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Islamic Microfinance for Sustainable Development

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A recently published book on "Islamic Microfinance for Sustainable Development" edited by Nasim Shah Shirazi, Abdelrahman Elzahi and Ishraga Khattab consists of 13 selected papers, which were presented during the second International Conference on "Inclusive Islamic Financial Sector Development: Enhancing Islamic Financial Services for the Microenterprises. In addition to the introduction, the book covers 13 chapters that are organized under five broad areas such as microfinance institutions experiences; efficiency and stability of microfinance institutions and microenterprises; microfinance models and job creation; Financial inclusion and Sharīʿah modes for microfinance; and microfinance and its relation with poverty reduction and women empowerment. The topics covered in the book draw on country experiences including Bangladesh, Indonesia, Nigeria, Pakistan and Sudan.

Islamic Social Finance Report 2014

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pp.125

This is a report on the Islamic social finance sector comprising institutions rooted in Islamic philanthropy, e.g. *zakāt*, *ṣadaqah* and *awqāf*. The report presents the historical trends, future challenges and prospects for the various segments of the Islamic social finance sector in South and South-East Asia, e.g. Indonesia, India, Pakistan, Bangladesh, Malaysia, Singapore and Brunei Darussalam. It examines the broad regulatory and policy environment at the macro level as well as good and bad practices at the intermediate and micro levels to suggest several policy alternatives with a view to encouraging healthy deliberations around them:

Zakāt:

1. Contrary to commonly held perceptions regarding lack of dependability in flow of donations, *zakāt* is sustainable, dependable and could be a growing source of funds for institutions that acquire the necessary professionalism in fund-raising and seek continued betterment in their social credibility through integrity, transparency and good governance.
2. At a macro-level growth in *zakāt* mobilization appears to be influenced more by incentives that make *zakāt* payment an attractive proposition and less by penalties and punishments.
3. There seems to be nothing inherently wrong with coexistence of public and private agencies as *zakāh* collectors.
4. Where *zakāt* collection and distribution is entrusted entirely to the state, *zakāt* may be seen as a component of aggregate resources available to the state. In this sense, *zakāt* payment may be seen as a perfect substitute of the direct taxes to the state and may be allowed as deductions to tax payable.
5. Corporatization that implies use of a large network of private institutional collectors for *zakāt* mobilization is seen to be far more efficient as compared to a large number of unconnected private individual collectors.
6. In the light of various legal opinions relating to distribution of *zakāt* among eligible beneficiaries there is a case in favor of a scheme of prioritization among different types of beneficiaries with highest priority being given to the needs of the ultra-poor.
7. Basic consumption needs are, by definition, more urgent than needs that may be deferred to a future date. However, there is also merit in using *zakāt* to enhance the wealth-creating capacity of the poor so that they are able to get out of the vicious circle of poverty and find lasting solutions to their needs.
8. Arguably, a professionally managed *zakāt*-financed microfinance program can potentially serve a much larger population of the poor as compared to the prospect of grant-making to a small number of beneficiaries. Further, a scenario where the poor are also made the sole owner of the revolving fund is on far stronger grounds.

9. *Zakāt* payment is an act of worship (*ʿibādah*) for the *zakāt* payer or *muzakki*. It is a matter of grave concern for the *muzakki* to ensure that his/her *zakāt* is not only paid, but also distributed in conformity with the norms of the Sharīʿah.
10. Separation of *zakāt* funds from other forms of donations is a primary concern for a *zakāt* institution acting as an agent of the *zakāt* payer or *muzakki* for distribution of *zakāt*.
11. A part of the *zakāt* mobilized by the institution may be utilized to absorb the administrative and operational costs of the *zakāt* institution.
12. There is a case in favor of using *zakāt* for covering genuine credit defaults by the poor, since such borrowers qualify as eligible beneficiaries in the eyes of Sharīʿah.

Waqf:

1. *Waqf* law should provide a comprehensive definition of *waqf* that includes both permanent and temporary *waqf*.
2. The legal framework must clearly articulate the permanent nature of *waqf*. At the same time, it must clearly recognize the importance of sustaining and enhancing the benefits flowing out of the *waqf*, this being the ultimate purpose of the act of *waqf*. This is possible only when the importance of development of *waqf* is clearly recognized.
3. The legal framework must not put undue restriction on creation of new *waqf* and should actually encourage creation of new *waqf* by minimizing financial and non-financial costs of *waqf* creation and management.
4. Incentivizing *waqf* in a manner similar to secular trusts and other forms of not-for-profit organizations, e.g. tax rebate on contributions for the donor/ endower would make the system both efficient and fair.
5. Whether ownership and management of *awqāf* should be in private hands or with the state has no clear answer. Contrary to general belief, state control may not necessarily hamper creativity and innovation in *awqāf* development.
6. Where *waqf* management is in private hands, the state agency as regulator should clearly stipulate elaborate and clear eligibility criteria for a *mutawalli* or nazir or trustee-manager not only covering aspects of integrity and trust-worthiness but also professional competence.
7. There is every reason for the state to take punitive action against *mutawallis* who fail the tests of efficiency, integrity, transparency.

8. *Waqf* development must be a mandatory obligation of the *waqf* management. Innovating financing methods may be employed that bring in new *waqf* capital for development of existing *awqāf*.
9. Financial penalties, especially when these are expressed in absolute numbers tend to lose their effectiveness as deterrents with time. These should either be subjected to continuous revision or be linked to the quantum of misappropriation. Physical punishments are potentially more effective.
10. It is compulsory to invest *waqf* assets. It would be rational to seek risk minimization through diversification or avoidance of high-risk investment avenues.

Islamic Financial Cooperatives & Non-Profit Organizations:

1. There are sound economic reasons why conventional microfinance and especially micro-credit may not be appropriate for the chronically poor and the destitute.
2. Given the Islamic emphasis on avoidance of debt, an Islamic MFI should refrain from seeking to entrap a client in ever-rising levels of debt.
3. *Zakāt* can form the basis of designing a range of programs for the poor, e.g. (i) safety net programs to meet basic consumption needs, health and education; (ii) economic empowerment programs involving skill enhancement and business development services; (iii) programs to provide emergency grants or credit; (iv) programs to provide micro-*takāful*; and (v) programs to provide guarantee against credit default.
4. The issue of high cost microfinance may be addressed by creating *waqf*s whose benefits may now be dedicated for absorption of specific cost elements so as to make microfinance affordable to the ultra-poor.
5. There seems to be merit in having a uniform regulatory framework for all forms of organizations that are engaged in microfinance activities.
6. Creative *fiqhī* solutions should be encouraged for addressing unique requirements of microfinance.
7. For-profit Sharīʿah compliant modes offer no in-built protection against exploitation and abuse through over-pricing. Identifying appropriate organizational structure may offer a bulwark against possible exploitation.
8. There is no consensus on how to estimate the actual cost of operations chargeable to the beneficiary under not-for-profit modes, such as, *qarḍ* and *kafālah*. There is a need to develop accounting standards for estimation of actual cost of operations.

9. A conventional MFIs seeking to transform into Islamic MFI is confronted with a range of issues at various levels. Law must recognize the special status of Islamic MFIs that are financial intermediaries as well as players in the real economy at the same time.
10. There is merit in the argument that Islamic MFIs should aim to empower families and not women alone.
11. Given the discomfort associated with high cost of microfinance making it unaffordable to the ultra-poor, the institutionalization of charity as well as voluntarism is a creative strategy that has the effect of drastically cutting down operational costs.
12. Models offering philanthropy and for-profit finance under one umbrella, as in case of BMTs may involve problems due to conflicting organizational culture and conflicting policy and regulatory framework.