The advent of Islamic microfinance in Senegal

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Abstract

In Senegal, as elsewhere in the WAEMU zone, access to credit for vulnerable micro entrepreneurs is a major concern despite the important role of traditional microfinance institutions. To effectively solve this problem, Islamic microfinance has been identified as an alternative offer, alongside conventional finance in order to give access to bank accounts to those underprivileged people that have not been sufficiently served by financial institutions. Thus, this article aims to study the advent of Islamic microfinance in Senegal. To do this, our research focuses on the history and role of the State of Senegal in the promotion of Islamic microfinance to finally present the characteristics of this new funding model for vulnerable populations often excluded from the traditional financial system.

Key-words: Classical microfinance, Islamic microfinance, vulnerable micro entrepreneurs

J.E.L classification: G20, G21, G23

1. Introduction

The practice of microfinance intermediation has been largely explained by the inability of the banking industry to respond effectively to the financing needs of vulnerable groups (Hugon, 1996). In this sense, microfinance institutions are considered as a financial alternative (Lelart, 2002, Barboza and Barreto, 2006), if not an additional complement of banking institutions in the Senegalese financial system. The objective of microfinance institutions (MFIs) is to seek to take into account the needs of vulnerable micro entrepreneurs through access to credit while diversifying their offer (Labie, 2009).
In Senegal, the evolution of the microfinance sector has made it possible, through creditfocused initiatives to embrace a wide range of financial services in order to achieve a more inclusive financial intermediation system service of those excluded from the conventional banking system with a view to giving them a chance

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to participate in the creation of wealth. In line with this principle, MFIs are committed to provide low-income segments of the population and micro entrepreneurs with opportunities to engage in productive activities and / or expand their business through regular access to microcredit. The latter is subject to purely conventional requirements (high interest rates, joint guarantee and guarantee ...).

According to recent data, the Senegalese microfinance sector has a total credit outstanding and a total volume of deposits respectively of 333 and 300 billion CFA francs for a clientele of 2,710,263 customers including 1,087,457 women, 1,418,949 men and 250,637 legal entities (DRS-SFD, 2017). These performances are considerable to make it clear that microfinance structures are real effective instruments for reducing poverty. However, although many poor people have seen their living conditions improved in recent decades thanks to the products and services of traditional MFIs, the high interest rates due to the cost structure associated with low credit amounts, guarantee were decried by the actors.

It is in this context that some authors have already begun to reflect on Islamic microfinance and its practicability within the Senegalese financial system. This new funding model for vulnerable populations abstains from any practices that do not conform to Sharia[3] law. In other words, Islamic microfinance offers a range of products whose object is to prevent against events that may constitute a threat or risk identified in advance and according to terms and conditions defined in advance.

Thus, its terms and conditions are more favorable and more accessible to vulnerable entrepreneurs and marginalized by the traditional financial system. On the other hand, Islamic microfinance presents a distinct model from that of traditional MFIs and an intermediation approach in which the lessor is also involved in sharing risks, losses and profits. It is also transparent in order to protect the social well-being of low-income clients.

The purpose of this article is to focus on the advent of Islamic microfinance and the main products and services it proposes for use by poor and resource-poor micro entrepreneurs. The article is divided into four parts. The first part is devoted to the history of microfinance in Senegal. The second part is to the promotion of Islamic microfinance: what role for the State of Senegal? The third part deals with the characteristics of Islamic microfinance and the fourth and final one will focus on the conclusion.

2. Historical background of microfinance in Senegal

Adapted to the needs of poor people in the margins of the traditional banking system, microfinance is a micro scale finance, which has considerably questioned the value judgment worn for ages, the insolvency of poor agents and low-income. For a long time, microfinance activities have been conducted by groups of people offering informally credit and accepting savings from vulnerable agents carrying out activities.

To this end, microfinance refers to a set of schemes that offer a range of financial services (microcredit, savings, micro insurance, transfer of funds, etc.) to poor families (Prescott, 1997), who are often excluded from the banking world for lack of tangible guarantees.

[3] Sharia is the Muslim canon law governing religious, political, social and individual life.

Microcredit was created in the 1970s with the creation of Grameen Bank in Bangladesh in 1976.This bank whose mission was to grant microcredit to poor women entrepreneurs is considered the starting point for microfinance modern. The idea of such a financial innovation, serving vulnerable people, was initiated by Professor Mohamed Yunus, the official founder of the Grameen Bank, which made microcredit popular with media impact.

Indeed, Professor Yunus has revealed to the world that it is possible and profitable to lend to vulnerable people because with the loan based on joint surety, problems related to asymmetric information and the likelihood of default are minimal.

In Senegal, microfinance was born in the mid-1980s in a context favorably linked to the achievement of the main social objectives through microfinance: poverty reduction, promotion to business creation, the diversification of enterprises and the social reinforcement of marginalized groups because of lack of wealth (Boye, Hajdenberg and Poursat, 2006).

It is clear from this observation that the arrival of microfinance in Senegal (1980-1984) coincided with the period of poor economic conditions characterized by a low economic growth rate of around 1.8%. In fact, the development models previously established by the State of Senegal, had not borne fruit on the population centered in their majority towards agriculture. Thus, on the initiative of such facts, the microfinance initiatives aimed at this population previously served by the traditional risky banks constituted a real hope for the financing of micro entrepreneurs' activities.

The first Microfinance Institutions (MFIs) created were created in the 1970s as microcredit experiments initiated by the National Council for the Promotion of Savings and Credit Unions (CONACAP) in the regions of Thies and Louga.

Other microcredit savings and loan credit union experiments were subsequently set up between 1985 and 1988 in Kaolack region with the help of technical and financial development partners. In addition, the emergence of the microfinance sector in Senegal also coincided with the withdrawal of the Senegalese state in some areas followed by the disappearance of the majority of the state bodies supporting and supervising the rural population whose level of precariousness was very high. This socio-economic situation, which is very unfavorable to the rural world, was certainly aggravated by the national banking crisis, which resulted in the closure of the public development banks (BNDS, BSK, SONA Banks, USB, etc.) whose mission was to increase the supply of finance to the economy in the hope of raising the productivity income and financial inclusion of marginalized small farmers.

Unfortunately, these development banks have failed for most of them and their closure in the period (1990-2000) was followed by the liberalization of the Senegalese banking sector and correlatively the extension of the microfinance sector (Nagarajan and Meyer, 2005).

Therefore it appears that in the early 1990s, the term microfinance began timidly to supplant that of microcredit to describe a wide range of financial services for the most vulnerable including savings, micro insurance money etc.

Despite the proven performance of traditional MFIs, the recurring problems of under-financing the economy remain. Thus, in 1993 on the initiative of the Association of Students and Muslim Students of Senegal (AMEES), the Mutual Savings and Islamic Credit of Senegal (MECIS) was created marking the

beginning of Islamic microfinance in Senegal. In this momentum, the Department of Islamic Finance (DEFI) was formally set up on 30 July 2011 by UM-PAMECAS to exploit this alternative financing offer. The beginnings of Islamic microfinance in Senegal coincided somewhat with the subprime crisis of 2007, which had adverse effects on the banking environment of sub-Saharan African countries such as Senegal.
These constraints reduce the access of vulnerable groups to fund and explain among other things the choice of public authorities in relation with certain public and private partners notably the IDB to initiate several projects and programs (PALAM, FNPEF / PADEF- EJ, PDESOC, PADES, Bouchra SA) to promote the development of products and services of Islamic microfinance.

Since its first experiences, it is indisputable that Islamic microfinance has begun to interest the actors of conventional finance and the government of Senegal. Despite its potential for development, Islamic microfinance remains little explored and currently represents a market that most poor people do not understand. Currently, in Senegal only 6.3% of households are familiar with Islamic finance (ESRIF, 2017). It is in this particular context that has attracted increasing interest among decision-makers notably the Central Bank of West African States (CBWAS) and the WAMU states to create favorable conditions for the development of this new model financing and deepen the level of financial inclusion of the population.

3. Promoting Islamic Microfinance: What Role for the State of Senegal?

In its policy to support economic growth, fight effectively against household poverty and job creation, the State of Senegal is largely committed to widen the access of vulnerable groups to financial services through the deepening and diversification of the microfinance sector's offer. Despite the notorious performance of microfinance institutions, the exorbitant costs of their services, including interest rates, have often been decried by low-income populations and some policy makers.

Concerning the situation, a regular and legal system allowing actors to lead Islamic microfinance activities is also available in the Central African Bank of Western States (CABWS).

The system is based on instructions and community law and aims to define the different conditions for the exercise of Islamic microfinance activities within the West African Monetary Union (WAMU). For this purpose, Article 3 of Instruction N ° 002-03-2018, defines the scope of Islamic microfinance, which may be applied by all credit institutions, complying on a global or partial basis in their operations, the principles and rules of Islamic finance.

It is also important to note that the motivations of public and private actors in Islamic microfinance are also largely explained by the highest demand of the large number of Muslims seeking Sharia-compliant financial services. In addition, there is the competitive nature of Islamic products and services, which are increasingly attracting vulnerable investors more specifically SMEs, on the fringe of the traditional financial sector.

Indeed, Senegal has set up with the support of the Islamic Development Bank (IDB) a range of projects whose main mission is to promote Islamic finance in particular Islamic microfinance at the service of the poor population.

As an illustration, the State of Senegal has established through the Ministry of Women, Family and Gender, the Support Project for the Development of Female Entrepreneurship and Youth Employment (PADEF-

EJ). The main mission of this project is to enable women and young entrepreneurs to have the opportunity to access finance to develop income-generating activities, with a financing line of 4 billion supported by the IDB.

In addition to this project, there is the Literacy and Apprenticeship Program for Poverty Alleviation (PALAM / IDB / SEN). This program is based in fact on the promotion of endogenous know-how, through the equitable access of rural youth and women workers to qualifying training programs and to Islamic microfinance favoring self-development. The Livestock Development Project in Eastern Senegal and Upper Casamance (PDESOC). The project to create a public limited company for Islamic microfinance (Bouchra SA) supported by UM-PAMECAS, the State of Senegal and private partners such as the IDB, etc.

In addition, in order to consolidate its programs and to have a favorable framework for the development of Islamic microfinance, a framework agreement was signed between the State of Senegal and the IDB, creating the National Development Program of the Islamic Microfinance in Senegal (PROMISE).

Like other programs, it is in full compliance with certain orientations of the Emerging Senegal Plan (ESP)[4] particularly the promotion of Islamic finance, which has so far been underutilized, the widening of financial inclusion to the benefit of poor, support and financing of SMEs. To this end, the main objective of the program is to contribute to the socio-economic development of Senegal through the financial inclusion of SMEs. This financial inclusion for SMEs would result in more jobs and social advancement for vulnerable groups. According to the expected results, 50 000 microentrepreneurs could benefit from this financing. This would create 25,000 new jobs by 2022 (Promise, 2018).

This innovative mechanism is part of the principles of sharia law and is an attractive source of funding for people and businesses outside the traditional financial sector.

4. Characteristics of Islamic microfinance

MFIs have played a crucial role in engaging the financial inclusion of the poor while promoting the spirit of entrepreneurship especially in underdeveloped countries (Dupas and Robinson, 2013). It is in such context that we consider it necessary to study Islamic microfinance. Indeed, Islamic microfinance is defined as the provision of financial services in accordance with Islamic law for the moderately poor and excluded from the conventional financial system in order to promote the financial inclusion of the latter.

It aims to ensure the well-being of the disadvantaged population with the help of a new intermediation whose basic principle is to promote harmony and social solidarity.

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[4] The Senegal Emergent Plan (PSE) is a program that was set up by the Government of Senegal whose horizon is set at 2035. The PSE in the perspective of boosting the Senegalese economy is based on a set of structural projects to high value-added content and job promotion. For that it is declined in three strategic axes of which:

✓ Structural transformation of the economy and growth; ✓ Human capital, social protection and sustainable development; ✓ Governance, institutions, peace and security.

This new funding model abstains from practices related to the negative principles [5]prohibited by sharia law and favors in its financing the adaptation to positive principles[6]. In this context, the returns and profits from the project are dictated by tangible assets or identifiable services as opposed to speculation and receivables as in conventional finance. For these reasons, the financing conditions of Islamic microfinance make it more accessible and more beneficial for vulnerable entrepreneurs. This explains the impressive growth of this new funding model. The specificity of Islamic microfinance allows us to distinguish two models characterizing the financing offer of Islamic microfinance institutions (IMFI):

4.1. Non-profit Islamic microfinance model

Charities are one of the pillars of Islam. Muslim law on all Muslims and business carrying out income-generating activities imposes them.

For example, Zakat or compulsory charity requires an obligation on every Muslim to pay an annual amount of 2.5% of all wealth held.

In addition, IMFIs can use non-compulsory forms of charity in their funding policies to help to eradicate poverty. ‘’Al Waqf’’ is a "*Sadaqa Jarriya*" that can be defined as "*the possession of a property, converted from private property into social property, and the usufruct of the generated income is allocated to defined beneficiaries*".

5 The negative principles of sharia are:

• Prohibition of the use of Interest and Wear (Riba);

• Prohibition of uncertainty (Gharar) and speculation (Maysir);

• More general prohibition of all that illicit such as Alcohol, speculation, Gambling and so on.

6 Positive Principles:

• Sharing of risks, losses and profits;

• Backing of any financial transaction to a tangible asset.

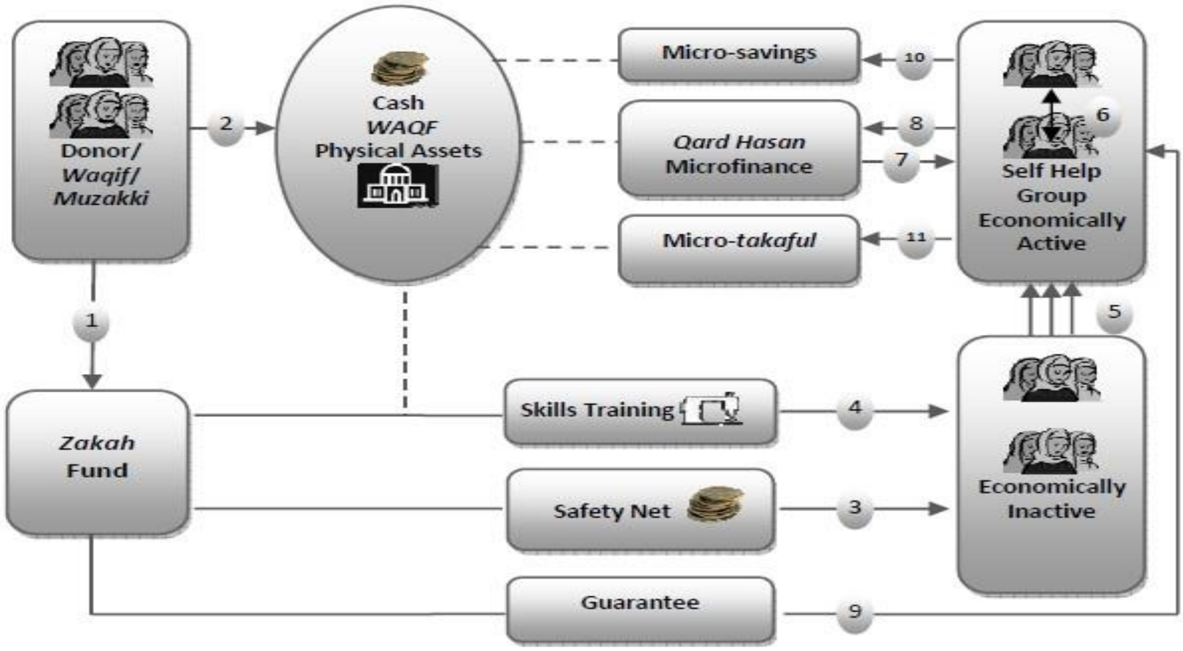
Thus, the “Waqf ‘’is the immobilization of a movable or immovable property an annuity or a service for the cause of God. This expression " for the cause of God " covers all charitable action aimed at improving the living conditions of the citizens as well as at meeting their needs in terms of infrastructure, health, education, education and training drinking water, roads, etc.

Added to this, there are other types of charity such as the Sadaqa Jaria, which is a continual charity, and the’’ Qard Hassan’’, which is the only product of Islamic finance which is to lend money to the poor entrepreneur without margin. The latter is a volunteer contract. Qard Hassan financing is a financing granted free of charge by the bank which receives no remuneration from the beneficiary. The only obligation of the customer is to repay at maturity, the amount of capital that has been lent to him.

When the lender asks for the amount he has lent to the borrowing client, he must immediately repay the amount without a profit margin. Qard Hassan was the base of Islamic microfinance during its early stages in Egypt.

Thus, in the context of Senegal, where poverty continues to plague the economy, these forms of charity offered by Islamic microfinance can play a key role in the fight against the financial exclusion of microentrepreneurs and participate in the promotion of poverty entrepreneurship of these.

Figure 1: Islamic Non-Profit Microfinance



Source: OBAIDULLA Mohammed, 2008, « Introduction to Islamic Microfinance », IBF Net, New Delhi, P.52.

This chart shows the different forms of charity that can be used in the practice of non-profit Islamic microfinance.

In view of this pattern we can emphasize that the interactions between different charities and active and inactive populations illustrate an Islamic microfinance model differ from the classical one. In explicit terms, donor Zakat funds are managed by Islamic microfinance institutions.

In addition, another body created by the Islamic microfinance structure deals with the endowment of other charities such as Waqf and Sadaka in the form of tangible assets (for example the training of poor microentrepreneurs selected by the Islamic microfinance structure). or monetary assets (for use of the Islamic product such as Qard Hassan). In addition, some capacity-building programs may be offered to poor inactive people seeking employment or income-generating business activities but lacking tools or investment funds. To facilitate and provide these training courses, IMFI can implement the Waqf.

4.2. For-profit Islamic microfinance model

The Quran is the first reference book of Islam in solving all problems. He explicitly and categorically forbids ''Riba''; payment and receipt of interest represent a form of ''Riba''. Because of this ban, many long-term poor Muslims are excluded from the formal financial system.

This means that those who have a surplus of funds will not put their savings surplus in these conventional banks that operate on the basis of the interest rate.

Similarly, those among them who have economically viable projects approved by Islamic law (Shari'a) will also not approach these traditional banks to find financing. The adverse effects of such attitudes on national income and productive activities are considerable.

The presence of Islamic microfinance institutions that offer alternative and Shariah compliant products would help address this problem. It is clear that the regulatory reform in France that allowed the introduction of sharia-compliant financial products was motivated by the opportunity that Islamic finance represents in increasing the wealth of their economy. In addition to the positive effect that Islamic microfinance has on the promotion of a seine economy, the diversification of the financing products it offers to the poor is a good method of managing the risks faced by lenders (asymmetry of information, credit risks, operational risks, legal risks ...).

Another source of stability for Islamic microfinance lies in the sharia provisions that make speculative activities difficult to conduct. In fact, IMFI's products are characterized by their performance linked to the connectivity between the financial sector and the real sector of the economy.

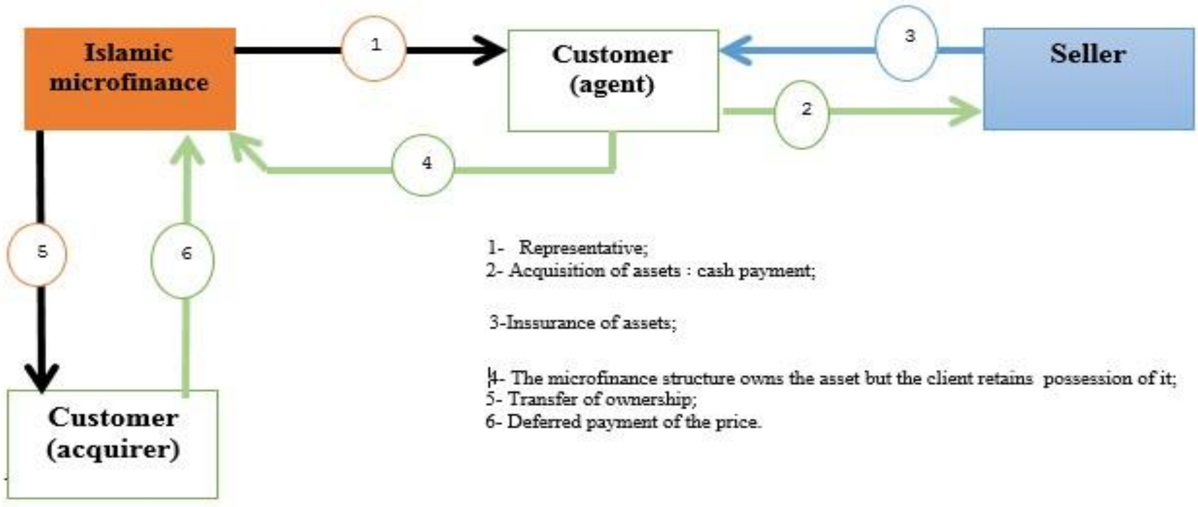
It is in this wake that Islamic microfinance institutions can develop a win-win partnership relationship with clients. Thus, it is almost impossible to imagine with such products that Islamic microfinance uses that a bubble as we saw during the subprime crisis of 2007, cannot occur.

This is why recently and especially after the consequences of the latter, that some financial entities including the IDB and the State of Senegal have committed to expand the financial system by facilitating access to Islamic microfinance products. Briefly presented, here are some of the benefits that Islamic for-profit microfinance products could bring to Senegal's economy. Indeed, in line with Islamic law, all operations or financing products of Islamic microfinance must be backed by real asset or Asset Backing held by IMFI. This obligation strengthens the potential for stability and control of different types of risks. This is why Islamic microfinance financing instruments have particular aspects compared to those of conventional microfinance. Thus, among the most well-known financing contracts we can note the contract of sale or purchase, order or partnership between IMFI and entrepreneur engaged in the realization of a common project. For example, we can list funding mechanisms such as:

- Murabaha, which are sales contract, which includes two parties a seller (IMFI) and a buyer (customer). The Islamic microfinance institution buys the goods required by a supplier and resells them to the customer with an increased selling price.

  When the Murabaha contract is signed between the two parties, the repayment period and the installments are specified at the time of signing the contract.

Figure 2: The working principle of Murabaha



Source: Author, based on Murabaha Principe Herbert Smith (2009), the guide to Islamic finance.

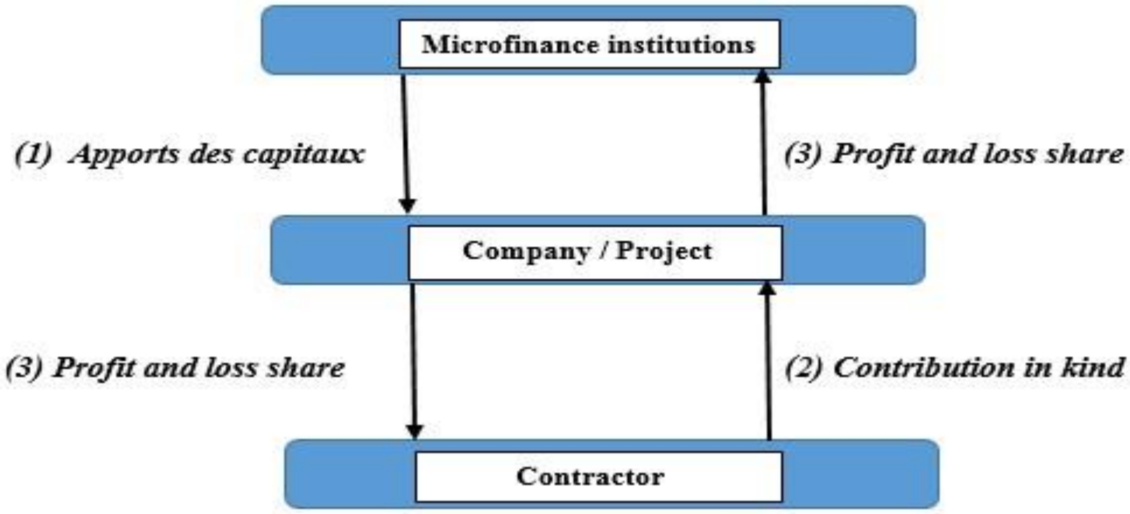
- ''Ijara and istina'': Regarding ijara, it is a means of financing that consists of buying materials or equipment and then transferring the usufruct to the customer, for a period of time according to which he retains and benefits from these equipments.

Unlike ijara, istina is a financing method based on a contract for manufacturing a property or building a real estate. The istina contract stipulates that the IMFI or vendor agrees to provide in a timely manner and at a price required in advance to the customer, the goods, once built. In this case, of contract the goods are specified at the signing of the contract.

There are also other financing mechanisms that Islamic microfinance uses to finance entrepreneurs, these are:

- The Moudharaba, which is a contract allowing the entrepreneur to carry out a project with the help of the investments coming from the Islamic microfinance structure. In this type of contract, any gains or losses incurred will be shared according to a criterion established at the time of signing the contract.
- Finally, we can also mention the contract of Mousharakah which is a contract that binds partners. The latter contribute together both to the capital and the management of the project and entrust to one of them the management for the success of the project.

Figure 3: The operating principle of Mousharakah



Source: Authors

Thus, for the effective use of these Islamic microfinance products, a number of challenges have recently been identified by the (CABWS), with the publication of the new instructions N ° 00203-2018 and N ° 003-03-2018 relating to specific provisions applicable to decentralized financial systems engaged in Islamic finance activity. Such a regulation facilitates the practice and expansion of Islamic finance particularly Islamic microfinance within the financial system of the countries of the West African Monetary Union (WAMU).

5. Conclusion

Islamic microfinance is an innovative financing model that combines the real and financial sphere based on Islamic law (sharia). In this context, we have tried in this article to address the advent of Islamic microfinance in Senegal and the different products that IMFI offers in order to meet the financing needs of poor populations and micro entrepreneurs in search of funding.

This is why the State of Senegal has undertaken initiatives with IDB and CABWS to allow this new financing model, which is aimed mainly at vulnerable entrepreneurs, to take off. Even though Senegal has not yet had a mature and dynamic Islamic microfinance model to address the growing financing needs of vulnerable entrepreneurs, the situation reveals that in-depth studies need to be done in this area.

It emerges from this analysis that, like the Islamic bank, Islamic microfinance structures are necessary complements to conventional ones in order to increase the financial inclusion of the poor since the conventional microfinance credit supply cannot satisfy all demands for credit from vulnerable micro entrepreneurs.

Thus, this additional weight of IMFI in the traditional microfinance sector can also be justified by the opportunities offered by Islamic microfinance products for agents on the margins of the banking sector who do not have the same needs. With a view to developing this sector, which is poorly known by the poor, CABWS has addressed this issue by proposing new instructions to facilitate the practice of microfinance-by-microfinance institutions.

Despite the efforts made, certain difficulties such as the lack of qualified human resources and the heterogeneity of the Islamic financial practices, the inadequacies of the principles and rules of Islamic finance linked to the divergent ideas of the "Shariah Central Board" are constantly gangrene the good practice of this new funding model.

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