

Integrating Financial and Non-Financial Programs for Sustainable and Empowering Islamic Social Finance

Dr. Salman Ahmed Shaikh

PhD, UKM, School of Economics

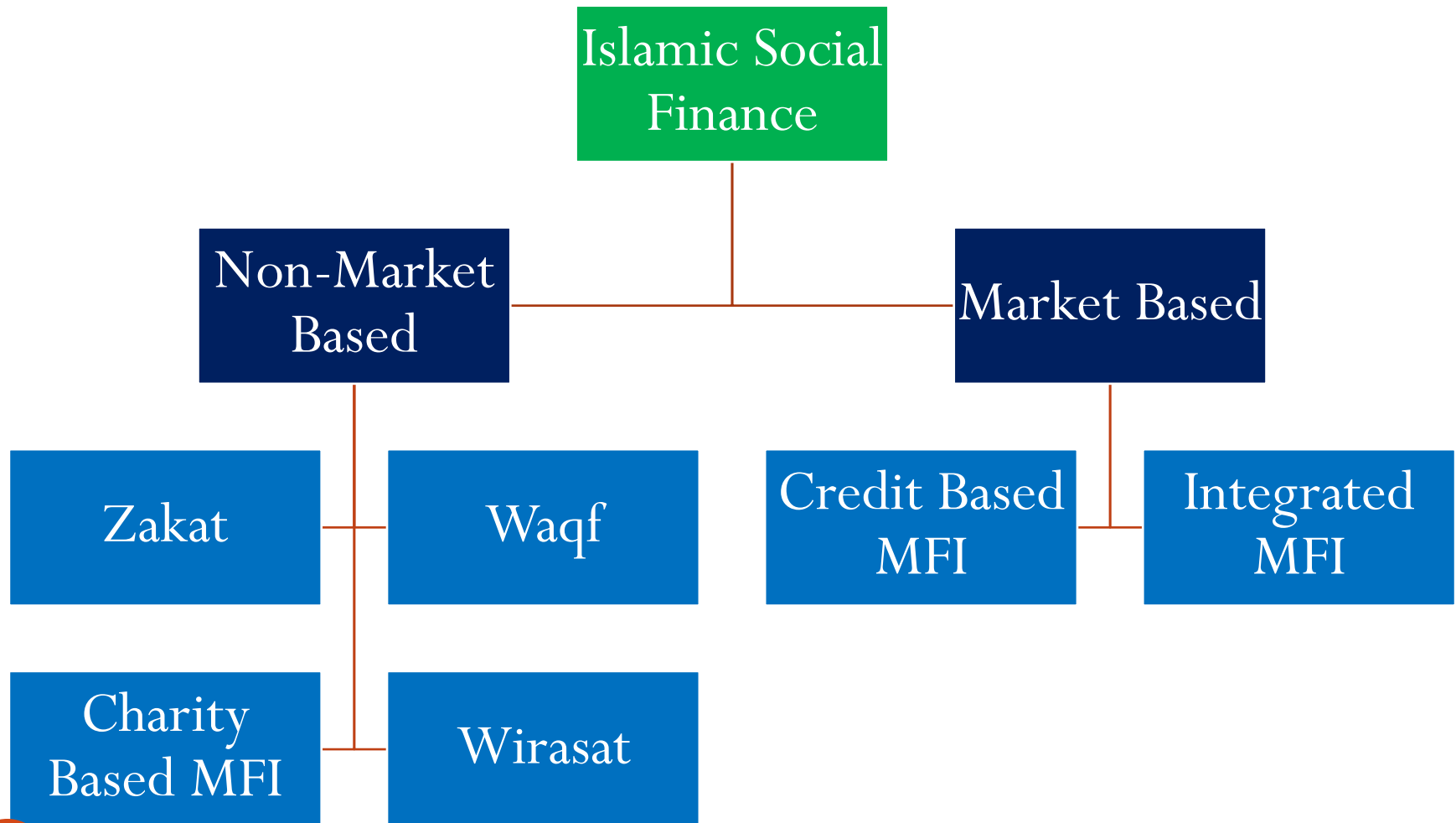
Director, Islamic Economics Project



Presentation Outline

- Institutions in Islamic Social Finance
- Economics of Islamic Social Finance Institutions
- Common Microfinance Structures
- Islamic Microfinance Structures: Cases & Illustrations
- Designing Incentives for Effective Targeting in Hybrid Models
- Operational Structure of a Hybrid & Integrated Model
- Q&A

Institutions in Islamic Social Finance



Economics of Zakat

- Targeted Intervention through redistribution from rich to poor.
- Empowerment through asset ownership.
- Funding consumption and productive needs.
- Boosts spending and thus aggregate demand and reduces wealth concentration.
- Encouraging investment and discourages keeping wealth idle.

Economics of Waqf

- Private funding of public goods.
- Reduces private concentration of wealth.
- Builds social safety nets.
- Funding source for skills enhancement and capacity building.
- Transfer of financial resources and beneficial services beyond markets.

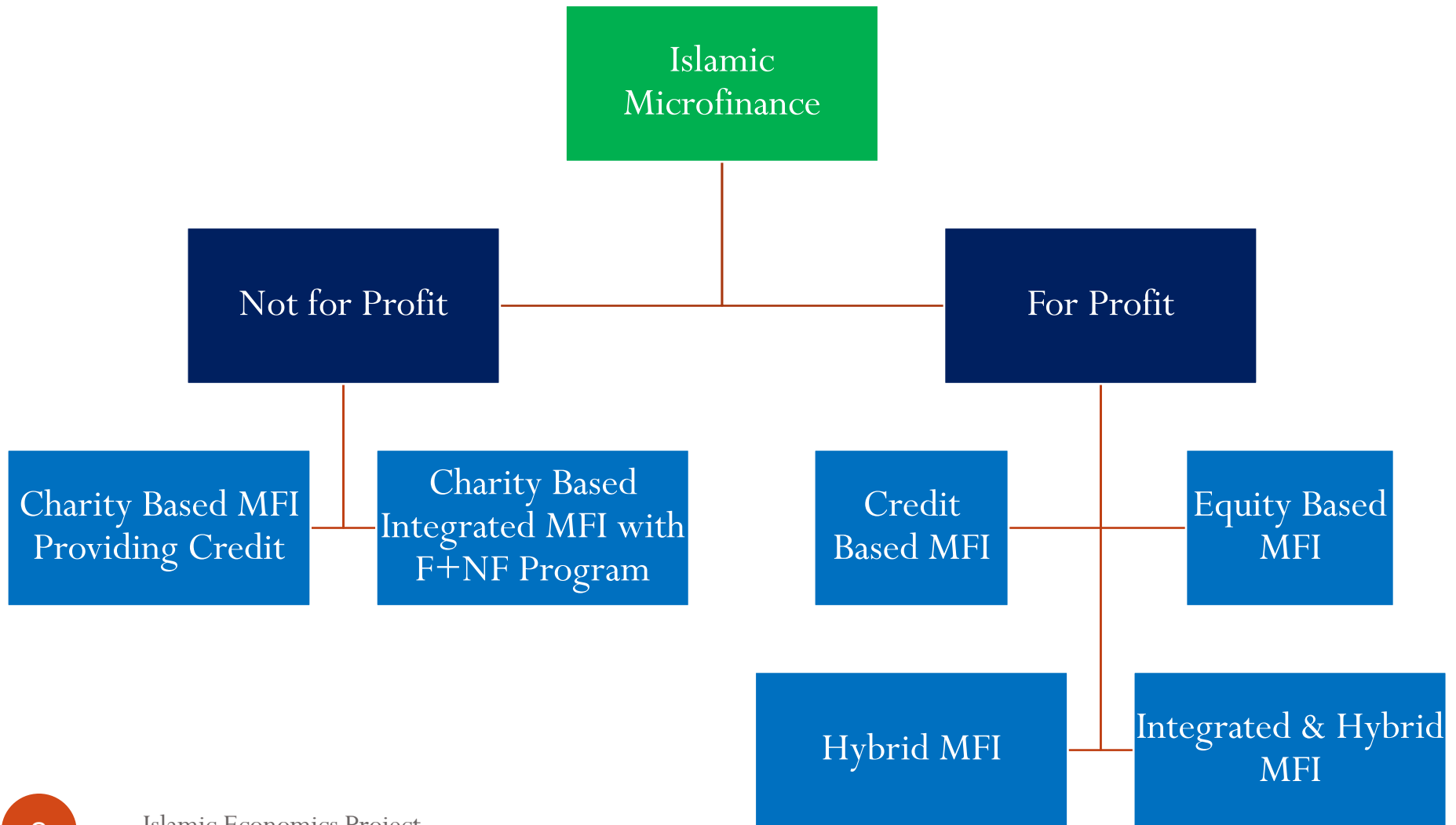
Economics of Islamic Inheritance Law

- Instead of fractional transfer of productive wealth alone, it transfers all types of wealth including personal wealth wholesomely.
- Transfer from one person to many persons disperses wealth and reduces wealth concentration.
- Intertemporal distribution of wealth in every family unit for every family member.

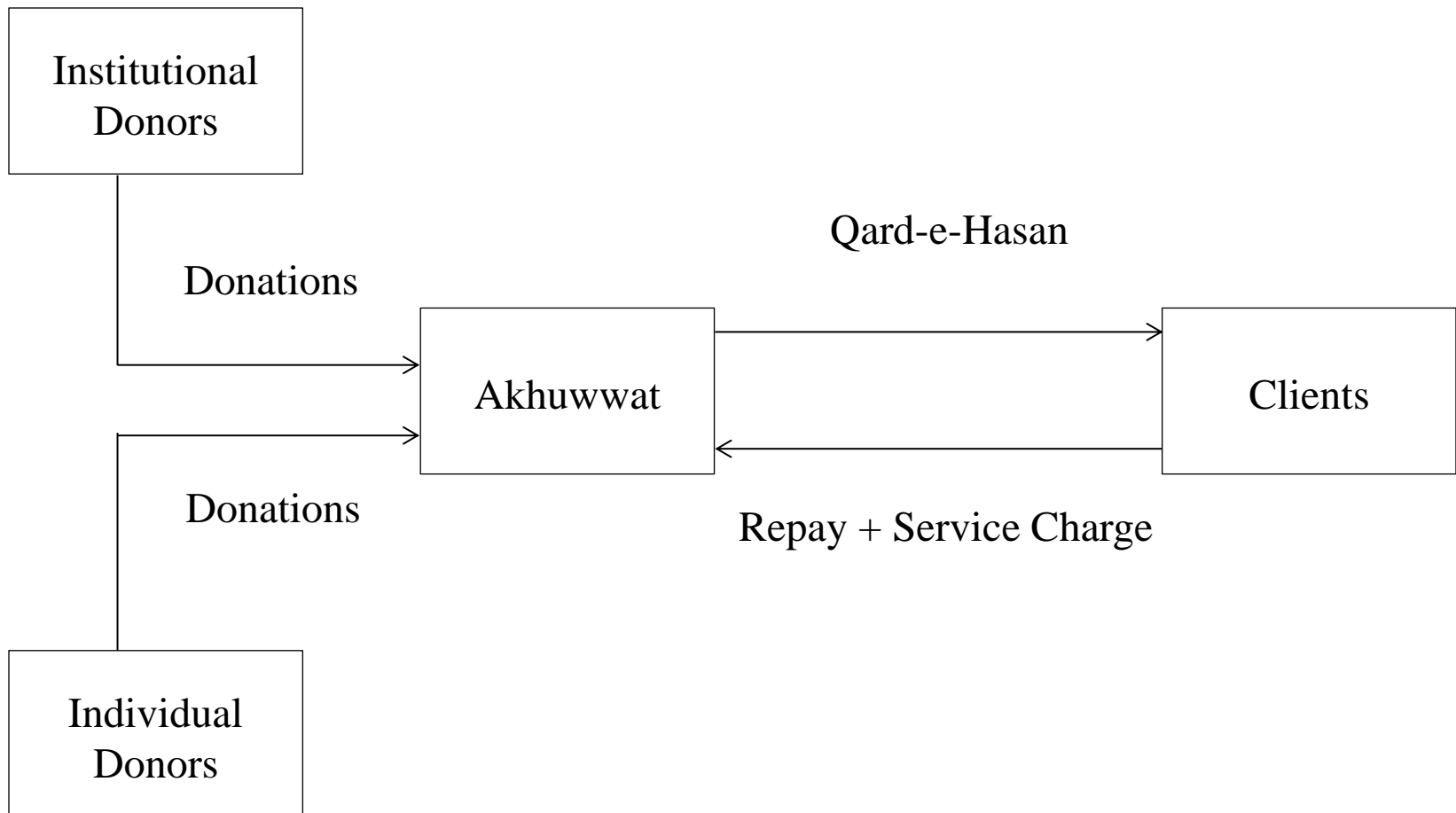
Common Microfinance Structures

- Individual Lending at High Interest Rate ($r_{\text{bank}} < r_{\text{mfi}} < r_{\text{loan shark}}$).
- Group Lending at High Interest Rate ($r_{\text{bank}} < r_{\text{mfi}} < r_{\text{loan shark}}$).
- Rotating Credit and Savings Association.
 - Pooling money and providing peer-to-peer lending on rotation basis.
- Credit Unions
 - Owned by and for participants to provide limited banking services.
 - Work on non-profit basis.
 - Tax exemptions

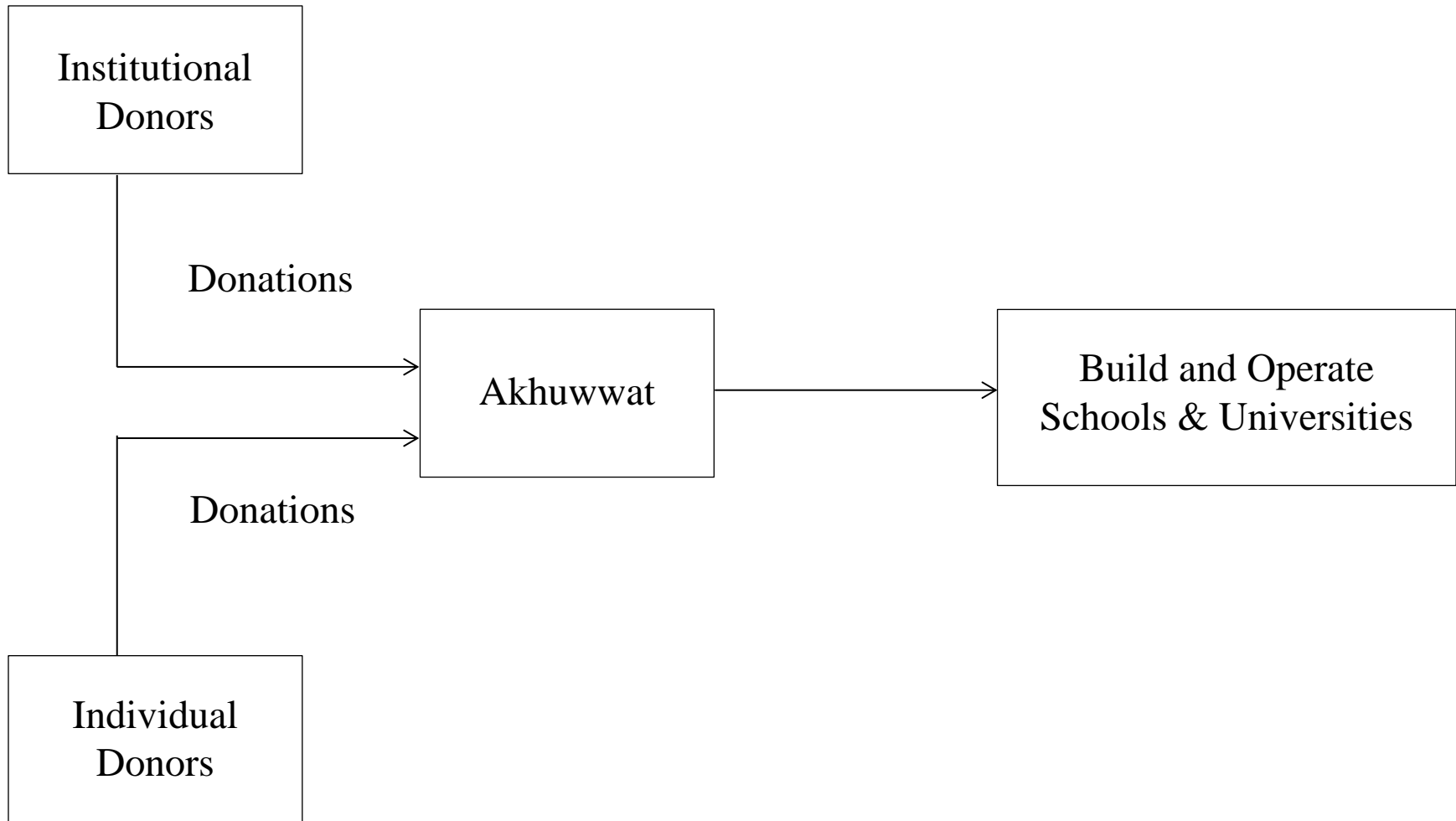
Islamic Microfinance Structures



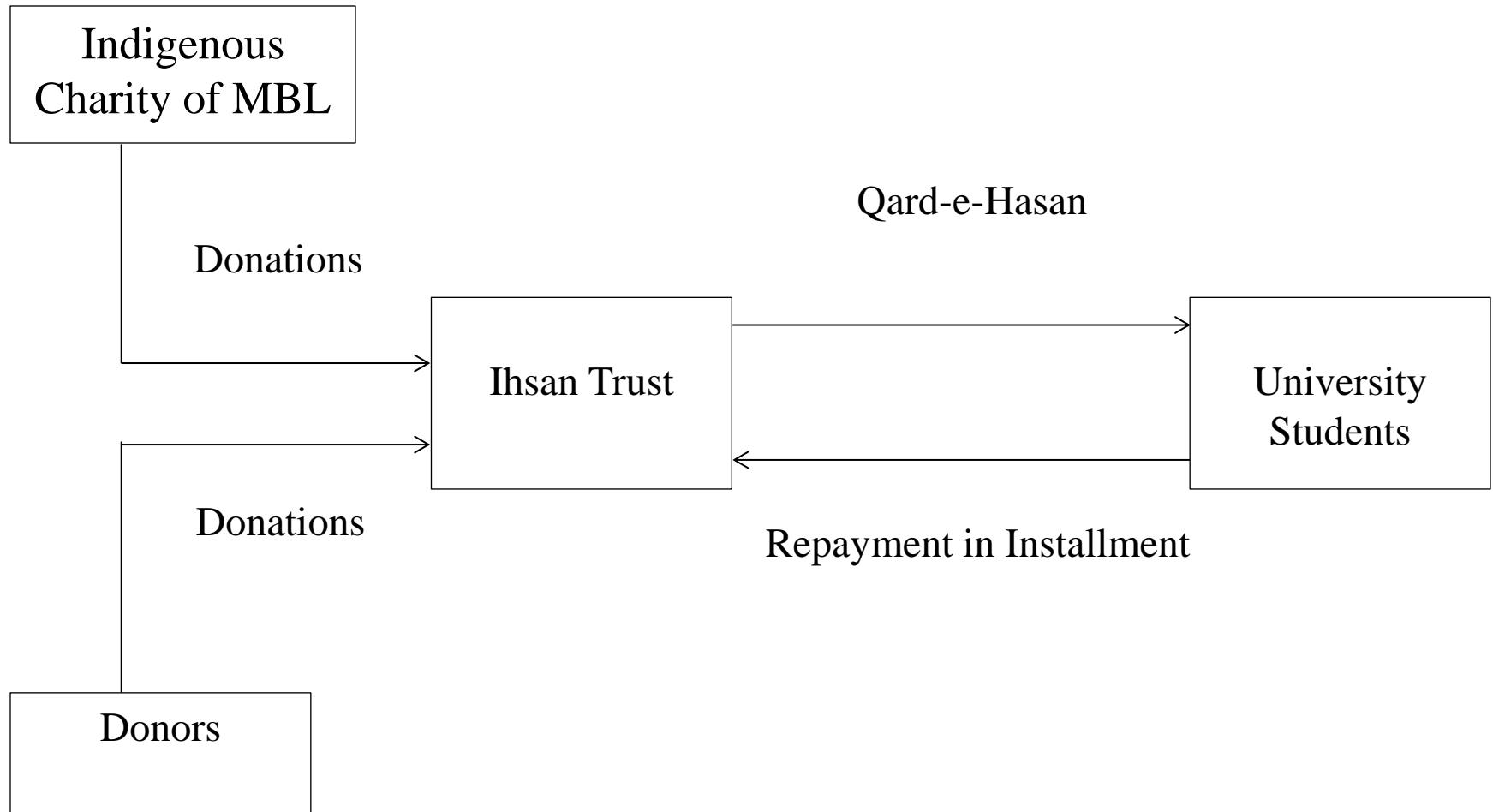
Akhuwwat Qard Based Microfinance Program



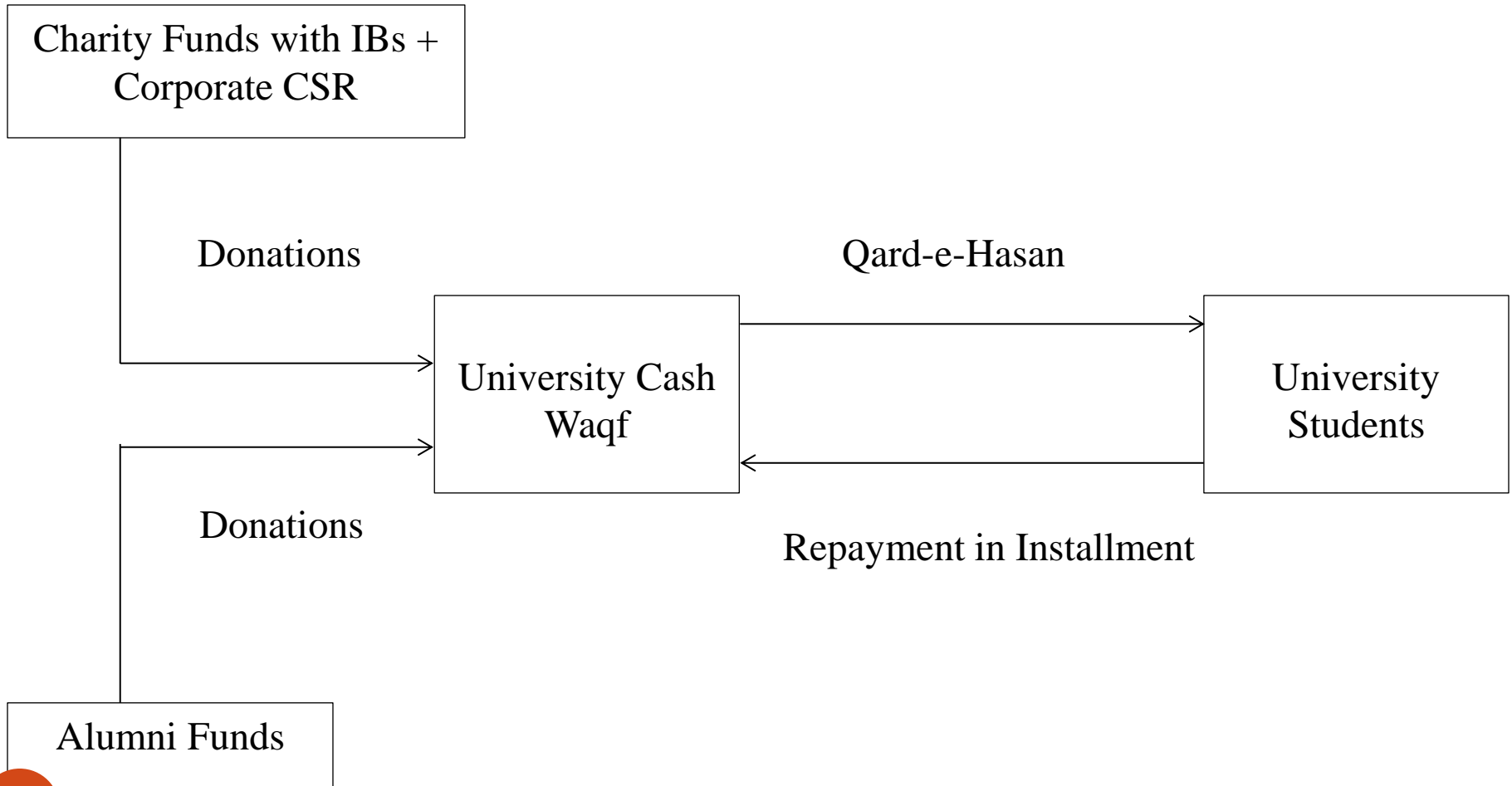
Crowdfunding for Provision of Public Goods



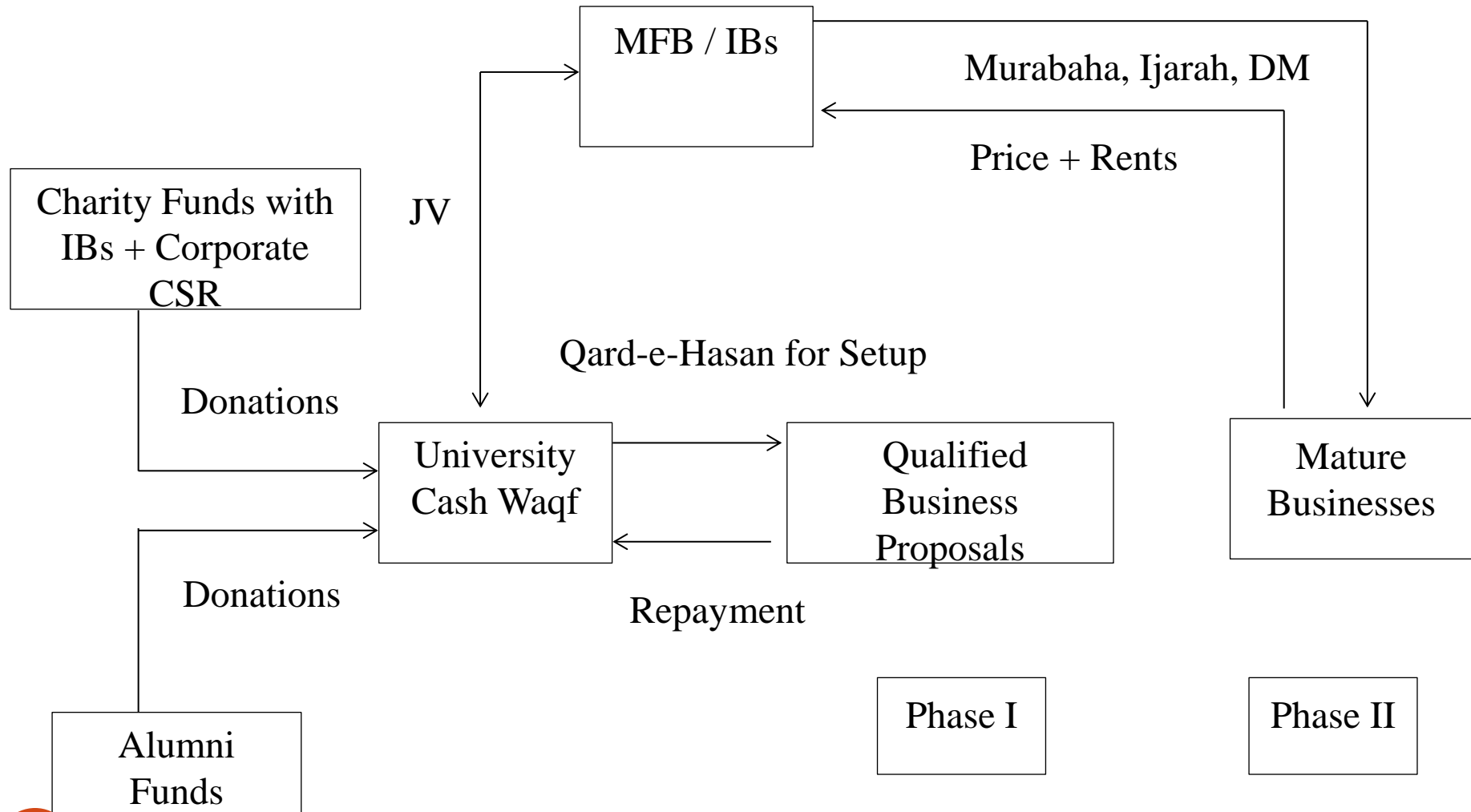
Ihsan Trust Education Finance



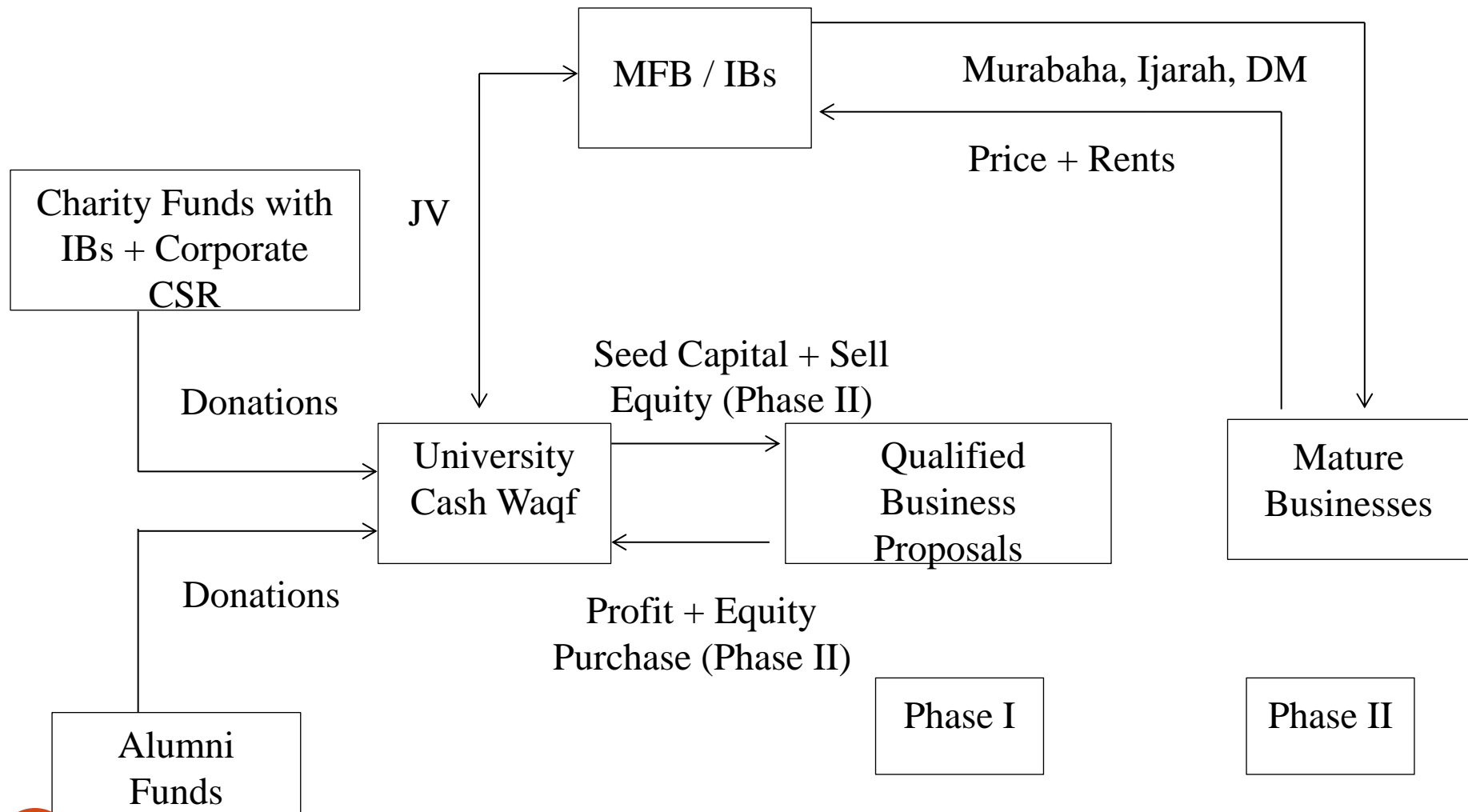
Financing Education Using Qard-e-Hasan



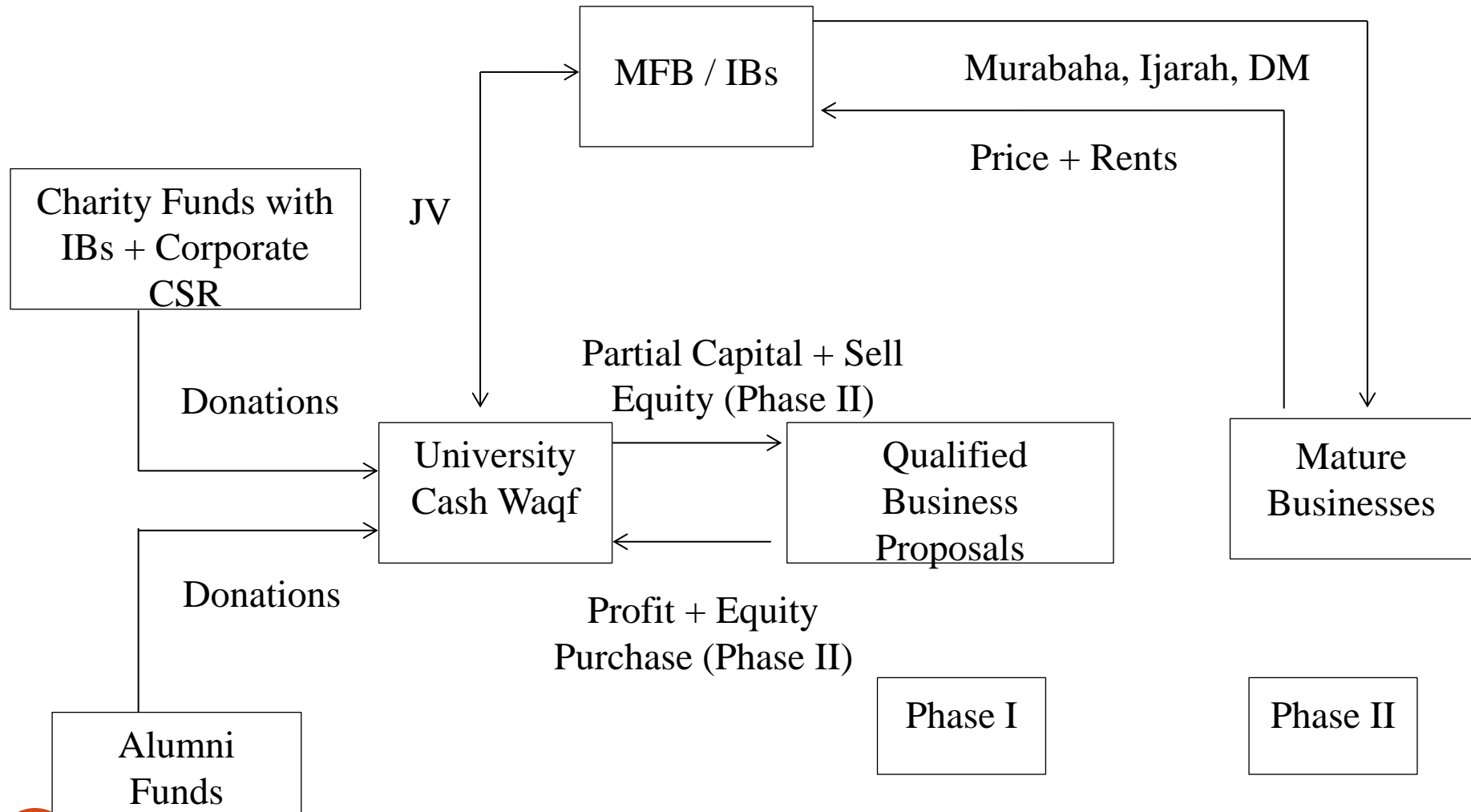
Financing Start-ups Using Qard-e-Hasan



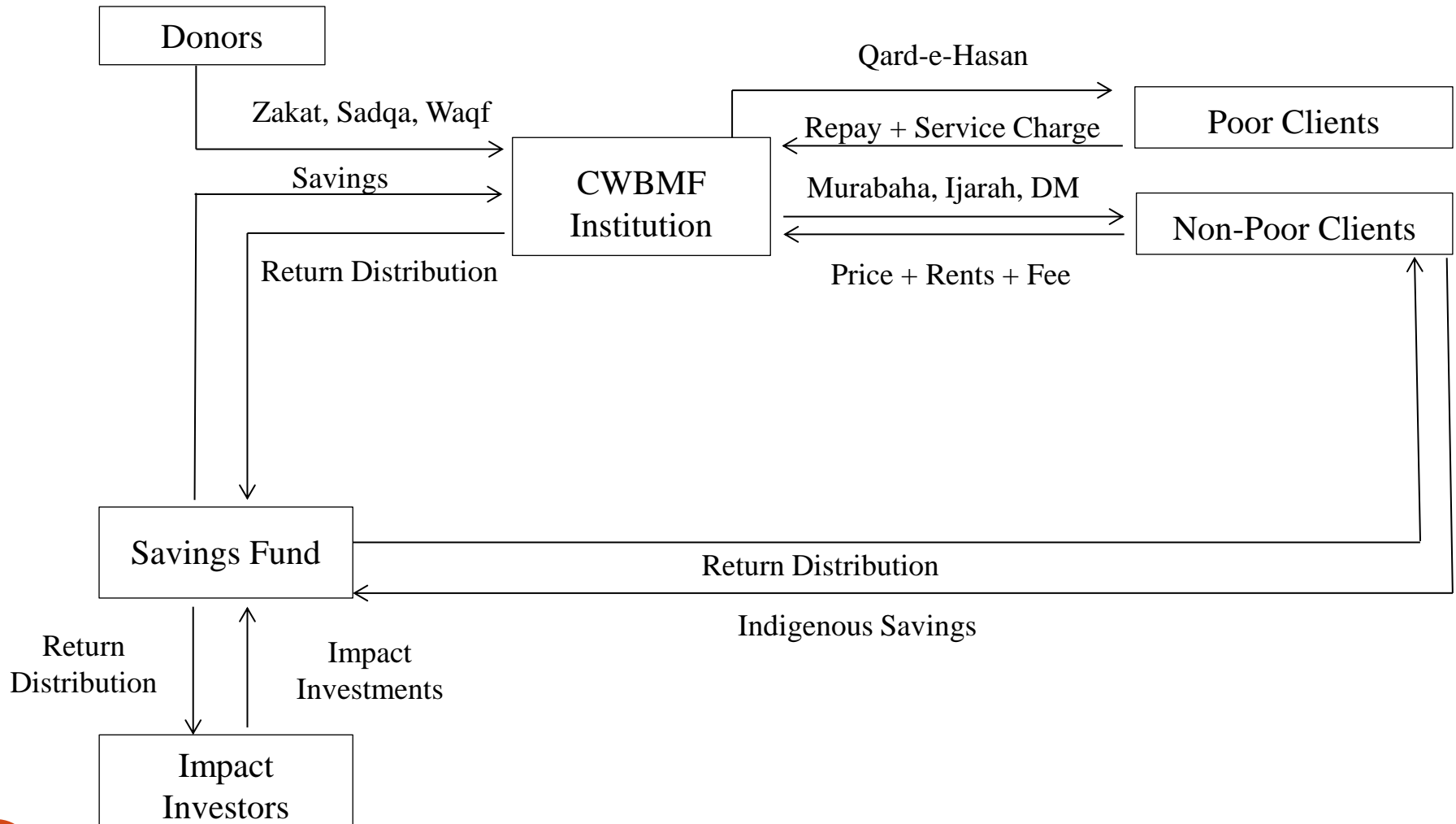
Financing Start-ups Using Mudarabah



Financing Start-ups Using Musharakah



Cash Waqf Based Micro Finance (CWBMF) Model



Designing Incentives for Effective Targeting

- Need to differentiate between the different categories of poor people.
- Let us define two categories of poor people in order to distinguish between moderate poor and ultra-poor.
- Non-poor people can be with and without investible capital.
- These four groups require income support, social and public support and market based finance.
- Usually, the poor people do not have investible capital.
- Non-poor people usually have an existing income source.
- In Table 1, the number in parenthesis denotes the level of priority. (1) Highest (2) Lower (3) Lowest.
- Priority rationalized through subsidized rates, rationing, and higher or lower PSR.
- Microenterprise is abbreviated as 'ME' and Profit Sharing Ratio is abbreviated as 'PSR' in Table 1.

Designing Incentives for Effective Targeting

Poverty Groups	Income Support	Social & Public Support	Market Based Finance
Ultra-Poor	Zakāt (1)	Bait-ul-Maal (1) Waqf	Mudarib in ME, PSR (2)
Moderate Poor	Zakāt (2) Qard-e-Hasan (1)	Bait-ul-Maal (2) Waqf	Mudarib in ME, PSR (3)
Non-Poor with Zero Investible Capital	Qard-e-Hasan (2)	Bait-ul-Maal (3) Waqf	Murabaha (1) Salam (1)
Non-Poor with Investible Capital	Not Applicable	Not Applicable	Murabaha (2) Salam (2) Musharakah Rabb-ul-Maal in ME, PSR (1)

Designing Incentives for Effective Targeting

- Ultra-poor will enjoy higher PSR than moderate poor people in microenterprise Mudarabah as Mudarib.
- They will not be provided with any debt with or without mark-up to avoid indebtedness before they reach a sustainable income and asset base to increase chances of poverty exit.
- They will have no incentive to underperform, shirk or free-ride. Their consumption needs can be fulfilled through Zakāt and Bait-ul-Maal.
- Their educational and health needs can be met through especially designed Waqf based educational and health centres.

Designing Incentives for Effective Targeting

- Moderate poor people will be provided with Qard-e-Hasan, but they will have lesser PSR in microenterprise Mudarabah.
- They will have lesser priority in Zakāt distribution and support from Bait-ul-Maal.
- They would want to show themselves as ultra-poor, but then they will not have availability of Qard-e-Hasan.
- If they want to access subsidized debt based modes of finance like Murabaha and Salam, they will have to show themselves as non-poor with zero investible capital. But, in that case, they:
 - Cannot remain Mudarib in microenterprise.
 - Will have lesser priority in access to Qard-e-Hasan.
 - Will have to make frequent rental or instalment price payments.
- Hence, the moderate poor people will have no clear incentive without any trade-offs to show themselves in any lower or higher poverty group.

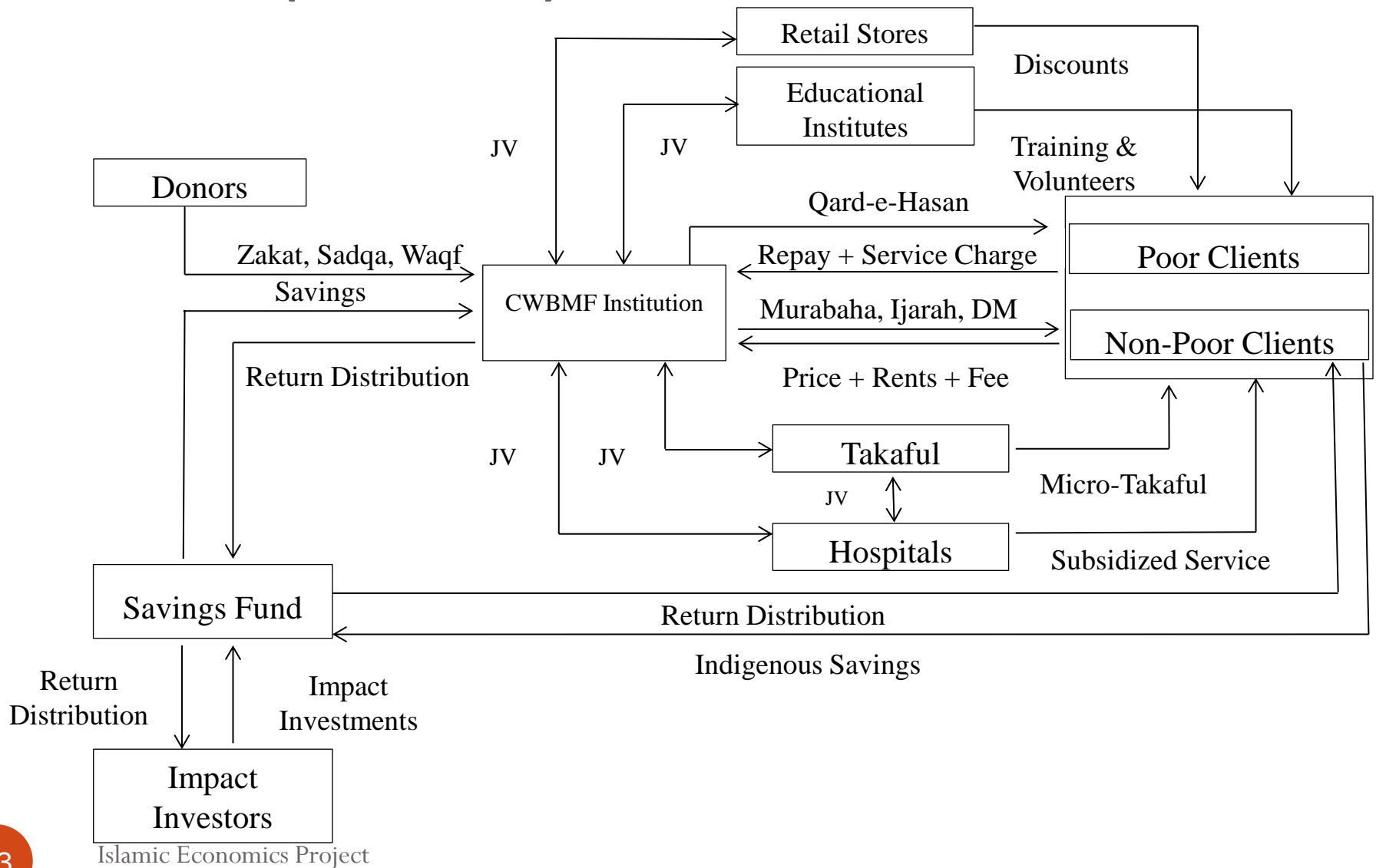
Designing Incentives for Effective Targeting

- Non-poor people with income source, but without investible capital would qualify to obtain subsidized finance using Murabaha and Salam.
- They will not be able to invest in microenterprise Mudarabah with highest PSR unless they show themselves as non-poor with investible capital.
- In that case, they will not qualify for Qard-e-Hasan or any income support from Zakāt or Bait-ul-Maal. They will also be disqualified from debt based Microfinance at the subsidized mark-up.
- If they show themselves as poor, then they will not be able to obtain debt based finance at subsidized mark-up. They will also not be able to keep their existing income earning occupation intact if they enter Mudarabah as Mudarib.
- Hence, these people also will not have any incentive to show in a higher or lower poverty group.

Designing Incentives for Effective Targeting

- Non-poor people with investible capital will qualify for debt based finance at market benchmark linked rates. It will encourage them to use equity based finance using the mode of Musharakah.
- They could also use their investible capital to enter in microenterprise Mudarabah as Rabb-ul-Maal. They will enjoy the highest PSR in order to incentivize their participation for creating a sustainable loop of funding for the microenterprises.
- But, these people would have an incentive to show themselves as non-poor with no investible capital so as to avail subsidized mark-up financing. But, they will lose out on availing higher PSR on investible capital.
- Tax incentives can be provided to the investment made and profits earned from microenterprise Mudarabah so as to incentivize investment participation.

Integrated Cash Waqf Based Micro Finance (CWBMF) Model



Operational Structure of the Integrated Program

Supply Side		Demand Side
Financial Funding & Contributions		
External	Social contributions via E-Crowdfunding to place Zakat, Sadqah and Waqf funds to IMFI.	Such contributions are used to provide Sadqah and Qard-e-Hasan to the needy clients.
	Social impact investing via E-Crowdfunding platform.	Proceeds are pooled and then used to provide sale and lease based Islamic financing.
Internal	Micro-savings using E-Wallet. Profit sharing ratio higher for micro-savers.	Clients open remunerative accounts and access money via E-wallet.
Non-Financial Contributions & Services		
Individuals	Micro-volunteering in training programs by students and professionals.	Volunteers provide training, vocational skills and business facilitation in the form of record keeping and basic calculations.
Institutions	Subsidized services from accredited schools, hospitals and retail stores.	Clients enjoy access to subsidized services only by spending through E-Wallet so as to incentivize its use.
	Micro-Takaful for health risks and accidents.	Clients with minimum E-Wallet balance get Micro-takaful. Higher savings ensure Micro-Takaful and higher profit share.
	E-Wallets / Debit Card issued by banks.	E-Wallets issued by banks are accessible through smartphones and smart cards.

Thank You

Questions & Feedback

salman@siswa.ukm.edu.my