
Islamic Microfinance Approach as a Tool of Poverty Alleviation : An Empirical Study

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Abstract

Islamic microfinance comes up as an approach to alleviate poverty by complying Shariah principles. But the programme can be successful only if people know about it. Therefore, a review of literature has been done corroborated with the opinions of people as empirical facts in this regard in order to arrive at the results. The present study strived to study the approaches which Islamic microfinance could resort to and factors that help this programme to alleviate poverty. It also deals with how government and donors could contribute towards the poverty-reducing capabilities of Islamic microfinance programme. The study is based on primary data collected through questionnaire distributed to a sample of 100 respondents. The stratified sampling technique was followed for the selection of samples. Various statistical tools such as mean, standard deviation and analysis of variance (ANOVA) were employed to analyse the data. The study revealed that law and regulatory framework could become impediments in the path of Islamic microfinance and this appeared as a major challenge for the provider of this programme.

Keywords : Islamic Micro-finance, Shariah Principles

1.0 Introduction

Poverty is a concept spread all over the world which can disturb peace. It is a major challenge before us to uproot or lessen poverty from the earth. In order to cover the poor living below the poverty line, **Dr. Muhammad Yunus**, a Nobel Prize winner from Bangladesh came up the idea of microfinance which challenged the whole banking world. Microfinance is considered as the most acclaimed innovation in the world of finance. It is a priceless tool to ease poverty by lending to bring on entrepreneurship among poor. However, it could not serve those who reject conventional finance due to their religious limitations, thereby leading to the advent of Shariah compliant solution known as Islamic microfinance. The origin of this concept basically, has its root from the first Islamic bank recognized as Tabung Haiji in 1956. It has been developed as another niche product to free the millions from the vicious shackles of poverty by complying with Shariah principles. The model of Islamic microfinance based their economic activities on Islamic principles which are derived from the holy book known as Quran and Sunna because Islam is not only considered as a religion but it also directs the life of the people by putting down several rules to lead them towards mutual

cooperation and solidarity (**Costa et al., 2010**). According to Islam every activity is thought to be ethical when it fulfils religious norms in order to benefit the community. It is believed that goods which are provided to humans for a particular period should be employed to earn money in such a way that it could bring change in the lives of people as per Islamic economy. Poverty as per Islamic perspective is not only considered material aspect rather also takes into account the moral and spiritual aspect so approach used to reduce it should reflect both the aspects (**Riwajanti, 2013**). But this has been missing from conventional counterparts. This model helps in building capacity development by giving the chance to become micro entrepreneur to poor which would lead to improve their economic as well as social life. In spite of this, Islamic microfinance has not been explored all across the world so far barring some countries like Bangladesh, Indonesia and so on. Islamic microfinance is needed to expand its countrywide outreach effectively. This model calls for more attention from the government and development-oriented organisations to alleviate poverty. Hence, like other countries, we should at least give a try to this concept to contend with the curse of

poverty. In this paper, an attempt has been made to study the approaches resorted by Islamic microfinance and what factors could help this programme to alleviate poverty. How government and donors could contribute towards the poverty-reducing capabilities of Islamic microfinance programme has also been dealt with.

2.0 Review of Literature

Islamic microfinance is an emerging model in the world of conventional finance. Though Islamic microfinance is in a nascent stage, one can foretell that how much it could be beneficial for the marginalised people. Various researchers and academicians studied at the national and international level that how Islamic microfinance could help in alleviating poverty. **Shabrawy (2011)**, examined the concepts of family bank which was founded as the first Islamic microfinance bank in Bahrain by taking into account the aim of alleviating poverty and socio-economic empowerment. The study suggested Islamic microfinance as a supplement to help out micro entrepreneurs of interest rate credit financing and also indicated the need of extensive research. **Nasution (2013)**, studied the efficiency of Islamic microfinance institutions with special reference to Baitul Maal wa Tamwil (BMT) in Indonesia by proposing a framework. The study had taken three inputs and outputs in order to measure the efficiency of BMT as in order to achieve the objective of reducing poverty, institutions have to sustain for longer periods and for this they should be efficient enough. The DEA method was employed to examine the performance of BMTs. The study suggested increasing inputs to maximize the outputs. It was also proposed that variables such as size, profitability and age would influence efficiency of BMTs positively while NPL negatively. **Kasim and Amer (2013)**, looked into the practices of innovative global Islamic microfinance governance with respect to independence, competency, confidentiality and consistency and Shariah compliance problems. The study used triangulation method among selected Islamic microfinance institutions in Malaysia and India which required qualitative and quantitative probe. The framework according to which Islamic microfinance institutions would be governed was developed and the results so indicated after examining it that institutions lacked specific policies for its commencement and higher-growth. The study proposed dire need of developing innovative framework to evaluate the present best practices of global Islamic micro finance governance. **Arabi and Meisami (2013)**, attempted to inquire the definition and characteristics of Islamic microfinance and experiences of some Islamic countries with regard to it were studied. The study also proposed the potential of Islamic microfinance if it would be established in Iran. The study reviewed the various literatures in order to get the answers of posed questions. The results of the study suggested that Islamic microfinance had its own definition and characteristics unlike its counterparts. It was also found that Islamic microfinance would improve the access of the poor and middle income people to financial services. **Fararah and Al-Swidi (2013)**, evaluated the effect of service quality of Islamic microfinance system on the satisfaction of SMEs' owners in Yemen. The data

were gathered with the help of self-administered questionnaire from owners of the SMEs. The study used structural equations modeling partial least squares (PLS) approach. The findings of the study supported the effect of service quality on the level of satisfaction and perceived benefits. The positive mediation of the perceived benefits was found between the service quality and satisfaction whereas no moderating effect was determined on the relationship between service quality and satisfaction. The study suggested including some other factors to establish the SMEs owners' satisfaction. **Riwajanti (2013)**, tried to evidence the potential of Islamic microfinance by evaluating the performance and its impact on poverty alleviation. The study found the performance of this programme very promising and could improve economic and social well-being of the clientson the other hand also suggested improvement in certain areas especially dealing with regulation and provision of training in social development. **Zouari & Nabi (2013)**, examined the challenges and opportunities of the Islamic microfinance by studying the best practices of some institutions in terms of efficiency of microcredit schemes, institutional viability, regulatory environment and sustainability through extensive review of literature. It was found that the development of successful Islamic microfinance depends upon development of the proper regulatory and institutional framework. The study also pointed out policy recommendations and direction for the sustainable growth of this industry in the OIC countries. **Mirghani (2011)**, analysed the scope of prospects and challenges of Islamic microfinance. The study suggested that beneficiaries should be acquainted with business and management skills so that they can make use of funds provided by the Islamic microfinance optimally for this they need to be trained and there is a need to take follow-up of the usage of funds made available to them.

The above review of literature throw light on those studies which examined the role of Islamic microfinance in alleviating poverty and socio-economic empowerment conducted at the international level but no worthy research has been done at the national level till now. Hence an attempt has been made to fill this research gap.

3.0 Objectives

The following objectives are considered for the study:

1. To study the approaches of Islamic microfinance to alleviate poverty
2. To study the factors that make Islamic microfinance successful in poverty alleviation
3. To examine the government and donor contributions to the poverty reducing capabilities of Islamic microfinance programme

4.0 Methodology

The present study strived to study the approaches which Islamic microfinance could resort to and factors that help

this programme to alleviate poverty. Also, how government and donors could contribute towards the poverty reducing capabilities of Islamic microfinance programme have been study. The study was based on primary data collected through framed questionnaire distributed to the sample of 100 respondents. The stratified sampling technique was followed for the selection of samples. Various statistical tools such as mean, standard deviation and analysis of variance (ANOVA) were employed to analyse the data.

5.0 Results and Discussion

This section deals with various approaches which Islamic microfinance provider could resort to in order to lessen or alleviate poverty. The findings of the study are given in the table below.

6.0 Approaches of Islamic Microfinance to Alleviate Poverty

As we have previously discussed that Islam regulates every facet of Muslim's life as written in the holy book Quran and the sayings and deeds of their Prophet in the book of Hadith. Islam considers poverty as a curse so mandated for all Muslims to part their wealth for the poor people to bring them out from that condition. Islamic microfinance is another effort made in the Islamic economic system to cater to the financial needs of poor people based on Islamic principles. It is believed that Islamic microfinance could prove to be an important tool to eradicate poverty. Therefore, a study was carried on to know the opinions of people on extent of agreement about the approach should Islamic microfinance adopt to alleviate poverty. Table 1 below exhibits the views of people.

Table 1 : Extent of Agreement on the Approaches of Islamic Microfinance to Alleviate Poverty

Approaches	Mean	SD	Extent	Overall Status
Discourages a culture of debt as this is viewed as undermining one's dignity in Islam	4.48	0.82	Agree	II
Inculcation of Islamic spirit of Cooperation & solidarity can also help in uprooting poverty	4.56	0.64	Strongly agree	I
Islamic microfinance based on Islamic norms can alleviate poverty	4.12	0.70	Agree	VII
Use of charity for meeting immediate needs and investment in productive project to generate income for poor	4.00	0.77	Agree	X
Promotes self-reliance among the poor and advocate social justice	4.13	0.64	Agree	V
Islam mandates for charity to poor	4.24	1.19	Agree	III
Employment of manpower for productive purposes	4.11	0.64	Agree	VIII
Imparting requisite training to poor for carrying out the business	4.04	0.70	Agree	IX
Proper evaluation of the financial health of the poor	4.12	0.65	Agree	VI
Increase self-confidence in borrowers by making them financially independent	4.21	0.67	Agree	IV
Meetings helps in overall human development	3.81	1.00	Agree	XI

Source : Computed

Table 1 (a) : ANOVA Table of Extent of Agreement on the Approaches of Islamic Microfinance to Alleviate Poverty

	Sum of Squares	Df	Mean Square	F	Sig.
Between Groups	44.007	10	4.401	7.091	*0.00
Within Groups	675.880	1089	.621		
Total	719.887	1099			

*p-value is significant at 0.05 level

Source : Computed

The study shows that the people expressed strong agreement for inculcation of Islamic spirit of cooperation and solidarity can also help in uprooting poverty (4.56) as the approach of Islamic microfinance to alleviate poverty because Islam does not view poverty as a virtue but regards it as a social anomaly which needs to be removed from the society so as to encourage Muslims to assist the needy and destitute people. Further, people had given their agreement that Islam discourages a culture of debt as this is viewed as undermining one's dignity (4.48) accompanied by Islam mandates for charity to poor (4.24), increase self-confidence in borrowers by making them financially independent (4.21), promotes self-reliance among the poor and advocate social justice (4.13), proper evaluation of the financial health of the poor (4.12), Islamic microfinance based on Islamic norms can alleviate poverty (4.12), employment of manpower for productive purposes (4.11) whereas imparting requisite training to poor for carrying out the business (4.04), use of charity for meeting immediate needs and investment in productive project to generate income for poor (4.00) and meetings helps in overall human development (3.81) as approach adopted by Islamic microfinance to alleviate poverty got minimum responses from them. Thus, analysis suggests that inculcating Islamic spirit of cooperation and solidarity and discouragement of debt

culture as this is viewed as undermining one's dignity in Islam are the significant approaches as people believed of Islamic microfinance programme to eradicate poverty. There was statistically significant difference in responses given by the people on extent of agreement for the approaches of Islamic microfinance as indicated by the F-ratio (7.09) at the five per cent level.

7.0 The Factors Responsible for Success in Alleviating Poverty

Islamic microfinance is a system of providing financial services based on Islamic law (refer to as Shariah) to those people who can't access formal financial institution. Research has been done previously, substantiates the fact that it has potential to fight against poverty and make them free from shackles of the poorness. It is significant in national development of the country as it has evolved to cater the needs of poor and to ensure a just and equitable distribution of income. In this section, we were trying to bring out which element or factors of Islamic microfinance make it successful in alleviating poverty. Thus, views of people were taken on extent of significance on the factors which make Islamic micro-finance successful in alleviating poverty. The result has been shown in the table below.

Table 2 : Extent of Significance on the Factors Which Make Islamic Micro-finance Successful

Factors	Mean	SD	Extent	Overall Status
Product that address the problems and needs of poor people	4.27	0.91	Significant	II
Fulfilling the requirements of your customer	4.41	0.90	Significant	I
Monitoring & Evaluation	3.98	0.79	Significant	IV
Fund size	4.18	0.98	Significant	III
Purpose of loan usage	3.38	1.17	No opinion	VI
Monitoring	3.94	0.76	Significant	V
Other	3.07	0.70	No opinion	VII

Source : Computed

Table 2(a) : ANOVA Table of Extent of Significance on the Factors Which Make Islamic Micro-Finance Successful in Alleviating Poverty

	Sum of Squares	Df	Mean Square	F	Sig.
Between Groups	144.200	6	24.033	29.724	*0.00
Within Groups	560.330	693	.809		
Total	704.530	699			

*p-value is significant at 0.05 level

Source : Computed

The analysis exhibited in the table 5.11 indicates that it is necessary to know the customer first by understanding them in order to fulfil their requirements so that one can add the value to their lives through the provision of Islamic microfinance (4.41) was the significant factor which makes this programme successful in alleviating poverty. It was reported by the people that it is very important to bring forth product which can address the problems and needs of poor people (4.27). However, fund size (4.18) is also a significant factor of Islamic microfinance because the provider must be themselves financially independent and sustainable else will not be able to achieve their full potential by depending on external funding or aid. People considered monitoring & Evaluation (3.98) followed by monitoring (3.94) significant whereas they showed no opinion for purpose of loan usage (3.38) and other factors of Islamic microfinance. Hence, the study suggest that Islamic microfinance could successful in alleviating poverty if provider fulfils the requirement of customer by understanding their needs and design the product and make available which will address the problems and

needs of poor people. Despite, the results showed statistically significant difference in the opinion of people on extent of significance on the factors which make Islamic micro-finance successful in alleviating poverty hinted by the F-ratio (29.72) at the five per cent level.

8.0 Government and Donor's Contribution to the Poverty Reducing Capabilities

Although Islamic microfinance is still in its infancy but has potential to help poor people. It gives an investor a chance to be engaged in worthwhile project which would help them to get out of their poor economic condition. Hence, a comprehensive approach has to be taken by the government and donors in order to alleviate poverty from the country. Because without the government and donors aid, no institution can achieve its full potential. Thus, the extent of agreement on the government and donors contribution to the poverty reducing capabilities of Islamic micro-finance programme among people as shown in the Table below.

Table 3 : Extent of Agreement on the Government and Donor's Contribution

Sl. No.	Poverty Reducing Capabilities	Mean	SD	Extent	Overall Status
1	Offer policy environment	4.55	0.57	Strongly agree	II
2	Suitable regulatory framework	4.56	0.55	Strongly agree	I
3	Enactment of enabling regulation	4.15	0.70	Agree	V
4	Empowerment of institution	4.19	0.61	Agree	IV
5	Provide funds for building capacity, self-sufficiency, sustainability	4.49	0.54	Agree	III

Source : Computed

Table 3(a) : ANOVA Table of Extent of Agreement on the Government and Donor's Contribution

	Sum of Squares	Df	Mean Square	F	Sig.
Between Groups	16.208	4	4.052	11.235	*0.00
Within Groups	178.520	495	.361		
Total	194.728	499			

*p-value is significant at 0.05 level

Source : Computed

An analysis of data stated in Table 5.12 shows that people gave strong agreement for suitable regulatory framework (4.56) and offer policy environment (4.55) which should be provided by the government to strengthen the poverty reducing capabilities of Islamic microfinance programme. In addition, donors can also lend hand to the poverty reducing capabilities of the programme by providing funds for building capacity, self-sufficiency and sustainability (4.49). It was further reported by the people that enactment of enabling regulation (4.15) and empowering the institution would

be helpful for Islamic microfinance programme to reduce poverty. Hence, the study suggests that government should pave the way for Islamic microfinance programme by rendering suitable regulatory framework and offer policy environment. The results pointed out statistically significant difference in the responses of people on the extent of agreement on the government and donor's contribution to the poverty reducing capabilities of Islamic micro-finance programme by the F-ratio (11.23) at the five per cent level.

Importance of Islamic microfinance in achieving the Millennium development Goals

In order to promote development in the world's poorest countries 193 United Nations member states and 23 international organisations have agreed to achieve eight international development goals known as Millennium development goals by the year 2015. And Islamic

microfinance can be an important tool in achieving the Millennium development goal of eradicating extreme poverty. People were asked to express their views on extent of agreement on importance of Islamic microfinance in achieving the millennium development Goals. The result is shown in the Table- 4.

Table 4 : Extent of Agreement on Importance of Islamic Microfinance

Q_1	Do you think Islamic microfinance is important for achieving the Millennium development Goals and remove extreme poverty in the developing world?
Strongly agree	29.00 (29%)
Agree	44.00 (44%)
Not sure	26.00 (26%)
Disagree	1.00 (1%)
Strongly Disagree	-
Mean	4.01
SD	0.77

Source : Computed

It is seen from Table 4 that 44% people agree with that the Islamic microfinance is important for achieving the Millennium development Goals and remove extreme poverty in the developing world because Islamic microfinance also aims to cater the needs of poor people operates on the basis of Shariah principles by enabling access to finance will lead to reduce poverty. While 29% of them strongly agree followed by 26% respondents were not sure that Islamic microfinance is important in achieving millennium development goal. But 1% per cent respondent expressed disagreement and none was responded strongly disagree for this. The study suggests

that Islamic microfinance can be used as a tool to reduce poverty effectively. Thus, Islamic microfinance is important for achieving the millennium development goals in the developing world as evident by the mean score (4.01).

Reduction of poverty should be the primary goal of Islamic microfinance

The people were asked to give their opinion on extent of agreement on reduction of poverty should be the primary goal of Islamic microfinance programme as shown in the Table 5.

Table 5 : Extent of Agreement on Reduction of Poverty should be the Primary Goal of Islamic Microfinance

Q_1	Do you think reduction of poverty should be the primary goal of Islamic microfinance programme?
Strongly agree	29.00 (29%)
Agree	54.00 (54%)
Not sure	17.00 (17%)
Disagree	-
Strongly Disagree	-
Mean	4.12
SD	0.67

Source : Computed

The study revealed that out of total sample 54% respondents agree for the reduction of poverty should be the primary goal of Islamic microfinance whereas 29 % strongly agree that Islamic microfinance by providing access to financial services and products to poor people will reduce poverty from the society to certain extent. While 17% respondents were not sure that the reduction of poverty should be the primary goal of this programme. No one responded as disagree and strongly disagree for the primary goal of Islamic microfinance. Thus, we can conclude that most of the people agreed that the reduction of poverty should be the primary goal of Islamic microfinance programme as suggested by the mean score (4.12).

9.0 Summary and Conclusion

Islamic microfinance based on Shariah principle is an emerging industry but still manage to captivate various countries to embrace it as one of the tools to alleviate poverty all around the world. People perceived that inculcation of Islamic spirit of Cooperation, solidarity and discouragement of debt culture which is viewed as undermining one's dignity in Islam were the significant approaches of Islamic microfinance to eradicate poverty because Islam does not consider poverty as a virtue but regard it as a social anomaly which needs to be removed from the society so encourage Muslims to assist the needy and destitute person. Also, Islam mandates for charity to poor. It was found out from the study that if provider fulfils the requirement of customer by understanding their needs and design the product and make available which will address the problems and cater the needs of poor people then Islamic microfinance could be successful in achieving the noble cause of alleviating poverty. In this direction, government and donors could also lend their hands towards paving the way for Islamic microfinance programme by rendering suitable regulatory framework and offer policy environment together with this by providing funds in order to build capacity, self-sufficiency and sustainability thereby leads to strengthen the poverty reducing capabilities of this programme. Majority of the people in this study expressed their agreement that reduction of poverty should be the primary goal of Islamic microfinance as it would play a primordial role in accomplishing the Millennium development goals. But, the study indicated that law and regulatory framework could become impediments in the path of Islamic microfinance and appeared as a major challenge for the provider of this programme.

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