

# Al-Mubadarat Al-Riyfiah: An Islamic finance product for the underserved segment and the third sector of the economy

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## ABSTRACT

This paper presents *al-Mubadarat al-Riyfiah*, an innovative Islamic financing product designed to serve the marginalised segment and the third sector of the economy. This paper aims to address the disparity in Islamic finance by emphasising inclusiveness and collective economic well-being. *Al-Mubadarat al-Riyfiah* adopts a group-based approach and focuses primarily on the real business sector, aligning with the principles of value-based intermediation (VBI) in Islamic financing. The primary objective is to provide sustainable financial services to households at low income levels, serving financial needs that often fall within the range of approximately RM500 to RM1000 (approximately US\$125-250). The initiative seeks to reach an estimated 40 million households worldwide. This initiative not only addresses the pressing issue of financial inclusion but also contributes significantly to the evolution of Islamic finance. It represents a pioneering effort to integrate underserved populations into the economic mainstream while upholding Islamic finance principles. The study's unique contribution lies in its potential to reshape the landscape of Islamic finance, foster shared prosperity, and provide a model for sustainable development.

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## 1. Introduction

The genesis of *al-Mubadarat al-Riyfiah*, the innovative Islamic finance product proposed in this paper, emerges from a critical observation and the imperative to address a pressing issue within the field of Islamic finance. This observation pertains to the longstanding challenge of fostering financial inclusion and shared prosperity, particularly among two distinct but interconnected segments of the population: the underserved segment and the third sector of the economy.

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The works of renowned scholars like Rusni Hassan (2020), whose call for reform in Islamic finance resonates deeply, highlight the urgency of addressing these interrelated issues. Hassan's insights illuminate the need for a paradigm shift—a shift that aligns with the principles of inclusivity, shared prosperity, and authentic implementation of Islamic finance—beyond mere theoretical discussions. In parallel, scholars like Ayub (2020) and Mustapha (2020) have echoed the imperative of Islamic finance effectively catering to these segments. Their scholarship amplifies global development objectives, including eradicating extreme poverty by 2030 and elevating the living standards of the world's bottom 40 percent.

Moreover, this paper introduces *al-Mubadarat al-Riyfiah* as a tangible response to these challenges. It serves as a catalyst for Islamic banks to integrate the underserved segment and the third sector of the economy, paving the way for a society characterised by shared prosperity. *Al-Mubadarat al-Riyfiah*, built on the foundations of interest-free finance, seeks to promote financial inclusion and guarantee a minimum standard of living for the vast population within the Muslim world.

The proposed initiative, *al-Mubadarat al-Riyfiah*, will give operational-level options for the future growth of the direct microfinance portfolio. This will help improve the overall performance of Islamic banks and support ongoing efforts to strengthen and improve Islamic finance practices, especially in the area of microfinance. It aims to align with the ongoing efforts to strengthen and improve Islamic finance practices, particularly in the area of microfinance. Furthermore, Islamic banks currently serve the small, medium, and agribusiness market layers, which also attract the attention of other banks offering similar services. However, when it comes to the bottom layers of the rural microfinance market, the potential outreach is significantly larger, while the number of financial service providers is limited, resulting in a significant demand-supply gap. Considering the reform agenda of Islamic banks, expanding their services to the bottom layers of the economy holds greater potential compared to focusing solely on the upper tiers. This rationale supports the pilot implementation of the proposed *al-Mubadarat al-Riyfiah* model as an additional step towards increasing outreach in the rural microfinance market. By tapping into the underserved segment of the economy, Islamic banks can leverage their comparative advantage and contribute to narrowing the financial inclusion gap in rural areas.

## 2. Literature review

The exploration of the role of *Shukuk* as a financing instrument for SMEs through the lens of the Resource-Based View (RBV) theory by (Zakzouk, et al. 2023) holds great relevance to the proposed Islamic finance product. This innovative finance product is designed with the specific aim of addressing the financial inclusion and shared prosperity challenges faced by two interconnected segments of the population: the underserved segment and the third sector of the economy. The RBV theory, traditionally applied in larger organisations, offers a compelling theoretical framework for understanding how *al-Mubadarat al-Riyfiah* can bridge the financing gap in the underserved segment and support the third sector. Access to finance, a key concept in RBV theory, highlights the acquisition of critical resources as a determinant of firm performance and growth. In this context, the theory is adapted to elucidate how *al-Mubadarat al-Riyfiah* serves as a strategic resource for Islamic banks to bolster their performance in supporting these marginalised segments. The underserved segment, composed of individuals and households earning less than US \$2 a day and largely excluded from conventional banking due to the prohibition of *riba* (interest), represents a critical resource pool that, when empowered through innovative finance products like *al-Mubadarat al-Riyfiah*, can contribute significantly to overall economic development.

Furthermore, the third sector of the economy, comprised of non-profit organisations, cooperatives, and community-driven initiatives, holds immense potential for socio-economic development. Leveraging *al-*

*Mubadarat al-Riyfiah's* innovative financing mechanisms can provide these entities with the financial resources needed to amplify their positive impact on society.

The empirical literature suggests that Islamic finance holds considerable promise for rural areas, with various facets contributing to its potential impact:

### 2.1 Islamic microfinance and *Qard al-Hassan*

Islamic microfinance, particularly the concept of *Qard al-Hassan*, emerges as a potent tool for addressing poverty and enhancing financial inclusion in rural areas. This benevolent lending mechanism, underscored by the International Fund for Agricultural Development (IFAD) and supported by empirical studies, holds significant promise for improving the economic well-being of rural communities.

Drawing from a body of research, including studies by Mojtahed & Hassanzadeh (2009), Iqbal & Shafiq (2015), Jamal & Sheikh (2013), and Firmansyah (2016), *Qard al-Hassan's* potential impact is multifaceted. Mojtahed & Hassanzadeh (2009) study in Iran highlights the positive effects of interest-free loans, including *Qard al-Hassan*, on poverty elimination and per-capita income. Iqbal & Shafiq (2015) case study of *Akhuwat* showcases how *Qard al-Hassan* reinforces social unity and cooperation within communities. Jamal & Sheikh (2013) endorsement of the Islamic microfinance model in rural Pakistan emphasises its comprehensive approach, including regulatory frameworks. Furthermore, Firmansyah (2016) evaluation in Indonesia reveals that government-owned banks play a significant role in distributing *Qard al-Hassan* to the disadvantaged and microbusinesses.

Collectively, these findings affirm the potential of *Qard al-Hassan* as a powerful instrument within the realm of Islamic microfinance. Its capacity to alleviate poverty, foster social cohesion, promote entrepreneurship, and support rural development underscores its significance in advancing financial inclusion and shared prosperity in rural areas.

### 2.2 Islamic banking and rural economic development

Studies collectively demonstrate that Islamic banking can play a constructive role in rural economic development. Fakhrunnas (2020) underscores the importance of factors like inflation and economic growth in shaping the financing activities of Islamic rural banks. Maintaining a stable inflation rate is recommended to support these banks and promote the overall financial industry. In Pakistan, Kalim et al. (2016) identifies a supply-side relationship between Islamic finance development and economic growth, suggesting that Islamic banking can stimulate economic progress in rural areas. Additionally, Dahduli (2009) emphasises the theoretical effectiveness of Islamic banking concepts in directing funds towards profitable industries and accelerating economic growth.

### 2.3 Islamic fintech for rural penetration

Islamic fintech is identified as a transformative force for rural areas. Khudhori, & Hendri (2021) advocate for collaboration between fintech firms and Islamic banks to enhance efficiency and customer outreach. Ahmed et al. (2019) highlight the positive relationship between Shariah-compliant fintech models and Islamic banking, reinforcing the potential synergy between innovative fintech solutions and established Islamic banking practices. Hidajat (2020) explores the transformative impact of fintech in the Islamic finance sector, especially through mobile payments, microfinance, and crowdfunding. Subagiyo (2019) points out the extensive opportunities for Shariah-compliant fintech to address unmet financial needs in rural communities, potentially revolutionising the Islamic banking sector.

This paper embarks on a multifaceted exploration, weaving together the Resource-Based View (RBV) theory and the innovative Islamic finance product, *al-Mubadarat al-Riyfiah*, to address the pressing

challenges of financial inclusion and shared prosperity in underserved segments of society and the third sector of the economy. By adapting the RBV theory to elucidate how *al-Mubadarat al-Riyfiah* serves as a strategic resource for Islamic banks, the paper aims to contribute a novel perspective to the discourse on Islamic finance. Furthermore, the synthesis of empirical literature showcases the multifaceted potential of Islamic finance, spanning Islamic microfinance, banking, and fintech, as potent drivers of economic development and financial inclusion. Through this, the study seeks not only to provide insights into the theoretical underpinnings of the proposed model but also to expand the discourse surrounding Islamic finance's transformative capacity. In doing so, the paper aims to contribute to the existing literature by offering a holistic view of Islamic finance's role in fostering economic growth, social cohesion, and financial access in underserved and rural areas, thereby amplifying its potential as a catalyst for inclusive and sustainable development.

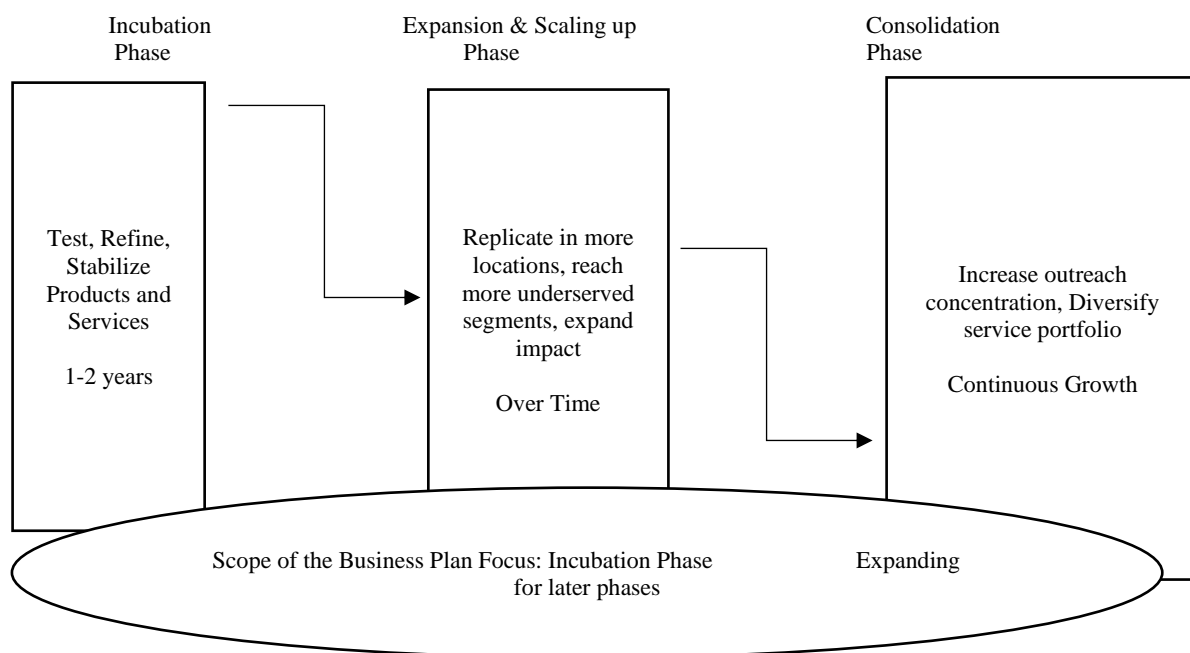
### 3. Phases of development, scope of the business plan, and branding

The proposed *al-Mubadarat al-Riyfiah* model will undergo three distinct phases of development, as outlined below:

- i. Incubation phase: During this initial phase, the initiative will be piloted in up to three locations for a period of 1-2 years, starting in 2024. Interested Islamic banks can participate in this phase, which will primarily focus on testing, refining, and stabilising the products and services. It will also assess the application of the business plan targets and breakeven plans, ensuring their feasibility and effectiveness.
- ii. Expansion and scaling up phase: The second phase will involve replicating the implementation units across a larger geographical area, with the objective of reaching a significant portion of the underserved segment of the economy over time. This phase aims to expand the initiative's coverage and impact, extending its reach to more communities and individuals in need of financial services.
- iii. Consolidation phase: The third phase will concentrate on increasing outreach concentration within the areas served by the units. It will involve diversifying the range of services offered to encompass various rural initiatives under the umbrella of the *al-Mubadarat al-Riyfiah* initiative. By consolidating its presence and expanding its service portfolio, the model can provide a comprehensive suite of financial solutions tailored to the specific needs of the underserved segment.
- iv. Scope of the business plan: This particular business plan focuses on the details of the incubation phase. However, as the initiative progresses, the plan will be further developed to encompass the broader scope of the expansion and consolidation phases, incorporating strategic considerations and operational guidelines for each stage of development.
- v. Branding: The initiative will be officially referred to as This distinct branding will help create awareness, build recognition, and establish a unique identity for the initiative within the Islamic finance sector and the communities it aims to serve.

### 3.1 Empirical illustration

Figure 1: *Al-Mubadarat Al-Riyfiah* Phases of Development



Source: Author's illustration.

Figure 1 illustrates the three phases of development: Incubation, Expansion & Scaling up, and Consolidation, along with the scope of the business plan, which initially focuses on the incubation phase and later expands to cover the broader scope of the subsequent phases. The distinct branding, *al-Mubadarat al-Riyfiah*, is highlighted as a unique identity within the Islamic finance sector and the target communities.

## 4. Strategic plan

### 4.1 Strategic plan

The primary aim of *al-Mubadarat al-Riyfiah* is to ensure the availability of sustainable finance services to households in the underserved segments of the rural market. The target market consists of individuals with financial needs ranging from RM 500 to RM 1,000 (approximately US\$125 - 250). Over a 10-year period, the initiative aims to reach approximately 40 million households within this market segment worldwide. The achievement of these aims will be facilitated through a phased implementation process that includes the incubation phase, expansion or scaling-up phases, and consolidation phase.

### 4.2 The objectives of the incubation phase

- i. Demonstrate the success of the *al-Mubadarat al-Riyfiah* model in terms of delinquency control, high levels of efficiency, and sustainability. This will establish the initiative as a viable option

for offering scalable and sustainable financial services to households in the bottom layers of the economy.

- ii. Foster partnerships between Islamic banks and various stakeholders to ensure the effective implementation of This involves developing a collaboration framework that promotes engagement and cooperation among key stakeholders. These partnerships will contribute to the success of the initiative and support its future expansion and scaling up.
- iii. Based on the implementation experience during the incubation phase, develop a framework for the subsequent expansion and scaling-up phase. This framework will provide guidance and strategies for the effective spread of *al-Mubadarat al-Riyfiah* to other regions and parts of the world, ensuring its impact and sustainability on a broader scale.

By achieving these objectives during the incubation phase, *al-Mubadarat al-Riyfiah* will lay a solid foundation for its future growth and expansion, leading to greater financial inclusion and empowerment of underserved households.

## 5. Target group

During the incubation phase, *al-Mubadarat al-Riyfiah* will primarily target poor households situated in the bottom layers of rural communities. The model will specifically focus on this target group, which typically requires loans ranging from RM500 to RM1000 (approximately US\$125). Initially, *al-Mubadarat al-Riyfiah* will provide financial services to households with loan requirements within this range, gradually expanding its coverage to encompass a broader spectrum of households with loan requirements up to RM10000.

The initial focus will be on households that aspire to initiate or expand small enterprise activities but face challenges in accessing interest-free sources of finance. *Al-Mubadarat al-Riyfiah* aims to provide financial support to these households, enabling them to realise their entrepreneurial aspirations. Additionally, the initiative will prioritise households that are open to accepting relatively smaller loan amounts initially and gradually accessing larger amounts as they progress. In line with an inclusive approach, a women-focused approach will be adopted by All financial transactions will be conducted through women's groups established in each village, adhering to specific criteria for linking to the model. This approach aims to empower women and promote their financial inclusion, recognizing their pivotal role in the development of rural economies and communities. By targeting these underserved households and adopting a women-focused approach, *al-Mubadarat al-Riyfiah* seeks to address the financial needs and aspirations of the rural population, contributing to their socio-economic upliftment.

## 6. Services and products strategy

In its initial phase, *al-Mubadarat al-Riyfiah* will primarily focus on providing savings and lending services to its target group. Recognising the importance of building financial resilience and promoting savings habits, the initiative will prioritise the establishment of regular savings accounts for its clients. This approach will encourage financial discipline among member households and create a common interest within the group, fostering a sense of community and providing a financial cushion for unforeseen emergencies.

Alongside savings services, *al-Mubadarat al-Riyfiah* will offer lending facilities to meet the diverse financing needs of its clients. The entry-level loan sizes will be set at a modest level to ensure access to finance for households in the bottom layers of the economy. This approach aims to maximize the effectiveness of group collateral as the principal guaranteed mechanism, facilitate successful loan

utilization, and cultivate positive lending history and repayment habits among clients. *Al-Mubadarat al-Riyfīa* will prioritize financing microenterprise activities with short gestation periods, generating regular cash flows for repayment. This emphasis on income-generating activities will contribute to sustainable lending performance and promote economic growth at the grassroots level. Initially, the focus will be on financing small-scale agricultural and non-agricultural enterprises that align with the target group's capacities and aspirations.

As *al-Mubadarat al-Riyfīa* progresses, the possibility of collaborating with insurance services will be explored. This strategic partnership would enhance the financial resilience of the target group, providing them with protection against unforeseen events and risks that could disrupt their livelihoods. By offering comprehensive savings and lending services, and potentially incorporating insurance services, *al-Mubadarat al-Riyfīa* aims to provide a holistic financial solution that empowers the underserved population, supports their entrepreneurial endeavors, and safeguards their financial well-being.

### 6.1 Savings

*Al-Mubadarat al-Riyfīa* will adopt a savings-led approach, recognizing the importance of cultivating a culture of saving among its clients. The relationship between the clients and *al-Mubadarat al-Riyfīa* will begin with regular monthly savings by the clients, contributing a specific amount determined by their financial capacities. This approach aims to instil financial discipline and promote savings habits among member households.

Regular monthly savings will serve as a significant common interest within the group, fostering a sense of collective responsibility and shared goals. Over time, these accumulated savings will create a financial cushion that can be accessed during times of emergency or to seize opportunities for business expansion. This practice encourages resilience and provides a safety net for the participating households. By prioritizing savings as an integral part of its financial services, *al-Mubadarat al-Riyfīa* seeks to empower its clients with greater financial security, stability, and the means to overcome unforeseen challenges.

### 6.2 Lending

To effectively reach the bottom layers of the economy, *al-Mubadarat al-Riyfīa* will initially offer small entry-level loan sizes. This approach ensures several key benefits:

- i. Greater effectiveness of group collateral: By providing smaller loan sizes, the reliance on group collateral as the principal guarantee mechanism is strengthened. This fosters a sense of collective responsibility among group members and enhances the likelihood of successful loan repayment.
- ii. Stronger impact of limited loan sizes: The smaller loan sizes have a more significant impact at the bottom layers of the economy, where financial resources are scarce. By addressing the specific financial needs of this target group, *al-Mubadarat al-Riyfīa* can make a meaningful difference in improving their economic conditions.
- iii. Successful loan utilisation and progress: The smaller loan sizes promote successful utilisation of funds by focusing on short-term microenterprise activities that generate regular cash flows. This ensures that clients can effectively utilise the funds for income-generating ventures and make timely repayments. Additionally, this approach facilitates the progression to the next loan cycle, allowing clients to access higher loan amounts based on their demonstrated repayment capacity.
- iv. Development of repayment habits and lending history: By starting with small loan sizes and shorter loan durations of 6 to 8 months, *al-Mubadarat al-Riyfīa* encourages clients to develop regular repayment habits and establish a positive lending history. This lays the

foundation for their future access to higher loan amounts and more extensive financing options.

During the initial stages, *al-Mubadarat al-Riyfiah* will minimize lending for crop production and livestock activities. Instead, these expenses will be covered, at least in part, through regular repayments from other household cash flows. After demonstrating consistent performance over 2 to 3 loan cycles, the possibility of expanding lending for crop production and livestock activities will be explored. By adopting this approach, *al-Mubadarat al-Riyfiah* aims to support sustainable microenterprises, promote regular cash flows, and empower clients to improve their economic well-being.

## 7. Delivery strategy

To ensure effective and efficient delivery of services, *al-Mubadarat al-Riyfiah* will adopt a group-based methodology. The following key elements will be incorporated into the delivery strategy:

- i. Group development: *al-Mubadarat al-Riyfiah* will exercise control over the group development process to ensure that it meets the necessary specifications for generating solidarity and peer pressure among group members. This approach helps establish an enforceable group collateral mechanism, enhancing the repayment commitment and accountability of the members. The groups will consist of relatively small-sized women's groups, which will serve as delivery points for savings and loan services.
- ii. Household economy as the unit of lending: *al-Mubadarat al-Riyfiah* will consider the household economy as the unit of lending. This means that the overall cash flows to the household from various sources, including the financed activities, will be assessed to determine the loan absorption capacity. Each member within the group will represent a single household, ensuring a comprehensive evaluation of the household's financial capabilities. Additionally, each group member will be financed separately for their specific activities, promoting loan diversification, reducing risk, and enhancing lending performance.
- iii. Field-based lending officers: *al-Mubadarat al-Riyfiah* will employ field-based lending officers who will be responsible for the doorstep delivery of services. These officers will play a crucial role in the entire service cycle, starting from group formation, loan origination, appraisal, collection of repayments, and savings. The doorstep service delivery approach aims to develop a close relationship between *al-Mubadarat al-Riyfiah* and its clients, fostering trust and regular engagement. Furthermore, it ensures consistent and effective monitoring of the clients' activities, facilitates early detection and resolution of issues, and contributes to enhanced lending performance.

By implementing this delivery strategy, *al-Mubadarat al-Riyfiah* aims to promote financial inclusion, build strong community networks, and provide personalised and accessible financial services to the underserved segments of the rural economy.

## 8. Sustainability strategy

To ensure long-term sustainability, *al-Mubadarat al-Riyfiah* will implement a comprehensive strategy focused on cost control and revenue optimization. The following key elements will be central to the sustainability strategy:



- i. **Cost Control:** *al-Mubadarat al-Riyfiah* will prioritise increased efficiency and streamlined operations to control costs effectively. This includes implementing measures to enhance operational processes, eliminate redundancies, and optimise resource allocation. By continuously monitoring and evaluating internal operations, the initiative will identify areas for improvement and implement cost-saving measures while maintaining service quality.
- ii. **Revenue Optimisation:** The sustainability strategy will also prioritise revenue optimisation to support the financial viability of This will involve expanding outreach to reach a larger customer base, particularly within the underserved segments of the rural market. By increasing the number of clients served, the initiative can generate a broader revenue base. Additionally, effective measures will be put in place to control delinquency and prevent defaults, ensuring a healthy loan portfolio and maximising revenue generation.

By striking a balance between cost control and revenue optimisation, *al-Mubadarat al-Riyfiah* aims to achieve financial sustainability while continuing to provide affordable and accessible financial services to the target market.

### 8.1 Lending

During the incubation phase, *al-Mubadarat al-Riyfiah* will employ a breakeven approach to stabilize the methodology and gradually achieve financial self-sufficiency. As this phase focuses on piloting the initiative with a limited number of communities and groups, the revenue levels may be restricted, particularly in the first year.

At the initial stage, the staff will be newly recruited, and their capacity and efficiency levels may be relatively low. However, there will be significant upfront investments in physical and human resources, training, and capacity building activities, resulting in high fixed and variable operational costs. Therefore, it is anticipated that the model will generate losses during the first 1-2 years. As the initiative progresses, staff efficiency will increase, and outreach will expand, leading to higher revenue growth. With a gradual increase in the revenue generation rate outpacing the costs, *al-Mubadarat al-Riyfiah* aims to reach the breakeven point between years 2 and 3 of the incubation phase. By implementing efficient operational processes, optimizing resource allocation, and continuously improving the delivery of services, *al-Mubadarat al-Riyfiah* will strive to achieve financial sustainability and gradually transition from a phase of initial investment to a self-sustaining model.

### 8.2 Key efficiency enhancement measures

To improve efficiency, *al-Mubadarat al-Riyfiah* will implement various measures aimed at optimizing operations and resource utilization. These measures include:

- i. **Streamlined Transportation System:** *al-Mubadarat al-Riyfiah* will establish a well-organised transportation system, utilising vehicles and motorbikes, to ensure the efficient deployment of lending officers at the community level. This streamlined transportation system will enable timely and effective delivery of services to clients, minimising delays and improving overall operational efficiency.
- ii. **Performance-Based Incentive Systems:** The organisation will introduce performance-based incentive systems to incentivise and reward higher staff efficiency. These systems will recognise and appreciate the efforts and achievements of lending officers and other

staff members who consistently demonstrate exceptional performance. By aligning incentives with performance, *al-Mubadarat al-Riyfiah* aims to foster a culture of excellence and encourage continuous improvement.

- iii. Culture of Cost Consciousness: *al-Mubadarat al-Riyfiah* will promote a culture of cost consciousness throughout the organisation. This involves developing awareness among staff members about the importance of managing operational costs efficiently. By instilling a mindset of cost consciousness, the organisation aims to ensure that resources are utilized judiciously, unnecessary expenses are minimised, and overall operational costs are effectively controlled.

Through the implementation of these efficiency enhancement measures, *al-Mubadarat al-Riyfiah* aims to optimise its operations, improve service delivery, and achieve cost-effective utilisation of resources.

### 8.3 Delinquency and default control

To effectively manage delinquency and prevent defaults, *al-Mubadarat al-Riyfiah* will implement a range of control measures and strategies. These measures are designed to minimise the risk of non-repayment and ensure the sustainability of the lending program. They include:

- i. Small-sized micro enterprise loans: *al-Mubadarat al-Riyfiah* will initiate the disbursement process with relatively small-sized loans that are specifically tailored to support regular cash flow-based activities. By focusing on micro-enterprises and their cash flow generation capabilities, the risk of default is reduced, as these businesses are more likely to have consistent income streams.
- ii. Development of strong women's groups: The group development process will be carefully controlled to establish strong women's groups that fulfil the necessary conditions for an effective mutual guaranteed system. These groups will provide support and accountability, enabling members to collectively guarantee each other's loans. This group-based approach enhances the likelihood of loan repayments and reduces the risk of non-repayment.
- iii. Gradual loan size increase: Initially, individual loans will be provided to group members to diversify the risk associated with business failure. As clients demonstrate their repayment capability and their absorption capacity increases, loan sizes will be gradually increased through progressive loan cycles. This step-by-step approach ensures that clients are provided with loans commensurate with their ability to repay, minimising the risk of default.
- iv. Cash flow-based loan appraisal system: *al-Mubadarat al-Riyfiah* will adopt a cash flow-based loan appraisal system to assess the repayment capacity of borrowers. This approach focuses on the evaluation of the borrower's cash flow generation ability rather than traditional collateral-based assessments. By considering the borrower's actual cash flow, the loan appraisal process becomes more aligned with the borrower's ability to repay the loan.
- v. Regular repayments and close monitoring: The organisation will emphasize the importance of regular repayments at short intervals, encouraging borrowers to make timely payments. A close monitoring and supervision system will be implemented to ensure that repayment schedules are adhered to and any potential issues are identified

and addressed promptly. This proactive monitoring helps to mitigate the risk of delinquency and default.

By implementing these delinquency and default control measures, *al-Mubadarat al-Riyfiah* aims to foster a culture of responsible borrowing, minimise the risk of non-repayment, and maintain a sustainable lending program.

## 9. Financing strategy

*Al-Mubadarat al-Riyfiah* will employ a comprehensive financing strategy that combines internal financing generated through the implementation of the model with external financing sources. This multi-faceted approach ensures the availability of sufficient funds to support the operations and growth of the initiative. The financing strategy includes the following components:

- i. Internal financing: Internal financing will be generated from various sources within These sources include revenue from profits generated by the initiative, application fees charged to clients, processing charges for loan services, and other income streams. Additionally, repayments collected from clients will be an important source of internal financing, as these funds can be reinvested into the program to support its sustainability and expansion.
- ii. External financing: *al-Mubadarat al-Riyfiah* will also seek external financing to supplement its internal funds. External financing sources can include portfolio funding from investors interested in supporting microfinance initiatives, grants or loans from development organisations or impact investors, and philanthropic contributions. These external funds will help bridge any gaps in operational costs, support fixed asset investments, and provide resources for technical assistance, capacity building training, and exposure trips.

By leveraging a combination of internal and external financing, *al-Mubadarat al-Riyfiah* aims to ensure a stable and adequate funding base to sustain its operations, scale up its activities, and fulfill its mission of providing financial services to underserved households in rural communities.

## 10. Institutional form and implementation approach

The implementation of *al-Mubadarat al-Riyfiah* will be carried out separately from the current direct lending portfolio of Islamic Banks. It will be structured as independent units, referred to as "Units", which will operate in physical locations separate from the existing branches of Islamic Banks. This separation ensures that the implementation of *al-Mubadarat al-Riyfiah* is not constrained by the existing systems and organisational structure of the direct lending portfolio. These Units will have their own dedicated full-time staff members and will adopt a distinct product and delivery methodology tailored to meet the specific requirements of serving the underserved segments at the bottom layers of the economy.

Initially, *al-Mubadarat al-Riyfiah* will be piloted in selected locations, and once the pilot phase proves successful, the participating Islamic Banks will scale up the initiative as a separate business arm. There is also the possibility of spinning off *al-Mubadarat al-Riyfiah* into a wholly or partly owned subsidiary dedicated to providing financial services to the rural areas' underserved segments. This approach allows for greater flexibility and focused attention on addressing the unique needs and challenges of the target population. *Al-Mubadarat al-Riyfiah* recognizes the importance of technological interventions in enhancing efficiency, reducing costs, and expanding services. While the initial focus will be on developing strong personal banking relationships through face-to-face interactions between clients and loan officers, the initiative will adopt relevant technological solutions to further improve its operations. This may include the introduction of mobile phone technology for facilitating cash transactions, as well as exploring innovative

services such as micro-remittances. Additionally, a robust Management Information System will be established to ensure efficient recording and reporting systems, contributing to organizational efficiency and informed decision-making. By implementing *al-Mubadarat al-Riyfiah* as separate Units and embracing technological advancements, the initiative aims to establish a sustainable and effective framework for providing financial services to the underserved rural communities, ultimately promoting economic empowerment and inclusive growth.

## 11. Pre-requisites for success

To ensure the successful implementation of *al-Mubadarat al-Riyfiah*, certain prerequisites need to be followed:

- i. Low key media and publicity. During the incubation phase, it is important to keep media and publicity activities low-key. This approach helps prevent undue external pressure and varying expectations during the testing and establishment stages. By avoiding excessive media attention, the focus can remain on refining the model and achieving tangible results. Once the model has stabilised and results are visible, appropriate media events can be organised to showcase the success and impact of *al-Mubadarat al-Riyfiah*.
- ii. Selection of suitable unit managers. The selection of capable and suitable Unit Managers is crucial for the success of *al-Mubadarat al-Riyfiah*. Ideally, Unit Managers should be chosen internally from the respective Islamic Banks. It is important to identify promising officers or managers who have demonstrated past performance and possess the necessary skills and competencies. The selection process should view the role of *al-Mubadarat al-Riyfiah* Unit Manager as an incentive for career growth. While failure may have setbacks, success in this role should lead to fast-track advancement in their careers. This approach ensures that motivated and qualified individuals are entrusted with the responsibility of managing and driving the success of *al-Mubadarat al-Riyfiah* Units.

By adhering to these prerequisites, *al-Mubadarat al-Riyfiah* can effectively navigate the implementation phase, maintain focus on its objectives, and establish a solid foundation for its long-term success.

## 12. Conclusion

*Al-Mubadarat al-Riyfiah* stands as a profound and innovative response to the pressing challenges within Islamic finance. Its core mission, centered on promoting shared prosperity, aligns seamlessly with the evolving needs of underserved segments and the third sector of the economy. By providing sustainable financial services to the most vulnerable households in rural areas, this initiative charts a path towards greater economic inclusivity. The phased implementation strategy, commencing with the incubation phase and culminating in expansion and consolidation, signifies a ten-year journey to reach approximately 40 million households globally. With a keen focus on savings and lending services, supplemented by potential collaborations with insurance providers, *al-Mubadarat al-Riyfiah* aspires to empower individuals and unlock the potential of small-scale enterprises that were previously stifled by the presence of interest-based finance. Central to its success is the adoption of a group-based methodology, with a particular emphasis on women's groups as conduits for delivering these financial services. This approach recognizes the household as the primary unit for lending, supported by field-based lending officers who provide doorstep services. It ensures not only the effectiveness of monitoring but also the timely resolution of any potential issues, contributing to sustainable financial relationships.

Furthermore, the initiative's commitment to sustainability is evident through measures aimed at cost control, heightened efficiency, and revenue optimization. Streamlined transportation, performance-driven

incentives, and a culture of cost consciousness all play vital roles in ensuring the financial viability of this endeavor. Delinquency and default control mechanisms, including the issuance of small-sized loans, the formation of resilient women's groups, and cash flow-based appraisals, provide additional layers of support to ensure the long-term success of *al-Mubadarat al-Riyfiah*. The financial backing for this ambitious project will derive from both internal and external sources. Internal financing generated through revenue, application fees, and client repayments will be complemented by external funding to support portfolio growth, operational expenses, and capacity building. The institutional autonomy of *al-Mubadarat al-Riyfiah*, distinct from the existing direct lending portfolio of Islamic Banks, safeguards its independence and efficient management. Furthermore, the gradual integration of technological interventions and the establishment of a robust Management Information System will elevate operational efficiency, further catalyzing the initiative's growth trajectory. Critical to the success of *al-Mubadarat al-Riyfiah* during its incubation phase is the strategic decision to maintain a low-key media and publicity profile. This approach allows for thorough testing and establishment without undue external pressures. Additionally, the careful selection of Unit Managers, incentivized by their past performance and recognizing their pivotal role in their career growth, stands as a cornerstone for the triumph of this transformative initiative.

Ultimately, *al-Mubadarat al-Riyfiah's* vision extends far beyond its immediate operational boundaries. It aspires to contribute significantly to the welfare of the 700 million individuals grappling with poverty across the Muslim world. By offering interest-free financial services, it seeks to advance financial inclusion and elevate the living standards of those who have long been underserved. Through a meticulously devised strategic plan, an innovative delivery approach, and an unwavering commitment to sustainability, *al-Mubadarat al-Riyfiah* has the potential to catalyze positive economic and social transformations, touching the lives of millions of households worldwide. Its contribution to Islamic finance literature, along with its resonance with the policies of Malaysia and beyond, heralds a new era of inclusive financial practices and shared prosperity.

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### **Conflict of interest statement**

The authors agree that this research was conducted in the absence of any self-benefits, commercial or financial conflicts and declare the absence of conflicting interests.

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### **Authors' contributions**

Adamu Ahmed Wudil wrote the original draft and revised the article. Rislanudeed Muhammad conceptualized the central idea and provided the theoretical framework. Rislanudeed Muhammad Visualization the revised version before the final submission.



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