Islamic Solidarity Fund for Development
Success Stories Series
ISFD-funded Microfinance Projects

ISLAMIC MICROFINANCE MAKES A DIFFERENCE

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Mutada Gasm Alseed earns a living making and selling handicrafts in Salab area, Port Sudan. With help from the Microfinance Support Program for Sudan, through the Port Sudan Association for Small Enterprise Development, he was granted a microfinance loan, with which he bought a three-wheeled vehicle (inset) to fetch supplies and transport his wares to his seafront stall. His business has improved greatly, and he has used the increased income to buy land and expand his business further: he previously sold goods in Port Sudan only, but now, he employs people to sell his handicrafts in four other places (Khartoum, Demazie, Dongola and Kasala).
The need for microfinance

There is a reason why poverty is often referred to as a ‘trap’ – it is because, without employment, poor people lack access to financial means to live with dignity. Poor people often lack the assets required by banks and other money-lending institutions to secure a loan. Even those who are able and want to work are constrained by lack of capital; they cannot start a business or invest in their existing activities.

Microfinance, the provision of small sums of money to individuals or groups, can be an effective solution. Its services, especially micro-credit, are granted to poor people who are economically active, so they can improve their lives. Those who are economically inactive first need support or aid to lift them out of chronic poverty, and become economically active; microfinance can then help build their livelihoods further.1

Developing microfinance is a strategic priority for the Islamic Development Bank (IsDB), and its poverty-alleviation arm, the Islamic Solidarity Fund for Development (ISFD), has established a number of microfinance projects to promote economic conditions of people in Sudan. Capital loans and technical assistance grants have been provided to national governments in IsDB member countries to fund projects that enable poor people to improve their livelihoods.

This success story looks at microfinance projects funded by ISFD, using Islamic microfinance projects in Benin, Kazakhstan and Sudan, and integrated projects in Senegal and Sierra Leone that included microfinance components. Each of these provides examples of the positive changes that microfinance can bring to people’s lives.2

Cover photo: Mrs Colette Tevi is the president of the Groupement Maria Gbê in Agla, Cotonou, Benin. Members of the group took progressively larger loans via the Integrated Program for Microfinance Support in Benin over several years. Little by little, women have saved and re-invested, making better lives for themselves and their families. “Thanks to this programme, I have been able to open a small shop and help my children and grandchildren,” says Mrs Tevi.

Nadia Akiyo of Togba, Benin, decided to start a business when her parents left her a hectare of land. “I started with 100 chickens, then slowly invested in housing. Now I have 3,000 square metres of housing, with a capacity for 15,000 chickens. I have 8,000 ‘layers’ at the moment – 5,500 thanks to the loan from UNACREP [a microfinance institution that was part of the Integrated Program for Microfinance Support in Benin]. The loan also helped me to buy 6,000 chicks, so soon I will have 14,000 layers and be near to my capacity.”
Most of the farmers who received funds from the Microfinance to Rural Areas project in Kazakhstan bought tractors, which are essential equipment for any farm. Yakupov Turganzhan of Penzhim village, Panfilov district, received KZT 2.3 million (US$6,792) in 2013 to buy a tractor. He uses it for land cultivation, seeding, harvesting, digging irrigation trenches and transporting coal in winter. Owning the tractor made his life easier, as he is able to do all the jobs he needs to in a much shorter time.
Islamic microfinance: a different approach

Islamic microfinance differs from other forms of microfinance in that it is based on Shariah principles. In particular, it follows the Qur’anic precept that fiat money has no intrinsic worth; those who provide funds are considered investors rather than creditors – they must share the business risks with the person who requires the funds. These two fundamental principles give rise to one of the central features of Islamic finance: it is forbidden to charge or pay interest. As Musa Jega Ibrahim, ISFD's Senior Economist, explains: “With Islamic microfinance you can profit from an activity, but not from money itself.”

Shariah-compliant financial services are essential for Muslims who want to access funds to improve their well-being. But many people worldwide also see Islamic microfinance as a fairer approach than conventional microfinance systems, which charge interest and place the business risks solely on the borrower.

Ignace Dovi, the Director of the national Microfinance Association in Benin (ALAFIA), believes that Islamic microfinance is “innovative ... ethical and could make business clearer and cleaner ... reimbursements depend on the profit (or loss) of an activity, not on fixed interest, and transparency is key.”

Clients also appreciate the principles of Islamic microfinance. Hospice Acclombessi of Griff Perso designers in Cotonou, Benin, which benefitted from the ISFD-supported project there, said, “we feel secure knowing that [the microfinance institution] would help us with our business plan, become partners, and follow us, be there, as we put the plan into action. That was really reassuring.”

Microfinance institutions are also learning to appreciate this different approach to providing funds. Ismaila Radji of Sian’son (Benin) said, “This product is better adapted for these situations and so can help the fight against poverty, increase employment and well-being, and [has] other social benefits. It is more work for us for sure, but it helps our NGO to better realize our social goals.”

“The future of microfinance is in Islamic microfinance”
– Mrs Mbake Khady Fall Ndiaye, Programme Director, VOLIP
ISFD-funded microfinance projects

ISFD funds microfinance projects in several member countries, through the Microfinance Support Programme, the Vocational Literacy Program, and other individual projects.

**Senegal**
The Vocational Literacy Program in Senegal (Le Programme d’Alphabétisation et d’Apprentissage de Métiers pour la Réduction de la Pauvreté) was a pilot programme that integrated basic education, and vocational and literacy training for women and youth with microfinance support for women and youth enterprises. Islamic finance was new to Senegal, and the project introduced *murabaha*. The project also established a revolving fund to sustain the availability of microfinance for future clients.

5,000 women and youth sensitized to the principles of Islamic microfinance, and 224 people trained in Islamic microfinance.

**Sierra Leone**
The ‘youth and micro-, small and medium-sized enterprise development’ component of the Sierra Leone Community Driven Development project included microfinance. ISFD contributed US$2.05 million to this component, out of the total cost of US$2.207 million. Micro-enterprise groups were established from pre-existing self-help groups, then trained in business and financial management, and given access to revolving microfinance funds. The microfinance was not managed according to Islamic principles, but the government intends to provide Islamic financial services in the project’s second phase.

150 micro-enterprise groups established, trained in microfinance and business management, and serviced with micro-grants and micro-credit from a revolving fund.
Benin

The Integrated Program for Microfinance Support (Programme Intégré d’Appui à la Microfinance) provided two lines of microfinance: one for income-generating activities that used conventional modes of financing, and one for micro- and small enterprises that used ‘participatory microfinance’, in the form of mudaraba. IsDB contributed US$10.45 million, including US$5 million from ISFD. The project laid the groundwork for capacity-building in Islamic finance for microfinance institutions.

256 micro- and very small businesses received Islamic microfinance support, comprising 989 direct beneficiaries.

Kazakhstan

The Microfinance to Rural Areas project in Kazakhstan was implemented by the state-owned Fund for Financial Support for Agriculture through its branches across the country. ISFD provided US$10.15 million of the total project cost of US$12.17 million. Microfinance was extended to clients using a version of murabaha, but the terms adopted included a markup based on an annual percentage rate. A popular feature was the finance ceiling (US$33,000), which enabled clients to purchase tractors and other machinery – something that was previously impossible.

96.7% payment rate by clients with outstanding finance at the end of 2015.

Sudan

The Microfinance Support Program for Sudan is a huge project with an estimated budget of US$63.5 million; IsDB provided US$14.45 million, including US$3 million from ISFD. The programme targeted seven groups: micro-entrepreneurs, female heads of households, unemployed graduates, skilled labourers, micro-entrepreneur start-up projects, deprived rural productive families and active disabled people. In line with Sudan’s national policy, all of the microfinance provided to clients was murabaha.

56,000 clients provided with microfinance, of whom 51% are women.
Mubarak Defan Defullah of Athoura Karery area, 29 district, Sudan, produces oil and cakes for livestock feed from sesame seed. In 2015, the six partners in the business received SDG25,000 (US$3,843) from the Sudan Development Foundation (a microfinance institution supported by ISFD’s Microfinance Support Program for Sudan) and others to buy this sesame seed press. Defullah was happy with the “smooth process” for obtaining the microfinance, and says there were “no problems”. He and his colleagues are making a success of the business, and he estimates their profit to be SDG1270 (US$195) each day.
Sudan: The ‘gold standard’

Of all the microfinance projects supported by ISFD, the Microfinance Support Program for Sudan is a leading example of how these interventions can make a real difference to reducing poverty. Some of the factors that made this a success are inherent to Sudan. For example, the national banking system is Islamic, and the policy environment promotes Islamic microfinance, which is one of the government’s highest development priorities. But several other characteristics could prove useful for other countries looking to establish Islamic microfinance products.

- **Oversight of the microfinance sector is centralized.** The Central Bank of Sudan regulates the sector and issues directives and policy. While the sector is supervised by a Higher Council for Microfinance, each state has a State Council of Microfinance, and there are microfinance units at each of the Central Bank’s regional branches and at the headquarters of each commercial bank. All these units reflect the government’s commitment to making microfinance as widely available as possible.

- **Sudanese microfinance institutions receive wholesale funding under muduraba.** According to Professor Badr El Din A. Ibrahim, former President of the Central Bank of Sudan’s semi-autonomous Microfinance Unit, “the mudaraba contract is not only reducing default cases and giving incentives to microfinance institutions [by] generating higher profits, it is also making sure that the wholesale finance is going to intended clients/projects”. The default rate on repayment is estimated at just 2 per cent.

- **The project provided training alongside financial products.** For example, the Sudan University of Science and Technology’s Institute of Family and Community Development Business Incubators Project obtained US$500,000 from the Microfinance Support Program to provide graduates with microfinance and vocational training, and establish business incubators. This means that those receiving microfinance are equipped with the skills they need to make their enterprises work, thus ensuring the funds are repaid and their businesses prosper.

The Sudan University of Science and Technology’s Institute of Family and Community Development fashion incubator runs short courses for 20–25 participants, covering topics from basic sewing to final design.
The four micro-enterprise groups in Kenema district, Sierra Leone, appreciated being trained in business enterprise management as part of the Sierra Leone Community Driven Development project, especially the improvement in their business skills and financial management; they also appreciated the easy access to microfinance facilitated by the project.

Success factors

The five projects profiled in this success story each achieved great impact in terms of improving access to finance for poor people. These successes were thanks to a number of different factors.

- **Integration with government services.** In Kazakhstan, Sierra Leone and Sudan, government agencies managed the project, while in Benin and Senegal, government agencies participated in a multi-stakeholder arrangement for project management. Government involvement makes it far more likely that a policy environment supportive of Islamic finance will be put in place.

- **Training in Islamic microfinance management.** Making training part of a project – for the project management unit, microfinance providers and clients – increases the chance of success, especially when this is carried out in advance of microfinance being made available. Training familiarizes people with the customs of Islamic financing, which may be a new approach in a country, making the process of applying for and receiving funds much smoother.

- **An integrated livelihoods approach.** Incorporating training – financial, vocational and business management – into microfinance projects makes it more likely that the micro-enterprises that access microfinance will increase their profits.

- **Cultural familiarity with Islamic finance or similar.** Familiarity with the principles makes it easier for people to adapt to this way of working. In Sudan, for example, the whole financial system is geared to Islamic finance, meaning the project held no surprises. In Benin, Islamic finance was called ‘participatory finance’ because of the predominance of Christianity in this secular state. As the basic principles were similar to the traditional tontines, they were widely accepted.

- **Credit monitoring of microfinance providers.** Oversight of projects by the project management unit, and of clients by the microfinance providers, is supportive. Microfinance institutions are encouraged to manage their clients with a compassionate but firm approach.

“**A big difference with Islamic microfinance is that it finances an activity, not a person**”

– Huette Assou, Coopérative pour la Promotion de l’Epargne et du Crédit, Benin
Islamic microfinance: A system with huge potential

The ability of microfinance to reduce poverty is clearly illustrated in the five country projects highlighted in this success story. And everyone involved – from the clients to the microfinance institutes – want more of the same.

The reasons are also clear – Islamic microfinance is a fairer system between client and provider. Because of this, the principles of Islamic microfinance are applicable beyond the Muslim world. Many new Islamic microfinance measures have the potential to be modified and used elsewhere. There are many people in the world who would appreciate the transparency of the mechanisms developed under a philosophy that strictly prohibits the taking or paying of interest. As Professor Badr El Din A. Ibrahim, former president of the Central Bank of Sudan’s Microfinance Unit, says: “All of these are applicable on a wider scale.”

ISFD’s contribution to supporting microfinance has already made a huge difference to thousands of lives – and the potential is there to help many thousands more.

1 Obaidullah, M. 2008. Introduction to Islamic Microfinance. IBF Net, India.
2 For more information on the IsDB/ISFD microfinance projects in Benin, Kazakhstan, Sudan, Senegal and Sierra Leone, see ISFD Success Stories Series Nos 2, 5, 4, 1 and 3, respectively.
3 All exchange rates are correct as of November 2016.
4 Islamic microfinance is known as participatory microfinance in secular Benin.
5 Mudaraba (trustee) financing is a contract between a financer and an investment manager or entrepreneur (the person requesting the money). Business risk is borne by the entrepreneur, and the financial risk solely by the financer, and profits are shared between the two in accordance with a contractually agreed ratio.
6 Murabaha is the credit sale of an asset, delivered on the spot, in which the purchaser can pay the price of the asset at a future date, either as a lump sum or in instalments. Microfinance institutions charge a markup percentage on top of the cost of the asset to cover administration charges. In pure murabaha, the markup does not change over time, so the client pays the fixed amount whether they pay on time, in advance or even late.
7 Tontines are informal revolving savings and credit groups widespread across West Africa. They generally comprise five to ten farmers of the same sex who contribute money at regular intervals, with each member in turn receiving the full amount collected.

“Our operators looked around for small businesses and asked them if they would be willing to teach their skills to local youth. In return, they would receive teacher training, and be provided with more equipment or space to be able take on small groups of apprentices. And it worked well!” – Mbacke Khady Fall Ndiaye, Director, PALAM, Senegal.
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