



An Exploratory Study of Islamic Banking in Private Banks in Kabul

By

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Declaration of Authorship

I hereby declare that:

- This thesis for the Master of Business Administration (MBA) degree at the American University of Afghanistan is my original work. I have written it under the supervision of the faculty assigned to me by the MBA Director in consultation with the Provost.
- To the best of my knowledge, I have cited accurately all sources I have used for this thesis.
- I have acknowledged those parts of the thesis, which are based on the collaborative work with third parties other than my supervisor.
- I have not submitted this thesis or substantial parts of it for a degree or any other qualification at another institution.

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Abstract

Afghanistan is a developing country. Though there have been some changes and growth in Islamic banking area, lack of awareness and doubt among people exist that whether is Islamic banking Islamic or not. This criticism raises a gap that this study wants to fill it with the assessment of distinguishing features of Islamic banking in three private banks in Kabul city. This study examined five different features of Islamic banking in private banks in Kabul respectively compliance with Sharia law, accounting system, legal aspect, the existence of Sharia Supervisory Board (SSB) , and bank customer's attitude, awareness, and reason for selection of Islamic banking. In order to gather data from three private banks, two surveys were shared with bank employees as well as with customers. From a total of 75 respondents 41 employees and 34 customers participated. Main findings of this study are: though Islamic banking products and services are complained with Islamic principles, but very limited products are available currently in the banks. Another finding is that Islamic banking funds are circulated in the same way as conventional banking, and there is not separate accounting and auditing systems. Lack of sharia board members in the bank and lack of awareness of sharia law among customers and employees are two other findings, most customers select Islamic banking because of their religious believes. The positive finding is that customers are satisfied by the Islamic banking products and services offered by banks. These findings are beneficial and relevant to both full-fledged Islamic banks as well as conventional banks with Islamic banking window to focus on them and use them efficiently for the development of Islamic banking.

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Dedication

I want to dedicate this project to my dear parents who have always stood beside me and encouraged me to further my studies till this point as well as my husband who looked after my daughter, helped and supported me during pursuing this project.

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Chapter One: Introduction

This chapter explains the research problem, research question, research objectives, research scope and limitation, research justification and importance, and presents a description of the Islamic banking industry and its challenges. Islamic banking, one of the fastest growing sectors in the past decade (Mastoor, 2014), has a vital role in the development of the economy of Afghanistan. A survey by Hrakat organization in 2015 found that the public had lost confidence and trust on Islamic services provided by Islamic banking because of the unavailability of an official framework. Fortunately, in October 2015, Da Afghanistan Bank (DAB) prepared and announced a framework for Islamic banking window to increase the accession of businesspersons to finance, and to attract depositors in Islamic communities based on the DAB report. For the purpose of development of Islamic banking it is very important to explore more about it.

1. 1 Research Problem

This study presents important features of Islamic banking in the context of Islamic banks in private sector in Kabul. The study identified five important factors from the prior work in this area, namely compliance with Islamic principles, accounting and auditing standards, legal and regulatory structures, sharia supervisory board, and Islamic banking customers selection of the bank, attitude and awareness toward Islamic banking products and principles.

Compliance with Islamic principles is the major feature of Islamic banks. The structure of Islamic banks should follow Islamic law. According to Kammer (2015), there are two authorised bodies having the authority to set standards: Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) and the Islamic Financial Services Board (IFSB) (Kammer et al., 2015). These bodies check Islamic bank standards against the

standards they set in terms of being consistent and coherent. However, implementation of these standards varies among different countries. This study found that among the 29 countries participating the survey, only small number, 8 out of 29, consistently applied AAOIFI standard and a smaller number, 6 out of 29, applied IFSB standards (Kammer et al., 2015). The study also found that lack of compliance between Islamic bank regulatory standards and above-mentioned standards can result in an unclear or non-transparent regulation system that can cause weak relationship among Islamic banks and these regulatory bodies (Kammer et al., 2015).

Sharia Supervisory Board (SSB) is essential for Islamic banking. It is composed of experts in religious matters who permit and approve new products. There are different scholars of jurisprudence and the success and failure of a new product in the market introduced and approved by specific religious scholars depends on the background of the expert team (Van Greuning & Iqbal, 2008). Van Greuning and Iqbal state that there is a lack of Sharia experts with a high level of education background in Islamic banking.

Finally, customer selection for Islamic products and services is another important feature. Most Customers of Islamic banking do not have adequate knowledge and awareness of the Islamic banking products and their compliance with Islamic principles, which negatively impacts the development of these banks (Mylenko & Iqbal, 2016). Government support and well-planned initiatives to educate and aware potential customers of Islamic banking products and services would probably have a positive impact on the development of Islamic finance (Mylenko & Iqbal, 2016).

1. 2 Research Question

Based on the research problem explained above, this study is going to answer the research question, which is structured as bellow:

What are the distinguishing features of Islamic banking in Afghanistan?

1. 3 Research Objectives

Current political and security instability in Afghanistan have negatively impacted the finance sector as well as economic growth. There might be some investors available in Afghanistan or are in aboard but they are afraid to return and invest because of security concerns. On the other hand, due to lack of awareness about products and services available by Islamic banking, entrepreneurs and businesspersons may intend to start new businesses by the help of Islamic financing. If Islamic banking products and services attract investors to make new investments in Afghanistan, it will help to decrease unemployment rate and increase economic growth.

Based on the literature section, it is clear that many study has been done already in Islamic banking area in other Islamic countries such as Malaysia, but as it is a new and recent development area in Afghanistan, therefore; this study will be done for the first time in Afghanistan. Thus, this paper will become part of this development and research in this area.

The objective of this study is to explore Islamic banking distinguishing features in private banking sector which will help Muslim investors, customers, government officials, bank heads, economists, and especially Islamic banking students to learn more about the private banks providing Islamic banking products and services, number of customers, the challenges and benefits of Islamic banking for the banks and society and other related concepts by exploring its features.

1. 4 Research Importance

The general topic area of this research is Islamic banking that manages huge amounts of money complained to Islamic principles. They can play a pivotal role in economy of Islamic communities. Banks are providing financial services through deposits and loans through two types of banks, conventional and Islamic. While conventional banks that operate

based on interest income, Islamic banks work as Islamic financial institutions that provide Islamic banking services based on the profit and loss sharing principle of Islamic law.

As a source of finance, Islamic finance and banking is growing and becoming important for Muslim investors around the world, especially for Muslims living in Middle East and southeastern Asian countries, who are uncomfortable with the western financial system, which involves the interest factor.

Afghanistan is an Islamic country and most residents are Muslims. They believe in Islam and based on Islamic principles, interest is forbidden and not permissible. After Afghanistan stepped into the global Islamic financial industry, Islamic finance system becomes a very important topic. It is new concept and fastest growing sector in Afghanistan's financial services market since last couple of years. Specifically, from the increase in the number of Islamic banking windows in banks in recent years and launch of the first full-fledged Islamic bank, Bakhter Bank, it can probably be inferred that the number of clients of Islamic banking is increasing. However, still there are many people who are unaware of such services.

1. 5 Research Scope

The specific scope of this research is finding out about the features of the Islamic banking in Afghanistan and then examining the challenges and advantage it will have for the bank and economy of the country. As there is not a bank available that operates only on the pure Islamic system, there are conventional banks with providing Islamic banking windows as well as Bakhtar bank is recently going to become the first full fledge Islamic bank in Afghanistan so this study will be done on Islamic banking windows available in banks and specifically on Bakhtar bank in the private sector.

1.6 Research Limitation

Security and study participant's attitude and coordination are the anticipated limitations in this study. The current security situation makes it difficult to visit banks and gather data from the participants. As not much research has been done in Afghanistan, the concern is the participant's cooperation and their on time response to the survey.

Chapter Two: Literature Survey

This section presents a broad overview of Islamic banking in terms of Islamic laws, prohibition of interest as the main principle of Islamic banking, the profit and loss sharing principle that clearly distinguishes Islamic banking from conventional banking, key Islamic instruments used in Islamic banking in different countries around the world, Islamic banking performance efficiency, Islamic banking economic growth, challenges of Islamic banking, Islamic banking comparison with non-Islamic banking, Islamic banking customers and satisfaction rate, and Islamic banking and risk management.

2. 1. 1 Islamic Banking Principles and Key Instruments

There are five foundation pillars of Islam namely, testimony of faith, pray, Ramadan, zakat, and hajj (Schumm & Kohler, 2006). Islam is not restricted to these five pillars (Basah & Yusuf, 2013). It covers all other areas of daily life. Every activity is counted and its good side is rewarded. In a business, profit is not supposed to be the main driver but also is about social benefits to society and development of community. There are interrelationship between the personal and public life of an individual that means every individual should consider Islamic principles while doing business, or taking any decision living in any Muslim or non-Muslim community (Basah & Yusuf, 2013). Such that relationship exists between five pillars of Islam and economic activities for example Zakat is the third pillar of Islam that support social and economic justice in a community (Basah & Yusuf, 2013). Zakat encourages wealthy part of community to share their wealth with poor portion of the community.

Ali and Myles (2010) in their study of exploring consequences of Zakat to accumulate capital related it as the foundation for financial activities such as financial and legal taxation (NORULAZIDAH PH OMAR ALI & Myles, 2010). Moreover, Hussain, Shahmoradi and Turk (2016) stated that beside the five pillars of Islam, there are three major principles of Islamic finance:

- **Equity principle:** this principle is based on three points, first; ban of predetermined payments or interest during the Islamic transaction to protect both parties in the contract from risk and share the profit between them in a fair manner. Second; this standard of equity is also based on prohibition of excessive uncertainty, means that both parties, investor and depositor, will have a clear disclosure of information about the contract so that the money of depositor is not going invested in activities with excessive uncertainty. Third; this principle is based on 2.5% of in-kind wealth or tax on cash on some specific income for the purpose of social prosperity (M. Hussain, Shahmoradi, & Turk, 2016).
- **Participation principle:** partnership or any contract based on Islamic principles is not only based on profit sharing but also based on risk sharing so this principle is based on to check that profit shared is from a productive investment (M. Hussain, Shahmoradi, & Turk, 2016).
- **Ownership principle:** this principle is based on real asset financing in other words, someone cannot use a property unless it has the right so the property right preservation is highly valued in Islamic principles (M. Hussain, Shahmoradi, & Turk, 2016).

The foundation of Islamic banking is based on Sharia law which is the legal system for Islamic banking (Bakar, 2010). Bakar (2010) classified sharia law that is foundation of Islamic banking into five following categories:

- Riba or abandon of interest.
- Gharar or prohibition of investment in uncertain project such as gambling.
- Zulm or ban of cruel behaviour in business and all other areas.
- Zakat or tax payment based on Islamic principles.
- Haram or avoidance of taking part in producing products and services that are against the Islamic law.

Based on Makhlof (2017) an overview of the Islamic banking industry in Middle East and North Africa (MENA) region, Egypt is the first country that started Islamic banking in 1960 with a slight growth all these years; however, other countries that stepped in Islamic banking market during 1970 and 1980 show a significant growth such as Saudi Arabia, Pakistan, Jordan, Yemen, Iraq, and Tunisia (Makhlof, 2017). According to table one, Pakistan is leading the Islamic banking market with five full-fledged Islamic banks and twelve conventional banks with Islamic banking windows, additionally; Iraq had 10 full-fledged Islamic banks but due to war none of them operate anymore. In recent years, while Islamic deposit activities have significantly grown in most of the countries in MENA region, there are countries such as Yemen and Iraq that political issues negatively impact their economy and Islamic banking activities (Makhlof, 2017). According to table two, Saudi Arabia had the highest growth in assets and deposits in the period of three years from 2010 to 2012.

There are five basic principles for Islamic finance interest prohibition, relationship between asset and finance, prohibition of investment in prohibited unethical activities such as alcohol production, and relationship between risk and return (Mylenko & Iqbal, 2016).

Islamic banks play an attorney or intermediary role between investor and capital supplier, who get fee for providing resources to investor from the depositor side and evaluate

the contract between two of them and finally transfer profit or loss proportion from the investment to the capital supplier (Bidabad & Allahyarifard, 2009). Investment with earning fair profit as well as social value, competence with Islamic law, and social justice are known as basic criteria for Islamic banking (Zaher & Kabir Hassan, 2001).

The essence of Islamic finance and banking is based on five main principles as follows:

- Preferring risk sharing over risk-shifting
- Prohibition of social and economic misuse
- Enhancement of ethical standards
- Development of social values
- Promoting prosperity by linking risk with profit

Prohibition of Interest is one of the Islamic banking principles. Shihata (2000) explained Riba or interest: Riba is the root word of Riba or interest in Arabic language that means additional increase to the principle amount; in other words, Riba or interest is religiously forbidden which is the amount earned by lending money or exchanging goods (Shihata, 2000).

The key principle of Islamic banking is ban of interest, earning money from money, which is a fundamental principle in Islamic finance (Abdalla, 2015). Earning money without taking part in risk and loss for the lending it is forbidden because money should be earned through taking part in trade or investing money, it can be only and only permitted for fair transactions that obey Islamic principles such as profit and loss sharing (Abdalla, 2015). Abdalla added more in his study of investigating banks that though the lender or depositor who supplies capital for an investment through bank has the right to be rewarded, for the purpose of fairness, the reward not only should be based on profit but also the risk and loss as

well as it should not be prefixed. He found that there is difference between profit and interest and summarized some of them as follows:

- Interest is extra money above the principle amount that a borrower should pay to the lender, however; profit is the earned income minus cost associated from the production.
- Interest is predetermined and based on certainty but profit is post determined and uncertain until cost is measured.
- Interest amount is always positive but profit can be negative amount due to excessive costs.
- Interest can have a positive impact on money supply in the market that can cause inflation but profit does not have a relation with money supply, consequently; neither increase nor decrease money supply in the market.

The issue of interest in Islamic banking is based on the conservative thoughts and knowledge of those who presents Sharia in in a society that whether they ban all forms of interest or some forms of it (Kamla & Alsoufi, 2015). According to Kamla and Alsoufi, Islamic banks provide innovative products that compliance with Sharia, however; to avoid the interest issue (Kamla & Alsoufi, 2015).

On October 2015, Oniango researched about the profitability factor of interest free income in Kenya. In this descriptive study he used regression for the analysis of the data that he gathered from 43 banks and found that there is a positive relation between interest free income and bank profitability (Oniango, 2015). As his data-gathering source was only the financial reports of the banks, it limited his study because financial reports do not provide complete information about the overall productivity of the bank. One of the points the

mentioned in his study is quite interesting that there is lesser risk in interest free income compare to income based on interest (Oniango, 2015).

The definition of interest or Riba is, “ To increase, to augment, swellings, forbidden “addition,” to make more than what is given, the practicing or taking of usury or the like, an excess or an addition, or an addition over and above the principal sum that is lent or expended” (Van Greuning & Iqbal, 2008).

Another key principle is the profit and loss sharing principle. The idea behind profit and loss sharing is that financial transitions accompany return and risk so the capital supplier should be taking part in both rather than only in return which is interest and banned in Islam, therefore; based on the profit and loss sharing principle, lender has the right to ask the intermediary, the bank, to provide information about the risk involved in the investment and evaluate the borrower and its activates to succeed (Abdalla, 2015).

Though Quran forbidden interest, it permits fair profit of an investment through a bank based on a rule (S. Hussain, Malik, & Bhat, 2015).The rule is that the lender or depositor invests his/ her money through intermediary or the bank to a borrower and should be included in the loss and profit of the investment with the borrower. This rule is against the conventional bank where the lender gives his/ her ownership to bank and bank works as a partner with borrower that the lender is only included in profit and takes a fixed share of profit that is accepted prior to the investment. Hussain, Malik and Bhat also added that with this rule there is a risk of loss to be shared with the lender so the role of bank is essential to have a good system to evaluate the borrower’s ability to succeed in his/ her business and return the bank principle and some profits so that they can earn the confidence of the lender (S. Hussain et al., 2015).

Bidabad and Allahyarifard (2009) believe that there is excessive lack of one definition and point of view for interest in different culture context and Islamic banks in different countries as well as lack of management, operations and supervisory systems impacted Islamic banking that created problem to develop (Bidabad & Allahyarifard, 2009). According to this study, reason for these problems is that these banks could not been able to use profit and loss sharing principle practically. This study found that by the help of profit and lost sharing system, Islamic banks announced two new innovative means for projects with specific time to end and those projects that their end time is not specific respectively specific end partnership or Musharakah as well as productive endless contracts or Pazireh. In addition, this study classified the elements of profit and loss sharing as shown in table three.

Key instruments of Islamic Banking are essential part of Islamic banking. Table four shows that Islamic finance instruments are divided to two parts based on its contractual feature as transactional Islamic contracts such as Qard Hassana, Murabaha, Bay Salam, Bay Mua'jal, Ijara, Istisna, and Musharaka, as well as Islamic intermediation contracts such as Mudarabaha, Kifala, Amana, Takaful, Wikala, and Ju'ala (Grais & Iqbal, 2004). Based on this study, the classification of Islamic instruments based on contracts develop economic activities by exchanging, trade and financing of these activities with the support of Islamic transactional contracts, additionally; efficient and transparent implementation of transactional contracts need existence of intermediations contracts (Grais & Iqbal, 2004). Islamic instruments and contracts are categorized in three different categories of financing, investing and others that each category is divided to other sub categories (Van Greuning & Iqbal, 2008). According to table five, main Islamic instruments are:

- Murabahah (Cost-plus-Sale)
- Bay' Salaam (Forward Sale)
- Bay' Muajil (Deferred Payment Sale)

- Ijarah (Leasing)
- Istisnah (Manufacturing)
- Mudarabah (Principal/Agent Partnership)
- Musharakah (Equity Partnership)
- Kifalah (Guarantee)
- Joalah (Fee-for-Service)
- Amanah (Custody)
- Wikalah (Representation)
- Qard Hassan
- Waqf
- Tikaful (Insurance)

Moisseron, Moschetto and Teulon classified major Islamic instruments based on the operations into three categories (Moisseron, Moschetto, & Teulon, 2015):

- Participatory operations
 - Modarabaha
 - Mushrakaha
- Operations without counterparts
 - Qard Hassana
- Commercial operations
 - Murabaha
 - Salam
 - Ijraha

According to Moisseron (2015), the first category is participatory operations instruments which are known as heart of Islamic finance however the commercial operations

instruments can function in even non Islamic environment (Moisseron et al., 2015). Another recent study found that the core instruments of Islamic banking are Murabahah, Ijarah , Mudarabah, Musharakaha, Bay' Mu'ajjal , Bay' Al-Salam, Sukuk (Mylenko & Iqbal, 2016).

Another study in same year found and explained efficiently the most used and important Islamic instruments such as Amana (demand deposits), Bay Mu'ajjal (pre-delivery, deferred payment), Murâbahah (mark-up financing), Ijârah (lease, lease purchase), Salam (prepayment, deferred delivery), Istisna (deferred payment, deferred delivery), Ju'ala (service charge), Kifala, Mudârabah (trustee finance contract), Musharakah (equity participation), and Qard Hassan based (beneficence loans) on table six (M. Hussain et al., 2016).

2. 1. 2 Islamic Banking Performance Efficiency

Measurement of efficiency and performance of any organization is based on maximization of profit and minimization of risk. Based on Berger and Humphrey (1997) study, bank efficiency can be measured through parametric and non-parametric approaches but there is no consensus that which one of them is superior (Berger & Humphrey, 1997). There are three types of parametric measurement approaches stochastic frontier approach, data envelopment analysis and the meta-regression analysis (Iršová & Havránek, 2010).

Financial ratios such as profitability, liquidity, efficiency and solvency can be used to measure performance of a bank (Saleh & Zeitun, 2006). This study found that profitability of Islamic banks increased in short term. Another study by (Samad, 2004) found that the remarkable difference between interest free and with interest banks in their credit performance and there is not much difference in their profitability and liquidity.

The theories above about Islamic banking efficiency and performance, based on different studies done, presented evidence that Islamic banking has less risk and more profits in stable environment than other bank systems. However, the competency of Islamic banking

is lower compared to conventional banks because their products are limited. The data of these studies were based on banks that were completely on Islamic rules or in pure conventional banks. The current study may extend the evidence of efficiency based on Afghanistan conventional banks which parts of their operations is functioning as Islamic banking. It might be challenging to compare different activities of one bank as conventional as well as Islamic banking window because there is not any bank available that provides only Islamic banking services. In addition, while different studies used different approaches of efficiency measurement, these measures can be done for studying banks from different dimensions such as technical and managerial.

Different methods can be used to do a research about the performance of a bank. One such empirical study is done by Imtiaz .P. Merchant at Global Journal of Management and Business Research (Merchant, 2012). He used quantitative method to study six performance parameters capital adequacy, asset quality, management quality, earnings, and liquidity and named it CAMEL (Merchant, 2012). The result of the study shows that there is not exist any significant difference between liquidity and asset quality of Islamic banks and conventional banks (Merchant, 2012). For the purpose of better understanding of performance efficiency, the study proceeded with examining the data before crisis and after crisis. The results showed that Islamic banks had high liquidity, which may lead to low profits, which result in less investment opportunity (Merchant, 2012). However, for the purpose of assessing performance of Islamic banks, Akhter, Raza and Akram (2011) study in Pakistan used trend analysis tool in order to check the trends of balance sheet and income statement (Akhter, Raza, & Akram, 2011).

2. 1. 3 Islamic banking Impact on Economic Growth

During the last decade, every year Islamic banking has an average growth rate of (10 to15) % and it is forecasted that this trend will continue to grow in next coming years (Bidabad & Allahyarifard, 2009). According to the Celebi, Hassan and Zirek study of the Islamic banking role in economic growth, there is a positive relationship between Islamic finance and economic growth in the short term(Furqani & Mulyany, 2009; Zirek, Celebi, & Hassan, 2016).

Another study used different growth indicators to explore the relationship between Islamic banking and economic growth (Ahmad & Hassan, 2007). This study used traditional indicators such as gross domestic product (GDP), the investment share of GDP, and the population as well as it used domestic interest rates along with the percentage of Muslim population. Additionally, banking variables such as real interest rate, deposit interest rate, lending interest rate are included. Finally, the ratio of total assets in banks to GDP, variable that indicates financial depth, is also included.

According to Furqani (2009), financial development and economic growth are connected to each other in three ways. Firstly, development in finance function as a determinant of growth in economy. Secondly, development in finance follows growth in economy. Finally, the causality between finance and growth is bidirectional (Furqani & Mulyany, 2009).

Bley and Kuehn in their study in 2004 surveyed Arabic and non-Arabic students studying business in Sharjah, United Arab Emirates to check their understanding of Islamic banking. As the primary finding, the main reason of Muslim students for preferring Islamic banking is their religious beliefs (Bley & Kuehn, 2004). Their secondary finding reveals that the level of knowledge of Islamic banking in Arabic students was higher than the non-

Arabic/Muslim students' in contrast non Arabic Muslim students had more knowledge about conventional banks though.

2. 1. 4 Challenges of Islamic Banking

Availability of developed financial markets, cooperation among Islamic institution, Islamic products, one united Islamic law for all Islamic banks operating in different countries in the world, and interest prohibition terminology are the main challenges of Islamic banking (Zaher & Kabir Hassan, 2001).

A study done by Garas and Manama (2007) found that there are two types of challenges for Islamic banking, internal and external. While the internal challenge is the competition with conventional banking products, due to lack of a complete Islamic regulatory system the external challenge is fulfilling the international transaction requirements (Garas & Manama, 2007). From this study, it is obvious that there is a relationship between efficiency and competition so if a system has a complete regulation system then it can compete well and consequently its efficacy will grow.

Problems in Islamic banks are discussed in an empirical study of Mansoor Khan and Ishaq Bhatti (2008) in Pakistan. Firstly, they found that Islamic banks still need development and research, as there have not been many research and development programs (Mansoor Khan & Ishaq Bhatti, 2008). Secondly, liquidity problem in Islamic banks is a result of lack of availability of wide ranging products in investment area so there is around 40 % more liquidity in Islamic banks in contrast to conventional banks (Mansoor Khan & Ishaq Bhatti, 2008). Another point they found was the lack of Islamic law experts in banking industry. Finally, the challenge rose by different interest rates and liquidity risk impacted the development of Islamic banks risk management strategies.

Baker (2010) explored some challenges that Islamic banks face and listed them as, "sharia's interpretation versus the financing commercial viability, legal jurisdictions and governing laws, transparency, accountability and governance for public and private sectors, tax incentives, pervasive government intervention and controls, supervisory and prudential regulatory framework, lack in depth capital markets and liquidity funding, accounting and auditing standards." (Bakar, 2010).

According to Makhlof (2017), though Pakistan, neighbor country with same religion, has full support of the government and show high development rate in Islamic banking but faces some primary challenges such as high cost for operations management and high risk of non-performing loans which result in lack of good risk management policy and Islamic banking infrastructure. However; there should be a research to find out that are these factors mentioned in their study are general problems that may apply in Afghanistan or there are other specific factors such as security and political issues exist that will negatively impact the development of Islamic banking in Afghanistan? What other specific problems might be in Islamic banks in Afghanistan?

2. 1. 5 Islamic Banking Verses Non-Islamic Banking

In comparison of Islamic banks and non-Islamic banks, study done by Shah (2012) found that Islamic banks are more efficient technically in loan base approach than conventional banks as well as scale efficiency of Islamic banks are better than conventional banks, however; in terms of income base approach Conventional banks are better than Islamic banks. They conducted this research study by estimating efficiency of Islamic banks and convention banks and found similar results (Shah, Shah, & Ahmad, 2012).

Based on Olson and Zoubi (2008) study, though Islamic banks and conventional banks provide same services, there are some differences that distinct them from each other

(Olson & Zoubi, 2008). Firstly, operation of Islamic bank is based on Sharia law of risk and profit sharing that result in interest prohibition so their agreement with depositors and lenders is based on profit and loss sharing (PLS). Secondly, to share profit and loss with depositors, Islamic banks through one of their products, Mudaraba, invests deposits of public funds. Thirdly, to become part of lender's profit and loss, business owners or lenders can borrow funds from Islamic banks through using one of their products Musharaka. They agree with banks to share profits and loss with them based on agreed ratios. Fourth, once banks receive profits or loss from investments in different areas, they share these profits or losses based on agreed ratios with their depositors. Fifth, the main operating drivers of Conventional banks debt and equity financing but Islamic banks operate based on equity financing and customer deposit accounts. Sixth, in conventional banks cost of debt and equity is depended on cost of capital but in Islamic banks, it is replaced by profit and loss sharing principle. Finally, though there is more return on equity variability exist in Islamic banks than in conventional banks, however; there is not exist default risk of not paying loan again (Olson & Zoubi, 2008).

Though study of Olson and Zoubi (2008) explained the difference between the operating structures of both banks and found that there is not a big difference in the operating structure of these banks so they can be distinguished by their annual balance sheet report and financial ratios (Olson & Zoubi, 2008).

Bakar (2010) distinguished Islamic banks from conventional banks in term of the following points (Bakar, 2010):

- **In terms of operating modes:** while operating means of conventional banking is based on manmade laws, Islamic banking is based on Islamic principles made by Allah.
- **In terms of risk sharing:** while conventional banking transactions are based on only

profit sharing based on predetermined rate of return, Islamic banking transactions are based on both profit and risk sharing and predetermine rate of return or interest is strictly banned.

- **In terms of profit maximization:** while there is no restriction on profit growth aim of conventional banking, Islamic banking aim is to grow profit too but considering Sharia law and restriction.
- **In terms of service oriented functions:** while conventional banking does not have any system for tax payments such as Zakat, Islamic banks collect Zakat from customers and itself pay Zakat.
- **In terms of fundamental function:** while the core function of conventional banking is lending and accepting returns as compounded interest rate such that money is the core motivation, in Islamic banking partnership is the main function of the bank as both parties invested and depositor share profit and risk in this partnership so learning about each party is the motivation.
- **In terms of defaults:** while conventional banks in case of defaults charge penalties, there is no charge or penalties for defaults in Islamic banks except for the case compensation to charities.
- **In terms of growth with equity insurance:** while in conventional banks the main aim for the bank is their own interest so they do not care about growth with equity, Islamic banks main function as mediator between investor and depositor so its main aim is the giving attention to public so they are more concern with growth and equity.
- **In terms of investing projects:** while there is predetermined interest rate is fixed by conventional banks so they show little interest in evaluation of investing projects as well as they pay more attention to the power of credit paying of customers, Islamic banks shoe more interest in appraising and evaluating investing and developing

projects as well as they viability of the project is more important for them than credit worthiness of the customers.

- **In terms of relationships:** while conventional banks have a creditor and debtor relationship with its customers and clients, Islamic banks have a relationship alike investor and trader with its clients or in other words alike partners or buyers and seller.
- **In terms of guarantee:** while conventional banks guarantee all deposit accounts of the clients, Islamic banks guarantee clients deposits of their funds based on the principle of Al Wadiha however, client having accounts based on Mudraba'ha are not guaranteed.

Based on (Moisseron et al., 2015) there are four main differences between Islamic banks and conventional banks:

- In terms of currency: while conventional bank and Islamic banks both use currency through trade but do not value money as asset, in contrast conventional bank value money as asset or in other words, Islamic banking system has an interest free monetary policy framework.
- In terms of nature of operations: while conventional banks do not allow depositors to know about where their money is invested or how it is used, and do not have the right to select their preferred investment, Islamic banks provide this opportunity for depositors and there is a relationship between investor, bank and depositor where bank plays as mediator role between them.
- In terms of logic of transactions: the difference is that transaction in conventional banks is through financial assets while in Islamic banking it is through real assets.
- In terms of payment: while conventional banks collect funds from customers through interest, Islamic bank does not allow interest and the partnership is based on profit

and loss sharing.

2. 1. 6 Islamic Banking Customers and Satisfaction Rate

Regarding customer satisfaction in banking sector in Turkey, Okumus (2005) done a study with focusing on the satisfaction degree of customers as well as on the customer awareness degree of Islamic banking products and services (Okumus, 2005). One of the most important findings was similar to Bley and Kuehn (2004) study findings that religious belief is the primary motivation to use Islamic banking services and product (Bley & Kuehn, 2004). Furthermore, according to (Okumus, 2005), customers preference on selecting a bank is based on the following factors:

- Bank location distance from the customer accommodation.
- Service quality and the variety of services offered by the bank.
- External and internal representation of the bank and available comfort such as parking space and internal design of bank.
- Staff behavior with customers.
- Lower service charges and interest charges on lending.
- Higher interest rate on savings.
- Reputation, confidentiality and confidence level of the bank.
- Counseling services and reception programs arranged by banks.
- Marketing and advertisement strategy.
- Family and friend's recommendation related to specific bank.

In addition, (Okumus, 2005) found that customer selection of the bank is depending on three specific criteria of whether which bank provides favorable conditions for credit, which bank provides lower service charges and interest rate charges for cheque and lending respectively, and which bank provides higher interest rate for savings.

In contrast, another study on how differences in demographic features can impact the decision of customers about selection of Islamic banks in Bangladesh run regression analysis to find the relationship between these demographic features and factors impacting selection of bank (Rashid & Hassan, 2009). This study found that mainly there are four customer demographic features, age, educational background, gender, and marital status that have high relationship with general features of the bank that is not specifically related to Islamic banking only such as service quality, confidence level, and bank performance efficiency (Rashid & Hassan, 2009). According to (Rashid & Hassan, 2009), while efficiency and confidence level factors were selected as major feature for selection of the bank by almost all demographic groups, however, interestingly quality of service have higher relationship with female and married customers selecting the bank, additionally; the study suggests some ways for the development of Islamic banking such as online banking services, more innovative marketing efforts, and qualified personal.

Similarly, another descriptive study in Malaysia studies customer preference factors of the Islamic banking how emergence and growth of technology as well as high expectation of customers played vital role in increasing competition standards in banking sector (Haque, Osman, & Ismail, 2009). According to (Haque et al., 2009), the most influential factors specifically for Islamic banks of their customer selection of the bank were:

- High service quality
- High confidence level of the bank
- Religious and social factors
- Service availability

Moreover, this study revealed that customer satisfaction is the key measurement tool for the bank performance, and quality service is the most influential factor known for the customer

satisfaction but negative perception of customers regarding confidence level of the bank can have a significant negative impact on customer satisfaction (Haque et al., 2009).

Another study done by Wajdi and Irwani, in their study of motivational factors for attracting customers in 2007 in Malaysia found that service quality, product price, religious beliefs, convenience, financial reputation and having social responsibility activates are the key factors that motivate customers to select Islamic bank (Wajdi Dusuki & Irwani Abdullah, 2007). Furthermore, this study recommends that quality service offering is the main factor for enhancement and good reputation of Islamic banks (Wajdi Dusuki & Irwani Abdullah, 2007).

Similarly, Kumar, Tat Kee and Charles studied the quality service delivery difference between Islamic and non-Islamic banks in 2010 by using SERQUAL model. Based on this model they found that there are four main factors that two of them, competence and convenience, are notably different in the mentioned banks that have a significant impact on the productivity of the bank (Kumar, Tat Kee, & Charles, 2010). In addition, the study found that the expectation of customers from Islamic bank in term of these two factors is significantly higher than non-Islamic banks (Kumar et al., 2010). However, the other two factors, tangibility and reliability, expectation of customers from conventional banks are much more higher than Islamic banks (Kumar et al., 2010). This study concludes that quality service gap is due to lack of attention, prompt services, convenient operating hours, special counters for people with special circumstance such as elder and disabled clients as well as lack of research and development for understanding their customers preference and needs (Kumar et al., 2010).

Another study done by (DOGBE, 2011) by using same method for analysis used by Kumar, Tat Kee and Charles in 2010. He studied the impact of service quality on customer satisfaction. In contradiction to the previous study results, the response from customers and employees of this study revealed that tangibility among the all other four factors (assurance,

empathy, reliability and responsiveness) is the main quality service-delivering factor to customers because any defect in tangibility factor will significantly impact the entire bank service quality. One of the recommendations for surviving in the competitive banking industry is being dynamic by responding to customer's need as soon as possible and reliability (Kumar et al., 2010).

2. 1. 7 Islamic Banking and Risk Management

According to Van Greuning and Iqbal (2008), four major risks threaten an independent bank: financial risks, operational risks, business risks and event risks. There are three vital steps in managing risk: firstly, setting objectives for risk management; secondly, identifying the target of risk management; thirdly, measurement and assessment of the operations structure; fourthly, recognition of the risk factors; and lastly, setting the extent degree of risk threatening the bank (Van Greuning & Iqbal, 2008). Van Greuning and Iqbal (2008) explained the process for the effective risk management for the banks in large competitive markets that function in economies that are instable and have changing environment, it classified the effective risk management process steps as below:

- Existence of risk management expertise in the high management team to manage risk and assess operations based on the policies and regulations.
- Establishment of an explicit strategy for risk management.
- Formulation of strategic decision for risk management.

Islamic banks beside the general risk that they are facing with conventional banks, they are coping with other risks such legal risks, credit risks, liquidity risks, operational risks and market risks exposed by the two features, sharia compliance of assets and liabilities, that differentiate them from conventional banks (M. Hussain et al., 2016). Furthermore to mitigate these risks Islamic banks practice only those measurement tools of the conventional banks that are not in contradiction to the Islamic principles such as internal rating and control

systems, external audits, matching of the maturity, GAP analysis, and risk reports, however; these measurement are not satisfy risk management measurement and there is need for extra measurement tools to satisfy risk management measurement specifically exposed to Islamic banking (M. Hussain et al., 2016).

Though implementation of Islamic principles protect Islamic banking from high risk degrees such as Islamic banking is more resilient facing some risks than conventional banking because the principle of equity protect the bank from investing in high risky and uncertain projects, however; the principle of ownership limits Islamic banking to invest in high leveraged investments such as short selling which may result in high financial risk in future (M. Hussain et al., 2016); furthermore, this study suggests three main solution to overcome the financial risk and develop Islamic banking financial system:

- **Liquidity infrastructure development:** liquidity infrastructure enhancement can help to manage risk by liquidity, help central bank to manage liquidity and monetary operations.
- **Supervision and regulation framework:** regulation framework is a very important in Islamic banking to provide standards for Islamic banking so that based on these frameworks Islamic banks are able to cope with risks such as loss sharing standard.
- **Financial safety infrastructure:** in times of distress it is very important for Islamic banks to have financial safety infrastructure and develop it time to time so that to have emergency financing system and deposit insurance so that to survive in high financial risky situation and react resiliently to financial distress.

2. 2 Conceptual Approach

This study is attempted to explore the features of Islamic banking in Islamic banks operation in Afghanistan. The current situation of Afghanistan is evidence of political and economic instability, however; there are some developments in banking sector especially

Islamic banking such as this year Bakhatar bank turned the first full-fledged Islamic bank in Afghanistan history. Based on the theoretical approach, this study is considering five main features as conceptual approach that can have influential impact on the operation and productivity of Islamic banks.

Based on (Sole, 2007) there are seven main features of Islamic banking

- Product and services compliance with Islamic principles
- Funds circulation system
- Accounting and auditing standards system
- Legal and regulatory aspects
- Transparency
- Awareness
- Disclosure

According to this study, sharia compliance promotes existence of sharia board and expertise that result in consistency by minimizing sharia risk. The second feature to be considered is its funds circulation system that should be different from non-Islamic banking system to insure that these funds are not involved in interest or other related activities that are against the Islamic principles. To ensure that accounting and auditing system obey Islamic principles, Islamic banks should make sure that they follow these the standards that are designed by Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI). As the forth criteria, two aspects should be taken in account for contracts and financial transactions, firstly; legal aspect while making contracts, secondly; regulatory aspect while making financial transactions. Other three features of transparency, awareness and disclosure are very important characteristics for the success and surviving of Islamic banking in banking industry. A similar study by Henry Chalu explored four main characteristics of Islamic banking as follows (Chalu, 2014):

- Compliance with Islamic principle of finance
- Customer selection
- Structure
- Competence of Sharia Supervisory Board (SSB)

This study covers some of the previous study main features and emphasize on customer selection. According to this study, the most distinguishing features are:

- Accounting and auditing standard system
- Customers knowledge of Islamic principles'
- Customer awareness of interest-free banking
- Islamic funds separation from conventional funds
- Alignment between employee's attitude and Islamic principles.

This study also found that there are some other features that do not distinguish Islamic banks from other banks, which is a contradictory finding compare to the study of Sole (Sole, 2007). According to (Chalu, 2014), these less impactful features are:

- General activates compliance with Islamic principles
- Ethical issues
- Customer's reasons for the selection of Islamic banks
- Customer's attitude
- Financial information disclosure
- Existence of Sharia Supervisory Board (SSB)

According to (Kammer et al., 2015), Sharia compliance is one of the important concerns for the Islamic banks that needs supervision of the regulators to check Islamic bank framework compliance with Islamic principles and Sharia board members expertise because these two points can have impact on trust that is why AAOIFI and IFSB recommendation is the existence of Sharia Supervisory Board in each Islamic bank that play the internal and

external system reviewer role in the bank.

2. 2. 1 Islamic Products and Services Compliance with Islamic Principles

In a recent empirical descriptive study of Islamic banking in Malaysia based on the data collected from the executives of Islamic banks, one of their finding is that it is essential that Islamic banking products and services should be complained with Sharia principles, however; ethics in banking sector should be considered beyond sharia compliance (Musa, 2015).

Another study efficiently studied the support of Islamic banking in terms of religious and social benefits in the community and its relationship with Sharia law compliance in Libya (Masoud, 2014). According to this study, the foundation of Islamic finance is based on Holy Quran, which is a complete guideline not only for people but for every area including Islamic banking (Masoud, 2014). Furthermore, the study found that in Libya, some Islamic banking products with in compliance with sharia law such as Islamic insurance, bond, financial charges, loans, and other financial products are developed effectively to compete in high competitive environment(Masoud, 2014).

Thus the two major features of Islamic banks are the degree of transparency in complaining their products and services to the Islamic principles as well as their engagement in social and welfare activates in community (Ali & Ahmad, 2007).

2. 2. 2 Accounting and Auditing

Abdalla (2015) found in his study that existence of expertise in accounting and auditing department of Islamic banking is necessary as they need to check whether the products they provide obey the Islamic principles or not (Abdalla, 2015). This study also emphasize the role of AAOIFI that can impact the growth Islamic industry by providing Islamic products that can be acceptable cross border in different countries. Consequently,

there will be more consistency worldwide and Islamic industry will grow significantly (Abdalla, 2015).

(Van Greuning & Iqbal, 2008) The existence of audit committee is essential for comparing Islamic principles with internal system of the bank, accounting activities and information system to address issues related to risk, corporate governance problems, and issues in bank's control system. Safieddine (2009) summarized the main tasks of audit committee as follows (Safieddine, 2009):

- Providing data about expected risk for the management team.
- Evaluating the operations management in terms of its efficiency and effectiveness.
- Providing appraisal as a transparent and independent body.
- Assessing Islamic principles with regulation and policy of the Islamic banks.
- Examining the accounting system for the purpose of reliability.
- Functioning as investigating body for the line management staff.

Similarly Van and Iqbal (2008) explained the responsibility of the audit committee, firstly; their main task is to support management team in exploring and dealing with risks threatening Islamic banks; secondly, independent appraisals delivery is their second major task, thirdly; assessment of the Islamic banking to check its compliance with law and regulations set for the bank is their third important task; fourthly, the forth core task of audit committee is to assess the reliability of the information provided by accounting department or computer system in the bank; lastly, their last task is to function as investigators in the bank and provide necessary information to the line management (Van Greuning & Iqbal, 2008).

2. 2. 3 Legal and Regulatory Aspects

The central bank of each country has a vital role in providing clear rule and regulation policies for banks (Moisseron et al., 2015), and its main duties are as followings:

- In order to prevent variation in employment rate and inflation rate, central bank task is adjustment of money supply.
- Regulating commercial bank activities
- Providing facilities to mobilize savings
- Providing facilities to ideally share resources
- Reassuring that exchange rate policy issued by government is effectively applied in banks.

Beside the judicial law, government support is essential for the development of Islamic banking such as guidelines and prudential regulations (Makhlof, 2017). Based on Makhlof (2017) study of Islamic banking sector in Middle East and North African region countries, Pakistan, Saudi Arabia and Tunisia have full support from government such as favorable tax system, more chances for conventional banks to open Islamic banking window, more competition, and more opportunities for expansion products in compliance to Islamic principles. Makhlof (2017) added more that though Jordan and Morocco government provided medium support to their Islamic banking sector but government of Egypt, Lebanon, Iraq and Yemen failed to cooperate Islamic banking sector development.

2. 2. 4 Sharia Supervisory Board (SSB)

A study suggested that the existence of internal bodies such as Institutions offering Islamic Financial Services (IIFS) is essential to confirm the Sharia compliance in Islamic banks that has relationship with corporate governance in terms of interdependency, confidentiality, competency, consistency and disclosure of information of Islamic banking (Grais & Pellegrini, 2006). According to (Grais & Pellegrini, 2006), Sharia Supervisory Board SSB is one of the mentioned bodies that not only supervise the internal system but also the structure of the Islamic banks, moreover; this study classified the role of SSB to five main categories as following:

- Certify the permission for using new Islamic financial tools by ex-post sharia audit.
- Confirm the fulfillment of ex-ante sharia audit with transitions.
- Playing intermediary role between shareholders and investors by providing them advice for how to distribute profit or risk among them.
- Providing terms and conditions for measuring and paying Zakat.
- Verifying and prohibiting earnings that are in contradiction with sharia compliance.

Another similar study (Kammer et al., 2015), classified the Sharia Supervisory Board of Islamic banking to three core responsibilities as following:

- Supervise the sharia compliance of the bank framework
- Enhance financial system of Islamic banking
- Develop measurement for the analysis of Islamic banking.

According to Grais and Pellegrini, beside the sharia supervisory board SSB there are some other internal sharia review independent departments that reassure the confirmatory of sharia compliance in the Islamic banks, in other words they confirm sharia supervisory board SSB rules and regulations application in the management level (Grais & Pellegrini, 2006).

Furthermore, both sharia supervisory board and internal sharia reviewer departments go through some issues in Islamic banks; firstly, as they play the role of assessing body of the management process as well as decisions took by this level so it may create conflict of interest between management level and these bodies by interference and status of these departments which is an independency concern; secondly, lack of professional board members with required knowledge of sharia and financial knowledge in these assessing bodies is another concern raise the issue of competency (Grais & Pellegrini, 2006).

2. 2. 5 Islamic Banking Customer's Selection, Attitude and Awareness

A study in Kuwait studied response from the 429 customers as the participant of the study regarding their awareness of the Islamic products and services as well as to find out

about their expectations and satisfaction from the Kuwait Islamic Financial House (Naser, Al Salem, & Nuseibeh, 2013). This study researched to find out the reasons behind customers selection of the bank, level of satisfaction, and level of awareness (Naser et al., 2013). One of their finding is quite interesting that in Arabic countries usually selection of a bank is based on the culture for example, quality is seen not in the product but in the investor and dealer honesty and trust, the study also found that there are different reasons behind selection, awareness and satisfaction of Islamic banking as follows:

Firstly, selection of Islamic banks by their customers are based on their high level of:

- Confidentiality,
- Credibility
- Confidence
- Existence of Sharia Supervisory Board (SSB)

Secondly, customer satisfaction was based on:

- Parking lot facilities
- Degree of advertisements
- Appearance of the bank
- Architecture of the bank
- Customer awareness level

Significant portion of the respondent reveled unawareness of the Islamic products and services.

Another study based on the customer perception and factors for selection of bank in Malaysia found that customer satisfaction can have major impact on performance efficiency of the bank (Haque et al., 2009). Moreover, the main driver of customer satisfaction is bank ability to provide high standard quality and interestingly religious believe is not the main driver of bank selection by customers and their satisfaction (Haque et al., 2009).

Chapter Three: Methodology and Research Design

This part of the study explains the methodology, which consists of the primary and secondary data, approach used to gather data, the target population and sampling methods, design and tools of the research plan for analysis of the data, and limitations during data collection. The main goal of this research is exploring the features of Islamic banking in three private banks in Afghanistan.

3. 1 Primary and Secondary Data

Primary research data was collected based on survey of three banks offering Islamic banking products and services: Bakhtar Bank, Afghanistan International Bank (AIB), and Ganzanfar Bank, all are located in Kabul, Afghanistan. According to the Afghanistan Banks Association (ABA), Bakhtar Bank, established in June 2009, is the third largest bank in Afghanistan that will soon be the first full fledge Islamic bank of Afghanistan. Data from this bank is all based on their near future products and services. AIB bank, established in 2004, is the first private bank with providing products and services locally and internationally; however, they have limited services through the Islamic banking window (Karimi, 2016). Based on Afghanistan Banks Association (ABA), Gazanfar Bank started its operations in March 2009 and it is a full fledge commercial bank but have an Islamic banking window.

Secondary data for this study was gathered from selected private banks from their annual reports, reliable prior research papers done in this area, articles and journals available in reliable Internet websites, and books.

3. 2 Data Collection Approach

For data collection two survey questionnaires, one for bank employees and another for customers, were distributed in three selected banks.

The questionnaires were distributed in person to employees and customers, and relevant clarification was provided on spot in case of any confusion to respondents. The responses are collected from the respondents after completing the questionnaires by researcher on the spot.

3. 3 Target Populations and Sampling

The target population of this study is customers and employees of the selected banks with sample size of 100 each.

Purposive or convenient (non-probability) sampling method is used in this study to gather data from employees. As approaching bank employees and customers are not easy, this method is used because it is more convenient, accessible, and easier to gather data for researcher. Another reason for using this method was to gather reliable data from a selected portion of employees such as Sharia Supervisory Board (SSB) members so the informal focus group method was used by informal interview and observation.

To gather data from customer target population, random (probability) sampling is used for collection of data from customers of conventional and Islamic banking products and services.

3. 4 Data Collection Tools

To collect data two questionnaires were prepared, one for customers and another one for employees of the banks. The questionnaire for customers was designed to gather data regarding their level of awareness about Islamic banking, level of their satisfaction regarding the bank they do business with, and their attitude toward Islamic banking products and services. The questionnaire for employees included questions regarding the bank products and services compliance with Islamic principles, accounting and auditing aspects of Islamic banking, legal and regulatory aspects, and existence of Sharia Supervisory Board (SSB). For

the purpose of reference, complete employee and customer questionnaires in both English and Persian languages are attached to appendix of this thesis.

3. 5 Data Analysis

For the purpose of data analysis, the raw data obtained from the study is transformed into information such as codes and labels that can be easily analysed and results can be extract from. For example raw survey questions on a scale of 1 to 5 were coded as such, and developed summaries are made based on statistical inferences. For this purpose, first step is taken to ensure participants consistency by editing the raw data to identify possible errors, thus, to correct them. Another step is taken to code or label the raw data that helped to group participants in categories as well as for the analysis of open-ended questions.

As a quantitative approach, statistical tools such as frequency and percentage are used to analyze the primary data, and to find about the quality of products and services provided by private banks in Kabul, the speed rate of its attracting customer and the impacts it has on society as well as on economy. In addition, Microsoft Excel software is used to present data in graphical and narrative forms by the usage of descriptive statistical tools such as frequency tables, and bar charts.

3. 6 Limitation during the Data Collection

Some unexpected security issues caused delay in data collection and data size. Most customers did not come to banks after the blasts due to security and road traffic issues. For many days, female staff of the bank were off duty. The sample size for this study was to be hundred for each survey. However, the sample size of this study decreased only forty one employees and thirty four customers participated due to very limited availability of customers during the data collection period after the attack.

Some other limitations such as lack of research culture and cooperation in the Afghani culture caused an accessibility problem with the bank employees. Some employees hesitated to share data, due to confidentiality policy of the banks.

Chapter Four: Empirical Analysis and Findings

This part of the study presents the analysis of the primary and secondary data based on which the research questions are answered and discussed in the discussion part and the results from the discussion are presented in the findings part.

4. 1 Data Analysis

For the purpose of analysis of the primary data, gathered from employees and customers, data is grouped in categories for each survey separately (employee survey is grouped in five categories and customer survey is grouped in four categories) that each category is explained and analyzed in this part.

4. 1. 1 Employees Survey Data Analysis

4. 1. 1 First Category: Employee Demographics

Questions related to this category are asked from the employees in the survey to know about the background of respondents as well as to confirm that they appeal to the target population of the research. Firstly, in response to the question about the gender of the employees, chart 1, reports that among the 41 respondents 36 of them are male which is 87.8% of the target population of employees and the rest 12.2% (5 out of 41) is female employees.

Chart 1. Employee Survey: Respondent Gender

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|----------------------|-------------------|------------|----------------|
| Participant's Gender | Male | 36 | 87.8 |
| | Female | 5 | 12.2 |

Secondly, chart 2, reports in response to the question regarding age of the employees, among the 41 respondents 27 respondents (65.9%) are in age group (18 – 28) years old, 11 respondents (26.8%) in age group (29 – 38) years old, and the rest 3 respondents (7.3%) are from age group (39 – 48) years old.

Chart 2. Employee Survey: Age of Respondents

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|----------------|------------------------|------------|----------------|
| Age Group | Less than 18 years old | 0 | 0 |
| | (18 - 28) years old | 27 | 65.9 |
| | (29 - 38) years old | 11 | 26.8 |
| | (39 – 48) years old | 3 | 7.3 |
| | (49 - 50) years old | 0 | 0 |
| | More than 50 years old | 0 | 0 |

Thirdly, chart 3, reports regarding to the responses about education level of the employees, 3 out of 41 or (7.3%) respondents have a secondary school education level, same figures for diploma level, bachelor level respondents were 28 out of 41 or (68.3%), and master level respondents are (17.1%) or 7 out of 41 respondents.

Chart 3. Employee Survey: Respondents Educational Level

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|-----------------|-------------------|------------|----------------|
| Education Level | Secondary School | 3 | 7.3 |
| | Diploma | 3 | 7.3 |
| | Bachelor | 28 | 68.3 |
| | Master | 7 | 17.1 |
| | PhD | 0 | 0 |

Finally, chart 4, reports about area of education of the respondents is another question related to demographic of the employees. 17.1% or 3 out of 41 respondents have business major, 10 out of 41 or 24.4% have major in finance, 12 out of 41 or (29.2%) have major in banking, 5 out of 41 or (12.2%) have major specifically in Islamic banking, and 7 out of 41 or (17.1%) selected other as their study field.

Chart 4. Employee Survey: Respondents Field of Education

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|----------------|-------------------|------------|----------------|
| Area of Study | Business | 7 | 17.1 |
| | Finance | 10 | 24.4 |
| | Banking | 12 | 29.2 |
| | Islamic Banking | 5 | 12.2 |
| | Other fields | 7 | 17.1 |

Those who selected other specified their field of study as follows:

- Major in Arabic language
- Majors in civil engineering
- Major in Islamic law and banking
- Major in computer science
- Major in journalism

4. 1. 1. 2 Second Category: Bank Related Questions

The first question related to bank asked from the participants is that which bank they are employed at, according to chart 5, 21 out of 41 or (51.22%) of the respondents are from the Bakhtar Bank, 13 out of 41 or (31.70%) are from Afghanistan International Bank (AIB), and 7 out of 41 or (17.07%) target employees are from Gazanfar Bank.

Chart 5. Employee Survey: Employees of Which Bank

| Characteristic | Response Category | F (n = 41) | % |
|------------------------|-------------------------------|------------|-------|
| Employee at which bank | Bakhtar Bank | 21 | 51.22 |
| | Afghanistan United Bank (AIB) | 13 | 31.7 |
| | Gazanfar Bank | 7 | 17.07 |

Based on the survey data and chart 6, the question about what is employees position in the bank, 20 out of 41 or (48.8%) of the respondents are working in customer service, 7 out of 41 or (17.1%) are working in operation department, 14 out of 41 or (34.1%) selected other.

Chart 6. Employee Survey: Respondents Occupation at Bank

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|------------------------|-------------------|------------|----------------|
| Occupation at the bank | Customer Service | 20 | 48.8 |
| | Treasury | 0 | 0 |
| | Operation | 7 | 17.1 |
| | Risk Management | 0 | 0 |
| | Others | 14 | 34.1 |

Those who selected other specified their area of education as follows:

- Cash Department
- Sharia Law Department
- Internal Audit Department
- Teller
- Chief Islamic Banking Officer

In response to question about duration of their work and based on chart 7, 9 out of 41 or (21.9%) stated that they have been working in the bank for less than a year, 13 out of 41 or (31.8%) have spent (1 – 2 years) in the bank, 4 out of 41 or (9.7%) has been working in the bank for (2 – 3 years), 5 out of 41 or (12.2%) has been working in the bank for group (3 – 4 years), none of the respondent selected 4 – 5 years' time frame but 10 out of 41 or (24.4%)

selected more than five years' time frame for working duration in the bank.

Chart 7. Employee Survey: Respondents Job Duration at Bank

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|----------------|--------------------|------------|----------------|
| Job Duration | Less than One year | 9 | 21.9 |
| | (1 – 2) years old | 13 | 31.8 |
| | (2 – 3) years old | 4 | 9.7 |
| | (3 – 4) years old | 5 | 12.2 |
| | (4 – 5) years old | 0 | 0 |
| | More than 5 years | 10 | 24.4 |

In response to the question “does bank share information with public or customers” 38 out of 41 or (92.7%) answered with yes and 3 out of 41 or (7.3%) said no to this question referred to chart 8.

Chart 8. Employee Survey: Employees Information Providence to Customers

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|--|-------------------|------------|----------------|
| Do you provide information about Islamic banking to customers? | Yes | 38 | 92.7 |
| | No | 3 | 7.3 |

Those who answered with yes specified the kind of information they share with public or their customers as follows:

- Information regarding Islamic law
- Limited Information based on public interest
- Information about products and accounts
- Information about financial statements
- Information about profit and loss rate
- Information about recent changes in products and services
- Information about terms and conditions of the products

- Information about the projects where their funds are invested
- Information about related to customers only

4. 1. 1. 3 Third Category: Questions Related to Islamic Banking Products

Questions asked in this part is about Islamic banking products and services of the bank that contains questions related to their awareness of the Islamic banking products and services provided by the bank and degree of demand for these products.

Referred to chart 9 and in response to question asked about which Islamic products are offered through their bank to their customers, for each percentage for each product is based on 41 respondent's response and it is clearly explained in the following chart.

Chart 9. Employee Survey: Products Offered by Bank

| Characteristic | Response Category | Percentage (%) |
|------------------------------|--|----------------|
| Products offered by the bank | Musharakah (Equity participation) | 53.60% |
| | Muârabah (Trustee finance contract) | 75.61% |
| | Bai'Salam (Forward Sale) | 17.10% |
| | Musowamah (Bargaining Sale) | 14.60% |
| | Wikalah (Representation) | 21.90% |
| | Ijârah (Lease, lease purchase) | 41.50% |
| | Wadiyah (Safekeeping of deposits) | 24.40% |
| | Aqad (Contract) | 24.40% |
| | Qard Hassan (Beneficence loans) | 41.50% |
| | Istisna (Deferred payment/delivery) | 21.90% |

In response to question related to degree of demand for Islamic banking products, while (17.1%) or 7 out of 41 stated that demand for Islamic products has significantly increased, 16 out of 41 or (39%) stated that it is increased. The other (39%) or 16 out of 41

respondents said that is neither decreased nor increased and it has a constant rate. However, 2 out of the 41 or (4.9) said it is decreased and none said it is significantly decreased referred to chart 10.

Chart 10. Employee Survey: Customers Demand Status

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|--|-------------------------|------------|----------------|
| Status of customer demand for Islamic banking products | Significantly Increased | 7 | 17.1 |
| | Increased | 16 | 39 |
| | Constant | 16 | 39 |
| | Decreased | 2 | 4.9 |
| | Significantly decreased | 0 | 0 |

4. 1. 1. 4 Fourth Category: Questions Related to Customers

This part of the employee survey is customer related questions from the employees that do customers ask for information, in response to this question 23 out of 31 or (74.2%) answered with yes and 8 out of 31 or (25.8%) answered with no referred to chart 11.

Chart 11. Employee Survey: Customers Request for Information

| Characteristic | Response Category | F (n = 31) | Percentage (%) |
|------------------------------------|-------------------|------------|----------------|
| Does customer ask for information? | Yes | 23 | 74.2 |
| | No | 8 | 25.8 |

In response to the question about how often do customers ask information about the difference between Islamic and non-Islamic products, 21 out of 41 or (51.2%) stated that customers always ask for information to know about the difference, 4 out of 41 or (9.8%) stated that they usually ask, 14 out of 41 or (34.1%) said they sometimes ask for such information, 2 out of 41 said they ask often and no one said that customers rarely or never asked for such information referred to chart 12.

Chart 12. Employee Survey: How Often Customers Ask for Information

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|--|-------------------|------------|----------------|
| How often customers ask for information about Islamic and non-Islamic banking differences. | Always | 21 | 51.2 |
| | Usually | 4 | 9.8 |
| | Sometimes | 14 | 34.1 |
| | Often | 2 | 4.9 |
| | Rarely | 0 | 0 |
| | Never | 0 | 0 |

In response to the question “who are the customers of Islamic banking” referred to chart 13, 39 out of 41 or (95.1%) of the participants said that their customers are from Muslim community, and 2 out of 41 or (4.9%) respondents said that their customers are from Muslim and non-Muslim communities.

Chart 13. Employee Survey: Most Customers of Islamic Banking

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|--|-------------------|------------|----------------|
| Who are most customers of Islamic banking? | Muslims | 39 | 95.1 |
| | Non-Muslims | 0 | 0 |
| | Both | 2 | 4.9 |

In response to question related to customers asked from the employees assessing the relationship of religion of customers with selection of Islamic banking products referred to chart 14, 28 out of 41 or (68.3%) of the target employees answered that the religion of customers does impact the decision of selection of Islamic banking products however, 13 out of 41 or (31.7%) said, “no there is not any relationship”.

Chart 14. Employee Survey: Religion Impact on Selection of Islamic Banking

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|---|-------------------|------------|----------------|
| Does religion of customer impact its decision to select Islamic banking products? | Yes | 28 | 68.3 |
| | No | 13 | 31.7 |

4. 1. 1. 5 Fifth Category: Questions Related to Conceptual Part

Questions related this part are about products and services compliance with Islamic principles, distinguishing features of Islamic banking, existence of Sharia Supervisory Board (SSB), coding circulation of Islamic banking funds which relates to accounting and auditing of Islamic banking system.

In response to question related to agreement or disagreement level of employees with the statement that products and service compliance with Islamic law, while 13 out of 37 or (35.1%) of the respondents strongly agreed, 19 out of 37 or (51.4%) agreed. 4 out of 37 or (10.8%) neither agree or disagree and no one among the respondents disagree but 1 out of 37 or (2.7%) strongly disagreed referred to chart 15.

Chart 15. Employee Survey: Product Compliance with Islamic Principles

| Characteristic | Response Category | F (n = 37) | Percentage (%) |
|---|----------------------------|------------|----------------|
| Products and services compliance with Islamic principles from employee perspective. | Strongly Agree | 13 | 35.1 |
| | Agree | 19 | 51.4 |
| | Neither Agree nor Disagree | 4 | 10.8 |
| | Disagree | 0 | 0 |
| | Strongly Disagree | 1 | 2.7 |

In response to the questions related to 4 distinguishing features of Islamic banking products and services, targeted employees responded with pointing out following distinguishing features of Islamic in contrast to conventional banking:

- Prohibition of interest
- Profit and loss sharing
- It is based on profit sharing
- It is based on real trade
- It is based on asset financing
- It has Sharia Supervisory Board
- It is based on risk sharing
- It has transaction transparency
- It is in favor of the society and public
- It generates wealth
- Products are Islamic
- It is based on valid contracts
- Prohibition of investing in gambling activities
- Existence of sharia law or Islamic principles
- Provide more facilities than conventional banks.
- Money is not commodity but it is medium of exchange in Islamic products
- Projects where funds are going to be invested can be evaluated
- It is based on actual demand of economy it take parts in real economy development.

In response to question about existence of Sharia Supervisory Board (SSB) in their banks and based on chart 16, 34 out of 38 or (89.5%) confirmed the existence of SSB in their banks but 4 out of 38 or (10.5%) did not know that it exist or not.

Chart 16. Employee Survey: Existence of Sharia Supervisory Board

| Characteristic | Response Category | F (n = 38) | Percentage (%) |
|-----------------------|-------------------|------------|----------------|
| Existence of (SSB) | Yes | 34 | 89.5 |
| | No | 0 | 0 |
| | I do not know | 4 | 10.5 |

In response to question coding circulation of Islamic banking funds which relates to accounting and auditing of Islamic banking system, 4 out of 41 or (9.7%) stated that coding circulation of Islamic funds are traced and controlled the same way as conventional banks but 14 out of 41 (34.2%) stated that it is traced and controlled in different way and 23 out of 41 or (56.1) said they do not know about it referred to chart 17.

Chart 17. Employee Survey: Coding Circulation of Fund System

| Characteristic | Response Category | F (n = 41) | Percentage (%) |
|------------------------------|-----------------------------------|------------|----------------|
| Coding circulation of funds. | Same as Conventional Banks | 4 | 9.7 |
| | Different from Conventional Banks | 14 | 34.2 |
| | I do not know | 23 | 56.1 |

4. 1. 2 Customer Survey Analyses

For the data analysis purposes customer survey is also grouped in categories of customer demographics, bank, products and services, conceptual part, which includes questions, related to Islamic principles and Sharia Supervisory Board (SSB).

4. 1. 2. 1 First Category: Customer Demographics

This category contains questions related to demographics of the customers that each of the questions of this part is explained and analyzed in following paragraphs. Firstly, based on chart 18, from the target customer sample 79.4 percent or 27 out of 34 are male and the rest 7 out of 34 or (20.6%) are female participants.

Chart 18. Customer Survey: Gender of Respondents

| Characteristic | Response Category | F (n = 34) | Percentage (%) |
|----------------------|-------------------|------------|----------------|
| Participant's Gender | Male | 27 | 79.4 |
| | Female | 7 | 20.6 |

Secondly, based on chart 19, age group of the customer is another aspect in the demographic category that in response to related question about this aspect, none of the respondents is less than 18 years old, 16 out of 34 or (47.1%) are in age group (18 – 28) years old, 14 out of 34 or (41.2%) are in age group (29 – 38) years old, 3 out of 34 or (8.8 %) are in age group (39 – 48) years old, 1 out of 34 or (2.9 %) are in age group (49 – 50) years old but none of the respondents were from the age group more than 50 years old.

Chart 19. Customer Survey: Age of Respondents

| Characteristic | Response Category | F (n = 34) | Percentage (%) |
|-----------------------|------------------------|------------|----------------|
| Respondents Age Group | Less than 18 years old | 0 | 0 |
| | (18 – 28) years old | 16 | 47.1 |
| | (29 – 38) years old | 14 | 41.2 |
| | (39 – 48) years old | 3 | 8.8 |
| | (49 – 50) years old | 1 | 2.9 |
| | More than 50 | 0 | 0 |

Thirdly, according to the chart 20, education level is another aspect related to customer demographics, while 4 out of 33 or (12.1%) of customers of the banks have secondary school education level, 6 out of 33 or (18.2%) have diploma. In addition, 16 out of 33 or (48.5%) have bachelor degree and 7 out of 33 or (21.2%) have master's degree but none of them have PhD level education.

Chart 20. Customer Survey: Respondents Education Level

| Characteristic | Response Category | F (n = 33) | Percentage (%) |
|--------------------------------------|-------------------|------------|----------------|
| Educational Level of the respondents | Secondary School | 4 | 12.1 |
| | Diploma | 6 | 18.2 |
| | Bachelor | 16 | 48.5 |
| | Master | 7 | 21.2 |
| | PhD | 0 | 0 |

Fourthly, occupation area is another question asked from the customers that in

response to this question, chart 21 reports that 7 out of 34 or (20.6%) are working in government sector, 23 out of 34 or (67.6%) are working in private sector, 4 out of 34 or (11.8%) are engaged with their private business, and none of the respondents were students.

Chart 21. Customer Survey: Respondents Occupation

| Characteristic | Response Category | F (n = 34) | Percentage (%) |
|-------------------------------|-------------------|------------|----------------|
| Occupation of the respondents | Government Sector | 7 | 20.6 |
| | Private Sector | 23 | 67.6 |
| | Private Business | 4 | 11.8 |
| | Student | 0 | 0 |
| | Others | 0 | 0 |

4. 1. 2. 2 Second Category: Bank Related Questions

This category includes questions from the customers related to bank, firstly, question of which bank they have account in, based on chart 22 and in response to this question, 10 out of 34 or (29.41%) are customers of Bakhtar bank from the target customer sample, 14 out of 34 or (41.17%) are from Afghanistan International Bank (AIB) and the rest 10 out of 34 or (29.41%) of the respondents are from the Gazanfar Bank.

Chart 22. Customer Survey: Customer of Which Bank

| Characteristic | Response Category | F (n = 34) | Percentage (%) |
|--------------------------------|--------------------------------------|------------|----------------|
| Customer of which of the banks | Bakhtar Bank | 10 | 29.41 |
| | Afghanistan International Bank (AIB) | 14 | 41.17 |
| | Gazanfar Bank | 10 | 29.41 |

Secondly, chart 23 reports about customers' three main reasons for selecting Islamic banking and responses are based on the percentage for the listed 14 features clearly shown in the chart.

Chart 23. Customer Survey: Reasons for Selection of the Bank

| Reasons for Selection of the Bank | Percentage (%) |
|--|-----------------------|
| Reputation | 38.20% |
| Service | 20.60% |
| Convenience | 2.94% |
| Productivity | 0% |
| Credibility | 17.60% |
| Confidence | 44.10% |
| Location | 0% |
| Cost efficiency | 2.94% |
| Ethical reasons | 20.60% |
| Confidence on SSB | 29.40% |
| Religion | 82.30% |
| Quality | 5.88% |
| Family and friends reference | 23.50% |
| Staff friendliness | 26.50% |

Thirdly, based on chart 24 in response to question about duration of being a customer of the bank, 13 out of 34 or (38.2%) of the customer survey respondents are customers of the bank less than one year, while 9 out of 34 or (26.5%) are customer of the bank for (1 – 2) years, 3 out of 34 or (8.8%) are for (2 – 3) years customer of the bank. 2 out of 34 customers or (5.9%) said that they have been customers of the bank for the time period of (3 – 4) years, 3 out of 34 or (8.8%) are customers of the bank for (4 – 5) years, and the rest 4 out of 34 or (11.8%) stated that they have been customers of the bank for more than five year.

Chart 24. Customer Survey: Duration of Being Customer of the Bank

| Characteristic | Response Category | F (n = 34) | Percentage (%) |
|--|--------------------|------------|----------------|
| Duration of being customer of the bank | Less than One Year | 13 | 38.2 |
| | (1 – 2) Years | 9 | 26.5 |
| | (2 – 3) Years | 3 | 8.8 |
| | (3 – 4) Years | 2 | 5.9 |
| | (4 – 5) Years | 3 | 8.8 |
| | More than 5 Years | 4 | 11.8 |

Fourthly, in response to the question, “have customers ever used non-Islamic banking products and services” and based on chart 25, 18 out of 34 or (52.9%) answered with yes they do used non Islamic products but 16 out of 34 or (47.1%) answered with no they never used non Islamic products.

Chart 25. Customer Survey: Do Customers Use Conventional Bank Products

| Characteristic | Response Category | F (n = 34) | Percentage (%) |
|-------------------|-------------------|------------|----------------|
| Non-Islamic Trial | Yes | 18 | 52.9 |
| | No | 16 | 47.1 |

When asked those who answered with yes that what three main differences they noticed between Islamic and conventional banks, the responses gathered are as follows:

- Islamic banking provide interest free products
- Profit and loss is shared in Islamic banking
- Islamic banking is based on Sharia Law
- Islamic banking gives their customers feeling of trust
- Islamic banking gives their customers psychological inner peace
- Islamic banking have less service charges
- Profit from Islamic banking is Halal
- Islamic banking provides Islamic products
- In Islamic banking money is invested in society welfare projects
- Islamic banking provides more profit
- Islamic banking develop economy

Fifth, based on chart 26 and in response to question asked from customers about their level of satisfaction from the bank, 16 out of 34 or (47.1%) are highly satisfied with bank

services and products, 15 out of 34 or (44.1%) are satisfied, 1 out of 34 or (2.9%) are neither satisfied nor dissatisfied but 2 out of 34 or (5.9%) are dissatisfied with bank products and services and none of them are highly dissatisfied.

Chart.26 Customer Survey: Level of Satisfaction from the Bank

| Characteristic | Response Category | F (n = 34) | Percentage (%) |
|---|------------------------------------|------------|----------------|
| Customer satisfaction level from the bank | Highly Satisfied | 16 | 47.1 |
| | Satisfied | 15 | 44.1 |
| | Neither Satisfied Nor Dissatisfied | 1 | 2.9 |
| | Dissatisfied | 2 | 5.9 |
| | Highly Dissatisfied | 0 | 0 |

4. 1. 2. 3 Third Category: Products and Services Related Questions

This category contains questions related products and services provided by Islamic banking, first question is asked about which products and services they use from the banks, in response they selected five most used products as follows in the chart 27.

Chart 27. Customer Survey: Most Used Products

| Characteristic | Response Category | Percentage (%) |
|--|-------------------|----------------|
| Products that are used the most by customers | Musharakah | 11.80 % |
| | Muarabah | 91.20 % |
| | Wadiyah | 02.90 % |
| | Qard Hassana | 38.20 % |
| | Istisna | 02.90 % |

Second question is asked from customers that while opening an account do they ask for information about where their money is used, in response to this question and referred to chart 28, 25 out of 32 or (78.1%) said yes to this question while 7 out of 32 or (21.9%) said no to this question.

Chart 28. Customer Survey: Query Where Money Is Invested

| Characteristic | Response Category | F (n = 32) | Percentage (%) |
|--|-------------------|------------|----------------|
| Do query about where their money is invested | Yes | 25 | 78.1 |
| | No | 7 | 21.9 |

Those who answered with yes to the above question specified that what kind of information they ask from the bank as follows:

- They ask for sharia law information.
- They ask for information about the project where their money is invested.
- They ask information about Islamic products
- They ask information about investment policy of Islamic banking.

4. 1. 2. 4 Fourth Category: Conceptual Part Related Questions

Fourth category contains questions related conceptual part of the survey.

First question is related to customer awareness level about Islamic banking, in response to this question and referred to chart 29, 4 out of 34 or (11.8%) of the customers mentioned that they are very well aware of the Islamic principles of Islamic banking products and services. 21 out of 34 or (61.8%) of customers said they have sufficient knowledge of Islamic principles, 8 out of 34 or (23.5%) stated that they are not much aware of these principles and 1 out of the 34 customers or (2.9%) said that he/she never thought about these principles.

Chart 29. Customers Survey: Awareness of Islamic Principles

| Characteristic | Response Category | F (n = 34) | Percentage (%) |
|--|-------------------------------|------------|----------------|
| Customer awareness level of Islamic principles | Very Well | 4 | 11.8 |
| | Sufficiently | 21 | 61.8 |
| | Not much | 8 | 23.5 |
| | Never thought before about it | 1 | 2.9 |

Second question is regarding interest that do customers know that interest is ban in Islamic banking products and services, as chart 30 reports, in response to this question, 31 out of 34 or (91.2%) answered to this question with yes they do know about prohibition of interest in Islamic banking products while 3 out of 34 customers said no, they do not know about this principle of Islamic banking.

Chart 30. Customer Survey: Awareness of Interest Ban Principle

| Characteristic | Response Category | F (n = 34) | Percentage (%) |
|---|-------------------|------------|----------------|
| Customers awareness level of interest ban principle | Yes | 31 | 91.2 |
| | No | 3 | 8.8 |
| | I do not know | 0 | 0 |

Third question is asked form customers about whether they know about profit and loss sharing principle of Islamic banking, as chart 31 reports, in response to this question, while 29 out of 34 or (85.3%) said yes they do know about this principle, 3 out of 34 or (8.8%) answered this question with no and the rest 2 out of 34 or (5.9%) respondents said they do not have any idea about it.

Chart 31. Customer Survey: Awareness of Profit and Loss Sharing Principle

| Characteristic | Response Category | F (n = 34) | % |
|--|-------------------|------------|------|
| Customers awareness level of profit and loss sharing principle | Yes | 29 | 85.3 |
| | No | 3 | 8.8 |
| | I do not know | 2 | 5.9 |

Finally, the last question of the customer survey is regarding sharia supervisory board that do they know about this board in the bank where they have account in. In response to this question and referred to chart 32, 11 out of 34 or (32.4%) answered with yes but 18 out of 34 or (52.9%) said no and 5 out of 34 or (14.7%) mentioned that they do not know about it.

Chart 32. Customer Survey: Awareness of Sharia Supervisory Board

| Characteristic | Response Category | F (n = 34) | Percentage (%) |
|--|-------------------|------------|----------------|
| Do customers have knowledge about Sharia Supervisory Board (SSB) | Yes | 11 | 32.4 |
| | No | 18 | 52.9 |
| | I do not know | 5 | 14.7 |

4. 2 Research Discussion

4. 2. 1 Employee Survey Discussion

First category of the employee survey presents demographic information about employees of the bank who participated in the survey. Figure 1, summarizes demographic data of the employee survey as below:

Figure 1. First Category

| Employee Survey First Category Data Summary | | |
|---|-------------------------|------------|
| Characteristics | Response category | % |
| Gender | Male | 88% |
| | Female | 12% |
| Age Group | 18-28 | 66% |
| | 29-38 | 27% |
| | 39-48 | 7% |
| Educational Level | Secondary School Level | 7% |
| | Diploma Level | 7% |
| | Bachelor Level | 68% |
| | Masters Level | 17% |
| Field of Study | Business | 17% |
| | Finance | 24% |
| | Banking | 29% |
| | Islamic Banking | 12% |
| | Other | 17% |
| Occupation | Customer service | 49% |
| | Operations | 17% |
| | Other | 34% |

According to this figure, it is very clear that most employees who participated in this survey are male employees. Though, during the research the effort was to reach to both

genders equally, but due to security issues for some days female staff were off duty; therefore, female staff respondents are only 12.20 percent of the target sample for employee survey. Age of the bank employee is another part of demographics, most employees are in young age group between 18 to 28 years old.

Referred to figure 1 and data gathered about educational level of employees' shows that most employees (68.30%) have bachelor degree and (17.10%) have master's degree. Only total of (14.6%) employees have less than bachelor level degree. Another important information about background of employees is their field of study. While a small portion (12.20%) of respondent employees have studied Islamic banking, the biggest portion of respondents have studies banking which both together makes more than half of the respondents education field. It is quite interesting that business and finance that are both related fields to banking equally are 17.10 percent of the results. Based on figure 1, some of those who selected other specified their field of study far different from the banking sector such as civil engraining and Journalism however, some others specified fields that are very close to Islamic banking sector such as Arabic language or Islamic law and banking.

From the occupation part it is clear that most of the respondents the randomly selected are employees are from customer care service department and a small portion of 17.10% are from operation department. However, 34.10% of employees who selected other as their occupation at bank includes those employees of the sample that are not selected randomly such as employees from the Sharia Board department.

The Second category of employee survey contains information related to bank, according to figure 2, more than half of the respondents are from Bakhatar Bank which will soon be the first full fledge Islamic bank in Afghanistan.

Figure 2. Second Category

| Employee Survey Second Category Data Summary | | |
|--|--------------------------------------|------------|
| Characteristics | Response category | % |
| Employee at which of the banks | Bakhtar Bank | 51% |
| | Afghanistan International Bank (AIB) | 32% |
| | Gazanfar Bank | 17% |
| Employee work duration at the bank | Less than an year | 22% |
| | 1-2 years | 32% |
| | 2-3 years | 10% |
| | 3-4 years | 12% |
| | More than 5 years | 24% |
| Does the bank disclose information to public? | Yes | 74% |
| | No | 26% |

From the rest 49%, AIB bank has contribution of 32% of the employee respondent portion and 17% relates to Gazanfar bank. When employees are asked to share data about their duration of work at banks, based on data presented in figure 2, the highest portion 32% of employees have been working in the bank for the period of time from one to two years. Interestingly, the second highest portion 24% has been working for more than five years. Other 22% of the employees have been working for less than a year, which means they are recent hired employees. Finally, there is not much difference between proportions of employees who have been working for 2 to 3 years or 3 to four years in the bank with a slight difference of 2 %. Furthermore, figure 2, reports about disclosure of information from the bank that 74.2% of the employees said yes the bank do share information with their customers and 25.80% says no the bank do not share information with customers.

Third category is related to products and services available at the bank that employee are working for. Figure 3, reports about the products offered by these banks among the 17 products, ten most selected products are Mudrabah, Musharakha, Ijarah, Qard Hassana, Wadiyah, Aqad, Wakalah, Istisna, Bai'Salam, and Musowamah.

Figure 3. Products Offered by Banks

| Employee Survey Third Category: Products of the Bank | | |
|--|-------------------|------------|
| Characteristics | Response category | % |
| | Musharakah | 54% |
| | Muarabah | 76% |
| | Bai'Salam | 17% |
| | Musowamah | 15% |
| | Wakalah | 22% |
| | Ijarah | 42% |
| | Wadiah | 24% |
| | Aqad | 24% |
| | Qard Hassana | 42% |
| Which products offered by the bank? | Istisna | 22% |

Referred to this figure, the demand for Islamic products and services has from the employee's perspective 39% increased and 17.10% highly increased which both makes 56.10% of the total portion. Other 39% shows that demand is constant and 4.9% of the employees think that demand for Islamic banking products has decreased.

Figure 4. Demand for Islamic Products

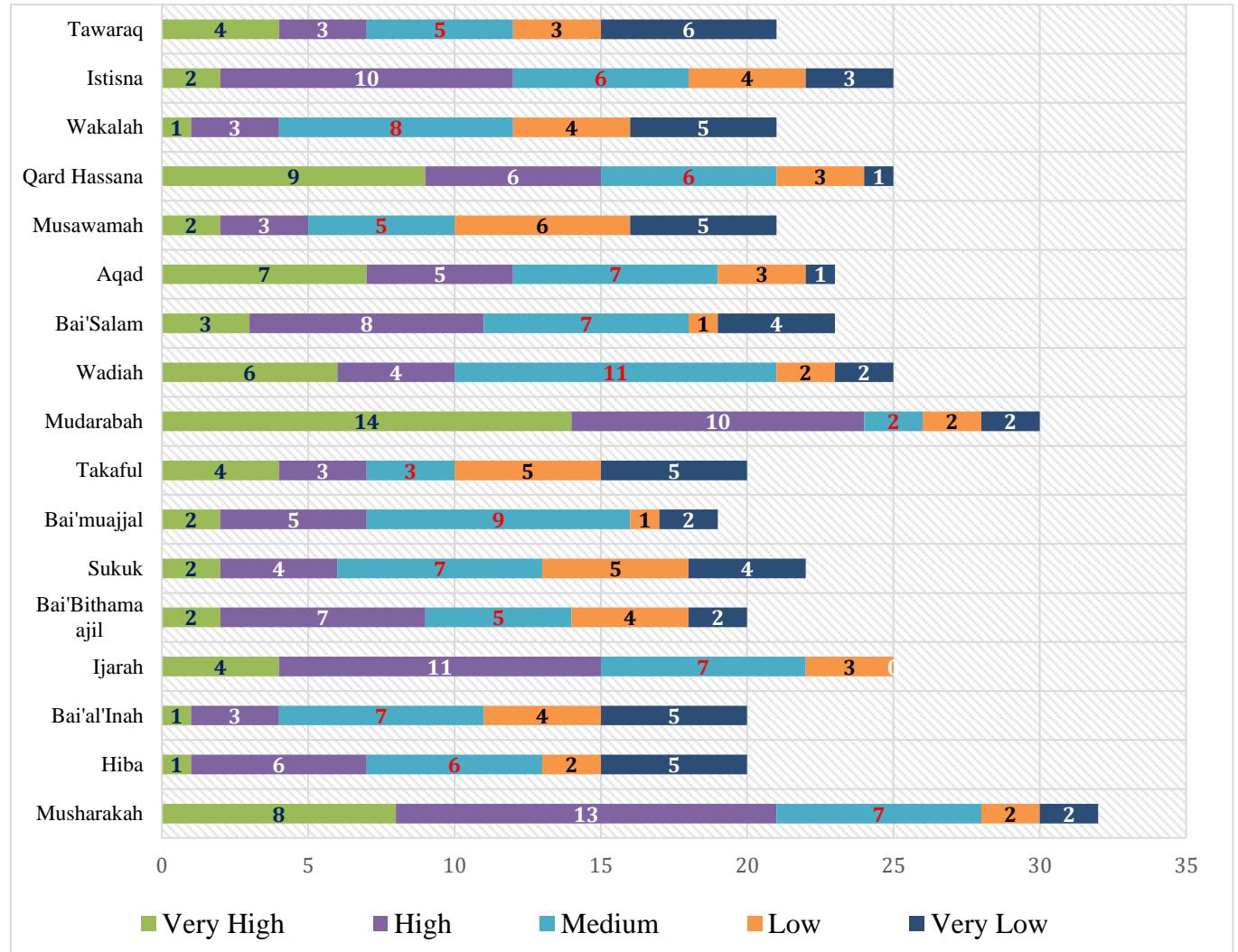
| Employee Survey Third Category: Bank Products Demand | | |
|--|-------------------------|------------|
| Characteristics | Response category | % |
| | Significantly increased | 17% |
| | Increased | 39% |
| | Been constant | 39% |
| Islamic banking products demand has | Decreased | 5% |

It is also very interesting to know about customer demand rate for the 17 Islamic banking products and services from the employee's point of view. Very High demand is for Musharakah, Qard Hassana, Mudrabaha, Aqad and Wadiah. The demand rate for Musharakah, Ijraha, Mudrabaha, Istisna and Bai'Salam is high than other products.

From the employee's perspective medium demand exist for almost for all products but for Mudrabah it is less because for Mudrabaha there is high and very high demand exists. Employees think that the degree of demand for products such as Tawaraq, Wakalah,

Musawamah, Takaful, Hiba and Bai'al'Inah is very lower than other products. Low demand exists for Sukuk, Takaful and Wakalah based on employee response in figure 5.

Figure 5. Degree of Demand for Islamic Products



The Fourth category of the employee survey asks employees questions related to customers. When employees are asked that do they brief customers about the different products and services provide by Islamic banking department in their banks, their responses are referred to figure 6, as it is clear that 92.70% of the employees said that yes they do brief customers about Islamic banking products and services while 7.3% said no they do not provide customers information.

Figure 6. Employee Survey Fourth Category

| Employee Survey Respondent Fourth Category Data Summary | | |
|--|--------------------------|------------|
| Characteristics | Response category | % |
| Do employees provide a brief detail about Islamic banking products? | Yes | 93% |
| | No | 7% |
| How often customers ask for a brief regarding Islamic banking products? | Always | 51% |
| | Usually | 10% |
| | Sometimes | 34% |
| | Often | 5% |
| Islamic banking most customers are? | Muslim | 95% |
| | Non-Muslim | 5% |
| Does customers religion impact selection of the bank | Yes | 68% |
| | No | 32% |

In contrast to the above question, employees are asked that how often customers themselves ask for information about difference between Islamic and non-Islamic products and services, data related to this part is well explained in figure 6. According to this figure, in the point of view of employees, while 51.20% of customers always ask for a brief about a product before opening an account, 9.8% usually ask to brief them. 34.10% always ask for information but 4.90 % often ask for information. According to figure 6, employee's response show that 95% of customers of Islamic banking are from Islamic communities and only 5% are believes that they are from Muslim and non-Muslim communities. Another question related to above question is asked from employees that weather religion of customers' impact their decision of selection of Islamic baking products and services referred to figure 6. This figure also reports that 68.3% of employees think that there is a relationship between customers' religion and selection of Islamic banking and 31.7% stated that there is not any relationship. Those who answered yes are asked the reason and they come up with following reasons regarding Islamic banking particularly:

- The reason is that Afghanistan is an Islamic country with most Muslim customers
- The reason is that Islamic banking is based on sharia law so most of the customers are Muslims.

- The reason is that Islamic banking provide sharia compliant products that attracts more customers from Islamic community.
- The reason is that Islamic banking provide Islamic and a complete rule of finance that is why most customers are Muslims.
- The reason is that Muslims are from religious sensitive societies so they select Islamic banking because it compliance with Islamic religion.
- The reason is that Islamic banking provide information about projects where money is invested, which is important to know, based on Islamic law.
- The reason is that Muslims trust more Islamic banking than conventional banking.
- The reason is that religion has limitations that based on which Muslims select Islamic banking.

Fifth category of employee's survey discusses conceptual questions. The first question from employees is that to which degree they agree that Islamic products compliance with Islamic principles. Based on figure 7, more than half 51.40% agreed that products provided by Islamic banking are in compliance with Islamic principles.

Figure 7. Employee Survey Fifth Category

| Employee Survey Respondent Fifth Category Data Summary | | |
|---|--|------------|
| Characteristics | Response category | % |
| Employee response to the statement: Islamic banking products are complained with Islamic law | Strongly Agree | 35% |
| | Agree | 51% |
| | Neither Agree Nor Disagree | 11% |
| | Disagree | 0% |
| | Strongly Disagree | 3% |
| Is there any Sharia Supervisory Board in the bank? | Yes | 90% |
| | No | 11% |
| How Islamic banking funds are circulated? | I do not know | 56% |
| | Different from conventional banking | 34% |
| | Same as conventional banking | 10% |

35.10% strongly agreed, a small portion 10.80% neither agreed nor disagreed and a very small portion of 2.7% highly disagreed but none disagreed.

When employees are asked about their opinion about four distinguishing characteristics of Islamic banking in their banks, they mentioned the following features that distinguishes Islamic banking from conventional banking:

- While Interest is prohibited in Islamic banking, conventional banking is based on predetermined interest rate.
- Another distinguishing feature is that Islamic banking is based on profit and loss sharing while conventional banking is only based on profit.
- Islamic banking is based on real trade as it shares profit and risk but conventional banking is not based on real trade.
- Islamic banking is based on asset financing but conventional banking is not.
- Islamic banking has Sharia Supervisory Board to complaint its products with Islamic laws.
- In Islamic banking there is higher transparency in its transaction compare to non-Islamic banking.
- Islamic banking guarantee wealth and it is more in favor of the society and public than conventional banking.
- Islamic banking contains more valid contracts than interest based banking.
- Interest free banking prohibits investing in gambling and prohibited activities but there is not such law for non-interest free banking.
- Islamic banking products are based on Islamic law under existence of SSB.
- Islamic banking provides better facilities than conventional banks.
- Money is not commodity but it is medium of exchange in Islamic products but in conventional banking money is used as a commodity.

- In Islamic banking depositors have the right to evaluate the project where their money is going to be invested as the bank plays the role of median but in conventional banking depositor does not have such right and after deposits the bank is the owner of funds to invest it anywhere it wants.
- Islamic banking is based on actual demand of economy it take parts in real economy development.

The data shown in figure 7, clearly show that employees approach to the question about Sharia Supervisory Board is that almost 90% mentioned that there is a sharia supervisory board in their banks but 10% were unsure about it. In this figure, the last question asked from employees is about coding circulation of funds system of Islamic banking. More than half of the respondents said that they do not know about coding circulation of Islamic funds. 34.20 said that the coding circulation Islamic funds are different than non-Islamic funds in conventional banks but 9.70% agreed that there is not different system for coding circulation of Islamic funds so they use the same system used for conventional banks.

4. 2. 2 Customer Survey Discussion

Demographic part of customer survey provides interesting background information about customer of Islamic banking of the selected banks. Firstly, from the figure 8 it is clear that almost 80% respondents are from male gender and around 20% are female.

Figure 8. Respondents Gender

| Customer Survey Respondent First Category Data Summary | | |
|---|--------------------------|------------|
| Characteristics | Response category | % |
| Gender | Male | 80% |
| | Female | 20% |
| Age Group | 18-28 | 48% |
| | 29-38 | 40% |
| | 39-48 | 9% |

| | | |
|--------------------------|------------------------|------------|
| | 49-50 | 3% |
| Educational Level | Secondary School Level | 12% |
| | Diploma Level | 18% |
| | Bachelor Level | 49% |
| | Masters Level | 21% |
| Occupation Field | Government sector | 21% |
| | Private sector | 68% |
| | Private business | 12% |

Secondly, according to this figure, the gender of respondent shows that two age groups of (18 – 28) and (29 – 38) are making almost 90% of the respondents. The rest around 10% of the respondents are from age groups of (39 – 48) and (49 – 50) of the customer survey. Thirdly, figure 8, reports about educational background of the customer survey respondents. According to this figure, almost 70% of the respondents are having master or bachelor educational level. However, 18.20% of the respondents have diploma level education and 12.10% secondary school level. Fourthly, figure 8, repots the occupation area of the respondents. It is clearly shown in the figure that most (67.60%) respondents work in private sector while (20.60%) work in private sector and (11.80%) have their own businesses.

Second part of the customer service asks questions related to bank from the customers. Figure 9 categories respondents of customer survey to each of the three banks. It is obvious that most customer who respondent to survey is form Afghanistan International Bank (AIB) and equally (29.41 %) of the respondents are from Bakhtar and Gazanfar Banks.

Figure 9. Customer of Which Bank

| Customer Survey Second Category Data Summary | | |
|--|---|------------|
| Characteristics | Response category | % |
| Customer of which of the banks? | Bakhtar Bank | 29% |
| | Afghanistan International Bank (AIB) | 41% |
| | Gazanfar Bank | 29% |

| | | |
|--|------------------------------------|------------|
| | Less than an year | 38% |
| | 1-2 years | 27% |
| | 2-3 years | 9% |
| | 3-4 years | 6% |
| | 4-5 years | 9% |
| | More than 5 years | 12% |
| For how many years being customer of the bank? | | |
| Have you ever used conventional banking products? | Yes | 53% |
| | No | 47% |
| Level of satisfaction from the bank? | Highly satisfied | 47% |
| | Satisfied | 44% |
| | Neither satisfied nor dissatisfied | 3% |
| | Dissatisfied | 6% |

This figure provides clear data about respondents time period of being customers.

Interesting, most respondents are customer of the banks for less than a year with (38.20%).

Then another significant period of time is (1 – 2) years that (26.50%) respondents are customer of the bank for this period of time. Only (11.80%) of the respondents are customers of the banks for more than five years. When customers are asked that do they ever-used non-Islamic products, figure 9 reports responses for this question. It is clear that more than half of customers have already used conventional banking products and 47.10% did not use it yet.

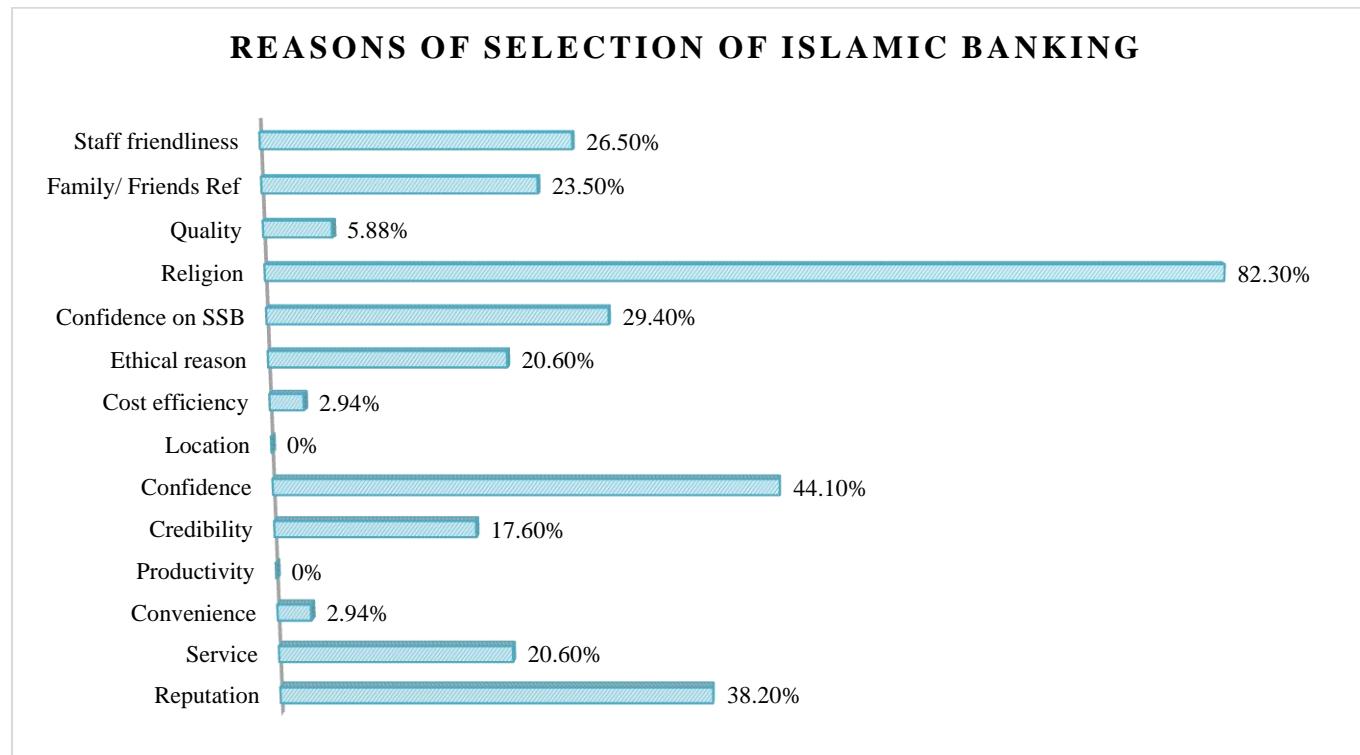
From those who said yes to this question more specification regarding the three main differences between interest based and non interest based products is asked.

When customer are asked about their level of satisfaction from the banks. More than 90% are of the respondents are satisfied or highly satisfied. Around 6% are neither satisfied nor dissatisfied and rest is dissatisfied or highly dissatisfied.

When customers are asked to select three main reasons for choosing Islamic banking, based on the responses the most important reasons are reported by figure 10. Based on this diagram, religion is the most important reason for the selection of Islamic banking based on the customer response with (82.3%). Then confidence is the second reason with (44.10%) respondents' agreement. Bank reputation is the third highest selected reason with (38.20%).

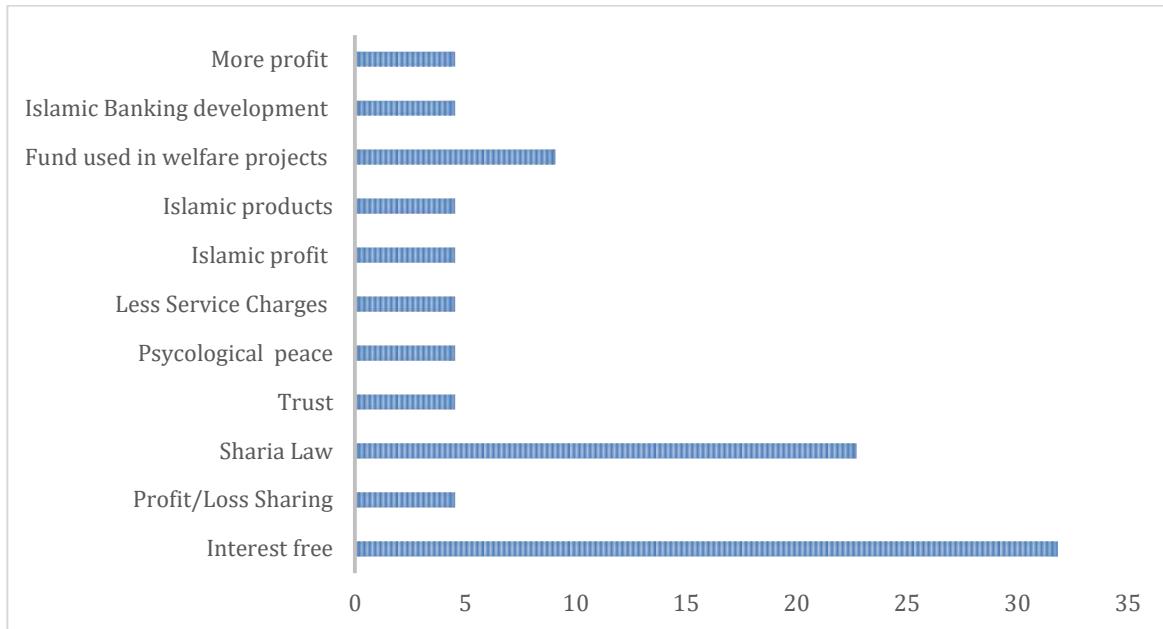
Some other reasons such as confidence on Sharia Supervisory Board (SSB), staff friendliness, friend and family reference, better services and ethical reason are respectively selected by customers as noticeable reasons for selection of Islamic banking with (29.40%), (26.50%), (23.50%), and (20.60%). The rest reasons selected by respondents are with less than (20%).

Figure 10. Respondents Reasons for Selection of Bank



In response, referred to figure 11, three most selected features of Islamic banking by respondents are interest free feature with more than 30% respondent's agreement on it, existence of Sharia law with more than 20 % agreement and funds usage in welfare projects with almost 10 % agreement of customers on this feature of Islamic banking. Interestingly, the rest 8 features are selected by almost 5% of the respondents.

Figure 11. Features of Islamic Banking



The third category of customer survey includes questions regarding Islamic products and services. Firstly, figure 12 reports the products that customer use them the most.

Figure 12. Most Used Islamic Products

| Customer Survey Third Category: Products and Services of the Bank | | |
|--|--|------------|
| Characteristics | Response category | % |
| Most used Islamic banking products and services | Musharakah | 12% |
| | Muarabah | 91% |
| | Wadiyah | 3% |
| | Qard Hassana | 38% |
| | Istisna | 3% |
| Do you ask the bank where your money is invested after deposit in the bank? | Yes | 78% |
| | No | 22% |
| What kind of information you ask from the bank before opening an account? | Islamic trade | 8% |
| | Information about the product | 23% |
| | Investment policy | 8% |
| | Where money is invested by bank | 53% |
| | Sharia law | 8% |

According to this figure, five products are selected Musharakah, Muarabaha, Wadiyah, Qard Hassana, and Istisna. Among these products Muarabaha is one of the products that is

selected by 91.2% of the respondents that they use this product. Qard Haassana is the second product that is used by 38.2% of customers. While Musharakah is used by 11.8% of customers Wadiyah and Istisna are used by small portion of customers of 2.9% each. About customers query related to their funds investment, most customers (78.10%) said yes they do query regarding projects where their or fund are going to be invested through bank. However, 21.90% of customers said they do not ask customer service before opening an account that where their money will be used. Those who said yes in response to the above question are asked to specify that usually what kind of information they do ask from customer service. It is also quite interesting that most ask about information to know where their money is invested. While some ask information about the product, others make small portion less than 10% who ask about Sharia law, Islamic trade and investment policy of Islamic banking.

Fourth category of customer survey contains questions related to conceptual part of the thesis. Firstly, figure 13 reports to find out degree of customers awareness about Islamic principles of Islamic banks. 61.80% of customers responded in a positive way that they have sufficient knowledge of Islamic principles. While 23.50% of customers stated that they do not have sufficient information, 10.80% of them said they are very well aware of these principles. Almost 3% mentioned they never thought about it before.

Figure 13. Respondents Awareness about Islamic Principles

| Customer Survey Fourth Category: Conceptual | | |
|---|----------------------------|------------|
| Characteristics | Response category | % |
| Customers awareness degree regarding sharia law | Very well | 12% |
| | Sufficiently | 62% |
| | Not much | 24% |
| | Never thought before about | 3% |
| Customers awareness of sharia law | Yes | 91% |
| | No | 9% |
| Customers awareness of the profit and loss sharing principle | Yes | 85% |
| | No | 9% |

| | | |
|--|---------------|-------|
| | I do not know | 5.90% |
|--|---------------|-------|

In regards to customer's response to the question asked from them about interest.

Almost 92% of the customers know that in Islamic banking interest is prohibited while 8% are unaware of this principle. Regarding profit and loss sharing principle of Islamic banking, 85.30% of customers have enough knowledge about profit and loss sharing principle of Islamic banks. While 8.8% respond negatively with no, 5.90% said they do not know.

Response of customers related to last question of about sharia supervisory board, surprisingly 52.9% of customers answered with no to this question related to sharia supervisory board.

While 32.4% said they know about it, 14.7% did not know anything about it.

4. 3 Research Findings

This descriptive study is done based on two surveys related to employees and customers to find out the distinguishing features of Islamic banking in three private banks located in Kabul. For the purpose of analysis, the primary data collected form these banks are grouped in different categories such as demographics, bank related information, product related information, customer or employee related information and conceptual part related information.

The First category of both surveys is allocated for demographic information of employees and customers. According to the employee survey analysis and discussion part, most respondents are male from young age group (18 – 38). Most of them have a bachelor or higher degree in banking, finance and business but a very small portion of them studies Islamic banking. In addition, most employees who responded to survey are working in the customer service and operation departments, however, in 34% who selected other option and then specified their occupation at bank a very small portion is employees working in managerial or sharia supervisory board. Though, due to security issues during data gathering, there was lack of female staff, but it is quite interesting to know that most employees of the

bank are young aged group. However, lack of experts specifically of Islamic banking education background exist. Based on these findings, to develop Islamic banking system, banks should provide some opportunities for their young employees to further study, specifically in Islamic banking area.

According to the customer survey analysis and discussion part of demographic, most customers are male from age group (18 – 38), having education level of bachelor or higher, working in private sector. Because of security reasons it can be inferred that the high portion of male respondents are reasonable but lack of other age group customers and lack of customers who work for government or have private business as customers in Islamic banking can be something that banks should consider for future development of Islamic banking. One recommendation for the bank for the purpose to increase number of customers can be to provide some specific products and services for those who work for government or have own businesses.

According to the employee survey primary data analysis and discussion, most respondents are from Bakhtar bank as it is going to be the first full fledge Islamic bank in Afghanistan and AIB bank. Due to security issues and as Gazanfar bank was located near to the blast so it was difficult to approach their employees during data collection period so small portion of respondents are from this bank. Most employees have been working for the bank for less than one or two years which is reasonable because most of the respondents were from operation and customer service departments only. Usually from these departments employees are given promotion or they change jobs but some who selected more than five years were working as sharia board members. Another very important point in this category was bank related information disclosure with public or customers. Around 75 percent said that they do share information and 25 percent said they do not, but even those who said yes and then specified the information they share is not enough information about a bank for disclosure to

enhance trust and credibility among its customers. As a recommendation for the Islamic window or bank, in respect to employees to increase number of loyal employees with specialization in Islamic area and in respect to customer to build trust, credibility and reputation banks should share more information with customers such as information about their corporate responsibilities and social activates.

According to the customer survey primary data analysis and discussion, similar finding for customers exist. Due to security concerns, most respondents are from Bakhtar and AIB banks. It is quite interesting that three most selected reasons for the selection of bank by customers are religion, confidence and reputation. Among these the main reason is religion based on the percentage. Something that can be recommended for the banks, for the purpose of sustainability in competitive market of banking, it is essential to develop different areas. For the purpose of profitability and value creation, it is important to attract and retain customers. As most customers have been using bank products for less than year or two, number of loyal customers are less so the bank can find out ways for increasing their loyal customer number. Another important part of this study was that almost 50% have already used non Islamic banking products so they share their view about three main distinguishing features of Islamic banking. Three most selected ones are interest free feature, compliance with sharia law feature, and bank fund contribution in social welfare projects feature. Customers are unaware of other important and distinguishing features of Islamic banking such as existence of SSB, and profit and loss sharing. However, it is interesting to find out that though there are some problems in Islamic banking but still more than 90% of customers are satisfied from these banks products and services.

According to the employee survey primary data analysis and discussion, the study find out that from the employee point of view among the 17 Islamic banking products, ten most selected products in descending order are Mudrabah, Musharakha, Ijarah, Qard

Hassana, Wadiyah, Aqad, Wakalah, Istisna, Bai'Salam, and Musowamah. Overall almost half of employees believe that demand for Islamic banking products have increased but other half believes that demand has been constant or decreased which means there has not been a significant change in demand for Islamic banking. Another finding is that for the above products offered by bank customer demand is high so the bank is only focusing on products where customer demand is high. One recommendation especially for Bakhtar bank that will be soon full fledge Islamic bank to focus more on their products and if possible to run programs to create demand and awareness in customers for products that are new to launch.

According to the customer survey primary data analysis and discussion, most customers selected Mudrabaha as the product they use the most, and some selected Qarz Hassana and Musharakha and very few Wadiyah. As a distinguishing feature of Islamic banking, where money invested through bank is very important and most customers said they do query about the projects by asking for information where their funds are invested to make sure their money is invested in social welfare projects and is not involve in non-Islamic activities such as gambling.

There is one extra category for employees that include information specifically about customers. Most of the employees said that they brief customers with different information, and customers said that they also do ask for information brief. In their point of view most customers of Islamic banking products are Muslims and reason for that is the religion sensitivity of the customers that impact their decision to use these products.

Last category for both employee and customer survey is based on conceptual part of the study. According to the employee survey discussion and analysis part, most employees believe that Islamic products are compliant with sharia law. When their asked to provide distinguishing features of Islamic banking, most of them provided reliable and credible features of Islamic banking. Another important aspect of Islamic banking, existence of sharia

supervisory board, based on employee respondents, the banks have sharia board, but there is one sharia supervisory board in Afghanistan National Bank (De Afghanistan Bank) or ADB that supervise all Islamic banking windows. Based on my personal observation of the banks, I find it out that though in each bank sharia board exists, but they have very limited board members that are not available and live abroad. Only I had been able to meet two members of the sharia board from Bakhtar bank that were very supportive and provided enough information about Islamic banking. Recommendation is that though Islamic products are in compliance with sharia law to some extent but for the development of Islamic banking and launching of new products, existence of sharia board and expert members are essential so that banks should be considering this important point. Another important distinguishing feature of Islamic banking is that there should be a separate system for the bank funds coding circulation, but most employees did not know about it and some said they use the same system as conventional banking which then contradicts the difference between these two banks. Recommendation is that banks should work on different accounting and auditing systems of Islamic banking, which is possible if they hire and train experts in these areas.

According to the customer survey discussion and analysis part of the conceptual part, customers are well aware of the interest ban and profit and loss sharing principles of Islamic banking, but they are not sufficiently aware of the sharia law principles and existence of sharia board. Recommendation is to increase awareness and knowledge of Islamic banking in customers through different programs such as Islamic marketing programs or school curriculum. To sum up the finding and recommendations, these findings and recommendations from different categories of the employee and customer surveys can be related to the five conceptual framework parts of this study as following:

- **Products and services compliance with Islamic principles:** the finding is that products and services are compliant with Islamic principles but there are very limited products

available, where the customer demand is medium but Islamic banking products had constant or decreasing growth. That means that there is lack of research and development programs in Islamic banking sector. Recommendations are to do more research and development programs, to focus more on launching new products in compliance with sharia law, creating demand in the market for them, running programs to aware target market about their benefits and distinguishing features based on Islamic religion.

- **Accounting and auditing system:** there is lack of separate accounting and auditing system for Islamic funds due to lack of professionals and experts in this area as well as decreasing or constant growth rate of Islamic banking. Recommendation is to hire more professional employees to develop a different accounting and auditing system for Islamic funds that will help the enhancement of Islamic banking and credibility of it.
- **Legal and regulatory aspects and Sharia Supervisory Board:** there is lack of sufficient sharia board members to control the legal and regulatory aspects of Islamic banking. Recommendations, as a short term goal in this regard banks can hire professionals but as a long term goal for development they can use their young employee's energy by providing them career development opportunities of trainings and specialization in Islamic banking area.
- **Customer selection of the bank, awareness and attitude:** as a whole customer attitude toward Islamic banking is positive though there is lack of awareness of sharia law and sharia board existence in Islamic banking among customers. Most customers select the bank because of religious reasons. Recommendations are to develop Islamic banking products and service and run programs of awareness through school curriculum or marketing programs to develop reputation, credibility and trust among customers by acknowledging them about the fundamentals of Islamic banking which is not only

compliance to Islamic principles and their religious beliefs but provide them Islamic profit.

Chapter Five: Conclusion

The findings of this study indicate that there is lack of sufficient Islamic products in compliance with sharia to match the demand of customers is decreasing or there is not enough efforts for creation of new demand for the sustainability of Islamic banking in the competitive market of banking sector.

There is also a lack of Islamic banking accounting and auditing professionals to develop a separate and credible system for its funds. To develop and control the legal and regulatory aspect of Islamic banking, banks can hire professionals, but for long-term purposes they can invest in their own young employees. To attract and retain customers, it is important to know the reasons they select the bank and how much they are aware about the features of new products so the bank can develop programs in response.

Thus, features such as separate accounting and auditing system, customer awareness of interest ban and profit and loss sharing principles of Islamic banking, and funds investment in social and welfare projects as well as existence of sharia board, probably can be the main distinguishing features of Islamic banking. In contrast, information disclosure, reasons of selection of Islamic banking, better service, ethical issues are not only relate to Islamic banking but also to conventional banking.

Based on the results, there is not much difference in operation of Islamic and conventional banks so Islamic banking should have taken more efforts to become distinguished from non-Islamic banking by providing more sharia compliance products for sharia loyalist segment target market with running programs for awareness of these products and increasing potential sharia board members.

Recommendations for future study in this area is, this study is based only on Islamic banking on three banks two with Islamic windows and one that is not yet a full fledge Islamic bank but will soon be so that would be better if selected more banks for the reliability of the research.

Another point is that this study is done in a descriptive way, which has some limitations but it is found that there is not much research done in this areas so this exploratory study as a pioneer study in this area is still remarkable in the limited time with security issues and limited sample size.

Lastly, there is still many other aspects for exploration and examination of Islamic banking concepts and standards that can be done in future studies such as to explore that how these distinguishing features impact Islamic banking growth and effectiveness.

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Appendix

Table 1. Islamic Banking Market in MENA Region

| Country | Number of full fledge Islamic banks | Number of conventional banks with Islamic banking window |
|--------------|-------------------------------------|--|
| Saudi Arabia | 4 | 8 |
| Egypt | 3 | 14 |
| Pakistan | 5 | 12 |
| Jordon | 4 | 0 |
| Yemen | 4 | 3 |
| Tunisia | 0 | 1 |
| Iraq | 10 | 0 |
| Morocco | 0 | |
| Lebanon | 0 | 5 |

Table 2. Islamic Assets and Deposit Development in MENA Region Countries

| Country | Year | Assets (A) / Financing (F) | Compounded annual growth rate | Deposits | Compounded annual growth rate |
|--------------|------|----------------------------|-------------------------------|----------|-------------------------------|
| Saudi Arabia | 2010 | 117.3 (F) | 23% | 155.8 | 15% |
| | 2011 | 143.1 (F) | | 181.5 | |
| | 2012 | 178.3 (F) | | 204.9 | |
| Egypt | 2010 | 9 (A) | 13% | 8.4 | 11% |
| | 2011 | 10.5 (A) | | 9.6 | |
| | 2012 | 11.5 (A) | | 10.4 | |
| Pakistan | 2010 | 4.8 (A) | 32% | 3.9 | 35% |
| | 2011 | 6.4 (A) | | 5.2 | |
| | 2012 | 8.4 (A) | | 7.1 | |
| Jordon | 2010 | 3.1 (F) | 28% | 0.5 | 8% |
| | 2011 | 3.4 (F) | | 5.7 | |
| | 2012 | 3.1 (F) | | 5.8 | |
| Yemen | 2010 | 0.9 (F) | 0% | 2.1 | 9% |
| | 2011 | 0.7 (F) | | 1.8 | |
| | 2012 | 0.9 (F) | | 2.5 | |
| Tunisia | 2010 | 0.6 (A) | 33% | 0.5 | 26% |
| | 2011 | 0.9 (A) | | 0.8 | |
| | 2012 | 1.1 (A) | | 0.8 | |
| Iraq | 2009 | 0.3 (F) | 28% | 0.5 | |
| | 2010 | 0.5 (F) | | | |
| Morocco | 2009 | 0.1 (F) | 13% | | |
| | 2012 | 0.1 (F) | | | |
| Lebanon | 2010 | 0.1 (F) | 26% | 0.2 | 28% |
| | 2011 | 0.1 (F) | | 0.2 | |

| | | | | | |
|--|------|---------|--|-----|--|
| | 2012 | 0.1 (F) | | 0.3 | |
|--|------|---------|--|-----|--|

Table 3. Elements of Profit and Loss Sharing

| | | |
|---|---|---|
| Products and Services | Projects with specific end (Musharakah) | Certificate for PLS on special projects |
| | | Certificate for PLS on a projects portfolio |
| | | Certificate for PLS on Islamic banking |
| Projects with unspecific end (Pazireh) | | Certificate to shares |
| Customers | Depositors | Real body |
| | | Legal body |
| | Entrepreneurs | Legal body entities |
| Financial mediums | Insurance representatives | |
| | Portfolio management team | |
| | | |
| | | |
| | Insurance certificate | To avoid moral hazard |
| | | To avoid adverse selection |
| | | To avoid asymmetric information |
| | Executive insurance | To insure responsibility To insure place for the project |
| IT base transaction system for Musharakah and Pazireh | Information system | |
| | Remote selling and buying system for Islamic banking products | |
| | 24 hours per week service system | |
| | Multi languages system | |
| | Multi currencies system | |
| | Integrated system | |
| | High security system | |
| | Privacy system | |
| Contractions | Depositor | Jualah |
| | | Wakalah |
| | | Solh |
| | Entrepreneur | Musharakah |
| | Consultant | Jualah |
| Infrastructure | Strategy committee for profit and loss sharing principle | |
| | Expertise committee for revising profit and loss sharing principles | |
| | Profit and loss sharing | Legal department |
| | | Project evaluation department |
| | | Financial management department |
| | | Trustees department |

| | | |
|--------------|------------------------------------|--|
| | departments | Auditing department PLS front office Cashier Consulting services department Transactions |
| Contracts | Contract with entrepreneurs | |
| | Contract with depositors | |
| | Contract with trustees | |
| | Contracts for evaluation | |
| Instructions | Required documents | |
| | Entrepreneur ability to reach | |
| | Reports for justifications | |
| | Accounting and auditing | |
| | Guarantees, collaterals and inputs | |
| | Returns | |
| | Contract conditions | |
| | Contract settings | |
| | Supervision standards | |
| | Competencies of trustee | |
| | Reports from entrepreneur | |
| | Transactions | |
| | Certificates exchange | |
| | Variation in time schedule | |
| | Partnership | |
| | Cancelation from depositor side | |
| | Settlement | |
| | Arbitration | |
| | Unexpected forces | |

Table 4. Classification of Islamic Instruments Based on Contractual Bases

| | | | | |
|--|--------------------------|---------------------------|-----------------------|-----------|
| Islamic instruments (Islamic contracts) | Contracts as transaction | Miscellaneous | Qard Hassana | |
| | | Securities based on asset | Trade Financing | |
| | | | Murabaha | |
| | | | Bay salam | |
| | | | Bay Mua'ajal | |
| | | Equity | Ijara | |
| | | | Collateral Securities | |
| | Contracts as mediator | Istisna | | Musharaka |
| | | Mudarabaha | | |
| | | Kifala | | |
| | | Amana | | |
| | | Takaful | | |
| | | Wikala | | |
| | | Ju'ala | | |

Table 5. Islamic Instrument and Contracts Catogorization

| | | | |
|---|------------------|--|--|
| Islamic instrument and contracts | Financing | Trade finance | Murabahah (Cost-plus-Sale) |
| | | | Bay' Salaam (Forward Sale) |
| | | | Bay' Muajil (Deferred Payment Sale) |
| | | Ijarah (Leasing) Istisnah (Manufacturing) | |
| | Investing | Mudarabah (Principal/Agent Partnership) | |
| | | Musharakah (Equity Partnership) | |
| | Other | Services with free base | Kifalah (Guarantee) |
| | | | Joalah (Fee-for Service) |
| | | | Amanah (Custody) |
| | | | Wikalah (Representation) |
| | | Social welfare | Qard Hassan |
| | | | Waqf |
| | | Tikaful (Insurance) | |

Table 6. Key Instruments of Islamic Finance

| Terms | Descriptions |
|---|---|
| Amana (Demand deposits) | Deposits held at the bank for safekeeping purpose. They are guaranteed in capital value, and earn no return. |
| Bay mu'ajal (Pre-delivery, deferred payment) | The seller can sell a product on the basis of a deferred payment, in installments or in a lump sum. The price of the product is agreed upon between the buyer and the seller at the time of the sale, and cannot include any charges for deferring payment. |
| Murâbahah (Mark-up financing) | The seller informs the buyer of his cost of acquiring or producing a specified product. The profit margin is then negotiated between them. The total cost is usually paid in installments. |
| Ijârah (Lease, lease purchase) | A party leases a particular product for a specific sum and a specific time period. In the case of a lease purchase, each payment includes a portion that goes toward the final purchase and transfer of ownership of the product. |

| | |
|--|---|
| Salam (Prepayment, deferred delivery) | The buyer pays the seller the full negotiated price of a product that the seller promises to deliver at a future date. |
| Istisna (Deferred payment, deferred delivery) | A manufacturer (contractor) agrees to produce (build) and to deliver a certain good (or premise) at a given price on a given date in the future. The price does not have to be paid in advance (in contrast to salam). It may be paid in installments or part may be paid in advance with the balance to be paid later on, based on the preferences of the parties. |
| Ju'ala (Service charge) | A party pays another a specified amount of money as a fee for rendering a specific service in accordance with the terms of the contract stipulated between the two parties. This mode usually applies to transactions such as consultations and professional services, fund placements and trust services. |
| Kifala | It is a pledge given to a creditor that the debtor will pay the debt, fine or liability. A third party becomes surety for the payment of the debt if unpaid by the person originally liable. |
| Mudârabah (Trustee finance contract) | Capital's owner provides the entire capital needed to finance a project while the entrepreneur offers labor and expertise. Profits are shared between them at a certain fixed ratio, whereas financial losses are exclusively borne by Capital's owner. The liability of the entrepreneur is limited only to his time and effort. |
| Musharakah (Equity participation), | The bank enters into an equity partnership agreement with one or more partners to jointly finance an investment project. Profits are distributed according to predetermined ratios, and losses are shared strictly in relation to the respective capital contributions. |
| Qard Hassan (Beneficence loans) | These are zero-return loans that the Qur'an encourages Muslims to make to the needy. Banks are allowed to charge borrowers a service fee to cover the administrative expenses of handling the loan. The fee should not be related to the loan amount or maturity. |

Source: (M. Hussain et al., 2016)

Questionnaire for Employees

American University of Afghanistan (AUAF)

Islamic Banking Research Study

Primary Research Data Source

I am one of the senior MBA program students at AUAF. This project is in Islamic banking area, “Islamic banking features”. Your time spent on taking part in this research study is highly appreciated.

Part One: Demographics

Please answer the following questions by tick marking the appropriate cell:

- 1. Gender:** Male Female
- 2. Age:** less than 18 years old 18 – 28 years old
 29 – 38 years old 39 – 48 years old
 49 – 50 years old more than 50 years old
- 3. Educational level:**
- Secondary school
 - Diploma
 - Bachelor
 - Master
 - PhD

4. Area of Education:

- Business
- Finance
- Banking
- Islamic Banking
- Other (Please specify)

Part Two: Bank Related Questions

5. Employee at:

- Bakhtar Bank
- AIB Bank

Ganzanfar Bank

6. Occupation at Bank

- Customer service
- Treasury
- Operations
- Risk management
- Other _____

7. For how many years you have been working in banking area:

- Less than one year 1 – 2 years
- 2 – 3 years 3 – 4 years
- 4 – 5 years more than 5 years

8. Do the bank provide any information disclosure for their costumers?

- Yes No

If yes, what kind of information they disclosure?

Please specify

Part Three: Product and Services Related Questions

9. Which products are offered through your bank?

- Musharakah (joint venture) Hiba (gift)
- Bai' al 'inah (sale and buy bank agreement) Ijarah (lease)
- Bai' bithamah ajil (differed payment sale) Sukuk (bond)
- Bai' muajjal (credit safe) Takaful (insurance)

- Mudrabah (Profit and Loss sharing)
- Wadiyah (safe keeping)
- Bai' Salam (contract with advance agreement)
- Aqad (contract)
- Musowmah (bargining)
- Qard hassana (good loan)
- Wakalah (power of attorney)
- Istisna (Manufacturing finance)
- Tawaraq (literally into silver)

10. The demand for Islamic banking products and services has:

- Significantly Increased
- Increased
- Constant
- Decreased
- Significantly decreased

11. Please rate the following products based on the customer demand using 1 – 5, while

1 stands for very high and 5 stand for very low:

| 1 | 2 | 3 | 4 | 5 |
|------------------|-------------|---------------|------------|-----------------|
| Very High | High | Medium | Low | Very Low |

| Products | 1 | 2 | 3 | 4 | 5 |
|--|---|---|---|---|---|
| Musharakah (joint venture) | | | | | |
| Hiba (gift) | | | | | |
| Bai' al 'inah (Sale and buy bank agreement) | | | | | |
| Ijarah (lease) | | | | | |
| Bai' bithamah ajil (Differed payment sale) | | | | | |
| Sukuk (bond) | | | | | |

| | | | | | |
|---|--|--|--|--|--|
| Bai' muajjal (Credit safe) | | | | | |
| Takaful (insurance) | | | | | |
| Mudrabah (Profit and Loss sharing) | | | | | |
| Wadiah (Safe keeping) | | | | | |
| Bai' Salam (Contract with advance agreement) | | | | | |
| Aqad (contract) | | | | | |
| Musowamah (bargining) | | | | | |
| Qard hassana (good loan) | | | | | |
| Wakalah (Power of attorney) | | | | | |
| Istisna (Manufacturing finance) | | | | | |
| Tawaraq (Literally into silver) | | | | | |

Part Fourth: Customer Related Questions

12. Do you brief customers about the different products and services provided by Islamic window/bank?

Yes NO

13. Based on your experience, do Islamic banking customers asking for a brief regarding the difference between Islamic and non-Islamic banking products and services before buying them?

Always Usually
 Sometimes Often
 Rarely Never

14. Who are most customers of Islamic banking products and services?

Muslims

- Non-Muslims
- Both

15. In your opinion is the religion of customers has any impact on the products they demand for?

- Yes
- No

If yes why what is the _____
reason?

Part Fifth: Conceptual Related Questions

16. To which extent do you agree or disagree that the products that your bank provide are in compliance with islamic principles:

- Strongly Agree
- Agree
- Neither Agree nor Disagree
- Disagree
- Strongly Disagree

17. In your opinion what are the four distinguishing features of Islamic banking?

18. Does your bank have sharia supervisory board (SSB)?

Yes

No

I do not know

19. Coding circulation of funds of Islamic banks traced and controlled:

Same way as conventional banks

In a differently from conventional banks

I do not know

Questionnaire for Customers

American University of Afghanistan (AUAF)

Islamic Banking Research Study

Primary Research Data Source

I am one of the senior MBA program students at AUAF. This project is in Islamic banking area, “Islamic banking features”. Your time spent on taking part in this research study is highly appreciated.

Part One: Demographic

Please answer the following questions by tick marking the appropriate cell:

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 29 – 38 years old 39 – 48 years old
 49 – 50 years old more than 50 years old
- 3. Educational level:**
- Secondary school
 - Diploma
 - Bachelor
 - Master
 - PhD
- 4. Occupation**
- Government sector
 - Private sector
 - Self-employed
 - Student
 - Other _____

Part Two: Bank Related Questions

5. Customer of:

- Bakhtar Bank
- AIB Bank
- Ganzanfar Bank

6. Please select three main reasons for selecting the bank that you are customer of:

- Reputation Confidence Religion
- Service Location Quality
- Convenience Cost efficiency Family and friends refer

- Productivity Ethical reasons Staff friendliness

- Credibility of the bank Confidence on Sharia Supervisory Board

7. Number of years being customer of bank:

- Less than one year One to tow years Two to three years
- Three to four year Four to five years More than five years

8. Did you ever use products and services of conventional banks?

- Yes No

If yes, what three main differences did you notice between Islamic banking and conventional banking?

9. To what extent you are satisfied of the products, services and overall facilities available by the bank:

| Highly Dissatisfied | Dissatisfied | Neither satisfied nor dissatisfied | Satisfied | Highly satisfied |
|---------------------|--------------|------------------------------------|-----------|------------------|
| | | | | |

Part Three: Product and Services Related Questions

10. Are you customer of which of the following products or services of the Islamic bank?

- Musharakah (joint venture) Hiba (gift)
- Bai' al 'inah (sale and buy bank agreement) Ijarah (lease)
- Bai' bithamah ajil (differed payment sale) Sukuk (bond)
- Bai' muajjal (credit safe) Takaful (insurance)
- Mudrabah (Profit and Loss sharing) Wadiyah (safe keeping)
- Bai' Salam (contract with advance agreement) Aqad (contract)
- Musowamah (bargining) Qard hassana (good loan)
- Wakalah (power of attorney) Istisna (Manufacturing finance)
- Tawaraq (literally into silver)

11. While depositing in Islamic banks do you ask the staff to provide information about how and where your deposits are invested?

- Yes No

If yes, usually what kind of information they provide:

Part Fourth: Conceptual Related Questions

12. How much do you know about sharia law for Islamic banking?

- Very well
- Sufficiently
- Not much
- Never thought about it before

13. Do you know that interest is prohibited in Islamic banks?

- Yes
- No
- I do not know

14. Do you know about the profit and loss sharing feature of Islamic banks?

- Yes
- No
- I do not know

15. Do you know about Sharia Supervisory Board in Islamic Banks?

- Yes
- No
- I do not know

Questionnaire for Customers in Persian language

بخش مشتریان

(پوهنتون آمریکایی افغانستان) AUAF

تحقیق درباره بانکداری اسلامی

خدمات و سهولت ها

من یکی از محصلین دوره ماستری تجارت و مدیریت پوهنتون آمریکایی افغانستان می باشم. تحقیق من در زمینه بانکداری اسلامی (خدمات و محصولات بانکداری اسلامی) در افغانستان است. اشتراک شما در این سروی قابل قدر می باشد.

لطفا سوالهای زیر را با پر کردن خانه خالی ها جواب دهید

۱. جنس:

مرد

زن

۲. سن:

کمتر از ۱۸ سال

۳۹ – ۲۹

بیشتر از ۶۰ سال

۵۹ – ۵۱

۳. میزان تحصیلات:

لیسه

دیپلم

لیسانس

ماستری

دکترا

۴. نوع شغل:

بخش دولتی

بخش خصوصی

کار شخصی

محصل

دیگر موارد

۵. مشتری کدام بانک میباشد:

باختر بانک

بانک بین المللی افغانستان (AIB)

غضنفر بانک

۶. لطفا سه دلیلی را که بانکداری اسلامی را انتخاب کرده اید را از گزینه های زیر مشخص کنید:

اعتبار دین اعتماد

خدمات کیفیت موقعیت

راحتی توصیه فامیل یا دوستان کم شدن مصارف

تولیدات رویه خوب کارمندان دلایل اخلاقی

اعتبار بانک اعتماد بالای بورد نظارتی شریعه

۷. چند سال مشتری این بانک هستید:

دو تا سه سال یک تا دو سال کمتر از یک سال

بیشتر از پنج سال چهار تا پنج سال سه تا چهار سال

۸. آیا گاهی خدمات بانکهای غیر اسلامی را امتحان کرده اید:

بلی

خیر

اگر بلی سه نفوایت عمدی بین بانکداری اسلامی و غیر اسلامی را شرح بدھید:

۹. به کدام اندازه از خدمات و امکانات بانک رضایت دارید:

| | | | | |
|-------------|--------|---------------------|------|-----------|
| خیلی ناراضی | ناراضی | نه راضی و نه ناراضی | راضی | خیلی راضی |
| | | | | |

۱۰. از کدام محصولات یا خدمات بانکداری اسلامی استفاده میکنید:

هبه

مشارکه

اجاره

بيع الاناء

صکوک

بيع بیتمان عاجل

تکافل

بيع معجل

ودیعه

مضاربه

عقد

بيع سلام

قرض الحسنہ

مساومہ

استصناع

وكاله

تورق

۱۱. وقتی که حساب یا اکانت باز میکنید از بانک میپرسید که پول شما در کجا و در چه راهی سرمایه گزاری میشود:

بلی

خیر

اگر بلی معمولاً چه نوع اطلاعاتی برای شما داده میشود:

۱. چقدر در مورد قوانین شریعت در بانکداری اسلامی معلومات دارید:

بسیار زیاد

به اندازه کافی

نه خیلی زیاد

قبل درباره آن فکر نکرده ام

۱. آیا میدانید سود در بانکداری اسلامی ممنوع است:

بلی

خیر

هیچ معلومات ندارم

۱. آیا در مورد شریک بودن در سود و زیان در سیستم بانکداری اسلامی معلومات دارید:

بلی

خیر

هیچ معلومات ندارم

۱. آیا در مورد بورد نظارتی شریعه در بانکداری اسلامی معلومات دارید:

هیچ معلومات ندارم