

INNOVATIONS IN ISLAMIC MICROFINANCE: LESSONS FROM MUSLIM AID'S SRI LANKAN EXPERIMENT

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Abstract

This paper seeks to highlight the need for creativity and innovation in poverty alleviation efforts using Shariah compliant mechanisms. Contemporary mechanisms in use by mainstream Islamic banks and financial institutions may indeed be grossly inappropriate in the context of local economies and for financing micro livelihood projects. Arguably, poverty alleviation efforts cannot be viewed similar to commercial transactions where an Islamic MFI seeks to provide a mix of services that include hand-holding and other forms of support to its client (which is often a loose group/ association of poor people). While some of its operations may involve for-profit transactions governed by sustainability concerns, the overall objective is benevolent and strictly not-for-profit. The present paper seeks to document a case study of Shariah-compliant microfinance undertaken by Muslim Aid in Sri Lanka to highlight the need to move beyond the "popular" Islamic banking instruments and to search for appropriate solutions. This study on financing paddy cultivation for impoverished and displaced farmers is demonstrative of one such innovative solution, that is also Shariah compliant, involving use of value-based *salam* and *mudharabah*.

1. Introduction

Microfinance for the poor has few similarities with banking. The well-known Grameen model according to its founder is exactly the opposite of the conventional banking methodology (Yunus 2008). This model is characterized by absence of any collateral, of any legal instrument between the lender and the borrower, any provision to enforce a contract by external intervention, such as, a court of law, or any transfer of liability to family members in case of death of a borrower. While models of microfinance vary in terms of exact features, they are invariably characterized by an overwhelming concern for the welfare of their members and clients. Profit seeking is seen as a means to ensure sustainability and not as end in itself. While

Shariah distinguishes between commercial and benevolent transactions and provides an elaborate framework for both kind of transactions that would ensure their freedom from *riba*, *gharar* and other prohibitions, some activities of microfinance institutions may not even involve contractual arrangements and stipulations and would call for a benevolence-driven framework rather than a prohibition-driven framework.

Where contracts form the basis of activities of microfinance institutions, the distinction between microfinance and commercial banking should be clearly recognized in product development efforts. Many of classical Shariah-nominate contracts have been modified by contemporary Islamic jurists to suit the needs of mainstream commercial banks. Arguably, these commercial banking products may not be appropriate for microfinance, given the points of difference between the two. Islamic microfinance product development would be a natural response to the unique needs of this sector, even while this remains a major challenge for this sector (Obaidullah and Khan 2008). A recent study by CGAP (Karim et al 2008) indicates that the industry lacks a profound degree of product diversification and most firms offer only one or two *Sharia*-compliant products. Another recent study (Obaidullah 2008) on microfinance in three IDB member countries, Turkey, Bangladesh and Indonesia notes that while there may be a multitude of Shariah-compliant modes of microfinance, it is important to take note of their comparative features to identify the ones that are practically and operationally more suitable than others. The present study captures these concerns, demonstrates the case of an innovative microfinance product being used successfully in Sri Lanka and highlights the richness of classical Islamic legal framework in providing such innovative solutions.

Bai-salam or *salam* sale is a deferred delivery mechanism. The classical *salam* has been used primarily as a financing mechanism for the agricultural sector under which farmers would receive the price of the produce in advance at the beginning of agricultural season against an obligation to deliver a defined quantity of the produce to the buyer after a definite time period in future (after harvest). The sale price received in advance is thus available to the farmer as a means of financing all farming related needs. Another advantage is that the farmers do not have to sell their produce at a time when the market has an oversupply due to harvest, thus depressing the prices and bringing down the realized income of farmers. While the mechanism provides for

much needed financing, it is subject to abuse by unscrupulous middle-men and traders who seek to take advantage of low bargaining power of the poverty-ridden farmers and execute *salam* at unrealistically low prices. To counter this, mutuality-based models of microfinance have been suggested. Farmers' cooperative organizations can dramatically enhance the bargaining power of farmers and replace middlemen. In a *salam*-based framework, these cooperatives would provide funds in the form of advance price and would take delivery of the produce after harvest as above. The cooperative would also create appropriate warehousing facilities for storage of the produce and market the same in a manner that avoids depressed prices resulting in increased income for the members. It may be noted that an act of seeking to even out supply to counter exploitation should be clearly distinguished from the evil practice of hoarding or creating artificial scarcity in the market. Recent experiments of *salam*-based financing by Islamic banks has not been very successful however. El Zahi (2002) documents the predicament of Sudanese Islamic banks extending *salam*-based financing to farmers in the form of advance sale prices only to witness large-scale diversion of funds away from intended use in farming and defaults at the time of delivery of the produce at harvest time. Another problem with classical *salam* for the financier arises out of its exposure to price risk or market risk. A financier who is not an astute player in the market for the concerned commodity and does not fully understand the economics of pricing in this market may be confronted with adverse prices and consequent losses when it seeks to sell the produce upon delivery by the farmer(s). This problem is taken care of in value-based *salam* as the case study highlights. The present case study is believed to be the first documented application of value-based *salam*, a creative variant of classical *salam* in the context of Islamic microfinance. The innovation enables a financier to hedge the risk of volatile agricultural prices associated with the classical *salam* sale.

Recent economic trends in Sri Lanka have discouraged paddy cultivation, paving the way for rice imports which is the main staple food of Sri Lankans. This paper outlines a model developed and piloted by Muslim Aid Sri Lanka based on a combination of two Shariah-based modes – *salam* sale and *mudharabah* partnership - to empower poor paddy farmers from Sri Lanka. The model was developed in order to reduce the dependence and consequent exploitation of the poor farmers by financier-middlemen through high-interest loans and artificially depressed market prices during harvesting season due to over-supply of agricultural produce.

2. Project Overview

The Sri Lankan agriculture sector has a long history of subsidies, government interventions and local food security measures. It is characterized by a decline in paddy cultivation over the last few decades. This is attributable to several reasons, such as, lack of productivity, lack of sufficient income in the sector, increase of production cost and above all, the ethnic conflict. These reasons may be interrelated. Therefore any rational response to this must involve a holistic approach. An average Sri Lankan farmer owns not more than 2 acres of paddy land. The only available financing option before him is to either pawn household assets, such as, jewelery or mortgage the paddy fields with money lenders (often the middle men) with the hope of paying back the loan with interest after harvest and perhaps redeeming the mortgaged property. Therefore, should there be a crop failure, the mortgaged property would be lost. Indeed, there have been incidents of farmers resorting to suicide on being unable to pay the debts. Moreover most middle men bargain to purchase the crop at a very low price and the farmer usually has no other option but to sell it to these middlemen. In addition mill owners also have to take loans from banks in order to purchase the paddy to process and sell on the market. This is normally given at a high interest rate. The farmer is therefore, caught in a vicious cycle of poverty. While the government of Sri Lanka has initiated several programs in the past to enhance the paddy cultivation through fertilizer subsidies, renovating irrigation systems and even cheaper microfinance loans, these have repeatedly failed to have the desired impact. The suggested model emphasizes on 'farmer participation' throughout the process as a 'cooperative' or 'association' to increase the bargaining power of the individual farmers and also to get a better value for their efforts.

Muslim Aid (MA) used a multi-stage model for provision of finance and other inputs to the farmers. The first stage involves a creative variant of the classical *bai-salam* or "deferred delivery" transaction. Under this mechanism, a farmer was provided funds in advance against a forward sale of his produce at the time of harvest. The funds were used by the farmer to finance purchase of the necessary inputs to start paddy cultivation. Unlike bank financings, no collateral was required from the farmer. Instead, a farmer needed to obtain a set of recommendations from the local mosque and community leaders who acted as guarantors.

The second stage began at harvest time once the agricultural produce was delivered to MA. It involved a partnership between MA and local miller(s) to take possession of the harvested paddy from the farmers, process it and sell the final product at the market with the profit being shared between MA and the miller(s) on the basis of a *mudharabah* partnership.

It was expected that the profit share of MA would cover the administration cost of the financing. In order to ensure that the over-all model was a not-for-profit one and that it was also sustainable one, any surplus of profit share over administrative cost was to be used to create a Revolving Fund for the farmers (See Figure 1). Farmers enjoying incremental income were also expected to make *zakah* contributions to this Fund and therefore, adding to its size and ability to provide financing to greater numbers. This was the third stage of the model.

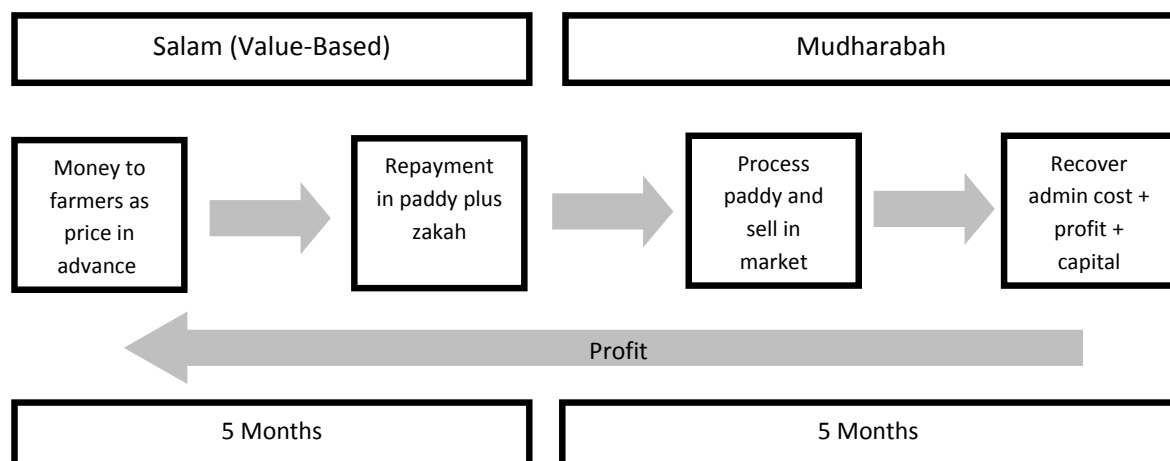


Figure 1: Overview of MA Model

3. Application of the Model

When the Asian Tsunami swept across the Indian Ocean in 2004 it killed more than 200,000 people and washed away the livelihoods of hundreds of thousands of people in the region. After this devastation very little progress was made in terms of constructive livelihood regeneration to elevate people's lives to the pre-tsunami period. In Sri Lanka in addition to this,

the ethnic conflict has made any reconstruction effort extremely difficult. Muttur is one such area which was a victim to both Tsunami and ethnic conflict. The Muttur division is based in the North east of Sri Lanka and is a part of Trincomalee district. Before the Tsunami and at the time of the conflict there was a near absence of manufacturing industries, small trade and service sectors to cater to the basic needs of the local population. Economic activities were based more on fishing, livestock and agriculture with the agriculture and fishing sector being badly affected due to security issues. The most severely affected by Tsunami were people in the lowest income strata who had no stable assets or means of income generation (Muttur DLDP Report 2006).

In August 2006, around 50,000 people were displaced from Muttur following a deterioration in security. For about six weeks, these people were refugees. As the region regained normalcy with improvement in security situation, these people returned and tried to restart their lives. In addition to this, for the first time in about 20 years, much of Muttur and surrounding villages had been cleared of rebel activity and were being repopulated, thereby opening the door for economic activity. There arose an opportunity to re-cultivate land that had been previously abandoned due to the conflict. The returning refugees found themselves strapped for cash as they looked for ways to get back to normalcy. This model was devised in response to the need and tested with two associations: the Jaya Farmers' Association and the Knox Farmers' Association during the 'Maha' season (October to February) 2006-07. While the model was experimented on cultivating paddy on irrigated as well as rain fed lands, it may also be applied to other crops and vegetable cultivation. It is believed though that the capacity and the credibility of the farmers and/or their associations would play a major role in the success of the project.

The Jaya Association cultivated 177 acres of paddy with 84 beneficiaries on irrigated lands, whilst the traditional method (rain fed lands) was implemented with Knox Farmers' Association to cultivate 150 acres of paddy benefiting 83 farmers. Due to the differences in farming methods, cost differences did occur between the processes.

3.1. Cost of Inputs

This included preparation and crop maintenance costs. The calculations were based on per farmer /per acre. The preparation costs included cost of seed paddy, fertilizer, and labor and

tractor charges for ploughing. The rain fed lands (Knox farmers) were ploughed two week earlier than the irrigated lands. Hence they were disadvantaged in getting subsidies in fertilizer and seed paddy due to the delay in government distribution of subsidies. Therefore the average preparation cost of rain fed land (Knox) was 33% higher than irrigated (Jaya) lands. However the maintenance cost of irrigated land was 30% higher than the rain fed lands. Most of the maintenance cost was for additional fertilizer and supervision costs. Therefore the total cost of production did not indicate drastic differences between the two (see table 1). Nevertheless it can be seen that the provision of financing to start the process is essential and productive.

As discussed above, the transactions were done in two stages. The first stage was a *salam* transaction which was in the form of provision of financing of about Rs 3.9 million (\$ 39,000) to the two farmer associations. These associations in turn provided loans in cash and kind to their members to help them purchase the necessary accessories to allow them to restart their farming. The money was used for hiring of the tractors, expenditure for fertilizer and agrochemicals, expenditure for seed paddy and labor charges (other than the farmer and his family). The work consisted of land preparation, distribution of the fertilizer, the sowing of the seed and the harvesting of the paddy.

Cost of Production per farmer /per acre in Rupees	Jaya	Knox
Seed Paddy	2,823	3,375
Fertilizer	3,390	3,700
Labor		4,500
Tractor Charges	3,390	3,750
MA Contribution	9,603	15,325
Farmer Contribution	12,000	9,500
Total Cost	21,603	24,825

Table 1: Comparative Cost of Inputs

3.2. Output and Repayment

Both the associations claimed some crop failures. However Jaya farmers received a relatively better harvest and hence found it easier to fulfill their commitment regarding delivery of produce. The average yield per acre was 30 and 40 bags (each bag consists of 69kg paddy) for Knox and Jaya farmers respectively. The Knox Farmers Association was unable to deliver paddy due to the crop failure and management issues. The Jaya Farmers Association was able to do so. While the total paddy production of Jaya farmers was estimated around 7080 bags, MA recovered 1351 bags or 16% of the yield. The farmers repayment also included a component of voluntary *zakah* payment (depending on the total harvest received), which was paid to the association, which subsequently was passed on to MA.

The second stage of this project entailed an arrangement between a miller and MA on the basis of a *mudharabah* partnership. The mill owner was recommended from the community and a legal agreement was entered into whereby he would proceed to mill the paddy (that MA had received) and sell the processed paddy at a higher rate (as the price had now increased since harvest time). The financial contribution of MA to the *mudharabah* enterprise was in the form of paddy as *mudharabah* capital plus the processing costs as a *qard* loan. Profits from the business (after repayment of *qard*) were to be shared between both MA as *rabb-al-maal* and the miller as the *mudharib* on an equal basis. Finally in the third stage, after taking back the equivalent of their financing and part of the operational costs, MA then voluntarily proceeded to donate its share of profits to the farmers' associations. All of this was done in a ten month cycle. This can be explained further with a simple working example as follows.

3.3. An Example

1. Farmer X wants to cultivate 3 acres of paddy.
2. He needs money to prepare and till the land.
3. He intends to take a loan for tilling, fertilizer and seed paddy.
4. Likewise if there are other farmers within his association who would like to take a similar loan, the association will itself apply for the loan on behalf of the farmers.

5. The association can approach banks or in this case it will apply to MA for financing.
6. Assessing the capacity and need, MA will come to an agreement with the farmers association. The amount of financing is agreed so as to pay for tractor charges, seed paddy and fertilizer whilst the farmer provides the labor costs. Some of the tractor charges are kept for expenses related to machine use during harvesting.
7. MA gives the money to the association and the goods and services are procured by the association and disbursed in kind to the individual members.
8. Hence farmer X will get his share of Rs 8470 worth seed paddy, Rs 10,100 worth tractor charges and another Rs 10,100 worth fertilizer in kind as a loan from the association based on his need. Hence his loan from MA is Rs 28,670.
9. If the harvest is successful, a minimum of 40-60 bags of rice will be the output per acre. Therefore, a 3 acre land should yield a minimum of 120 bags (40 x3). If the value of each bag is Rs. 900 (approximately \$9), the total value of the yield (120 bags) will be Rs 108,000 (\$1080).
10. However with mutual agreement with the farmers, MA will receive as a loan repayment in kind, paddy at a value of Rs 1000 (\$10) per bag. Hence for farmer X, he will need to repay his loan of Rs 28,670 which is the equivalent of 28.67 bags.
11. This paddy is now given to the miller on a 50/50 profit sharing basis.
12. Normally the milling cost will be about Rs 100 (approximately) per bag with the miller normally taking a loan (with interest) to purchase and process the paddy into rice, which he then proceeds to pay back after selling the rice. Hence for 28.67 bags it would cost approximately Rs 2867 to process.
13. Processing / milling 28.67 bags of paddy will give on average 1260 kg of rice. If it is sold at Rs 32 (price as in May, 2007 against the current market price of Rs 65 per kg) the total turnover will be Rs 40,320.
14. The cost of production (investment from MA + processing costs) is Rs 31,527. Therefore the profit (turnover – cost of production) is Rs 8800 (approx). MA and the miller will share a profit of Rs 4400 each. This is sufficient for MA to cover the operation cost of the project.
15. If all farmers have paid back the loan, a percentage of profit may go to them when MA passes on the surplus to the farmers' association to strengthen its funds position and

which can be subsequently used to meet basic needs of its members.

3.4. Impact of the Model

The experiment was conducted in a post conflict/ disaster situation. This is a common practice among development agencies in such a situation to give grants to farmers. Certainly the farmer needs capital to start cultivation and grants or loans from agencies would encourage the farmer to cultivate. However, MA believes that grants may increase 'dependency syndrome' as the farmer will continue to seek subsidies and grants to cultivate. But with the present model, a revolving fund can be established from where the farmers can continue seeking loans for cultivation with an assurance of repayment. This will empower the farmers association to be self reliant and also the farmer to engage and lobby collectively for better outcome for his efforts.

Ideally from an Islamic perspective, farmer should use his own resources before he seeks a loan. This means the farmer should save for the upcoming season. In order to save he needs to get enough profit to reinvest. Hence a better price for his paddy is needed. A way to get a better price is to lobby as an association rather than individuals. The proposed model facilitates the association to become a lobby in the long run to ensure a fair deal to the farmer. Moreover this model brings the middle men (some of the millers) to a win-win situation too. Thus, the model encourages local millers to buy paddy, which not only increases local economic activities but also increase local food security.

The model does not intend to distort market prices. However the model expects to build capacity of the farmers to have a better bargaining position. This may result in increase in market prices of paddy which is in favor of the farmer. However as there is no fixed price for paddy the market demand and supply will determine the price. Moreover, unless the model is practiced by the majority it is unlikely bring a major impact on the price of paddy at macro level.

The model emphasizes on a cooperative structure of operation throughout the cultivation process. The decision making is done through the association with periodic meetings. This model has a potential to become a strong bargaining platform for subsidies, selling price and other

services and facilities. Further, it is anticipated that farmers' associations could become self-reliant within five years or nine financing cycles.

Though in the experiment a component of *zakah* distribution was included it was not very successful. However future projects can include a collective *zakah* component that will benefit the community at large.

4. Shariah Issues

As is clear from an analysis of the project, the composite model can be viewed as comprising three distinct components or stages. The first stage involves organizing the farmers into a cooperative/ association and provision of financing to the cooperative on the basis of *bai-salam*. The association as a mutual entity in turn extends *qard-hasan* loans to its members to finance their farming related needs. The second stage involves a *mudharabah* partnership of the microfinance institution (MFI) with miller under which the former provides *mudharabah* capital in the form of paddy and the miller performs the role of manager or *mudharib*. MFI also provides funds for covering the processing cost through a *qard* loan that is recovered before profits are calculated and distributed between both parties as per pre-agreed ratio. Thus there is creation of additional value or wealth and its equitable sharing among both the parties. A for-profit mechanism is combined with not-for-profit financing to provide sustainability to the overall model. In the final stage MFI donates the surplus if any, back to the farmers' cooperative to create a Revolving Fund to cater to basic needs and provide a safety net to members. The farmers themselves contribute *zakah* to the Fund from their augmented income. The Fund is expected to mature into a Takaful Fund that can provide micro-*takaful* to its members against unforeseen adversities on an on-going basis.

4.1. Conditions for Shariah Compliance

In a composite model as above the first and foremost requirement for Shariah compliance is that the terms of the contracts must be clearly and objectively stated and understood by the parties and there must not be any element of interdependence between the contracts. It is

important to move from verbal arrangements (that is quite common in a rural setting of a micro-economy) to written contracts. Each contract must be independent of the other in terms of rights and obligations of the parties. For example, if the MFI dons two hats - of a *rabb-al-maal* (capital provider) in the *mudharabah* partnership - and of a lender to the *mudharabah*, the rights of MFI being repaid the *qard* loan amount in full is independent of its share in profits or losses.

The cooperative organization is a voluntary association of farmers who become members by contributing a membership amount that should ideally be viewed as a *tabarru/ sadaqa* or a voluntary contribution to the Fund and not charged as a fee against various services provided. This is important if the association plans to undertake *takaful* in future on a cooperative and not-for-profit basis to its members.

When the cooperative extends *qard hasan* loans to its members, the contract must be free from any conditions, such as, mandatory payment of *zakah* to the Revolving Fund or payment of any other benefit in kind along with their repayment.

4.2. A Shariah-Compliant Innovation

The MFI in the present case extends financing to the cooperative entity based on a value-based *salam* contract. Therefore, it is important here to highlight the difference between classical *salam* and the "value-based" *salam* and examine the Shariah basis of the latter. In a classical *salam*, the quantity of object of sale (agricultural produce), the price per unit of the object of sale are pre-determined at the time of contracting. If Q amount of paddy is sold on forward basis at price P on *salam* basis, then the financier (buyer) would pay the value of transaction PQ to the farmer (seller) at the time of contracting (before commencement of farming). After a defined and known time period (harvest time), the farmer would deliver Q amount of paddy to the financier. The financier in turn, would find a way to dispose of Q amount of paddy in the market at the prevailing market price P*. If market price increases during the financing period, P* would be higher than P. In other words, P*Q would be higher than PQ and the financier would have positive profits (P*Q-PQ). If however (and this is quite likely given the abundant supply of produce during harvesting season) the prevailing market price is depressed and P* is lower than

P, the financier would end up with losses. The value of $P^*Q - PQ$ would be negative.

This market risk or price risk is mitigated in case of a value-based *salam*. In the latter type of *salam*, the MFI would pay an amount (say V) to the farmers' cooperative at the time of the contract against an obligation of the farmer to repay in physical quantities of its produce whose value at the time of delivery at a future date (after harvest) is pre-determined (say V^*). In other words, the farmer would deliver V^*/P_1 quantity of paddy to the MFI if the future price at the time of delivery is P_1 ; V^*/P_2 quantity of paddy if the future price is P_2 and V^*/P^* quantity of paddy if the future price is P^* . This settlement value (V^*) may indeed be in excess of the original value (V) received in advance by the farmer resulting in a known profit ($V^* - V$) to the financier. This form of contracting is not commonplace and is erroneously questioned on twin grounds of (i) violating the condition of pre-specifying quantity and object of sale as in classical *salam* and (ii) suspicion of *riba* as the transaction appears dangerously close to cash-for-cash resulting in pre-determined profits.

Suweilem (2007) advocates the use of value-based *salam* as a Shariah-compliant hedging device. While noting the approval of scholars like Ibn Taymiah to value-based *salam*, Suweilem cites the following reasons why value-based *salam* should be accepted as a valid and Shariah compliant product. One, the condition of pre-specifying quantity of produce to be delivered is essentially to avoid possibility of conflict between parties. In value-based *salam*, no such possibility exists. Two, the mechanism neither involves *riba* in form, nor in substance. The buyer in this case receives commodities and not money. Hence, this is not tantamount to cash-for-cash. Indeed the mechanism is exactly equivalent to *murabahah* where the MFI would buy spot and sell on a deferred basis for a mark-up. In value-based *salam* the MFI buys on a deferred basis and sells spot. The only difference is the sequence of steps.

It follows from the above that value-based *salam* would result in pre-determined profits for the MFI that could be further augmented through *mudharabah* in the subsequent phase. An MFI seeking profits as a means of achieving sustainability may opt for this model. The case of MA is however different as it seeks moderate profits only through *mudharabah* with the millers in stage two and not through *salam* with farmers in stage one. Muslim Aid (MA) in the present

case ensures that *salam* is undertaken without any element of profits. In other words, for MA, $V=V^*$. The farmers collectively would deliver PQ/P^* quantity of paddy to the MFI. By ensuring equality between funds that MFI originally provided to farmer and what it received later, value-based *salam* enables the MFI to hedge the price risk associated with classical *salam*. MFI essentially receives back the same amount of funds it provided to the farmers in the beginning and it is easy to see the similarity of this mechanism with a simple *qard-hasan* loan that is repayable at par on maturity without any increment. However, they are not same. A merit with *salam* involving physical produce as compared to a *riba*-free financial loan is its effect on market prices that tend to be depressed during harvest. As the case demonstrates, MA in the process of settlement of the transaction is able to intervene in the market with a settlement price that is more fair to the farmers.

5. Summary & Conclusion

Islamic microfinance, as the case of MA financing of paddy cultivation in Sri Lanka demonstrates, is often a composite mechanism that involves benevolent intervention. Such intervention by an Islamic MFI may use a complex web of contracts that may be based on donations, loans, trade and partnership. However, it is extremely important that all contracts – not-for-profit and for-profit – are independent of each other with the rights and obligations originating there from clearly understood by stakeholders. Models of microfinance may vary in terms of exact features, but they are invariably characterized by an overwhelming concern for the welfare of their members and clients. Profit seeking is seen as a means to ensure sustainability and not as end in itself. It follows from the case study that some activities of microfinance institutions may not involve contractual obligations, as exemplified by the overwhelming concern of MA to take care of the safety needs of the poor farmers, to build a sustainable source of funds for them as a cooperative organization and to free them from exploitation by trader-middlemen by intervention through the market mechanism. MA also seeks to create a win-win situation for the trader-middlemen by forming a partnership with them. Needless to say, the ultimate objective of an Islamic MFI is benevolence and benevolence alone. Profits are a means to achieve benevolence that sustains itself and not an end in themselves.

The study also highlights the need to move beyond the "popular" Islamic banking instruments, such as, *murabaha* and to search for innovative and appropriate solutions. This study on financing paddy cultivation for impoverished and displaced farmers is demonstrative of one such innovative solution, that is also Shariah compliant, involving use of value-based *salam* and *mudharabah* in a benevolence-driven framework as distinct from a prohibition-driven framework. Of course, the framework remains free from Shariah prohibitions relating to *riba* and *gharar*. The study also highlights the need to develop the institutions of *zakah* and perhaps cash *waqf* and integrate them with microfinance.

Islamic MFIs should practice inclusive microfinance. The beauty of the MA model is that it addresses the needs of all stakeholders - the farmers as well as the millers - and therefore should encourage an interest in agriculture contributing to food security. A mutuality based cooperative model of organizing the farmers is seen as the preferred alternative to improve their bargaining power on the one hand and to ensure proper end use of funds on the other. Of no less importance is the need to do away with dependence of the farmers. Dependence, whether on government grants or on *zakah* is incompatible with true empowerment. A holistic approach to livelihood development that includes the use of market mechanism as the tool of intervention as demonstrated in the present study should lead to desired outcomes.

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