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Small Entrepreneurs finance by Islamic banks: An empirical review (An institutional-network approach)

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ABSTRACT

Purpose: The purpose of this paper is to delineate Islamic banking finance and its impact on Small Entrepreneurs (SEs) in a particular country context.

Design/methodology/approach: An Institutional-Network theoretical frame of references is used to study this particular phenomenon. The research methodology applied in the study is of a *qualitative nature*. A multiple explanatory case study is adopted as a research strategy in order to focus on contemporary phenomenon within the real life context of SEs.

Findings: Among others, the finding includes the extent to which interest free financing by Islamic banks contributes in developing network relationships between the lenders and the borrowers and other related economic actors in a society. The finding also reveals the impact of societal sector institutions in accelerating the Islamic financing activities in a particular socio-cultural environment.

Research limitations/implications: The study mainly relates the Islamic banking finance to SEs by different branches of the





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Islami Bank Bangladesh Limited (IBBL) in the greater Chittagong. The bank is one of the leading sharia¹ – based bank in the money market of Bangladesh.

Practical implications: Since lending organisations under the Islamic Financing System (IFS) renders services to their clientele without interest, the lender-borrowers relationships is featured by a close supervision of their borrowed funds. While lending funds to its customers; the Islamic banks invest funds under different investment modes of funding like the Mudaraba, Musharaka, Murabaha and Bai-Muajjal.

Originality/value: The study is based on the socio-cultural context of Bangladesh where the paper premised on its theoretical perspective and ‘Institutional-Network Approach’ in the field of Islamic finance towards SEs.

Keywords: Small Entrepreneurs; SEs; Islami bank Bangladesh Limited; IBBL; Bangladesh; institutions; networks; societal sector; Islamic Financing Systems; IFSs; Musharaka; Bai-Muajjal.

INTRODUCTION

Small Entrepreneurs (SEs) in less developed countries, as in developing nations play significant roles in the elimination of the unemployment problem, which remains a serious obstruction to a nation’s economic growth. Even though, the large-scale industries are involved in mass-production and invest large amounts of capital, these industries are mostly urban based. Consequently, large-scale industries fail to play a significant role in solving unemployment problems related to the rural people. In this regard, Anderson (1982), Anderson and Khambata (1982) and Macuja (1981), in their studies observed that, this is exactly where SEs succeed better. A number of researchers (Ashe and Cosselett, 1989; Little et al., 1987) in their studies have highlighted the issue as to how and to what extent this sector of economy contributes towards the development of a nation’s economy. The main contribution of this sector of economy is that it creates job facilities for many unemployed rural people in the country. Skilled workers can thus contribute towards the development of the national growth. In spite of its contribution towards economic growth SEs in almost all developing nations lacks institutional credit. Now-a-days, many interest-free banks in different countries have started investing funds towards SEs sector. These banks

¹Sharia means the law and moral code, which is to be followed by individuals. It is based on instructions provided by the Koran. <http://www.oxforddictionaries.com/definition/english/sharia>





usually apply various interest-free modes of finance while giving loans to the SEs.

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SEs AND LENDING ORGANISATIONS IN BANGLADESH: A LITERATURE REVIEW

The People's Republic of Bangladesh, a nation on the map of the world, attained its independence in 1971. It is one of the world's most densely populated countries with more than 160 million people 43% of whom live below the national poverty line of US \$1.25 per day (2007–2011 study)². Since its independence, the nation has increased its real per capita income by more than 130%. The country has also reduced its poverty level by more than half by striving to achieve most of its Millennium Development Goals. In spite of such progress, Bangladesh remains a low-income country with substantial poverty, inequality and deprivation. More than one third of the population live below the poverty line, and a significant proportion live in extreme poverty. The poverty rate is highest in rural areas, at 36%, compared to 28% in urban centers. Many people are unemployed, have an inadequate diet and suffer from periods of food shortage. Most of Bangladesh's laborers are engaged in informal, low-income jobs with limited productivity. Although agriculture now accounts for less than 20% of GDP, the farm sector still employs about 44% of the labour force. However, with urbanisation, the amount of farmland is shrinking, and most rural households have very little, if any, cultivable land. Rice is the dominant crop, but production increases are limited by farmers' lack of access to critical production tools such as high-yielding rice seeds. Like other similar nations, SEs play a predominant role in enhancing the economic growth of Bangladesh.³

In his studies Alam (2009, 2003), observed that the great hindrance of rural-based SEs in Bangladesh is the lack of institutional credit facilities. Although there are many formal financing institutions like government and privately owned commercial banks, cooperative banks, etc. they normally do not lend funds to SEs. Due to the shortage of capital, SEs are compelled to borrow funds from local moneylenders who charge a high rate of interest on their borrowed fund. As observed by Alam (2003, p.3), SEs in rural Bangladesh are heavily dependent on rural money lenders who consume the lion's share of their profit.

It is observed in the IPPF (2010) report that, The People's Republic of Bangladesh provides a large consumer market for potential industries. Even though, it holds one of the lowest wage structures

²<http://www.compassion.com/about/where/bangladesh.htm>.

³<http://www.ruralpovertyportal.org/country/home/tags/bangladesh>.





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in the world, the comparative advantage of Bangladesh lies primarily in its agro-processing industries. However, besides from agriculture, the rural-based SE sector in Bangladesh is a potentially lucrative field of investment. In spite of its major contributions towards economic development, the rural-based SEs in Bangladesh suffer from a lack in working capital, institutional credit facilities and poor management. Besides from traditional banking, 'Shariah' based financing also plays a predominant role in solving financial problems related to this sector of the economy in Bangladesh SEs also receive small loans from different credit institutions. In this regard, Molla et al. (1988) observed that this sort of credit is usually delivered in a scheme of joint-liability use (peer pressure) to enforce loan repayment. Different studies on a 'Shariah Based Financing', which also known as Islamic banking finance (Ahmad, 1994; Ahsan, 1989; Alam, 2002, 2003; Chapra, 1985, 1970; Gathura, 1996; Heffernan, 1999; Kazarian, 1991; Ken, 1994; Khan, 1986; Nassief, 1989; Parker, 1993; Roula, 1995), reveals that the system essentially involves sharing of risk between the owner of capital and the entrepreneurs, as well as sharing the result of the collective efforts. Thus, it differs from an interest-based system in which the risk is mainly borne by the entrepreneur or by the user of capital. In another way, Islamic banking may be termed as a participatory banking.

In Bangladesh, Yunus (1982, 1993) promoted a microcredit program under the name 'Grameen Bank (2009)', as an effective tool for enhancing the income of the poor through the creation of self-employment in various informal activities. However, Nabi (1996) in his study noted that the interest charged on such loans is very high. However, it has nonetheless provided the poor with access to the necessary credit to establish economic enterprises based on their existing skills, in an effort to earn a higher income.

In Bangladesh, one of the leading 'shariah' based financing institution is Islami Bank Bangladesh Limited (IBBL). The IBBL is a Joint Venture Public Limited Company engaged in commercial banking business based on Islamic Shari'ah with 63.09% foreign shareholding, having the largest branch network among the private sector banks in Bangladesh. It was established on 13 March 1983 as the first Islamic Bank in South East Asia.⁴

As it is reported in the IBBL Annual Report (2014)

"The fundamental aim of the bank is to establish and maintain modern banking techniques, to ensure soundness and development of the financial system based on Islamic Principles and to become a strong and efficient organization with highly

⁴<http://www.islamibankbd.com/abtIBBL/abtIBBLAtaGlance.php>.





motivated professionals, working for the benefit of people, based on accountability, transparency and integrity to ensure stability of the financial systems” (p.6).

Among other modes of financing, this specialised bank gives credit to SEs through different ‘Musharaka’ and ‘Bai-Muajjal’ modes of Islamic financing. In comparison to credit by conventional banks and other loan giving agencies like NGOs and village money lenders, the ‘Shariah’ based Islamic banking credit is considered to be a challenging and contributing financing tool which facilitates greatly in creating job opportunities for the rural poor and eliminating rural poverty in the country. The bank also invests its fund on the basis of ‘Shariah’ principles in microfinance and SMEs. In this respect the IBBL Annual Report (2014) observes as

“.... IBBL started its microfinance operation through Rural Development Scheme (RDS) since 1995. So far, out of 294 branches, 221 carry out RDS activities in the country. The Bank launched another micro-finance scheme for urban poor in 2012 in the name of ‘Urban Poor Development Scheme (UPDS) on pilot basis under its 23 urban branches. These two schemes enable IBBL to achieve financial inclusion of poor women of rural & urban areas. To expedite SME investment, the Bank has opened 30 SME & Agriculture Branches especially in the rural areas of the country”. (Annual Report IBBL, p.122).

The study of interest free financing by Islamic Bank Bangladesh Limited (IBBL) in this article is based on the socio-cultural context of Bangladesh and its relationship with the Islamic banking system. As mentioned above, one of the acute problems of rural-based SEs in Bangladesh is the shortage of capital, the interest-free finance initiated by different Islami banks through their different ‘shariah’ based modes of financing are found effective not only in solving financing problems of rural based SEs but also in enhancing the network relationships between lenders and borrowers.

Based on the above discussion, the main research questions addressed in the study are:

1. How and to what extent does IBBL succeeded in financing SEs in Bangladesh?
2. How do interest free modes of financing of IBBL contribute in promoting lender-borrower network relationships?
3. To what extent do societal sector institutions like the country culture, religion, family/clan, political systems, legal systems and government influence interest free financing activities by IBBL?

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THE INSTITUTIONAL-NETWORK THEORETICAL APPROACH

The concept of an 'Institutional-Network' theoretical frame of reference (Alam, 2002) is used to study this particular phenomenon. The Institutional-Network theoretical concept is developed based on Whitley's (1992a) 'Business System' (BS) institutional approach and Jansson's (2002) 'Network Institutional Model'. The BSs Approach is an institutional approach used by Whitley (1992b) to study business organisations, *inter alia* in Asian countries. The author, in his comparative study of BSs in East Asian countries, for example, Chinese Family Business (CFB) units in Taiwan and Hong Kong, Japanese Kaisha and Korean Chaebol, attempted to determine how firms are constituted as relatively distinct economic actors in different market societies as well as how they organise economic activities in the form of dominant hierarchy-market configurations. The comparative analysis of BSs, as Whitley (1992b) observed, is the study of these configurations. In this regard, the author argued that, a key task concerning the comparative study of BSs is to analyse how distinctive patterns of economic organisations become established and effective in different societies and how they change in relation to their institutional context. In his study, Whitley (1992a) also observed that these patterns concern the nature of economic activities that are coordinated through managerial hierarchies. The author further investigated how these hierarchies organise their cooperative and competitive relations through markets.

Since one of the objectives of the study relates to finding how and to what extent 'shariah' based interest free financing by IBBL contributes in promoting SEs and by enhancing the lender-borrower network relationships, apart from Whitley's (1992a,b) institutional concept, the network concepts of Jansson's (2002) 'Networks Institutions' model, is also used in the theoretical framework. The author integrated network with institutions in order to view the network from an institutional perspective. According to Jansson (2002), institutions also concern different types of habitual or recognised behaviour, such as habits, rules and procedures, implying that institutions are characterised by a rule-like or governing nature, an ability to facilitate and constrain inter-human and inter-social relations, and by predictive behaviour. Veblen (1919, p.239) in this regard observed that, institutions themselves are comprised of settled habits of thought common to the generality of men. In order to study the relationships between Multi-National Corporations (MNCs) and their commercial partners, the author used a network approach and developed a theory to analyse such linkages. Furthermore, to study the network relationships between and within organisations belonging to the two focused institutions, for example, Small Entrepreneurs Systems (SES) and Major Financing Systems (MFS) and their relationships with other economic actors in the organisational fields,





the concept of Jansson's (2002) Trans-organisational Network theory is also used in the theory. Since the networks are observed from different angles, the study also used the network concepts defined by different authors for example, Rasmussen (1988), Kuklinski and Knoke, (1988), Anderson and Carlos (1976), Easton and Araujo (1991), Elg and Johansson (1992), Easton (1992), Håkansson (1993), Aldrich and Whetten (1981) and Emerson and Cook (1984).

The Institutional-Network theoretical model, which is developed based on the above discussion, is shown below in Figure 1.

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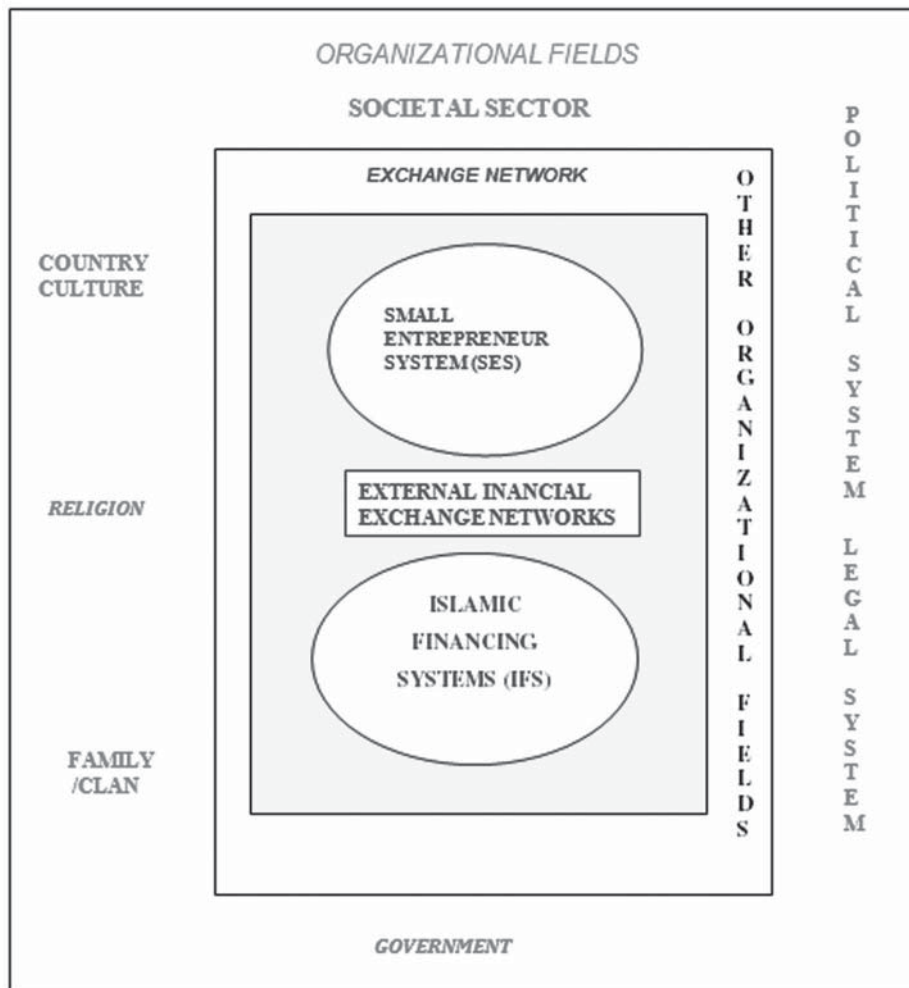


Figure 1 Institutional-network framework

Source: Adopted Alam (2002).

The theoretical model shown in the above figure consists of two major fields: the financial market and other organisational fields. The focus of the present study is concentrated on interest free financing by Islamic banks to SEs under the SES and their relationships with the IBBL under Islamic Financing System (IFS). Thus, these issues are viewed under the





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organisational fields in the first rectangle. The SE System and the IFS are viewed as two different institutions in the organisational fields. The second box or major field consists of different actors in the other organisation fields. These actors are for example, customers, intermediaries (local leaders, seniors), competitors and suppliers. They are related to the product and service exchange networks, influencing the major organisational field of the financial market in the first rectangle. The external financial exchange network between the SES and the IFS shown in the framework is meant for studying the exchange network relationships between and within different organisational units belonging to SES and the IFSs in the financing market of the major organisational fields.

Since the exchange activities and network relations of different actors in the organisation fields are influenced by societal sector institutions like country culture, religion, family/clan, political system, legal system and government, these institutions are placed in the outer rectangle. These macro institutions surround the major institutions in the first and the second organisational fields. They are shown in the outer rectangle in order to study their influences on the exchange functions with regards to interest free financing to different small-enterprises under the SE Systems by financing organisation IBBL under the IFS and also other institutions within and between these organisational fields.

RESEARCH METHODOLOGY

The research methodology applied in the study is of a qualitative nature (Jick, 1979; Merriam, 1998; Patton, 1985; Sherman and Webb, 1988). A qualitative type of research is characterised by collection of data directly from respondents in the field. This is because the entire research program is based on facts acquired from the material world, that is, the practical field of study. While interviewing respondents at various branches of the IBBL under review, based on Merriam's (1998) 'Interview Structure Continuum', I used highly structured, semi structured and unstructured interviews to suit the respective situation that arose. A multiple explanatory case study (Yin, 1994) method was adopted as a research strategy in order to focus on contemporary phenomenon within the real life context of Islamic bank and their relationships with SEs.

As a part of the data collection processes, interviews were conducted with senior officials of six IBBL branches in greater Chittagong areas. The interview period was about three months. In total, 12 senior IBBL personnel, who are responsible for giving loans to the rural-based SEs, were interviewed. A list of different branches interviewed is shown in the following Table 1.





Table 1 List of branches interviewed

<i>S.No.</i>	<i>Branch Name</i>
1	Anderkila Branch
2	Borodargarhat Ahaddar Hat Branch
3	Muradpur Branch
4	Patiya Branch
5	Shitakunda Branch
6	Station Road Branch

Source: Direct interviews conducted to all IBBL branches.

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Regarding the collection of data from the field, a direct interview method was used. While conducting interviews the following steps were taken.

- Both formal and informal means of interview methods were used.
- Structured and semi structured questionnaires were prepared and the same were used while interviewing respondents. The questionnaire was used depending on the circumstances and the qualifications of the respondents.
- Audio tape recorders were used to record respondents' answers. Where the use of a tape recorder was difficult, the answers were recorded in a notebook.
- Questionnaires were prepared taking different issues into considerations such as, lending procedures, bank-customer relationships and also other issues related to small-finance to rural-based SEs.
- Subsequent to the interview, the recorded tape was replayed and the data was recorded in a spreadsheet. A similar procedure was applied to the data that was recorded in the notebook.
- Based on the interviews and respondents information, data was arranged and analysed from a theoretical perspective.

The interviews were conducted during March to July 2015.

THE IBBL FINANCE TO SEs: AN EMPIRICAL REVIEW

This section represents a summary of information gathered through interviews from senior IBBL personnel in different rural branches in the greater Chittagong area. It includes a description of different issues like, different modes of financing used by the bank while lending funds to its clientele, bank-clientele network relationships, formalities that borrowers must observe to be eligible for obtaining loans, mode of the repayment of loans, securities required to obtain loans and other related aspects regarding financing to rural-based SEs.





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The nature of rural-based SEs under review

SEs who form the clientele of the IBBL to whom the bank gives loans through a 'Mushaka' and Bai-Muajjal mode of financing, as reported by the respondents of the bank, are of an average age of 25 to 35 years. Among the customers, more than 50% and more than 30% finished their college level education and undergraduate education, respectively. Almost all customers have prior business experience. The amount of loan given to customers ranges from BDT 50,000 to BDT 200,000⁵ depending on the type and the nature of the business. The nature of the business consists of local and foreign trade, dairy farm, agro-based business, etc.

The Musharaka and the Bai-Muajjal mode of financing used by IBBL

While conducting interview with the senior officials of different branches of the IBBL, it is known that the bank normally give loans to SEs mainly under the Musharaka and the Bai-Muajjal modes of financing. A brief description of these two financing modes is given below.

Regarding 'Musharaka' financing mode, Alam (2000), observed that the Islami Bank Bangladesh Limited and its clientele contribute capital jointly. The bank also takes parts in the management and thus contribute managerial expertise and other services to their clienteles as agreed upon. Like a joint venture under the 'Musharaka' mode of financing profits and losses are shared by the lender and the borrower according to the agreed shares of profits and losses. The most striking feature of this mode of financing is that the IBBL works as a provider of capital and not as provider of loan at a certain rate of interest as a traditional banks do. The Bai-Muajjal mode of investment on the other hand is similar to a Murabaha (cost plus profit) mode of financing. Under this mode of financing the bank agrees to purchase goods on behalf of the customer and re-sell the same to them at an agreed profit. The customer later repays the entire amount in certain installments. The loans in such cases are provided in kind rather than cash.

Financing procedures followed under 'The Musharaka' and 'The Bai-Muajjal Mode of Islamic Banking Finance'

It is known from the respondents' information that, once a project proposal of a particular client is considered favourably, one of the officer responsible for sanctioning loans, visit customer's business site and makes a feasibility study on the prospect of business and its environmental conditions. The officer gathers various information from





customer and once he is satisfied prepares a report and give it to the Musharaka manager for the approval of the loan. The manager then prepares necessary 'Musharaka' documents like contracts and the terms and conditions, etc. Once the contract is signed by the both parties the bank requests the customer to open profit and loss sharing account with the bank. As mentioned in the above the section, under this mode of financing the customer is responsible for administrative and management activities of the entire business even though bank assist the customer with their expertise. It is the customer who is required to maintain accounts of all expenses and incomes and periodically submits an income statement to the bank. The profit thus determined is shared between the bank and the client as an agreed proportion. The respondents under review also informed that a customer is required to give collateral securities for the money received from the bank based on the partnership agreement. Islamic bank also asks the clientele to supply two letter of recommendation from the local influential persons or from the old and reputed customers of the bank. It is to be noted here that the bank gives funds for the business in kind and not in cash.

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The clienteles under the Bai-Muajjal mode of financing, on the hand needs to form a group before applying for a loan. The group leader normally works on behalf of the group members and makes initial contact with the bank. Like Musharaka mode of financing every individual member of belonging to different groups under Bai-Muajjal mode of financing needs to open an account with the bank. All members are required to deposit a certain amount of money (not less than 5% of the loans applied for) in their account within a specific period of about ten weeks. Once the saving period is over each member in the group submit their project proposals and apply for loan. The bank considers each proposal carefully before giving loans. Once loans are sanctioned the entire loan amount is deposited in the respective account of the customers. Like 'Musharaka' financing in 'Bai-Muajjal' mode of finance the give loans in kind rather than cash. Under this process, the bank buys goods and materials on behalf of the customer and add profit to it and again re-sell the same to the clients. The entire amount is realised in certain installments where the first installments began once the customer begin to sell their products in the market. Like the 'Musharaka' mode of financing as a security measure, a customer is required to produce their land property title documents as collateral and also require two letters of recommendation either from the reputed and old customers of the bank or influential local leaders in the locality.

Branch Wise SEs Clienteles

It is known from the respondents in different branches reported that the bank normally gives loans to SEs belonging to both trading and manufacturing concerns. The following Table 2 shows a branch-wise SEs'

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clienteles to whom the IBBL gives loan under both Bai-Muajjal and Musharaka mode of financing.

Table 2 Branch wise SEs clienteles

<i>Branch Name</i>	<i>Total</i>	<i>Trading</i>	<i>Manufacturing</i>
Anderkila Branch	20	13	7
Borodargarhat Ahaddar Hat Branch	25	15	10
Muradpur Branch	30	20	10
Patiya Branch	15	10	5
Shitakunda Branch	17	10	7
Station Road Branch	10	5	5
Total	117	73	44

Source: Direct interviews with IBB staff in different branches.

It is apparent from the above table that in the Muradpur branch there are more customers than the other branches. It was reported by the respondents in this branch that the bank is situated in commercially busy areas and many of the customers who are a little far are engaged in small scale manufacturing concerns. It is also known from the above information that about 62% of the SEs borrowed funds for trading and 38% for manufacturing businesses. Almost all clienteles of the trading concerns deals with the bank under the 'Musharaka' mode of financing while manufacturing concerns borrow funds under the 'Bai-Muajjal' mode of financing.

The respondents reported that, once the loan is sanctioned and the clientele start their business, the bank staff pays regular visit to them. Even though the supervision and control of the business is in the hands of customers, from time to time, the bank gives advice and look after the business progress. The senior officials from every branch retain a close contact with their clientele and also help in maintaining proper business records. In case the customers face any difficult situations, the bank experts in the related field advise and guide them accordingly. Apart from that, the bank assists indirectly in promoting their business by informing about their products to the other potential customers of the bank.

It is also known from the respondents of different IBBL branches under review that, customers are free to visit banks at any time and may discuss different business issues directly with the bank manager and other responsible officials. In every branch, there is a liaison officer who organises the interview between bank officials responsible in both 'Musharaka' and 'Bai-Muajjal' financing and the customers. Clienteles





are not required to pre-book an appointment to see the officers or the branch manager. They are always welcome by the bank officials to discuss any business related issues during office hours.

It is reported by bank officials that the country culture and religion do not have any direct impact while lending funds under the two important modes of IBBL financing. Many branches have non-Muslim customers who follow the Islamic banking principles while borrow funds from the IBBL. However, it is observed by bank officials that many customers sometimes become victims of their cultural influence and bound to spend a lion's share of their income in different functions and cultural occasions like marriage, religious ceremonies, etc. Due to that, many clients face problems in procuring working capital for their day to day business. In order to educate their customers, the bank officials often arrange meetings and gather to discuss different issues regarding spending from the perspective of Shari'ah. The bank's officials voluntarily assist their customers in using their borrowed funds in proper and profitable ways. It is reported by all respondents that the bank lends funds to everyone regardless cast, creed and religion.

As informed by the respondents interviewed, the IBBL did not experience any difficulties from the viewpoint of legal and political system of the country. They have every option to lend funds in a business that complies with Shari'ah laws and regulations. However, the bank officials reported that they have many complaints from their customers about the local legal system in the country. Many of their clients who intend to initiate a new business become victims of a group of local political leaders who demand a high amount as donations. If they do not fulfill their demand, it becomes very challenging and almost impossible for them to start a business. In such cases, rural-based SEs seldom get any help from local law regulating authority.

The respondents in different IBBL branches under review informed that, the bank closely monitor the borrowed funds of their clienteles and be sure that the borrowed funds are utilised for the same purpose it is borrowed for. In order to be sure on this specific issue, the bank releases borrowed fund once customers buy goods for resale or buy raw materials for production.

It is also noted from the interview that almost all branches of the IBBL under review follow the same system while giving loans to rural-based SEs. However, direct contact with customers and supervision of the borrowed funds sometimes differ from branch to branch. Since the credit is given in kind rather than cash, the supervision of loans is done according to the plan and program developed by each individual branch of the IBBL.

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ANALYSIS OF EMPIRICAL FINDINGS

The following section includes a brief analysis of the empirical findings.

Development of personal network through direct contact with customers

It is known from the study that, due to the nature of the business under the 'Musharaka' and Bai-Muajjal modes of financing, the bank personnel mostly contacts their customers directly. Apart from physical visits, some of the clientele in rural areas are also contacted through telephone and faxes. The means of customers' contact by the bank is shown on a percentage basis by the following Table 3.

Direct contact with customers develop personal networks

It is apparent from the above table that all branches of the IBBL under review does not use middlemen in establishing contact with their customers. Rather the bank contacts their customers directly. This in turn develops personal network between the lenders and the borrowers. It also enhance a close supervision of the borrowed funds of the SEs.

Table 3 Means of contact with customers in percenta

IBBL Branches Branch Name	Means of Communication in Percentage				
	Personal Contact	Through agents or middleman	Through agents or middleman	Through Mail	Through other media
Anderkila Branch	75 to 100%	Nil	10 to 20%	20 to 30%	01 to 10%
Borodargarhat Ahaddar Hat Branch	80 to 100%	Nil	10 to 30%	20 to 30%	01 to 10%
Muradpur Branch	90 to 100%	Nil	01 to 10%	10 to 20%	01 to 10%
Patiya Branch	75 to 100%	Nil	5 to 10%	20 to 30%	01 to 10%
Shitakunda Branch	85 to 100%	Nil	10 to 15%	20 to 30%	01 to 10%
Station Road Branch	70 to 100%	Nil	01 to 10%	10 to 20%	01 to 10%

Source: Direct interviews with IBB staff in different branches.

Bank-customer relationships: a unique means of promoting clientele business

It is revealed from the study that almost all branches allow their customers to visit senior officials or managers in charge of the department directly when needed. Formalities to meet senior officials are very simple and customers of all levels can avail the opportunity to discuss their business issue and gain advice regarding their business. Since the senior officials of the bank in charge of both 'Musharaka' and Bai-Muajjal mode of financing pay a regular visit to their customers in





rural as well as in urban areas and consult various issues regarding business outside the bank premises, this promotes the customers' business and encourages them to conduct their business successfully. Based on the respondents' view extent of bank customer relationships is demonstrated by the following Table 4.

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Table 4 The extent of the bank-customer relationships

IBBL Branches Branch Name	Extent of the Bank's Relationship with its Customers				
	Access to bank's senior staffs	Visit of bank staffs to customers	Guide to customers	Assistance in marketing products	Discuss issues other than business affairs
Anderkila Branch	1	3	1	3	4
Borodargarhat Ahaddar Hat Branch	1	2	4	4	3
Muradpur Branch	1	2	1	4	3
Patiya Branch	1	1	1	4	2
Shitakunda Branch	1	3	2	3	1
Station Road Branch	1	1	1	3	2

Note: 1. Always; 2. Very often; 3. Often; 4. Sometimes; 5. Not at all.

It is known from the above table that almost all branches maintain a strong relationship with their customers and also assist them by providing necessary advice and marketing of their products.

Delay in the repayment of loans by a customer

The study also reveals that, once a customer fails to repay the loan in due time, or does not comply with the contract, the bank takes legal actions. Before taking a legal action, in case of default, the bank contacts customers personally. Apart from that, the following steps are also taken by the bank.

- inform through correspondences;
- influence through people related to the customers;
- influence through local leaders;
- influence through guarantors and
- contact through organisations with whom the customer is related.

There is a provision with the IBBL that, if any borrower becomes bankrupt or fail to repay the loan or comply with the terms and conditions, due to unavoidable circumstances, such as, natural disaster or political unrest, etc., the customer is given a further loan to develop his business position. Customers in some cases are given partial relief from their loans when it is discovered that they are truly unable to repay the entire amount of their loan.





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Influences of religion and country cultural on the IBBL financing

As it was reported by respondents in different branches under review, the IBBL is based on Islamic principles, which aims at making the maximum utilisation of public savings and proper distribution of wealth. Sometimes societal sector institutions like religion, customs, country culture, norms and the habits of people hinder the realisation of these objectives. In rural Bangladesh, rural-based SEs are not highly educated. The religious beliefs and faith of the people are influenced by the culture of the society. Although, every religion teaches all well to mankind, when it mingles with culture, it loses its strength and fails to bring any changes to human life. Islamic bank experienced many problems that arose from cultural influence, habits and norms of people. Although family ties play a great role in promoting business or production activities, such relations are also influenced by certain cultural factors. It is observed that the IBBL find it difficult to educate people and to make them understand that expenditure in an unproductive way does not bring any benefit to the individual or to society.

The role of the government

Almost all senior personnel of the IBBL interviewed in different branches under review opine that the 'Shariah' based financing system is encouraged by the Government of Bangladesh. The government often issue circulars regarding the credit policy, which the bank finds very helpful when dealing with their clientele. Most rules and regulations of the government are helpful for the bank, especially to administer their loan activities. In some cases, the government discriminate their policy which Islamic banks find unfavorable for them.

Encourage and promote institutional credit facilities

The results revealed from the empirical study shows that the 'Shariah' based financing by Islamic banks under discussion, provides institutional credit facility by which it saves needy SEs from the paws of the local money lenders in the country. It is also noted from the study that most conventional banks in the country are mostly urban based and profit oriented. They invest a very negligible amount of their deposits towards SE sector. Moreover, it is noted that the lending procedures used by the traditional banks are lengthy and complicated. Due to that, rural-based SEs fail to obtain loans on time. This in turn gives opportunities to informal money lenders to promote their money lending business among SEs at a higher rate of interest. Thus, it may be concluded from the study that the Bai-Muajjal and the 'Musharaka' modes of IBBL financing to SEs enhances the institutional credit facilities. This is a positive contribution towards the economic enhancement and alleviation of poverty in a poverty-stricken nation like Bangladesh.





Simple lending procedures of Islamic bank encourages SEs

It is found from the study that under the 'Musharaka' and 'Bai-Muajjal' modes of financing, the bank officials assist their customers to be organised and provide them with guidance as to how to open and operate an account with the bank. This in turn encourages SEs. The simple loan giving procedure under these modes not only educates customers about interest free loans but also organises their activities by close supervisions so that they may contribute to society. Apart from that, the entire lending activities of the banks are organised in such a way that borrowers are benefited from the beginning to the final stage of their projects. In order to make the system simple the bank uses simple forms to fill up. Thus, it may be concluded that, the loan giving procedures from the beginning to the end makes the activities of the rural-based SEs more easy, understandable and organised.

The bank ensure borrowers' credit worthiness

The result of the present study also reveals that in order to be sure about a borrower's credit worthiness, besides collateral securities the bank ask its clienteles for two letters of recommendation either from local influential leaders or from the reputed customers of the bank in the locality. These letters must contain that they will act as a guarantor for the customers in any case they fail to comply with the bank's terms and conditions. By adopting this procedure, the bank ultimately ensures that borrowers are really worthy of giving credit.

Middlemen interferences and exploitation are eliminated

It is also revealed from the study that, due to the bank officials direct contact middlemen interference is drastically reduced. Many senior bank officials of different branches under review, reported that while they used to work with the traditional bank they experienced the middlemen interference in procuring loans. Rural-based SEs used to entrust middlemen to work on their behalf and in turn they used to grab a significance portion of borrowed fund as their fee. The study reveals that Islamic banks do not allow any middlemen to work on behalf of their customers. Rather, the bank officers enthusiastically assist their customers in observing all official formalities to obtain a loan. Thus, the IBBL saves their clienteles from the interference of middlemen. Hence, SEs can save a lion's share of their borrowed funds and are able to use the same for productive purposes.

In kind loans make sure of proper utilisation of borrowed funds

It is found from the study that the 'in kind' financing system under the 'Musharaka' and 'Bai-Muajjal' financing modes ensures that the





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clienteles use their borrowed funds for the same purpose they borrowed for. It is already mentioned in the discussion that the Islami banking finance under 'Musharaka' and 'Bai-Muajjal' modes of financing the bank does not extend credit to their clients in kind rather than cash. By doing so, the bank receives surety of the customers' use of funds for the purpose they borrowed for. The application of the 'in-kind' (e.g. loan in material or goods rather than cash) lending principle shows that the loan recovery rate is higher in almost all of the IBBL branches under review.

Creates mutual obligations between the lender and the borrower

Alam (2009, 2003, 2002), in his studies argued that, the 'Musharaka' and 'Bai-Muajjal' modes of Islamic banking fiancé develop a mutual obligation between the bank and the clientele. The present study reveals that, SEs are bound to fulfill their obligation by discharging the responsibility of managing the business. This system makes the customers conscious of making proper use of their borrowed funds. Furthermore, this system develops initiative among rural-based SEs to work hard and to be sincere in dealing with bank loans. It also encourages them to save more as they need to repay the loans after a certain period of time.

CONCLUSION

In conclusion, to answer the two research questions addressed at the beginning, it may be said that the IBBL is yet to succeed in promoting the 'Musharaka' and 'Bai-Muajjal' modes of financing among SEs in both the trading and the manufacturing sectors in Bangladesh. It is reported by the senior officials interviewed that, the customers who borrow funds under 'Musharaka' mode of financing must be more morally conscious, since the interest free financing under this investing mode ISE based on faith and honesty of the customer. As mentioned earlier under the 'Musharaka' mode of financing the bank and the clientele own the business jointly. The Islami bank invest fund jointly with customers in good faith. If customers do not disclose all facts of the business honestly it is hard for the bank to determine exact profits or losses. It is also reported by respondents that many of their customers belonging to the 'Musharaka' mode of financing fail to disclose all business transactions properly. Since the responsibility of the entire business rests upon the SEs, the bank usually depends on its financial records and expects a financial statement that records all facts properly in order to determine the true profit or loss of the business. It is reported that in many cases, the bank experienced dishonesty among customers while determining profit or losses of the business. This discourages bank officials and as





a result, the bank loses their interest in investing funds under 'Musharaka' mode of mode of financing. With respect to the 'Bai-Muajjal' mode of financing it is reported by the informants under review that, this specific mode of funding is working well with the SEs, especially in the manufacturing sector. Since under this financing mode bank buys goods and materials for customers and then resell them at a profit and thus determine the total amount of loans to be repaid, every customer is aware of how much he or she must pay in each instalment. Thus, it is easy for the bank to follow up the customers' activities and realise the loans in time. It is also concluded from the study that, the entire lending procedure develops a good network relationships between the bank and its clienteles. This ultimately enhances close supervisions of the borrowers' activities and the borrowed funds. It is also revealed from the study that, societal sector institutions have an indirect impact on this specific financing mode. As mentioned in the earlier sections, the country culture combined with religious faith compels many rural-based SEs to spend their borrowed funds on unproductive activities. This ultimately causes a great loss in their business. It is also concluded from the study that SEs in many cases become victims of local political leaders. In order to start a new venture, they need to give donations to leaders of different political groups. If they do not comply with the illegitimate demands, they cannot commence their business. Those who are responsible for regulating law in the society do not help these needy rural-based SEs when they suffer. Thus, it is concluded that even though, the government encourages the system, the law-regulating bodies at the rural areas stand as a barrier in promoting interest-free modes of financing. Rather, the law maintaining officials take parts in favor of the influential local leaders. This ultimately results in losses for many SEs and the bank eventually faces problems in realising their objective of earning profit. Thus, it may be concluded that, although, these modes of financing has many positive aspects and advantages, SEs need to be more honest with their attitude and the law regulating body needs to come forward in assisting them. By doing so, both Bai-Muahjjal and Musharaka modes of financing could work magnificently in promoting SEs in society, particularly, by creating job opportunities for many unemployed youth in Bangladesh.

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