Influences of Devaluation in foreign currencies on the performance of local businesses in Afghanistan with reference to Pakistan's currency (Rupee) –An empirical study of Jalalabad city.

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Abstract— The currency of Pakistan (Rupee) has been in circulation in the eastern and southeastern markets of Afghanistan. after the civil war intensified in Afghanistan in late 1992 and onwards, the Taliban militants took over control of the country's agencies and eventually the whole government, as a result they laid off the contract with Russian firms to put out printing the Afghani notes they claimed were worthless. Besides, macro factors (e.g. political instability and foreign interference) have caused the country's economy to steep, therefore the Afghani lost its value both in the regional and international markets. different Warlords in Afghanistan used to print their own introduced currencies without any formal approval and standard procedure of the state's central bank (i.e. Da Afghanistan Bank). Therefore, people who were living across the Durand line were forced to start their daily transactions using Rupee which has caused Afghanistan to be financially, economically and politically relied on Pakistan. Ever since Rupee has dominated the Afghani in the eastern and south-eastern markets of Afghanistan. A survey was carried out to collect the required data in the city of Jalalabad using both primary and secondary sources, the secondary data was collected through already Published articles using google scholars as search engine. Findings of the research indicate that the financial performance/profit making of the local businesses has been negatively affected by the devaluation in the rate of Rupee, vendors have had two alternatives; (1) retention of customers and (2) increasing the profitability of the business, given the inflation caused by Rupee devaluation, the vendors have chosen to adopt customer retention which is indeed a lucrative strategy, therefore the financial performance of the local businesses in terms of enhancing profitability have deteriorated. As Pakistan's current account deficit has faced downslides and having been estimated to bear further crises, which will lower the value of Rupee, and ultimately will affect both the rate of Afghani and the performance of the local businesses in Afghanistan. The research; based on the results drawn from the findings and analysis suggests some corrective measures required to be taken to intercept the risks caused by the currency devaluation.

Index Terms— Currency Devaluation**,** Rupee, Afghani, Local businesses, Monetary system.

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1 INTRODUCTION

The collapse of ex-president of Afghanistan Dr. Najeebullah's Government and the escalation of the then civil embroil in Afghanistan, the currency of Pakistan (Rupee) has been in circulation in the eastern and southeastern markets of the country. after the civil war intensified in Afghanistan in late 1992 and onwards, the Taliban militants took over control of the country's agencies and eventually the whole government, as a result they laid off the contract with Russian firms to put out printing the Afghani notes they claimed were worthless. Besides, macro factors (e.g. political instability and foreign interference) have caused the country's economy to steep, therefore the Afghani lost its value both in the regional and international markets.

In that point of time different Warlords in Afghanistan used to print their own introduced currencies without any formal approval and standard procedure of the state's central bank (i.e. Da Afghanistan Bank). Therefore, people who were living across the Durand line were forced to start their daily transactions using Rupee which has caused Afghanistan to be financially, economically and politically relied on Pakistan. Ever since Rupee has dominated the Afghani in the eastern and

south-eastern markets of Afghanistan. Nonetheless, After the US and North Atlantic Treaty Organization (NATO) allies pushed the Taliban in the year 2001, almost all the agencies were reinstated, the new Afghani currency notes were printed with the assistance of the United State of America (USA) and the NATO-allied states, the country's economy was revitalized, hence Afghanistan started diverting somewhat from the economic influence of Pakistan. Over the last two years, the sprint in the slowdown of Pakistan's economy which has led to its currency (Rupee) depreciation in the international market has woefully affected businesses and ordinary life of its users in the eastern and South-east regions of Afghanistan.

To avoid further loss, the local authorities along with the central government require taking up earnest control measures for the stoppage of Rupee's circulation. The current study ascertains major symptoms of Rupee's circulation in the Afghan Markets and recommends disciplinary measures needed to be taken to help provide useful insights to the central and local governments to avert the potential consequences.

1. 2 AFGHANISTAN'S CURRENCY (AFGHANI)

Afghanistan's currency known as (Afghani) symbolized as Afs with code being AFN, Afghani is issued by the country's central bank called Da Afghanistan Bank (DAB). It is nominally subdivided into 100 puls (paisa) although due to the fact that the country's economy is in developing stage therefore, there are no puls coins currently in circulation. In 2019, one U.S. dollar was exchanged for approximately 75 Afghanis which is currently $1=Afs 78. (Wikipedia 2020)

1.2.1 A brief history of Afghani

Afghanistan's original currency (Afghani) was first introduced in the year 1925 which was earlier known as Afghani Rupee and later replaced with Afghani, the use of Afghani Rupee was first started in the year 1891. The current currency's formal name is Afghan Afghani and code is (AFN, ISO 4217) Afs is used when the amount exceeds two or three. At the initial stages Afghani contained 9 grams of silver which was later reduced and currently the silver coins have been replaced with the printed notes, the Afghani Banknotes and coins currently being used are:

Table 1: Afghani Notes and Coins

Banknotes	Coins
1 AFN	1 AFN
2 Afs	2 Afs
5 Afs	5 Afs
10 Afs	
20 Afs	
50 Afs	
100 Afs	
500 Afs	
1000 Afs	

Afghanistan's currency exchange rate was being determined by macro-factors and market forces, after a long period of time when a dual exchange rate policy was in existence in the country an official exchange rate fixed by the central Bank of Afghanistan Bank-e-Millie (National Bank), later on the Da Afghanistan Bank (DAB) was established and all the responsibilities were shifted from Bank-e-Millie and DAB was recognized as the central Bank of the country, and Afghanistan's Money Bazaar known as Saraye Shahzada located in the capital city Kabul wherein the supply and demand forced determined and also currently determining the Afghani's exchange rate.

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In the late 1935 the Bank-e-Millie agreed to exchange Afghani at 4 Afs against 1 Indian Rupee, After the establishment of Da Afghanistan Bank as the central Bank of Afghanistan, an official fixed rate and a formal procedure of the currency regulations were determined. However, Da Afghanistan Bank have always tried to keep its official rate confined but to the Sarai Shahzada exchange rate, the gap between the official and free-market exchange rates were widened in the 1980s and during the civil war ignited thereafter. After the start of a civil war in 1992, $ 1 bought 16,000 Afs. During the civil war in late 90s foreign powers and forgers each made their own Afghani banknotes to support themselves financially, with no standardized regulation and procedure or any serial number or code.

In December 1996, after the Taliban seized control of Afghanistan's institutions the chairman of the Taliban's central Bank Ehsanullah Ehsan cancelled the contract with the Russian firms that had been printing Afghani since 1992 and declared the Afghani worthless approximately 100 trillion Afghani was wasted, as a result the exchange rate of Afghani was drastically fallen, the currency was traded at 73,000 Afs against 1 US Dollar.

Before the USA war of Afghanistan, the country's currency was destabilized, slowly, the currency soared to 23,000 Afs against 1 US dollar, but after the fall of the Taliban regime in November 2001, the currency again downed to 36,000 Afs in 2002. In the same year with the USA and International partners the new Afghani notes were printed with formal procedure of the central Bank of Afghanistan. Da Afghanistan Bank has adopted a floating exchange rate regime and has let the exchange rate to be determined freely by market forces. The new Afghani was valued at 43 Afghanis to one U.S. dollar.

After depreciating during the last quarter of 2003/04, the Afghani has been appreciating steadily, gaining 8 percent against the U.S. dollar between March 2004 and July 2004. This appreciation, at a time of increasing inflation, appears to reflect a greater willingness by the population to use the Afghani as a medium of exchange and as a store of value. This trend appears to be attributable to the relative stability of the exchange rate since the introduction of the new currency, administrative measures aimed at promoting its use, such as the requirement that shopkeepers must price goods in Afghani. Donors are increasingly making payments in Afghanis instead of U.S. dollars and this appears to be widely accepted. By 2009, the Afghani was valued at Afs 45 per one U.S. dollar. In 2019, the Afghani reached Afs 75 to 1 U.S. dollar.

1.2.2 Da Afghanistan Bank (DAB) and its foreign currency regulations

Da Afghanistan Bank (DAB) is the central and a government-regulated bank, responsible for undertaking the regulation of

monetary and banking systems and framing the fiscal policy of Afghanistan, the headquarter of DAB is located in Kabul, the capital city of the country. Currently there are total 47 branches of the Bank being active all over the country of them 5 are situated within the Kabul city. DAB has been established in the year 1939, with a mission to regulate the outright framework of the banking system and outline policies for country's financial institutions. Besides, DAB has additional responsibilities such as:

1. Formulation, execution and adopting the monetary policy of Afghanistan.
2. Printing and issuing Afghani banknotes and coins.
3. Managing the official foreign exchange reserves of Afghanistan.
4. Acting as banker and advisor to, and as agent of the country.
5. Accepting foreign bank applications from banks that are wishing to operate in Afghanistan.
6. Maintaining and promoting subtle and efficient systems for payments, for transfers of securities issued by the state or DAB and for the clearing and settlement of payment transactions.
7. Providing license and overseeing banks, foreign exchange dealers, money service providers, payment system operators, securities service providers, securities transfer system operator.

1.1.1. Board of Directors

The Board of Directors of DAB is comprised of:
1. Khaliq Sediq – The Governor and Chairman of the Executive Board, Supervisory Board and Board of Directors.
2. Wahidullah Nosher – The first Deputy Governor and Vice Chairman of the Executive Board, Supervisory Board and Board of Directors.
3. Dr. Abdul Ghani Ghawasi.
4. Nargas Nehan.
5. Dr. Shah Mohammad Mehrabi

1.1.2. Monetary policy

In the year 2003 a law was framed by DAB stating that the primary objective of outlining the monetary policy in Afghanistan was to maintain a domestic price stability, meaning up gradation of the value of the home currency(Afghani). As a secondary objective, DAB aims to bolster the proper functioning of the financial system and promote a sound national payment system. Operationally, DAB has been maintaining price stability based on its policy decisions on a growth rate targeting for currency in circulation (CIC). When consistent with its target for CIC, DAB has also aimed at smoothing short-term exchange rate.

Given the high impact caused by currency fluctuations can

have on inflationary expectations and inflation itself. Monthly targets for CIC, consistent with the ceiling on CIC which is agreed upon the context of the PRGF-supported program, are set on the basis of expected real GDP growth, the velocity of CIC, the target for inflation, and seasonal variations in the demand for liquidity.

1.1.3. Foreign Exchange Regulation

Both in foreign currency and in domestic securities the Open-market operations (OMO) influences the base currency (domestic currency). In countries where financial system is more developed, it is common for the central bank to rely on foreign exchange interventions to meet its foreign reserve objectives, and on OMO in domestic securities to achieve base money or short-term interest rate operational targets. In Afghanistan, however, the market for capital notes (CNs) is still too clumsy for CNs to become the primary instrument of monetary policy, and DAB has been unwilling, until recently, to expand the CNs volume because of concerns about the associated higher interest costs. Currently, DAB aims to sell up to Afs 400 million worth of 28-day notes and up to Afs 100 million worth of 182-day notes in weekly auctions.3 This compares with average weekly sales of foreign exchange of US$18 million (equivalent to approximately AFN 900 million) in the foreign exchange auctions to date in 2007/08. DAB also operates standing credit and deposit facilities and maintains a reserve requirement for commercial banks.

1.3 RESEARCH AREA

The city of Jalalabad bears an economic and commercial significance, which is why the current research mainly considers the facts and figures taking place in Jalalabad. However, Rupee is used in other regions across the Durand line (e.g. eastern, and south eastern regions of Afghanistan), due to the macro-economic importance that the city of Jalalabad is holding in terms of trade, geo-political location, and most importantly nearness to the Durand line and commercial importance, for carrying out the current research the city of Jalalabad has been taken as sample.
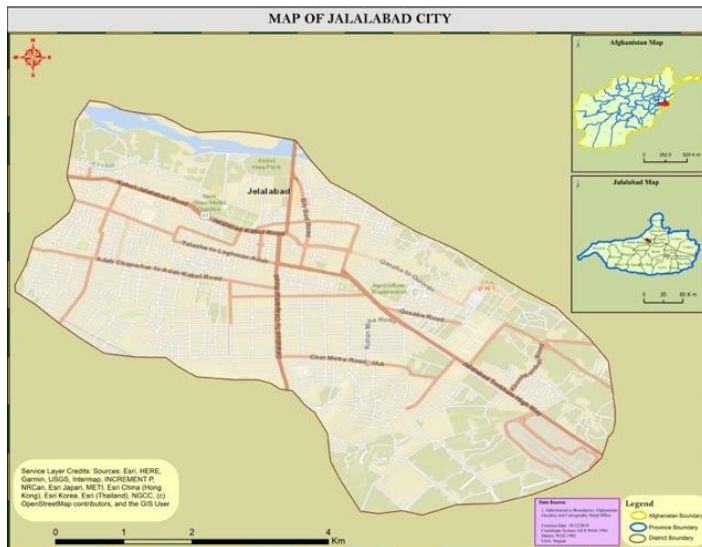
Figure 1: Map of Jalalabad City

1.4 SIGNIFICANCE OF THE STUDY

Over the last five years the increased rate of inflation in Pakistan has led to the devaluation of its currency (Rupee) which has created economic hitches and currency mismatch for the Afghan people living across the Durand line and use Rupee as a daily transactional currency. This study is conducted with a main focus on figuring out the major financial and economic complications engendered by the Rupee devaluation facing the Afghans, local vendors in particular. Although the local government in the city of Jalalabad has banned the use of Rupee, this practice has proven to be beneficial for the vendors but has on the other hand created problems for the customers. Therefore, this research analyzes the volatility impact of Rupee depreciation and suggest required measure need to be taken to overcome further loss.

The key questions of the research are as follows:

1. Analyzing and finding out the volatility impacts of Rupee depreciation on the performance local businesses in Afghanistan, taking into account the city of Jalalabad.
2. Use of Rupee has recently banned in the city of Jalalabad, the local authorities has imposed sanctions over the rules' breakers, this research tries to find out the Potential fallout borne by the local vendors.
3. Shedding light on the currency of Afghanistan (Afghan Afghani), rules and regulations framed by the central Bank of Afghanistan (Da Afghanistan Bank).

2 RESEARCH METHODS & INSTRUMENTS

2.1.   Meaning

The term "Research" has been defined by many renowned research scholars, in common, "research methodology

is used to describe a number of similar and overlapping activities relating a search for required information. "something that people undertake in order to find things out in a systematic way, thereby increasing their knowledge" (Saunders et al. 2009). According to Kothari (2004), "endeavor of any research is to uncover the concealed reality that is yet to be exposed or revealed". However, research is constantly used to solve organizational problems through systematic strategies (Ojo, 2008).

2.2.   Research Design

Quantitative in nature, the research uses regression analysis as a data analysis tool and the variables shown in the form of graphs and charts representing the collected data using questionnaire as an instrument.

2.3.   Methods and Instruments

Since, the nature of the research is quantitative therefore, questionnaire has been used as a data collection tool.

2.4.   Data Sources

Both primary and secondary data has been collected for the research that are categorized as such:

2.4.1.   Primary data
Primary data has been collected through:
1. Questionnaire method and
2. Personal observation.

2.4.2.   Secondary data
Secondary data has been collected through the following sources:
1. Published Research papers
2. Published Thesis
3. Webpages and
4. Da Afghanistan Bank website

2.5.   Sampling

Sampling has defined by many research scholars and many dictionaries, i.e. Question Pro defines Sampling as "A smaller set of data that is chosen and/or selected from a larger population by using a predefined selection method." (Aditya 2020)

2.6. Market type

For analyzing the impacts of fluctuation in the rate of rupee over businesses in Afghanistan, market type has been chosen as a parameter to find out which type of market is more susceptible.

The graph above indicates that out of a total 70 responses that have been obtained from the survey a handful of 71.4 of the markets in the city of Jalalabad are of perfect market competition, 14.30 are slotting at the monopolistic bar, 4 at oligopoly and 10 others are at monopoly bar.

Given the sprint in transformation of Afghanistan from a sever disputed into a developing country, business firms try to enter into the Afghan market so as to take over and leverage the free market, which is why majority of the markets in Afghanistan have turned out to be perfect competitive market. Followed by

Figure 3: Market type

monopolistic type of market wherein only one or a few firms have the possession to frame policies and determine price of the products offered at the market.

2.7. Store type

There are mainly two types of stores vis; wholesaler and retailer, but many a time depending on the nature of location, business, and access to raw materials the type of a store varies. Whereas for the current research two types of store has been considered (e.g. Wholesaler and Retailer).
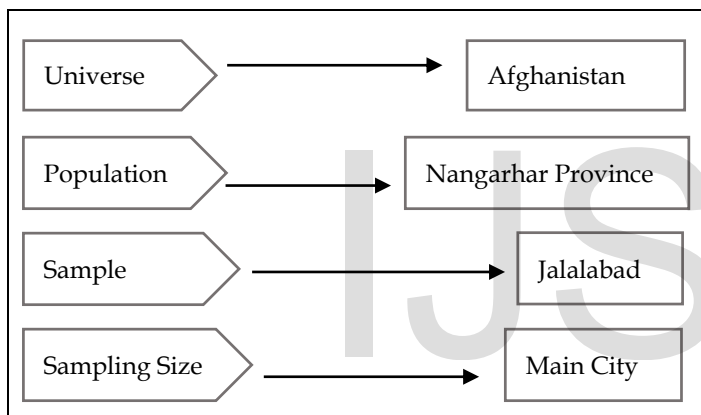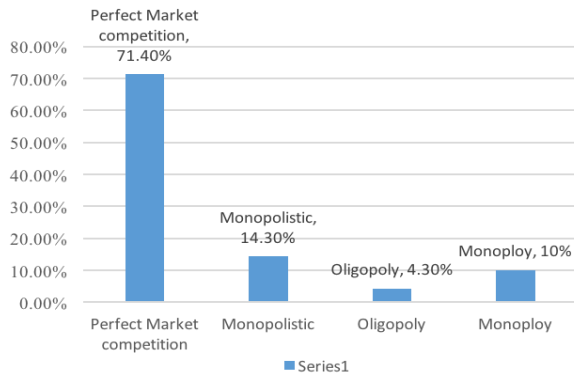
Figure 2: Sampling Design

The diagram above is the illustration of the sampling design, which shows that Afghanistan for the research has been taken as universe, Nangarhar Province as Population, Jalalabad as Sample and the main city as sampling size.

2.5.1. Period of the Study

The study considers two years starting from August 18, 2018 to the current.

3 RESULTS AND ANALYSIS

Data at the initial stage has been illustrated in the form of charts and graphs and qualitatively been explained. In the second section statistical tool (e.g. regression and correlation analysis have been applied to find out the relationship between dependent and independent variables. the overall collected data has been categorized into the following sub-portions:
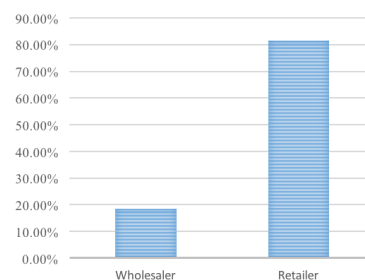
Figure 4: Types of Retailer

Figure 5: Store type

Given the data shown in the above chart, 81% of the stores out

of 70 responses are retailer and 19% other wholesaler, meaning in the eastern Afghanistan sole proprietorship is more and people believe on having a sole control over businesses, due to the lack of facilities many of the stores are thought to be retailer.

2.8. Types of Wholesaler

Wholesalers are operating as middlemen between a manufacturer and a final consumer or customer. (Small Business). In simple words, a wholesaler is the one who is engaged in buying goods from a manufacturer and resell those to the final consumer or retailers in order to gain profit.

2.9. Types of Retailer

There are total 24 specialized retailers with 40.70%, followed by 10 with a 16.90% of Drug stores retailer, 9 convenient retailers, 7 others both super and departmental stores being equal with 11.90% and 2 super markets with a 3.40% of super stores retailer out of 70 respondents as per the survey.

Figure 6: Types of Wholesaler
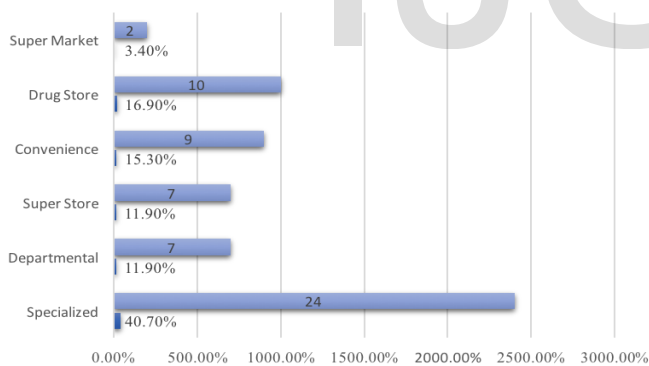
sales level, and Employees' satisfaction with regard to salary) taken as variables to ascertain the effects of Rupee devaluation on the performance of local businesses in the city of Jalalabad.

The assimilated data in the figure below shows that, devaluation in the rate of Rupee has had significant impact on the financial performance of the local businesses as represented numerically, out of a total of 70 respondents 57.14% are of the belief that there is a significant negative impact on the financial performance/profit of local businesses. Similarly, 42.85% others claim the the level of sales has also been negatively affected
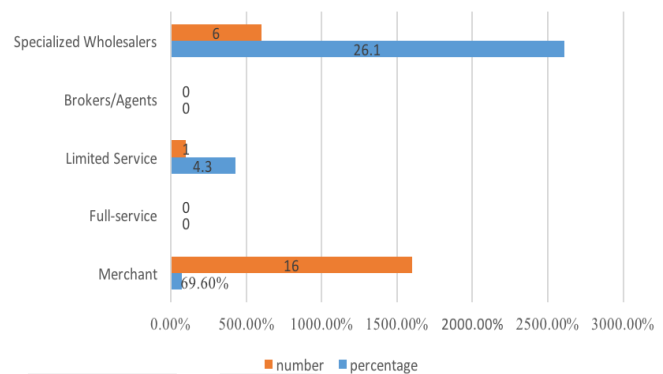
as shown in the graph the bar slots at 30 representing that out 70 a handful of 30 respondents believe that there is a considerable impact of Rupee devaluation on the level of sales. whereas, Employees; those who are working in the local firms are satisfied, no significant impact can be observed, as claimed by 21.4% of the respondents.

On the other hand, 35 of the respondents which is 1.4% claim that there is an increase in the satisfaction level of employees with regard to salary. While 24.4 and 21.4% others claim that there is no significant increase in the level of sales and financial performance respectively. A large percent of respondents, for instance 54.2% are of the belief that sales level has remained at average during the Rupee devaluation, 42 and 47% others claim the same for the financial performance and employees' satisfaction concerning to salary respectively. According to 38.2% of the respondents, the sales level, financial performance, and employees' satisfaction have remained unchanged during the Rupee devaluation.
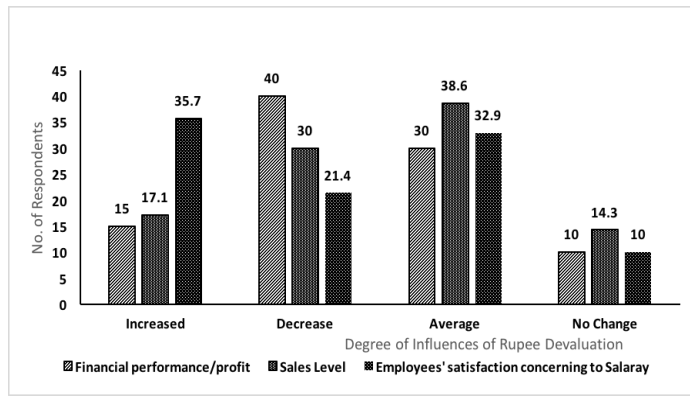
2.10. Influences of Rupee devaluation on Financial Performance/profit, Sales Level, and Employee Satisfaction concerning to Salary

The data condensed in the figure 5.11 illustrates the comparison between three parameters (e.g. Financial performance/profit,

Figure 7: Effects of Rupee Devaluation on Financial performance, Sales Level, & Employees satisfcation of Salary

2.11. Effects of Rupee devaluation on Price and Quality of the Commodities

Price and quality of the commodities being sold in the markets of the Jalalabad city have been taken as other important parameters for analyzing the effects caused by the Rupee devaluation on the performance of local businesses. As observed in the data represented by the chart below, 85% of the respondents are of the belief that there is a large amount of decrease in the quality of the commodities during the Rupee devaluation. Meaning, after the rate of Rupee has fallen quality of the products sold in the markets of the Jalalabad city have negatively been affected,

while 55% others about the price of the products think that there is not as significant impact of Rupee devaluation on the price as it is there on the quality, means the prices of the commodities are proportionally linked to the number of potential customers, if the vendors try to increase profit margin they should increase the prices as a result they will have to lose customers because customers are not willing to pay higher prices, on the other hand if the vendors want to retain the potential customers they should lesson the prices, which will lead to loss in sales. Therefore, in order to maintain a proper marketable equilibrium, the vendor require determining the prices at ordinary level equal to the prices of other markets.

In addition, 57% of the respondents claim that there is an increase in the quality of the products, while 15% others think there is somewhat increase the prices of the commodities, to infer, it can be inscribed that during fall in the rate of Rupee, prices of the commodities have increased, yet their quality has increased, the available data interprets that vendors have focused on the quality and price of the products during the Rupee devaluation. 38.5 and 1.11% others during the field work expressed that the price and quality of the products during the Rupee depreciation have remained at average. Whereas, 32.8 and 2% of the respondents believe that the price and quality of the products have remained unchanged and bears no impact caused by the Rupee devaluation.
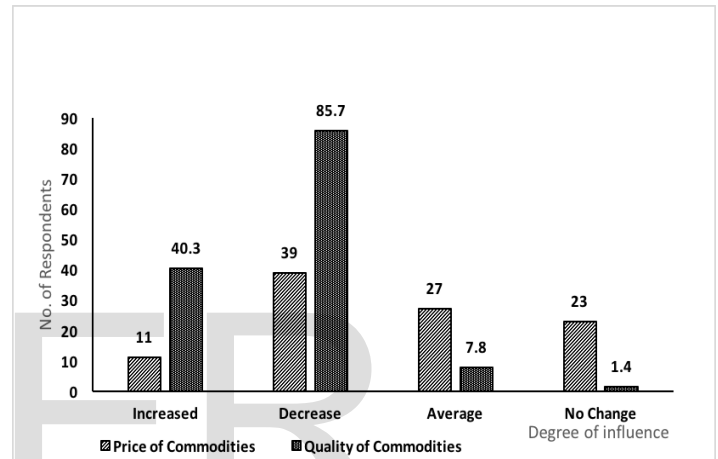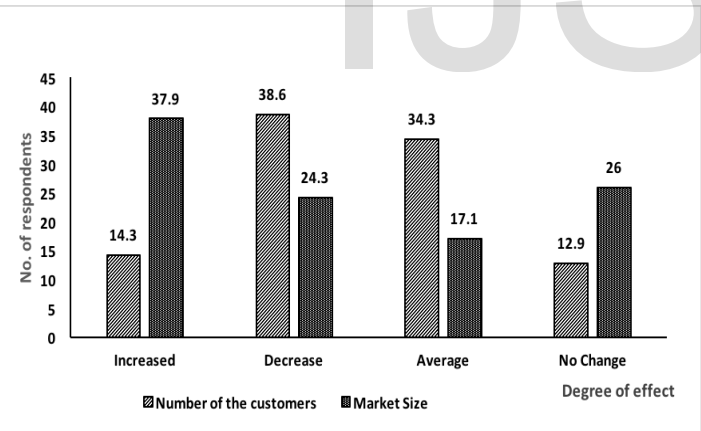

Figure 8: Effects of Rupee devaluation on the price and Quality of the commodities

2.12. Effects of Rupee devaluation on the number of customers and the market size

Market size have been increased, but on the contrary, the number of potential customers have been fallen. Data being represented by the chart illustrates that 54.2% of the respondents claim a momentous fall in the number of customers as shown by the bar slotting at 38.6, meaning, fall in the rate of Rupee has led to the customer loss, whilst 53% of the respondents with a total of 37 are of the belief that the market size has been otherwise increased, and people have started visiting the market more as compared to the past. The data further indicates that 20% of the respondents claim the number of customers have been increased which is quite less when compared to the market size.

The average bar slotting 34.3 with a 49% of the respondents who believe that the number of customers stays at average, whereas in the case of market size a handful of 24% respondents at the bar of 17.1 claim an average impact of the Rupee devaluation. According to 37% out of the total respondents claim no change on the market size which is shown by the bar 26, similarly, 18.4% others claims no change for the number of customers, which that bar slotting is at 12. In general, the

market size bears a positive and the number of customer a negative impact due to the Rupee devaluation, this shows an increased inflation in the markets wherein due to currency devaluation risks leads to an increase in the price of commodities that ultimately leads to the loss of potential customers, yet more people tend to visit more to the market perhaps to get updated

Figure 9: Effects of Rupee devaluation on Number of customrrs and market size

of the market's scenario.

4 CONCLUSION

In whole, the financial performance/profit making of the local businesses has been woefully affected by the devaluation in the rate of Rupee, vendors have had two alternatives; (1) retention of customers and (2) increasing the profitability of the business, given the inflation caused by Rupee devaluation, the vendors have chosen to adopt customer retention which is indeed a lucrative strategy, therefore the the financial performance of the local businesses in terms of enhancing profitability have deteriorated. In case of the internal operation of the businesses, employees are satisfied with the payroll, which means there has been no considerable impact of Rupee devaluation on the perception of employees with regard to the salary they are paid, and has remained unaffected.

Customers are not satisfied with the quality of the products offered by the retailers and wholesalers in the city of Jalalabad. Many complain that due to depreciation the value of Rupee vendors focus on retaining the customers and therefor, concentrate on lessoning the prices in order avoid losses which results in the quality of the products get affected, because many a time wholesalers try to purchase in bulk the products that are not carrying a satisfactory quality and having less costs. Whereas, the prices are not affected meaning, customers are satisfied with the prices being determined by the vendors, regardless of the quality that is perceived as being negatively affected by the Rupee devaluation, customers are satisfied with the current prices which shows the equilibrium being maintained by the wholesalers to avoid consequences predicted to be occurred due Rupee devaluation.

In addition, after the value of Rupee has downed people have started comparatively more to the market, as a result the Market size have increased, customer generally want to get updated of the daily scenario of the market. Unlike market size the number of potential customers have decreased because, as per the survey which shows that, at the initial stage when the Rupee started to fall the local vendors put higher prices on their products thinking that it would profit their business, but it all went otherwise and they end up losing their customers, therefore a conclusion can be drawn that the local vendors have focused more on increasing their profitability while having lost the potential customers.

Ordinary citizens have been doing all their deals in Rupee, similarly shopkeepers also do their transactions using Rupee, therefore an unplanned decision for changing the rules have proven to be financially detrimental both for the citizens and the businesses. Further, there is a mismatch occurring between the Afghani and the Rupee, because a rate of a country's currency is linked to the level of macro factors, export and imports, likewise Pakistan's current account deficit has faced downslides and having been estimated to bear further crises, which will lower the value of Rupee, and ultimately will affect both the rate of Afghani and the performance of the local businesses in Afghanistan.

4 RECOMMENDATIONS

The research; based on the results drawn from the findings and analysis suggests the following measures required to be taken to chase off the risks caused by the currency devaluation.

1. The Da Afghanistan Bank (DAB) could preclude the threats caused by the circulation of Rupee in the markets of eastern and south-eastern Afghanistan by printing new Afghani notes, which will be thus exchanged with Rupee and the old Afghani notes by the local banks across Nangarhar and southeastern Afghanistan lapsing up to a specified time limit.
2. The shopkeepers and marketers, should stop selling their products on Rupee and replace it with Afghani not quickly but gradually, so that the customers will be compelled to slowly stop using Rupee as a daily currency.
3. The Ministry of Finance of Afghanistan (MoF) should frame a new financial law outlining regulations for the currency exchange tellers and the money market so as to avert the open access money market of the country and the extent of the flow of foreign currencies to Afghanistan will be confined to a specified level.

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