

Microfinance Sector in Afghanistan (2026): Stabilization, Constraints, and Emerging Pathways

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1. Sector Snapshot: A Small but Stabilizing Ecosystem

Afghanistan is considered to be one of the youngest nations in the world, with an estimated 70% of its population under the age of 25 ^[1]. The Afghan economy is predominantly driven by Micro, Small and Medium Enterprises (MSMEs), which — based on industry expert estimates — account for over 80% of private sector activity. Given this structural dependence on small-scale enterprise, the microfinance sector's role as a provider of productive finance is critically important. However, with an active client base of approximately 66,498 as of Q1 2026, the sector currently serves only a small fraction of its potential market, leaving a vast financing gap unaddressed.

The principal Islamic financing product in use today is Murabaha — a cost-plus sale arrangement — which was the first product formally approved by the Supreme Court of Afghanistan and relevant regulatory authorities. In addition, several MFIs have received approval from Da Afghanistan Bank (DAB), the central bank and primary regulatory authority, to offer additional instruments including *Salam* ^[2] and *Wakala* ^[3]. Financing under these products is in its initial

phases, and the sector faces operational challenges related to client awareness, transactional complexity, and the limited experience of institutional staff in managing these instruments.

As of early 2026, Afghanistan's microfinance sector remains small in size but structurally resilient, operating under a constrained economic and regulatory environment.

Key Sector Indicators (Q1 2026):

- Active Islamic Financing Clients: 66,498
- Gross Financing Portfolio (GFP) Outstanding: USD 77.3 million (AFN 4.96 billion)
- Active institutions: 6 MFIs and 1 microfinance bank
- Branch network: 96 branches across the country
- Geographic outreach: 24 provinces

Institutional Snapshot and Financing Patterns:

Institution	Gross Islamic Financing Outstanding (AFN)	Active Islamic Financing Clients	Average Financing / Client (AFN)
First MicroFinance Bank Afghanistan (FMFB)	1,927,770,482	20,601	93,577
Mutahid Development Finance Institution (MUTAHID)	609,589,270	14,267	42,727
OXUS Afghanistan	1,726,914,678	28,949	59,654
Shahy Khazana Microfinance (SKM)	61,309,682	871	70,390
Momin Afghan Microfinance Institution (MAMI)	109,035,989	967	112,757
Lamen Microfinance Institution (LAMEN)	25,527,371	186	137,244
Hassel (Agriculture Development Fund)	502,878,549	657	765,416
Total	4,963,026,022	66,498	74,634

Source: MISFA Monthly Performance Report, Q1 2026

As evident from the table above, the microfinance sector in Afghanistan is comprised of established institutions such as FMFB, Mutahid and OXUS which have been operating for nearly two decades and the new institutions (MAMI, LAMEN, SKM and Hassel) that entered the market following the enforcement of the 'microfinance regulation' by DAB in late 2024.

The distribution of average financing sizes across institutions clearly reflects intentional market segmentation. Institutions such as Mutahid Development Finance Institution (MUTAHID) are focused on the ultra-micro and vulnerable segment, with significantly smaller ticket sizes — consistent with a financial inclusion mandate aimed at bottom-of-the-pyramid clients. While this approach may involve higher operational costs due to smaller transaction sizes, it delivers significant social impact by reaching underserved populations.

In contrast, mid-tier players like OXUS Afghanistan and Shahy Khazana Microfinance Institution (SKM) operate in the core microenterprise space, offering moderate financing sizes aligned with typical working capital and business investment needs. OXUS in particular stands out as a

balanced and scalable model — combining the largest client outreach with moderate financing sizes — positioning it effectively between financial inclusion and operational sustainability.

At the upper end of the market, First MicroFinance Bank Afghanistan (FMFB), MAMI, and LAMEN cater to upper-micro and SME segments. FMFB's positioning is particularly notable: its average financing size is well above the overall sector average of AFN 74,634 per client. This likely reflects a deliberate strategy toward financial self-sustainability — larger financings reduce administrative cost per unit of portfolio and are better aligned with established businesses that have stronger documentation and repayment capacity. Alternatively, FMFB may be focusing on providing larger and more expensive productive assets to clients, consistent with its identity as a bank-led microfinance institution.

Most notably, Hassel — the microfinance arm of the Agriculture Development Fund — emerges as an outlier with the highest average financing size in the sector at AFN 765,416, significantly exceeding even FMFB. Hassel's model is specialized and distinct: it operates predominantly in rural areas across 18 provinces, focusing almost entirely on agriculture (AFN 235.5 million) and livestock/poultry (AFN 112.3 million) financing. Unlike other MFIs, Hassel provides a grace period feature that aligns repayment with agricultural harvest cycles — a critical design element for agricultural financing. With 88% of its clients being male and rural, Hassel fills a unique niche that no other sector actor currently occupies at scale.

Institutions like LAMEN and MAMI, while showing high average financing sizes with limited outreach, appear to be operating in pilot or niche segments — potentially targeting salaried individuals, SME financing, or asset-backed arrangements. This reflects an early-stage movement within the sector toward upstream client segments, albeit on a limited scale.

On the question of client demographics, the sector serves a mix of self-employed micro-entrepreneurs (the dominant profile) and salaried individuals (particularly at MAMI). Female clients constitute approximately 43% of the active client base across MISFA-supported MFIs — a notable level of gender inclusion given Afghanistan's current operating environment — though Hassel's client base remains predominantly male, reflecting the rural and agricultural nature of its outreach.

This layered institutional positioning illustrates a sector that is not uniform but rather strategically diversified across outreach, impact, and commercial sustainability objectives. This footprint reflects a post-crisis recovery phase, with institutions maintaining operations despite funding shortages, regulatory changes, and macroeconomic uncertainty.

2. Regulatory Shift: Stronger Oversight and Profit Controls

The political developments in mid-August 2021 fundamentally changed the regulatory environment of the sector, leading to complete termination of the conventional (interest-based) financial system and replacement with a system based on Sharia-compliant principles and practices. This ongoing transition involves waiver of outstanding interests, the cessation of conventional lending and its replacement with approved Islamic financing products as well as the development of Sharia-compliant governance structure, policies and institutional capacity. The other most significant development during 2025–2026 has been the enforcement of a microfinance regulation which include an increasing role of Da Afghanistan Bank (DAB) in the microfinance sector. Two major regulatory shifts stand out:

a. Direct Supervision of MFIs

- DAB has begun actively supervising microfinance institutions, moving from a largely passive oversight role to direct regulatory engagement
- Approval processes now include vetting of senior management and board members

This marks a transition toward formal regulatory integration, which strengthens governance standards but also increases compliance requirements and administrative burden — particularly for smaller institutions with limited capacity.

b. Introduction of a Profit Rate Cap (16% p.a.)

- MFIs are now restricted from charging above a 16% profit rate p.a. on financing products

While the profit cap is positive for client protection and affordability in theory, its practical impact on sector behavior warrants careful scrutiny. Given Afghanistan's high operational costs, low borrower density, and weak infrastructure, the cap compresses margins significantly — particularly for institutions serving remote or rural areas where the cost per client is structurally higher.

A critical risk is that the cap may further entrench the sector's urban bias. Institutions operating in underserved or excluded provinces — where financial exclusion is already severe — face higher per-client costs due to poor road networks, sparse populations, and limited digital infrastructure. Under the 16% ceiling, expanding into such areas becomes financially unviable for commercially oriented institutions, potentially making the sector even more concentrated in urban and peri-urban areas. Rather than promoting inclusion, the cap may inadvertently restrict it.

Compared to regional markets such as Pakistan and India, where profit rate ceilings are either absent or set at higher levels, Afghanistan's cap is relatively restrictive. Policymakers and DAB may wish to consider a differentiated pricing framework that accounts for the cost of rural and agricultural outreach, rather than applying a uniform ceiling that disadvantages institutions serving the hardest-to-reach segments.

3. Portfolio Quality: Exceptionally Strong but Context-Specific

The sector demonstrates very strong portfolio performance indicators:

- Repayment rate: 95.5%
- Portfolio at Risk (PAR) greater than 30 days: 0.2%
- Write-offs: minimal (USD 592)
- Restructured portfolio: USD 19,016

This exceptional performance can be attributed to several factors: The Islamic financing structure which involves transfer of physical commodities and goods rather than cash disbursements; conservative financing practices with strong client selection; a relatively low client-to-financing officer ratio that enables close relationship management; and the overall modest scale of the sector, which limits systemic risk.

Portfolio quality is being maintained through cautious growth rather than scale expansion — a deliberate strategy that prioritizes credit discipline over rapid outreach.

4. Demand Dynamics: Trade, Services, and Agriculture

Microfinance demand in Afghanistan is currently driven by income-generating activities. The sector financing portfolio by economic sector (inclusive of Hassel data) as of Q1 2026 is as follows:

Sector	Portfolio Outstanding (AFN)	Share (%)
Trade and Services	2,167,038,845	43.7%
Agriculture	1,135,601,018	22.9%
Livestock (Small & Large Animals)	670,999,021	13.5%
Handicrafts and Manufacturing	674,386,686	13.6%
Housing	172,504,132	3.5%
Others	141,103,973	2.8%
Household Consumption	1,392,346	0.03%
Total	4,963,025,021	100%

Source: MISFA Monthly Performance Report and Hassel data, Q1 2026

The dominance of trade and services (43.7% of the portfolio) reflects the preference for faster cash conversion cycles, stronger collateral arrangements, and lower market volatility compared to primary sector activities. When agriculture and livestock are combined (36.4%), however, primary sector financing constitutes a highly significant share — a level largely attributable to Hassel's specialized agricultural mandate.

The near absence of consumption financing (less than 0.1% of the portfolio) reflects both the sector's adherence to productive Islamic finance principles and MFIs' deliberate focus on sustainability of repayment. This contrasts with many other emerging microfinance markets where consumption-driven lending constitutes a more significant share.

5. Financial Inclusion: Gradual Expansion with Gender Progress

Despite the challenges of Afghanistan's operating environment, there is measurable expansion in outreach. MFIs are actively extending services to previously underserved provinces including Nangarhar, Kunar, Kandahar, Logar, Paktia, and Panjshir, bringing the total geographic reach to 24 provinces as of Q1 2026. Female clients constitute approximately 43% of the active client base across MISFA-supported MFIs, indicating continued commitment to gender-inclusive financing and underscoring the importance of microfinance as a tool for women's economic participation.

Nevertheless, the sector remains strongly urban-centric, with an estimated 75–80% of the portfolio concentrated in major cities. Rural financial inclusion — particularly through agricultural and livestock financing — remains largely dependent on specialized actors such as Hassel, rather than mainstream MFIs. Addressing this structural urban bias will require deliberate incentives for rural outreach, appropriate product design (including grace periods and harvest-aligned repayment schedules), and a regulatory framework that does not penalize higher-cost rural operations.

6. Structural Challenges: A Sector Under Pressure

The Afghan microfinance sector faces deep structural constraints that limit its growth potential and long-term sustainability:

a. Funding Concentration Risk

The Microfinance Investment and Support Facility for Afghanistan (MISFA) provides approximately 54% of total sector funding — rising to an estimated 81% for smaller MFIs excluding banks. This extreme concentration in a single funding source creates systemic vulnerability. If MISFA faces liquidity constraints, donor reductions, or strategic realignment, a significant portion of the sector's lending capacity would be directly at risk. This is not merely a resilience issue — it represents a concentration risk that could trigger institutional failures across multiple MFIs simultaneously.

b. Limited Access to Commercial and International Investors

The absence of commercial investors and wholesale financiers restricts portfolio growth and product innovation, leaving the sector almost entirely dependent on donor-linked capital.

c. Geographic and Infrastructure Constraints

Poor road networks, high outreach costs, and limited rural penetration keep microfinance predominantly urban-centric, excluding the large majority of Afghanistan's rural and agricultural population.

d. Product Concentration

The dominance of Murabaha financing — while appropriate given the regulatory clarity it has received — limits the sector's ability to serve diverse client needs. Limited use of Ijarah, Musharakah, Mudarabah, and other Islamic instruments stems from capacity gaps within MFIs and limited client familiarity with such products.

e. Weak Digital Ecosystem

The lack of interoperability between institutions and the limited functionality of the national payment switch (APS) means that Digital Financial Services (DFS) remain underdeveloped. This restricts the sector's ability to reduce operational costs, extend reach, and leverage mobile and

digital channels for client acquisition and servicing. The ability to scale efficiently is fundamentally constrained without a robust digital infrastructure.

f. Donor Fragmentation

The absence of a coordinated funding mechanism and direct donor-MFI engagement has led to uneven access to funding across institutions. In some cases, fragmented donor relationships risk weakening credit discipline — particularly where grants or subsidized facilities are not structured with performance conditionalities.

g. Human Capital and Governance Deficits

One of the most significant but underappreciated challenges facing the sector in the short to medium term is the weakness of human capital and organizational governance. Staff are often not adequately qualified in Islamic finance product structuring, credit analysis, or financial management. The sector is heavily reliant on a small number of key individuals, creating succession risk and knowledge concentration. Governance structures in many MFIs remain underdeveloped, with boards that may lack the technical expertise needed to provide effective strategic oversight. Addressing this challenge is essential for sustainable growth and is arguably more foundational than any other structural reform.

h. Profit Cap Pressure

As discussed in Section 2, the 16% profit rate cap intensifies sustainability concerns and may discourage outreach to higher-cost rural and underserved areas, compounding the sector's geographic inclusion challenges.

7. Future Outlook: Growth with Strategic Opportunities

The outlook for Afghanistan's microfinance sector reflects cautious optimism, underpinned by gradual institutional expansion and a steady shift toward sustainability. The expected entry of 2–3 new microfinance institutions currently in the licensing pipeline signals renewed confidence in the sector despite a challenging operating environment. This expansion, coupled with outreach into previously underserved provinces, is likely to deepen financial inclusion and improve geographic coverage. At the same time, existing institutions are increasingly focused on strengthening operational efficiency and moving toward self-sustainability, reducing long-term dependence on donor funding and external support.

An important and forward-looking development is the emergence of **green finance** within the microfinance ecosystem. MISFA has independently decided — as a strategic decision of its own, not a regulatory directive from DAB — to allocate at least 5% of its funding toward environmentally sustainable initiatives. This creates opportunities for financing solar solutions, climate-resilient agriculture, and energy-efficient microenterprises — areas that align well with Afghanistan's socio-economic needs and the global shift toward sustainable development finance.

However, these opportunities are tempered by persistent structural and external risks. Reliance on MISFA — a national body whose own funding is subject to donor decisions — represents a key vulnerability for the sector's capacity to respond to existing demand. Regulatory constraints, particularly the profit cap, may limit commercial viability and discourage private sector participation. Weak digital infrastructure remains a critical bottleneck, and the human capital gap described above will constrain the sector's ability to manage complexity and scale efficiently.

Addressing these risks will be essential for translating the sector's positive momentum into long-term, sustainable growth.

8. Strategic Priorities for Sector Strengthening

Based on current realities, the following areas require urgent focus — listed in approximate order of priority:

1. Building Human Capital and Institutional Governance

- Invest in structured training programs for Islamic finance product design, credit analysis, and portfolio management
- Strengthen MFI boards through governance reforms and external expertise
- Develop sector-wide succession planning and knowledge management frameworks

2. Diversification of Funding Sources

- Attract international impact investors and social development finance institutions
- Develop a structured wholesale lending market to reduce dependence on MISFA
- Explore Islamic finance structures (Sukuk, Musharakah-based facilities) to access international capital markets

3. Product Innovation

- Expand beyond Murabaha to include Ijarah, Salam, Wakala, and Musharakah instruments
- Develop agriculture-linked financing products with grace periods and harvest-aligned repayment schedules
- Introduce green finance products targeting solar energy, climate-resilient farming, and energy efficiency

4. Digital Infrastructure Development

- Improve interoperability between MFI systems and national payment infrastructure
- Strengthen the Afghanistan Payment System (APS) to enable real-time digital transactions
- Develop agent banking and mobile-based client acquisition models for rural outreach

5. Rural Expansion Strategy

- Design incentive frameworks for MFIs to extend outreach beyond urban centers
- Explore partnerships with Hassel and other agricultural finance actors for co-financing models

6. Balanced Regulation

- Work with DAB to develop a differentiated profit rate framework that accounts for higher costs in rural and underserved markets
- Establish a clear regulatory roadmap for new Islamic finance instruments

7. Donor Coordination Mechanism

- Re-establish structured funding coordination, potentially through MISFA, to reduce fragmentation
- Link donor disbursements to institutional performance metrics to preserve credit discipline

Conclusion

The Afghan microfinance sector in 2026 presents a paradox of strength and constraint. On the positive side: a strong repayment culture with PAR at just 0.2%; expanding geographic inclusion across 24 provinces; improving regulatory oversight by DAB; and growing interest in green and diversified Islamic finance products. At the same time, the sector is held back by heavy funding dependence — particularly on a single national body — limited scale, significant human capital and governance deficits, and structural barriers including poor infrastructure, a restrictive profit cap, and weak digital ecosystems.

The sector is not in decline — it is in **controlled stabilization**. Its future will depend on unlocking diversified funding, enabling product and digital innovation, and — above all — building the human capital and institutional governance capacity that the sector urgently needs. These are not quick fixes, but they are the foundational investments required to move Afghanistan's microfinance sector from stabilization to sustainable, inclusive growth.

Notes and Definitions:

[1] World Bank (2020), Afghanistan — Population. <https://documents.worldbank.org/en/publication/documents-reports/documentdetail/225051587482483158>. The estimate of 70% under age 25 reflects UNFPA and World Bank demographic assessments.

[2] Salam (also known as Bai Salam or forward sale) is an Islamic financial contract where the buyer makes full payment in advance for specified goods to be delivered by the seller at a designated future date. It is an exception to the general Shariah rule prohibiting the sale of goods not yet in the seller's possession, and is particularly used to provide liquidity to producers and farmers.

[3] Wakala is an Islamic financial agency contract where a principal (such as an MFI) appoints an agent (the client or Wakil) to invest funds or conduct business on their behalf, in strict compliance with Shariah principles.