

Afghanistan Housing Sector Assessment

Updated in July 2013

Updated by: ShoreBank International Ltd. Prepared for: International Finance Corporation

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# EXECUTIVE SUMMARY

This report updates the study on housing finance sector in Afghanistan prepared for International Finance Corporation (IFC) in 2007 by a combined team of ShoreBank International Ltd. (SBI) and CHF International (CHF). To prepare the report the SBI team conducted field and desk research on the mortgage and non-mortgage housing finance sector of Afghanistan in June-July, 2013. The team interviewed public and private sector stakeholders based in Kabul and analyzed relevant housing finance policies and other documents. A list of interviewed individuals and institutions is included in Annex-3 of this report.

This paper outlines the current situation in which financial institutions operate within the housing sector, the role the Central Bank of Afghanistan (DAB) needs to play by establishing an effective regulatory regime on housing, and the need for dialogue and coordination between the actors in the private sector, donor community, DAB and the government to increase housing finance activities in Afghanistan. The authors described the major constraints affecting the housing finance sector, indicated existing micro, meso, and macro-level approaches to stimulate effective housing finance delivery, and outlined recommendations to address existing challenges and support the development of a secure and transparent housing finance sector in Afghanistan.

The team focused on assessing the following components:

1. **Housing Finance Challenges**

* Finance side constraints, both to the formal banking sector and microfinance sector;
* Significance of Sharia-Compatible housing finance, diversification of products.
* Dollarization of economy. For long term funding and mortgage finance, funding needs to be denominated in local currency, since finding any viable and sustainable FX hedging mechanism would not be affordable for the banks and/or clients.

1. **Regulatory and Legal Issues**

* Assessment of the existing Regulatory Regime at DAB, and what more is needed to be done to establish an effective regulatory role of DAB in order to stimulate and discipline the housing finance market. The mitigation of regulatory and environmental obstacles, which result from a poor or non-extant policy environment.
* Strengthening of legal framework and titles to ensure effective lien on security in case of foreclosure

1. **Housing Supply**

* New housing supply, and possible move towards low-cost housing
* Informal settlements including Hill Housing, and initiatives for their rehabilitation and resettling.
* Urbanization and influx of returnees in major cities, mostly in Kabul.

1. **Supporting Services and Capacity Constrains**

* Strengthening of Insurance sector, more so the Sharia-Compatible Takaful Insurance.
* Need for a consultative platform of stakeholders in housing finance, housing supply, the Governmental agencies, DAB, financial institutions, etc. Capacity building at all levels, the commercial banks, DAB, judiciary/mortgage law, property valuation, title search, etc.

Afghanistan is experiencing an unprecedented population growth and rapid urbanization while facing an already insufficient and dilapidated housing stock. The Afghan government is under significant pressure to provide appropriate housing to its population and recognizes that increasing finance opportunities in the housing sector is a necessary precursor to large-scale development and alleviation of the housing supply issues.

Worldwide, homeownership is a primary means of long-term wealth accumulation and financial security for most families. It plays an important role in promoting neighborhood stability and civic engagement. Acknowledging this, housing has become a priority issue for the Government of Afghanistan. Despite this pressure there has been little in the way of concrete actions to overcome the housing deficit or promote private housing finance. This is evident by seeing recommendations various reports on housing, including the Shorebank/CHF report prepared in 2008 vis-à-vis the progress on ground. Ironically various reports on housing in Afghanistan prepared since then have, by and large, carried identical recommendations with a little progress on ground.

Currently the supply of housing finance in Afghanistan by banks and microfinance institutions (MFIs) is very limited. Several MFIs, like First Microfinance Bank (FMFB-A ), have set up housing loan products available for low income clients, but commercial banks are generally less active in this sector. At present there is no financial institution specialized in housing finance in the country, although several stakeholders, including certain government officials, are considering the need for establishing such an institution. Some of the problems are caused by the lack of capacity within the sector itself, but most of the impediments exist as a result of an insecure legislative environment for the sector to operate in. While some positive steps have been taken in the past years, like the enactment of the Mortgage Law and Secure Transaction Law, these pieces of legislation operate as part of an overall poorly functioning system. The Mortgage Law and Secured Transactins Law were enacted in 2010.

Afghanistan has suffered from decades of war and resulting ineffective, or competing, governments. This has left a legacy of an undeveloped legal infrastructure, unskilled banking sector, and unclear land ownership. Since the systemic shortcomings are too complex, it is not feasible to introduce quick solutions that can solve all challenges. Instead a logical step-by-step approach must be implemented to address a range of needs.

***“Issues we know, Answers we need”*** is the general feeling among housing sector and housing finance stakeholders who call for designing and implementing explicit solutions.

The paper concludes with a set of recommendations for a way forward in the areas indicated above, some of which are to be implemented in immediate term, while others would require a medium to long term time horizon.

# ECONOMIC OVERVIEW

Afghanistan ranks in the bottom 13 of 186 countries in the human development index due to the lingering effects of war and the resulting poor governance, and 41% of its population lives below the poverty line[[1]](#footnote-1). Great progress though has been made since the fall of Taliban in 2001, and, since then the country’s GDP has been growing at the rate of 17% annually, while the projected GDP growth rate is estimated at 10-12% for 2013. The annual GDP/per capita was $300 in 2005/06 and $482 in 2010. In 2012 the official GDP/per capita was estimated at $542, while some unofficial records place it at around $785[[2]](#footnote-2). However, large segments of the population have yet to experience the tangible benefits of a growing economy.

Additionally, Afghanistan faces many obstacles to keep this growth sustainable. Much of the current growth is related to the $56.7 billion of foreign aid that has flowed into the country from international community since 2001[[3]](#footnote-3). This inflow will inevitably decrease in future, particularly in post-2014 scenario. Some estimates put the current inflow at $16 billion a year, which is likely to drop to $8 billion in the years after 2014. This uncertainty is generally referred to as Post-2014 scenario. According to Mr. Qurban Haqjo, the CEO of Afghan Chamber of Commerce and Industry[[4]](#footnote-4), the Afghan economy is less likely to be impacted by forthcoming elections in 2014, and is more likely to be impacted by the pull-out of the foreign forces from Afghanistan. Apart from its impact on the inflow of foreign aid, this may also impact the employment of a large number of Afghans who are currently employed by NGOs/Donor Agencies at jobs that are very well compensated.

Furthermore, more than any country in the world the Afghan economy derives a high percentage of its income from the narcotics industry. In 2012 Afghanistan’s opium export was 10% of its licit GDP[[5]](#footnote-5). Although this is down from 15% in the previous year, the narcotics traffic continues to be an issue, as any interruption to the opium trade without adequate recompense in the non-drug economy would be expected to have a dramatic effect on the domestic economy and security of Afghanistan.

Afghanistan also has the youngest population in the world with an estimated 65% being under 24 years of age.[[6]](#footnote-6) The high unemployment rate allows its youth entering the workplace, regardless of education levels, with few job options. The struggling school system is recovering from years of neglect, leaving Afghanistan with a low overall literacy level, and the highest rate of female illiteracy in the world.[[7]](#footnote-7)

Debt also continues to be a burden for many Afghans, with a large percentage of Afghans' expenditures exceeding their income year to year. This indebtedness is mainly due to one-time expenses such as marriages or other ceremonies, but also debt incurred for household consumption or healthcare. While the median debt burden varies from city to city, Kabul, where the situation is most grave, has a median level of indebtedness of 18,400 Afghanis ($368 USD) according to an AREU study published in 2006. This indebtedness is largely owed to relatives, neighbors and shopkeepers, and rarely to the formal sector. Nearly 18% of respondents in the AREU survey indicated that the debt was incurred for housing, although this again varied from city to city.

# FINANCIAL AND BANKING SECTORS

## Background

The financial sector in Afghanistan has experienced considerable growth since 2004; however, long-term housing finance has remained limited for various reasons. The banks’ lending ability for housing finance, though very limited, is restricted to short tenors of 2-3 years. While the banks have excess liquidity, the tenor of their liability book does not permit creating long-tenor asset books. The financial system has timidly experimented with traditional and Islamic housing finance products as well as developer finance schemes.

There are 14 private and 2 state-owned licensed commercial banks operating in Afghanistan. The banks are concentrated mostly in Kabul and provide services primarily to international donors, large businesses mostly for trade finance, foreign NGOs, and following a recent trend for funding commercial real estate. In spite of this large banking sector, only 5% of the population uses formal banking services, primarily because of faith considerations and the absence of Islamic banking. The vast majority of the population, which is mainly in the low income category, relies on informal sources of finance like friends, relatives, and moneylenders, as is prevalent in over 85% of economic activity in Afghanistan. The microfinance sector is largely funded by the Microfinance Investment Support Facility for Afghanistan (MISFA). MISFA now supports 15 microfinance institutions, operating in 23 provinces and 111 districts.

***Deposits***: Total banking deposits were at $3.68 billion as of April, 2013, with nearly 67% of all deposits being in USD. An estimated 90% of the deposits with the banks are held in current accounts, and 10% in Savings, showing that the people use bank accounts for safe money keeping.[[8]](#footnote-8) The absence of term deposits further reveals that the banking sector does not carry any medium or long term funding. Any short term lending, which is in small amounts and with tenors of 2-3 years, leads to tenor mismatch. Since the current banking in Afghanistan is based on conventional system and not Sharia-Compatible, the Bank’s clients use banks only for services, keeping their money in largely in current accounts, and avoiding interest through term deposits. This also indicates a great potential for Islamic banking in Afghanistan.

***Advances***: About 60% of total advances by the banks are for less than one year and made for medium term of 2-3 years. The non-performing loans (NPLs) stood at 4.01%. Nearly 77% of Bank’s total loans/advances are denominated in USD and 23% in Afghani, the local currency (Afs). Dollarization of financial transactions, both in deposits and advances, is much higher in the private sector banks, but the informal sector is also highly dollarized. The high dollarization of the economy presents a challenge for raising long term funds in Afghanis (Afs), and the long term funding for housing finance will not be viable and sustainable in USD because of the risk of rapid FX fluctuations in Post-2014 scenario. Furthermore, any FX risk hedging will be too expensive, if available at all.

***Country’s Foreign Exchange Reserves*** are US$6.2 Billion with DAB and US$3 Billion available with commercial banks.

The deposit rates are as follows:

* 28 Days: 3.5%
* 6 Months: 4.5%
* 1 Year: 6%

In terms of **geographical spread**, 80% of the banks are located in Kabul, 7% in Herat, 5% in Badakhshan and Mazare-Sharif and less than 1% in rest of the country. Total Assets of the banking sector as of April 2013 were at US$ 4.3 billion or Afghani (Afs) 23.5 billion. In terms of loans/advances, 85% of the loans were made by private sector banks, 10% by state-owned banks and 5% by foreign banks. That demonstrates a proactive role of the private sector banks. In terms of sectorial allocation, 29% of the of the loans are for trade finance, 17% for services, 11% for manufacturing and 14% for real estate.

***Islamic Banking***: While Afghanistan has developed an Islamic Banking Law, it is yet to be fully implemented for various reasons, including availability of an effective regulatory mechanism for DAB. Three banks, namely Bank Millie Afghanistan, Ghazanfar Bank and Bank Al-Falah, have already set up Islamic banking windows.

***Long Term Funding***: None of the commercial banks have assets or liability books with a tenor beyond 2 years, while more than 90% of liability books are in demand deposits. Commercial banks realize they will have to develop long term funding through market based instruments. DAB will need to play a lead role in developing a long term yield curve through its treasury operations to facilitate active market making. Commercial banks are also concerned about making mortgage loans denominated in local currency since any long term FX risk hedging will either be unavailable or too expensive. Again, any long term funding will have to be raised on Sharia-compatible instruments to facilitate long term lending for housing finance. Any long term liquidity facility institution will be possible only after the commercial banks have developed a sizeable long term mortgage portfolio.

***Specialized Housing Finance Institution***: Currently in Afghanistan there are no financial institutions specialized in housing finance. Prior to 2001-02 Mortgage and Construction Bank has operated as a bank specialized in housing finance, but the institution has not been re-licensed, primarily due to its poor operations and massive non-performing loan portfolio[[9]](#footnote-9).

## Overview housing finance in Afghanistan

The team confirmed that the state of housing finance in Afghanistan is still very low compared with the findings gathered during the 2007 assessment. Nearly all of the Banks interviewed are either engaged or have been engaged in construction finance. Azizi Bank provides the most construction loans, which are more mostly funding its group’s construction projects. Two state­ owned banks, Millie Bank and Pashtuny Bank, have made small housing finance pilots but did not actively pursue the mortgage business. On the microfinance side, the team found that First Microfinance Bank of Afghanistan (FMFB-A) is actively providing housing microfinance, and has recently launched a Rural Housing Microfinance Product.

The team interviewed the management of 4 private sector banks, one state-owned bank and the First Microfinance Bank. The team had interviewed the senior management/CEOs of Ghazanfar bank (June 23, 2013), Bank e Millie Afghanistan (June 23, 2013), Afghan International Bank (June 23, 2013), Azizi Bank (June 24, 2013), Bank Al Falah (June 26, 2013) and First Microfinance Bank (June 26, 2013). All banks interviewed agree that a strong demand for housing finance exists and that they have plans to enter into housing finance, once the right legal and regulatory environment exists. The overarching conclusion is that despite the prospects of a sizeable market opportunity for mortgage finance, most financial institutions do not feel the environment is compatible with housing finance. A brief overview of these discussions is presented below:

***Bank Millie Afghanistan (BMA)***: BMA has both conventional finance and Islamic banking windows. It has its own Sharia Advisory Board. More than 90% of its deposits are in current account, whereas 98% of its advances are to corporate sector and 2% are consumer loans. Nearly all of its business is dollar denominated with 90% of deposits and 80% of advances being in USD. BMA is actively pursuing Islamic banking through window operations, and has relationships with Bank Islam Malaysia and Dar-e Sharia. Basic infrastructure for Islamic Banking is ready at BMA and it will enter into Islamic Banking on a larger scale once the right environment is provided by DAB.

In the area of real estate sector, BMA is already engaged in construction finance and has signed an MOU with New Kabul City for this purpose. BMA believes there is a large demand for housing finance and it intends to expand its mortgage portfolio once the some of the risks and regulatory considerations are addressed by DAB and the government (particularly regarding the legal framework and effectiveness of foreclosure procedures). BMA considers DAB and the government (the Ministry of Finance) need to establish a clear Policy Framework on mortgage finance for effective regulation which will send a clear message to the financial sector that it is committed to promote and support mortgage finance[[10]](#footnote-10).

***Ghazanfar Bank***: Established in 2009 Ghazanfar Bank is a relatively new bank, which operates out of 10 branch networks through both conventional and Islamic banking windows. Its operations are highly dollarized, with 90% of Deposits in USD, 5% in Euros and only 5% in Afs, and its entire advance portfolio is in USD. About 80% of its advances are to corporate sector, and 20% to the SME sector. While 90% of its deposits under conventional banking are in current account, 85% of its deposits under Islamic banking window are held as time deposits. Under the Islamic banking mode, the bank shares profits with the clients at 60:40, giving 40% share to the client.

Ghazanfar Bank used to provide construction loans but currently does not provide any housing finance products. The bank aims at entering into mortgage finance once the right environment is provided by DAB/Government in terms of effective regulatory environment by DAB, including secure titles, effective and efficient foreclosures, establishment of a credit bureau, availability of qualitative and quantitative data on housing supply, property valuation etc. DAB is currently working on developing a Sharia-compatible housing finance product, to be launched once right environment is available[[11]](#footnote-11).

***Afghanistan International Bank (AIB):*** AIB also has its entire liability book (99%) in current deposits, and 95% of all deposits are in USD. About 95% of its advances are for trade, and all are denominated in USD. The CEO of AIB commented that traders are earning profit margins of 15-30% in a six months cycle, so taking loans in USD at current interest rates is not an issue. Currently AIB is not in the mortgage business, and has only provided some construction finance loans for commercial real estate. It is however considering introducing housing loans up to $100,000 for tenors up to 3 years. However, its CEO shared apprehensions on security of mortgage loans similar to the views expressed by other bankers. AIB is also skeptical about post-2014 scenario and would like to wait until the uncertainty clears out on that front as well[[12]](#footnote-12).

***Azizi Bank***: The Azizi Bank has a deposit book of $700 million, two-third of which is in USD. Its total advances are $300 million, and 80% of advances are in USD. The Bank is actively funding its Group Companies, including its own construction projects. Azizi Bank’s exposure to the construction sector is around 36%, which is exceeding DAB regulations restricting banks’ sectorial exposure to 15% (with DAB’s knowledge). About 15% of its portfolio (Afs 2.2 Billion) is invested in DAB Capital Notes.

Azizi Bank is not considering actively entering into mortgage business, and the management would like to wait until the uncertainty on post-2014 scenario is cleared. In fact, post-2014 they are anticipating a large capital flight that will further adversely affect the exchange rate. The management realizes that any reasonable tenor mortgage book will have to be denominated in local currency, and for that DAB will need to initiate consultations with the market players. In view of the uncertainty and expected devaluation of Afs, the Bank considers even 2-3 years tenors being risky[[13]](#footnote-13).

***Bank Al Falah***: Bank AlFalah has 95% of its deposits in current account, and all in USD. In total, 85% of its overall deposits are in USD. The bank currently is equally active in Kabul and Herat while in the past 70% of its business was in Herat. The Bank is quite active in Islamic banking through window operations, since it has the support of its parent bank based in UAE, which has a well-known standing in Islamic banking. The bank intends to expand its outreach, but has put its expansion plans on hold in view of post-2014 uncertainty. It believes that the real size of Afghani economy will be determined in post-2014.

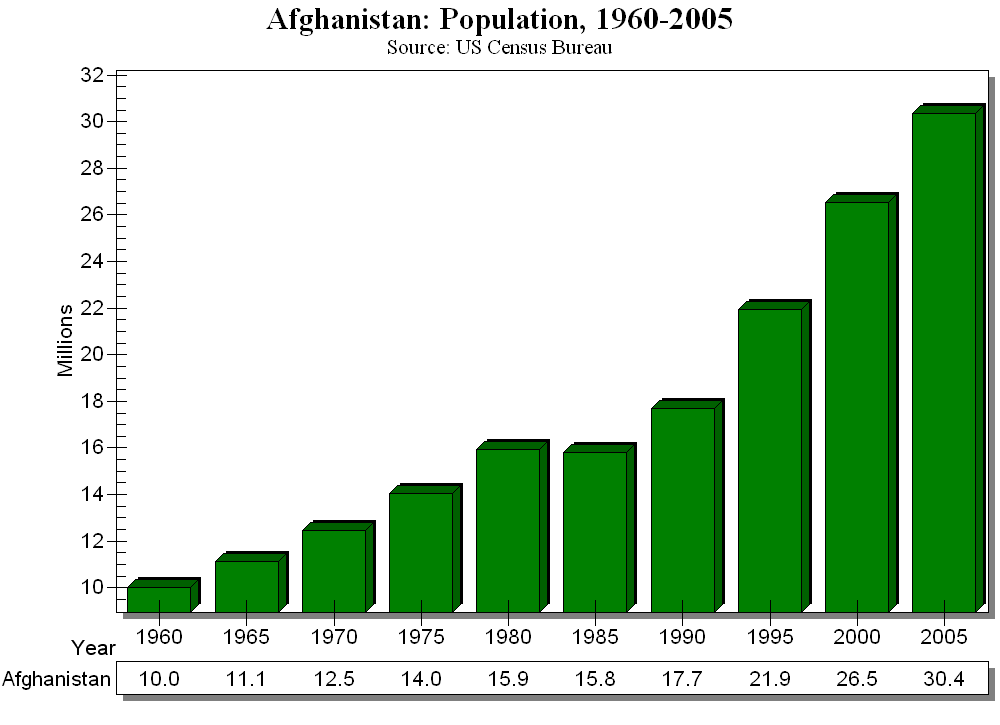
Bank Al-Falah is currently not active in mortgages business, although it has investment of $30 million in commercial real estate finance. Its views on security of mortgage finance are similar to those of other commercial banks. Its management strongly feels that the Government, DAB and the legal system has to take a conscious view to address these issues and take decisive steps for mortgages to become attractive for the financial sector[[14]](#footnote-14).

# HOUSING OVERVIEW

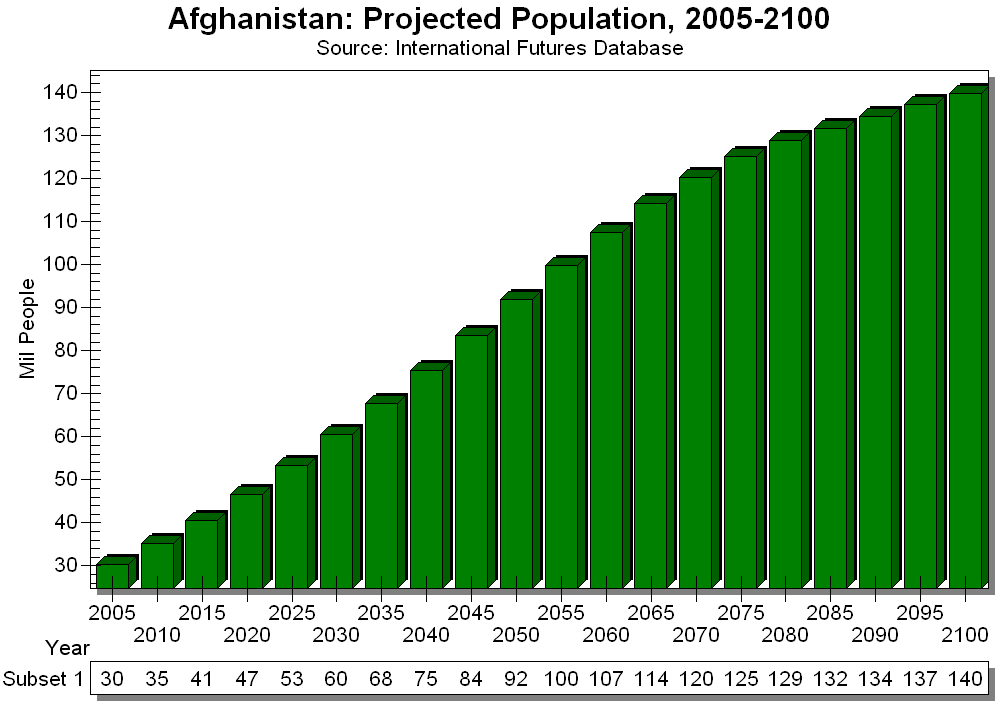
## Population growth and growing housing needs

Until the modern period, urban dwellings in Afghanistan were located within modest-sized walled cities, unchanged for centuries in their basic layout. It was only in the 20th century that urban centers began to spill outside the city walls and take on characteristics associated with Western models, including high-rises, paved roads, and city services. Urban life deteriorated rapidly after the collapse of the communist regime, and a number of cities suffered severe damage to their [infrastructures](http://www.britannica.com/EBchecked/topic/7798/Afghanistan/226136/Housing) during the late 90’s and early 21st century. The city of Kabul seems worst of all, where a large segment of the housing is partially or totally damaged/destroyed, and its infrastructure is badly damaged. By that time, very few city services - electricity, water, sewage disposal - remained intact. As a result, a large number of people fled to the countryside, seeking shelter from the civil war. These people remained poorly housed and, lacking a central government, were forced to rely on private means for shelter. Rebuilding the country’s housing sector has been and still is one of the major tasks in national reconstruction.

Afghanistan’s conflict-ridden past and rapid current growth in both income and population pose unique challenges for the housing and housing finance sectors. Afghanistan’s population is estimated at 31 million in 2010[[15]](#footnote-15). The population according to UN estimates is expected to grow to 37 million (Fig.1- and Fig. 2) by 2015.[[16]](#footnote-16)

***Figure 1.***

***Figure 2.***



The total number of household in Afghanistan is estimated at around 3.4 million. This implies an average household size of 9.1 persons[[17]](#footnote-17). The population of Kabul grew by 15% a year during 1999 to 2002, and is expected to grow at 5% annually as a result of migration and natural growth.

The returnee immigrants from neighboring Pakistan and Iran are mostly settling in Kabul. In 2001 the population of Kabul was 1.2 million; in 2005 it was estimated at 2.5 million. While the current population of Kabul is officially quoted at 3.1 million, its unofficial estimates are in excess of 5 million. It is expected to cross 8 million in next 15 years. Urbanization is very high, particularly for Kabul, with no precise estimates available on urbanization rates and population. The returning refugees are further exacerbating urbanization challenges and the housing gap. The city of Kabul is growing and expanding horizontally, joining its boundaries with neighboring cities. A large number of Kabul populations are living in Hill Housing Settlements, which is mushrooming and presenting a challenge to the city administration. Municipal and City Services in the city of Kabul are now getting insufficient due to this unplanned urbanization, including Informal Hill Settlements. The City’s Social, Physical and Economic Infrastructure are extremely overloaded and seek an immediate address to the issue[[18]](#footnote-18).

Current estimates for housing shortages in Afghanistan stand at 1.0-1.25 million, 70% of which are in urban areas, and the shortage is likely to go up to 1.5 million by 2015[[19]](#footnote-19). The rehabilitation of existing damaged housing stock and new construction of housing units in Kabul alone are estimated at $2.5 billion of fixed capital investment only[[20]](#footnote-20). A large part of existing housing is in dire need of an upgrade. Kabul’s informal settlements shelter 80% of the population and cover 69% of the residential land in Kabul[[21]](#footnote-21). The quality of housing stock is poor, while construction standards are weakly enforced. Both public and private housing provision has been lagging even the yearly incremental demand, thus adding to the already existing shortage. This made the housing shortage reach to 1.25 million units by 2010[[22]](#footnote-22). Limited government capacity and an insufficiently supportive legal framework for private sector involvement on one side, and very nominal mortgage finance by the banks on the other, is responsible for this shortcoming. The existing housing portfolio in the asset book of financial sector is even less than 1% of the advances, and that too for short tenors[[23]](#footnote-23). The fear of loan losses and resulting provisioning cost due to poor land titling and loan security is the major factor inhibiting Banks/FIs from entering into mortgage finance business.

The financial sector in Afghanistan has experienced considerable growth since 2004; however, the long-term housing finance has remained limited for various reasons. According to banking sources, most of the secondary market transactions in housing are usually for cash. The banks’ lending ability for housing finance is restricted to short tenors of 2-3 years. While the banks have excess liquidity, the tenor of their liability book does not permit creating long-term assets. The financial system has timidly experimented with traditional and Islamic housing finance products, as well as developer and/or construction finance. There is a general view in the banking circles that construction finance should be considered by DAB under its own category, distinct from the mortgage finance. The penetration and affordability of housing and housing finance remains limited to the upper income bracket. The diversified products for mortgage finance, including home insurance, are non-existent.

The vast majority of the population, which is mainly in the low income category, relies on informal sources of finance like friends, relatives, and moneylenders, as is prevalent in over 85% of economic activity in Afghanistan. These considerations and large market potential suggest a micro and low-income housing finance approach, mostly oriented towards home improvement loans. The microfinance sector, which is gaining momentum in Afghanistan, is making initial efforts to expand into low-income housing, relying on its comparative advantage of experience and knowledge of the borrowers. The sector is also uniquely suited to service women, who have limited access to formal and informal finance because of the cultural limitations and their lack of guarantees and title deeds. Potential demand in Micro and SME finance is considerable, since four out of five people fall at bottom of income/affordability pyramid. Estimates suggest a total financing need of $276 million a year for home improvement and new construction in Kabul’s informal housing sector.[[24]](#footnote-24) Future growth of the micro-housing sector might create funding bottlenecks, pushing microfinance institutions towards market funding, thus posing a challenge of commercial sustainability, and possibly leading towards the need for a second-tier institution for long-term funding provision.

According to UN estimates, from year 2000 to 2015, the population of Afghanistan is expected to increase by 14 million, from the then estimate of 23 million to about 37 million. Rapid population growth and urbanization will further compound the housing problem in Afghanistan, especially in such cities as Kabul, Jalalabad, Maser-e Sharif, and Kandahar. The population census of 2005/06 has estimated that, 22% live in urban areas and 78% in rural areas[[25]](#footnote-25). More than half of the projected growth will be in urban areas, where the housing deficit is already severe.[[26]](#footnote-26) There are no official figures on urbanization, and it is stated in meeting with Ministry of Urban Development to be around 15%[[27]](#footnote-27), and probably more in Kabul. The country also has the youngest population in the world, with an estimated 42.6 % under the age of 14.[[28]](#footnote-28) An estimated 65% of the population is young Afghans, candidates for good employment opportunities and independent housing units[[29]](#footnote-29). As these young people get into employment, they would need places to live, that will add to the pressure on the urban housing sector and represents a potential for housing market. The rising income levels may provide opportunities for a growing housing market as long as the right kinds of policies and interventions are put into place.[[30]](#footnote-30)

A third of the country’s population is concentrated in 5 of its 34 provinces: Kabul (around 5 million), Herat (1.78 million), Nangarhar (1.43 million), Balkh (1.25 million), and Kandahar (1.15 million)[[31]](#footnote-31). These provinces have large urban concentrations and perennial housing shortages. Population growth is now estimated at around 5%. This rapid growth and urbanization result in substantial migration into informal settlements in major metropolitans like Kabul, Herat, Kandahar, Nangarhar, Mazar-e-Sharif, which challenges urban planning as the city expands in an ad-hoc manner.

## Kabul City

Kabul City is the capital of Afghanistan, as well as the capital of Kabul province, with a population of 4,378,000. Kabul City is the leading economic and cultural center of Afghanistan. The majority of the inhabitants of Kabul City are Farsi (Dari) speaking Tajiks, alongside a large Pathan (Pashtun) minority. Kabul City commands the strategic routes to Pakistan via the Khyber Pass. The city was captured by the Taliban on 27 September 1996, and recaptured in November 2001 by forces of the Northern Alliance during the U.S.-led invasion.

Kabul is the biggest city in the country and one of the fastest-growing in Asia, according to reports from the Afghanistan Research and Evaluation Unit (AREU). AREU's report, citing a World Bank presentation, states: "With an estimated population of about three million in 2005, growth rates reached as high as 17 percent in recent years, and currently the city continues to grow annually by five percent." The expansion is largely unplanned, and is based on rapid immigration into informal settlements. Kabul is also facing a huge settlement problem. Kabul’s 80% population is living in informal settlements, which are said to be built on about 69% of the city’s residential land[[32]](#footnote-32). The recently emerging and fast growing Informal Hill Settlements would significantly increase these numbers.

Mr. Khalid Maftoon, the Doing Business Advisor at the Ministry of Finance is a strong promoter of the need to expand cities like Kabul in vertical direction rather than horizontally in order to maximize the efficient use of land[[33]](#footnote-33). This seems to be already in progress, as a large number of high rise apartment complexes have been recently built and many being under construction. However all of this new housing supply in high-rise building is for high income segment of the population.

## Jalalabad

Jalalabad is the capital of Nangarhar province, in eastern Afghanistan. The total population of the province is around 1.43 million. The city is situated on the road from Kabul to Peshawar in Pakistan and as such is a major transportation route. The population of this city is estimated at 206,500. Jalalabad is well-placed to handle much of the trade between Afghanistan to the west and Pakistan to the east, and is the commercial center for the irrigated plain around it. It trades in almonds, rice, grain, and fruit, while industries include sugar refining and handicrafts.

# HOUSING SUPPLY

## Housing: Growing Demand and Growing Shortages

Afghanistan, like many other countries in the region is facing a massive housing shortage, in relation to its population, and the shortage is further intensified by the discrepancy between the limited housing supply and the incremental growth of housing demand. Housing shortage is estimated at about 1.25 million units, and the shortfall is likely to exceed 1.5 million by 2015[[34]](#footnote-34). A long history of conflict and resulting destructions, high population growth, rapid urbanization and returning refugees has aggravated the housing shortages in Afghanistan.

Development of a large amount of illegal and overcrowded housing, without access to basic city services, has been another challenge for the urban planners. Many of the more than six million returning refugees that left the country during the conflict are now returning, putting upward pressure on the demand for housing, and adding to the already existing backlog. Nearly entire housing shortage in major cities like Kabul is in low-income segment of the population, while people characterized as being at the Bottom-of-Pyramid (BOP) live in informal settlements.

**Factors influencing high demand for housing**

* Historical housing shortages;
* New demand due to population growth;
* Damaged/destroyed housing stock during the military conflict;
* Additional housing needs for returnee refugees;
* Increased urbanization.

## Supply side challenges

According to a survey carried out in the post-Taliban era, the condition of the housing stock in Afghanistan is very poor and it is estimated that one fourth of the housing stock is seriously damaged or destroyed. The conditions since 2001-02, in the post-Taliban era, however have not much improved. While there are different plans in this direction, these plans are constrained by the unavailability of resources, most important of which are financial resources.[[35]](#footnote-35)  Most indications are that aside from some improvements to the roads and, and to a lesser extent to the water system, the challenges in housing supply and infrastructure remain severe.[[36]](#footnote-36)

Recently Afghanistan, more so in Kabul, is seeing surge of housing supply, with the launch of many large scale developments and settlements. Municipalities, the Ministry of Returnees, and the Ministry of Urban Development have several public sector projects which are in the planning and development stages. Mostly the Municipalities programs cover the provision of serviced/developed plots of land with clear titles for housing construction, while the initiatives taken by the Ministry of Urban Development aim at providing finished housing units[[37]](#footnote-37).

**Summary of issues affecting low housing supply:**

* + **Land Availability:** Land in major cities is getting scarce because of the rise of informal settlements and illegal appropriation of refugees’ properties by powerful interest groups;
  + **Land Titles:** Difficulties in establishing clear title to property is hindering the growth of new construction;
  + **Damaged and Destroyed Housing and Infrastructure:** More than three decades of war has severely damaged the existing housing stock as well as any supporting infrastructure;
  + **Affordability:** Availability of affordable housing is a major challenge, exacerbated by very slow or no transition in the past decades of low income population into the middle class bracket;
  + **Legal Issues:** Lack of clear legal framework including building codes, transaction and foreclosure laws further disincentives both increased construction and housing finance;
  + **Financing:** Limited financing available for construction finance and practically no housing finance available for individuals from the formal financial sector;
  + **Financial Institutions:** Financial institutions don’t have the capacity to advance housing loans even if the capital is available;
  + **Regulatory Regime:** DAB is yet to develop an effective regulatory regime to promote housing finance, and particularly to promote low-income affordable housing and housing microfinance;
  + **Home Improvement Loans vs. Mortgages**: There is a great need in both rural and urban areas to bring partially or totally destroyed properties in a better shape, thus presenting a strong demand for home improvement loans;
* **Urbanization and Returnee Refugees:** People prefer to live in urban areas due to better social, physical and economic infrastructure. This is main reason that even the Returnees are mostly settling in city of Kabul.

These initiatives include housing construction for returnees from Pakistan and Iran. In Kabul, some semi-public sector initiatives are also in progress like housing development through Abu-Dhabi Fund and by Turkish Developers. Progress in new construction has been slow because of limited capacity, the scarcity of serviced land, and the lack of funds for re-constructing and developing infrastructure.

However, all this new supply is marketed at very high prices and thus it caters to the housing needs of high income segments of the population. Practically there is no supply of low income housing, or any public initiatives that cater to the housing needs of middle and low-income segments of the population.

## Various housing supply programs:

1. **New Kabul City:** The “new city” project, divided into four parcels, plans to build 80,000 units in its first phase[[38]](#footnote-38).The Ministry of Urban Development intends the New Kabul City Project to run independently in a transparent manner based on a corporate business model.

Parcel-2 comprising of 30,000 units was awarded to a local investor - Basir Omarzai. This Parcel is already contracted and the land has been purchased from local owners.

IHFD/QMC has been awarded 12,000 housing units part of Parcel-1 and is close to signing the contract. IHFD/QMC would also have to purchase the land for this parcel from local owners. The government of Afghanistan is facilitating this purchase, and the necessary legal formalities have been completed. Currently IHFD/QMC has two international partners; 1) Gulf Cup Group - large brokers and builders from Dubai and 2) Pinnacle, an Australian Company that is responsible for arranging funds through Chinese Bank(s). IHFD/QMC is also looking for additional support from OPIC through its funding/guarantee instruments. OPIC may also be offered shareholder position in the project. The group also stated its intentions to set up a mortgage company under the project that would provide long term mortgages. IHFD/QMC intends to invest $1 billion over a period of 6 years. The project would be managed by Ellisdon, a specialized Canadian management company experiences in building large scale housing projects. The USA based insurance company, MIGA, is seen as a potential partner for providing housing insurance.

Commenting on political and security environment post-2104 after ISAF withdrawal from Afghanistan, Mr. Sultan Maqsood Fazel of IHFD/QMC generally sounded optimist. Against the general perception of lawlessness and chaos in 2014, Mr. Sultan sounds confident in the future of the project, citing US commitment of providing $8 billion yearly support for security and civil works/development purposes, the ongoing talks between Taliban and US and the need for housing in Afghanistan and Kabul in particular, as major factors that will drive the success of the New Kabul City project. However, he also acknowledged that a temporary dip in economic activities in 2014 may be seen.

1. **Abu Dhabi Fund** is building 111 blocks which will be having 3,333 apartments, and have started the foundation work. The developer offers 2, 3 and 4 bedroom apartments and 5 year mortgages.
2. **A Turkish Developer** formed a joint venture with the Ministry of Urban Development-MoUD and is building 15-story high-rise buildings for approximately 900 apartment units.
3. **Azizi Development** is the largest developer in Afghanistan. Construction on their housing development of 15,000 apartment units is underway.
4. **ARYA City** is a Project of Century Land Corp owned by Haji Rasheed. A local real estate developer, Century Land Corp. has launched a project to build high-rise multi-family housing complexes, each with 45 apartment units, for high income segments of the population, offering 2 to 6 bedroom apartments. The project is progressing well, and some buildings have been completed and the residents have already moved in.
5. 

Community life in Arya City is very active and integrated, with schooling and health services available to residents. The neighborhood has very wide roads, community parks and children play areas, its own mosque, a school up to the six grade, and a shopping area. The originally announced price range was $60,000-$240,000 per unit but the prices have increased since the successful launch of the project.

In the first phase 20 apartment complexes were completed and all have been sold out. There was no mortgage finance facility available for clients, nor had the developer accessed any bank finance to complete the construction. Century Land Corp. has available land to build up to 100 such apartment complexes, and is working on purchasing more land to complete a total of 360 blocks. By any standards ARYA City is a residential compound comparable to any international standard housing[[39]](#footnote-39).

1. The government has been working on a **National Housing Program** to build 150,000 units in different parts of the country. The Minister of Urban Development stated that the country-wide program will cover 157 locations. Under the program, some projects are under construction while others are in planning stage[[40]](#footnote-40).
2. In a past **Government/Municipalities housing program,** 450,000 plots were distributed with the expectation that the recipients would construct individually their housing dwellings. Unfortunately, houses were built only on 15% of the plots and the rest were either sold or are otherwise still unutilized. In fact such schemes only promoted land speculation in the market.
3. **Housing Schemes for Teachers**: The Ministry of Education has an overarching goal to reform the educational sector, and puts a strong emphasis on female teachers. Its objective is to increase the number of female teachers by 50%. The Ministry plans to implement a housing incentive to accomplish this goal by providing land for women teachers who live in, or are willing to move to rural regions. Legislation is expected to be passed to distribute land to teachers, but a key missing piece is the lack of housing finance to complete the construction. Unfortunately, this plan is being considered by the Ministry of Urban Development since 2007-08 (by the then Minister Engr. Yusuf Pashtoon) and no tangible progress is seen on ground. If such program could be implemented, it would offer a practical example for low-income housing solutions for civil servants, police, and other government employees. However, for this housing scheme to be a viable low income housing solution, it is necessary to develop a housing finance facility to support the construction. This could serve as an interesting lower-risk housing finance pilot for financial institutions – the land offered as part of the scheme will not have title issues, the repayment capacity of government employees would be easily verifiable, and the repayments could be directly deducted from clients’ salaries.

## Housing Costs

The formal housing in Kabul is in short supply, expensive, and offers little for too much money - both in terms of purchasing and renting housing units[[41]](#footnote-41). The current housing market in the country, and particularly in Kabul City, caters mainly to the high income segment of the market, i.e., households earning more than $3,500 per month. According to a World Bank study on housing in Afghanistan[[42]](#footnote-42), the housing costs, mostly based on Kabul city estimates, were:

* Upper Middle Segment: a 200 Sq. Meter apartment - $40,000-$50,000
* Low Income Segment: for a two room dwelling - $5,000-$10,000
* Home Improvement: to upgrade a two room house - $500-$1000
* Home Improvement: for improvement and room addition - $100-$5,000

***Factors responsible for high cost of housing***:

There are several constraints in the housing sector that directly impact cost, reduce affordability, and limit the ability of the housing market to deliver adequate products. Some of these constraints are discussed below:

**Cost of Construction**: All basic construction materials used in conventional building systems in Afghanistan (steel, glass, cement, pipes, sanitary wares, etc.) are imported. This makes cost of construction at $400-500/m2**.**

**Cost of Land:** Building within the Kabul city is about 20-30 % more expensive than building in the outskirts, because of the higher cost of land, which can take up to 50-60 % of the project cost in a good location within Kabul.

**Unit Size:** Supply is limited to large size units of 100-200 m2, and high construction costs makes it affordable only for high income segment.

**Developer Skills and Capacity:** The developers yet need to acquire low-cost construction technology and skills, as well as use low-cost construction materials to lower the construction costs. For lowering the construction costs, housing development has to be done at scale, and Afghan developers may need to form joint ventures with large scale developers in the region to acquire experience, skills and capacity.

**Poor Construction Quality and lack of enforcement of construction standards:** The quality of construction has become a major source of concern in Afghanistan. The main reasons are lack of quality control in the materials used for construction, lack of supervision, and prevailing corruption in enforcement of construction standards. Municipalities, responsible for setting and enforcing building codes, have been very poorly in enforcing existing regulations. Some of this stems from old zoning and planning maps, which in many cases forces people to build in illegal and thus unregulated areas, with poor building methods. When people are building in zoned areas, they are required to get proper permits based on municipality approved blueprints and titles. However, in reality there is no oversight and the final constructions are rarely up to the building codes, or according to the approved blueprints. Anecdotally, when city engineers do visit construction sites, it is commonly commented that for a small payment they will move on to the next building site without any negative comments, despite obvious signs of code violations. The enforcement of the edicts at municipality level will be as important as setting the standards for material and construction quality.

The current applicable Construction Standards and Building Codes are:

* **Construction Standards:** The Afghan National Standards Authority, established by the Ministry of Commerce in May 2004, is responsible to set standards for both imported and locally sourced construction materials, and the results will depend on enforcement of these standards.
* **Building Codes:** The enforcement of building codes is municipalities’ responsibility. Those building in zoned areas are required to get proper building permits, issued only after the municipality approves blueprints and title. However, the oversight has been poor. In order to control construction quality standards, the Municipality has a separate Construction Control Department, which is generally alleged for poor controls. In practice there does not seem any construction oversight and most home construction neither follows the existing codes, nor approved blueprints. City engineers often ignore code violations for a small payment[[43]](#footnote-43).

# RETURNEE REFUGEES

Twenty-six years of almost continuous warfare forced nearly six million refugees to flee Afghanistan mainly into Pakistan, and some into Iran and other countries. The actual number of these refugees is not determined, except the official figure of registered refugees. In the process of natural population growth, considering a figure of four in a family, the refugees by now might be in somewhere 15-20 million. In the post-Taliban era, with peace settling in, the country is seeing a gradual return of many refugees. A special Ministry of Refugees and Repatriates is responsible for resettlement of returnees. During the years many have returned to find housing infrastructure that has been badly damaged by war and repeated earthquakes, their land legally appropriated by others during successive governments or illegally grabbed by powerful informal groups. The continued inflow of returnees will further exacerbate the problem of inadequate housing and infrastructure, particularly in larger cities like Kabul, Jalalabad, Mazar and Kandahar.

According to Dr. Jamaher Anwari, Minister of Refugees, about 1.7 million people registered as Afghan Refugees are still living in Pakistan, and their Refugee cards are expiring on June 30, 2013. The government is negotiating with the government of Pakistan to extend this period, but if an agreement is not reached, many of these registered refugees may return to Afghanistan. Another one million un-registered refugees are likely to return in the near future.

The government has taken some steps to facilitate accommodation/resettlement of about 2 million returnees/refugees, which include:

* 48 sites planned across 22 provinces for resettlement of Returnees;
* 22 MOUs have been signed with different Ministries to provide various facilities at those sites;
* A total of 314,667 plots are being earmarked for Returnees;
* The Ministry mentioned that it will facilitate provision of housing loans to the refuges resettling on these sites, once a specialized housing finance institution starts functioning in Afghanistan.

# HOUSING FINANCE MARKET:

This section focuses primarily on mortgage and collateralized housing finance (in Sharia-Compatible mode it is termed as Housing Finance and not Mortgage), and the overall economic and policy background for the Afghanistan housing market. While some issues of micro finance are discussed, non-collateralized forms of housing finance are reviewed in greater detail in Section 7: Housing Microfinance**.**

## Background

Housing is a driving factor in the economy and is a major contributor to wealth accumulation in all segments of society. Houses are often the single most important component of the asset side of households' balance sheets. The availability of housing finance can help alleviate poverty by helping families acquire homes and help increase near-term consumption by spreading housing payments over an extended period. Equally important is the follow-on effect of creating a large pool of unskilled and semi-skilled employment in the construction industry. In Afghanistan, where the conditions of a large housing deficit and high unemployment exist, access to affordable housing and housing finance would facilitate the growth of housing and living standards.

The housing shortage in the urban areas has resulted in the mushrooming of illegal slum settlements without access to the most basic of city services. The World Bank has done a series of housing need assessments in Kabul, and estimates that: "Informal settlements shelter about 80% of Kabul's population ( about 2.44 million people), cover 69% of the city's residential land, and represent a fixed private capital investment of $2.5 billion (not including land value)."[[44]](#footnote-44) This policy note and others in the series conclude that the informal settlements should be upgraded rather than demolished or ignored, and that the tenure of the households living in these settlements should be regularized. It further notes that these informal settlements currently contribute to Kabul's tax base in the form of purchase of sanitation and electricity payment books (67% of the population), which can be expanded to include income taxes over time.[[45]](#footnote-45) According to the Mayor of Kabul, Mr. M.Y. Nawandish, about 80% of the Kabul population, estimated at 5 million in 2013, lives in informal settlements, occupying about 70% of City’s residential land. These estimates do not include the informal fast-growing Hill Housing Settlements.

Due to this unplanned population explosion and the expansion of informal settlements, the Municipal and City Services in the City of Kabul are getting insufficient and deteriorating in quality. The City’s Social, Physical and Economic infrastructure is deteriorating fast. The government is working on plans to enforce some kind of tax for the services they are already using[[46]](#footnote-46). The illegal status of these informal settlements does not signify the residents live rent-free; most inhabitants pay a fee to different groups to avoid eviction and are often harassed or intimidated by powerful groups such as land grabbers. In fact, the rents are increasing even in these settlements, and a number of low income people are being evicted from these slums and forced to find even more meager shelter. Because of housing shortages it is estimated that over 1/3 of all houses, in both legal and illegal settlements in Kabul, accommodate two or more families.[[47]](#footnote-47).

In rural areas access to land is less problematic, although women face a larger challenge to claim or reclaim their rightful property. Without policy interventions to address this issue and without enabling environment for investment in housing stock, the housing shortage may worsen. The Government has recently announced a policy on slums rehabilitation and resettlement (Annex-5).

## Impediments to development of Mortgage Finance

The following impediments to increasing the level of mortgage finance were generally quoted by the interviewed banks:

* ***Bankable Titles***: There are four kind of titles generally found in Afghanistan, and at present Banks feel comfortable with only one kind i.e., Urfi Title.
* ***Lien Registration and Transfer***: Afghanistan needs to establish efficient and cost effective system for lien registration and title transfers. Banks were appreciative of some steps taken by the Government in this direction.
* ***Efficient Foreclosure***: While, introducing the Mortgage Law is seen as a positive development, there are still several pressing issues related to foreclosure procedures that need to be addressed. For example, currently it is not possible to foreclose on a property without court orders, and court proceedings take very long time. There is also a Sharia Judgment that does not permit eviction generally quoted by the Bankers. This judgment stipulates that a person cannot be evicted under Sharia rules if the defaulting borrower has only one shelter and does not have another house to move in after eviction. The team could not find any documentary evidence of such a Sharia injunction, and believes that if such an injunction exists, it could be counter-argued on the fact that honoring the terms of a contract is binding according to Sharia. Additionally, according to Bankers their main concern is clarity, efficiency and effectiveness of the Judiciary system and not the deficiency in Mortgage Law. One solution would be to organize workshops on Mortgage Law and Foreclosure proceedings with participants from main stakeholders such as the Banks, Judiciary, and the Government.
* ***Credit Risk Assessment***: Lenders perceive housing finance as having a significant credit risk, citing challenges such as the absence of client credit history, appropriate property valuation methods, formal records to assess income, as some of the reasons for their cautiousness in entering or expanding these products.
* ***Capacity Building at the Banks***: Commercial banks have limited or no experience providing housing finance, and lack capacity and trained staff to effectively carry out mortgage business. The banks consider that once a regulatory function is effectively established at DAB with Mortgage Prudential Regulations and Mortgage Guidelines in place, a Capacity Building Program, with some Technical Assistance for commercial banks, could be initiated by DAB in association with Afghanistan Banks Association.
* ***Property Valuation***: Property valuation is currently being done by real estate brokers, who are not trained in property valuation and often over-value the properties, causing the risk of over-lending.
* ***Income assessment***: A large section of the urban population is self-employed or is involved in informal trading activities, making it difficult for banks to assess the sustainability of their incomes. Additionally, most medium and low income segments in Afghanistan [[48]](#footnote-48).cannot afford the formal housing doweling currently available in Kabul. As such, these population segments are not an immediate priority for the banks. Instead, banks initiating housing finance programs in major cities like in Kabul could focus on serving population formally employed who lack acceptable housing arrangements, such as those employed by NGOs, donor agencies, civil servants and security forces.
* ***Regulatory Regime for Mortgage Finance***: Currently DAB has no mortgage-specific Prudential Regulations, Mortgage Guidelines, and Developer Finance Rules etc. Most of the real estate lending by the banks is for commercial real estate and a small proportion goes for residential real estate. The commercial banks feel that DAB needs to strengthen its regulatory function and that housing finance and mortgage finance should be treated distinctly from construction finance in terms of loan limits and other regulations.
* ***Credit Bureau***: Currently there is no Credit Bureau and Credit Rating System in Afghanistan, which makes client’s credit assessment a major issue. Although DAB is in the process of establishing a Credit Bureau with some foreign technical assistance, in the absence of a national identification number and any historic credit data, the implementation of credit checks for loan assessment purposes will take a significant time.
* ***Sharia-Compatibles Financing Modes and Products***: The unavailability of “Sharia Compatible” finance is quoted as an important reason for not taking bank loans to finance ones business and housing needs[[49]](#footnote-49). DAB has been considering inviting the private sector to set exclusive Islamic Commercial banks, but no progress been seen yet. Several banks like Bank-AlFalah, Bank Millie and Ghazanfar Bank have started Islamic banking through window operations. . The Mortgage Law already addresses some issues related to Islamic Mortgage finance, and DAB has also announced new Islamic Banking Laws (Annex-2) for issuance of Islamic Banking licenses, and is developing its regulatory policies. DAB believes that once clients are provided with faith-based housing finance options through a diversified product range, the housing finance market will substantially improve.
* ***Long Term Liquidity***: Since more than 90% of banks’ liabilities are demand deposits, they don’t have sufficient long term liquidity to provide term lending for mortgages loans. The banks recommended that DAB, in consultation with the Association of Banks in Afghanistan, to develop a plan to facilitate long term liquidity for mortgage lending. Such long term funds could possibly be raised in the financial market through L/Cy denominated Bonds/Sukuks.
* ***High Interest Rates***: The prevailing interest rates in the market for short term lending are around 13-15%, and mortgage lending for medium and long term is expected to be even more expensive and thus unaffordable for low-income clients.
* ***Property and life insurance coverage***: The state owned Insurance Corporation is not very active in providing property insurance. Life insurance coverage is also not widely available in Afghanistan. Additionally, it is expected that clients would mostly prefer the Islamic insurance mode (Takaful), which currently does not exist in Afghanistan.
* ***Dollarization of economy and FX Risk Management***: Banking business in Afghanistan is largely USD denominated. The banks will not be able to hedge FX risk on their own or pass the FX risk on to the clients. Therefore, banks hesitate about providing medium to long term mortgage lending until long term funds are available in Afs or some viable hedging mechanism is available.
* ***Specialized Housing Finance Institution***: The Mortgage and Construction Bank (MCB) established 1948, and later nationalized, used to finance residential and commercial construction in Afghanistan, including the purchase of land and construction materials. MCB also offered a savings product linked to housing loans, through which the customers who had savings accounts with MCB were given priority in the processing of mortgage loan applications. MCB’s performance began to decline due to political and civil strife during the Taliban regime, and in 1995 most of its records were burned down or destroyed during fighting. MCB was not relicensed in 2001-2002 because of its heavy losses and very poor performance.

DAB’S Deputy Governor stated that DAB is considering setting up a housing sector stakeholder consultative group to discuss different options regarding setting up a public-private partnership to catalyze housing finance for low and middle income groups.[[50]](#footnote-50).

# HOUSING MICROFINANCE

## Overview

Microfinance clients in Afghanistan have demonstrated a large demand for housing loans, often their financing need being covered by misallocating business micro-loans, borrowing from relatives and friends, labor sharing, and family savings.

Housing microfinance could provide an immediate solution to the existing housing shortage in Kabul and other main cities since MFIs cater to low income segments who often live in informal housing and/or have informal incomes. By introducing new financial products such as micro-mortgage or home improvement loans, MFIs would be able to better serve their target clients’ needs and also diversify their portfolios.

**Estimated Need for Housing Finance in Kabul’s Informal Sector**

**Home Improvement**

* Estimated 2.44 million people living in informal housing in Kabul
* Average household size is 7.5 people

**= About 325,333 informal homes**

* Assumes 50% of these informal houses need some improvement every year
* The average cost of house improvement is $750 per home,

**= Potential annual financing needs for home improvement - $122 million.**

**Housing Construction**

* World Bank estimates the construction cost of Kabul’s informal sector housing— about $2.5 billion
* Assuming there are 325,333 informal homes

**= Average cost of building an home - $7,684 per household**

* Assuming 20,000 new houses can be constructed annually
* At the average cost of $7,684 per unit

**= Financing needs for new construction - $154 million a year**

These estimates suggest a total **yearly financing need of $276 million** for home improvement and new construction in Kabul’s informal housing sector.

There are several encouraging housing microfinance initiatives in Afghanistan, including MISFA’s funding support to MFIs and NGOs for housing microfinance lending. The First Microfinance Bank of Afghanistan (FMFB-A) launched a rural housing microfinance product in 2011 and is currently preparing an independent evaluation of the pilot, which will inform its plans to scale the program.

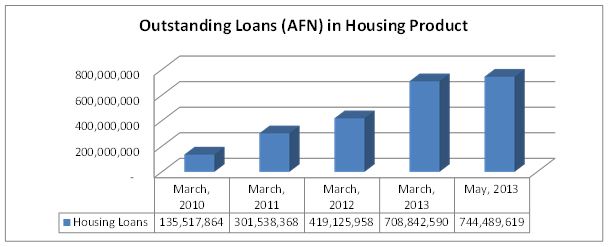
Microfinance institutions have few funding mechanisms at their disposal, including internally mobilized resources and capital from MISFA (discussed in Section-7.2 in detail). However, if housing finance activity expands to meet the growing demand, microfinance institutions would need commercial sources of longer-term funding that will enable them to make larger loans needed for construction and major renovations without causing asset-liability mismatches. Market-based funding sources should be encouraged to promote the commercial sustainability of microfinance institutions.

## Microfinance Investment Support Facility for Afghanistan (MISFA)

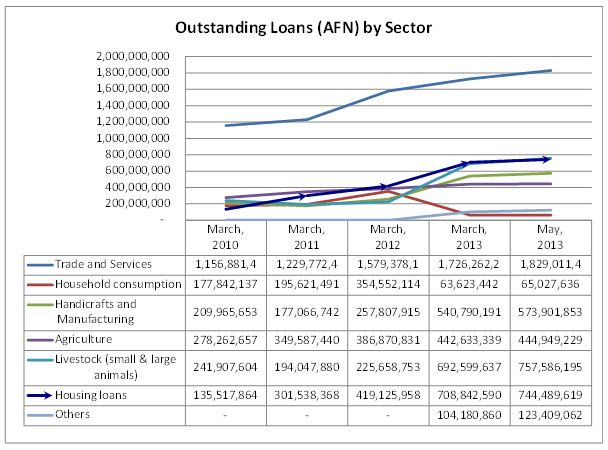
MISFA commenced its operations in 2003, with the primary objective to promote and support microfinance lending and entrepreneurship development in Afghanistan. In 2009-2010 MISFA decisively entered into housing microfinance business. Its outstanding housing portfolio was Afs 135 million as of March 2010, and by May 2013 it had reached Afs 745 million (see Figure No. 3 and Figure No. 4 below). Over the years MISFA focused on updating its policies and consolidating its operations to better manage its portfolio. MISFA, as the apex organization in charge of development and oversight of the microfinance sector, it is now facilitating the consolidation process of a few partner institutions. The Table-1 Below presents MISFA’s outreach data, which clearly shows that FMFB-A, largest MFI in Afghanistan, is also MISFA’s largest partner.

***Table 1. Outreach data of MISFA Partners***

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
| **Outreach data of MISFA Partners** | | | | | | |
| *As of April 2013* | | | | | | |
| **Outreach-Overall** | **ASA** | **FMFB-A** | **HFL** | **MUTAHID** | **OXUS** | **Total** |
| **Provinces** | 2 | 14 | 1 | 7 | 8 | 14 |
| **Districts** | - | 80 | - | 1 | 3 | 82 |
| **Active Clients** | 7,457 | 126,125 | 3,120 | 3,290 | 8,853 | 148,845 |
| **Active borrowers** | 5,007 | 62,586 | 3,120 | 3,290 | 8,853 | 82,856 |
| **No. of loans disbursed (cumulative)** | 31,798 | 309,310 | 24,651 | 8,316 | 76,169 | 450,244 |
| **Amount of loans disbursed $ (cumulative)** | 8,652,050 | 514,033,678 | 8,756,542 | 2,943,617 | 47,587,212 | 581,973,100 |
| **No. of loans outstanding** | 5,007 | 62,586 | 3,120 | 3,290 | 8,853 | 82,856 |
| **Gross Loans**  **outstanding $** | 804,648 | 81,588,311 | 1,023,981 | 1,116,910 | 8,709,324 | 93,243,173 |
| **Client voluntary savings** | - | 15,652,442 | - | - | - | 15,652,442 |
| **Client compulsory savings** | 89,740 | - | - | 31,263 | 630,617 | 751,619 |
| **Women clients** | 7,131 | 21,994 | 1,695 | 647 | 2,543 | 34,010 |
| **Women as % of Total Clients** | 95.6% | 17.4% | 54.3% | 19.7% | 28.7% | 22.8% |
| **Women borrowers** | 4.796 | 9.891 | 1,695 | 647 | 2,543 | 19,572 |
| **Total staff (incl. Loan Officers)** | 27 | 1,004 | 47 | 226 | 271 | 1,575 |

***Figure 3. MISFA Housing Finance (July 2013)***

***Figure 4. MISFA Housing Finance (July 2013)***



## Housing Finance Products

From discussions with financial institutions as well as their clients it is clear that a wide range of financial products are required to meet the needs of the diverse Afghan population. In the area of housing microfinance, FMFB-A has developed and launched rural housing microfinance product in 2011-12. To rapidly expand housing finance options it is necessary that financial institutions develop Sharia-compatible housing loans. Bank Al Falah, whose parent institution in UAE has extensive experience Sharia-compatible finance, considers that Murabaha and diminishing Musharka modes would be most appropriate for the Afghanistan market.

Commercial banks have been less active in providing housing finance, with a few attempts by Pashtany Bank and Mille Bank. Afghanistan International Bank’s CEO had stated that they also intend to launch a product under which housing loans up to $100,000 for a 3 years’ tenor would be provided. However they would wait until the post-2014 uncertainty clears out to make the final decisions[[51]](#footnote-51).

There is also a large opportunity to develop financial products that will link developers with the actual end-buyers, by approving loans in clients’ names with the mortgage installments being released to the developer on behalf of the client.

**First Micro-Finance Bank (FMFB)**

FMFB started its operations in 2004 under a commercial banking license, with a business focus on microfinance. With an equity capital of $6 million, it is 51% owned by Agha Khan Foundation, along with IFC, KFW and others. It started with economic empowerment of the poor through individuals and group lending microfinance loans, but its current portfolio also includes SME clients. FMFB’s individual loans include consumption loans, loans for trade finance, services, agriculture and housing finance. FMFB has a network of 45 branches, 17 of which are located in rural areas, covering 14 provinces. The number of individual depositors went up from 37,342 in 2009 to 57,841 in 2010. By 2010, FMFB disbursed $79.4 million in microfinance loans, of which $51.6 million were outstanding at the end of 2010. In addition to microfinance loans, since 2005 FMFB has been offering SME loans in 18 of its branches, based in 9 cities. At the end of 2010, the outstanding SME portfolio was $ 5.9 million to 466 active borrowers. These SME borrowers support over 11,000 full and part time jobs in Afghanistan. With support from the IFC, FMFB has developed a housing microfinance loan product, which is now available in both urban and rural areas. A detailed review of FMFB’s Home Improvement Product of is given in Annex-1. FMFB’s management of is quite optimist about the success of this product, it intends to expand its housing improvement loans and is leveraging the Housing Microfinance Toolkit.

## Women's Access to Finance through Home Ownership

Women’s ability to own property titles is important not only for sanctioning female home ownership, but also because it facilitates access to bank credit. A recent IFC GEM Report[[52]](#footnote-52) showed that women's access to formal finance in Afghanistan is constrained because women more often than men lacked guarantees and title deeds. Even institutions like FMFB-A 's, who are proactively focusing on diversifying their product offerings to expand access to finance to women entrepreneurs, are facing major challenges. FMFB-A currently offers individual micro and SME loans secured by title deeds and other guarantees. However, women find it difficult to access such loans since in the Afghanistan context women rarely possess title deeds or have easy access to guarantees. As an example, FMFB-A’s loans to women currently stand at approximately 19% of its total loan portfolio. FMFB-A intends to address women entrepreneur's lack of access to formal credit by introducing joint liability group lending and by increasing outreach to women entrepreneurs.

## Informal Finance

Afghan businessmen and homeowners rely almost entirely on friends, relatives, and moneylenders to meet their financing needs. Informal financing still plays an important part in manufacturing and commercial activities, but such funds are often costly and therefore inappropriate for long-term private sector or housing development.

The factors behind the prevalence of informal finance:

* Less than 5% of Afghans have access to banking services, and most of the banking is concentrated in Kabul and a few other larger cities.
* Bank’s lack of interest reaching the low-income clients
* Ease of securing finance from informal channels
* Absence of bankable titles
* Strong preference for Islamic banking through Sharia-compatible financial product

**Other housing finance options**

Due to a fragmented society and long-term conflict Afghanistan has developed efficient informal financial services, generally grouped under the label Hawala. The Hawala system consists of an underground financing network based on ancient methods of paperless transactions. Its roots can be traced back to a financial practice known as Fei Quan, or "flying money," used by the Chinese along the Old Silk Route. In modern times, based on the Arabic banking terminology, the Hawala system refers to money transfer or wire. With the development of the formal financial system, Afghan banks and MFIs are now better able to compete with the efficiency and speed of the Hawala system in price and quality of services. The Hawala system has also been liked to major laundering of drug money in Afghanistan, thus supporting the continued influence of drug lords and terrorist activities. Beginning in September of 2004 there has been a concerted effort by DAB, funded by donors, to better regulate the informal financial sector to induce Hawaladars to standardize and report their activities. Extensive resources of the Government of Afghanistan and donors have helped to pass the Anti-Money Laundering and the Combating Terrorist Financing laws, and a monitoring unit has been installed within DAB to support both laws.

Hawaladars have mainly been involved in the transfer and exchange of money, and rarely in the lending or deposit taking activities, although during the Taliban era, when there were no operational banks, to some extent they took on additional services.

Low income Afghans, who look for credit outside of the formal financial system, generally short-term consumption loans, overwhelmingly appeal to relatives. To a lesser extent they request loans from local money lenders. It is estimated that less than 10% of credit in urban areas is obtained from money lenders[[53]](#footnote-53) Clients of MFIs have pointed out that money lenders are avoided because of the high interest rates charged, and fear of potential repercussions in case of delinquencies caused by these high rates.

# LAND OWNERSHIP, REGISTRATION AND TITLING

## Land registration and transfer

Lack of an appropriate legal and regulatory regime has prevented commercial banks and, to a lesser extent, microfinance institutions from entering into the housing finance market. Inadequate enforcement of laws and structural weaknesses in the housing market has made housing finance an overly risky proposition. Among the reasons for staying out of the housing market cited by commercial banks are the inability to establish clear titles to property, high cost of registering liens, and the absence of secured transaction or foreclosure laws.

Simple, affordable procedures for property transfer and registration would encourage people to use formal registration and thus help prevent further fragmentation of the land holding. The government is committed to lowering the cost of land registration, which includes stamp duty and legal and other charges, from 10% of the property value to 2%.

The Afghan Supreme Court recently took some steps to encourage people in using the formal land titling regime. The steps involved in the titling process have been reduced from more than 30 to just four, reducing the time, costs and opportunities for corruption formerly prevalent in this process. However, each step is still time consuming and expensive. As a result, many people continue to avoid formal registration in favor of traditional means of declaring ownership. The procedure now involves the following steps:

* Register with the provincial land title office (Makhzan)
* Register with the Municipality
* Pay taxes at tax office (Mustofiat)
* If not completed previously, must complete cadastral process (the act of surveying the boundaries of the property) at cadaster office
* Register new title in primary court

## Titles

Without clear land titles financial institutions are unwilling to provide the financing needed by developers and home buyers. Establishing clear titles to land in Afghanistan is complicated by the several regulations:

* Customary Law (Urfi or Rawaj)
* Religious Law (Shar’ia)
* Civil Law (Qanoon Madani)
* Statutory or National State Law( Qanun-e Asasi)

A brief description of these titles, as explained by Liz Alden Wily[[54]](#footnote-54), is presented below:

***Customary Law (Urfi or Rawaj***): Traditionally in Afghanistan land ownership was guaranteed through community based means, with elders endorsing the rights of a family. Sometimes written documents may be made to record the transfers and transactions, and were to be witnessed by the elders and state appointed headmen (Maliks) or Mullahs (religious leaders). Customary Law therefore depends upon community made norms that may change over time. Its application also depends upon mediation and arbitration to reach consensus. In the process the practices and rules may alter.

***Religious Law (Shar’ia):*** Interpretation under different sects is not as divergent on property matters as it is in some other aspects. Protection of property is a major objective of the Islamic Law and its jurisprudence is comprehensive on this matter. Transfer of ownership under inheritance is also quite comprehensive and binding.

***Civil Law (Qanoon Madani)***: An attempt to bring Sharia into formal title regime was made through Civil Code compiled in the 1970’s. The Code comprises of 2,416 articles, 1,000 of which are directives relevant to land and property such as Inheritance (Matruka), Mortgage (Rahn), Leasing (Ijara), and Rental (Keraya, Sarofi).

***Statutory or National State Law (Qanun-e Asasi):*** The national land law was besides the constitutional law (Qanun-e Asasi). Prior to this more than 70 Laws, Edicts (Layehe) and Decrees (Muqarrarat) existed on the subject, along with Orders (Farman) and administrative decisions. The main subjects covered under Qanune-e Asasi are: land classification for tax purposes, land entitlement, compulsory acquisition of land, pasture management, distribution of public land by the State, management of Government and public properties in urban areas under Master Plans etc.

Shar’ia is largely enshrined in the Civil Law, but it often differs from Customary Law. And both are applicable where state law does not apply. In addition, frequent regime change has led to more than 60 different land laws and amendments to the State Law. As a result, property may be legally held in several different ways, some of which may not involve a formal registration with the municipality. Instead, ownership is legitimized through a customary document certified by the local Shura or Jirga.

The already difficult land titling process has been further complicated during the past quarter century of conflict, as land was appropriated by several stakeholder groups in turn, and frequently legitimized by the relevant institutions at the time of transfer. In addition, squatters moved onto land, government or private, and built homes while the real owners were abroad during the period of conflict. This complex situation makes for a significant amount of land disputes, which need to be mitigated through stronger land tenure systems.

## Initiatives on land management and administration

With drafting of the new Constitution in 2004, Afghanistan saw a new stage in governance in the country, including land rights and administration. By late 2004 a handful of projects were underway. These included: the USAID funded 204-2009 Land Titling and Registration Project (LTERA), followed by the 2009-2013 Land Reforms in Afghanistan (LARA).

***LEITRA Program***: Land Administration in Afghanistan: Rehabilitating Land Records: Afghanistan's land administration infrastructure was nearly destroyed during two decades of war. Its land records including property deeds and transfer deeds were eaten by mice, burned or destroyed completely. In late 2004, the USAID/LTERA project began refurbishing more than half of the provincial registration courts (Makhzans) in the country.

The USAID/LTERA Project launched two pilot projects in Districts no. 7 and 13 of Kabul City with the aim to develop and test methodologies to improve tenure security of residents in informal settlements.

The project used three guiding principles:

1. The communities have the means to solve most land problems themselves. Since the community elders are knowledgeable about residents' property and are generally able to back ownership claims, they resolve disputes and weed out fraudulent documents.

2. Solutions must be integrated into the formal legal and land planning systems.

3. There must be a partnership between authorities, communities and donors to accomplish the process.

As Dec 2009, the reorganization teams have cleaned, restored and reorganized 5.4 million legal documents, including 500,000 title deeds[[55]](#footnote-55).

The National Land Policy was principally drafted by the USAID funded LTERA project. Ministers of Urban Development, Agriculture and Irrigation, and Justice approved the policy in 2007. However, later on, with changes in the Ministers, the new Ministers did not take the ownership. By 2009, knowledge of the policy faded, and development of a new urban land policy also came to a halt. Consequently, once the Chief Facilitator of the USAID-Funded left the country, the LTERA project got practically shelved[[56]](#footnote-56).

***Land Reforms in Afghanistan Program (LARA***): The Land Management Law is the most important land law in Afghanistan. It has origins in 1960s law and has been amended many times since then, most recently in 2008. In 2011 the new Afghanistan Land Authority (ALA or ARAZI) decided to review the Land Management Law. This was at the urging of the USAID-funded LARA Program. The Land Reform in Afghanistan (LARA) project is working with the appropriate Afghan authorities to implement an IT solution for improving the inventory management of cadastral information. The main objective of the Cadastral Data Management System (CDMS) solution is to provide an electronic repository of land and property information in a database management system for Afghanistan.

***Cadaster:*** Technology that would allow the mapping to be done properly is now available in Afghanistan. The Afghan Geodesy and Cartography Head Office have begun digitizing existing cadastral maps of about 800,000 properties. Producing accurate maps will be a key to establishing an accurate titling system in the country.

**Titling Registration:** Lack of confidence in property titles is a major hurdle in developing housing finance in Afghanistan. Ownership security may be less critical for microfinance institutions, which are less likely to require title for a mortgage guarantee as they use alternative forms of collateral. However, a secure title is a minimum requirement for commercial banks and other market participants for doing housing finance business.

Two types of titles are generally used in secondary market transactions. These are:

* ***Qabala Sharae***: It is an acknowledged legal document. The Sale/Purchase Agreement is registered with the Court. The court process involves thorough scrutiny of the document, by the court and by the Municipality records, whereas applicable fees are paid, and at the completion of the process the Court issues a legal title as an evidence of “Ownership”.
* ***Qabala Urfi***: In this case the sale/purchase agreement is witnessed by the community elders/representatives, based on common knowledge of real ownership. It is not registered in the court/municipal records, and therefore is not recognized as a legal document by the Court and the banks/mortgage lenders.

In Kabul, less than 20% housing is “formal”, and remaining 80% is “informal.” The “informal” housing includes those built on “own land” which generally have Qabalae Urfi titles. Those built on “illegally occupied land” and on “public lands” have no titles whatsoever. The formal housing is considered to be having legal (Qabalae Sharae) titles, and remaining 80% have either no title or non-bankable titles.

In Kabul for lien registration, the banks pass on the property documents to the courts, which after completing its verification process (at 6% fee) pass on the property documents to the Kabul Municipality (at 1% fee), which would then verify the titles as per its record and enter into its register. However there is no coherent land registration law. In addition to several traditional means of property transfer, conflicting registry schemes have been put into place over the decades. And corruption and forgeries often lead to several competing claims to the same piece of property.

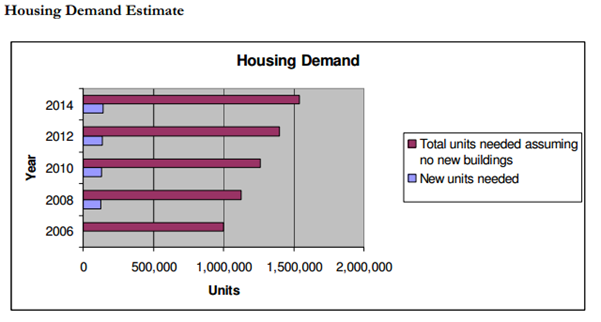
# DEMAND PROJECTIONS, INCOME AND AFFORDABILITY

## Demand projection

The World Bank reports that Kabul has grown 15% per year between 1999 and 2002, and that growth will remain about 5% per year due to migration and "natural" growth.[[57]](#footnote-57) In addition, as the situation stabilizes, more refugees will return from Pakistan. In Kabul and Jalalabad, approximately 60% of the households surveyed in an AREU working paper[[58]](#footnote-58) have built their own homes, with the rest living on rent (20%) or staying for free on charity (20%). According to World Bank estimates, only 0.5% of Kabul's population can be considered homeless, including 10,000 living in tents and 5,000 living in destroyed buildings[[59]](#footnote-59).

Several studies show that low income segments have been able to construct their own houses after migrating to the cities (UNICEF estimates that around 80% of the new houses constructed in Kabul in the 1990s have been self-built[[60]](#footnote-60)). However, this population is still faced with poor housing quality, as well as housing insecurity, since they are essentially squatters with no land rights. An AREU case study notes that insecure titles "may discourage households from improving their housing, as it appears irrational to invest under such conditions, where final ownership is not established. However, it also has been observed during the study that investments in housing improvement serve as an explicit strategy to secure tenure."[[61]](#footnote-61) The housing situation in Kabul and Jalalabad can be extrapolated to other major cities in Afghanistan, since all have experienced a significant growth in their population during the last decade.

The overall housing shortage in Afghanistan is estimated at 1.5 million units, which does not include the need for housing upgrades. The incremental yearly demand due to population growth is estimated at 200,000-230,000 units. Conversely there are few units being built to meet this demand, with most homes being self-built. The following figure shows the demand for houses at the estimated growth rate.

**FIGURE - 5**

Satellite images from 2004 indicated that nearly two-thirds of houses constructed since 2004 in Afghanistan were informal dwellings, generally built on government land. These figures are expected to be representative of today's situation as well. To address this dire situation A very large investment is needed at all levels, according to the Ministry of Urban Development, which would cover incentives to developer, alongside developing housing finance institutional framework, and strengthening regulatory framework.

## Assessing income levels

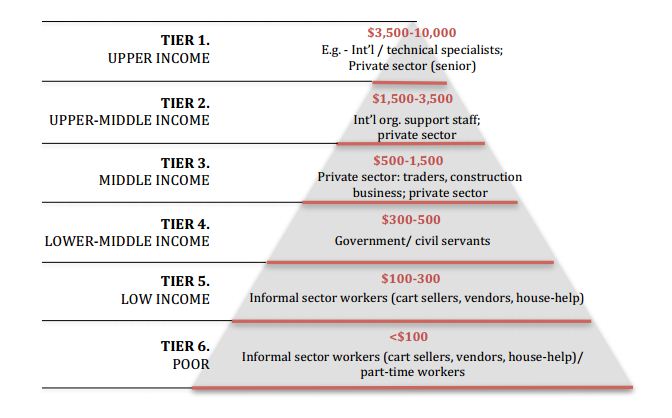
Monthly household income distribution according to the Kabul City Initiative survey:

***Table 2. Income distribution***

|  |  |  |  |
| --- | --- | --- | --- |
| **Income Range** | **All %** | **Rural %** | **Urban %** |
| Less than $100 | 46 | 51 | 26 |
| $101-$200 | 28 | 27 | 30 |
| $201-$300 | 13 | 12 | 10 |
| $301-$400 | 7 | 5 | 13 |
| $400-$500 | 2 | 1 | 5 |
| $600-$800 | 1 | 1 | 4 |
| More than $800 | 1 | \* | 2 |

The income Pyramid, presented in World Bank housing Study on Kabul (Ref: World Bank Study by Asana Mathema) presents Income Grouping from “poor” households earning less than $100 per month at the bottom of the pyramid to upper income household earning between $3,500 and $10,000 per month at the top of the pyramid. Those earning more than $10,000 per month; constitute a relatively small percentage of the population, and are not generally an under-served or un-served segment of the housing market. Tier 2, 3 and 4 in the pyramid represent upper-middle income ($1,500-3,500 per month), middle income ($500-1,500 per month), and lower-middle income ($300-500 per month) households.

**FIGURE - 6. Purposive Income Pyramid – Household Income per month**

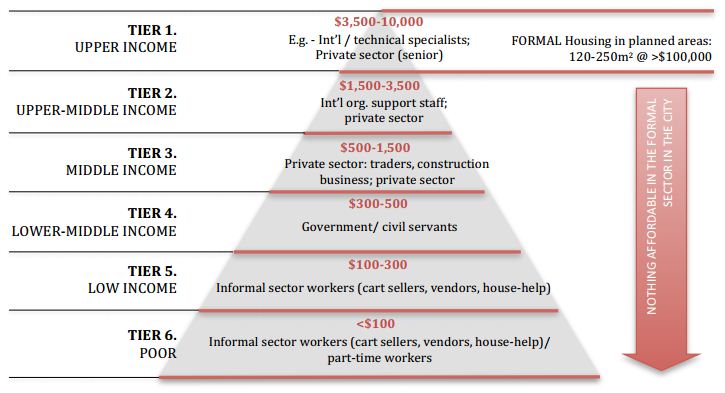


## Assessing housing costs

The unstable security and economic situation in Kabul is contributing to the extreme price volatility in the real estate market and in the housing sector. House prices have reportedly tripled in the past 3 years: for example, a 2-bedroom unit which could be purchased for $30,000 in 2008 is now priced at $100,000[[62]](#footnote-62).

As revealed during Team’s recent visit to Kabul in June, 2013, the prices of the new developments are anywhere from $150,000-250,000 for apartment buildings to around 1 million USD and above for villas. That means that, the formal housing sector is currently only catering to the top end of the market demand, i.e., households earning more than $3,500 per month. There is a little, if anything, affordable in the Kabul city market for households in the middle or lower income segments, i.e., Income Tiers 2,3,4,5, and 6. The scale of unplanned settlements in Kabul is indicative of how few households earn $3,500 or more a month.

**FIGURE - 7**. Unaffordability of the ‘Formal’ Housing Sector



## Home Owners’ Insurance

The banks in Afghanistan, based on the interviews held during the teams visit to Kabul in June, 2013, are reluctant to offer large loans without insurance of collateral. For mortgage finance, the client is also required to secure life insurance. There are only two insurance companies in Afghanistan, and no one currently offers homeowners property insurance. Although the country’s insurance law was revised in January 2006, only one private insurance company, namely The Insurance Corporation of Afghanistan (AIC), has started doing business. Meanwhile, the public sector Afghan National Insurance Company is barely functional. It is also substantially undercapitalized. Until more private insurance companies establish operations and begin providing homeowners insurance in Afghanistan, the risk of lending to homeowners may remain too high for banks. In case of mortgage lending, the banks essentially need both property insurance and borrower life insurance.

Currently there is no life insurance coverage available in Afghanistan, and it would be essentially needed by the Banks/FIs to promote consumer and housing finance. Insurance coverage would be acceptable to the clients if it is sharia-compatible i.e., Takaful Insurance. Since most of the potential clientele are strong faith followers, an Islamic Life Insurance facility (Life or Family Takaful) will be needed alongside Property Takaful. Since insurance sector is controlled by the Ministry of Finance, any steps in that direction will have to be initiated by the Ministry[[63]](#footnote-63).

The CEO of the Afghan Chamber, Mr. Haqjo also observed that insurance has great potential once banks’ financing shift towards long term assets, industry and mortgage financing. There are indications to the Chamber that an Association of Insurance Companies is in the pipeline. He further expressed his preference for privately-run insurance companies. In view of strong faith of Afghan people, Mr. Haqjo also stressed on the need for Islamic Insurance system (Takaful) in Afghanistan.[[64]](#footnote-64)

# REVIEW OF FINDINGS AND WAY FORWARD

1. ***Regulatory Regimes*- Finance (Demand) Side Regulations:** DAB’s housing finance regulatory function is currently very weak. In the absence of a proper housing regulatory function at DAB, most initiatives attempted were liked to individual staff, and any progress ended when these individuals left DAB. Most of DAB’s staff also has limited prior knowledge or experience in housing finance. The Governor of DAB has now appointed a professional with mortgage industry experience who will lead the process of setting up a specific function to regulate and supervise housing finance in the financial sector. To establish an efficient regulatory regime DAB ,needs to develop the following:

* Mortgage-specific Prudential Regulations
* Mortgage Guidelines
* Housing Finance Data gathering and analysis
* Regular interaction with Banks Association on issues related to housing finance
* Credit information system and Credit Bureau
* Regulatory regime for housing microfinance by MFIs

***Way Forward***:

* DAB should move forward in its plans to set up its specialized Housing Finance function and equip it with the experienced staff.
* Seek Technical Assistance for developing the above-mentioned mortgage specific regulations
* Arrange regular meetings with Afghanistan Association of Banks(,proceedings should be documented and follow-up ensured)

1. ***Promoting Housing Finance*:**

* ***Setting up a specialized Housing Finance Institution or Housing Liquidity Facility:*** In the past, there were several unsuccessful proposals to establish a specialized financial institution (by reopening an earlier institution or converting an existing one). Based on the discussions held with different stakeholders, more so the officials of DAB, MoUD, Ministry of Economy and the Afghanistan Chamber, it appears to have more support now.

***Way Forward***: Pursuing a public sponsored housing finance institution will require significant planning, management and resources from government and donor stakeholders. Additionally, it should be noted that state-run mortgage finance programs and institutions have had mixed results in other emerging markets. The team recommends first supporting the private sector initiatives and creating the enabling environment for private sector mortgage market to thrive. A government sponsored guarantee program or liquidity facility may be the best use of scare government subsidies.

* ***Need for a specialized Housing Microfinance Institution***: Since there is a large informal housing sector in Kabul and other cities, a specialized housing microfinance liquidity facility, possibly managed by MISFA, is desired in Afghanistan.

***Way Forward***: DAB may start exploring this in consultation with MISFA, and the lead market players like FMFB-A.

* ***Promoting the role of Commercial Banks in Mortgage Finance***: Out of 16 commercial banks in Afghanistan, only seven have taken some timid initiatives in the area of housing finance. The banks are hesitant for various reasons as discussed in the report. The team is of the opinion that banks’ concerns could be addressed by joint private and public initiatives once the banks feel that they have a role to play in promoting housing finance.

***Way Forward***: Those solutions could be explored in regular meetings of ABA and DAB, as suggested in Section-A above. It is expected that banks will start their mortgage finance operations by focusing on mid and higher-income segments. The banks in partnership with public programs could develop certain programs that will expand the use of housing finance. For example financial institutions could be encouraged to develop mortgage finance schemes for the civil servants, teachers etc. These salary-backed loans would be less risky for banks as the public servants clients have less challenges presenting clear titles and the assessment of their income assessment is easier because of salary formal records. Another program that financial institutions could consider is providing mortgages to the high income clients buying apartments (who don’t have issue with titles and valuation) by linking mortgage finance with developers.

* ***Long Term Liquidity***: For a sustainable and viable medium to long term housing finance, the Financial Institutions need more access to long term funding, ideally in local currency and in Sharia-compatible modes. Currently, neither the commercial banks nor their clients could bear the currency risk in term loans. Currently there is no long term yield curve in the local financial market, nor any rating mechanism to rate financial instruments like Bonds/Sukuks. As announced by the Governor DAB, Mr. Noorullah Delawri, DAB is considering to float Islamic Bills, as it prepares for an expected drop in the inflow of foreign aid in post-2014 scenario. The offering of longer-maturity Sukuk will possibly take place by end of 2013. That will enhance the market confidence in Government long term paper (Bloomberg Business Week, June 11, 2012).

***Way Forward***: DAB needs to start consultations with Afghanistan Banks Association for generating long term liquidity denominated in local currency through market based instruments such as Sukuk. Bankers are expected to favorable respond to such an initiative, particularly if it is implemented in tandem with more supportive regulations in terms of Risk Weightage, SLR eligibility, Sharia-Compatibility etc.

* ***Sharia-compatible Housing Finance***: Banks are expected to work on developing Sharia-compatible housing finance products based on the new Islamic Banking Law (Annex-2). Some banks like Bank Millie and Bank Al Falah, already have technical alliances with institutions experienced in Sharia-Compatible lending, which can facilitate their quick development of appropriate housing finance policies and products. These banks are well positioned to take the lead in launching Sharia-compatible housing finance products in Afghanistan. .

***Way Forward***: DAB may encourage certain commercial banks to take the lead in developing Sharia-compatible housing finance products, and serve as role model for the financial sector. DAB will need to establish additional regulations specific to Sharia-compatible housing finance.

* ***Insurance coverage of property and life on clients***: Stakeholders interviewed are cognizant that promoting housing finance in Afghanistan also should include strengthening the Afghanistan insurance sector to increase the availability of property and life insurance. Ministry of Finance, the regulator for the insurance sector, should develop some initiatives to promote Sharia-compatible modes for insurance coverage (Takaful).

***Way Forward***: DAB should coordinate with the Ministry of Finance on the steps needed to strengthen the insurance sector and in setting up Takaful Insurance in Afghanistan.

* ***Risk Management***: Commercial banks are concerned about the credit risk associated with appraising mortgage applications, and their limited risk management capabilities.

***Way Forward***: DAB’s Mortgage Guidelines should be complemented with capacity building programs and trainings for commercial banks. These programs could be implemented with the support of the Afghanistan Banks Association to gradually improve risk management capacity of primary mortgage lenders.

* **Credit Bureau:** DAB is in the process of setting up a Credit Bureau to address the lack of borrower credit history information. Since currently less than 5% of the population is formally banked, and that mortgage loans are generally perceived by banks as more secure(lower LTVs, better income assessment, high repayment rates related to effective foreclosures etc.), a credit bureau will not produce significant short-term benefits to promoting housing finance in Afghanistan.
* **Property Valuation:** Afghanistan needs a certification program on property valuation and significant capacity building. Until the property valuation processes improve, banks could continue lending at lower LTVs which largely addresses the issue of valuation.
* **Income assessment:** To address the challenges in assessing borrowers’ income MFIs like FMFB-A focus on formally employed segments, like teachers and civil servants, and use salary backed repayments in structuring their loans. Financial institutions should also ensure they are conducting exhaustive on-sight assessment of income and consider assessing family income for housing loans instead of individual income.
* **Title Search:** Currently this function performed by the Real Estate Brokers with staff who has no prior training on the subject. Since there are few people in Afghanistan trained in how to properly conduct title searches, a certification program and relevant trainings will enhance capacity in this area.

1. ***Way to make humble beginning in mortgage finance***: Since there is already a sizeable supply of housing for high income segment in major cities like Kabul, which does have commonly cited issues like title, valuation, bankable clients etc. a humble beginning could be made by the banks in providing medium term mortgage loans. Also, if the Government plans to develop housing schemers for teachers, civil servants etc. that will also create opportunity for salary backed mortgage loans to middle-income segments. If the Government could create

***Mortgage Guarantee Fund*** for middle and lower income segment will further give a boost to establishing mortgage business in Afghanistan**.**

1. ***Improve accessibility for women***: Women generally encounter significant difficulties in accessing titles to property and often must rely on male relatives to hold title for them. Only a very small percentage of urban women hold land titles, mainly through inheritance, but in rural regions it is almost unheard of.
2. ***Improve Security of Mortgage*:**

* ***Land Title***: Title security issues are most relevant to individuals whose houses are built on private land, or those who have built their dwellings on land illegally occupied during three decades of civil war. The individual housing being built on Qabalae-Sharae titles and the housing schemes developed on Government land have secured bankable titles. Based on the principles of deciding titles’ validity under LTERA Project, most of Urfi Titles could also be given bankable authenticity.
* ***Cadaster***: The lack of clear boundaries has led to many, sometimes fatal, land disputes. The years of conflict have hampered the implementation of modern mapping techniques, which could have resolved these disputes. Few properties have been properly surveyed and most customary deeds offer only vaguely defined boundaries. These are often described as abutting someone else's land which itself is not surveyed. Technology is available that would allow the mapping to be done properly. The Afghan Geodesy and Cartography Head Office (AGCHO), has already begun digitizing existing cadastral maps, but these are only a small portion of the property in the country, estimated at 800,000 properties. Producing accurate maps will be a necessary cornerstone to an accurate titling system in the country.
* ***Title transfer and registry***: Government’s policies for reducing the steps needed for property transfer/registration and their appropriate fees, reduction are expected to give more confidence to the mortgage business. However, real efficiency will come with gradual computerization and digitization of land titles, their registration and transfer. There is an urgent need to scale up the business model developed under the LTERA Project and the computer aided models piloted under the LARA Project.
* ***Foreclosure efficiency and effectiveness***: There is a need to standardize mortgage contracts to conform with the relevant provisions of the Mortgage Law, so that in case of default the compliance is strictly defined by the relevant provisions in the Mortgage Law. The Sharia issue based on which a person who defaults on its mortgage cannot be evicted if he does not have another place to live needs to be properly addressed. Sharia scholars may be approached to ensure sanctity of a Contract per Sharia rules should take precedence.

***Way Forward***: A task force with representatives from the Ministry of Justice, the Judiciary, DAB and Afghanistan Banks Association should be set up to review this issue and give its recommendations to the Ministry of Justice.

1. ***Regulatory environment*:**

* A regulatory framework for developers should be set up, perhaps in the form of a Real Estate Regulatory Authority which would provide a mechanism for supervision and monitoring of developers’ compliance with building codes.

1. ***Promoting Housing Supply*:**

* ***Developer Finance Rules***: DAB should develop additional policies that differentiate between the financing limits imposed to the commercial banks’ lending for the construction sector and for mortgage loans.
* ***Land Banking and supply of serviced Land by the State***: In Kabul and other major cities, the Government is an important owner of land, which is currently being gradually illegally occupied by informal settlements and criminal groups. The Government should prioritize taking effective control of all such lands and placing it under an independentant entity having stock of raw and serviced land parcels ( generally termed as Land Bank). The Land Bank may then transform the “raw land” into “serviced land” and make such land parcels available for development of affordable housing schemes for low income groups under a Private-Public Partnership.
* ***Low-Cost Construction Technology and Materials***: The developers in Afghanistan lack knowledge and experience in globally acknowledged low-cost construction technologies.
* ***Housing Schemes for Public Sector Employees:*** There are many discussions among Government officials about setting up different housing schemes for teachers, civil servants and other public employees. .So far these schemes have not translated into actual programs but there seems to be sufficient support from both government institutions and commercial banks to roll out such programs. The banks seem willing to provide housing loans as part of such schemes, since these clients will have less challenges presenting clear titles, their incomes are easily verifiable and the loan repayment can be linked to salaries.

1. ***Housing Microfinance***:

* ***Specialized liquidity facility for Housing Microfinance***: DAB may initiate dialogue with the Ministry of Finance, MISFA, donor agencies etc. to explore prospects of such facility, with possible Technical Assistance from World Bank/IFC and other multi-lateral agencies
* ***Expanding Outreach and Financial Inclusion***: Afghanistan is a severely under banked country, where only about 5% of the population has formal bank accounts. In Kabul the situation is better but low income segments are still very poorly served by formal financial institutions and banks in particular. Some financial inclusion efforts have been attributed to MFIs but DAB should continue the dialogue with the Association of Banks to further promote financial inclusion. If needed, financial inclusion may also be expanded by DAB through regulatory measures.
* ***Informal Housing and Hill Housing***: The Mayor of Kabul indicated that Kabul Municipality is working on several initiatives to address the challenges in the Informal Hill Housing., such as bringing the settlements under a tax net, since they are considered as burdening the social, physical and economic infrastructure of the city, without making any contribution towards its infrastructure. The Government of Afghanistan has announced its policy on “Upgrading Informal Settlements-July 2013” (Annex-5). Once a degree of formality is achieved, MFIs may also consider housing finance products for home improvement and new construction.

1. ***Capacity Building***:

* Understanding of Mortgage law
* Mortgage Guidelines
* Property Valuation
* Title Search

***Way Forward***: The specific function/department on housing to be set up at DAB will also need to conduct Capacity Building Programs in the areas indicated above, with possible Technical Assistance from multilateral agencies like World Bank/IFC.

1. ***Development of Rental Housing:*** There is surge of interest among the wealthy Afghans in real estate development, particularly commercial real estate which is mushrooming in Kabul. If an adequate regulatory environment was set up in Afghanistan, developers may shift towards building of rentable residential units. .Further analysis should be completed on the potential for developing residential real estate as rentable properties. The Government may consider adopting several regulations that would promote this practice such as tenancy laws like Condominium Act in the West, efficient eviction of rent defaulters, and binding lease contracts.

***Way Forward:*** The Ministry of Urban Development (MoUD) and DAB could explore this further through a possible technical assistance from World Bank/IFC.

1. ***Housing Consultative Group***:

DAB’S Deputy Governor stated that DAB is considering setting up a housing sector stakeholder consultative group to discuss different options regarding setting up a public-private partnership to catalyze housing finance for low and middle income groups.[[65]](#footnote-65).

1. There is a need to coordinate the efforts of the large number of governmental entities, financial institutions and other market participants interested in developing an effective housing finance system in Afghanistan. Nearly all the stakeholders interviewed during Team’s visit to Kabul on June22-27, 2013, expressed the need for setting up a housing sector stakeholder Consultative Group, where DAB and representatives of different ministries, Afghanistan Builders Association, Afghanistan Banks Association, Afghanistan Chamber of Commerce etc., could meet regularly.

The Consultative Group would allow all interested parties to develop a shared agenda, as well as an agreed-upon schedule by which each institution or group would complete particular actions, such as the enactment of statutes, the creation of new governmental organizations, the issuance of needed regulations, the development and roll-out of mortgage products by financial institutions, and the training and certification of other parties. Such a mechanism would permit all the parties to understand how the actions of each body affect the other institutions, and thus the ultimate success of housing lending. The suggestive TORs for the Group are given at Annex‑4.

***Way Forward***: DAB’s Advisor on Housing, Mr. Asad Zafari was present in all these meetings and aware of all the discussions pertaining to this recommendation. Therefore DAB may initiate steps for implementing this recommendation.

# ANNEXES

## Annex-1: FMFB-A OPERATIONS Review

Housing loan initiative aims to scale-up and expand First Microfinance Bank-Afghanistan's (FMFB-A 's) urban housing micro finance portfolio while developing, piloting and rolling our housing micro finance products for rural areas. The program, which has received technical support from USAID, IFC and Aga Khan Foundation (AKF) - USA, also seeks to significantly improve the quality of housing by offering construction appraisal and advisory services.

At present, housing loan products are offered across FMFB-A’s branch network. The Bank disbursed 1,857 loans equaling $3,129,195 in the last quarter of 2012 of which 63 loans were to rural borrowers. Kabul has the highest average loan disbursement of $1,822 for urban while Mazar-e-Sharif for rural equaling $968 in 2012.

The pilot of the rural housing product also concluded in the last quarter of2012 with branches being able to achieve 99% of the targeted 200 loans. A pilot review is planned for 2013 to understand branch experience and various challenges linked to seasonality, client feedback and market expansion. An automated seasonal repayment module has been developed and is currently being tested; seasonal repayments emerged strongly as a key need for rural clients given the seasonality of their income. It is expected that this module will be installed across FMFB-A by mid-2013.

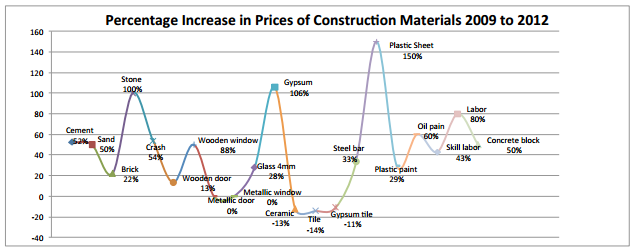
During Q4-2012, an analysis was conducted to understand the cost increase for various housing improvement activities since 2009. It was observed, that the labor cost has increased by almost 70%, with up to 80% on key supplies and material.

With the technical assistance grant through USAID & AKF concluding in July 2013, FMFB-A plans to initiate an evaluation to understand the performance and challenges linked to the housing product.

From the sector perspective, FMFB-A continues to maintain its dominant position, while other micro finance institutions face challenges. At present, FMFB-A is the market leader with a total outstanding portfolio of$80 million and an active client base of more than 60,000. FMFB-A is the only financial institution in the country that offers a housing improvement product, which constitutes about 17% of its micro finance portfolio (by value). As of December 2013, FMFB-A has disbursed 18,857 housing loans amounting to over $33.6 million.

The housing project of FMFB-A has received international recognition and the Bank is providing consultancy to an IFC local partner in Egypt to develop a housing improvement product.

Since 2009, the cost of construction has seen a continuous increase with major expenses linked to raw materials and labor. With very little manufacturing capacity in Afghanistan, majority of material such as steel, sanitary fixtures and others are imported from Pakistan, Iran, Russia and China and are thus costly. Clients often select sub-standard material because of cost and limited awareness or appreciation of the safety benefits of higher quality materials, which makes community mobilization on safer construction practices even more critical and difficult to achieve. Rising construction costs coupled with the lack of qualified technical officers makes the challenges of community mobilization and awareness raising even more difficult for the Bank.



**The Number Story**

*Highlights*

10,899 active housing loan clients with a portfolio outstanding of $12,456, 160 Percentage of women borrowers was at 19%

PAR more than 30-days is 0.87%

Average loan size in urban areas: $ 1,801

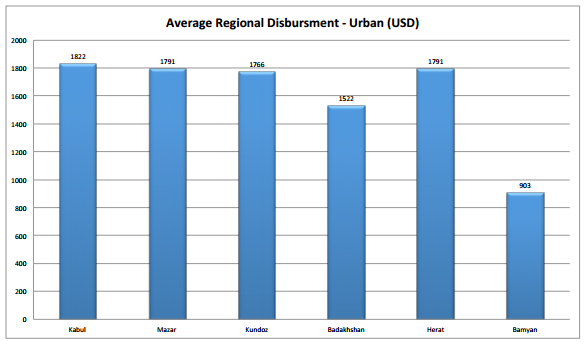
Average loan size in rural areas: $ 801

**Outreach & Performance:**

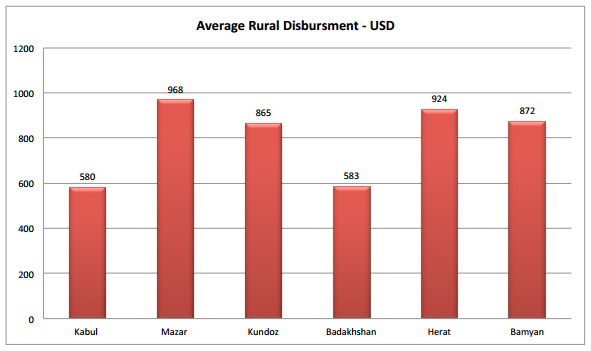
Active housing portfolio as of 31st December 2012 was 10,899 compared to 10,375 in September valuing $12,247,640. PAR over 30 days is 0.87%. Of the total disbursement, almost 2% represents rural clients.

Women in Afghanistan have limited ownership of property, which is generally channeled through inheritance. For the quarter, 19% of the total outstanding portfolio comprises of female borrowers, 2,093. Overall, 300 new loans were disbursed to female clients during the quarter, 5% of which being for females.

The average loan amount for Kabul remains higher compared to other regions, followed by Mazar and Heart.

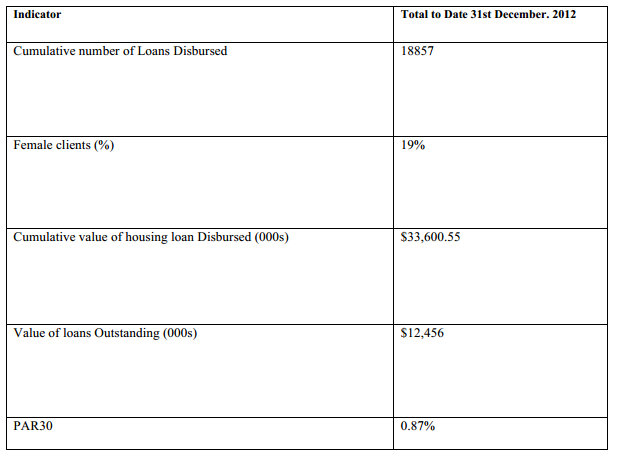


The comparison between urban and rural also reflects clients demand and cost of construction in two different markets within the same region.



**Table of Indicators**

The table below shows achievements to date of Housing Loan Initiative.



## Annex-2: Islamic Banking Law

**CHAPTER VII Islamic Banks**

**Article 87. General banking principles**

87.1. Islamic banks shall conduct their administration and operations in a sound and prudent manner and in accordance with the requirements of the law, any conditions and restrictions attached to their Islamic banking license or permits issued by Da Afghanistan Bank, and the regulations, guidelines and orders issued by Da Afghanistan Bank.

87. 2. Islamic banks shall: maintain adequate capital and liquid resources; make adequate provision for depreciation of assets, for discharge of liabilities, and for losses; maintain adequate accounting and other records of business; observe sufficient and effective risk controls; and ensure that their assets are diversified as to risk of loss.

87.3. Da Afghanistan Bank shall by regulation prescribe detailed standards of conduct for Islamic banks which Da Afghanistan Bank shall use in its prudential supervision.

87.4. Islamic banks and their Sharia Boards shall be responsible for all matters relating to compliance with Sharia; Da Afghanistan Bank shall have no responsibility in this regard.

87.5. Whenever an administrator of an Islamic bank discovers that the capital of the Islamic bank is less than the capital required by law or by regulation of Da Afghanistan Bank, the administrator must promptly notify Da Afghanistan Bank thereof.

87.6. Da Afghanistan Bank shall issue separate regulations to apply the provisions of this Chapter or regulations issued by Da Afghanistan Bank pursuant to this Chapter shall apply to domestic branch offices of non-resident Islamic banks.

87.7. All the provisions of this law that are consistence with Sharia are applicable for Islamic Banks.

**Article 88. Conversion of a conventional bank to an Islamic bank, opening an Islamic banking window by a conventional bank.**

1. With the prior approval of Da Afghanistan Bank and subject to the provisions of Article 7:

A) A conventional bank licensed under the laws of Afghanistan and having its headquarters in Afghanistan may convert to an Islamic bank,

B) A conventional bank licensed to engage in the banking business in Afghanistan may open an Islamic banking window, and

C) A conventional bank may terminate operations at an Islamic banking window.

2. Da Afghanistan Bank may impose such conditions as it sees fit in connection with its approval of any applications filed under this Article.

3. Da Afghanistan Bank shall not grant an application of a conventional bank for authority to convert to an Islamic bank or to open an Islamic banking window unless it concludes, based on its review of the proposed Sharia Board and the bank’s operating procedures, that there is reasonable assurance that the applicant’s operations as an Islamic bank or as an Islamic banking window will be conducted in a safe and sound manner.

**Article 89. Revocation of an Islamic banking license or revocation of a permit for an Islamic banking window upon request**

1. An Islamic bank may apply to Da Afghanistan Bank in writing to revoke its banking license or its permit for a branch office or a representative office. The application shall be accompanied by a liquidation plan adopted by the Islamic bank and by the financial statements of the Islamic bank as of a date preceding the application by not more than three months, together with a report of an independent external auditor acceptable to Da Afghanistan Bank. Within ninety days after its receipt of the request, Da Afghanistan Bank shall decide on the request.

2. The request may be approved only if Da Afghanistan Bank approves the liquidation plan, and if Da Afghanistan Bank is satisfied that the Islamic bank or office will be liquidated in accordance with the provisions of Article 64 and that the Islamic bank is solvent and will have adequate liquid funds to pay its liabilities to depositors and other creditors upon revocation of the Islamic banking license or permit.

3. The decision of Da Afghanistan Bank shall be communicated in writing by Da Afghanistan Bank to the Islamic bank as soon as possible, giving, in the event of a denial of the request, the grounds therefor.

4. Decisions to revoke an Islamic banking license or permit upon request pursuant to this Article shall be promptly registered in the central register of banks by Da Afghanistan Bank and have immediate effect.

5. A bank may apply to Da Afghanistan Bank for authority to terminate Islamic banking activities at an Islamic banking window. If the bank operating the Islamic banking window is solvent, Da Afghanistan Bank may approve such request upon being satisfied that the bank has an adequate plan for the orderly termination of Islamic banking activities at the Islamic banking window.

**Article 90. The Sharia Board**

1. The Sharia Board of an Islamic bank shall be responsible for compliance with Sharia in all of the Islamic bank’s products and operations. The Sharia Board and its members shall not serve in a supervisory, executive or managerial role. A conventional bank operating an Islamic banking window shall also establish a Sharia Board which shall operate as provided in this Article.

2. The Sharia Board shall be comprised of an uneven number of not less than three fit and proper members who shall be scholars who are expert in matters relating to compliance of financial products and services with Sharia. The members of the Sharia Board shall be appointed by the bank’s Board of Supervisors and shall serve for periods of not more than three years; they may be reappointed for subsequent terms of equal length. The Sharia Board shall choose one of its own members to act as Chairman.

3. A person shall not become a member of a Sharia Board, or shall by a decision of The General Meeting of Shareholders of the Islamic bank be relieved of his membership on the Sharia Board, in the event that he is or becomes ineligible for service pursuant to Article 29.

4. The Sharia Board may make valid decisions by a simple majority of the votes of its members participating in a meeting. Members may not abstain from voting.

5. Members of the Sharia Board of one bank shall not serve as administrators of another bank unless the Governor of Da Afghanistan Bank, acting on a case by-case basis, determines that such interlocking service is not likely to lead to the unauthorized disclosure of confidential information or a loss of competition.

**Article 91 Islamic banking activities**

Islamic banks may engage in the following activities subject to the provisions of their banking license:

91.1) receiving money deposits (in the form of demand deposits, time deposits or other types of deposit) or other repayable funds including investment accounts; and

91.2) such other financial activities as Da Afghanistan Bank may determine by regulation to be appropriate activities for an Islamic bank.

In formulating regulations setting out permissible financing activities for Islamic banks, Da Afghanistan Bank shall take into consideration, in the case of each proposed activity:

a) whether the activity in question is the functional equivalent of a financing technique traditionally performed by conventional banks for their customers; and

b) whether the risk of liability to the Islamic bank as a joint-venture or partner, from engaging in the activity in question, may be mitigated by conditions imposed by Da Afghanistan Bank.

The regulations adopted under this Article may condition an Islamic bank’s performance of an activity on such requirements as Da Afghanistan Bank sees fit, including conditions intended to (i) limit risk from performance of an activity, and (ii) ensure that the Islamic bank’s performance of any of the activities discussed in Article 35 is based on the financing needs of its customers. In addition, the regulations may prescribe (i) the documentation to be used by the parties to these transactions, and (ii) the remedies that shall be available to the parties in the event of default or nonperformance.

**Article 92. Prohibited activities**

No Islamic bank shall engage in or participate as an agent, partner or co-owner in wholesale or retail trade, manufacturing, transportation, agriculture or fisheries, mining, building, insurance or other business activities except for activities that are authorized by Article 91; provided, however, that this prohibition shall not limit an Islamic bank, at the request of a customer, from providing a service that is the functional equivalent of a financial service traditionally provided by conventional banks, as determined by Da Afghanistan Bank under Article 91. In addition, with the prior written authorization of Da Afghanistan Bank, an Islamic bank may temporarily carry on or participate in the carrying on of the activities described in the first sentence to the extent necessary to obtain satisfaction of claims; Da Afghanistan Bank may require the Islamic bank to cease such activities by a date specified in the authorization.

**Article 93. Prudential requirements**

93.1. When prescribed by regulation of Da Afghanistan Bank applicable to banks generally, each Islamic bank shall observe the maximum and minimum ratios, exposures and other prudential requirements to be maintained by it concerning its assets, off-balance sheet items and various categories of capital and reserves. Such regulations, as applicable to Islamic banks, may be modified by Da Afghanistan Bank to incorporate the standards and procedures prescribed by recognized standard-setting organizations for Islamic banks; and they shall prescribe the common procedures and methods of calculation to be followed in their application.

93.2. In particular, Islamic banks shall observe the following requirements when prescribed by regulation of Da Afghanistan Bank:

1) requirements concerning their liquid resources in relation to the value or change in value of their assets (including guarantees and collateral received), or in relation to their liabilities; Islamic banks shall be permitted to meet the requirements concerning liquid resources by maintaining with Da Afghanistan Bank money deposits of an equivalent value;

2) requirements concerning the maximum aggregate amount of all or certain categories of their credits and investments;

3) requirements, prescribed in response to exceptional circumstances, concerning the terms, maturity and other conditions applicable to any type or form of financing extended or received (including deposits) or applicable to contingent liabilities;

4) requirements concerning the classification and evaluation of assets, and provisions to be made on the basis of such classification and evaluation, and the time when earnings on non-performing loans may no longer be accounted for as income except as received in cash; and

5) prohibitions, restrictions or conditions concerning:

a) the types or forms of credits and investments made, and liabilities assumed (contingent or otherwise);

b) matching as to maturity and returns in respect of assets and liabilities (contingent or otherwise); and

c) un-hedged positions, exceeding a specified ratio, in foreign currencies, precious metals or precious stones; exchange rate instruments; stocks and other securities; and such other instruments permitted under regulations issued by Da Afghanistan Bank.

93.3. Each Islamic bank shall ensure that at all times the value of its regulatory capital, including its unimpaired capital and reserves, shall be equivalent to not less than 12 percent of the total value of its assets determined on a risk-adjusted basis, or such higher percentage as specified by regulations issued by Da Afghanistan Bank, whereby not less than one-half of regulatory capital shall consist of core capital. In applying this paragraph, the meaning of the terms “regulatory capital” and “core capital” shall be defined, and the values of regulatory capital, core capital and assets shall be determined, in accordance with the provisions of regulations issued by Da Afghanistan Bank.

93.4. No Islamic bank shall grant credit to a person if as a result thereof:

1) the aggregate outstanding principal amount of all its credits to that person would exceed or increase the amount by which such aggregate outstanding principal exceeds the equivalent of fifteen percent, or such higher percentage as specified by regulations issued by Da Afghanistan Bank, of the Islamic bank’s unimpaired capital and reserves; or

2) the aggregate amount of principal of large loans that have credit risks, as defined in a regulation of Da Afghanistan Bank, would exceed or increase the amount by which such aggregate outstanding principal exceeds the equivalent of two hundred percent, or such higher percentage as specified by regulations issued by Da Afghanistan Bank, of the Islamic bank’s unimpaired capital and reserves.

93.5. The limitations specified in paragraph 4 shall not apply to any principal amount of credit that is fully secured by readily marketable collateral as defined by regulation of Da Afghanistan Bank; however, no Islamic bank shall grant such secured credit if as a result thereof the aggregate outstanding principal amount of all its secured credits to the person receiving such credit would exceed or increase the amount by which such aggregate outstanding principal exceeds the equivalent of 15 percent of the Islamic bank’s unimpaired capital and reserves, or such higher percentage as specified by regulations issued by Da Afghanistan Bank.

93.6. For the purposes of applying this Article or any regulations issued pursuant thereto, a person shall be deemed to include any other person with whom such person is connected directly or indirectly in such a way that the financial soundness of any of them may affect the financial soundness of the other or others or the same factors may affect the financial soundness of some or all of them, or if as a result of the structure of their relationship the other person is in fact ultimately responsible for the credit outstanding.

**Article 94. Relations between Islamic banks and their customers**

94.1. The relations between Islamic banks, Islamic banking windows and their customers shall be governed by agreements between them whose terms and conditions may not be changed unilaterally by one of the parties, except as provided by the agreements. Da Afghanistan Bank may, as described in Article 35, prescribe by regulation the documentation

to be used by Islamic banks in conducting Islamic banking activities.

94.2. Each Islamic bank shall be free to determine by or pursuant to written agreements with its customers the terms and conditions on which it does business with its customers, including fees and charges payable by the Islamic bank on account balances, or payable by its customers on credits and other financial services provided by the Islamic bank, as well as the repayment terms of credits provided by the Islamic bank.

94.3. Da Afghanistan Bank may issue regulations requiring Islamic banks to provide to their customers adequate information concerning the terms and conditions associated with deposits, savings and Islamic bank credit in such form and substance as the regulations shall

specify.

94.4. All disputes between domestic Islamic banks and their domestic customers, and all claims of domestic customers on non-resident Islamic banks on account of activities of domestic branch offices of the Islamic banks, shall be adjudicated by the courts of Afghanistan, except for matters specifically within the jurisdiction of the Financial Services Tribunal.

94.5. Amounts on deposit in an account at an Islamic bank, including Da Afghanistan Bank, are subject to special rules if the accounts are considered dormant accounts. If an account holder has not evidenced any interest in the amounts on deposit by recorded transaction or written correspondence with the Islamic bank for ten years, on the first business day of the following calendar year the Islamic bank shall dispatch by registered post a notice to the account holder at his last known address containing particulars of the dormant account and publish in at least one local newspaper and in the Official Gazette the name of the account holder and the particulars of the dormant account. Not less than thirty days after such notice and publication, if the account holder cannot be located, the Islamic bank shall make a detailed report to Da Afghanistan Bank and shall turn over the amount on deposit to Da Afghanistan Bank, to be held in a special account at Da Afghanistan Bank. Da Afghanistan Bank may use the funds in such special account for such purposes as it may determine. In this case for a period of ten years any owner, who to the satisfaction of Da Afghanistan Bank furnishes proof of ownership, is entitled to the immediate repayment of the amounts by Da Afghanistan Bank. After expiration of such period, any remaining unclaimed amounts shall be transferred to the Ministry of Finance for inclusion in the revenues of the Government of Afghanistan.

**Article 95. Payment of debt in advance of maturity**

Each debtor of an Islamic bank may pay all or part of his debt to the Islamic bank at any time in advance of its agreed maturity date in accordance with the principles of Sharia. Such prepayments may be made subject to a contractually agreed prepayment fee. With respect to debt payable in installments, the Islamic bank may elect to apply partial prepayments proportionately to all installments or only to the latest installment. Covenants excluding or restricting this statutory right of prepayment shall be null and void.

**Article 96. Secured debt**

96.1. Islamic banks shall be free to determine in agreement with their counterparties whether their respective obligations shall be secured by collateral, guarantees or other commitments. No Islamic bank shall accept shares in its own capital stock as security for a debt to the bank without the prior written authorization from Da Afghanistan Bank.

96.2. In the event of a payment default on debt to an Islamic bank secured by a pledge of or a lien on movable goods, or by a mortgage on immovable or other registered goods, the goods may be sold by public auction or through a broker on a public exchange in accordance with law. The Islamic bank may participate in the bidding for the goods. For the event that the goods cannot readily be sold by public auction or on a public exchange for a price that is at least equal to the amount of the debt together with sales costs, the interested parties may agree by notarized agreement, or failing such agreement the court may decide at the request of any interested party, that the goods shall be sold otherwise or that the Islamic bank may purchase the goods for a price determined by or in accordance with the provisions of that agreement or a decision of the court. After deduction of the amount of the outstanding debt and costs, the balance of the purchase price shall be paid promptly to the debtor who owned the goods after having satisfied any other person to whom the goods are proven to be pledged by the debtor. If the sales price of the goods net of costs is insufficient to cover the amount of the outstanding debt, the unpaid amount remains an obligation of the debtor to the Islamic bank.

**Article 97. Records of transactions and commitments**

97.1. Islamic banks shall keep on file for at least ten years the pertinent documents for each one of their transactions, namely:

1) the application and all contract documents pertaining to the transaction (including credit, guarantee and collateral agreements);

2) the financial records of the Islamic bank's counter parties (including borrowers and guarantors), and any other documentary evidence on which the Islamic bank relied in approving the transaction;

3) a signed written record of the decision of the Islamic bank approving the transaction;

4) the account agreements with its customers; and

5) such other documents as Da Afghanistan Bank may specify by regulation.

97. 2. Records may be kept in electronic form to the extent that adequate data recovery systems and procedures are in place. Da Afghanistan Bank may issue regulations setting out detailed systems requirements.

**Article 98. Islamic bank exposure to related persons**

98.1. No Islamic bank may engage in any financial service described in Article 35 for the benefit of a related person:

1) if the service and its financial terms and conditions have not been approved by its Management Board or its Board of Supervisors; or

2) if the service is granted for the benefit of an administrator of the Islamic bank and performance of the service would cause the aggregate amount of exposure of the Islamic bank to that person and outstanding to exceed the equivalent of 25 percent of the annual remuneration of that person, or if performance of the service would cause the aggregate exposure of the Islamic bank to all related persons and outstanding to exceed or increase the amount by which such aggregate exceeds the unimpaired capital and reserves of the Islamic bank; except that the foregoing percentage limits shall not apply to any principal amount of credit that is secured in compliance with standards prescribed for that purpose by regulation of Da Afghanistan Bank by a mortgage on property whose appraised value at the time that the credit is granted exceeds the principal amount of the credit by not less than one-third of that principal amount; or

3) if the service is provided on terms and conditions that are less favorable to the Islamic bank than the terms and conditions that are offered by the Islamic bank to the public in the ordinary course of business when the service is performed.

98.2. Every financial service performed by an Islamic bank for the benefit of a related person shall be promptly reported to the Audit Committee of the Islamic bank. If a financial service has been performed by an Islamic bank for the benefit of a related person in violation of the provisions of paragraph 1, such credit must be immediately repaid, and the members of the Management Board and the Supervisory Board shall be personally liable, jointly and severally, for payment of any loss incurred by the Islamic bank in performing a financial service in violation of paragraph 1 with their knowledge and without their objection.

98.3. For the purposes of this Article, a related person means:

1) any administrator of the Islamic bank;

2) any person who is related to an administrator of the Islamic bank by marriage, blood or kinship up to the second degree, or who is the adopted child or foster child of an administrator of the Islamic bank; and

3) any person who alone or in concert with one or more others or through one or more others has a qualifying holding in the Islamic bank, and any enterprise in which any such person or the Islamic bank or any administrator of the Islamic bank has alone or in concert with one or more others or through one or more others a qualifying holding, and any administrator of such person or enterprise.

**Article 99 Prevention of Islamic banking services in support of crime**

99.1. No Islamic bank shall maintain accounts on its books or provide services to or for the benefit of undisclosed persons.

99.2. Each Islamic bank shall register the identity of each one of its clients who maintains an account with the Islamic bank or otherwise uses the Islamic bank for activities including transfers of funds or securities, securities transactions, or the negotiation of payment instruments, or such other activities as Da Afghanistan Bank shall specify by regulation. Each

Islamic bank shall require each such client to provide adequate information to the Islamic bank about the identity of any other person who is a beneficiary of such account or for whose

account such activities are conducted and shall register the identity of each such other person. Banks shall maintain proof of the identity of the persons so registered.

99.3. No Islamic bank shall maintain an account on its books or provide services to or for the benefit of a person, and each Islamic bank shall report to Da Afghanistan Bank any request or instruction to maintain such account or to provide such services, if there are substantiated reasons to suspect that such person engages in transactions connected with money laundering, terrorism or another criminal activity. Da Afghanistan Bank may by regulation issue rules concerning the form, time and content of such reports.

## Annex-3: Institutions and Individuals interviewed by the team

|  |  |
| --- | --- |
| **MINISTRY OF URBAN DEVELOPMENT AFFAIRS (MUDA),**  **SATURDAY 22nd JUNE 2013- (10.30 AM)** | |
| **NAME** | **DESIGINATION** |
| DR.HASSAN ABDULAHI | MINISTER FOR URBAN DEVELOPMENT AFFAIRS |
| ENG.HAMID JALIL | DEUPUTY MINISTER FOR URBAN DEVELOPMENT AFFAIRS |
| ENG.RAHIM | PLAN AND POLICY DIRECTOR |
| **DA AFGHANISTAN BANK,**  SATURDAY 22nd JUNE 2013- (4.30 PM) | |
| MR.KHAN AFZAAL HADWAL | FIRST DEPUTY GOVERNOR |
|  | HEAD OF MONETRY POLICY DIVISION |
| **GHAZANFAR BANK AFGHANISTAN,**  SUNDAY 23rd JUNE 2013 (9.30 AM) | |
| MR.AHMAD SIAR KHORESHI | CHIEF EXECUTIVE OFFICER (CEO) |
| **BANK E MILLIE AFGHANISTAN (BMA),**  SUNDAY 23rd JUNE 2013 (11.00 AM) | |
| MR.MOHIB ULLAH SAIFI | CHIEF EXECUTIVE OFFICER (CEO) |
| **FINANCIAL SUPERVISION DEPARTMENT-DA AFGHANISTAN BANK,**  SUNDAY 23rd JUNE 2013 (12.30 PM) | |
| MR.SALIM SALLAH | DEPUTY DIRECTOR GENERAL |
| **AFGHANISTAN INTERNATIONAL BANK (AIB),**  SUNDAY 23rd JUNE 2013 (02.30 PM) | |
| MR.KHALIL SEDIQ | CHIEF EXECUTIVE OFFICER (CEO)/ CHAIRMAN AFGHANI BANKS ASSOCIATION |
| **AFGHANISTAN CHAMBER OF COMMERCE AND INDUSRTY,**  MONDAY 24th JUNE 2013- (10.00 AM) | |
| MR.QURBAN HAQJO | CHIEF EXECUTIVE OFFICER |
| **MINISTRY OF COMMERCE AFGHANISTAN,**  MONDAY 24th JUNE 2013 (12.30 PM) | |
| MR.KHALID MAFTOON | DOING BUSINESS ADVISOR |
| MR.AHMED ZIA SAYED KHAILI | DIRECTOR SME MANAGEMENT AND DEVELOPMENT AFFAIRS |
| **KABUL MUNICIPALITY,**  MONDAY 24th JUNE 2013- (02.00 PM) | |
| MR.M.Y NAWANDISH | MAYOR |
| MR.KHOGMAN “ULOMI” | DEPUTY MAYOR |
| **MINISTRY OF REFUGEES AND REPATRIATES**,  MONDAY 24th JUNE 2013- (04.00 PM) | |
| DR.JAMAHER ANWARI | MINISTER |
| DR.NILOFER HESSARI | RE-INTEGRATION ADVISOR TO MINISTER/ ACTING PROJECT MANAGER |
| ENG.MOHAMMAD ZIA LERWANY | ACTING PROJECT MANAGER |
| **AZIZI BANK AFGHANISTAN**,  MONDAY 24th JUNE 2013- (05.00 PM) | |
| MR.SALEEM OMAID | DEPUTY CEO |
| **MINISTRY OF ECONOMY,**  TUESDAY 25th JUNE 2013-(10.00 AM) | |
| MR.HUKUM KHAN HABIBI | DEPUTY MINISTER TECHNICAL AFFAIRS |
| **AREU**,  TUESDAY 25th JUNE 2013-(10.30 AM) | |
| MR.NADIR NADRI | CHIEF EXECUTIVE |
|  |  |
| **FIRST MICROFINANCE BANK AFGHANISTAN,**  WEDNESDAY JUNE 26TH 2013-(10.00 AM) | |
| MR.CHRIS UNDERWOOD | CHIEF EXECUTIVE OFFICER |
| MR.NAEEM RIZWANI | HEAD OF PRODUCT DEVELOPMENT AND MARKETING |
| **BANK AL-FALLAH AFGHANISTAN,**  WEDNESDAY JUNE 26TH 2013-(11.30 AM) | |
| MR.SARFARAZ NAZIR | COUNTRY HEAD |
| MR.EHSAN UL HAQ | COUNTRY OPERATIONS HEAD |
| MR.MUHAMMAD NASIR | COUNTRY MANAGER CREDITS |
| **USAID,**  THURSDAY JUNE 27TH 2013-(09.30 AM) | |
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| **MISFA,**  THURDAY 27TH JUNE 2013-(10.15 AM) | |
| MS.KATRINE FAKHRI | MANAGING DIRECTOR |
| **IFC AFGHANISTAN,**  THURSDAY 27TH JUNE 2012-(11.15 AM) | |
| Ms. MEAGAN ANDREWS | SENIOR OPERATIONS OFFICER |
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## Annex-4: Suggestive TOR for Housing Consultative Group

**Housing Consultative Group (HCG)**

Were the Afghan stakeholders in housing undertaking to create a Housing Consultative Group, the

Terms of Reference for such an effort might include:

* 1. Identify the current and potential future actors that would be included as members of the Group, to include appropriate representatives of the Government of Afghanistan through concerned Ministries; Da Afghanistan Bank; Banks including those with Islamic Banking Windows that are now providing mortgage loans, or that are committed to doing so in the future; Afghanistan Builders Association, Municipality; Regulators of Building Codes and By-Laws; and other real estate professionals, and possibly representatives of potential housing finance consumers.
  2. Determine how each stakeholder group would select representatives to be part of the HCG, as well as how vacancies would be filled and how newly formed institutions would be accommodated as the housing finance system evolves.
  3. Prepare a list of Issues to be addressed in the short term, medium and long term. The HCG will determine priority and time frame of each for report in each issue by the respective Task Force.
  4. Set up Task-Forces/Sub-Committees for each issue and decide Issue Champions
  5. Assignments as to which institution(s) would have the lead responsibility in each instance, and target dates by which proposed actions would be completed. Provision should also be made for input from Task Force members that may not have lead responsibility for a particular action, but that would be affected by the outcomes - for example, how financial institutions would be permitted to have input into the development of regulations governing the activity of mortgage lenders.
  6. Specify how the Consultative Group would monitor the outcomes of the housing finance system - for example, the volume of mortgages written by financial institutions, the types of borrowers who are served, and the performance of outstanding mortgage loans.
  7. Evolve a mechanism for effective monitoring of execution of recommendations of different Task forces. The lead role to monitor and submit progress on respective Issue will be the responsibility of Issue Champion.

## Annex-5: Policy on Upgrading of Informal Settlements-July 2013

**Preamble**

It is widely acknowledged that significant proportion of the urban population of Afghanistan is currently residing in property which has not been formally registered or that falls outside the formally planned parts of urban areas. At a time of unprecedented urban growth, this poses a significant challenge to the authorities mandated to guide and manage urban development. As things stand, these authorities do not formally recognize informal settlements as part of the urban fabric which has resulted in a significant disconnect between the ‘formal city’ and the reality on the ground. As a consequence, despite the fact that they are home to a significant (and growing) proportion of urban inhabitants, informal settlements do not receive adequate development attention whether in the form of orderly upgrading or the provision of meaningful interventions aimed at improving living conditions.

This lack of investment in basic services has an adverse impact on the social and economic development of those inhabiting informal settlements. Although there is little accurate baseline data on urban communities, it is clear that poor sanitation and unsafe water supplies affect the wellbeing of many households, especially those in areas where the extension of basic services is ruled out due to their informal status. Although a good number of residents of these settlements are legitimate occupiers, they have no security of tenure and no means by which to regularize and register their property rights. At the same time, the existing situation deprives municipalities of substantial potential for enhancing their revenue that could be collected for provision of services in informal settlements.

Over the last decade, an erratic application of development controls, along with ambiguity in the official position with respect to upgrading of informal settlements, has exacerbated the sense of insecurity within informal settlements, even though this seems not to have prevented significant expansion in their extent in most urban centers. At the same time, small scale physical infrastructure upgrading and tenure improvement projects have been implemented in consultation with pertinent municipalities and in partnership with the resident communities, thus demonstrating the potential of incremental upgrading in certain circumstances.

Despite this experience, municipalities and other relevant government agencies continue to undertake or allow such upgrading initiatives on an ad hoc basis, without a coherent policy framework or legislation. This document aims to provide policy guidance, so that informal settlements can be properly integrated into the urban landscape, and residents realize their true potential through private investment in property and infrastructure.

According to the USAID Thematic Report on Land Dispute Resolution referenced below, almost 70%[[66]](#footnote-66) of Afghan population is living in unregistered and informal urban real estate settlement.

Considering the above mentioned percentage about the unregistered and informal settlement, it is not normally feasible to abolish them all and redesign and restructure the whole, thus, in some areas, it is highly required to undertake the upgrading schemes according to the developed upgrading policy and procedures.

**CHAPTER ONE**

**Purpose**

The purpose of this policy is to set forth a clearly defined set of issues and policy statements that will serve as general guidance to inform administrative and legislative measures that need to be taken by the Government to officially recognize, upgrade, and, as appropriate, regularize informal settlements. Moreover, under this policy framework, the Ministry of Urban Development Affairs, IDLG/GDMA, Kabul Municipality and other municipalities shall formulate or adjust their strategies and plans of action to tackle challenges pertaining to informal settlements.

1. **Policy Objectives**

The objectives of this policy framework are the following:

1. Enabling the upgrading of basic services in informal settlements;
2. Promote the Improvement of tenure security along the continuum of property rights principle;
3. Laying the ground for processes that would allow for adjudication and recording of rights to immovable property in informal settlements;
4. Facilitate the identification of appropriate level of planning standards in informal settlements;
5. Enable municipalities to enhance their revenue through betterment levies upon delivery of basic municipal services;
6. Facilitate regularization of informal settlements in an orderly manner;
7. Promote key stakeholders’ coordination and engagement.
8. **Policy Principles**

The underlying principles of the general guidance provided by this policy framework are the following:

1. Upgrading of informal settlements shall contribute to the integration of informal settlements into the urban fabric;
2. Upgrading programs shall promote holistic, integrated and locally appropriate development of informal settlements, with minimum or no disruption of livelihoods and existing community structures and networks;
3. Partnership between pertinent government authorities and community members is vital to ensure mobilization of local resources and the design of locally appropriate solutions.
4. **Scope of the policy**
5. This policy shall be applicable to informal settlements:
6. Where landless squatters have occupied State-owned land;
7. Where the majority of the inhabitants formally or informally (customarily) own the land;
8. Provided such settlements are on environmentally tenable land as certified by the Ministry of Urban Development Affairs.
9. It is essential that clear distinction be drawn between situations in which land has been grabbed by powerful interests for distribution to a specific group or sold off speculatively for profit and instances where homeless squatters have occupied State-owned land to accommodate themselves as a last resort. Informal settlements that have been on land grabbed for speculation by powerful interest shall be dealt with by separate policy and legislative framework.

**NB. Option 2 is to omit sub-provision (2). Omitting sub-provision 2 would include informal settlements inhabited by people who acquired occupancy from land grabbers. However, this may have the undesirable effect of encouraging further land grabbing. This needs to be considered prudently.**

1. Informal settlement on agriculture land shall not be upgraded for the latter is not legally allowed for settlement.
2. Tasfia (Land Right Identification) shall take place prior to any informal settlement upgrading activity.
3. Guidelines and procedures for the implementation of this policy may be developed by the relative stakeholders after the policy is approved.
4. This policy may be subject to review after each 5 years.
5. **Integrated response to problems of informal settlements**

**Issue:** Informal settlements pose a variety of challenges. Primary among these is a lack of access to basic services, tenure insecurity and exclusion from official development plans. It is therefore vital for the government to deal with the question of informal settlements in a holistic manner, by promoting an integrated approach that enables upgrading of basic services in parallel with enhancement of tenure security, while ensuring environmentally sustainable land use. Such an approach would also facilitate the integration of informal settlements in the formal urban planning process.

**CHAPTER TWO**

**Policy Statement:**

Laws, regulations, administrative procedures and plans pertaining to informal settlements shall aim at upgrading of basic services, incremental improvement of tenure security, and gradual incorporation of informal settlements into urban development plans in an integrated and equitable manner.

1. **Institutional responsibilities**

**Issue:** The prevailing institutional arrangement for urban planning and management, especially with respect to informal settlements lack clarity and coordination. While moves have recently been made to clarify and re-define specific official roles and responsibilities of government agencies, there remain outstanding issues with respect to formulating policy, planning, and implementation, which remain unresolved.

**Policy Statements:**

1. **Designing upgrading programs**

Except for Kabul city, MUDA, in consultation with residents or occupants of the area selected for upgrading and the municipality within whose jurisdiction the proposed scheme is situated(or most closely contiguous) is responsible for designing upgrading measures in accordance with the spirit of this policy and any pertinent legislation.

1. **Implementing upgrading programs**

Except for Kabul city, municipalities, under the direction of GDMA, shall be responsible for the implementation upgrading projects, but may delegate the whole or any part of the implementation of such scheme to the District municipalities where the upgrading area is situated or to which it is most closely contiguous.

1. **Monitoring upgrading programs**

To ensure proper implementation of upgrading policy in targeted areas where the upgrading schemes are being implemented, MUDA, GDMA, relevant Municipalities and respected communities representative as a joined team shall monitor the upgrading activities so that to be in compliance with the relevant legislations and policies.

1. **Upgrading of basic services**

Notwithstanding the policy statements above, except for upgrading of access to water supply, projects for upgrading of basic services shall be carried out by relevant municipalities in partnership with target communities and when appropriate with private or public utility providers.

1. **Transformation**

After the upgrading programs and basic services are implemented, the informal settlements will be transformed into a new shape and the respective residents will have access to schools, clinics, parks etc. and also get use of water sanitation, drainage, streets and etcetera with the support and cooperation of the relevant entities.

1. **Formulating and designing regularization schemes**

It is essential that municipalities, in partnership with informal settlement communities, formulate and implement schemes for regularization of property rights.

1. **Tenure regularization**

**Issue:** There is no procedure by which to regularize the property rights of citizens who have occupied land in informal settlements. Given the extent of such settlements within the urban landscape, it is essential that ways are found to provide some form of official recognition of informal property rights held through long, peaceful and continuous occupation of land, in order to redress inequity in land occupation in urban areas.

**Policy Statements:**

1. The principle of adverse possession as defined in this policy will be applied in accordance with the principles of Islamic jurisprudence to redress problems created by the lack of effective land use management in the country. The application of this principle to all current occupation or *de facto* ownership of residences will provide the basis to determine which land occupation or ownership is legitimate and which is not.
2. The principle of adverse possession shall not apply in cases where land has been occupied by force or where continued occupation is not in the public interest, for example, where it is environmentally unsound or unsafe to continue to occupy land.
3. In this policy document the term ‘adverse possession ‘represents a legal concept that enables a person to acquire a legal right to a land if he maintains a peaceful, open, actual and continuous possession of it, to the exclusion of the real owner and others, for a prescribed amount of time.
4. **Upgrading of basic services**

**Issue**: There is wide disparity in access to service between urban communities, which can in part be addressed by investments in upgrading of existing structures/systems, or through provisions of new services. Many of the service-poor areas lie outside the remit of the ‘master plan’ and are therefore not officially eligible for investments in upgrading.

**Policy Statements:**

1. The primary objective of urban upgrading is to address the needs of communities identified as ’service-poor’ i.e. without access to safe water, functioning drains, adequate household sanitation, electricity or where there is no reliable waste collection or pedestrian/vehicular access is difficult for residents.
2. Where upgrading is technically feasible and deemed cost-effective, all informal settlements that fall within the scope of this policy document will be deemed to be eligible for such investments.
3. **Land Use Planning**

**Issue:** There are no standards by which to incorporate informal settlements into the process of urban planning. This presents a challenge both in land use planning and in efforts to protect the physical environment.

**Policy Statements:**

1. Where appropriate and cost effective, appropriate technical standards for infrastructure provision will be developed and agreements to spatial readjustment deemed necessary for service provision be sought with community representatives of the target community.
2. Any informal settlement upgrading project must promote coordinated working relationship between the relevant municipality (and its district office), and the concerned community in relation to any appropriate planning standards that may be applicable to an informal settlement eligible for upgrading.
3. A revised or new urban planning law should consider incorporating provisions that promote appropriate and locally specific planning standards for declared regularization areas. Planning instruments must aim at preserving existing layout in unplanned areas, unless there are compelling interests that warrant planning alterations to the existing layout. Such compelling reasons would include creating adequate vehicular access to parcels, either by establishing a new road, right of way, or widening an existing road.
4. In accordance with the National Land Policy, a revised or new law should incorporate a provision that strikes a balance between promoting necessary spatial readjustment to improve access roads and the need to do so with no or minimal physical, social or livelihood disruption in the areas selected for regularization. To this effect, a revised or new urban planning law should realistically deal with enforcement of land planning control, thereby excluding unplanned areas on which a scheme of regularization is declared from the existing enforcement of land planning control provisions.
5. **Community participation**

**Issue:** Planners, engineers and municipal officials often perceive upgrading of informal settlement as mere technical and legal issue. However, relevant experience suggests that the success of implementing any upgrading scheme is to a large extent determined by the level of community participation.

**Policy Statement:**

It is vital that upgrading of informal settlement schemes address tenure security, planning and upgrading of basic services issues from the perspective of the needs of the community, while conforming to the relevant official policies and legislation. Such schemes shall allow community participation, specifically with respect to identifying and prioritizing basic upgrading needs, creating community or neighborhood land use plan, resolving land-related disputes, negotiating spatial re-arrangements, identifying and demarcating property boundaries, and determining and recording property rights.

**CHAPTER THREE**

1. **Relocation**

**Issue:** Upgrading of informal settlements may involve the relocating of existing households as a last resort for compelling public policy reasons such as in instances where continued occupation of public land is environmentally unsafe or to implement appropriate planning standards as indicated in this policy document.

**Policy Statement:**

1. In cases where continued occupation of land is deemed to be against public interest, the occupants of such land will be protected from eviction until such time as the relevant authorities are able to allocate alternative land, ideally as close as possible to their existing location.
2. Anti-eviction law will be proclaimed to protect people from arbitrary eviction or eviction without suitable relocation and resettlement options.
3. **Verification & Determination of property rights**

**Issue:** Regularization of informal property rights presupposes clarification and settlement of rights. Past experience suggest that conflicting claims over the same property are not a rare occurrence in informal settlements. Such conflicting claims must be settled through an effective and just mechanism when implementing a regularization scheme.

**Policy Statement:**

Claims of property rights will be verified and determined by the relative Tasfia (Land Right Identification) team with close collaboration of relative community regularization schemes in which the relative Tasfia team collects the required data and information and applies the prevalent legal principles and norms pertaining to proof of rights to land and the principle of adverse possession to determine whether residents legitimately occupy or own the land that they claim. If such claims of property rights may not be verified and determined by the Tasfia team and community, it shall be referred to relative court for final decision.

1. **Dispute resolution**

**Issue:** Certain types of land-related disputes are common in informal settlements, and are usually resolved through informal means, in the absence of an effective or affordable formal dispute resolution system for low-income inhabitants of informal settlements.

**Policy Statement:**

Disputes over boundaries, inheritance and other interpersonal disputes regarding rights to immovable property should be resolved by Tasfia (Land Right Identification) team with the close cooperation of community-based dispute resolution mechanism when Tasfia takes place therein. If such disputes may not be resolved by the previous, then shall be referred to the competent court for final decision.

1. **Recording of property rights**

**Issue:** Implementing regularization schemes require a suitable land records system which recognizes the need to distinguish between the formal and participatory land management processes. Such a system is essential for the collection of land records data required for upgrading and regularization schemes as well as in terms of improving the tenure security of the inhabitants of informal settlements.

**Policy Statements:**

1. Community based and simplified land recording system will be established in each local area declared for a regularization scheme. Property rights shall be registered after duly elected and authorized community representative body in each of such local area has gathered information, assessed and confirmed the legitimacy of each resident’s claim of right of occupation or ownership in accordance with the principle of adverse possession and legal principles and norms pertaining to proof of right to property. Community based land record system shall be absolutely consistent with Tasfia team record and data collection.
2. The data to be collected by the Tasfia team with close cooperation of community representative body will include identification of boundaries of each parcel of land recorded on adequate mapping, together with details of the occupier, and proof of right of ownership or alternatively proof of the occupier having met the requirements for ownership under the principle of adverse possession.
3. To ensure accessibility, accountability and transparency of the land records, it is a national policy to promote partnership between the Tasfia team of Arazi, communities and local municipal authorities in keeping and maintaining the land records. The land records kept by the Tasfia team, communities and the local municipal authorities shall be linked to each other and reflect the same data.
4. **Land taxation**

**Issue:** Past experiences in Afghanistan suggest that informal settlement upgrading schemes that were funded by donors covered the initial provision of basic services and land tenure related expenses but did not reserve funding for maintaining the upgraded services and updating land-related records. While it may not always be feasible to design an upgrading scheme that envisages maintenance costs to be recovered from levying taxes, betterment levies on individuals or group of individuals on demarcated land boundaries of an upgraded area can serve as a means to enhance the revenue base of the local municipality as well as to ensure community connection and participation to maintenance of services.

**Policy Statement:**

Pertinent government authorities shall use betterment levies and/or sanitation tax (*safayee)* concessions to encourage informal settlement dwellers to regularize their rights to land. Sanitation taxation shall primarily be used to provide finance for land development and for the provision and maintenance of local services and land records.

1. **Selection of Settlements for Regularization Schemes**

**Issue:** Upgrading programs for informal settlements should be designed and implemented in a fair, transparent and equitable manner. Criteria for the inclusion of settlements into upgrading programs can serve as a tool to achieve fairness and transparency in the design and implementation of upgrading programs on a phased basis.

**Policy Statements:**

1. It is vital that vulnerability, deficiency in service delivery, land tenure and use, existence of community organization or harmony, suitability for human habitation in terms of environmental tenability and conditions for improvement and maintenance of basic services shall be the key factors to be considered in determining criteria for selecting or prioritizing upgrading of informal settlements.
2. Informal settlements formed on informally held private land and on State-owned land occupied by needy squatters and have been in existence for a period exceeding fifteen years shall be selected as priority for implementing schemes of land tenure regularization and upgrading of basic services, in so far as the areas are deemed to be habitable.
3. MUDA, in consultation with IDLG/GDMA and Kabul Municipality, shall issue guidelines for selection and prioritization criteria for upgrading and regularization of informal settlements.

## Annex-6: Informal Settlement Upgrading: Selection Criteria Guidelines

In accordance, with the draft policy for regularization/upgrading of informal settlements, MUDA in consultation with IDLG/GDMA and Kabul Municipality, hereby issues the following selection and prioritization guidelines for upgrading informal settlements.

These guidelines may not be applicable in their totality by all informal settlements that are eligible for implementing upgrading and regularization schemes. In such events, the relevant municipality may weigh the relevance and trade-off of these guidelines in the context of the local reality.

1. Vulnerability consideration

Addressing the needs of settlements where the majority of the inhabitants are critically poor as evaluated by socio-economic indicators will rate high in determining priority settlements for upgrading. Settlements with undeveloped connection to urban infrastructure networks and inadequate social services making dwellers more deserving of assistance.

1. Land use considerations

Informal settlements developed in areas that are earmarked for large infrastructure of city-wide interest or allocated for housing development for predetermined beneficiary group and encroached by other people will not be eligible for upgrading or tenure regularization.

1. Land Tenure consideration

Informal settlements formed on land that is *de facto* privately owned by the settlers or land belonging to the state or other public entities shall be selected prior to those formed on grabbed land which was owned by communities or individuals, which might face legal challenges and thus cause delay in implementation.

1. Environmental risk

Informal settlements located in areas that are susceptible for natural hazard such as flooding or landslides will not be included in upgrading or regularization schemes.

1. Topography of settlement

Topographical conditions may determine the technical as well as financial feasibility of upgrading the basic services of a given informal settlement. Upgrading of basic services in settlements formed on plain areas will be given priority as they are likely to be more feasible than upgrading of settlements formed on complicated mountain sides.

1. Community organization

Settlements with well-established community organizations and social networks are expected to facilitate consultations and negotiations compared to those situations where there is weak cohesion, implying more complications and potentially more disputes.

1. Proximity to trunk infrastructure:

Informal settlements located close by existing spare capacity of trunk infrastructure will be given priority since upgrading investments will be more cost effective.

**Definitions**

In this policy, unless the context otherwise requires: Adverse possession means the acquisition of a legal right to land, through peaceful, open, actual and continuous possession of a land, to the exclusion of the real owner and others, for a period prescribed by law.

Continuum of property rights means range of land rights which occupy a continuum from complete illegality to the highest form of formal tenure.

* Informal settlements means unauthorized or unplanned settlements consisting of houses built on unlawfully or informally occupied land.
* Land grab means usurpation of land by powerful interests for distribution to a specific group or for disposing off speculatively for profit.
* Recording of property rights means recording in a register the property rights in land.
* Squatter means a person who occupies land to satisfy his shelter needs without meeting legal requirements.
* Tenure Regularization means giving formal recognition to informally held tenure.
* Tenure security means right to land held without risk of loss and for a long period of time.
* Unplanned settlement means informal settlement.

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2. Interview with Dy. Minister of Economy Mr. Hukum Khan Habibi, June 25, 2013. [↑](#footnote-ref-2)
3. Mr. Wahid Tawhidi, Finance Ministry Spokesman, June 10, 2012 Bloomberg Business Week, June 12, 2012 [↑](#footnote-ref-3)
4. Interview with Mr. Qurban Haqjo on June 24th, 2013 [↑](#footnote-ref-4)
5. Afghanistan Opium Survey 2012, by UNODC and Ministry of Counter Narcotics, Afghanistan [↑](#footnote-ref-5)
6. The World Factbook, CIA [↑](#footnote-ref-6)
7. The World Factbook, CIA [↑](#footnote-ref-7)
8. Meeting with Head of Monetary Policy Division, DAB, on June 22nd, 2013 [↑](#footnote-ref-8)
9. Meeting with Mr. Khan Afzal Hadwal, First Dy. Governor of DAB on June 22, 2013, Head of Monetary Policy Division at DAB on june 22, 2013 and Mr. Salim Ullah Dy. Director General at Financial Supervision Department of DAB on June 23, 2013 [↑](#footnote-ref-9)
10. Meeting with Mr. Mohib Ullah safi CEO Bank Millie on June 23, 2013 [↑](#footnote-ref-10)
11. Meeting with Mr. Ahmed Siar Khoreshi, CEO on June 23, 2013 [↑](#footnote-ref-11)
12. Meeting with Mr. Khalil Sadiq, CEO AIB on June 23, 2013 [↑](#footnote-ref-12)
13. Meeting with Mr. Salem Omaid, Dy CEO Azizi bank on June 24, 2013 [↑](#footnote-ref-13)
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