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PROCEEDING

2nd AICIF

2nd ASEAN INTERNATIONAL CONFERENCE ON ISLAMIC FINANCE

"Islamic Finance and Its Role in Economic Development and the Creation of Just and Stable Financial System in Light of Maqosid Syariah"

State Islamic University Sunan Kalijaga
Royal Ambarukmo Hotel

Yogyakarta, 12th - 14th November 2014

2nd ASEAN INTERNATIONAL CONFERENCE ON ISLAMIC FINANCE

Jointly organized by:

Faculty of Islamic Economics and Business-UIN Sunan Kalijaga

Institute of Islamic Banking & Finance-IIU Malaysia

Faculty of Economics-UNISSULA

PREFACE

State Islamic University, as the oldest State Islamic University in Indonesia, has strong commitment in developing Islamic Economics in the world, especially in ASEAN Countries. 2nd ASEAN International Conference on Islamic Finance is the annual conference which has been jointly organized by State Islamic University Sunan Kalijaga Yogyakarta, International Islamic University Malaysia and University Islam Sultan Agung Semarang supported by Islamic Research and Training Institute (IRTI-IDB). The idea of having this international conference sparked from the discussion between II*i*BF and two universities from Indonesia i.e. UNISSULA and UIN Jogjakarta. They have agreed to strengthen their cooperation and the body of knowledge of Islamic banking and finance by jointly organizing an annual international conference which will be held in Malaysia and Indonesia subsequently.The purpose of this conference has been to generate and disseminate ideas to encourage the best practices as a way for enhancing the growth of Islamic economics around for betterment to all mankind.
The topic of the international conference was "*Islamic Finance and Its Role in Economic Development and the Creation of Just and Stable Monetary System in light of Maqosid Syariah*". The background of this topics are to address some significant issues, including a) addressing the issue of Islamic finance in the era of ASEAN Economics community that will be started 2015. b) its implication for Islamic economics development of ASEAN members countries. c) the role of Islamic finance on the creation of Islamic monetary system, both in theoretical and practical basis, supported by the integration of ASEAN Community, to enhance the role of Islamic finance. 4) the challange of Muslim countries for robustness the development of Ummah in ASEAN Community, that mostly are muslem.

Therefore, addressing some above issues, the conference is designed to serve as forum and platform for the academician, practicioners and researchers to share their knowledge, experience and to learn lessons in managing the Islamic finance especially in the market integration. The conference is answering the need of some ASEAN Countries which much focuses on development of Islamic finance in dealing with the issues of ASEAN Economics community, namely 1) ideas in the creation of just and stable Monetary policy that comply with shariah rule and guidlines. 2) the solution for encouraging the development of Islamic banking and finance in the ASEAN Economics community. 3) Current issues of Islamic banking and finance in managing Hajj fund which is uderstood as crucial isssues for Muslim Countries particularly ASEAN Countries such as Indonesia. The conference also highlighted some issues related to shariah compliant financial Instruments that are very important in providing safeguards against the ribawi system in ASEAN Members countries.

To answer all above issues, some panelists, namely Dr. Dadang Muljawan from Bank Indonesia, Mr. Adiwarman Azwar Karim (nominated by IRTI-IDB) will present some issue regarding the role of OIC countries for ASEAN Economics Community. In addition, Prof. Dr. Amin Abdullah will discuss some issue regarding Islamic Economics from philosopics perspective, and Prof Tjiptohadi Sawarjuwono from University Airlangga will discuss accounting issues in Islam. In the plenary session, there are Chief Executive Officers (CEO) from 6 Islamic Banks, namely Bank Mandiri Syariah, Bank Muamalat Indonesia, Bank BNI Syariah, Bank BRI Syariah, Bank Mega Syariah and Bank Permata Syariah who will highlight their experience in managing Islamic banking. Followed by the discussion on issue of Hajj Fund Management and the role of Islamic Finance: Best Practised in Malaysia and Indonesia. Directur General, Hajj and Umroh, Minisitry of Religious Affair, Prof. Dr. H. Abdul Djamil and Dean of Institute of Islamic Banking and Finance, IIUM, Prof. Dr. Syed Musa Al-Habsyi will deliver speech on this issues.

In addition, in this conference there are 70 articles that will be presented in many area of Islamic economics. This proceeding consists the abstracts of that articles, which is hopefully can be a general guideline for the participant of the conference to understand all isssue discussed during the event. Therefore, the conference's participant will generate useful discussion on some pertinent issues and will encourage the finding of new ideas to develop Islamic finance.

Yogyakarta, 05 November 2014

Dr. Misnen Ardiansyah, SE, M.Si.Ak.CA.
Chairman

AGENDA
2ND ASEAN INTERNATIONAL CONFERENCE ON ISLAMIC FINANCE
Royal Ambarukmo Hotel & Convention Hall UIN Sunan Kalijaga
12th-14th November 2014

Day 1: Wednesday, 12 November 2014	
Venue: Convention Hall UIN Sunan Kalijaga Yogyakarta	
OPENING CEREMONY AND INTERNATIONAL SEMINAR	
12.30-12.45	Registration
12.45-13.00	Welcoming Remarks by the Rector of the UIN Sunan Kalijaga: Prof. Dr. Musa Asy'arie
13.00-13.15	Official Launching by Ministry of Religious Affair : Prof. Dr. Nur Syam, M.Si
13.15-13.30	MOU Signing: UIN Sunan Kaliga and BSM, BMI, BRI Syariah, BNI Syariah, Bank Mega Syariah, Bank Permata Syariah
13.30-14.00	KEYNOTE SPEECH: Deputy Commissioner of OJK: Dr. Mulya E. Siregar
14.00-14.45	Special Address : Dr. Muhammad Syafii Antonio
14.45-15.15	Break and Ashar Prayer
INTERNATIONAL SEMINAR	
15.15-17.30	Moderator: Assoc. Prof. Dr. Muhammad Abduh
	1. Adiwarman Azwar Karim (IRTI-Islamic Development Bank) *"Islamic Finance development in OIC Countries and Its Role for the ASEAN Economics Community"*
	2. Prof. Dr. H. Amin Abdullah (UIN Sunan Kalijaga) *"Islamic Economics in the paradigm of Intergration and Interconnection: Developing New Economics Mainstream for the Betterment of the Ummah."*
	3. Prof. Dr. Tjiptohadi Sawarjuwono (UNAIR) *"Islamic Accounting in the Era of ASEAN Economics Community: Opportunity and Challange"*
	4. Dr. Dadang Muljawan (Bank Indonesia) *"Islamic Finance and Monetary Policy: the Case of Indonesia"*
17.30	End of Session
GALA DINNER AND ISLAMIC ART PERFORMANCE: ***Theme: "Sunan Kalijaga and Islamic Propagation in Java Island"***	
20.00-22.00	Islamic Music Performance: Sunan Kalijaga - *Gambus Al-Jamiah* - *Ilir-ilir Sunan Kalijaga and Islamic Propagation*

Day 2: Thursday, 13 November 2014	
Venue : Royal Ambarukmo Hotel	
Plenary Session: CEO Talk: *Panel Discussion on Indonesia Shariah Banking*	
08:00-10.10	Registration
	Moderator : Dr. Anggito Abimanyu
	1. *CEO Bank Syariah Mandiri*
	2. *CEO Bank BRI Syariah*
	3. *CEO Bank BNI Syariah*
	4. *CEO Bank Muammalat Indonesia*
	5. *CEO Bank Mega Syariah*
	6. *CEO Bank Permata Syariah*
10.10-10.15	**Coffee Break**
Plenary Session: ***Hajj Fund Management : Malaysia and Indonesia Experience***	
10.15-11.30	Moderator : M. Kurnia Rahman Abadi
	1. Prof. Dr. Syed Musa Al-Habsyi *(Tabung Haji Malaysia)*
	2. Prof. Dr. H. Abdul Jamil *(Director General of Hajj, Religious Ministry of RI)*
11.30-12.30	**Lunch and Dhuhr Prayer**
2ND ASEAN INTERANATIONAL CONFERENCE ON ISLAMIC FINANCE	
12:30-14.00	SESSION ONE: (Parallel Session in 5 different Venue)
14.00-15.30	SESSION TWO: (Parallel Session in 5 different Venue)
15.30-16.00	**Coffe Break and Ashr Prayer**
16.00-17.30	SESSION THREE: (Parallel Session in 5 different Venue)

Day 3: Friday, 14 November 2014	
Venue : Royal Ambarukmo Hotel	
08.00-09.30	SESSION FOUR: (Parallel Session in 5 different Venue)
09.30-10.00	**Coffee Break**
CLOSING CEREMONY	
10.00-10.30	Speech : FEBI-UIN, IIiBF-IIUM, FE-UNISULA
10.30-10.45	Closing Remarks : Prof. Dr. H. Anis Malik Thoha (Rector of Universitas Islam Semarang)
10.45-11.00	Award Announcement: Dr. Misnen Ardiansyah
11.00	End of Session

Table of Content

Musyarakah Analysis On Islamic Financial Institution In Semarang

ARDIAN ADHIATMA[1]
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Abstract

Musyarakah is Islamic principle that is applied to joint ventures where interest is not charged by the creditor of the loan, instead an agreement is made between the creditor and the buyer as to the share the creditor will get from the profit made from the venture. This also applies to any losses made in the business. The purpose of this study is to what extent the strengths, weaknesses, opportunities and challenges faced by Islamic Financial Institutions in musyarakah cooperation deal with the regulations of Bank Indonesia and jurisprudence of muammalah. The results of analysis show that 5 statements cannot be used because the r-count is smaller than r-table, so it can be said to be ineligible to meet the validity criteria. Whereas, 10 statements can be used because r-count is greater than r-table, so it can be said that it meets the conditions of validity on the statement of musyarakah partnership funding by sharia banks. Furthermore, the analysis of jurisprudence and regulation of bank indonesia in accordance is the contract is set rights and obligations, the bank does not engage in the customer management, funding, human resources understand about islamic banking operations, funding goes to the legitimate business, product offered by BMI is according to *sharia*, and financing to the employees.

Keyword : *Human resources, Management, Musyarakah , Operational System, SWOT Analysis*

1. Introduction

Countries from around the world are giving increasing attention to microfinance institutions (MFIs) in view of their important roles in generating employment and economic growth (Bhasin and Akpalu, 2001; Santos, 2003). MFIs in many countries such as Grameen Bank in Bangladesh, BancoSol in Bolivia, and Bank Rakyat Indonesia (BRI) in Indonesia have shown to be successful in alleviating poverty and improving microenterprise performance. In line with this, there is also an increasing research interests on various aspects of microfinance such as that of Simeyo, Martin, Nyamao, Patrick, and Odondo, 2011; Karlan and Zinman, 2009; Saad and Duasa, 2011; Al-Mamun, Adaikalam, and Mazumder, 2012. Studies focusing on role of microfinance in improving the performance of microenterprise, providing job opportunities, and increasing productivity, however, is still very limited (Hawariyuni, 2014).

Mosley (1997), for example, deliberated on how microfinance has helped to improve the income and employment of borrowers of the BancoSol lending programme. In a related study where the Subsidy Dependence Index (SDI) was used, Mosley and Hulme (1998) showed how BancoSol has had a positive impact on income in Bolivia. In the case of Bangladesh, Khandker, Samad and Khan (1998) demonstrated how MFIs in the country, such as Grameen Bank, Bangladesh Rural Advancement Committee (BRAC) and Rural Development Project (RD 12) had positively affected income, production, and employment of the microfinance participants; while Bhasin et al. (2001) and Vogelgesang (2001) showed that microfinance has helped improve technical efficiency, productivity, and growth of microenterprises in Cape Coast and Bolivia respectively.

As microfinance grows faster in the world including in countries with huge Muslim population such as Indonesia, Malaysia, and Bangladesh, there is a pressing need to explore the viability of offering Islamic microfinance. Goud (2006) argued that the microfinance based on Islamic model provides new image of social enterprise by replacing the interest-based micro-financing with that based on the profit-loss sharing model. The emergence of Islamic microfinance model cause many government and non-government organizations such as Islamic Development Bank (IDB) and Consultative Group to Assist the Poor (CGAP) to transfer financial and technical knowledge and resources related with Islamic microfinance as a new approach to alleviate poverty. It is suggested that in the beginning of the establishment of Islamic microfinance, mostly loan paid in terms of *qard hasan* (loans without fee), and every costs earned will be covered by *sadaqa* and using *zakat* as loan forgiveness for the people who do not have ability for repayment. In terms of implementation, Islamic microfinance can offer similar instruments as the Islamic banks based on the various contracts proposed in Islamic finance such as *mudarabah*, *murabahah*, and *musyarakah* contracts.

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Indonesia is one of the countries with huge Muslim population with a variety of both conventional and Islamic microfinance (Seibel, 2007; Ascarya, 2014). In most cases, microfinance programs related with the Indonesian government program aim to combat poverty and reduce unemployment. Ascarya (2014) highlights that there are varieties of models of microfinance in Indonesia ranging from cooperative model, Grameen model, micro unit of commercial bank model, to rural bank model. He further argues that even though this is the case, these MFIs are still unable to reach the demand of 55.9 million microenterprises (ME) in the country. There are still a lot of microenterprises that could not access loans from both these conventional and Islamic MFIs. Indonesia Delegation for SMEs Ministerial Meeting (2003) in APEC (Asia-Pacific Economic Cooperation) meeting points out several main reasons that cause Small and Medium Enterprises (SMEs) facing obstacles in accessing loan in Indonesia, namely:

i. Products of banks do not match the needs and conditions of SMEs
ii. Banks often overestimate lending risk to SMEs
iii. High credit transaction costs for SMEs
iv. SMEs are not able to fulfil banking technical requirements
v. Limited access of SMEs to financial equity
vi. Inefficiency in monitoring and collection of SMEs credit
vii. Less effective technical assistance provided by the bank itself, therefore service cost for SMEs is high
viii. General bank is not used to financing SMEs.

Additionally, commercial banking in general creates complexity requirements for SMEs in accessing loans, particularly in terms of collateral and administrative conditions. It becomes obstacles for micro, small, and medium enterprises to start or to expand business productivity[2].

One of the most successful conventional microfinance in Indonesia is the Bank Rakyat Indonesia (BRI) unit. Indeed, it is also known as one of the most successful conventional microfinance globally (Seibel, 2007). BRI unit is not only focusing on micro, small and medium enterprises, but also on small vendors or economically active poor. Since October 2008, BRI expanded its banking activities by launching BRI Syariah as well as BRI Syariah Unit Mikro. Besides BRI Unit or BRI microbanking owned by Indonesian government, Indonesia also has variety of conventional and Islamic microfinance institutions. Both of these conventional and Islamic microfinance institutions particularly work for microenterprises with profit or without profit motives (Ascarya, 2014).

The conventional micro banking unit owned by BRI noted as one of the successful microfinance institutions not only in Indonesia but also worldwide. However, BRI syariah micro unit is still left behind compared to others conventional and Islamic microfinance in Indonesia including BRI Microbanking Unit and Bank Syariah Mandiri (BSM) Warung Mikro in terms of sustainable microfinance model such as financial sustainability, unique characteristics, impact, and external shocks sustainability (Ascarya, 2014). Thus, there is a need to propose Islamic microfinance model for BRI Syariah Micro Unit in order to achieve and expand its outreach not only for the economically active poor but also for extremely poor. This study attempts to propose an integrated Islamic microfinance model for BRI Syariah Unit Micro in alleviating poverty and improving the performance of microenterprises.

2. Literature Review

2.1 Microfinance Institutions: Experiences in Several Countries

Microfinance institutions provides financial services in terms of very small loans, insurance, savings, and other financial services for clients with low income and the self-employed, which involve financial and social intermediations (Ledgerwood, 1999; Olu, 2009; ELLE, 2011; Imboden, 2005; Santos, 2003; Karlan and Goldberg, 2007). Financial intermediation means savings and credit while social intermediation means group formation, self-confidence improvement, training in financial literacy, and management practices for the clients. There are nine elements that can be categorised as elements of microfinance (Karlan and Goldberg, 2007). These elements are they exist in small loans, insurance or savings; loans accessed for business productivities; loans granted without collateral; lending based on group; the intention being to reach poor clients; the process of application is uncomplicated; and the interest charged is based on market level.

The objectives of microfinance are to alleviate poverty, to encourage female empowerment and serve poor clients, generate more employment, assist existing enterprises to expand their business productivity, and support the improvement of new businesses (Ledgerwood, 1999). Thus, it could be concluded that microfinance not only plays a vital role in alleviating poverty, but also in the development of microenterprises.

Microfinance emerged in the 1980s, resulting from the scepticism of government policy to deliver credit to poor farmers, and huge losses recorded by credit facilities operating based on subsidies given by donors (Ledgerwood, 1999). Microfinance were mostly subsidised by non-governmental organisations (NGOs) or the government, which moved from the status of subsidised credit to population targeting to serve poor people. MFIs

[2] Indonesia Delegation for APEC SMEs Ministerial Meeting, 2003; b. Timberg, A. Thomas. (1999). Small and Microenterprise Finance in Indonesia: What Do We Know? USAID-fundedPartnership for Economic Growth (PEG) Project. The views expressed in this report are those of the author and not necessarily those of USAID, the U.S. Government or the Government of Indonesia.

would commonly have target clients such as that of Grameen Bank in Bangladesh which focuses on landless people, ACCION encourages the development of group lending based on solidarity for urban vendors in Latin America and Fundación Carvajal, while BRI focuses on the institutional approach based on the principle of market. During the 1980s and 1990s, many non-NGO microfinance and NGO microfinance increased significantly in providing microloans based on individual and group lending, such as PRODEM/BancoSol in Bolivia, K-REP in Kenya, and, finally, ADEMI/Banco ADEMI in the Republic of Dominica; which transformed into formal financial institutions offering savings services and accessing funds from market sources (Ledgwerwood, 1999; Imboden, 2005).

A few MFIs also mobilised public savings after becoming formal financial institutions, such as the Bangladesh Rural Advancement Committee (BRAC) and ACLEDA Bank in Cambodia. Amanah Ikhtiar Malaysia (AIM) is also noted as one of the most successful microfinance institutions in delivering microcredit with the aim of alleviating poverty in rural and urban areas in Malaysia. AIM is a nongovernmental organisation which implemented the Grameen Bank model for rural micro financing (Norma and Duasa, 2011). Nowadays, numerous commercial banks, financial and insurance firms have moved into microfinance as wholesalers. They include multinational institutions such as Citigroup, Santander bank, Deutsche bank, ING direct, ABN Amro Group, and Rabobank. Other institutions serve mostly their respective local and social markets such as the Oikocredit and Triodos banks[3] in the Netherlands, Blue Orchard Finance in Switzerland and SHARE Microfinance Ltd[4] in Hyderabad in India (Imboden, 2005).

Islamic microfinance is a relatively new financial solution compared with the conventional microfinance, which emerges due to the weaknesses of conventional microfinance which charges high interest cost to their customers (Morduch, 2010; Ledgerwood, 2000). Further, Obaidullah (2008) added that the high fixed interest rate charged make the poor to be in trouble and face financial difficulties. Based on these reasons, Islamic microfinance is viewed as a good solution by providing products based on assets approach and not based on debt approach (Riwajanti, 2013). In this regard, Ascarya (2014) defined Islamic microfinance as an Islamic method to alleviate poverty, and the outreach is not only to the poor but also the extreme poor which never targeted by conventional microfinance. Meanwhile, Islamic microfinance defined as an institution offering financial and non-financial services based on shari'ah principles with the purpose to advocate justice for everyone (Riwajanti, 2013). According to Fadlallah (2012) that the Islamic financial approach to poverty alleviation includes charity and development based interventions. It means that the Islamic financial approach is seen as more comprehensive than the conventional one in the social field by providing two types of contributions, namely (i) It does not seek any material gain (zakat, Qard Hassan, etc), and (ii) It is profit seeking and involves market based services. He also defined Islamic microfinance as a type of microfinance that complies with the principles of Sharia by both prohibiting interest (Riba) and achieving welfare while avoiding unfair practices. Ahmad (2002) summarizes the differences between Islamic microfinance and conventional microfinance through Table 1 below.

Table 1. Differences Between Conventional and Islamic Microfinance

Items	Conventional Microfinance	Islamic Microfinance
Liabilities (Source of fund)	External funds, saving of clients	External funds, saving of clients, Islamic charitable sources
Asset (Mode of financing)	Interest based	Islamic financial instrument
Financing the poorest	Poorest are left out	Takes care of the poorest by integrating zakat with microfinance
Funds transfer	Cash given	Goods are transferred
Deduction at Inception of contract	Part of the funds is deducted at inception	No deduction is made at inception
Target group	Women	Family
Objective of Targeting Women	Empowerment of women	Ease of availability
Liability of the loan (Given to women)	Recipient	Recipient and Spouse
Work Incentive of Employees	Monetary	Monetary and religious

[3] Oikocredit and Triodos banks are socially responsible investors who withdraw their self to microfinance due its capability in providing the social and financial returns. Oikocredit is recognised by the United Nations and delivers finance for low income countries to encourage micro and small entrepreneurs. It is one of the world's largest sources of private funding to the microfinance sector. It provides credit and equity to small businesses through MFIs across the developing world, and directly to trade cooperatives, fair trade organisations and small to medium sized enterprises (SMEs). "FMO and Oikocredit Creating Opportunities in Low Income Countries", https://www.fmo.nl/k/news.

[4] SHARE Microfinance Ltd is a regulated non-banking financial company (NBFC) which delivers financial and support services to the marginalised sectors in society, especially for the poor rural and urban women across India. SHARE helps women to become productive microenterprises, and it is indirectly giving contribution for the sustainable communities through its income generating loans and business development services. http: //www.SHARELtd.com

Dealing with Default	Group/ center pressure and threat	Group/center/spouse guarantee, and Islamic ethics
Social Development program	Secular (non Islamic) behavioural, ethical, and social development	Religious (includes behaviour, ethics and social)

Source: Ahmad (2002)

Despite the differences, Islamic microfinance and conventional microfinance also have some similarities which include: (1) instill self-reliant and self-confident among the participants/clients, (2) provide financial services with the objective of achieving the principles of social justice, (3) link financial operations to the activities of real economy, (4) providing financial support, (5) depend on the principles of equality and non-exclusion, (6) give priority to the poor, the underprivileged and the marginalized over other groups, (7) refuse harmful activities, such as gambling, illegal business, and (8) provide strong support to entrepreneurs, especially when no collaterals are required in exchange for loans (Fadlallah, 2012).

In designing a successful Islamic microfinance, three main instruments which is suitable in achieving the objectives of Islamic microfinance are Mudaraba, Murabaha, and Musharaka. While these instruments are available to be implemented in realising the ideals of Islamic microfinance, several studies have shown that Islamic microfinance faced several issues and challenges. A global survey indicated that the outreach of Islamic microfinance is very limited (Karim, Tarazi, and Reille, 2008). In this regard, Islamic microfinance has only served 300,000 clients through 126 Islamic microfinance institutions in 14 countries.

In this regards, Khalid (2011) argued that there are five main reasons which affect Islamic microfinance is still left behind compared to conventional microfinance, particularly in attaining more clients as much as conventional microfinance. These five core reasons are:

1. Focusing only on murabaha product

So far, Islamic microfinance institutions (IMFIs) have minimum Islamic financing product. Mostly they provide only Murabaha product. In the meantime, this murabaha product is criticized as the complexity procedures in terms of additional cost and also about shariah compliance. Based on these reasons, it led IMFIs is still far away from conventional microfinance particularly in terms of limited products offered.

2. IMFIs have few experiences related with Profit and Loss Sharing (PLS) schemes

Khalid (2011) argued that players in Islamic microfinance should innovate new Islamic financing products by uniting all Islamic financial contracts, particularly on PLS products and avoid replicating business model which is originated from conventional microfinance. He also commented that new models built by players in IMFIs should ensure the transparency of the data and maintain cost efficiency.

3. Islamic microfinance has limited outreach in terms of number of clients

In Arab countries, the outreach of conventional microfinance in terms of number of clients is more than Islamic microfinance. Conventional microfinance can reach lots of clients compared to Islamic microfinance.

4. Lack of financing resources compared to conventional microfinance

Khalid (2011) also noted that conventional microfinance has a lot of donations from donors compared to Islamic microfinance. It allows conventional microfinance become more sustainable, and it also convinces commercial banks based on its historical performance that they are creditworthy. Thus, they can easily making use of loan from those banks, distributing these loans to their clients, and doing repayment with interest to the banks. It is not similar with Islamic microfinance. Islamic microfinance is still unable to build up the Islamic model based on profit oriented in order to grasp more client as much as conventional microfinance and it also find challenging to show their potential to the Islamic banks. Islamic banks are reluctance to invest Islamic microfinance portfolio as they look at Islamic microfinance as a risky business. They only give them loan with interest free. It leaves IMFIs are trapped in financing sources.

5. Build up new business model for Islamic microfinance

Practitioners of Islamic microfinance are expected to do innovation by creating new model for Islamic microfinance. It is expected that business model should mix variety of Islamic financing tools and contracts.

In this regard, we also discuss previous studies on the impact of conventional and Islamic microfinance on poverty alleviation and performance of microenterprises in the following section.

2.2 Impact of Conventional and Islamic Microfinance on Poverty Alleviation and Performance of Microenterprise

In assessing the economic impact of microfinance program, the Ford Foundation of Development Finance Affinity Group found the Imp-Act (Improving the Impact of Microfinance on Poverty) in 1988. Imp-Act aims to receive information on poverty alleviation and evaluate results of microfinance investment. The types of impact of microfinance can be divided into two: direct impact and indirect impact (Copestake, Fanning, and Mckay, 2005). The direct impact covers income, assets, food consumption, health, and education. It also views the effect on the individual in terms of skills, knowledge, and self-esteem. Meanwhile, the indirect impact influences others besides the clients, such as family members, competitors, neighbours, and others at the community level.

Many previous studies have empirically examined the impact of microfinance on microenterprises and poverty alleviation. Various methodologies were used to measure the impact of microfinance on microenterprises and poverty alleviation. They are for instance the double difference estimation between participants and non-participants and villages with and without microfinance programmes[5], the Index of Fulfilment of Basic Needs (IFBN)[6], the two staged least squares and Maximum Likelihood (MLE) test[7], probit[8], logit[9], tobit[10], the Subsidy Dependence Index (SDI)[11], the Heckman two step techniques[12], and others.

Other studies examined the impact of microfinance by reviewing various secondary data[13]. They focused on impact assessments of microfinance on poverty alleviation and microenterprises conducted in numerous countries, such as Bolivia, Indonesia, Bangladesh, and others including in a few developed countries. Results of impact assessment are mixed. Several studies show that microfinance has made an impact on the stability of microenterprises and on poverty alleviation. However, some studies indicates that microfinance has no impact on microenterprises in terms of stability and expansion of businesses.

In this respect, some studies conducted in Bolivia indicate that microfinance institutions (MFIs) had a positive significant impact on income, employment, assets, technology, productivity, growth of clients, and sales revenue (Mosley, 1993; Vogelgesang, 2001). However, they also illustrate that lenders of microfinance tend to only focus on poor people whose standards of living are close to the poverty line rather than poor people whose standards of living are below the poverty line as the latter are considered less creditworthy (Navajas, Schreiner, Meyer, Gonzalez, and Rodriguez-Meza, 2000). Furthermore, it also shows that microfinance has a negative impact on poor households who are low risk takers and has low return on investment (Mosley, 2001).

For the case of Indonesia, empirical studies have shown that loan of MFIs have a positive impact on poverty and the performance of microenterprises. This demonstrates that MFIs, such as the BRI Units, *Badan Kredit Kecamatan* or Credit Distric Institution (BKK), *Kredit Usaha Rakyat Kecil* or Credit for Small Business People (KURK), and others have made positive impacts on job creation and household income (Mosley, 1992; Yamauchi, 2005). Studies also illustrate that microfinance has a positive effect on the performance of microenterprises in terms of sales, and the standard of living of female entrepreneurs (Rahmat, Megananda, and Maulana, 2006; Retno and Adwin, 2011). However, other studies indicate that microfinance has no impact on sales, profit or poor households (Morduch, 2002, Retno and Adwin, 2011).

Similarly, studies carried out in Malaysia indicate that microfinance has made positive impact on poverty alleviation and performance of microenterprises. Al-Mamun, Abdul Wahab, and Malarvizhi (2010), for example, demonstrated that microfinancing facilities from Amanah Ikhtiar Malaysia (AIM) have had positive effect on assets of microenterprises owned by the hardcore poor. Saad and Duasa (2011) also demonstrated that the amount of microloans, which are accessed from AIM, has impacted significantly the economic performance of borrowers. Al-Mamum, Adaikalam, and Mazumder (2012) illustrated that the current market value of livestock's agricultural or production equipments, agriculture stock and raw materials, enterprise assets and motor vehicles owned by older clients are higher than new clients.

The empirical studies conducted in Bangladesh show that most of loans of MFIs in Bangladesh, such as Grameen Bank, Bangladesh Rural Advancement Committee (BRAC), and others, have given positive effects on poverty alleviation in terms of household income, livelihood strategy, assets, production, employment, vulnerability, and female empowerment (Montgomery, Bhattacharya, and Hulme, 1993; Khandker, Samad, and Khan, 1998; Zaman, 2000/2001). These studies also demonstrated that older clients then to do better than new clients. Nonetheless, other findings have illustrated that the impact of microfinance on poverty is only positive for around six years, and it tends to even out after six years (Chowdhury, Ghosh, and Wright, 2005).

Only a few studies concentrate on the impact of microfinance on poverty in Sri Lanka. These studies, nonetheless, indicate that microfinance has a positive effect on income, employment, productive and household assets, and technology (Hulme, Montgomery, and Bhattacharya, 1992). On the other hand, other findings also prove that microfinance has a positive impact on the more affluent microenterprises compared to poor microenterprises, and that its impact on poverty depends on the location. In this regard, microenterprises in urban areas generally perform better than those in rural areas (Shaw, 2004). Some studies in India demonstrate that microfinance has a positive influence on generating employment for family members and non-family members; as well as on assets, savings, poverty alleviation, expenditures for food, health, education, and clothes; increase in income, source of income, stabilising normal income, and mitigating financial problems (Basu and Pradeep, 2005; Agricultural Finance Corporation Limited, 2008). Basu et al (2005) and Agricultural Finance Corporation Limited (2008) also illustrate that on average, the household income of clients is more than those of non-clients. Notwithstanding, a few studies indicate that microfinance has a significant impact only on borrowers whose standard of living is above the poverty line, and that the loans accessed were used mainly for consumption instead of production (Mosley, 1994).

5 Coleman (1999, 2006)
6 Navajas, Schreiner, Meyer, Gonzalez, and Rodriguez-Meza (2000)
7 Kaboski and Townsend (2005)
8 Park (2001)
9 Abiola (2011)
10 Coleman (1999, 2006)
11 Hulme and Mosley (1998)
12 Kaboski and Townsend (2005)
13 Shaw (2004); Agricultural Finance Corporation Limited (2008)

The issue of impact of Islamic microfinance on poverty alleviation and performance of microenterprises, however, remained largely unexplored. Riwajanti (2013) stated that the impact of Islamic microfinance can be viewed from two sides, namely social and economic sides. Meanwhile, she also argued that Islamic microfinance also able to eradicate poverty as it is debt based. She further said that it will not make clients into bad situation. Further, Obaidullah (2008) founded that Islamic microfinance is better than conventional microfinance in terms of growth, dropout rate, and operational efficiency compared in Bangladesh. He added as well that IMFIs provide spiritual training with the aim to increase client responsiveness on social right and accountability in enhancing best relationship with others. Rahman and Ahmad (2010) point out that Islamic microfinance has positive economic impact on rural poverty in terms of household income, harvest and cattle production, generating employment, particularly increasing family employment, and they also indicate that types of assets belonging are also increase. Besides that, IMFIs also has social impact as number of clients increase in terms of drinking quality water and latrine for sanitation. Ahmed (2002) shows his findings that the three IMFIs examined in Bangladesh have positive economic impact on production activities in terms of number of goods and services produced, product innovation, and enlarge number of assets and other properties. However, Seibel (2007) contradicted with the previous studies on Islamic microfinance since he finds that Islamic microfinance is deficient of demand and Islamic banking skill. Further, he demonstrated three main reasons behind the failure of the development of Islamic microfinance based on Indonesia study, namely:

- Most commercial banks have ability in gaining Islamic banking knowledge by educating active and youthful people. However, commercial banks in general are deficient in terms of microfinance experience.

- Bank Perkreditan Rakyat Shari'ah (BPRS) or Islamic Rural Banks have been unsuccessful in proving themselves as the good supplier of Islamic microfinance services.

- Cooperatives are considered as absolute hazard for their member-shareholders and depositors due to risk business in terms of loosing money.

Also, there seems to be insufficient information to study the impact of Islamic microfinance in Indonesia. According to Seibel (2007), there has yet to be information related with progress of Islamic microfinance for the last three years, except in Aceh.

It can be concluded from the previous studies that Islamic microfinance need to be taken into account as one of crucial tools in eradicating poverty and improving the performance of microenterprises. However, there are some factors or fields related with the development of Islamic microfinance need to be improved, particularly in terms of Islamic microfinance expertise, source of financing, client outreach, product innovation, new model of Islamic microfinance, and also the need of government supervisory and regulatory.

Conditions that occur in the Bank Muamalat Indonesia	BI Regulation	*Fiqh* rules
1. Agreement is determined by the ratio of bank financing 2. Contract is set up right and obligation 3. The Bank is not involved in the management of business customers 4. It is required collateral for financed customer 5. Entire cost of operation is charged to customers 6. Financing is in accordance with the terms and conditions of contract financing. 7. HR understand the operational prevalence of *Sharia* banking 8. Funding goes to the legitimate (*halal*) business 9. Products offered by BMI is in accordance with *Sharia* 10. Monitoring customer funds (savings and deposits) of the origin of lawful money 11. In funding employees there is; a. *shilatul Ilmi* (being together	1. The financing is done at the beginning of the contract which is determined by the bank 2. Transaction object, terms and conditions on the type of contract and the documentation used in the activities of Islamic banking must be arranged in bank financing. 3. A bank does not participate in the management of a business but it is entitled to supervision and coaching clients 4. Banks can request a guarantee or collateral to anticipate risk when the client is unable to meet obligations as contained in the contract due to negligence or dishonesty 5. Each customer payment instructions (phone banking, internet banking, and credit card or debit card/ATM) is charged directly to the customers' account.	1. There is consensus among all parties as well as the client where the ratio of bank financing could not be determined early in the contract. 2. Contract happens depends on the shape or object types that do contract (contract basis of *sharia* banking is based on *Muamalat* principles) 3. *Sharia financing institution* (LKS) does not participate in the management of the enterprise or project, but right in the construction and supervision. 4. Not required to ask for collateral as warranty. 5. Involving only two parties i.e the seller and buyer 6. Financing contract is in accordance with the type of financing done.

to obtain knowledge) b. *shilatul itiqad* (being together with same vision) c. *Shilatul fi 'li* (cooperation to work) d. *Shilaturrahmi* (working with faith in the work)	6. Contract activities on financing company are based the principles of *sharia*. 7. The operation system of Islamic banks is profit sharing system. 8. Funding is channeled to productive effort. 9. Bank must specify terms and conditions for any products whether collecting or channeling funds of *sharia* banking. 10. *Sharia* banking must enact principles and precautionary principle. 11. Bank must enhance the role of Islamic banking with a focus on financing employees by: a. Collaboration to improve knowledge especially Islamic banking b. Enhancing community cooperation with sufficient and confident knowledge and information. c. Understanding the function and role of the benefit and risk of bank service products to be able to manage wisely in improving the quality of life. d. Cooperation in providing quality products e. Cooperation in the form of professional services to ensure customer loyalty	7. Operating on *sharia* principle that is profit sharing principles. 8. LKS (*Sharia* Financing Institutions) should be more selective and careful in doing lawful business 9. Designing contract for *sharia* banking products 10. Conducting surveillance for productive business without element of *riba* and *gharar* 11. Improving understanding of the science of jurisprudence (*fiqh*) in Islamic banking by: a. Cooperation in understanding banking knowledge, especially knowledge of *fiqh*. b. Being together to improve the understanding of people about *sharia* banking by promoting and preserving the common points and overriding the points of difference. c. Cooperation in the conduct of lawful business. d. Cooperation in improving the welfare of society

Source: Revenue Analysis, (May 2011)

2.3 Islamic Microfinance and Poverty Alleviation

Steidlmeier (1987) viewed that poverty is a troubling paradox since in a moral sense, poverty is an injustice that derives primarily from the failure of collective human responsibility and it is unsettling in a political economic sense because it breeds social instability and diminishes the possibility of improving the general quality of life. There are two broad concepts of poverty: absolute poverty and poverty. Absolute poverty is defined in terms of subsistence and is concerned with the provision of the minimum needed to maintain health and working capacity. Its terms of reference are the maintenance of physical health, the development of human capacities, and survival. The primary focus is meeting the basic human needs.

Furthermore, Amartya Sen (cited in Steidlmeier, 1987) says that the key defining characteristics of poverty is that it is an absolute deprivation of a person’s capacities. This means a failure to develop a person’s ability to do various things which would ordinarily be within his or her reach. It touches physical, intellectual, artistic, communicative and other functional capacities and it is contrary with the approach of poverty which simply focuses upon baskets of commodities, incomes, and resources which will invariably lead to a relative notion of poverty since the necessities of life and the means to meet them are not fixed. Steidlmeier (1987) defined three definitions of relative poverty. They are:

- **Policy definitions of poverty that define a poverty line based on income**
  Policy definitions of poverty represent a pragmatic effort to set social priorities and to implement policies to meet the set of social goals that a society may establish and such policies represent what is desired by those who exercise effective social voice and they usually result in the establishment of poverty lines which serve as guideposts to various social welfare benefits.
- **Relative disparities between income groups**
  Poverty defined in terms of inequalities between income groups is concerned with the relative position of income groups to each other. The composition of society is seen as a strata of income layers, and relative

poverty compares how those on the bottom fare with respect to those who are on the top. In this case, the focus is in social inequalities rather than on basic human needs.

- **Dynamically changing nature of human needs**
  The relative notion of poverty is that human needs are dynamic, changing, and always reconstituting themselves. It follows that what is considered necessary or adequate to meet those needs is also always in flux.

According to Hasan (1997), the concept of a basic needs approach to development emerged as a consequence of the failure of the standard growth approach to check the spread of poverty and destitution in the developing economies. Besides that, to formulate meaningful programs for the purpose, poverty had to be defined in precise terms and the poor had to be identified accordingly. This was attempted through specifying a basket of goods which could be fulfilled at the minimum i.e. the basic needs of food, clothing, shelter, medicare and education, to grant the recipients a living standard which society could accept as tolerable, if not decent. In this case, Hasan (1997) highlighted the absolute and relative versions of poverty within the Basic Need Fulfillment (BNF) program.

The idea of a physical basket of goods and services is considered to be an absolute version of the basic needs concept such as removing malnutrition in children, eradicating disease or educating girls, are concrete specific achievements that meet the basic human needs of the deprived groups, whereas reducing inequality is abstract. Another objection to a relative notion is that it defines poverty only in a such way that it may never be erased, despite any rise in the absolute income levels unless the measure of inequality is itself changed. He further said that since human stomachs do not differ much in size, the possible differences in the calories intake between the rich and the poor has a limit. Here, one may probably stretch the argument to accommodate an 'absolute' view of the requirement but that clearly cannot be the case with the other basic needs. For example, the size and equality of a shelter, and the range and level of the accompanying services relating to water, electricity, sewerage, transportation etc can only be thought of meaningfully in some relative terms. Provision of services concerning health and education their quantum and standard is all the more difficult to conceive on an absolute basis. Poverty by its very nature is a relative concept.

There are some points of view about the poverty and socio-economic development from contemporary Islamic scholars. Chapra (1980 and 1985, as cited in IDB reports) maintains that eradication of poverty, socio-economic justice and equitable distribution of income are considered as the underlying features of an Islamic economic system. Since the establishment of justice is one of the primary goals of Islam, and as such, the Islamic economic system should endeavor to eradicate all forms of inequity, injustice, exploitation, oppression and wrong doing. Furthermore, Siddiqi (1988, as cited in IDB reports) asserts that in an ideal Islamic state, the basic needs of all in the society will be fulfilled. It goes without saying that zakat and waqf are expected to alleviate poverty and to develop the socio-economic system in Muslim countries. The Islamic point of view of poverty is that Islam does not only represent deprivation of goods and services, but also lack richness/poverty in spirit (Mannan, 1988, as cited in IDB reports). According to Rahman (1974, as cited in IDB reports), individuals can improve their spiritual lives by improving their material life. The Qur'an says:

> " It is not righteousness that ye turn your faces to the East
> or the West, but righteous is who believeth in Allah and the
> last day and the angels, and the scripture and the Prophets,
> and giveth his wealth, for love of Him, to kinsfolk and to
> orphans and the needy and the wayfarer and to those who
> ask, and to set slaves free; and observeth proper worship
> and payeth the poor due…Such are they who are sincere.
> Such are the good fearing. [Surah al-Baqarah (2): ayat 177].

In this case, the verse above emphasises that the wealthier people must help the poor and needy. In Islam, the Muslims believe that they live not only in the world but also in the hereafter. They believe that life in the world is a test for them. Allah will give rewards or punishments to them based on what they have done in the world. By doing so, the rich and the poor are required to behave in line with Shari'ah principles (Al-Qur'an and Al-Hadits). There are also some verses from Qur'an which ask the Muslims to make charity.

> " They ask thee (O Muhammad) what they shall spend, say; that
> which ye spend for good (must go) to parents and near kindred
> and orphans and the needy and the wayfarer. And whatever good
> ye do, lo: Allah is aware of it." [Surah al-Baqarah (2): ayat 215].
>
> " Ye shall never attain to goodness till ye give alms of that which
> ye love, and whatever ye give, of a truth, God knoweth.:
> [Surah Ali Imran (3): 86].

The verses above also highlight the important role of charity in an Islamic economy, where the rich people are expected to share their wealth with the needy and poor people. Islam strives to reduce inequality in income distribution and poverty. However, more oftenly than not, poverty and income inequality are unavoidable due to economic crisis, political situation, calamity and others. The Islamic approach to distributional equity is qualitatively different from the customary approach of making income distribution less skewed and more flat-topped.

In this case, Islam aims at preventing the emergence of the malady rather than treating it after its emergence. The elements of its grand scheme flow from its all-pervading concept of amanah. According to Hasan (1986), the concept of Amanah is fundamental to Islam, although other religions may also touch upon it. It seeks to convert the material ambitions of man into the means for attaining spiritual heights i.e. his ultimate goal. Amanah underlines Islam's entire socio-economic philosophy and encompasses its program from the individual to the state. For spending in the way of God, the Qur'an uses the words *infaq, sadaqah and zakah* as perfect synonyms. Redistribution is based squarely on Islam's worldview. God alone is the Creator and the true owner of everything. Individual income and wealth are truly a trust and a test from God, even when it is earned with one's expert knowledge or the "sweat of one's brow.' This is because one's own body, mind and faculties are themselves gifts from God. So are the natural resources, free or scarce, that man works with to produce wealth (as cited in Al-Jarhi, 2005).

Poverty makes people unable to perform individual, social and moral obligation and, therefore man is asked to seek Allah's protection from poverty, scarcity and ignominy. Poverty is declared undesirable as much as Kufr (apostasy) is abhorred (as cited in Sadeq, 1987). There are seven major causes of poverty in present-day Muslim countries (Mannan, 1986). They are: (1) colonial exploitation in the past; (2) colonial legacy (the continuation of unsuitable development policies in the post-independence period); (3) Regional disparities and discrimination; (4) Neglect of human resources; (5) Economic dualism; (6) Financial dualism; (7) Inadequacies of the market system; (8) low labour productivity.

In view of this, Mannan (1986) provides some policy recommendations to eradicate poverty such as restructuring development policies to fulfill the needs of the rural population, providing extension services and necessary credit facilities to the farmers, land reforms and progressive taxation in addition to reactivating the tools of the Islamic redistributive policy. Poverty from the Islamic worldview indicated that the definition of poverty and wealthy is not only focusing on neediness of goods and services but also short of poverty character (Possumah and Ismail, 2011). Islamic jurists argued that it is the duty of Muslim population to make sure the basic needs of the poor (Ascarya, 2014). There are several approaches for poverty eradication in Islam, namely: (1) Zakah; sadaqa jariya and waqf. These are compulsory and voluntary charities respectively; (2) In Islam, Muslim society is persuaded to become self-reliant including self-reliant in terms of monetary; (3) staying away from debt; (4) collaboration and unity among Muslim people; (5) Having family coherency in Muslim society; (6) Islamic microfinance product and contract must be based on shari'ah compliance; and finally (7) Necessities of Islamic norms and best practices of microfinance in encouraging the progress of Islamic microfinance by combining charity and market based.

Obaidullah (2008) stated that Islamic charities in terms of *shadaqa*, *zakat*, and *waqf* are considered crucial tools in eradicating poverty. *Shadaqa* is considered as common charity, while *zakat* is considered as compulsory charity. Finally *waqf* is considered as permanent charity which is applied for long-standing investment. It dedicates for the poor in terms of health, education, employment, and physical resources (Hassan, 2010). Table 1 below points out the comparison among Islamic charity tools for poverty eradication based on Yumna and Clarke (2011).

Table1. Islamic Charity Tools

Characteristics	**Zakat**	**Shadaqa**	**Waqf**
Compulsory/voluntary	Compulsory	Voluntary	Voluntary
Rate	Fixed rate	Any amount	Any amount
Spend	Spent in one year	Spent in one year	Capitalized commonly
Investments	Not invested, need to be released as soon as possible	Not invested, released due to need and mandate	Invest in social and economic sectors
Time for payment	Paid at any time, including ramadan	Paid at any time	Paid at any time
Structure of payment	Paid in cash or stocks	Any types of assets	Any types of assets, including cash, land, coins, and jewellery

Several Islamic banking instruments can be applied in supporting a successful Islamic microfinance (Segrado, 2005; IFAD, 2012), including:

- Murabaha sale is the commonly Islamic banking instruments used to support goods needed as working capital. Here, financial provider will buy specific good which is needed by the customers in the market. Then, they will resell to the customers plus fixed fees charged as services.

- Musharaka and mudaraba. Musharaka refers to participation in equity in business venture. Parties portion profits or losses based on predetermined proportion in terms of assets or working capital. Mudaraba denotes as a financing instrument which can be trusted. One party acts as a finance provider, and others act as an expertise in the carried out project.

• Istisna'a. It denotes as an agreement of transfer between merchant and buyer in terms of selling an asset. The merchant can either fabricate the product themselves or acquire them from the third party. The final buyer can pay up in the lump sum process based on the agreement or in the diverse stages of production process.

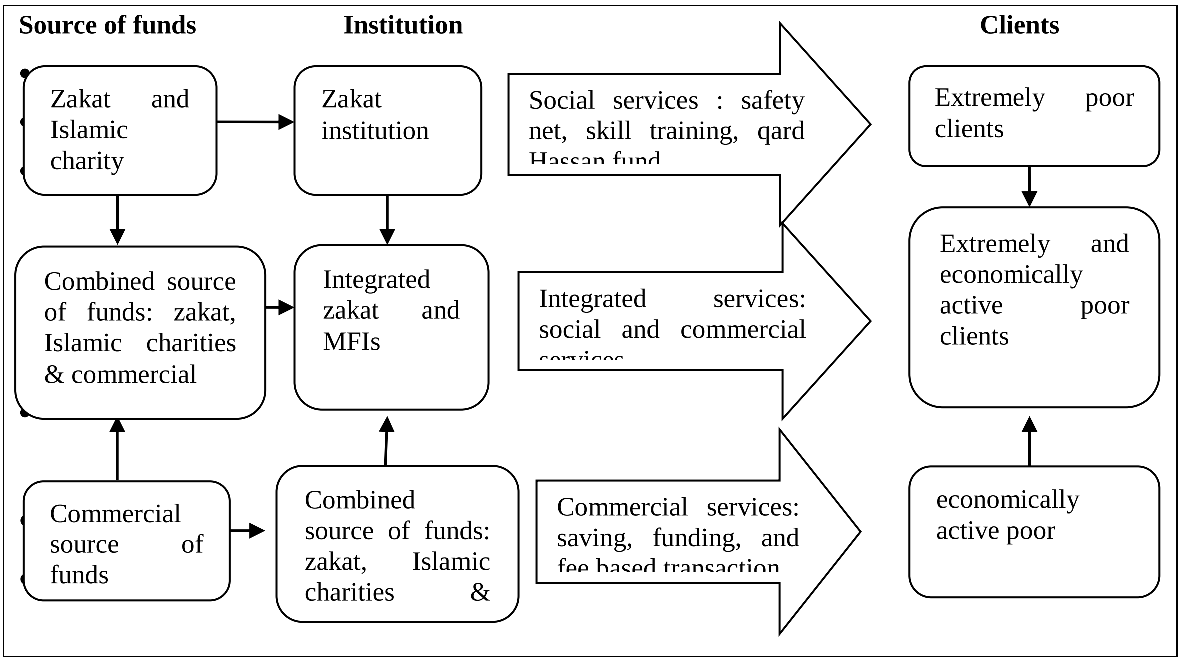
• Qard al Hassan is considered as loan without interest based. The borrower pay the principal amount of loan without interest based charged. This type of financing is dedicated for the poor or the poorest people.

2. A Review of Selected Islamic Microfinance Models

Having reviewed the possible models for Islamic microfinance, this section presents the proposed integrated Islamic microfinance model for BRISyariah Micro for poverty eradication and development of performance of microenterprise. Currently, there are various types of microfinance in the world, including (1) association model; (2) bank guarantee model;(3) community banking model; (4) cooperative model; (5) credit union model; (6) Grameen bank model; (7) Group model; (8) individual model; (9) intermediary model; (10) non-government organization (NGO); (11) peer pressure model; (12) rotating saving and credit association (rosca); (13) small business model; (14) village banking model; (15) self help group model; (16) graduation model; and (17) micro banking unit model (Ascarya, 2014). In the context of Indonesia, there are several microfinance models being successfully executed including (1) Grameen bank model which is replicated by various NGOs, cooperatives, Baitul Maal Wa Tamweels (BMTs), and venture capital; (2) Cooperative model which is duplicated by some cooperatives and BMTs; (3) Community banking model which is imitated by conventional and Islamic rural banks; and (4) Micro Banking Unit (MBU) which is replicated by conventional and Islamic commercial banks.

In this regard, some scholars promoted several Islamic microfinance models with the purpose to build successful microfinance. Yumna and Clarke (2011)suggested an integrated model in building the successful of Islamic microfinance in Indonesia. An integrated model involving two institutions, namely Islamic charities institutions including zakat and others; and Islamic microfinance institutions is presented. The sources of funds are originated from mixture of zakat fund, Islamic charities fund, and commercial source of fund. Further, they stated that Islamic microfinance institution can present both social and commercial services by using mixture of funds from variety of institutions. Commercial services can offer numerous types of financial services including saving, funding, and product fees for economically active poor. Meanwhile, social services can provide skill training to improve capabilities of the extremely poor in executing business activities.

Figure 1. Model 1: Integrated Model



Source: Yumna and Clarke (2011)

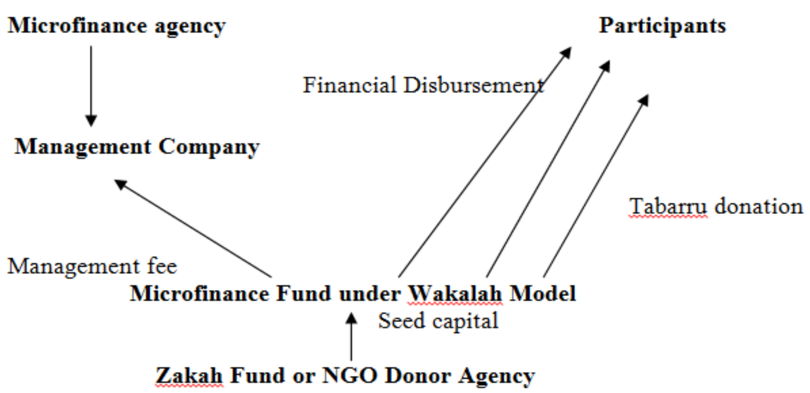
The essence of the above model is that the microfinance model above integrates zakat, others Islamic charities institution, and Islamic microfinance institutions. Several advantages of the model include: (1)

Offering enough services for the extremely poor and economically active poor clients in terms of commercial and services; (2) Building sustainable microfinance as it is not only depend on donor funds, and also can offers numerous financial services in terms of saving, credit and other fees; (3) Improving accountability of those institutions as they have to write report to zakat institution, payers of Islamic charities, shariah compliance, and supervisory board of MFIs; (4) Building sustainable MFIs with at a low level of default rate and decrease the chance to misuse loan as the microcredit is only for skilled people; (5) Decreasing moral hazard or asymmetric problems as these institutions have similar objectives; (6) and finally Islamic microfinance use funds from donors as supporting funds of non-investment activities, and at the same time it become commercial microfinance attaining funds from commercial market.

Overall, this microfinance model is quite establish as they offer commercial and social services for targeting clients, namely extremely poor clients, extremely and economically active poor clients, and economically active poor. Besides that, it is also sustainable as source of funds originated from Islamic charities institutions, including zakat, and also from Islamic microfinance institutions (commercial funds or from donors). However, this models needs further improvement in terms of expanding the outreach in terms of targeting clients, variety of products and services, and the need of f government regulation in building successful Islamic microfinance. In terms of targeting clients, this model not only focuses on clients based on individual basis, but also focuses on clients based on family basis or family empowerment. This family clients means husband and wife which are working together to earn money for their own family, and they are could be extremely poor clients, economically active poor, and; extremely and economically active poor clients. In terms of variety of product and services offered, they also should provide pension fund, Islamic insurance for health and children's education, and finally for pilgrimage. Further, there is a need for government support in terms of Islamic microfinance regulation from central bank of Indonesia and shariah supervisory board for shariah compliance. At long last, authors should clear in giving limited time for skill training offered by these institutions, at least three months from loan given.

Another Islamic microfinance model to be assessed is that introduced by Wilson (2007). This model is based on the wakalah and mudarabah contracts in promoting successful of Islamic microfinance. For wakalah agency model, source of fund is originated from zakah institution and NGO donors. The type of financing distributed to clients is in the form of *Qard Hasan*. In terms of credit application, staffs from this managing company act as an agent and evaluate the credibility of clients in receiving microloans. Fixed fees charged to the staffs as a reward in executing the micro financing activity. This model is similar with the credit union but add some elements in terms of insurance for clients and quality financial administration. Further, he argued that this model is widely used in Islamic insurance or takaful for having *tabarru* (solidarity) fund as revenue accumulation among clients or participants.

Figure 2. Model 2: Wakalah Agency Model

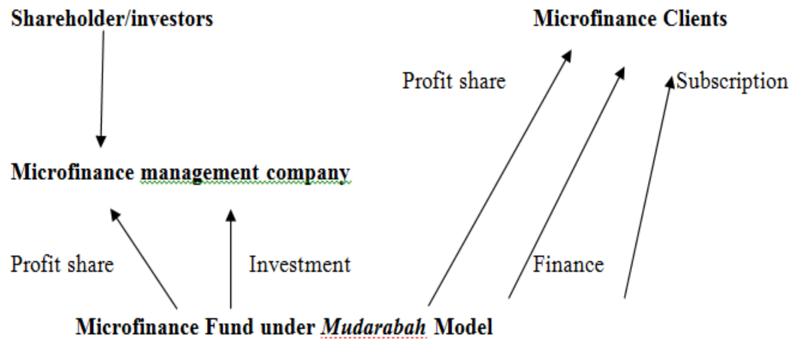


Source: Wilson (2007)

While Model 2 is practical from implementation point of view, there are still some improvements needed for this wakalah agency model. Target-wise, it is still unclear of the specific targeting clients whether the participants or clients are come from extremely poor, economically poor, extremely economically active poor, or female clients. Further, this model does not provide specifically what kind of product and services offered to participants such as business skill training, and saving product. Finally, it brings about moral hazard problem since the repayment competence of clients in not being assessed.

At the same time, Wilson (2007) also introduced other Islamic microfinance model by using mudarabah scheme (Model 3). Based on the profit-loss sharing mode, the MFI will act as a financial provider *(Rabb al Mal)*, placing fund to the clients *(mudharib)*, and obtaining pre-determined ratio of profit share as return. This model looks like joint venture model. Nevertheless, the sum of shared will be fluctuated as profit will be fluctuated. If loss incur, probably bank will not receive fund back and clients do not get profit as business reward.

Figure 3. Model 3: Mudarabah model



Source: Wilson (2007)

Model 3, similar to the previous two models, has several limitations. This model does not offer saving protection as the fluctuated profit could possibly result in no return in the venture. It is also unclear about the targeting clients whether focusing on economically active poor, extremely poor, female or family clients. It is not providing as well services product such as saving product, business skill training, health insurance, and others services. Mudarabah model probably could create moral hazard problem as the capability of clients in making repayment to the MFIs are not addressed.

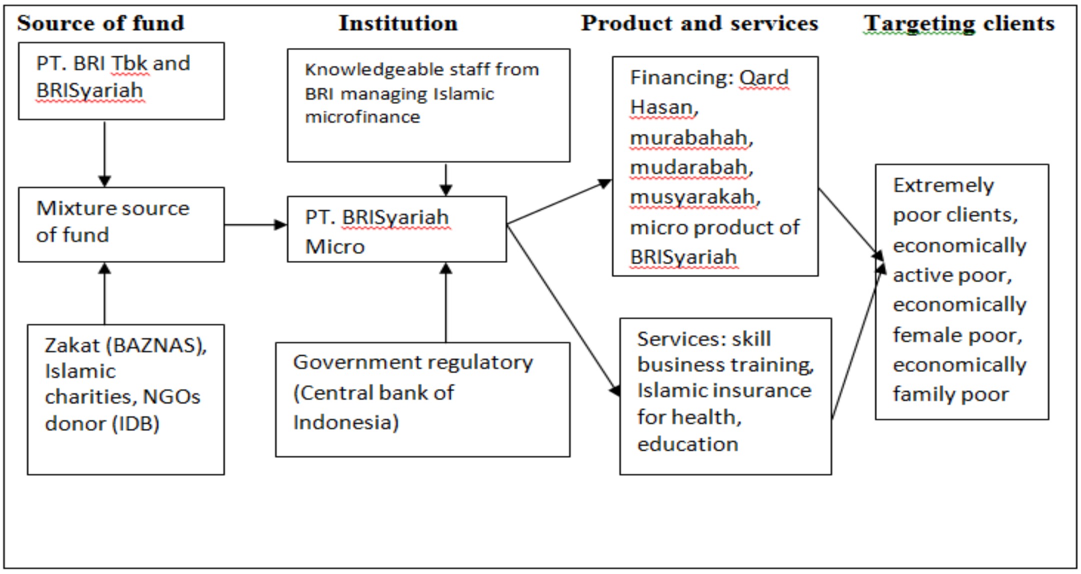
Meanwhile, Ismail and Possumah (2011) promoted zakat as the only source of fund for Islamic microfinance. They promoted Islamic microfinance model by integrating zakat as capital provider with capital user or IMFIs'clients. In this regard, they argued that there are numerous benefits obtained from this model, including: (1) Reaching the poorest of the poor as poor people commonly are excluded from formal financial institution due to inability in doing repayment; (2) Doing assessment of the financial health of the poor as generally poor people use fund not for doing business productivity but for consuming good and services; (3) Aiding poor people doing transformation of unproductive assets become productive assets. Many poor people have land valued highly but they do not have fund to generate income; (4) Fulfilment of basic needs; (5) Zakat also has allegiance and enthusiasm on poverty eradication; (6) Need of technical assistance in connecting with zakah institution; and lastly zakah provides translucent accounting of operation activity.

Further, they also argued zakah model working through three stages, namely: (1) Sources of fund is originated from Qur'an where the wealthy people must give their part for the needy and poor people in reducing gap between rich and poor people; (2) it is basic necessities for all of government and societies to take care fulfilment of basic needs of the needy and poor people, including needs for education and productivity; and finally (3) type of financing zakat is *Qard al Hasan* (benevolent loan) and used for productive purposes. Nonetheless, there are several flaws for their model. The type of target clients as to whether they are extremely poor, economically active poor, extremely and economically active poor, female poor, or family poor should be clearly identified. This model also could not depend heavily on zakah fund as it is charity fund which always have fluctuation or unstable situation causes fluctuation in terms of profit shared (Wilson, 2007). This model needs working together with commercial banking or Islamic banking in delivering Islamic microloan. This model does not provide as well services product in terms of skill business training, saving protection, Islamic insurance for health and education for clients targeting.

3. An Integrated Islamic Microfinance Model for BRISyariah Micro in Alleviating Poverty and Improving Microenterprise Performance

Having reviewed the various models of Islamic microfinance, we propose integrated model for BRISyariah Micro. Robinson (2005) stated that BRI is one of the successful commercial microfinances in the world, particularly through the Micro Banking Unit (MBU). However, BRISyariah, a unit of PT. Bank BRI Tbk established in 2009, is left behind compared Micro Banking Unit (MBU), particularly in terms of outreach. Also, BRISyariah is still far away compared to Bank Syariah Mandiri (BSM) Warung Mikro in terms of Islamic micro banking unit model (Ascarya, 2014). In view of this, following we would like to propose integrated model for BRISyariah in building successful of Islamic microfinance.

Figure 4. Model 4: Proposed Integrated Model of Islamic Microfinance



Source: Authors' suggestion.

Model 4 demonstrates an integrated model for BRISyariah in building successful of BRISyariah Micro. To ensure a financially sustainable model, BRISyariah integrates with Zakat (BAZNAS) institution, Islamic charities institution including waqf and sadaqah, and finally integrate with NGOs (donor) such as Islamic Development Bank (IDB) in providing source of funds for targeting clients. Similarly important as source of fund, PT BRISyariah Micro also requires knowledgeable staff from PT. BRI Tbk and BRISyariah in managing operation activities which is critical in developing a successful micro-finance program. This is in line with Ahmed (2012) who suggested for having Islamic bankers in managing Islamic microfinance activities. Besides that, BRISyariah Micro need supported from Indonesia government through Central Bank of Indonesia (BI) in promoting Islamic microfinance for society in terms of regulatory framework. It leads Indonesia society more realize about the existence of Islamic microfinance, including BRISyariah Micro.

In terms of products, it is suggested that BRISyariah Micro should produce variety of microfinance products that are shariah complaints that are appealing to a wide client-base. In terms of financing product, it is not present only micro product originated from BRISyariah but also need provides Islamic finance product such as *mudarabah*, *murabahah*, *musyakarah*, and *Qard Al Hasan*. In terms of services product, BRISyariah Micro also need to offer skill business training, Islamic insurance for health and education. Due to one of type of targeting clients is extremely poor, there is a need of skill business training in improving capability in doing business activities. Skill business training is also important for other types of clients in expanding their business productivity. Saving protection and Islamic insurance for health and education also regarded as a crucial tool in increasing standard of living of clients.

Further, targeting clients are comprise of extremely poor, economically active poor, economically female poor, and economically family poor. For extremely poor people, BRISyariah Micro need apply hiwalah contract. Hiwalah contract is a "transfer of debt from the transferor (muhil) to the payer (muhalalayh)" (Possumah and Ismail, 2011). It means that poor people as debtors or Muhil can transfer their own debt to the Muhal'Alaihi (payer or Islamic Microfinance). It leads reducing burden of the poor when they begin their business activity. They no need feel worry as funds accepted only for paying the debt. For extremely poor and economically family poor, BRISyariah Micro need provide credit union or sabiyah concept in delivering microloan in reducing default rate.

In summary, the current model proposed in this study is enriching to the existing models in the following aspects: (i)economic and; (ii)social aspects.

4. Conclusion

Islamic microfinance emerged due to highly demand from Muslim countries. Currently, it is also considered as one of crucial tools in eradicating poverty and improving the performance of microenterprises. Some scholars had been attempted to build successful Islamic microfinance model by using Islamic financing instruments such as mudarabah, musyarakah, and murabahah. In this study, we attempt to build integrated Islamic microfinance model by using BRISyariah Micro as case study. It is expected that this integrated Islamic microfinance model can enrich existing models in terms of social and economic aspects.

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