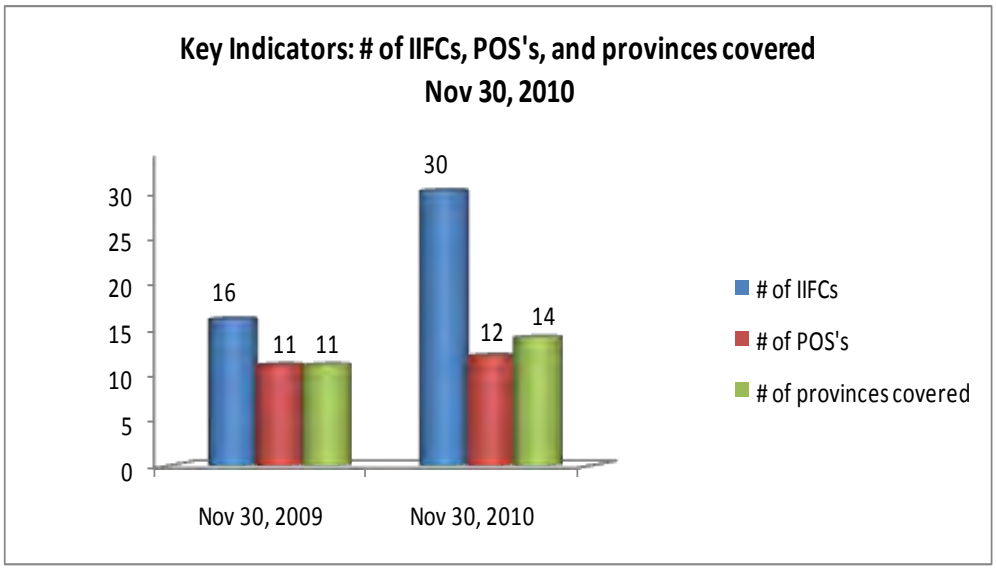
program being implemented by MRRD - to create a partnership with AREDP. Through this collaboration, RUFCOD will support the savings and loan associations that are expected to be created by AREDP in areas where IIFCs operate. AREDP is at its initial stages of operations. As the program develops and the Village Savings and Loan Associations (VSLAs) are formed, RUFCOD will investigate various ways to support those groups.

This year the project Chief of Party, Mr. Normunds Mizis, met with USAID Afghanistan's Office of Economic Growth's regional representative, Mr. David Baley in Kandahar province. He also talked to the representatives of Chemonics International, a USAID partner in the province in an effort to create coordination with USAID RCS and other USAID supported programs in the region to enhance coordination and avoid duplication of efforts

B. RUFCOD Countrywide Indicators

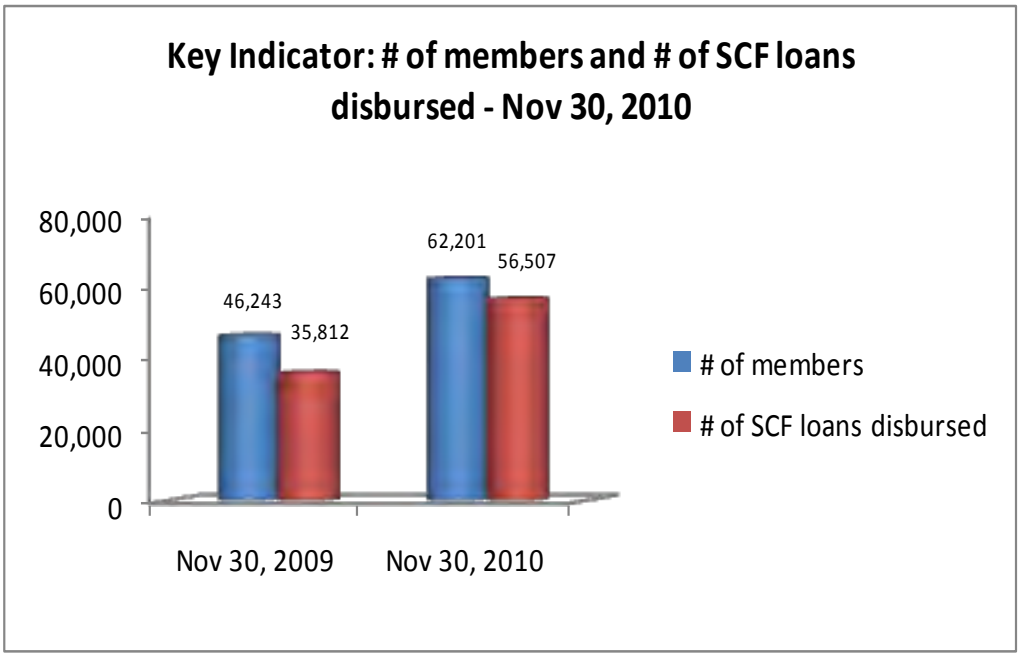
USAID/Afghanistan **Strategic Objective: A thriving licit economy led by the private sector**	
USAID Indicator	**RUFCOD's Contribution to Result**
Achievement of RUFCOD project objectives will improve the living conditions and livelihoods of cooperative members, greatly increase economic activity and employment opportunities in the communities served by the project and lead to more full time jobs.	15,958 new members joined the 30 IIFCs operating nationwide. This represents an increase of 5,335 members in the south, 2,551 members in the east, and 7,899 members in the north and 173 in the central region this year. 14 new IIFCs and 3 new POS's were established in RCS, RCE, RCN and the central region. The IIFCs, including the most recently-established, disbursed 20,695 *Sharia*-compliant financing loans worth $17,081,545 which led to the creation of 31,043 jobs during this year alone. The IIFCs are independent financial instructions owned by their members who also elect and form their boards of directors governing them. The prime intention of the efforts made has been to prepare the appropriate grounds wherein the 30 IIFCs can thrive as independent financial institutions and become self sustainable.

Intermediate Result Accelerated growth in the rural economy	
Result: Enhanced outreach of retail rural finance/cooperative institutions	
USAID Year 1 Indicators	**Status**
Indicator 1 - Number of IIFCs and Provinces covered (cumulative)	A total of 30 IIFCs including 14 new ones were operating in the 14 provinces of RCS, RCE, RCN and the central region. Three new additional provinces were added to the project's AoO: Kunduz (RCN), Logar (RCE) and Kabul (central).
Indicator 2 - Number of Points of Service (not cumulative)	Three new POSs, Marjah in Helmand, Surkhrod in Nangarhar and Almar in Faryab, were established in the locations approved by USAID. The total number of POSs operational this year was 12 including the 3 newly established POSs.

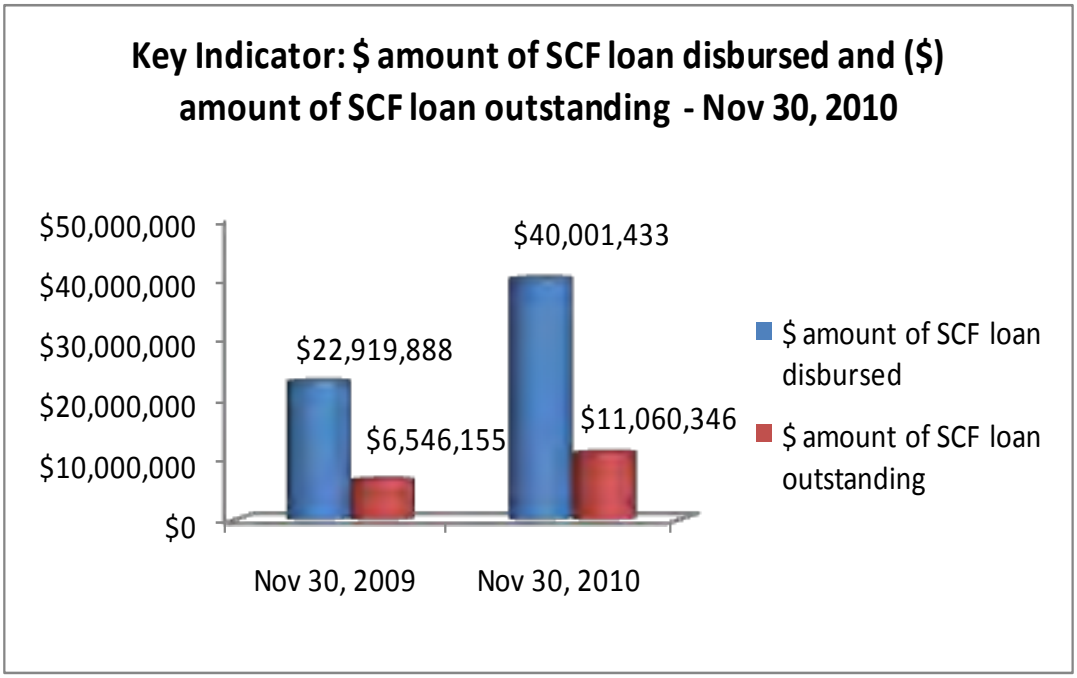


Indicator 3 - Number of members	15,958 new members joined the 30 IIFCs operating nationwide. This represents an increase of 5,335 members in the south, 2,551 members in the east, and 7,899 members in the north and 173 in the central region this year. A total of 62,201 members received financial services and products from the 30 IIFCs across Afghanistan as of the end of November 2010.

Indicator 4a - Number of SCF disbursed (cumulative)	20,695 new SCF loans were disbursed to the IIFC members this year representing an increase of 5,585 SCF loans in RCS, 2,002 in RCE, 13,049 in RCN and 59 in the central region. The total number of SCF loans disbursed throughout the IIFC network was 56,507 as of the end of November 2010.



Indicator 4b – SCF Disbursed (not cumulative)	An amount of $17,081,545 were disbursed in SCF loans to the members of the IIFCs representing an increase of $4,063,401 in RCS, $1,826,841 in RCE, $11,084,703 in RCN and $106,600 in the central region this year alone.
Indicator 5 - Net SCF Outstanding	A total amount of $11,060,346 were outstanding with the members of the IIFCs throughout the network as of this reporting period representing an increase of $4,514,191 added this year alone.
Indicator 6 - Value of SCF disbursed (cumulative)	The total amount of SCF loans disbursed throughout the IIFC network was $40,001,433 as of the end of November 2010.



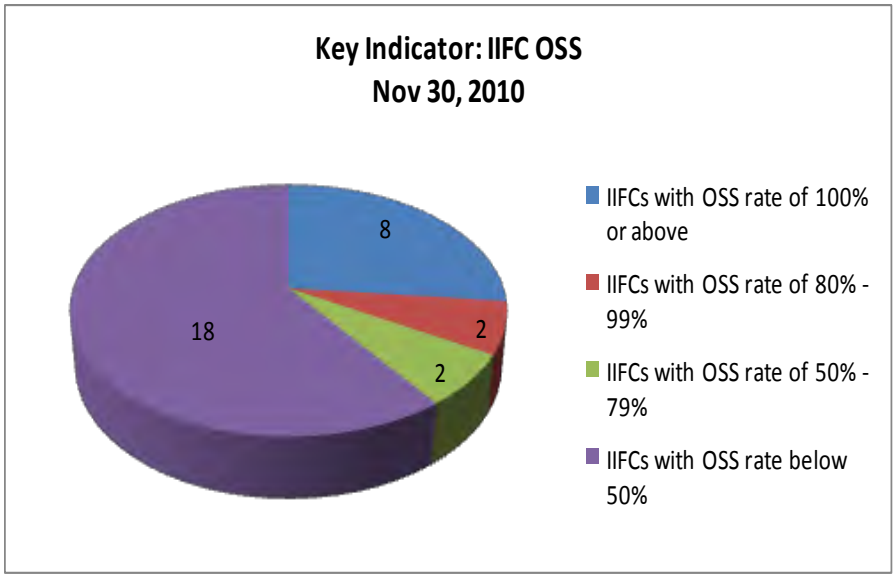
Indicator 7 - Portfolio at Risk	The aggregate PAR of the whole IIFC network was 5.6% as of the end of November 2010, well below the annual target of 7%.
Indicator 8 - IIFC Operational self sufficiency (OSS) IIFC > 3 years = 100% IIFC > 2 years = 80% IIFC > 1 year = 50%	The following list provides the OSS rates for the IIFCs having reached third year of their operations as of the end of November 2010: 1. Helmand IIFC = 43% 2. Nangarhar IIFC = 39% 3. Laghman IIFC = 46% 4. Aqcha IIFC = 97% 5. Balkh IIFC = 152% 6. Jawzjan IIFC = 126% 7. Samangan IIFC = 124% 8. Baghlan IIFC = 122% 9. Sholgara IIFC = 110% 10. Kholm IIFC = 107% Below are the OSS rates of the IIFCs having reached the second year of their operations as of the end of November, 2010:

1. Kandahar IIFC = 45%
2. Uruzgan IIFC = 83%
3. Dehrawod IIFC = 50%
4. Kunar IIFC = 60%
5. Balkh Employees IIFC = 129%

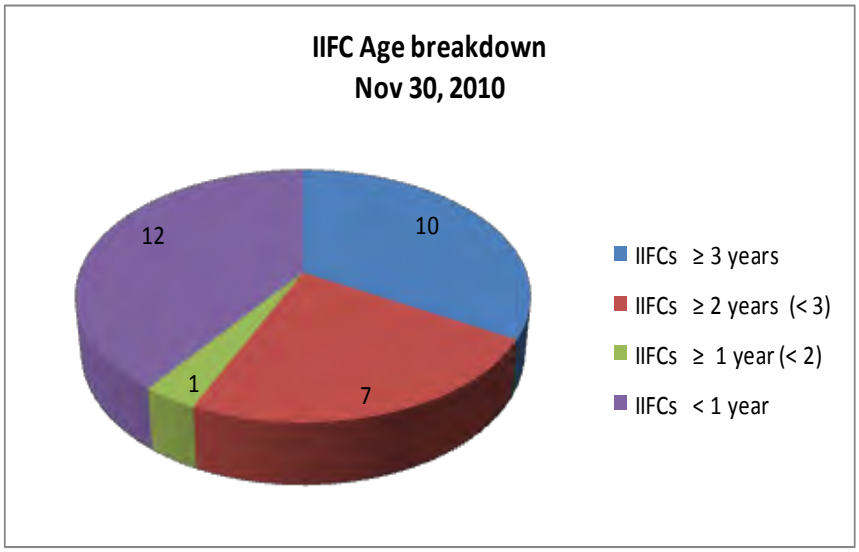
The following IIFC reached its first year of operations as of this reporting period:

1. Andkoi IIFC = 121%

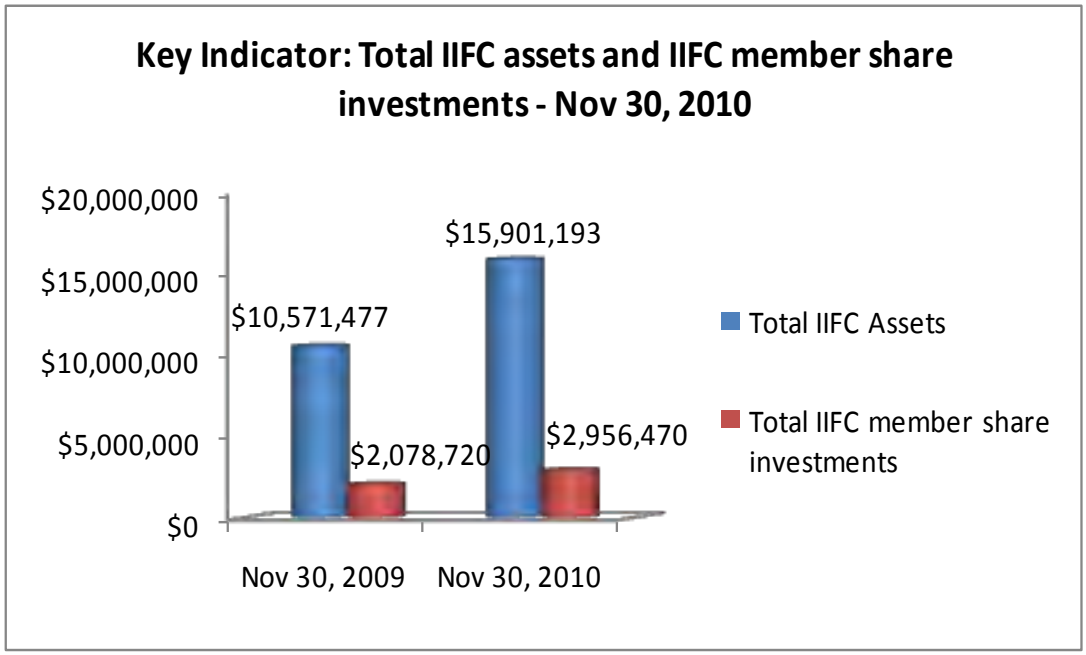
To sum up, of the 30 IIFCs operating, 8 have achieved full OSS, 2 are between 80% - 99% just closer to reaching full, another 2 are between 50%-79% OSS and the rest 18 are below 50% OSS as of the end of November 2010 as illustrated in graph below.



12 of the 18 IIFCs who stand below 50% OSS were established less than a year ago. Please look at the graph below illustrating IIFCs based on their years of operations:



Indicator 9 - Total IIFC Assets	Total amount of IIFCs' assets increased by $5,329,716 bringing the total assets of the IIFCs to $15,901,193 as of the end of November 2010.
Indicator 10 - Total IIFC member share investments	A total amount of $2,956,470 were mobilized as share savings representing an increase of $877,750 this year alone.



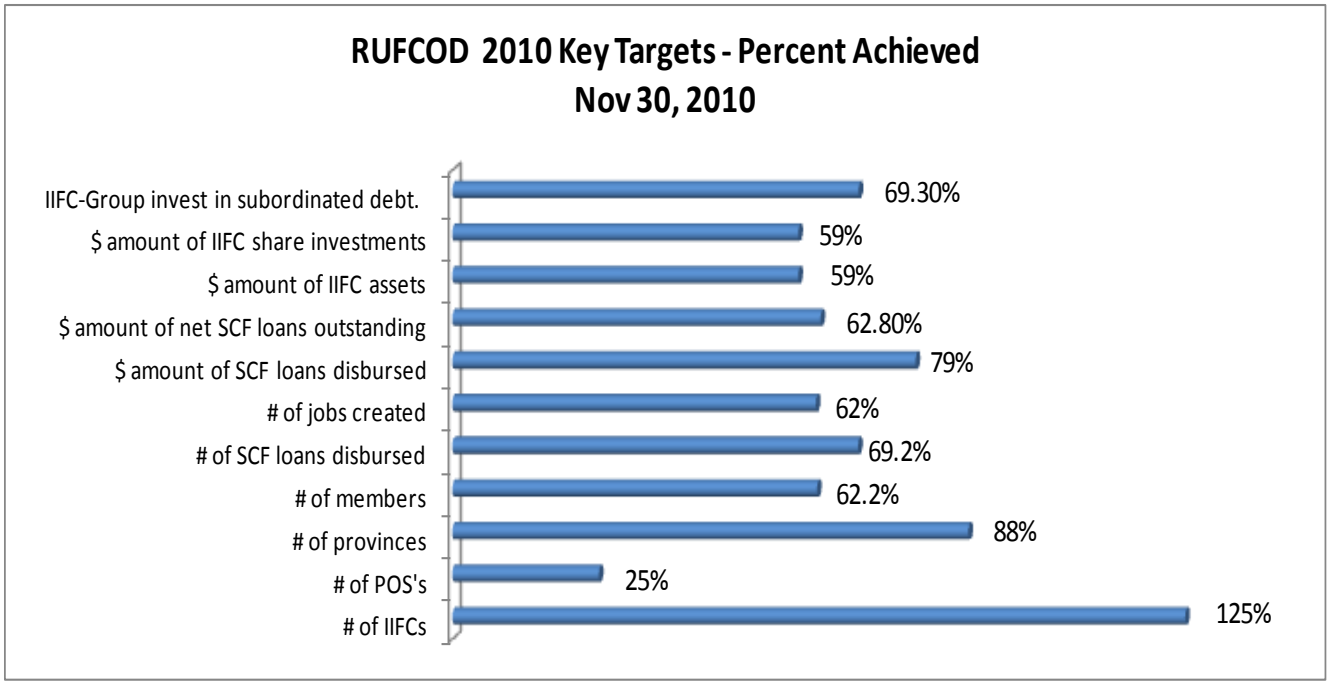
Indicator 11 - Number of jobs created by SCF (not cumulative)	As a result of SCF loan disbursement, 31,043 new jobs were created this year in the 14 provinces increasing the total number of jobs created to 84,761 as of the end of November, 2010.
Number of new financial products developed	None
Amount of direct expenditure on ICT tools	None
$ amount spent on additional activities	No dollar amount was spent on direct expenditures during the reporting period. Specific reasons include: • **Branchless Banking:** Based on an assessment conducted, it was concluded that the demand for the use of technology particularly M-Paisa in areas where IIFCs are operating is considerably low and the estimated cost of it is significantly high. Therefore, RUFCOD did not use M-Paisa in providing *Sharia* compliant financing to the IIFC members; • **Support to AREDP:** Afghanistan Rural Enterprise Development Program (AREDP) is at its initial stages of operations. As the program develops and the Village Savings and Loan Associations (VSLAs) are formed, RUFCOD will investigate various ways to support those groups; • **Credit Program for Farm Store Customers:** Most of the areas served by RUFCOD specifically in the South and East are considered to be high risk areas. This caused the project not to be able to reach out to the farms store customers. However, the project anticipates investigating the possibilities of targeting farm store customers and providing financial services to them.

Number of MOUs signed and amount spent on additional activities	None
Intermediate Result Accelerated growth in the rural economy	
Result 2: Enhanced capacity or rural finance and cooperative support and infrastructure	
IIFC Group will have achieved 40% Operational self sufficiency by the end of base year of RUFCOD.	Since its registration as corporation at the Afghanistan Investment Support Facility Agency (AISA) in 2010, the IIFC Group has made considerable strides including the successful formation of its board of directors, hiring of competent staff for its positions, and setting up a separate office space in Kabul as its headquarters. However, the institution is still nascent and is provided with the required technical assistance by WOCCU so that it grows more mature and takes over the responsibilities from WOCCU as RUFCOD closes out. Therefore, it was not able to achieve the target OSS during the past year. It is expected that the IIFC Group will earn a significant amount of income from the $5.2 million invested in the IIFCs in the months to come. This will increase the IIFC Group's OSS rate as a result. However, it is important to note here that before the IIFC Group assumes the ownership of that income; a formal agreement or permission from USAID will be sought allowing the IIFC Group to record that amount of money as income from its profitable operations.
IIFC Group PAR	None
IIFC Group investment in subordinated debt.	$5,202,499 was invested in the IIFCs across the network as of the end of November 2010.
# of IIFCs that have joined the IIFC Group	30 IFCs joined the IIFC Group this year.

C. RUFCOD PMP Summary Table

Indicator	Unit of Measure	Baseline Value	2010 Target	Base Year (2010) Actual	% 2010 target
Indicator 1 - Number of IIFCs and Provinces covered	Number	16 in 11 provinces	24 in 16 provinces	30 in 14 provinces	125% in 88% of provinces
Indicator 2 - Number of Points of Service	Number	11	4	1	25%
Indicator 3 - Number of members	Number	46,865	100,000	62,201	62.2%
Indicator 4a - Number of SCF disbursed (cumulative)	Number	35,812	81,666	56,507	69.2%
Indicator 4b - SCF Disbursed (not cumulative)	Dollar value	n/a	n/a	$17,081,545	n/a
Indicator 5 - Net SCF Outstanding	Dollar value	$6,546,150	$17,600,000	$11,060,346	62.8%
Indicator 6 – Value of SCF disbursed (cumulative)	Dollar value	$22,919,888	$50,600,000	$40,001,433	79%
Indicator 7 - Portfolio at Risk	Percentage	3.6%	7%	5.6%	n/a
Indicator 8 - IIFC Operational self sufficiency	Percentage	5	n/a	n/a	n/a
IIFC > 3 years			100.0%	8	
IIFC > 2 years			80.0%	2	
IIFC > 1 year			50.0%	2	
Indicator 9 - Total IIFC Assets	Dollar value	$10,571,477	$26,900,000	$15,901,193	59%
Indicator 10 - Total IIFC member share investments	Dollar value	$2,078,720	$5,000,000	$2,956,470	59%
Indicator 11 - Number of jobs created by SCF (not cumulative)	Number	53,718	50,000	31,043	62%
Number of new financial products developed	Number	n/a	2	0	n/a

Amount of direct expenditure on ICT tools	Dollar value	n/a	n/a	n/a	n/a
$ amount spent on additional activities	Dollar value	n/a	$834,000	$0	n/a
Number of MOUs signed and amount spent on additional activities	Dollar value	n/a	n/a	0	n/a
IIFC Group Operational self sufficiency	Percentage	n/a	40%	0	n/a
IIFC Group PAR	Percentage	n/a	PAR under 7%	n/a	
IIFC Group investment in subordinated debt.	Dollar Amount	n/a	$7,500,000	$5,202,499	69.3%
# of IIFCs that have joined the IIFC Group	Number	n/a	n/a	30	n/a



D. Key Achievements

Key achievements of RUFCOD in 2010 are briefly noted below:

1) The successful establishment of fourteen new IIFCs and three POSs in the various provinces of RCS, RCE, RCN and the central region as listed hereunder:

1. Nadali IIFC – Helmand province;
2. Nawa IIFC - Helmand province;
3. Shawali Kot IIFC – Kandahar province;
4. Spin Boldak IIFC – Kandahar province;
5. Dand IIFC- Kandahar province;
6. Chora IIFC - Uruzgan province;
7. Shinwari IIFC - Nangarhar province;
8. Sarkani IIFC - Kunar province;
9. Sholgara IIFC – Balkh province;
10. Khulm IIFC - Balkh province;[2]
11. Maimana IIFC - Faryab province;
12. Kunduz - Kunduz province;
13. Kabul - Kabul province; and
14. Baraki Barak - Logar province.

The POSs launched this year are as follows:

1. Marjah POS - Helmand province;
2. Surkhrod POS – Nangarhar province;
3. Almar POS – Faryab province.

2) The successful establishment of a national apex entity, the IIFC Group, that provides supervision, technical assistance and loan assistance to the IIFCs in country. This entity was registered as a corporation in the GIRoA's Investment Support Facility Agency known as the AISA. It also formed a nine-member board of directors and set up an independent office in Kabul. This entity is fully staffed and quickly taking over responsibilities of leading the IIFC industry in Afghanistan.

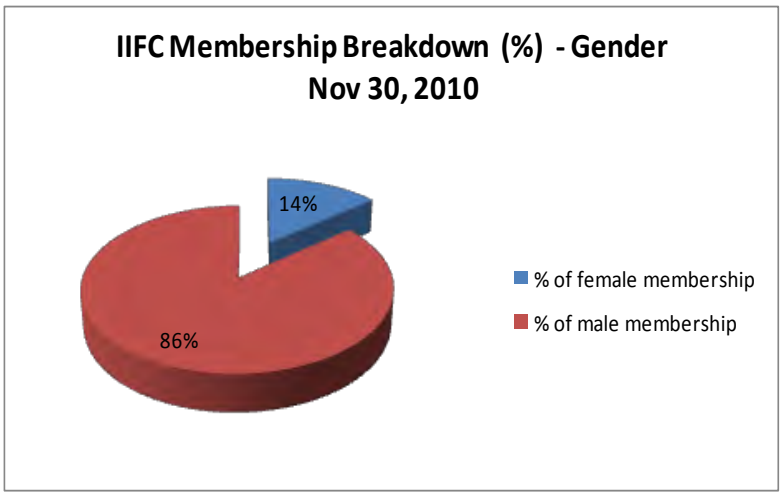
3) As a significant step towards the sustainability of the IIFC Group, $5,202,499 was invested through the IIFC Group in the IIFCs, whose interest is expected to yield a large sum of income for the same entity.

4) A cooperation agreement was signed between the IIFC Group and a USAID-funded project, *Agricultural Credit Enhancement or ACE*. Under this agreement, $3 million will be invested in the IIFCs operating in the north in form of credit to support agricultural activities of their farmer members.

[2] Sholgara and Khulm started operations as points of service under the management of Balkh IIFC long before they were turned into independent full-service IIFCs in 2010.

5) The IIFCs disbursed $17,081,545 this year in SCF loans to their members in fourteen provinces of Afghanistan - Helmand, Kandahar and Uruzgan (RCS), Nangarhar, Kunar, Laghman and Logar (RCE), Balkh, Jawzjan, Samangan, Faryab, Baghlan and Kunduz (RCN), and Kabul (Central region). The agricultural loan disbursements represented 39% of the total loan disbursements as of the end of November 2010.

6) The IIFCs served 62,201 members this year, 15,958 of which were new members. Female membership represented 14% of the total membership.



7) As a result of SCF loan disbursements, 31,043 new jobs were created in the fourteen provinces where IIFCs operate;

8) An additional four IIFCs became fully operationally self-sufficient institutions this year bringing the total number of self sufficient institutions to eight. Another two IIFCs, Aqcha 97% and Uruzgan 83%, are up fast towards becoming self sufficient;

9) $5,329,716 were added to the IIFCs' assets this year alone, increasing the total value of the IIFC networks assets $15,901,193 as of the end of November 2010;

10) $877,750 were mobilized as member shares this year increasing the total value of member share investments to $2,956,470 as of the end of November 2010.

III. KEY ACTIVITIES PLANNED FOR 2011

In 2011, RUFCOD's operations will primarily focus on further improving financial and operational performance and sustainability of the IIFC Group, increasing membership in the existing 30 IIFCs and 12 POSs as well as establishing at least 10 new financial services outlets including additional 5 IIFCs and 5 POSs, particularly in the Southern and Eastern provinces. Additionally, the project will further expand the range of SCF financing to include small and

medium enterprises and increase the extension of loans to a larger number of medium-scale farmers. Major priority areas comprise the following:

A. The Islamic Investment and Finance Group (IIFC Group) will continue to expand in 2011 by increasing the number of shareholders from initial eighteen to include all registered IIFCs operating in the country. The growth of the IIFC network will be supported by technical and financial assistance and guarantee services from the IIFC Group and will result in a total membership of 100,000 by the end of option year one, $28 million in combined assets, $22 million in outstanding loans, and approximately $3 million in share savings. The number of actual jobs to be created by IIFC loans is estimated to total 54,000 during Option Year One.

B. The IIFC Group, headquartered in Kabul, is linked to all the IIFCs through the MicroBanker MIS software installed in each IIFC and point-of-service (POS). On monthly basis the IIFC Group evaluates the financial performance of the IIFCs and measures growth against the pre-established monthly targets. Last year, the capability to regularly monitor IIFC performance from the Group's headquarters in Kabul was established. In 2011, WOCCU will make further improvements to the monitoring system, as well as introduce a risk rating capacity, "red flags" reporting, and further refinements to the regulatory and enforcement mechanisms now under development.

C. During 2010, WOCCU transferred its technical staff operating in the regions over to the IIFC Group, while in 2011 the Group will become the main source of technical assistance and back office support for the IIFCs. Further development of the Group's capabilities is needed to ensure staff possesses the right skills and knowledge to successfully implement the expansion program that will double or triple the growth of existing IIFCs and achieve the targets established for Option Year 1. The IIFC Group will expand its field examination programs and supervisory visits to maintain IIFC compliance with minimum performance standards. It will also add a Fraud Audit to its array of tools to provide better control over asset quality and minimize the probability of fraudulent activities by IIFC personnel and their members. In 2011, the IIFC Group will also develop a mutual guarantee system; a two-tier risk monitoring and reporting mechanism; introduce short-term emergency and liquidity management loans for the benefit of the IIFCs; set up a Stabilization Fund and introduce financial stabilization services for the IIFCs. Early in 2011, WOCCU will transfer all share investment agreements to the IIFC Group, a process that will consolidate the investment and supervisory roles of the Group.

D. By the end of Option Year 1, the IIFC Group will have reached 50 percent operational self-sufficiency. This result will be achieved by transferring the management of the share investments to the IIFC Group, and those investments yield an 8 percent annual return. Share investment management requires disciplined monthly monitoring of asset quality of the IIFCs; IIFC compliance with the rules, regulations and prudential norms and standards issued by the IIFC Group; on site and off site monitoring, evaluation and enforcement of the standards; and a reasonable degree of control over reinvestment of the funds mobilized by the IIFCs through issuing subordinated shares.

E. The IIFC Group will finalize the regulatory framework for the IIFCs after final approval of drafted regulations, prudential standards and model bylaws, policies and procedures that are mandatory for all IIFCs. In addition, RUFCOD will actively engage in dialog with the Central Bank in the attempt to develop adequate legislative and regulatory framework to support the financial cooperative model introduced by WOCCU and RUFCOD.

IV. CRITICAL ASSUMPTIONS

Critical Assumptions Table		
Critical Performance Challenge	**Challenges**	**Assumptions**
1.Security	RCE and RCS continue to be areas where Taliban are active. Enhanced security is required to operate effectively in the AoO. This tight security may have an impact on staff's/members' ability to access IIFCs which would have an impact on overall project targets. Security problems will also impact the ability of small businesses to operate freely in some regions of the country.	1. The RUFCOD AoO will receive security assistance from the Afghan National Army and international military forces in the more insecure communities and provinces so the project can operate as designed in RCE and RCS. 2. The *Shura* Board members will represent and defend the IIFCs as belonging to their communities. If the IIFCs are seen as linked to the government or the international community, they are at greater risks. Board members will make the community aware that IIFCs are community owned and compliant with *Sharia* law. 3. Project security systems are fully operational. 4. The use of a virtual IIFC point of service "model" will permit financial services to be delivered in highly kinetic environments.

2. Acceptance of the IIFCs as legitimate, *Sharia*-compliant financial institutions	Many rural Afghan households are religiously conservative and unfamiliar with formal financial institutions. They do not want to associate with any institutions that are not in line with Islamic law. Alleviating this concern requires that all IIFC financial products be *Sharia*-compliant.	1. The IIFCs will continue to obtain and publish *fatwas* from local religious leaders and those *fatwas* will be respected. 2. Local *mullahs* and *Maliks* will speak out about the Islamic compliance of the financial products being offered by their IIFCs.
3. Creating a network of financially sustainable rural financial cooperatives and an effective and sustainable national association in the current environment is complicated and difficult.	The IIFCs and the national apex (i.e., the IIFC Group) have been established using a European cooperative banking model where the primary IIFCs operate independently, but use policies and procedures introduced and maintained by their national association. These entities require well trained, capable staff and leaders; access to external resources to supplement local deposits and finance increased lending; good control over operating expenses; and low rates of loan delinquency if they are to become operationally and financially sustainable over the next 3 years.	1. The national IIFC association (i.e., the IIFC Group) "owns" a piece of every IIFC through the investment of subordinated debt. It is expected that IIFC Group ownership will enable it to regulate and intervene in the operations of individual IIFCs that do not comply with the IIFC Group's minimum operating standards. 2. Training of Board members and IIFC staff is continual; higher level regulatory training is being provided to the staff of the IIFC Group to permit it to closely monitor and regulate IIFC financial operations; and the MicroBanker software permits off-site monitoring on a monthly basis. 3. Local deposit mobilization will be continued while recognizing that few rural households have excess cash that can be saved; market rate pricing of all IIFCs products and services will be maintained; salaries will remain competitive to keep staff from moving elsewhere; and capital reserves are being created.
4. The Central Bank of Afghanistan will register the IIFC Group and issue a license as a deposit-taking financial	The Central Bank supports the broad financial cooperative approach of the IIFC network but it has expressed specific interest in: 1) WOCCU's participation on the board of the	1. WOCCU's participation on the board is being explained as necessary to protect the investments made by the Government and donor community. We expect the Central

institution.	IIFC Group and 2) the ownership structure wherein the IIFC Group owns a portion of each individual IIFC.	Bank to agree such participation is necessary. 2. The Group's ownership structure and relationship with the IIFC's is unfamiliar to the DaB because it is familiar with the structure of commercial financial institutions that often have individual owners. The cooperative ownership structure is relatively new. 3. We expect the performance of IIFC's and their continued compliance with minimum standards as included in supervisory reports will convince the DaB to actively support the ownership structure of the IIFC Group. 4. The DaB has expressed support for the intended regulatory role of the IIFC Group and will support the ownership structure once the regulatory capabilities have been effectively demonstrated.
5. Farming in drought conditions	One of the key objectives of RUFCOD is to expand credit access to farmers**.** Due to record low rainfall and lower mountain snow cap levels it is anticipated that drought will have an impact on future farming activities and impact the demand for credit as well as repayment rates.	1. RUCOD's ability to mitigate the impact of drought conditions will be enhanced by partnering with other rural focused project and partners (Min of Ag) to address water access constraints and more effective use of available water supplies. 2. RUFCOD will be able to develop new financial products and outreach methodologies that will increase number of agricultural loans in spite of marginal conditions in some provinces.
6. IIFC financing for agriculture and MSME's will generate new employment opportunities	All IIFCs have continued to diversify lending for productive activities, as well as for consumption and household needs in rural areas.	1. According to MISFA studies, each loan disbursed for micro and small enterprise creates 1.5 new jobs. RUFCOD will apply that principle to measure jobs created each SCF

	Diversification is a risk mitigation technique, but it also creates new employment opportunities and stimulates job creation.	loan disbursed but will also try to identify those that are purely consumptive such as medical treatment, weddings, etc.
7. Establishment of Afghan National Army (ANA) Points of Service in areas where ANA operates	How to provide access to financial services to ANA personnel while providing financial services to the general population/ membership.	1. Point-of-sale devices and other technology solutions will be used to ensure the IIFC points of service are open to all community members while they also offer financial services to ANA personnel.
8. All IIFCs one year or older will be operationally self-sufficient and the Group will be 40% sustainable at the end of Year 3.	Low human resource capacity in the financial sector means that a priority needs to be given to training on enforcement of financial disciplines that lead towards operational self sufficiency.	1. All project development activities remain on schedule as detailed in the Workplan; security remains under control; project remains fully staffed, and IIFCs are able to control their operations and remain eligible and capable of using the loan funds from the Group.

V. CONCLUSION

RUFCOD is one of very few projects of USAID that is operating in the most difficult conflict areas in the South and East of Afghanistan. Despite the mounting security challenges in the provinces of RCS and RCE, WOCCU adhered to its plan of implementing RUFCOD and more specifically launching new IIFCs and POSs and disbursing *Sharia*-compliant financing to the communities not only in the RCS and RCE but also in RCN and the central region. With all the successes RUFCOD had last year, there were a number of serious challenges facing the project implementation that brought about setbacks in meeting its 2010 targets. In conclusion, positive lessons were learned that can be used to improve the performance in the two remaining years of the project as briefly noted below:

A. Challenges, Corrective Actions Taken, Lessons Learned and Recommendations:

1. **Challenge - Exacerbated Security:** According to a recent UN report, the year 2010 was the deadliest year in Afghanistan in the past nine years, heavily affecting the lives of millions of the country's civilian population. As a result of the many clean-up operations conducted by the Afghan armed forces and international coalition forces in the southern provinces of Helmand and Kandahar in particular, thousands of people were displaced from their homes and communities where IIFCs operate. The day-to-day lives of the population in Uruzgan and

eastern provinces of Kunar, Laghman, and Logar were not an exception to this situation. Serious fears of intimidation by Taliban or other insurgent groups were the normal realities people in those areas had to deal with every day. Furthermore, the relatively secure North, specifically the provinces of Kunduz and some areas in Balkh, witnessed a spike in insurgency in 2010. Without a doubt, the security situation in the provinces served by RUFCOD has had an enormous negative impact on the project's ability to meet its 2010 targets successfully.

Specifically, because of security issues the IIFC network members could not move freely to increase their income generating activities, to be able to pay off their loans ultimately contributing to the self sustainability of the IIFCs they belong to. *Shura* members, who bridge the gap between the IIFCs and their communities and play a key role in sustaining these institutions, were also discouraged from publicly supporting the IIFCs in some instances in the South for serious security reasons, which has adversely impacted performance of the relevant IIFCs. The project staff could not regularly visit some of the high risk areas such as Nawa, Nadali, Chora, Arghandab, Sarkani to closely monitor their operations this year.

Corrective actions taken: The project collaborated and coordinated closely with the local government including the district governors and *Shuras* (councils) as well as Afghan national security forces and international security forces to mitigate the negative impact of the security to a minimal level on the project's ability to meet its obligations as required.

Lesson Learned: Controlling the overall security situation in areas where RUFCOD operates is beyond the ability of the project. Therefore, it should be anticipated that the deteriorating security situation on the ground can only pose challenges for the project's success as it did last year in the South and the East particularly, where the project could not make progress towards its targets as expected. However, closer collaboration and coordination with the influential *Shura* members, tribal leaders, Afghan security forces and, in some areas, international security forces can mitigate but not eliminate the negative impact of security on the success of the project.

Recommendation for 2011: It is vital for that *Shura* members' lives must not be endangered because of their affiliation and support of the IIFCs, as such incidents will put the viability of the IIFC at greater risk. Hence, it is strongly recommended that visits of the non-Afghan technical advisors of the project or others be limited to the IIFC. If such visits are made, they should be with a low profile security presence as high security profile at the IIFC attracts the attention of insurgents not only to the IIFC but also to those associated to and supporting the IIFC (i.e. the staff, *Shura* members and the members). Moreover, the local religious leaders or *Mullahs* should be met regularly to inform and remind them of *Sharia*-compliance aspect of the financial services and products being offered by the IIFCs.

2. **Challenge – low female membership in the South and East:** Female membership in IIFCs in the South and the East is much lower as compared to IIFCs in the North. It is mostly due to the disintegrating security situation and the more traditional cultural norms in the areas.

   Corrective actions taken: IIFC membership development officers (MDOs) have made efforts through encouraging people to introduce female members to their respective IIFCs. The

current female members have also been encouraged to convince their female relatives, neighbors and other acquaintances to introduce female members to the IIFCs.

Lesson Learned: Although the overall environment in the South and East is not conducive to attracting a greater number of female members, devoted and focused efforts can lead to some progress in this specific area. For instance, the efforts made last year led to the addition of 199 female members in IIFCs in the South, and 137 in the IIFCs in the East.

Recommendation for 2011: The IIFCs should recruit additional female MDOs who can have direct contact with potential female members in the communities to encourage them to become members of the IIFCs in their respective areas. This way the orientation or presentation being delivered to the female members can become more female-friendly and open for the prospective (female) members to address their concerns and ask questions.

3. **Challenge – Lack of female employees:** Finding female employees for the IIFCs, particularly in the South and the East, is also a constraint facing the project implementation in the field. Female employees are needed to work with the current female staff members of the IIFCs or encourage female membership in those IIFCs.

   Corrective actions taken: The project staff members in the South have asked the project employees and members of the IIFCs to look for female employees who might be willing to work for the IIFCs or the IIFC Group in the region.

   Lessons learned: Efforts by project staff or the IIFC Group employees will only attract limited female membership in the South and the East. This situation will improve when the overall security environment in the areas is back to normal. However, eight women were working for RUFCOD in various professional and support capacities in the South and East in 2010.

   Recommendation for 2011: The IIFCs should provide a safe working environment appropriate for females and helpful in attracting more female employees. Strictly considering Islamic values in professional dealings in the IIFCs in the South and East may convince potential employees to work for the IIFCs.

ANNEX I

Table of IIFC Locations

Region	Province	District	Islamic Investment and Finance Cooperative (IIFC)	IIFC Serial Number
South	Helmand	Lashkargah	Helmand IIFC	1
		Greshk	Greshk IIFC	2
		Garamser	Garamser IIFC	3
		Nadali	Nadali IIFC	4
		Nawa	Nawa IIFC	5
	Kandahar	Kandahar city	Kandahar IIFC	6
		Shawali Kot	Shawali Kot IIFC	7
		Dand	Dand IIFC	8
		Spin Boldak	Spin Boldak IIFC	9
	Uruzgan	Taren Kowt	Uruzgan IIFC	10
		Derawod	Derawod IIFC	11
		Chora	Chora IIFC	12
East	Nangarhar	Jalalabad	Nangarhar IIFC	13
		Shinwari	Shinwari IIFC	14
	Laghman	Mehtarlam	Laghman IIFC	15
	Kunar	Asadabad	Kunar IIFC	16
		Sarkani	Sarkani IIFC	17
	Logar	Baraki Barak	Baraki Barak IIFC	18
North				
	Jawzjan	Shibarghan	Jawzjan IIFC	19
		Aqcha	Aqcha IIFC	20
	Balkh	Mazar-e-Sharif	Balkh IIFC	21
		Mazar-e-Sharif	Balkh Employees IIFC	22
		Sholgara	Sholgara IIFC	23
		Khulm	Khulm IIFC	24
	Faryab	Andkhoi	Andkhoi IIFC	25
		Maimana	Maimana IIFC	26
	Baghlan	Pole Khumri	Baghlan IIFC	27
	Samangan	Aybak	Samangan IIFC	28
	Kunduz	Kunduz city	Kunduz IIFC	29
Central	Kabul	All Sub-districts in Kabul City	Kabul IIFC	30

Table of POS Locations

Region	Province	District	Point of Service (POS)	POS Serial Number
South	Kandahar	Maiwand	Maiwand POS	1
		Panjwaee	Panjwaee POS	2
		Arghandab	Arghandab POS	3
		Kandahar city	Kandahar Employees' POS	4
	Helmand	Marjah	Marjah POS	5
East	Nangarhar	Jalalabad	Jalalabad Employees' POS	6
		Behsood	Behsood POS	7
		Surkhrod	Surkhrod POS	8
	Laghman	Alishang	Alishang POS	9
North	Balkh	Balkh district	Balkh district POS	10
	Baghlan	Doshi	Doshi POS	11
	Faryab	Almar	Almar POS	12