

A review on Analysis of the flow of Islamic banking and economic growth in Afghanistan

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Abstract - The primary goal of this paper is to empirically analyze the performance of Islamic banking and economic growth as Islamic banking and finance is one of the most rapidly growing segment of the worldwide financial system and it is expected to be having a significant relationship and contribution toward cooperation and contribution towards into the economic growth of any country this review empirically analyze Islamic finance and economic growth in Afghanistan using and analyze previous study of the different authors with different tests and investigation related to the topic our empirical result generally signify that Islamic banking financing has a positive and significant relation with economic growth in Afghanistan. The results of this paper point out to several implications for policy. One of its implications for policy is that Islamic banking positively contributes to country's macroeconomic stability. The study found that more than 99 percent of the populations are Muslims so Islamic banking has a positive impact than conventional banks on economic growth.

Key Words: Islamic Banking, Economic Growth, Afghanistan.

1. INTRODUCTION

Islamic banking and finance is one of the most speedily growing segment of the worldwide financial system and it is expected to having a significant relationship and contribution towards the economic growth of any country the first modern experiment with Islamic banking was established in a small town in Egypt, called Mit Ghamr, in 1963 by Dr. (Ahmed El Najjar). The bank took the form of a saving-investment bank based on profit sharing and free interest, rather than commercial bank. (Ariff, 1988; Siddiqi, 2006).

Islamic banking mainly has been introduced in Islamic world forty years ago (ali 2014) in the starting Islamic and financial institution incorporated by private initiator in numerous parts around the world including non-Muslim countries in the past during the centuries of eighteenth and nineteenth some Islamic countries like Iran ,and Sudan had fully Islamized their banking system with that Islamic finance got

the form of commercial banks ,investment banks and also investment and finance companies including financial services (Sundararajan and errico 2002) and at present they are more than hundred (Islam &rahim2017).

Afterward the entire financial system convert by experts into Islamic rules and regulation in Muslim countries and that was the benefits process which is going on than some other rules and regulation effects the same direction and made that way according to Islamic sharia like, Malaysia, Iran, Sudan, Afghanistan, and Pakistan thus the experiment have been operating since more than two decades (Islam &Rahman 2017).

Islamic banking is a source of finance for Islamic and to other investors in worldwide it can be mentionable that in the past few years one of the growing stars on the world of finance was Islamic finance hence the year 2013 has been marked as turning and growing point for Islamic finance growth in this review the focused are on the Islamic banking and economic growth in Afghanistan the banking sector has a very vital role in the economy of Afghanistan (mastoor 2014) there are two parallel banking system in Afghanistan ,Islamic banking (IB) and conventional banking (CB).

Afghanistan has a developed banking system which consist a wide variety of institution and that is ranging from central bank of Afghanistan the (DAB) as Islamic banking is a new concept according to activity in Afghanistan all civilian and resident those who are busy with their life and living in Afghanistan are Muslim so their interest will be more with Islamic banking then conventional banking system (<https://www.dab.gov.af/>) and this study will help them to understand and recognize all the Islamic banking and its activities .

1.1 Scope of Paper

The Islamic banking in Afghanistan is not a new concept so here in this review paper we compare the Islamic banking with non-Islamic banking as Afghanistan is a Islamic country for this purpose the society refer more Islamic banking then non Islamic banking and Islam has showed its better way according to Sharia in Islam.

2. Islamic Finance in Afghanistan

Banking activities in Afghanistan has been started from (1171) Afghanistan is an Islamic country around 99% population are Muslims and Islamic banking is completely in growing stage beyond that Afghanistan economy has seen lots of challenges and ups and down in the last decades, the prolong war has severely depressed the activities of economic until 2001, Afghanistan banking and financial services sector (Heritage website, 2013), particularly Islamic banking, have profited from the area boom determined by demand for dry fruits and the production of industry in hand made like, carpet, and many agriculture products the gross domestic products (GDP) in Afghanistan was look in and the worth was 19.10 billion us dollars in 2019 the gross domestic product overall real (GDP) growth rate it was maintained at an impressive level of 11.2 percent in 2005 particularly the economic growth and development in Afghanistan to increase the GDP is the demand for mining and agriculture production (<https://www.dab.gov.af/>).

1.2 Islamic banking and economic growth

The relationship between Islamic banks (IBs) and economic activities or economic growth had more researcher in the local level in the recently few years. Some literature has emerged to seriously and empirically look at Islamic banking and finance unlike in classical banking where money was trading as a commodity apart of that Islamic banking system founded on real asset the risk shared between borrower and lender in that system according to the principals of partnership, ownership, joint, lease and sale also, according to Islamic finance principal the money is qualified only as a tool of exchange with the (fasih (2012) and Huda (2012) although Islamic banking has the futuristic to support the unerable groups such as farmers and (SMES) can stimulate inclusive economic growth in case some studies has been focused on that links (Abduh and Chudhry (2012) Abduh & Omar 2012) Barlow (1982) Bahlla 2002, Collins & Bosworth 1996, .

2.2 Key instruments in the Islamic banking

As the sharia matter of faith a Muslim has not the right lend money to or receive money from someone and expect to benefit its men that interest (known as Riba in Islam that isn't allowed and making money from money is forbidden there are four main Islamic financing techniques have developed the Islamic banks which are, Mudaraba, Musharaka, Ijara and murabaha (Chapra 1998) Haroon 1998, Schaik 2001 Alam and AAOIFI 2010).

1.2.2 Mudaraba (trust financing)

Mudaraba is a partnership of a financing partner the one partner is entrust his capital to the managing partner and he involving in the investment with bearing the loss and profit by the managing person, (Chapra 1998, Schaik 2001 and AAOIFI 2010).

2.2.2 Musharaka: (joint venture or profit loss sharing)

Profit and loss both are sharing joint venture it is intended to combine the talents of two or more partners in a business enterprises and all formalities and activities are divide between the partner in this partnership applied in Islamic bank (Schaik 2001 Alam 2003 and AAOIFI 2010)

3.2.2 Ijara (leasing)

Ijara in Islam is simply a lease agreement that also defined by AAOIFI (2010) as ownership of the right to the benefit of using an asset in return for consideration for example the bank purchase a piece of equipment selected by a client and back lease it to him/her for a specified rental that is called ijara (Ali 2004, Suleiman 2000).

4.2.2 Murabaha

Murabaha is in Islamic fiqh s the sale of goods at cost plus an agreed profit mark up (Al Maws Eli 1963) Al Gzaairi 1979).

3. Literature review

According the previous studies Islamic banking is based on a legal system founded by sharia law (Baker 2010) he has classified sharia law into five following categories (Riba) prohibition of interest, (Gharar) gambling to Zulm, is ban on cruel behavior in business and all other areas, Zakat tax payment based on Islamic principle and the last categories is Haram producing the product and services that are against Islamic law.

The key principle of Islamic banking is a ban on interest Abdulla 2015, earning money without taking part in any risk of loss or lending money and exchange goods without loss is strictly forbidden (Shihata 2000) Afghanistan is a Muslim country however Afghan bank customer do have different perceptions of sharia banking the perception influenced by many factors including faith, awareness, customer, attitude and the availability or lack thereof government support (Hassan 2007) Zainal ey al 2008, Fans Uri 2010, Vizcaino and Suroyo 2014).

More of the economists argue that understanding both legal system and financial is magistral to understand economic development (Levine 1998) their major impact on how people are able to respond and take advantage of economic

opportunities, access to liquidity and capacity to save contribute to a positive economic environment that has the ability to increase investment and the finding by previous evidence supported that Islamic banking has been appear to complement rather than substitute for conventional banks (imam kpodar 2010).

According to previous study some authors emphasized and analyzed in the literature some author consider finance an important element of growth and the analyzed of myself that is the backbones of growth (Schumpeter 1934) (gold smith 1969), McKinnon 1973, shaw 1973, king liven 1993, it is only a minor factor (Robinson 1952, Lucas 1988) Schumpeter (1934) sees the banking sector is as an engine of economic growth and it is funding of productive investment, Some of the previous studies and researcher, using cost and/or profit functions to compare the efficiency and effectiveness of Islamic and Conventional banks, concluded also that Islamic banks are more efficient than conventional banks (Alshammari, 2003; Al-Jar rah and Molyneux, 2005). Researchers particularly since the last two decades have been accentuating on the effects of Islamic banking system precisely on the economic growth because in such periods the growth of Islamic financial assets and the numbers of Islamic banks had a fast growth globally even western countries are now focusing to implement the performs of Islamic banks in their banks and they have been also addition Islamic financial assets by protection their rapid growth and increased demand in concern. (Caporale and Helmi, 2018).

4. Discussion

The Islamic banking in the world of competitiveness report (2016) revealed that in the last three decades of sharia compliant financial assets have grown at double digit rates at 15% of an average per annum us US \$5 billion in late 1980 to US \$2.4 trillion in 2015.

Islamic banking has been introduce in Afghanistan between 2008-2009 the law of Islamic banking for the first time prepared by the da Afghanistan bank (central bank of Afghanistan) the Islamic banking section operates under the technical support of the sharia council consisted of famous religious scholars from Afghanistan and worldwide Islamic countries.

According to estimation that US\$ 33 billion are in market circulation in Afghanistan economy while more than US \$4.2 billion is deposited in 17 banks and branches of national and international banks beside that the da Afghanistan bank, Kabul bank also has the Islamic banking section their operation has been started in February 2010 and extended Islamic banking in all branches the only reason for less

development of Islamic investment in Afghanistan is the lack of law and regulation.

Islamic financial sector development plays an important role overall development of an economy so this review tries to examine empirically the relationship between both economic growth and Islamic finance and it is direction in Afghanistan. As per the info most researches had been done by Muslims and a small portion by the non-Muslims the work of erol and El-bdour (1989).

5. Conclusion

- Islamic banking or IB is growing as a viable financial institution in areas with Muslim populations across the world this review paper has attempted to add to the literature on Islamic banks by empirically investigations the determinants of the diffusion of Islamic banking (imam kpodar 2010) the presence of Muslim population is the most significant indicator of Islamic banking.
- Increasing in oil price and also in agriculture product has a positive effect on the number of Islamic banking and conventional banking in Afghanistan, Islamic banks, financing and economic growth has a long term relationship in Afghanistan it is mean that Islamic banks economic growth move together in the long run as the study mentioned in the introduction part that Afghanistan has faced lots of economic challenges in the last few decades, as per the self-interpretation Afghanistan is located in the hearth of Asia by annihilating security and political issues it is not far that each and every thing in every part as development and growth will get well.
- This paper analyzed an found evidence that in the long run Islamic financial development is positively and significantly correlated with economic growth and capital accumulation here the result show and support that current as well as past changes in Islamic banks financing have significant impact on the changes in income in Afghanistan some other Muslim countries like Pakistan, Sudan and Iran also started Islamic banking system furthermore results show the reliability and contribution of Islamic banking to the economic sectors of the country specifically economic growth.
- On the basis of the reviewed literature it is concluded that the part of Islamic banking industry

has improved its profits. The factor which the Islamic banking making attractive to customer is loyalty to the rules of sharia their good behave and encourage the Muslim to be attractive by the Islamic banks.

- The main emphasis of this paper is to analysis the literature correlated to the relationship between Islamic financing, in overall, and Islamic banking, in specific, and financialization and economic growth. It is also concerted on the literature that conferred the relative performance between Islamic and conventional banking.

Suggestions and recommendation

At the end some current challenges for Islamic banking in Afghanistan here the following suggestions are presented below.

1. It suggest to da Afghanistan bank to have an independent department and law for Islamic banking.
2. the da Afghanistan bank is responsible for the supervise and administrate the commercial banks as well the procedure of Islamic banking.
3. according to the new technology all the necessary readiness and system should be in modern.
4. da Afghanistan bank should make a good mechanism for the Islamic banking to grow and effect the economic growth.
5. The people Afghanistan are Muslims so it will be better to refer more to Islamic banking than conventional banking's.

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