

IS THERE ANY DIFFERENCE BETWEEN ISLAMIC AND CONVENTIONAL MICROFINANCE? EVIDENCE FROM BANGLADESH

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ABSTRACT

This study aims to compare the microfinance operation of Grameen Bank and the Rural Development Scheme of Islami Bank Bangladesh Limited. Qualitative approach is employed to obtain in-depth information concerning the operation of Grameen Bank and Rural Development Scheme. The data were collected through interviews conducted with Grameen Bank and Islamic Bank Bangladesh Limited officers and the customers of both microfinance providers. The study found that Grameen Bank was an interest-based microfinance organization, which used peer pressure as collateral for distributing loans, while the Rural Development Scheme implemented different types of investment modes to finance the poor. Moreover, it targeted the family as borrower instead of merely targeting women. Although Grameen Bank had a higher number of members and greater coverage, in some cases, the performance of the Rural Development Scheme was better, such as the effectiveness of the credit. Although conceptually Islamic microfinance is different from the conventional microfinance but few studies have been done on how they differ each other in terms of their operations. The study may contribute to determine the weaknesses and strengths for both types of institution.

Keywords: Microfinance; Islamic Microfinance; Bangladesh; Grameen Bank; Islamic Bank Bangladesh Limited; Rural Development Scheme.

1. INTRODUCTION

Although conceptually Islamic microfinance is different from conventional microfinance but it is a question that whether its real operation is different from the conventional microfinance or otherwise. Very few case studies have been done on the operation of Islamic microfinance in comparison with its conventional microfinance. Although a number of studies have been made analysing the Grameen model with Islamic law, those studies were very conceptual (Rahman, 2010a; Feroz and Goud, 2009; Smolo and Ismail, 2011; Saeed and Saqib, 2011). In this respect, a comparative case study between Grameen Bank (GB) and Rural Development

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Scheme (RDS) can provide better understanding of the differences of operations between conventional and Islamic microfinance institutions.

The comparative case study may contribute to determine the gaps and strengths for both types of institution. In the recent past, a number of studies have been conducted to evaluate the impact of microfinance on the poor and poverty alleviation (Mahjabeen, 2008; Duvendack et al. 2011; Rahman and Ahmad, 2010; Ashraf *et al.*, 2014). Various issues have been found on the operation of microfinance in different parts of the world. It was an endeavour by several studies to figure out the best model for microfinance institutions (Toindepi, 2016; Sarma and Mehta, 2014; Rahman and Dean, 2013; Rahman *et al.*, 2011). This study may contribute to this attempt through discovering the strengths and weaknesses in GB and RDS's operations.

According to United Nations' (UN) 2030 sustainable development agenda, alleviating all types of poverty which includes the extreme level of poverty is the biggest global challenge and essential for sustainable development. Bangladesh as a member country of UN is making its utmost effort to achieve this goal. A number of non-government organizations (NGOs) including micro-finance institutions are attempting to improve the socio-economic status of the people in Bangladesh (United Nations, 2015; United Nations in Bangladesh, 2013). Towards this end, it is necessary to examine in what ways these two types of micro-finance institutions contribute to the development of the socio-economic status of the people. This study analyses the operations of the institutions, mode of investments, method of targeting the borrowers, risk management techniques, training of the members, marketing strategies, social development and overall performance of the institutions.

2. MICROFINANCE IN BANGLADESH

Microfinance institutions play a great role in the socio-economic development of Bangladesh (Fowler, 2010). Among the microfinance institutions, Grameen Bank (GB) is the most well-known institution (Mahjabeen, 2008). Although GB contributes to poverty alleviation in the rural areas of Bangladesh, its operation is based on interest (Smolo and Ismail, 2011). Islamic law strongly prohibits any involvement with interest (Rahman, 2010a). As a Muslim, interest is a notable barrier to choose a conventional microfinance like GB. A significant number of Muslim customers state that they do not approach conventional microfinance for religious reasons (El-Komi and Croson, 2013). As the majority of the Bangladeshi population are Muslims, Islamic micro-finance institutions emerged in Bangladesh to fulfil the demand from the Muslim customers. The pioneer of Islamic microfinance in Bangladesh is Islami Bank Bangladesh Limited (IBBL). IBBL introduced its Islamic microfinance programme under its Rural Development Scheme (RDS) in 1995 (Kroessin, 2011; Haque and Yamao, 2011; Rahman, 2010b).

3. RESEARCH METHOD

A comparative case study requires a detailed investigation of the contexts and characteristics of two or more objects (Campbell, 2010; Hartley, 2004). Therefore, qualitative approach is employed to obtain in-depth information concerning the operation of GB and RDS. Secondary data were gathered, first through the available literature and official websites, and,

subsequently, qualitative interviews were conducted to achieve deep information and to validate the secondary information. Qualitative interviews are necessary to obtain in-depth information and knowledge (Johnson, 2001). The interviews were conducted with the field officers and customers of RDS and GB.

We interviewed three RDS officials and four customers. On the other hand, two GB officers and two GB customers were interviewed. The GB officials were centre managers for GB. The clients of GB who were interviewed took loans from GB and were paying back on weekly instalments with interest. Among the officials of RDS who were interviewed were an RDS co-ordinator of an IBBL branch and the other two were field officers of RDS. The clients of RDS who were interviewed took several types of financing from RDS. The interviewees are kept anonymous to maintain respondents' confidentiality.

In the discussion of this paper, we have labelled the interviewees. The officers of GB will be referred to as G₁ and G₂ and the clients will be referred to as H₁ and H₂. Similarly, the officials of RDS will be referred to as R₁, R₂ and R₃, and the clients as S₁, S₂, S₃ and S₄.

The officers of GB and RDS were contacted by phones and taken permission for interview by presenting the summary of the interview questions. The customers were then contacted through the representatives of the researchers who explained to them the interview questions and took their permissions. Each interview took approximately 45 minutes to one hour. The officials of GB and RDS were interviewed in respect of the following themes, i.e. organizational structure, funding of the organization, mode of financing, method of targeting the borrowers, risk management techniques, marketing strategies, training programmes, social development plans and performance. Following this, the customers of GB and RDS were interviewed to obtain their opinions concerning the mode of financing, methods of targeting the borrowers, risk management techniques, marketing strategies, social development plans and performance. The two different categories of interviewees strengthen the validity of the data collected. The possible biases of the officials of GB and RDS as the representatives of their respected institutions were minimized through requesting them to share their real experiences and through keeping their names as confidential. Moreover, interviewing the customers validates the claims of the officers of the respected microfinance institution.

After the data were collected from the interviews, they were analysed according to the themes. The data were read several times with considering the relevant research questions. Looking at the data several times, the researcher identified the themes and their relationships through the patterns and processes, commonalities and differences through coding system, and arranged them through thematic analysis. Finally, a comparative analysis was made between GB and RDS. In this approach, a number of themes were examined to determine the similarities and differences.

4. FINDINGS

The comparison between GB and IBBL will be presented in relation to the following aspects – organizational infrastructure, process of getting funds, mode of financing, methods of targeting the borrower, risk management, marketing strategies, training, social development and general overall performance.

4.1. *Organizational Structure*

GB is solely a microfinance organization. It opens its branches based on the demands of the borrowers. Each branch of GB is managed by a branch manager and a few centre managers. A branch usually covers 15 to 22 villages. The branch manager and the centre managers study their area of operation and attempt to improve the tight relationship with the customers. In GB, normally ten members form a group, and eight to ten groups make a centre. The centres are managed by the branch office.

On the other hand, IBBL is a commercial Islamic bank that runs its Islamic microfinance programme under the Rural Development Scheme (RDS). In RDS, around five to six members make a group and several groups make a centre. A number of centres run under the respective branch of IBBL. RDS operates within 10 kilometres of the branch office of IBBL.

4.2. *Funding and Deposit Collection*

Since 1995, GB has been funding 90 percent of its loans from the deposits and interest income. Grameen has made a major distinction from the commercial banks as it raises deposits from the village and also distributes loans to the women in the village. In addition, GB used to open new branches with central loans and used to pay back from the deposits they collected. Now, the new branches are opened without taking any central loans. To open a new branch, the staff go to the villages and market their products and motivate people to deposit their money in Grameen. On the opening day, people deposit money in Grameen office and the next day Grameen distributes loans to the borrowers. G₁ pointed out that, currently, GB is totally successful in becoming self-reliant as it does not need to depend on the branch or others.

Borrowers are allowed to purchase one share of Grameen Bank when their savings reach a certain amount. Savers get access to the standard deposit account and mutual fund accounts. In this way, Grameen permits borrowers to invest in different ventures within the Grameen portfolio. When borrowers are being converted to depositors and shareholders they come under the common goal of Grameen, which is sustainable poverty eradication.

In contrast, RDS is funded by IBBL. R₂ and R₃ mentioned that RDS is not fully self-reliant as it has to rely on the branch of IBBL.

4.3. *Modes of financing*

Grameen provides loans to the borrowers based on their needs. The minimum loan amount is USD35 and the average is USD200. The interest rate is 20 percent per annum. Although Grameen only gives loans to the poor with interest, RDS is practicing different kinds of financing modes to share risks with the poor. This is due to the prohibition of interest in *Shari'ah*. Basically, RDS implements *murabahah* and *bay'mu'ajjal* modes of investment for financing with the customers.

Bay'murabahah is a cost plus agreed profit sale. It is a contract between a buyer and a seller under which the seller purchases a commodity, and sells it to the buyer with an agreed profit between them. The payment can be made either in cash, or instalments, or at a fixed future date. In the case of RDS, it asserts that it would take 10 percent profit from the first price of

the product. In fact, *bay' murabahah* is a contract of trust in which the seller's honesty is essential. Moreover, the first sale contract should be on the spot but not on credit. The second sale contract can be on a deferred price. This is the actual practice in RDS where the bank buys the products and then sells them to the client.

Secondly, *bay' mu'ajjalis* a contract between the bank and the client in which the bank sells the commodity to the client with a fixed agreed price, and the client pays the price at a certain future date, in sum or fixed instalments. This is a credit sale. Here, the ownership of the goods is transferred to the client at present, but the payment is made in future, either in lump sum or fixed instalments. The client can make an order to the bank, and can identify the features of the commodity.

Although *bay' mu'ajjal* appears to resemble *bay' murabahah*, there is a difference between the two. *Bay' murabahah* is a cost plus agreed profit sale. Meaning to say, in *bay' murabahah*, the bank reveals the cost of the commodity, and the price of the commodity is decided by both of the parties with the cost price plus the proportion of profit. On the other hand, in *bay' mu'ajjal*, the bank does not reveal the cost of the goods and the proportion of profit.

It might be deemed that both *bay' murabahah* and *bay' mu'ajjal* differ from *riba* as they have mark-up, and mark-up is similar to interest. However, the justification of *Shari'ah* scholars is that the mark-up has nothing to do with time. It is fixed at the beginning of the contract. Therefore, it does not increase because of the expansion of time. If the client cannot pay by the due date then he is not charged an extra amount.

In RDS, the bank gives a rebate (a deduction from an amount to be paid) of 2.5 percent for on time payment. This is different from *Grameen*. In *Grameen*, there is no rebate for on time payment. Giving rebate helps RDS to get repayments on time, which may reduce the burden of risk management on RDS as giving a rebate works as a tool of risk mitigation.

In addition to *bay' mu'ajjal*, *mudarabah* is used for financing. A *mudarabah* contract is based on the principles of sharing profit and loss where one party provides capital and another party provides labour for business or investment. The profit is distributed between them based on a predetermined ratio. In the case of a loss, the capital provider bears the loss and the entrepreneur loses his labour. The bank provides capital to the clients to do small business. The profit will be distributed between the bank and the client (the entrepreneur) according to the predetermined ratio.

Furthermore, 'hire-purchase under joint ownership' is included in RDS's financing. This is a contract in which the bank and the client initially enters into joint ownership of a property, or equipment, or any commercial enterprise. Subsequently, the client hires that property from the bank. The bank promises to the client that after a certain period of time the client can be the sole owner of the property by paying the price of the property in sum or instalments.

Under hire-purchase in joint ownership, the bank provides a house to the needy people. The clients will pay the rental of the house, and, gradually, buy the bank's share. In addition, hire-purchase joint ownership can be practiced through providing agricultural instruments for the farmers.

Finally, *salam* is a deferred delivery contract through which the buyer pays the full price in advance for goods that will be delivered at a specified future date. Farmers usually use this contract to raise money before the harvest for agricultural goods that will be delivered later.

In the case of GB, the 20 percent interest rate is a big burden for the poor people. Moreover, the payment is on weekly basis. This is another problem for the borrowers since it is very hard to get return from a small business within one week. H₂ mentioned that she bought a cow using the Grameen loan. She sells the cow's milk to repay her loan but it is difficult for her to repay the loan on a weekly basis. She mentions that a partnership business would be better if business knowledge was available.

On the other hand, depending on the contract mode, the repayment in RDS is once, weekly and monthly. S₁ mentions that she has taken three types of financing from RDS and the repayment modes for all of them are on a lump sum basis. She started a fishery project as a partnership business with RDS. She states, "previously I thought that loan was very helpful but now, after I started the partnership business with RDS I have experienced that partnership business is more helpful". However, S₃ signifies that in partnership business it needs to wait for a long period to get the profit.

4.4. Targeting the borrower

In giving loans, GB targets the poorest of the poor with special priority for women. Women receive 95 percent of Grameen loans. Women are the majority of Grameen Bank's clients because they have very little access to conventional bank loans and other alternatives. Until now, women only had a one percent share of bank loans from the commercial banks. Giving loans to women also helps the empowerment of women (Mainsah *et al.*, 2004; Yunus and Jolis, 1998). In addition, the necessary criteria for selecting a borrower is whether the woman is a member of another Non-Government Organization (NGO), a house owner and their ability to repay the loan. The husband's occupation is also a notable criterion for selecting a borrower (G₁ and G₂).

However, RDS does not differentiate between men and women in targeting the borrowers. Usually, RDS targets the family. Therefore, when giving loans both the husband and wife are mutually responsible for repaying the loan. Moreover, RDS has different criteria to choose the borrowers. It chooses the able bodied and industrious poor who can work hard with the financing they receive. In addition, RDS targets the people who have cultivatable land or a small farm (Islami Bank Bangladesh Limited, 2012).

4.5. Risk Management

In GB, women form a group of 5 to 10 members to come into the credit system. The group members will rank themselves according to their financial strength. Based on this ranking, the most needy will get the loan first. A leader for the group will be elected who will receive a loan after the most needy members fulfil the terms of their loans, which involves the frequent weekly schedule for repayments (Mainsah *et al.*, 2004; Wahid and Hsu, 2000).

In addition to the domain of the central bank, Grameen Bank has its own regulation system for risk management. Grameen Bank significantly depends on the social pressure of the group

members to minimize the default rates. Members of each group face considerable peer pressure from their peers to repay the loans, as they know that if one of the members defaults then nobody in the group will receive a loan. The default of a member causes the individual's loss of reputation among their peers as they deprive the others from being able to get loans. Therefore, both the support and the pressure of the peers motivate each borrower to repay the loans (Mainsah *et al.*, 2004; Hussain *et al.*, 2001).

In addition to peer pressure, the centre manager works as the second layer of control. The centre manager plays an active role in selecting the borrowers, approving loans for a group and supervising the income-generating projects. The centre manager visits the loan receivers and monitors the repayment of loans. Moreover, the branch manager works as another supportive risk mitigation instrument in approving the loans for the group borrowers (Mainsah *et al.*, 2004).

Furthermore, every group member needs to save one Bangladeshi Taka (BDT) per week into a Group Savings Fund (GSF). These savings work as collateral for any credit default. Moreover, the bank's Management Information System is introduced to analyse data and identify any risk warning, such as unusual fall of loan repayments in a particular branch or location (Wahid and Hsu, 2000; Hussain *et al.*, 2001; Hassan, 2002).

Similar to GB, RDS also uses peer pressure, savings accounts and monitoring as risk management tools. However, RDS has some distinct risk management tools, such as mutual guarantee, which is where one person is liable for another. This is a personal guarantee given by a specific person to another person. In addition, the wife will be responsible for the husband's payment as the family is responsible for repaying the loans. Furthermore, the Islamic religious teaching in each weekly meeting acts as a motivation for the clients to be sincere in their dealings with the bank. S_1 reveals that religious responsibility, accountability in the Hereafter and the obligation of a promise lead her to be committed and sincere with RDS. Additionally, the desire to get more loans/financing encourages the clients to fulfil their financial responsibilities with RDS (S_2). To minimize the *Shari'ah* risk, IBBL has the central *Shari'ah* advisory board consists of *Shari'ah* scholars who will advise on the overall business of the bank (Haque and Yamao, 2011).

4.6. Marketing

GB designs its products based on its customer's needs and then goes to the houses of the clients in the rural villages to market them. Each Grameen branch is established based on the response of the clients. Grameen has become very sustainable as they give financing after they have received deposits from the clients. However, due to the involvement of interest it is a hindrance for the officers to market the GB products (G_1).

However, RDS's marketing is limited to the nearest branch office of IBBL. They cannot go beyond ten kilometres from the branch office. Nevertheless, RDS has different types of product compared to Grameen. RDS introduced different risk sharing joint-venture products along with the debt financing. Therefore, RDS has more potential to attract the clients. Moreover, many choose RDS as it is free from interest and sometimes RDS gives benevolent loans to its members in crucial situations (S_4).

4.7. Training

RDS disburses financing after the eight weeks training programme. Within these eight weeks, members receive training on investments and rules and regulations for the clients. Members' attendance and sincerity is evaluated before providing financing to them. In contrast, Grameen provides one week training programme before giving loans to its clients. Grameen's training focus is on educating the members and informing them of the terms and conditions of the clients. Both GB and IBBL have a weekly meeting where they can train their members. The training provides the members with the necessary knowledge about investments, and the repayment procedures, rules and regulations of the organization.

4.8. Social development

GB works for social development through the empowerment of women in the society. G₂ points out that GB has brought about social change by making the women self-reliant. On the other hand, RDS targets social development through the development of the families as a whole. However, both emphasize the education of the children, as well as the better health and nutrition of the members. R₁ reveals that RDS made social change through the establishment of an ideal village and family, providing education for the children and motivating religious practice.

GB has developed particular social development objectives. Its 16 decisions are a list of goals that the borrowers and their family members need to achieve and strive towards. The decisions comprise the promise of improved sanitation, education, family planning, housing, good nutrition, etc.

Similar to Grameen, RDS has developed 18 goals. RDS has added some religious teachings to its social development goals and omitted some of the Grameen ideologies that are contradictory to Islamic teachings. The different social development goals of RDS are: seeking Allah's help in all conditions of life, commending others to do good deeds and prohibiting bad deeds, to abide by the laws and not to rely on others, to give preference to others over one's self, competing in good deeds and encouraging others to do likewise, accomplishing all the promises and not to break the trust, and not to tell a lie.

Conversely, GB's distinct goals are living in a better house, keeping the family small, not to do injustice to others, collectivity in doing big investments and solving problems. However, some social development goals of GB and RDS are similar to each other, such as the development of the family, planting and eating vegetables for good health and nutrition, helping each other, drinking pure water, using sanitary latrines, keeping the households and the environment clean and not taking dowry for weddings.

4.9. Performance

GB has a higher growth rate and greater coverage than RDS. While RDS's members were 608,703 in 2010, GB's members numbered 8,340,000. The total amount of outstanding loans for GB was 96,149 million BDT in 2010 while RDS had an amount of 7,072.02 million BDT (Islamic Bank Bangladesh Limited, 2012; Grameen Bank, 2013). In 2009, the number of branches of GB was 2,556 while RDS was 136. Up until 2009, GB covered 84,388 villages

out of 87,000 villages in Bangladesh while RDS only covered 10,682 villages. The rate of recovery for GB was 97.66 per cent and for RDS it was 99.00 percent (Haque and Yamao, 2011).

GB has improved the income of the people as well as productivity, nutrition and housing. Particularly, the 'Shanirbar Bangladesh' movement helped members to have the second highest average per capita income rise (BDT 623.5). Women members of GB achieved a higher growth of income in general. Agricultural productivity increased for the members after getting loans from GB. Grameen borrowers, on average, acquired improved houses and quality food after receiving loans (Wahid and Hsu, 2000; Sarker, 2001).

H₁ and H₂ state that GB is the best among the interest-based microfinance organizations because, compared to the others, it provides more facilities, e.g. it provides all banking facilities. G₁ cites that GB provides more facilities compared to the others and its members work harder than other micro-credit organizations.

In the case of RDS, Rahman and Ahmad (2010) showed that household income, productivity of agricultural products and animals, spending and jobs had increased dramatically as a result of the money invested. Parveen (2009) indicated that RDS has been earning profit consistently since its establishment. The sustainability of the Islamic microfinance programme of IBBL is satisfactory as its recovery rate is more than 99 percent and its loan portfolio per member, investment and cost per loan is pleasing.

Bhuiyan et al. (2011) concluded that the RDS of IBBL has played a significant role in the socio-economic development and enriching the livelihood of the rural needy people. The funds provided to the borrowers under RDS have been used in the constructive income generating sector. The loan repayment was satisfactory, and RDS was capable of providing services to all types of poor living under the poverty line, including the hard-core poor.

S₁ mentioned that RDS is better than any other micro-credit organization because it is interest-free. It provides more facilities compared to others, i.e. sometimes it provides *qard-hasan*. Moreover, RDS combines both the religious laws with the contemporary financial matters. Finally, RDS emphasizes the strengthening of the relationship between husband and wife in the family. S₄ adds that she prefers RDS because she can practice her religious duties in RDS. Similarly, S₂ and S₃ choose RDS because, firstly, it is interest-free, and, secondly, it has more facilities, e.g. *qard-hasan*. Based on the findings mentioned above, the table 1 summarizes the differences and similarities between GB and RDS.

5. DISCUSSION OF THE FINDINGS

In terms of the organizational structure, it is difficult for RDS to reach the poorest people as the branch offices of IBBL are usually in a rich area where there are many commercial activities. If a village is more than ten kilometres from a branch office then it is out of reach even though there are numerous poor people. In addition, IBBL is a commercial bank. Therefore, its concern forgetting a return on its investment may be a barrier to achieving Islamic microfinance objectives. However, as RDS sometimes gets funding from its 'Islamic Bank Foundation', which is a charity based foundation, it is easier for them to combine charity

work with microfinance. On the other hand, although GB is solely a microfinance institution its concern for getting the returns from the loans is higher than the IBBL. This is because, the interest rate of Grameen is 20 percent per annum while IBBL imposes a fixed profit of 10 percent on the contract price.

Table 1: Summary of the Comparison between GB and RDS

Features	Grameen Bank (GB)	Rural Development Scheme (RDS)
Organizational Structure	<ul style="list-style-type: none"> ▪ Ten members form a group, and eight to ten groups make a centre. ▪ The centres are managed by the branch office. ▪ Branches are opened solely based on the demand of the borrowers ▪ One branch covers 15 to 22 villages. 	<ul style="list-style-type: none"> ▪ Five to six members make a group and several groups make a centre. ▪ A number of centres run under the respective branch of IBBL. ▪ RDS operates within 10 kilometres of the branch office of IBBL.
Funding and Deposit Collection	<ul style="list-style-type: none"> ▪ 90 percent of its loans are from the deposits and interest income. ▪ New branches are opened without taking any central loan. 	<ul style="list-style-type: none"> ▪ RDS is not fully self-reliant as it has to rely on the branch office of IBBL.
Modes of financing	<ul style="list-style-type: none"> ▪ Loan with 20 percent interest rate per annum 	<ul style="list-style-type: none"> ▪ Different modes of financing i.e. <i>murabahah</i>, <i>bay' mu'ajjal</i>, hire-purchase in joint ownership and <i>salam</i> ▪ 10 percent profit fixed rate ▪ A rebate of 2.5 percent for on time payment
Targeting the borrower	<ul style="list-style-type: none"> ▪ Targets the poor with special priority for women. ▪ Women receive 95 percent of Grameen loans. ▪ Criteria for selecting a borrower – whether the woman is a member of another Non-Government Organization (NGO) House ownership Ability to repay the loan Husband's occupation 	<ul style="list-style-type: none"> ▪ Targets the poor family without differentiating between men and women ▪ Criteria for selecting the borrowers – Able bodied and industrious poor People who have cultivatable land or a small farm
Risk Management	<ul style="list-style-type: none"> ▪ Depends on the social pressure of the group members to minimize the default rates. ▪ The centre manager works as the second layer of control. ▪ Saving accounts of the borrowers ▪ The bank's management information system 	<ul style="list-style-type: none"> ▪ Peer pressure of the group members ▪ Savings accounts of the borrowers ▪ Monitoring by the centre manager ▪ Bank's management information system ▪ Mutual guarantee where one person is liable for another. ▪ The wife is responsible for the husband's payment ▪ Islamic religious teaching

Table 1: Summary of the Comparison between GB and RDS (con't)

Features	Grameen Bank (GB)	Rural Development Scheme (RDS)
Marketing	<ul style="list-style-type: none"> ▪ Designs its products based on its customer's needs and goes to the houses of the clients in the rural villages. ▪ Involvement of interest is a hindrance to market them to the clients 	<ul style="list-style-type: none"> ▪ Marketing is limited to ten kilometres from the branch office of IBBL. ▪ It has different types of products to attract the clients. ▪ Being interest-free is an advantage ▪ Frequent distribution of benevolent loans is another advantage
Training	<ul style="list-style-type: none"> ▪ One week training programme before giving loans ▪ Training focuses on educating the members and informing them of the terms and conditions of the loans. ▪ Have a weekly meeting 	<ul style="list-style-type: none"> ▪ Disburses financing after eight weeks training programme. ▪ Training focuses on investments techniques, rules and regulations for the clients. ▪ Have a weekly meeting
Social development	<ul style="list-style-type: none"> ▪ Empowerment of women in the society. ▪ Focuses on the education of the children, better health and nutrition of the members 	<ul style="list-style-type: none"> ▪ Development of the families as a whole ▪ Emphasizes on the education of the children, better health and nutrition of the members ▪ Added some religious teachings to its social development goals and omitted some of the Grameen ideologies that are contradictory to Islamic teachings.
Performance	<ul style="list-style-type: none"> ▪ In 2010, GB's members numbered 8,340,000 ▪ The total amount of outstanding loans was 96,149 million BDT ▪ In 2009, the number of branches was 2,556 ▪ Up until 2009, GB covered 84,388 villages ▪ The rate of recovery was 97.66 per cent ▪ Significantly improved the income of the people as well as productivity, nutrition and housing 	<ul style="list-style-type: none"> ▪ In 2010, RDS's members were 608,703 ▪ The total amount of outstanding loans was 7,072.02 million BDT ▪ In 2009, the number of branches was 136 ▪ Up until 2009, RDS covered 10,682 villages ▪ The rate of recovery was 99.00 percent ▪ Dramatically improved household income, productivity of agricultural products and animals and increased spending and jobs

IBBL has the opportunity to use endowment funds like *waqaf* funds and *zakah* to introduce charity-based microfinancing. In Islam, there are several types of charity mechanisms – *sadaqah*, *zakah*, *waqf* and *qard-hasan*. *Sadaqah* is a general term that includes all kinds of voluntary donations that are not compulsory. *Zakah* is the compulsory prescribed donation on the rich. Two and a half percent of the property should be given to the poor once a year through

zakah. *Waqf* means endowment, which involves donating the physical assets or land property for perpetual charity. Finally, *qard-hasan* refers to benevolent loan, which is given to the needy without any kind of condition, such as interest (Kaleem and Ahmed, 2010; Obaidullah, 2008). Currently, sufficient charity-based modes do not exist in RDS. Only *qard-hasan* is given to a limited number of people. However, the charity-based mode should be extended through *zakah* and *waqf*. Although RDS is a commercial type of microfinancing, practicing the charity is still highly recommended, as it helps the poorest of the poor, and Islamic law highly recommends this mode of financing (Kaleem and Ahmed, 2010).

In the case of debt financing, RDS usually charges a 10 percent mark-up, which is a fixed contract price, while for profit sharing financing, RDS usually shares the profit of between 30 to 40 percent. In contrast, GB charges a 20 percent interest rate, which is very high and even higher than the commercial banks in Bangladesh. In Bangladesh, the interest rate for commercial banks is around 7 to 8 percent (Bangladesh Bank, 2012). This is a big burden for the poor people to repay the loans with this high interest rate from a small business. Moreover, the payment is on a weekly basis. This is another problem for the borrowers since it is very hard to get a return from a small business within one week. In some cases, the borrowers need to take a loan from others to repay the GB loan. Therefore, the loans from GB may exacerbate the poverty.

GB's method of mostly targeting the women is questionable. One field research shows that most of the women borrowers of GB are not the immediate beneficiary of the loans. They merely work as an intermediary to get loans on behalf of their husbands (Selinger, 2008). Therefore, women may face more problems in this case as the husband may not use the money for the specified investment. Therefore, empowering women economically may not succeed through this method. In addition, a number of poor men who are single would be excluded from GB's method. Although Khandker (2012) finds that women face a lower credit risk than men in GB's lending, men can still influence women based on the existing social structure in Bangladesh. Therefore, women can default as a consequence of being the intermediary of their husbands.

Furthermore, although the primary objective of giving loans to women was to empower them, Naher (2005) argues that the activities that women are involved in with the non-government organizations including the micro-credit organizations, i.e. GB, can barely free them from the gender inequality that they are facing in the society. Memorizing a few mottos and learning how to sign as a requirement to get a loan cannot really empower them in the society. Instead, changing the attitudes and gender relationships in the family and society can empower the women. Accordingly, we would like to argue that the empowerment of women would be more effective if the micro-credit organizations target the family as their borrowers rather than only targeting the women. This is because changing the attitudes and gender relationships can be done more fruitfully by teaching both men and women about their rights and responsibilities.

Concerning the risk management factor, RDS has to share profit and loss with the clients as it practices some Islamic modes of investment, such as *mudarabah* and *musharakah*. In these contracts, monitoring by the field officers and the sincerity of the clients are essential tools for risk management. However, the debt based contracts, e.g. *murabahah* and *bay' mu'ajjal*, are less risky than the partnership contracts. Therefore, RDS mainly uses *murabaha* and *bay'*

mu'ajjal contracts. Nevertheless, ultimately, RDS's risk is higher than that of GB as they are practicing Islamic risk sharing contracts.

Pertaining to the profit and loss sharing contracts, it is recommended that RDS should increase the income sharing ratio with the clients. Currently, the income sharing ratio for the client of RDS is 30 to 40 percent. However, to make the ratio fairer it can be 40 to 50 percent. Accordingly, the clients would be more encouraged to join the profit and loss sharing businesses. According to El-Din (2008), usually, economically weaker parties are at a disadvantage in profit and loss sharing business as they share a small income ratio while sharing a similar amount of risk. Therefore, a fair and balanced income sharing ratio between the RDS and its clients should be practiced.

GB's marketing is more effective than RDS in the sense that GB designs its products based on its customer's needs and then goes to the houses of the clients in the rural villages to market the product. Each GB branch is established based on the response of the clients. GB has become very sustainable as they give financing after they have received deposits from the clients. However, due to the involvement of interest it is a hindrance for the officers to market the GB products. On the other hand, RDS's marketing is limited to the nearest branch office of IBBL. They cannot go beyond ten kilometres from the branch office (Islamic Bank Bangladesh Limited, 2012). However, RDS has different types of product compared to Grameen. RDS introduced different risk sharing joint-venture products along with the debt financing. Therefore, RDS has more potential to attract the clients. Moreover, many choose RDS as it is free from interest. Khan et al. (2007) found that a number of Bangladeshi customers choose Islamic banks because they are based on Islamic principles. Therefore, this is an advantage for RDS to reach out to the customers. In addition, RDS's Islamic benevolent loans attract a number of clients (S_1, S_2, S_3, S_4).

It is a praise worthy aspect for GB that it contributes to educate people through training programmes even though these are very short. The weekly meetings of GB and RDS are very important as they provide the members with the necessary knowledge about the investments, repayments procedures, rules and regulations of the organization. However, RDS is more acceptable to Muslim customers as it contributes to developing the Islamic moral teachings and practices among the members. In contrast, some of GB's teachings are contradictory with the noble teachings of Islam, i.e. keeping the family small. Therefore, it may hinder GB in reaching the devoted Muslims in Bangladesh.

With regard to the growth of RDS, it has fewer members because it is newer than GB. GB was founded in 1983, while RDS was introduced in 1995. As Grameen has a higher number of members it is a challenge for RDS to grow as it has to compete with the giant. However, although the coverage of RDS is very small, it is performing pretty well as it has a satisfactory loan recovery rate and is contributing considerably well in the socioeconomic development of rural poor people. One distinguished performance of RDS is that it gives credit in kind and not credit in cash. Therefore, it is ensured that the credit is properly utilized and not transferred to other family members or relatives. For instance, there are some incidences in conventional microfinance where borrowers utilized the loans for some ineffective matters (Parveen, 2009). Consequently, they once again needed to borrow money from the moneylenders to pay the weekly repayment, which eventually created a worse scenario both for the borrowers and the microfinance institutions.

6. CONCLUSION

GB has a greater micro-credit coverage compared to the RDS of IBBL. However, while GB only provides loans based on interest, IBBL implements different types of financing to avoid interest as it is prohibited in Islamic law. Although RDS is newer and smaller than Grameen, it might be more effective in terms of empowering the poor families in the rural areas as it targets the family instead of just targeting the women member of the family. In some cases, Islamic micro-credit is more effective than Grameen as it gives credit in kind. However, GB's marketing strategies are stronger than RDS and it is more self-reliant than RDS. Both GB and RDS contribute to the socio economic development of their members through their training programs. However, RDS contributes further through developing Islamic moral teachings and practices among the members.

The study suggests that RDS should expand its coverage. Rather than running under a separate scheme like RDS, IBBL should establish a microfinance subsidiary organization that can work freely. Then, it will be easy for the subsidiary organization to reach the poorest people in the rural areas. Moreover, RDS should improve its marketing strategies to compete with GB. This can be done by going directly to the customers' houses and explaining the importance of Islamic microfinance and the harm of interest-based microfinance. Along with this, RDS should expand charity-based Islamic microfinance, which will be done through the collection and distribution of *zakat* and establishing a *waqf* fund. The *waqf*-based micro-financing would be a powerful tool to reach the poorest of the poor. This mode will be more effective to develop the socio-economic status of the people in Bangladesh.

In addition, GB should use the credit in kind to be more effective. Therefore, GB can implement different financing modes rather than just giving loans with interest, e.g. *salam* financing, selling a commodity on a deferred basis. Furthermore, GB can target the families as the potential borrowers rather than targeting women only, as it will improve the efficiency of their credit and minimize credit risks. Finally, GB should minimize the interest rate, because, in many circumstances, it may exacerbate poverty rather than help in its eradication. This may ultimately go against the socio-economic development agenda of the government of Bangladesh.

This study is a qualitative examination on the operation of GB and RDS. Further research can be carried out on examining a few issues i.e. the effectiveness of credit in kind for microfinance institutions, issues and challenges for credit in kind, and the effectiveness of targeting the family as the loan-recipient instead of only the women member of the family.

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