

# Islamic Microfinance

## Challenges & Prospects

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# Introduction

- Concept of **conventional microfinance** is a recent phenomena: conceived in 1970s
- On the backdrop of the **constraints of** conventional microfinance Islamic microfinance emerged with **growing demand**
- However, IMF faces many challenges particularly from the **supply-side**

# Key words of Microfinance

- -- program that extend **loans** to **poor** for **self-employment** that generate **income** in allowing them to **take care** of themselves and their **families** (*Microcredit Summit 1997*)
- ***Key words:***
- loans to poor
- self-employment
- generate income
- Caring families

# Holistic objectives of CMF

- To increase **poor's household income & economic security**, build their **assets**, reduce their **vulnerability**, create demand for other **goods & services**
- World Bank has recognized microfinance program as **an approach** to address income inequalities
- Access to Credit is a **fundamental right** (Prof. Yunus)

## Success & Failure of CMF

- Micro-credit do help the poor in **consumption** smoothing as well as in **asset building** (BIDS & WB)
- MF promote investment in **human capital** like schooling, raises awareness to reproductive health and increases both individual and household welfare.
- While the **short run impact** of micro-credit has been widely acknowledged, the questions are raised about its **long run and aggregate impacts**.

# Big Questions???

- Is MF **sustainable** overtime?
- Given the high incidence of poverty in countries like Bangladesh where micro-credit programs are widespread and successful, critics argue that this reflects **the limitations of micro-credit** as an instrument for poverty reduction. (Latiffee, 2003)
- **Credit alone** on its own is inadequate to fight poverty. The need for other services is also important

## Elements Needed for Filling Gap

- **Multi-dimensional Composite** interventions for arresting poverty
- **Extreme poor** be targeted first
- Economic empowerment with **capital/assets**
- **Liability free** (interest-free) investment
- **Moral filtering** on faith-based approach
- **Sustainable approach** for financial inclusion
- Reasonable **overhead cost**

# Beauties of Islamic Microfinance/1

- ❖ Composite approach (Microfinance Plus)
- ❖ Religiously friendly to Muslims
- ❖ Maintain ethical standard
- ❖ Direct transfer of asset or goods
- ❖ Collateral-free financing
- ❖ Interest-free financing
- ❖ 'Risk sharing mechanism in group fund'



## Beauties of Islamic Microfinance/2

- ❖ Scope for entrepreneurship development
- ❖ Shariah-based investment modes
- ❖ Family empowerment
- ❖ Targeting extreme poor
- ❖ Zakat, Awqaf are permanent institutions
- ❖ Islamic banks & insurances have emerged with sustainability
- ❖ Low operating cost

# Global Scenario of IMF Providers/1

- Globally successful IMF providers are **small in number**
- Most IMF providers are not formally **integrated** with national & global financial systems
- Most IMF programs are **experimental**
- **Very few** Islamic banks practice IMF program
- IMF got wide **variation** in models, instruments & operational methods

## Global Scenario of IMF Providers/2

- Some IMF are registered as cooperatives, some have **no registration**
- Most IMF have **no Shariah Supervisory Board**
- Many differences of opinion on **fiqh issues**
- Lack of clear understanding on different Shariah **investment modes**
- IMFs are **far behind** the CMF in terms of expansion & penetration to rural borrowers

## Global Scenario of IMF Providers/3

- Islamic Microfinance contributes only **1% in global outreach**
- In Bangladesh, Islamic Microfinance contributes only **1% in microfinance market**
- Only **300 IMF providers** across 32 countries (whereas 10,000 NGOs are working with conventional microcredit in Bangladesh alone)

## Global Scenario of IMF Providers/4

- Total number of Islamic microfinance borrowers are **1.00 million** in Bangladesh
- 80% Islamic microfinance borrowers are from Afghanistan, **Bangladesh** & Indonesia
- National regulatory regime are not always very **friendly**
- Small IMF providers suffers **lack of fund** for IMF

# Constraints of IMF Providers/1

- Lack of product **diversification of IMF**
- **Absence** of savings, takaful insurance, transfer service
- **Lack of linkage** with banks & capital market
- IMF providers also **allow non-poor clients**
- **Absence** of credit-guarantee scheme
- **Lack of capital & liquidity**
- **Lack of Institutional & organizational capacity**
- Lack of **dedicated management** in vision

## Constraints of IMF Providers/2

- **Regulatory environments** are sometimes not friendly for IMF Providers
- IMF Providers suffer **lack of funds**
- Donors conditions are sometimes **very hard**
- Lack of **integration** with Zakat, Sadaqa & Awqaf
- Human resource constraints
- **Poor compensation** packages of the employees

## Demand-side Constraints of IMF

- **Entrepreneurship** and **marketing** challenges
- **Poor understanding** of the beneficiaries about different systems and practices of IMF
- Borrowers are not interested for **profit-loss** sharing project
- **Most borrowers** of interest-based CMF are Muslims
- Most poor borrowers are **unskilled**



# Potentials of Islamic Microfinance/1

- 3.00 billion people live in **abject poverty** in the world
- **600 million** of them live in Muslim countries
- Indonesia alone 129 million people are poor
- Indian sub-continent 200 m+ people are poor
- **70% people** living in Muslim countries do not use formal financial services
- Borrowers of conventional microfinance are **44% in Muslim countries**

## Potentials of Islamic Microfinance/2

- **One Study shows-**
- 80% Muslims in Bangladesh, 60% West Bank & Gazaian, 40% Yemeni, 43% Syrian, 49% Indonesian prefers Islamic microfinance
- It indicates huge demand for Islamic microfinance
- Conventional microfinance has been proved very slow in addressing poverty

# Success Stories

- **Islamic Bank Bangladesh Ltd. (IBBL)** as Islamic Microfinance Providers with more than 1.00 million borrower
- **Center for Zakat Management** has become successful in utilizing Zakat as microfinance for enterprise development.
- It involves corporate business houses to sponsor the projects

# Recommendations/1

- **Islamic Commercial banks** should be persuaded to introduce Islamic microfinance like IBBL
- **Zakat & Awqaf** should be blended with Islamic microfinance scheme after its transfer to Mustahiq like CZM
- **Common platform** for dialogue should be organized frequently for product diversification

## Recommendations/2

- Islamic **savings & insurance** (takaful) scheme should be widely introduced integrating Islamic microfinance
- International **training center** for Zakat, Awqaf & Islamic microfinance organizations should be established by IDB
- All Islamic microfinance providers should cover **capacity building**, ethical values along with financing

## Recommendations/3

- All Islamic microfinance providers should facilitate **business promotion** and market linkages for the borrowers
- **Poverty alleviations** should be the prime objective of Islamic microfinance
- All Islamic microfinance providers should participate in the **capital market** where possible

## Recommendations/4

- **Standard accounting** procedure and transparency in disclosure should be insured by all
- **International networking** should be developed for all Islamic microfinance providers
- Islamic Micro-finance providers should develop a **common standard** to be followed by all under the leadership of IDB

**Many thanks**  
**for patient hearing---**