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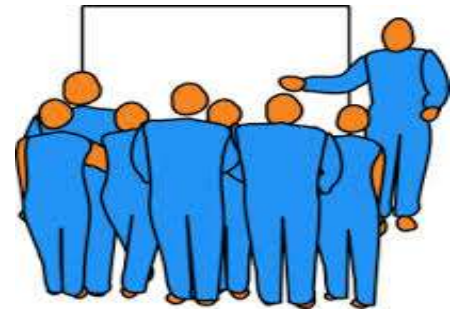
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Potential Role of Waqf in Enhancing the Economic Performance of Muslim SMEs



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PRESENTATION OVERVIEW



○ **SMEs**

- Economic Importance of SMEs for Socio-Economic Development
- Challenges of Islamic Finance Techniques in Promoting SMEs

POSSIBLE SOLUTION... WAQF

○ **WAQF**

- Historical Importance of Waqf in Islamic Societies
- Obstacles Confronting Waqf
- Beneficiaries of Waqf

○ **WAQF AS A PROBLEM-SOLVING TOOL FOR SMEs**

○ **CONCLUSION**



ECONOMIC IMPORTANCE OF SMEs FOR SOCIO-ECONOMIC DEVELOPMENT



- Powerful engine for growth in both developed and developing countries (**Durrani & Boocock, 2006**)
- Play an important role in promoting economic growth, creating job opportunities and further encourage social and development activities (**Cravoy et al, 2009**)
- One important goal of an SME is the maximisation of social benefits as opposed to profit maximisation (**Ahmad, 1993**)
- Development of SMEs as the achievement of greater socioeconomic goals, which includes poverty alleviation (**Nixon & Cook, 2005**)



CHALLENGES OF ISLAMIC FINANCE TECHNIQUES IN PROMOTING SMEs



SMEs

- Despite their robust role in socio-economic development and creating job opportunities, SMEs continue to face increasing challenges around the world especially with the recent financial crisis, Eurozone debt dilemma and Arab Spring crisis
- In the least developing OIC member countries, access to finance is one of the most intimidating challenges facing SMEs


ISLAMIC FINANCE

- Muslim individuals are becoming more religious conscious and fully aware that Islam encompasses all aspects of life including financial dealings, thus they are now more eager to adopt Shari'ah compliant financing
- The negative outcome of the recent financial crisis has underlined the importance of Islamic finance as an alternative financing technique for promoting economic activities particularly in SMEs

BUT...



CHALLENGES OF ISLAMIC FINANCE TECHNIQUES IN PROMOTING SMEs

- Islamic banks may not be able to reciprocate adequately to meet the growing SMEs demand
 - Majority of Islamic banking products have been developed to cater for certain types of financing where SMEs are not part of the equation
 - Islamic banks are also attuned to firstly evaluate the repayment capacity of the borrowers through necessary procedures.
 - This act might cause a hindrance to the SMEs to attain financing as SMEs lack the proper financing infrastructure in keeping track of their performance mainly due to the high costs associated with the preparation and maintenance of those type of accounting records.
 - SMEs keep track of their performance through simple accounting records only
 - Challenging for Islamic banks to offer Islamic banking products that cater for the needs of SMEs & SMEs will also express reluctance due to obstacles highlighted above
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EXAMPLES



- In Pakistan, for example, 51% of SMEs find it very hard to attain finance from Bank.
- In Malaysia, only 55.6% of the total SMEs surveyed attained financing from banks
- In Malaysia, even though there are abundant subsidized loan schemes under Majlis Amanah Rakyat (MARA) and Malaysian Industrial Development Finance Berhad (MIDF), only few that actually benefitted from it.

SOLUTION...



WAQF

- It is vital to look for alternative approaches which can allow Muslim SMEs to adopt the Shari'ah-compliant financing without shying away from Islamic finance institutions due to their cumbersome financing procedures
- One such promising alternative is the concept of the **ISLAMIC WAQF**
- But why Waqf?



HISTORICAL IMPORTANCE OF WAQF IN ISLAMIC SOCIETIES



- The glorious *waqf* administration continued from the birth of Islam till the times of the Ottoman Khelafa– from the 15th century till the 19th century
- During the period of Ottoman Khelafa, it was estimated that three-quarters of all the arable land belonged to *waqf*
- *Waqf* also had a strong presence in other Muslim and Muslim minority countries
- Through the *waqf* lands, a major economic problem such as employment was addressed by creating job opportunities



HISTORICAL IMPORTANCE OF WAQF IN ISLAMIC SOCIETIES

- Apart from the religious *waqf*, general education has been the second largest recipient of *waqf* proceeds and other forms of voluntary contributions since the advent of Islam
- Financing education through *waqf* has led to several positive outcomes:
 - It created freedom of education whereby not only the rich and the ruling classes became educated, but also the poor
 - Through this approach, majority of the Muslim scholars originated from the lower-level of the society, thus reducing the disparity between the rich and the poor
- Impact of *waqf* was so enormous that a person could entirely use the services provided by *waqf* from the day he/she was born till he/she dies



OBSTACLES CONFRONTING WAQF

- Unfortunately ever since the colonial occupation, the development of *waqf* properties has been slow
- Situation is further worsened by the presence of vast idle and stagnant *waqf* lands attributed to poor management and administration of the institutions handling *awqaf*
- General public chooses to believe that *waqf* is mostly associated with properties related to religious and educational purposes
- Lack the knowledge of understanding the dynamic aspect of *waqf*
- **FINALLY** with all the positive attributes and the present obstacles faced by *waqf*, in order to propose *waqf* to fill in the present gap faced by the Muslim SMEs, it is important that the *waqf*-based model be established under the auspices of a reputable and respected *waqf* organization

BENEFICIARIES OF WAQF



No.	Types of Waqf	Types of Beneficiaries
1.	Waqf Zuhri	Religious purposes – e.g. creation of mosques, madrasahs, supply of Quran and performing hajj.
2.	Waqf Khayri	Charitable purposes – e.g. poor and needy, the destitute, the orphan, the widow, scholarships, drinking water, medicine, etc.
3.	Waqf Ahli	Family members – e.g. relatives and descendants of the waqif.



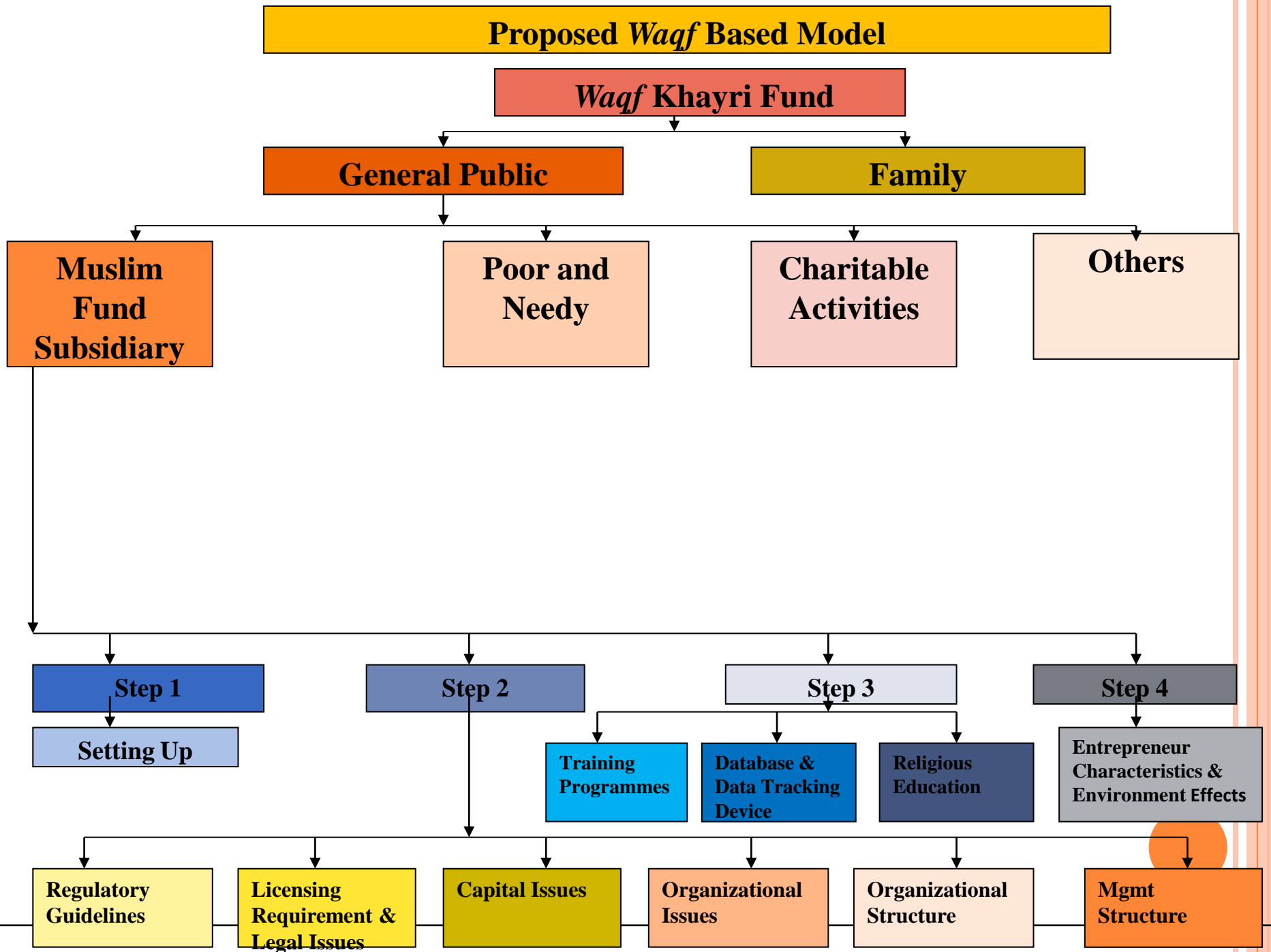
Types of waqf	Beneficiaries of waqf	
	Religious	Khayri [Philanthropic]
Family	A	B
General Public	C	D

PROPOSED WAQF-BASED MODEL



- For the purposes of poverty alleviation and providing opportunities to the general public, the most appropriate type of *waqf* for the general public is the *waqf khayri* funds (***waqf D***).
- The proposed *waqf*-based model that is founded on Islamic principles shall be established under the auspices of a reputable and respected *waqf* organization as this type of institution will have a moral authority to take leadership in the implementation of this model.
- The proposed *waqf*-based model seeks to utilise the *waqf khayri* fund from the main *waqf* body for the purpose of providing technical assistance and start-up capital to lower-end SMEs entrepreneurs.



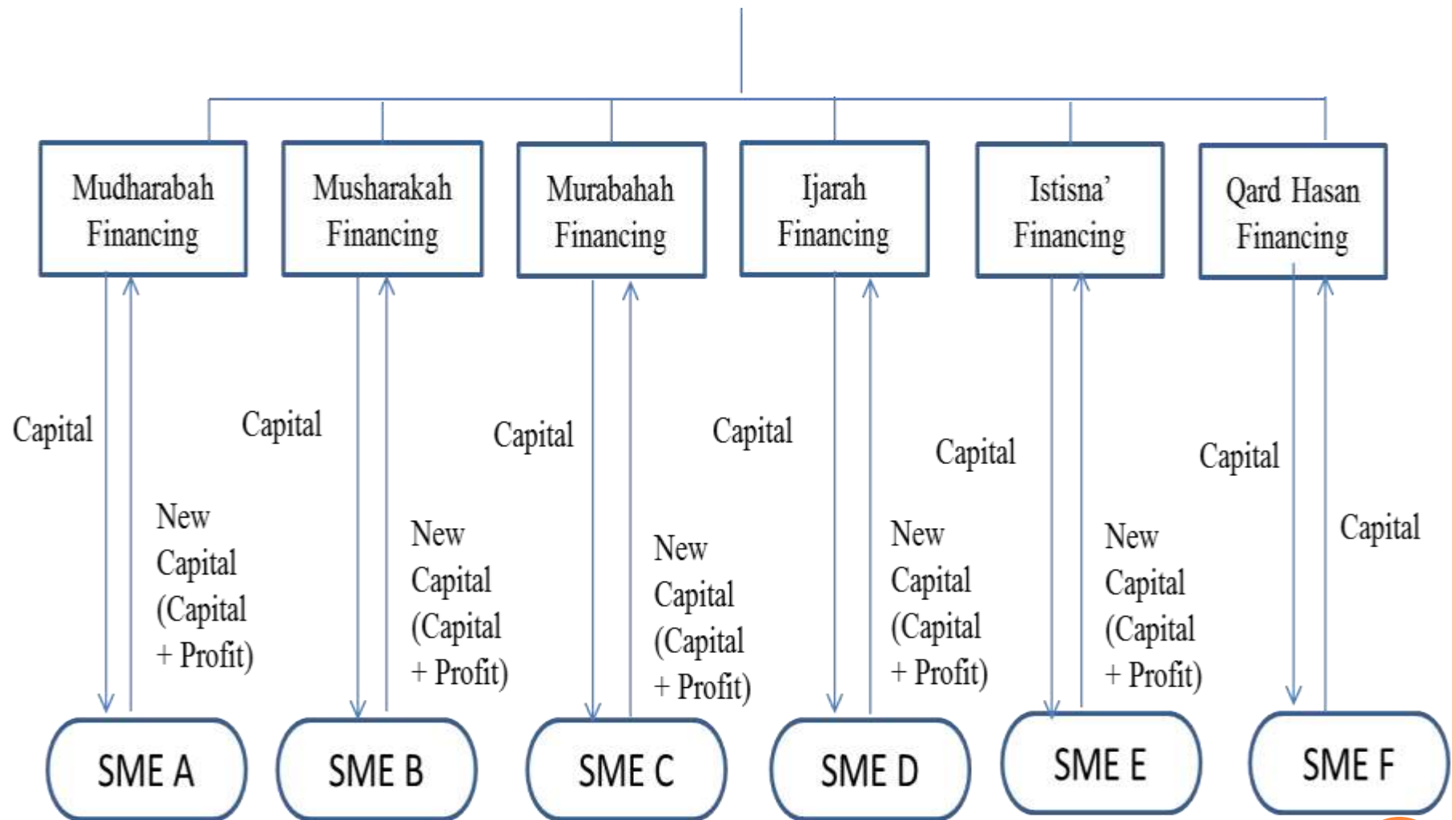


PROPOSED WAQF-BASED MODEL

- Similar to the poor and needy, charitable activities and others, the proposed waqf-based model will also receive funding from the *waqf khayri* fund.
- **Main Difference:** Unlike the poor and needy, charitable activities and others who are recipients of the *waqf khayri* funds, Muslim SMEs are also investors.
- Once they have attained profit after running the business, Muslim SMEs will channel back the original capital and a certain percentage of the profit to the proposed waqf-based model to be used for reserves and to further offer financing to other Muslim SMEs. Similar processes will be repeated.
- Without the financial capacity and strength of a bank, reserve funds will need to be created in order to ensure that, in times of low performance, the model will remain stable.



Muslim Fund Subsidiary



BRIEF SCENARIO OF MUDHARABAH FINANCING

- **Step 1:** The potential applicant is qualified to participate after the application has been approved.
- **Step 2:** Having assessed the recipient, he/she is entered into the database for SME Category A (*Mudharabah* financing).
- **Step 3:** Muslim Fund Subsidiary provides the capital and the participant will allocate his/her time, skill and effort to running the business.
- **Step 4:** The business is closely monitored on a regular basis by Muslim Fund Subsidiary. If the business achieves profit, it will be distributed according to the agreed Profit Sharing Ratio (PSR) between Muslim Fund Subsidiary and the participant. If the business incurs losses, Muslim Fund Subsidiary will lose the capital and the participant will lose the time and effort. In case of negligence from the participant, he/she will then have to pay for the losses in the capital.



OTHER IMPORTANT FACTORS

- Database and Data-tracking device
- Religious Supervisory Committee
- Training Programmes



DATABASE AND DATA-TRACKING DEVICE



DATABASE

- Set-up a database which holds the details of all members wishing to benefit from the subsidiary
- Members with similar characteristics or those facing similar problems would be grouped together in the database - provided with the most appropriate type of permissible *Shari'ah* financing instruments
- Simplify the tasks of the employees of the proposed waqf-based model, and hence improve efficiency

DATA-TRACKING DEVICE

- Data-tracking device - developments of the participants will be monitored, and the appropriate financial services will be provided as the participants' progress towards a higher development in their economic prospects.
- Device will also determine whether the participants are qualified to proceed to the next level of financing with the proposed subsidiary



RELIGIOUS SUPERVISORY COMMITTEE



- Role of the committee would be to provide religious classes in order to increase the spiritual and ethical sensibilities of the employees, applicants and future members
- Instilling the concept of *Asabiyah* in both the supply and demand elements, as it is this which promotes positive values, such as establishing a sense of co-operation and developing a sense of belonging towards the company itself
- Indirectly reduce the costs of the proposed waqf-based model as it creates a working environment characterised by a sense of social responsibility
- Engender a sense of obligation in applicants to repay the capital provided to them
- Increase the revenue of the model as the default rates decrease correspondingly



TRAINING PROGRAMMES

- Future participants would undergo several weeks of training aimed at familiarising themselves with various rules and procedures of the company
- Lead to an increase in both productivity and revenue, which will ultimately enhance the viability and profitability of the company
- Alleviate the economic status of the Muslim entrepreneurs
- Win-win situation for both the proposed waqf-based model and the Muslim SMEs





CONCLUSION

- Establishment of the proposed waqf-based model will create opportunities for the lower-end Muslim SME entrepreneurs who can never otherwise be reached by banks or Islamic financial institutions
- Allows the transformation of the poor sections of the community to potentially dynamic entrepreneurs
- Expected that the establishment of the proposed model will subsequently lead to income growth, poverty alleviation, self-employment, asset ownership and a more active participation of Muslims in the labour force
- Proposed waqf-based model offers the hope of establishing a socially responsible institution which fulfils a collective religious obligation
- If the proposed *waqf*-based model under the flagship of a respectable *waqf* body is accepted and founded, it is believed that this would help to renew the confidence of the community and further confirm the importance of the *waqf* institution as an important tool for poverty alleviation.



الشُّكْرُ أَمْرٌ عَلَيْكُمْ وَرَحْمَةٌ مِنْ اللَّهِ وَبَرَكَاتٌ

