

Reasons For Failure Of The Practices In Islamic Microfinance Of Commercial Credit In Sri Lanka – With Special Reference To Commercial Credit Head Office Colombo

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Abstract : *Islamic Microfinance has been identified as an important tool in increasing the productivity of poor and help to economic development and it has become one of the new recent hottest topics that provide alternative way for funding poor Muslim people and The purpose of this research is to investigate serious reasons for failure of the practices in Islamic Microfinance of Commercial Credit in Sri Lanka. There are lack of financial techniques and human resources etc. Therefore, this study examines the impact of selected reasons in Islamic Microfinance failure and it is practiced by Commercial Credit. Qualitative and quantitative methods are used to carry out the research which includes personal interview, questionnaire and secondary data materials. Questionnaires are dealing with selected reasons for failure of the practices in Islamic Microfinance of Commercial Credit. The target population for this study considers the staff of Commercial Credit Head office. A simple random sampling technique is used to select the respondents surveyed for this study. For data statistical analysis, the researcher applied statistical package for Social Science (SPSS) 21.0 computer software package under which person Coefficient, Coefficient of determination and Regression analysis were calculated to analyze data. This study is identified the reasons for failure of the practices in Islamic Microfinance of Commercial Credit in Sri Lanka. Findings indicate that there is a significant positive relationship between selected reasons and failure of the practices in Islamic Microfinance from the sample point of view. This research reveals that staffs at Commercial Credit have perceptions that the selected reasons for failure of Islamic microfinance on practices of Commercial Credit in Sri Lanka. The study recommends for Islamic Microfinance staff working in market needs adequate training, motivate the staff, use the latest technological systems, learn and get knowledge in Islamic Law, government must invest in supportive financial*

infrastructure and appropriate Shariah supervisory board.

Key words: *Microfinance, Islamic Microfinance, Commercial Credit, Failure, Sri Lanka.*

Introduction

Islamic Microfinance has become one of the new recent hottest topics that provide alternative way for funding poor Muslim people. This type of funding depends basically on following the Islam instructions of not to charge interest rate on loans disbursed. However, Islamic micro financial institutions can charge borrowers specific amount decided in advance to cover up the operating expenses incurred by the institutions when operating. The main idea behind the interest rate forbidding lies in the theory that money cannot be treated as a commodity hence it cannot be increased alone or without involving other factors with it.

The religious perception about the interest rate along with other qualification requirements represent the major obstacles that hinder poor Muslim people to approach Conventional Commercial banks and other financial institutions for credit. This clearly indicates the need to establish a suitable credit system capable of meeting the un-banked Muslim people's needs without breaking their religious rules. This Islamic finance gives an opportunity for needy Muslim poor people to apply for loans that might be used in creating new job opportunities which will eventually contribute in mitigating their poverty level.

Islamic finance has another branch of finance called Islamic Microfinance. Islamic Microfinance is specifically designed for underprivileged people

who lack access to credit and who do not want to violate the Islamic laws of borrowing.

The basic principle of Microfinance as succinctly expounded by *Dr. Muhammad Yunus*, the Founder of Grameen Bank Bangladesh and the recipient of the Nobel Peace Prize in 2006, that Credit is a fundamental human right. The primary mission of Microfinance is, therefore to help poor people in assisting themselves to become economically independent. Credit or loan is given for self-employment and for financing additional income generating activities. The assumption of the Grameen model is that the expertise of the poor is under-utilized. In addition, it is also believed that charity will not be effective in eradicating poverty as it will lead to dependency and lack of initiative among the poor.

Microfinance is a powerful poverty alleviation tool. It implies provision of financial services to poor and low income people whose low economic standing excludes them from formal financial system. Access to services such as credit, venture capital, saving, insurance, remittance is provided on micro scale enabling participation of those with severally. The provision of financial services to the poor helps to increasing household income and economic security, build assets and reduce vulnerability creates demand for other goods and services and stimulates local economic.

During the long journey of Islamic Microfinance in Sri Lanka massive numbers of Islamic Microfinance programs have been launched targeting the rural population. Government organization and non-government organization have contributed significantly to the development of Islamic microfinance activities in Sri Lanka.

Islamic Microfinance is most applicable on Commercial Credit in Sri Lanka and they introduce their products to market in 2013. They give some products for consumers but these days they faces many problems for sell their products to market. . So this study is going to find out the Reasons for failure of the practices in Islamic Microfinance of Commercial Credit in Sri Lanka with special reference for Commercial Credit head office-Colombo.

Problem Statement

Islamic Microfinance applicable on Commercial Credit in and it is a first license commercial Bank in Islamic Microfinance applicable in Sri Lanka. Commercial credit produces their Microfinance for customers and towards that they have achieved

profit. But when they exercising this program they certainly failure to produce their Islamic Microfinance products to market they should stopped their servicers in the market also. Through this study researcher attempts to explain the reasons for failure of the practices in Islamic Microfinance of Commercial Credit in Sri Lanka and the solution can be taken it.

Research Question

The research is based on following research question:

1. What are the reasons for failure of the practices in Islamic Microfinance of Commercial Credit?

Follow up Question

This problem is analyze through these follow up Questions

- ✓ What are the internal reasons (in side of the office)for failure of Islamic Microfinance in Commercial Credit?
- ✓ What are the external reasons (out of the office)for failure of Islamic Microfinance in Commercial Credit?
- ✓ What are the Shariah based reasons (based on Islamic Law)for failure of Islamic Microfinance in Commercial Credit?

Objectives of study

General Objective

The general objective of the study is to find out the internal and external reasons for the failure of Islamic Microfinance in Sri Lanka.

Specific Objectives

- ✓ To find out the internal reasons for failure of the practices in Islamic Microfinance of Commercial Credit in Sri Lanka.
- ✓ To identify the external reasons for failure of the practices in Islamic Microfinance of Commercial Credit in Sri Lanka.
- ✓ To find out Shariah based reasons for failure of the practices in Islamic Microfinance of Commercial Credit in Sri Lanka.

Research Methodology

Type of study

Commercial credit is taken for the study. This study has been carried out with their reason for failure of the practices in Islamic Microfinance and identifies the accurate reasons. Researcher has carried out a pilot survey. Therefore, this research is an exploratory research design to explore to the selected reasons for failure of the practices in Islamic Microfinance providing better understanding.

Data and method of Data collection

While deciding about the method of data collection to be used for the researcher should keep in mind two types of data.

Primary Data

Primary data is collected by Dream Fulfiller (Microfinance) of Commercial Credit and staff were interviewed and discussed with and had recorded their collective information. In addition, needed information was collected through a self-designed structured questionnaire. Questionnaires were distributed directly to the Dream Fulfiller and Islamic Bank unit Staff. The questionnaires contain questions that are related to selected factors of Islamic Microfinance.

Secondary Data

Category	No. of population	Sample Selected	Percentage (%)
Staff	30	30	100%

Table: Population and Sample of commercial credit

Hypothesis

Some selected serious reasons are taken for the hypothesis testing. Islamic Microfinance sector in Sri Lanka Commercial Credit is affected by these

Secondary data mean which have already have been collected by someone else and which have already been through the statistical processes. When the researcher utilizes secondary data then he has look into various sources from where he can be obtain them. In addition to this other relevant secondary sources and analyzed to archive the research objectives. It is as follows:

- ✓ Magazine, Books, Journals, Research Article and Newspapers.
- ✓ Annual report of commercial credit.
- ✓ Websites, audios, video and broadcasts.

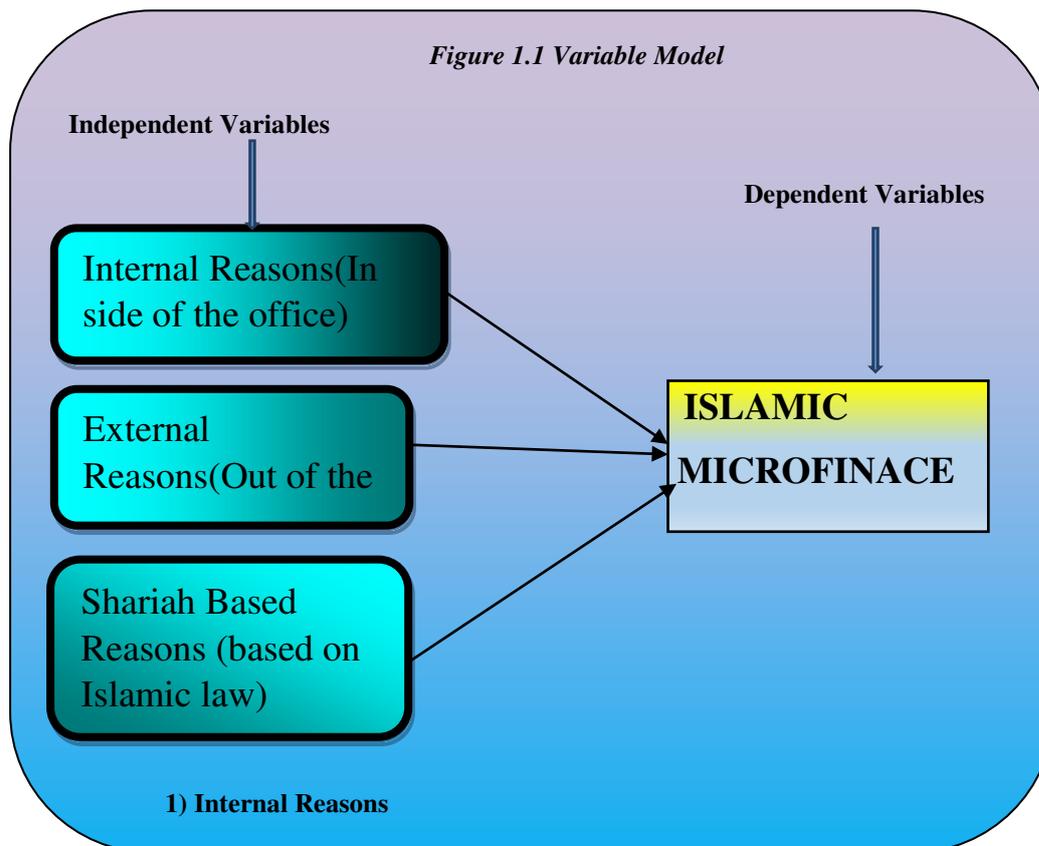
Method of Measurement

For data analysis, descriptive analytical techniques such as column charts, line charts, pie charts, graphical illustration etc. were used. For the statistical analysis, the researcher applied statistical package for Social Sciences (SPSS) 21.0.

Population and Sample

The target population for this study comprised Dream Fulfiller (Microfinance) and staff of Commercial Credit head office Colombo. The samples of 30 them are randomly selected and were collected.

reasons. Therefore the reasons have been considered as independent variables. Islamic Microfinance has been considered as dependent variable.



- ✓ H1 There is a negative relationship between internal reasons and Islamic Microfinance an inside of the bank
- ✓ H0 There is no negative relationship between internal reasons and Islamic Microfinance an inside of the bank

2) External Reasons

- ✓ H2 There is a negative relationship between external reasons and Islamic Microfinance in outside of bank
- ✓ H0 There is no negative relationship between external reasons and Islamic Microfinance in outside of bank

3) Shariah Based Reasons

- ✓ H3 There is a negative relationship between Shariah Based reasons and Islamic Microfinance in bank
- ✓ H0 There is no negative relationship between Shariah Based reasons and Islamic Microfinance in bank

The theory of Islamic finance gives view to the development of Islamic banking where the functions of a bank do not vary between conventional and Islamic banks. However the operations, philosophy and objectives differ significantly between the conventional and Islamic banks.

Despite the wide acceptance of Islamic banking worldwide, the concept of financing for the poor or microfinance by Islamic banks not well developed. Many elements of microfinance would be considered consistent with the broader goals of Islamic banking both system advocate entrepreneurship and risk sharing and believe the poor should take part in such activities.

Toward that commercial credit also provide Islamic Microfinance facilitates for the poor persons in Sri Lanka But when they provide their performance they face many problems. So this problems will impact the growth of Islamic Microfinance sector and that is the reason for failure of the practice in Islamic Microfinance in Sri Lanka.

So finding those reasons and suggests some alternatives and recommendations for those reasons

Significant of Study

that may create the positive answers in Islamic microfinance sector in future. This will also affect the country's economic growth.

According to Commercial Credit potential, the failure of reasons was not researched in details. Hence, this study is very significant.

Scope of the Study

This study is based on reasons for failure of the practice in Islamic Microfinance of Commercial Credit in Sri Lanka and it's carried out especially about Commercial Credit in Commercial head office - Colombo. Therefore it describes how the Commercial Credit exercising the microfinance and what is the output and reasons for failure towards on it. (With special reference to Commercial Credit- Colombo head office)

Limitation of the Study

- ✓ The limitation of the study concerns the instruments Dream Fulfiller and staff the research. This study was limited to an interview and questionnaire administration methods with the hope of clarifying or explaining issues that cropped up during administration questionnaires.
- ✓ The sample size will also make it extremely difficult to generalize of the study to cover commercial credit.
- ✓ Due to workload and long hours of bank work, the researcher could not have all respondents responding to the questions asked especially staff.

Literature Review

The research article on "Microfinance Banking in Nigeria: Problems and Prospects" (Acha Ikechukwu A, 2015). He said the failure of community banking scheme and many previous government's micro financing schemes was predicated on the challenges they faced. Many of these challenges are still bedeviling microfinance banking. The lack of banking culture in the rural areas and among the urban poor is another factor militating against the progress of microfinance banks, the issue of frowning at interest on loans takes a religious dimension, have badly damaged public confidence in these banks. Another important factor identified to militate against the performance of microfinance banks identified by is limited support for human an institutional capacity building. Include lack of training opportunities and poor conditions of service. The quality of

manpower in these banks is reflected in the poor performance of many of them, inefficiency and high levels of frauds and forgeries. The banks also suffer from high labour turnover a further indication of low staff motivation and poor personnel practices, The standard of corporate governance in many microfinance banks are poor, the multiplicity of the institutions and their diverse nature possess a regulatory challenge, Another prevalent problem among microfinance banks is the copying, competing and mimicking the practices of commercial banks. The constant government policy changes offer its set of challenges to the microfinance banks.

The journal on "Challenges Facing Islamic Financial Industry" (Zamir Iqbal, 2012) indicates, for Islamic financial institutions, a financial engineering challenge is to introduce new Shariah compatible products that enhance liquidity, risk management, and portfolio diversification. Generally, attempts to apply financial engineering techniques to Islamic banking will require committing a great deal of resources to understanding the risk-return characteristics of each building block of the system and offering new products with different risk-return profiles that meet the demand of investors, financial intermediaries, and entrepreneurs for liquidity and safety. Securitization is a prime candidate for financial engineering. And the other hand Related to the challenge of financial engineering is another operational challenge for Islamic banks: the need to standardize the process for introducing new products in the market. And the other hand Risk Management and Diversification is one another challenge. Risk management is practiced widely in conventional financial markets; it is underdeveloped in Islamic financial markets. Due to limited resources, Islamic banks are often unable to afford high cost management information systems or the technology to assess and monitor risk in timely fashion. And development of capital markets is another challenge. Responding to the current wave of oil revenues and growing demand for Shariah-compliant products, Islamic capital markets are expanding at a quickening pace, and stakeholders are starting to realize their potential. Furthermore, Muslim stakeholders in middle-income countries are increasingly expressing their preference for Shariah-complain.

The journal article on "Islamic Microfinance Industry in Yemen- Challenges and Opportunities" (Ali Saleh Alshebami, 2015).Islamic Microfinance industry in Yemen is still in its infancy, both conventional and Islamic micro finance face a lot of difficulties and challenges in the market.

However due the religious view and complex culture that exists in Yemen society, it is believed that, the traditional microfinance faces more challenges than the Islamic one. Such as, There are no proper ways and techniques for spreading awareness about the significance of the Islamic microfinance industry to low income people in particular and the country in general, People generally do not prefer to use their own jewelries and properties as guarantees because they have the fear of losing them if they are given for collateral purpose, The limited source for funds for micro financial institutions restricts the outreach of Islamic Microfinance is to reach the rural people in far areas, as most of the Islamic Microfinance are funded by the social fund for development only, The negative role played by the commercial and Islamic banks in not down scaling their operations to the level of the poor households, The new threats from the extremists to conventional micro financial institutions that provide both Islamic and conventional products and services lead to shutting down the whole institution.

Here above researchers found the reasons for failure of Islamic microfinance in other countries. It is not researched the "Reasons for Failure of the practice of Islamic Microfinance particularly based on commercial credit in Sri Lanka". With this background in the present study is exploring the "Reasons for Failure of the practice in Islamic Microfinance of Commercial Credit: with special reference on Commercial Credit Head Office - Colombo".

Conclusion

Successful Microfinance increases access to financial services for a growing number of low income clients, offering them quick and simple savings and loan services. Smaller loans are easy to manage, and, thus, often, short-term, with larger loans dispatched based on timely repayments, the borrower's cash flow and character with alternative forms of collateral used to motivate repayment.

Islamic Microfinance is still being acting in Sri Lanka in various places now, such as NGOs, BOC and etc. But they were also facing many difficulties to produce their servicers to market. Sri Lanka becomes as one of the few countries in the World which has specific legislation for Shariah compliant financial operations. That's for the reason banks are bear to provide Islamic Microfinance product and services to customers.

Islamic Microfinance needs dedicated and competent managers supported by well-trained and

motivated staff. There is a need to constantly build capacity through internal and external training. The current awareness of Islamic Microfinance needs to evolve from basic bookkeeping, portfolio management and loan officer training and incentive schemes to internal and external auditing, financial and treasury management, diversification, fraud control and accessing commercial funds. Learning needs to change but never stop.

This study attempts to explain some selected reasons for failure of Islamic Microfinance in Commercial Credit Sri Lanka. To find the solution to the research problem, this study examines about selected reasons for failure Islamic Microfinance. Those reasons are internal, external and Shariah based reasons. Which were faced by Islamic Microfinance in Commercial Credit. It is concluded from this research, most of the professionals in Islamic Microfinance industry do not have clear understanding about these reasons.

Internal Reasons (in side of the office)

According to the research, the first variable identify about internal reasons faced by Islamic Microfinance in Commercial Credit Sri Lanka. We have discussed different reasons, such as poor quality of human resources, inadequacy IT knowledge, lack of education, etc...in the research, most of the professional agreed that Islamic Microfinance industry faced those internal reasons. Most important thing is that they faced those internal reasons for failure their product because of that, very important reason is lack of human capital. Due to the shortage of this human capital created on biggest problem in growth of Islamic Microfinance in Market. The research statistically examines the internal reasons for failure of Islamic Microfinance in Commercial Credit.

External Reasons (out of the office)

In the above research analysis, the external reasons for failure of the practices in Islamic Microfinance in the Commercial Credit in Sri Lanka. Most important fact is to identify that this external reasons are binding on government rules and regulations systems.

Shariah based Reasons (based on Islamic Law)

According to the research, it is concluded that the importance of scholars with Islamic Microfinance Shariah knowledge is outstanding for the development of Islamic and Islamic banking industry. In the research, most of the professionals agreed that Islamic Microfinance industry faces the

shortage of Islamic banking scholars. Because of this one scholar, take part in various poses and various banks.

The users of Islamic banking are worried about lack of scholars in this field because Islamic Microfinance is a fast growing sector and it contains solutions of all financial problems. Due to this shortage of scholars, it is difficult to update the system according to current requirements of the society and this problem will affect the growth of

Islamic Microfinance industry in Commercial Credit in Sri Lanka.

Findings

Analysis testing have been done to find out the relationship pattern between Islamic Microfinance and selected reasons of the practices in Islamic Microfinance industry of Commercial Credit in Sri Lanka.

Correlation analysis expose that all the variables are positively correlated. This means that the relationship

Variables	Hypothesis	Correlation	Results
internal reasons (in side of the office)and Islamic microfinance	H1 – negative relationship	0.318	H1 is rejected
	H ₀ – no negative relationship		H0 is accepted
external Reasons(out of the office)and Islamic microfinance	H2 – negative relationship	0.310	H2 is rejected
	H ₀ – no negative relationship		H0 is accepted
shariah based Reasons(based on Islamic Law)and Islamic microfinance	H3– negative relationship	0.361	H3 is rejected
	H ₀ – no negative relationship		H0 is accepted

between the variables is positive. The results of the correlation analysis and hypothesis testing are as follows:

(Source: field research, 2017)

Results of Correlation Analysis

Correlation of selected Reasons and Islamic Microfinance is shown in the above table. It is positively correlated. The significant value (P-Value) is higher than the tested alpha value (α) 0.01. Hence, the correlation is significant. Therefore, H1, H2, H3 are rejected and H0 hypothesis are accepted. This analysis has been made on overall selected Reasons and Islamic Microfinance. In that analysis also the relationship of the variables are positive.

Recommendations

Based on the analyses the researcher has recommended the following recommendations as suggestions to the consideration of the readers.

Internal Reasons (in side of the office)

Islamic Microfinance staff working in market needs adequate training. Ultimately, their training will draw some positive impacts on Microfinance sector in specific and may benefit the economy of the country at large. Microfinance are not putting due efforts in their business because their client is usually not only poor but also lacking management and other skills.

Islamic Microfinance need dedicated and competent managers supported by well-trained and motivated staff. There is a need to constantly build capacity through internal and external training. The current awareness of Islamic Microfinance needs to evolve from basic bookkeeping, portfolio management and loan officer straining and incentive schemes to internal and external auditing, financial and treasury management, diversification, fraud control and accessing commercial funds. Learning needs to change but never stop.

Islamic banking to meet all IT requirements from Islamic Microfinance technology providers should improve in Sri Lanka. It must adopt according to technology. And also there is considerable scope for Islamic Microfinance providers to develop new products as solution to a variety of financial problems.

External Reasons (out of the office)

Governments must invest in supportive financial infrastructure, which would lower the costs and risks faced by the microfinance industry. In the long-term, microfinance success can bring the benefits to the country, such as taxes and

consumption from those who have graduated to a non-poor status.

Governments also play a proactive role in the regulation, supervision, design and operation of an inclusive financial sector. Barring the differing views, it is generally agreed that the benefits of regulation outweigh its costs. Consumer protection attracts more deposits, giving depositors more comfort with oversight serving as a source for low cost financing. Regulations can promote best practice offering Islamic Microfinance buffers and guidelines for risks. Defined parameters still allow Islamic Microfinance flexibility to innovate and grow into a sustainable business.

When the Islamic Microfinance to be successful, government should provide for policy environment that allows diverse and competitive Islamic Microfinance. A good policy environment supported by the government would allow a range of financial service providers to coexist, compete and offer lower cost but higher quality services to large number of people.

And also Islamic Microfinance will reach its full potential only if it is integrated into countries mainstream of finance. This is necessary to promote greater awareness of products, standardize regulations, and improve transparency and strength outreach mechanism.

When the government provides these facilities to the bank the can achieved their target in the market.

Shariah based Shariah based Reasons (based on Islamic Law)

The Central Bank policy in Muslim countries needs to take place to encourage banks to engage in microfinance .The policies should license new banks to deal exclusively with microfinance and provide regulations on capital requirements, capital adequacy norms and limits on unsecured lending.

Sri Lanka has General Law in all bank nowadays and be haven't particular law in Islamic product and servicers. So here want to a particular law in Islamic transactions like Islamic Microfinance. It will concern based on Islamic Law.

I recognize the Central Bank of Sri Lanka will be start new system and it wants to concerning main be Shariah. They identify this system bankers can get perfect knowledge in Fiqhul Muamalah. It's for against to help growth of Islamic Microfinance Products in Commercial Credit in Sri Lanka.

We can ask while we want private so national Shariah supervisory board/ council at Islamic Banks and its product and servicers. Because of this national Shariah supervisory board/ council can supervise all Islamic Banks and its transactions individually. This can control every registration product and servicers. For an Example Commercial Credit take for Shariah supervisory board/ council for their banking products only.

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