Steady road to Islamic banking in Afghanistan

Afghanistan will enact its Islamic banking law by September this year to pave the way for fully fledged Islamic banks. While industry players see this as a positive move, an area of concern for bankers is the actual implementation and adherence to Islamic banking principles.

The draft law was reviewed on the 13th February by the Shariah board of Da Afghanistan Bank (DAB), the central bank, and now awaits approval from the ministry of justice, and ratification by parliament. The draft law was developed after considering those in Malaysia, Indonesia Pakistan, Bahrain, and the UAE, and was designed in consultation with Islamic scholars and practitioners globally.

With this, the future of Islamic banking is almost cemented, as Zulfiqar Ali Khan, head of the Islamic banking division at the central bank, said, “we expect that Islamic banking will lead the market.” Following the passing of the law, the central bank will give permission for all Islamic banking products to be offered to the public, added Zulfiqar.

However, the challenges for Islamic banking are not necessarily resolved with the introduction of the law. While appreciating the efforts of the central bank, Dr Alam Khan Hamdard, chief of Islamic banking at Kabul Bank, said that it is too early to say how comprehensive the framework will be for regulatory and legal purposes. He stressed that DAB would have to play a crucial role to ensure strict Shariah compliance in order to prevent corruption, malpractice and misinterpretation of the law for a successful Islamic banking industry.

To which Zulfiqar said, DAB will ensure careful licensing criteria, in addition to policies and regulations, for long-term sustainability and confidence in the Islamic banking sector.

With the enactment of the Islamic banking law, the industry is expected to introduce new product lines, “Liability and deposit products for small and medium enterprises (SMEs), Islamic microfinance and agricultural Islamic financing are top priorities,” said Dr Alam. Islamic banking investment products in corporate, retail, consumer and SME banking are most wanted and the need of the hour, he added.

With Islamic banking in its nascent state and a general lack of products available, the biggest challenge facing Islamic practitioners is the investment of Islamic banking funds, and ensuring the transparency of these investments, explained Dr Alam. With the majority of people living in rural areas, a major hurdle for Islamic banks also exists in the promotion of the concept of Shariah compliant investments.

On the flip side, Afghanistan’s economy has been growing at a rate of 10% supported by over US$32 billion in international aid the country has received since the Taliban was toppled in 2001. The potential of the banking industry in Afghanistan stands large with a deposit base of US$4.1 billion and up to US$33 billion estimated to be in circulation, said Dr Alam.

He highlighted that of the 30 million population, only 2 million banking customers exist, with half of them banking with Kabul Bank. He cited the presence of riba (interest) in conventional banks as the biggest reason for its low penetration rate.

Khan Afzal Dawal, CEO of Bank-e-Millie Afghan believes that the Islamic banking sector in Afghanistan can attract up to US$6 billion in five years. Dr Alam is bullish and expects over US$15 billion to be attracted by Islamic banking citing the strong Shariah sensitivity of the population.

The strong religious affiliation of Afghans looks to be a major contribution to Islamic banking, Zulfiqar said, “Islamic banking is part of the Islamic system and it will survive in all situations in Afghanistan. More than 30 years of war with different laws did not change the Afghans, they are still Muslims and the only successful system will be an Islamic one.”

The main focus now is the development of human resources in Islamic finance, said Zulfiqar. To this end, DAB has collaborated with the State Bank of Pakistan, as well as sent employees for training to Malaysia. Zulfiqar commented that DAB has also begun on a series of awareness programs and workshops with the Afghan Institute of Banking and Finance to develop Islamic finance experts locally.

Qatar — More clarity unveiled

Still reeling from the news of Qatar Central Bank’s (QCB) directive to shut down Islamic banking windows in the country by year end, bankers are both optimistic and pessimistic about the exercise. QCB’s decision is to separate Islamic banking windows from conventional banks without issuing additional banking licences. This translates into conventional banks with Islamic windows being forced to wind up their Shariah compliant businesses without the option of establishing an Islamic banking subsidiary.

Practitioners, while grappling with the gravity and reasoning behind the abrupt decision, have hailed it generally as encouraging. Muath Mubarak, Qatar based banking practitioner considered it as a positive move for the Islamic banking industry as it will create clear demarcations between conventional and Islamic banks and bring more transparency and improved governance.

The comings and goings of funds between conventional and Islamic has been cited as the major reason behind this decision. Referring to QCB’s motivation to maintain focused business growth, be it Islamic or conventional, Muath highlighted that the steady growth and increasing demand for Islamic banking products along with the push for standardization and governance of banking practices may have played their part in the decision.

The merging of funds has also raised concerns among practitioners, as Muath explained that this could give rise to the exploitation of large combined balance sheets by conventional financiers to go for bigger Islamic transactions. He further added that this also creates monitoring and supervisory issues on both the banker’s and regulator’s side.

On the conventional banker’s side, Salah Jassim Murad, CEO of Ahli Bank, said that QCB’s decision will reduce the number of players in an already saturated market.

The gain of Islamic banks will be at the expense of the loss of revenue streams from the Islamic windows of conventional banks. Salah said as a regulator, QCB has no obligation to compensate for loss of revenue, if any. The conventional banks will have to adapt quickly to make up for any losses.

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