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**DR ATEF ELSHABRAWY**

**EX. CEO-FOUNDER OF FAMILY BANK,  
M&SEM'S ISLAMIC FIANANCE**

***“SHARIA PRINCIPLES,  
OPERATIONAL MECHANISM  
AND MARKETING STRATEGIES  
OF ISLAMIC MICROFINANCE”.***

# ELEMENTS OF OUR INDUSTRY

**Islamic**

**MICRO**

**FINANCE**

- Sharia compliant products
- Sharia advisory board
- Sharia auditor

- Micro-entrepreneurs
- Self-employed
- Low income populations
- Excluded populations

- Business, health, educational loans
- Savings
- Micro-insurances
- Remittances

**Islamic Micro finance**



# ***MICROENTERPRISE ..THE WORLDWIDE MOVE***

# WHAT TO DO?

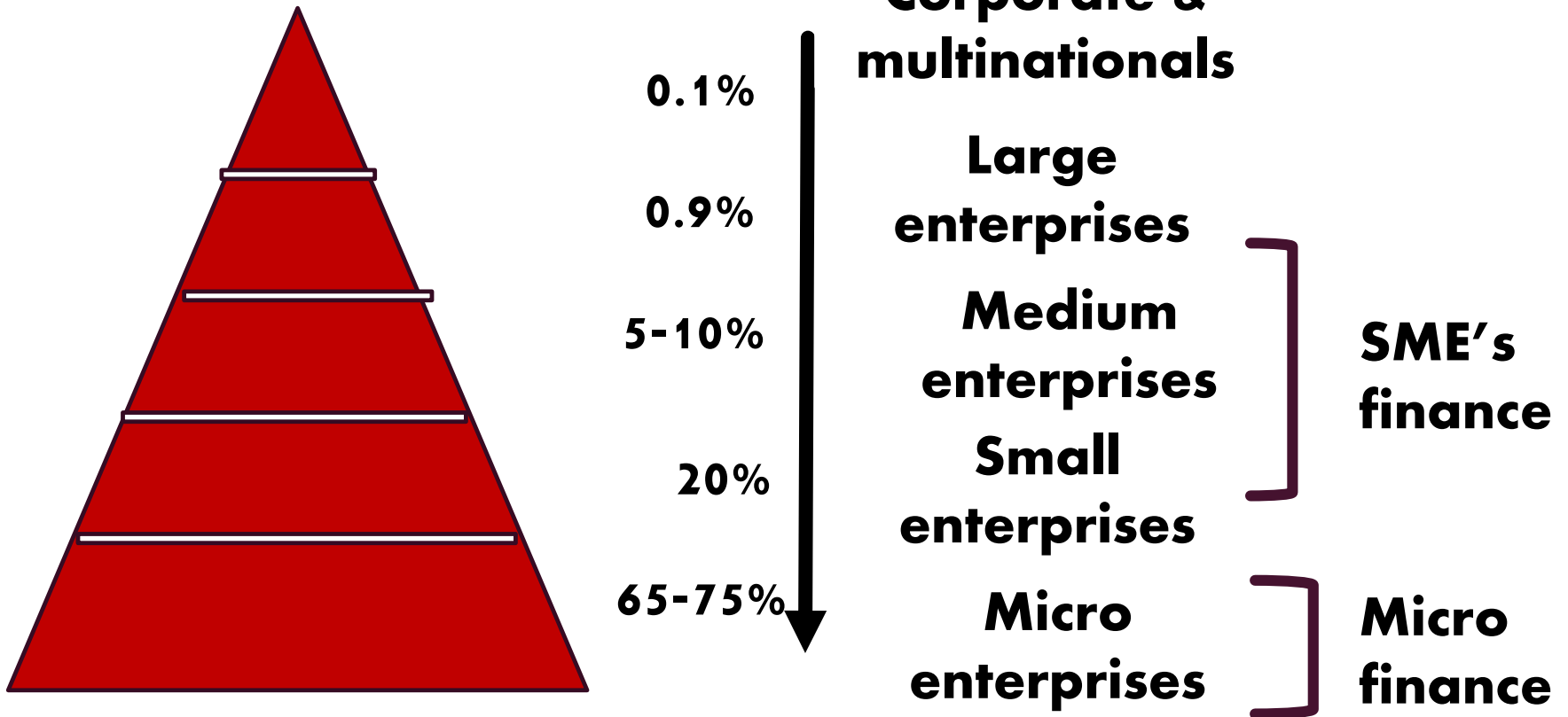
## ■ **More Business:**

- **Micro-entrepreneurs:** 450-500 million Micro & SME worldwide in 2013
- **Low income populations (1.5 billions poor)**
- **Unemployed (200 millions in 2012)**

## ■ **More sophisticated needs:**

- Tarde
- Ijara
- Musharaka
- Istissna

# LANDSCAPE IN EMERGING ECONOMIES





# *SHARIA PRINCIPLES*

# SHARIA PRINCIPLES

1. No interest (*riba*),
2. No hazard, uncertainty (*gharar*),
3. No forbidden assets (*haraam*)
4. Risk-and Loss-sharing
5. Promotions of real economy
6. Disclosure of information

# ISLAMIC ECONOMIC MODEL

1. Emphasising fairness, social justice and the economic prosperity of the whole community
2. Encouraging individuals to pursue economic wellbeing,
3. Distinguish allowed from forbidden activities
4. Strict and explicit prohibition of interest (Riba).
5. Based on a profit-and-loss sharing philosophy.
6. Disclosure of information, contracts play a pivotal role



# CHALLENGES IN SHARIA

## **1. Sharia complaint product ‘arbitrage’**

Due to a diversity of opinions some products & services may be approved as being Sharia- compliant by some Sharia scholars but not by others.

## **2. Sharia compliance throughout the product life cycle**

Sharia compliance is a continuous process that means their products and services should be adequately monitored. It means to reinforce the Internal Sharia Audit process and by developing knowledge and expertise within the firm.

## **3. Availability of Sharia scholars**

The shortage of qualified Sharia scholars in the Islamic finance means it is common for individual scholars to hold positions on the SSBs of a number of Islamic firms, raising concerns over their ability to provide enough rigorous oversight of firms’ products and services.

# CHALLENGES IN SHARIA

## 4. Availability of Sharia internal auditors

The shortage of qualified Sharia scholars in the Islamic finance is also extended to the internal sharia auditor who have an important role to monitor the day-to-day implementation of sharia rules.

## 5. Sharia awareness

- In many countries the level of awareness and understanding of sharia-compliant products is very low.
- The increased competition resulting from a larger number of providers will lead to improve the attractiveness of sharia-compliant finance

# CHALLENGES IN SHARIA

- **6- Trade rules should be respected**
  - Items must
    - tangible in the moment of sale.
    - Owned by the seller.
    - In a physical or constructive ownership.
    - Known to either party.
  - Delivery must be evident & unconditioned
  - The price must be clear & understood
  - Purchase must be on the spot and immediate, with a real value.
  - Finance cannot be used for haram.



# ***ISLAMIC MICROFINANCE OPERATIONAL ISSUES***

# I- INTERNAL ISSUES (CONT)

## Governance and Institutional issues

Functions	Conventional MFI's	Additions In Islamic MFI's
Governance	Board of Directors	Shari'ah Board
Control	Internal Auditor External Auditor	Internal Shariah Review Unit External Shariah Review
Compliance	Regulatory and Financial Compliance	Internal Shariah Compliance Unit

# I- INTERNAL ISSUES

## I. Operations:

1. Understanding Elements of Operation
2. Information Systems and Costs
3. Risk management (market / credit / operational / currency)
4. Mitigating risks & Preventive controls (credit committees)

## 2. Respecting full audit functions :

- Sharia audits
- External audits
- Internal audit function

# I- INTERNAL ISSUES (CONT)

## 4. Human resources

The shortage of experienced professionals is going beyond the limits of the Islamic microfinance sector especially in emerging countries. More education and training are needed. The nature of the work required special calibres.

## 5. Contract and documentation risk

To mitigate the risks of misconduct of finance, contracts have to be prepared and written very carefully to minimise potential disputes and state the governing law.

# 2- EXTERNAL ISSUES

- **1- Regulation and laws imposed on MFIs**
  1. Either to control MFIs, or to increase their efficiency and performance.
  2. Does regulation affect the sustainability of MFIs, or lead to mission drift in MFI's outreach?
  
- **2- lack of supporting services :**
  1. Rarity of specialized intermediation and sharia complaint services (like Tawarruq)
  2. Poor links with credit bureaus & banking information system



# CHALLENGES OF ISLAMIC MICROFINANCE

1. Misuse of finance:
2. High Drop-out rate and Non Graduation from Poverty
3. Transparent Pricing
4. Multiple Lending and Over-Indebtedness
5. Lack of training for the finance officer & clients
6. Lack of financial education of the clients
7. Lack of proper selection of target groups:
8. Need to Keep Clients



# ***MARKETING STRATEGIES***

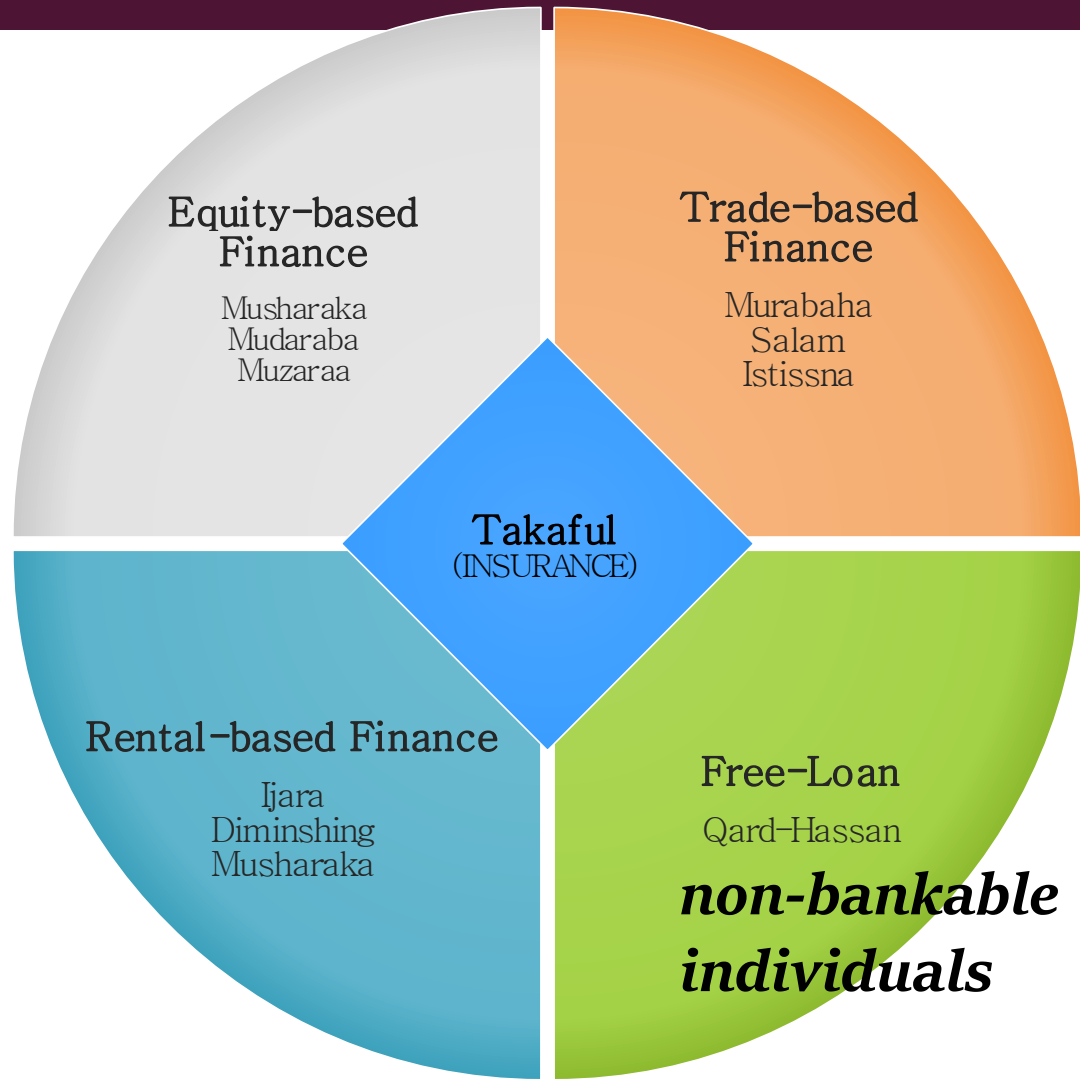
# THE MARKET

Two factors are behind the expansion of Islamic finance throughout the Muslim world, :

1. The countries in which Islamic finance has thrived most effectively are those that already contain established western or conventional banking centres.
2. The success of the Islamic financial institutions within a country is tied to the Islamic compliant finance practices by the financial products, customers, followers and local governments' ability to support.

# THE PRODUCTS

1. **Equity**
2. **Trade**
3. **Rental**
4. **Free loans**



# THE TARGETED BUSINESSES

Sharia states that all kind of businesses are permissible on condition that they do not deal with:

1. Forbidden asset: Alcohol, pork, Prostitution, Pornography, dangerous drugs,
2. Unjust personal & business behaviours :cheating, fraud, and hoarding),
3. Forbidden way to transact :using usury (riba), speculative motive (gharar), and gambling (maysir).

# SELECTION OF APPROPRIATE PRODUCTS

- Experience shows that *murabahah* is preferred over *mudarabah* primarily because it eliminates the need for written records, often unavailable at the micro enterprise level or if available, the client may be unwilling to share them.
- Further, in case of *murabahah* a well-defined contract exists, with pre-defined amounts; a fixed contract creates a less complicated process and a lower implementation cost to the institution.

# PRODUCT DEVELOPMENT CAPABILITY

The key requirements to establish product development capability:

1. A market intelligence process to capture customers' needs;
2. A robust methodology for rapid development & product deployment;
3. A mechanism to engage the sharia board early on to seek approval for the proposed product or service;
4. A quasi-automated monitoring tool that ensure compliance of products with the relevant fatwa, and
5. A management information system to track performance and fine-tune the product or service as needed.

# PRODUCT DEVELOPMENT CAPABILITY

**Based on the statistic, the dominant contracts (70%-90%) offered by Islamic banks in the world as well as in Indonesia are in the forms of trade based contracts especially murabahah and service based contracts such as hawalah, kafalah and wakalah**



# CHALLENGES OF ISLAMIC MICROFINANCE

- **Size.** Many Islamic banks are considerably smaller than their conventional competitors in their domestic markets.
- **Competition.** The number of Islamic banks and financial services firms is growing even as market growth slows down. differentiator.
- **Standardization and regulation.** Standardization and regulation present ongoing challenges for Islamic banks.
- **Cost structure.** Despite strong growth, most Islamic banks have not been consistently profitable, particularly since the global financial crisis.



**Transformation of business practices around the 3 r's**

**WORLD ISLAMIC BANKING COMPETITIVENESS REPORT 2013 -  
E&Y.**

# MARKETING CHALLENGES

The future sources of differentiation for Islamic microfinance will likely revolve around three areas:

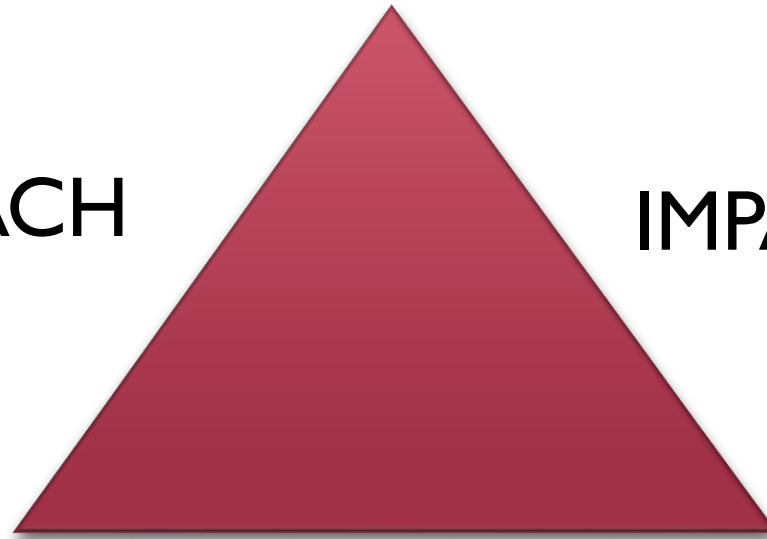
1. Product development and innovation
2. Distribution & coverage
3. Operational excellence

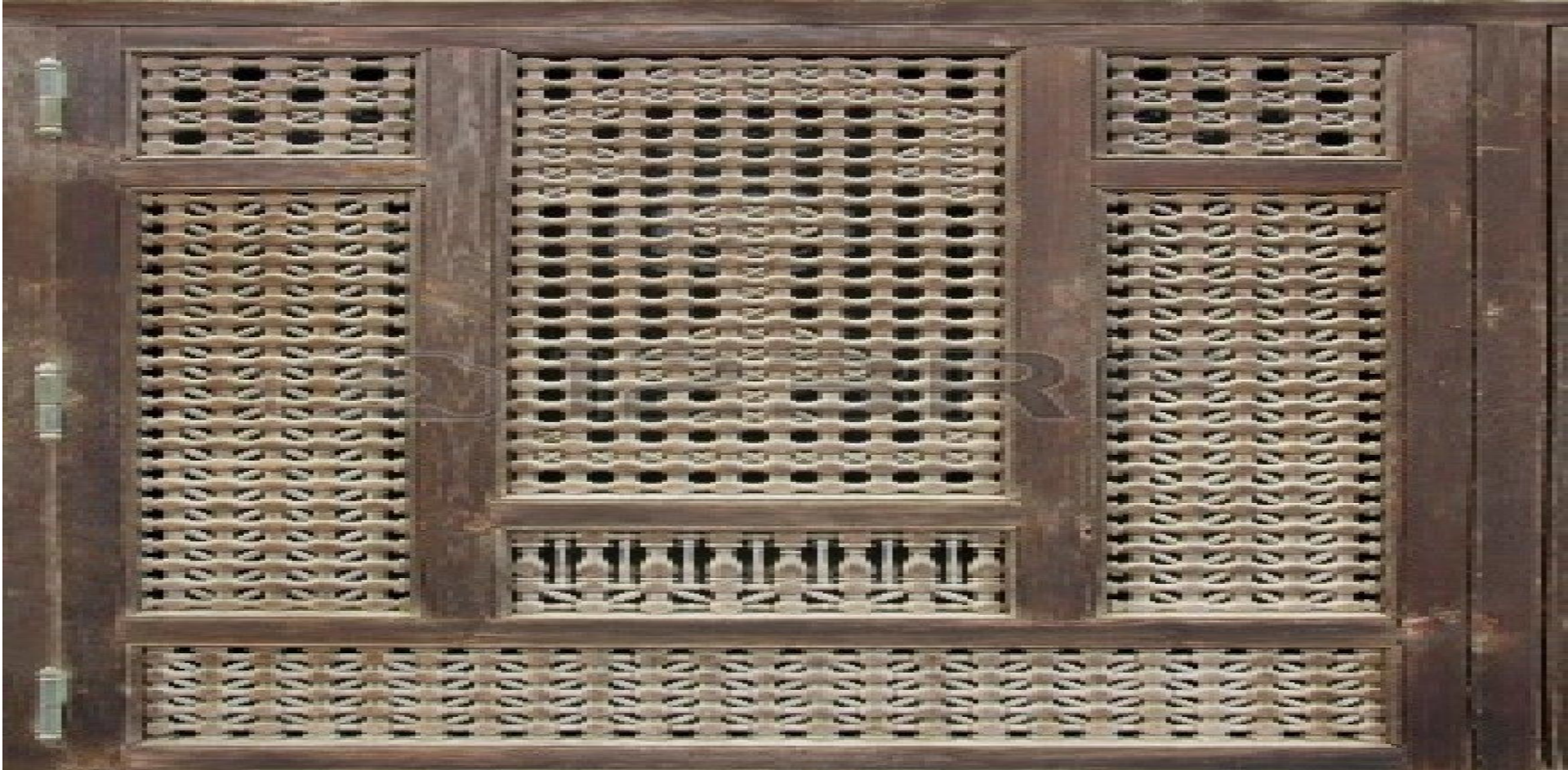
# FUTURE OF ISLAMIC MICROFINANCE

OUTREACH

IMPACT

SUSTAINABILITY





**Thank you for your  
attention**