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. Younus)
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. (Latifee, 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 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---