

BAITUL MAL WAT TAMWIL (BMT) AND POVERTY EMPOWERMENT

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ABSTRACT

The aim of the study was to examine the role of Baitul Mal Wat Tamwil (BMT) on poverty empowerment in Demak, Central Java, Indonesia. The poverty empowerment was measured by increase of income levels, family education, health care, and business progress. This study used the sample of one hundred borrowers from 13 BMT were taken into consideration and questionnaires were distributed among them using purposive sampling method. Out of 100 questionnaires distributed, the researchers received back 74 responses. The empirical tests indicated that BMT has a significant role on improving income level, family education, and business progress. However, the study did not find any significant role of Islamic microfinance on access to health care. Implication, limitation and suggestion for future research are discussed.

Keywords: *Islamic microfinance, poverty, income levels, children's education, health care, and business progress*

INTRODUCTION

Microfinance has been gaining popularity for the last few decades, especially after the experience of the Grameen Bank in Bangladesh. The microfinance industry stands at a crossroads between increased commercialization and increased philanthropic aid (Emily, 2005 in Shirazi and Khan, 2009). Microfinance refers to small-scale financial services primarily credit and

savings provided to small enterprises or micro enterprises. However, The field of microfinance has broaden greatly beyond credit only, to include micro-savings, micro insurance, remittances and other payments all of which have a great impact on the lives of the poor.

Poverty has been a major development problem of Indonesia. According Indonesian Statistical biro (2012) around 29 million people are living in poor condition. Poor people not only have low income but also lack access to basic needs such as education, health care, clean drinking water and proper sanitation. The most important constraint that poor people face to come out of poverty is lack of access to credit to run their own businesses due to the several reasons. First, formal financial institutions require collateral. Second, they prefer for high-income clients with large loans. Third, the bureaucratic processes and procedures in providing loan. Finally, the loan for the poor is not attractive and unprofitable (Gebru and Paul, 2011). So, microfinance became a solution for these problems.

Several studies indicate that microfinance has positive impacts in reducing poverty (e.g. Gebru and Paul, 2011; Shirazi and Khan, 2009; Kessy and Urion, 2006; Durrani, Usman, Malik, and Ahmad, 2011). Moreover, conventional microfinance products have been successful in Muslim majority countries such as Indonesia, Bangladesh, Pakistan, Turkey and etc. However, these products do not fulfil the needs of all Muslim clients. Combining the Islamic social principle of caring for the less fortunate with microfinance's power to provide financial access to the poor especially for those whom think that interest is prohibition in Islam (Dasuki, 2006). The prohibition of interest in Islam provides the microfinance industry create an opportunity to offer financial services to the poor mainly through a new emphasis on profit-generating activities in Islamic microfinance (Shirazi and Khan, 2009).

Despite the call for Islamic microfinance, there has been very little academic research on the topic. There have been even fewer attempts to investigate the implementation of Islamic microfinance to poverty especially Indonesia. Therefore, the goal of this study is to examine the role of BMT to poverty empowerment in Indonesia.

LITERATURE REVIEW

***Baitul Mal Wat Tamwil* (BMT)**

Baitul Mal Wat Tamwil (BMT) is one of the Islamic microfinance institutions (IMFIs) model in Indonesia, beside Bank Perkreditan Rakyat (BPRS/ syariah rural bank. BMTs are important new sources for the establishment of micro

institutions and while gaining support from the Islamic community; they have also rapidly spread the establishment of microfinance institutions in Indonesia. Obviously, there are some Muslims in Indonesia who would never use the conventional banking services. This is because these MSMEs use interest that is not in accordance with the Islamic value. Therefore, the establishment of BMT becomes one of the alternative ways to solve the problem of lack of capital (Widiyanto, 2007). BMTs are a grass-root development supported by funds from the Islamic community members. These micro-finance institutions usually operate on the principle of profit-loss sharing and use the Islamic moral values and group solidarity as social capital to encourage repayment of loans (Sakai and Marijan, 2008). Group solidarity has been fostered through regular meetings and counseling. Hence, this study will focus on the BMTs, which have a large numbers that can produce a big impact on the practice of the Islamic microfinance in Central Java. Currently, BMTs are an important part of the micro-enterprises development in Central Java. Thus, in this study, the term BMTs and IMFIs are interchangeably used.

The word Baitul Mal Wat Tamwil (BMT) comes from the two terms, i.e., *baitul mal* and *baitul tamwil* (Azis, 2008). As such, a more specific definition can be derived as follows:

1. *Baitul mal* means the house of wealth which refers to the social mission of BMT as an institution that distributes the donation of *zakat*, *infaq*, and *shadaqah* to the persons who are eligible to receive (*Mustahiq*).
2. *Baitul tamwil* means the house of wealth development, which is the business mission of BMT. It is meant to conduct business development efforts and investments in productive economy in order to improve the quality of micro and small entrepreneurs, especially, by encouraging saving activities and supporting the financing of economic activities.

BMTs operate under cooperative principles, which are regulated under the cooperative law of Act No. 25/1992. They are registered with the ministry of cooperatives, small and medium enterprises, but not all BMTs operate as legal entities. The establishment of BMT has to be attested by a notary and BMT statutes are standardized that include subjects, such as, identity, area of operation, objectives, and transaction under profit-loss sharing principle and using the Islamic moral values as guidance in the transactions (Sakai and Marijan, 2008).

This is in the form of profit and loss sharing and no-profit loss sharing system (trade financing). The profit and loss sharing system embraces: trustee financing (*mudharabah*) and partnership financing (*musyarakah*) while the

trade financing system includes: markup financing (*murabahah*), deferred payment sale financing (*bai' u bithaman ajil*), leasing (*ijarah*) and benevolent loans (*qard al hasan*) (Seibel and Agung, 2008; Sakai and Marijan, 2008).

As a viable financial institution, BMT is offering products and services similar to the Islamic banks and syari'ah rural banks (BPRS). However, it has a different market sector in terms of patronage, where the Islamic banks mainly cater for the middle class and the white collar Muslims. BPRS on the other hand mainly provides services for Muslims from the middle and the lower income groups. While BMT usually serves the Muslim customers who run small and medium enterprises and whose access to the banks is relatively limited, some customer overlapping occurs among the Islamic bank, BPRS and BMT (Sakai and Marijan, 2008). According to Yumna and Clarke (2012), the main features of BMT are:

1. Providing adequate services for the extremely poor clients and lift some of them to the economically active poor clients.
2. It is possible to create a sustainable microfinance since it does not only depend on the donor fund to provide the microfinance.
3. It increases the accountability of the both institutions since they need to report to zakat and islamic charities payers and its potential payers, shari'ah compliance finance as well as the microfinance institution supervisory board.
4. It will create sustainable microfinance with lower default rate and reduce the possibility of misuse of the loans since the microcredit is only for the skilled people who conduct some income generating activities.
5. It will reduce the agency problems since both institution engage in the same value and objectives.

BMT and Poverty Empowerment

Microfinance like BMT can be a critical element of an affective poverty reduction strategy especially for developing countries. To redress the issue, the policy of increasing access to both production and consumption credit by the poor has been articulated. The services provided by microfinance institutions can enable the poor to smoothen their consumption, manage their risks better, build their assets gradually, develop their micro enterprises, enhance their income earning capacities, and enjoy an improves quality life of poor people (Kessy and Urion, 2006; Gebru And Paul, 2011).

Poverty is defined by several authors as it is the situation of having no

enough money to meet the basic need of human beings. Englama and Bamidele (1997) define poverty as a state where an individual is not able to cater adequately for his/her basic needs of food, clothing and shelter, meet social and economic obligations; lacks gainful employment, skills, assets and self-esteem; and has limited access to social and economic infrastructures (in Okpora, 2010).

Hassan (2010) notes that the Islamic approach to poverty alleviation ideally involves comprehensive approaches including (a) increasing income levels with pro-poor programs, (b) achieving an equitable distribution of income and (c) providing equal opportunities for all social segments. The most important constraint that poor people face to come out of poverty is lack of access to credit to run their own businesses. One of the identified key constraints facing the poor is lack of access to formal sector credit to enable them to take advantage of economic opportunities to increase their level of output, hence move out of poverty (Gebru and Paul, 2011).

The researchers have paid attention to microfinance as one of the contributors in reducing poverty through increased income and standard of living, empower women, develop the business sector through growth potentials, develop a parallel financial sector, improve quality of women's life empowerment, health care, education, democratization and environmental improvement (Kessy and Urion, 2006; Gebru and Paul, 2011; Okpora, 2010; Shirazi and Khan, 2009 and Durrani et al, 2011).

Studies have also been conducted to quantify the impact of microfinance on poverty alleviation. Hulme and Mosley (1996), for instance, based on the counterfactual combined approach, analyzed the impact of microfinance on poverty alleviation using sample data from Indonesia, India, Bangladesh and Sri Lanka. They found that growth of income of borrowers always exceeds that of control group and that increase in borrowers income was larger for better-off borrowers (in Shirazi and Khan, 2009).

Study conducted by Khandker (1998) in Bangladesh has focused on Grameen Bank, and Bangladesh Rural Advancement Committee (BRAC). He found that microcredit alleviated poverty up to 5 percent annually (in Shirazi and Khan, 2009). Moreover, Rena, Ravinder and Ghirmai (2006) found that microfinance is the founding stone for poverty reduction. They showed that there is a fundamental linkage between microfinance and poverty eradication (in Durrani et al, 2011).

Similar studies have also been done in other countries. Gurses (2009) conducted a study in Turkey and mentioned that microfinance especially

micro credit is a powerful tool to reduce poverty. In Pakistan, Shirazi and Khan (2009) examined the impact of micro credit on poverty alleviation. They divide poor into two categories: the poor and the extreme poor. They found that Micro credit had reduced the overall poverty level by 3.07 percentage points. The poverty status of the extremely poor borrowers has been marginally increased by 0.63 percentage point.

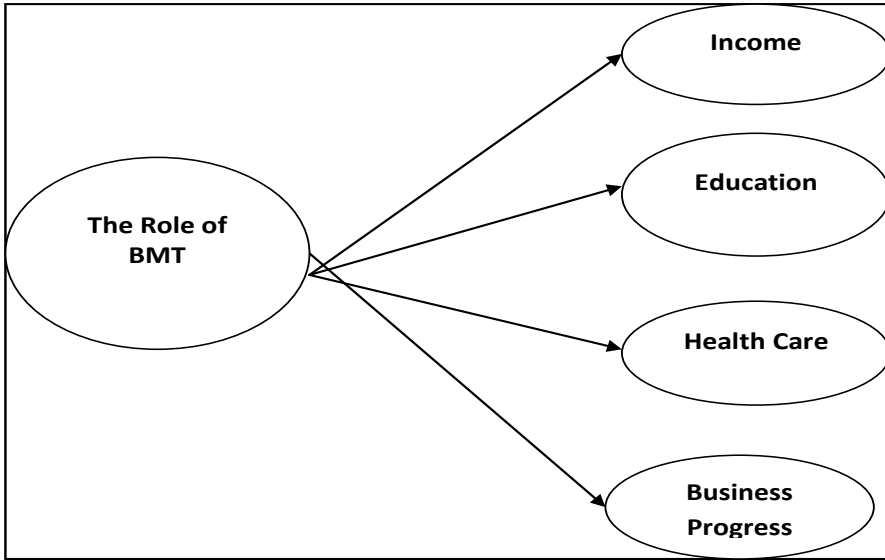
However, in Thailand, Coleman (1999) studied the role of Thailand village banks on poverty. He found no evidence of any impact of microfinance on poverty. Another study by Coleman (2004), found that programs are not reaching the poor as much as they reach relatively wealthy people (in Shirazi and Khan, 2009).

A similar study was also conducted on Islamic microfinance by Akhtar, Akhtar and Jafri (2009). They found that Islamic microfinance is one of effective way to fight poverty. The authors mentioned that in Muslim world, the conventional micro finance could not be fruitful because of the Islamic social principles. Most of the people prefer Islamic microfinance rather than the conventional microfinance (Durrani et al., 2011). Chowdhury and Bhuiya (2004) examined the impact of credit programme on the Bangladeshi borrowers under the BRAC projects and found positive impacts on human well-being, survival rate and schooling of children.

Based on the above discussion, the following hypotheses are discernable:

- H1. BMT has significant role on income improvement.
- H2. BMT has significant role on education.
- H3. BMT has significant role on health care.
- H4. BMT has significant role on business progress.

Figure: Research Model



RESEARCH METHOD

Sample

This study was conducted to examine the role of BMT on poverty empowerment. This study used the sample of *Baitul Mal Wat Tamwil* (BMT), as Islamic microfinance institution in Indonesia. A total of one hundred borrowers from 13 BMT in Demak regency, Central Java, Indonesia were taken into consideration. The questionnaires were distributed among the lower borrowers using purposive sampling method. Out of 100 distributed questionnaires, the researchers received back 74 responses. The questions relating to effect of Islamic microfinance on income, education, health care, and business progress were asked. Five options were given to the respondents for filling the questionnaire such as strongly agree, agree, neither agree nor disagree, disagree and strongly disagree. Table below shows the demographic characteristic of respondents:

Table I
The Characteristics of Respondents

Demographic Variables	Frequency	Percentage
Gender		
Male	39	51
Female	37	49
Total	76	100

Age		
20 - 30	38	50
31 - 40	22	29
41 – above	16	21
Total	76	100
Education Level		
No Education	18	23
Primary	24	32
Secondary	29	38
Post Secondary	5	7
Total	76	100
Profession		
Entrepreneur	40	53
Farmer	19	25
Worker	17	22
Total	76	100
Loan Amount (US \$)		
Less than 100	37	49
100 – 350	15	20
350– 500	24	31
Total	76	100
Time with Islamic Microfinance (year)		
1 – 2	16	21
2 – 5	42	55
More than 5	18	24
Total	76	100

From the above table, one can deduce that about fifty one percent (51%) of the respondent are male, thirty-eight respondents representing fifty percent (50%) are fall between the ages of 20-30 years. With regards to educational background as shown in table above, 23% had no formal education, 32% had up to primary level, and 38 % forming the larger group had up to secondary and the rest at post secondary. Also for occupation, the majority of respondents (53%) were entrepreneur, farmer forming the second largest group of 25%, and the rest were workers.

In term of loan, the study analyzed the loans granted to individuals on three different scales, less than 100 US \$ (around less than 1 million rupiah), 100 to 350 US \$ (between 1 to 3 million Rupiah), and 300 to 500 US \$. The Majority of loans granted, around 49% (49 respondents) are less than 100 US \$, which

implies that IMFIs, basically emphasize on micro-credit. Regarding time with Islamic microfinance, the majority of respondents (55%) were already with Islamic microfinance between 2 to 5 years.

Measurement

The questionnaire comprised of questions about background information such as gender, age, education, number of loans, income per month, and time with Islamic microfinance. Besides demographic information of the respondents 18 different questions were asked about the microfinance and its effects on reducing poverty. The items for the said scale are adapted from a number of relevant research studies (Durrani et al. 2011, Hassan, 2010; Shirazi and Khan, 2009; Ali, & Alam, 2010; Akhtar, Akhtar, & Jaffri, 2009).

Analysis

The data was analyzed using SPSS 15.0 software. The analysis included descriptive statistics such as frequencies and percentage to present the main characteristics of the sample. For testing the hypotheses, this research used simple regression analysis as the main method of analysis. Here, we examined the role of Islamic microfinance on income, education, health care and business progress one after the other.

RESULT

The following table II displays the mean, standard deviation, standard error mean and correlation for four variables: role of Islamic microfinance, education access, health care, income and business progress. All the variables show the satisfaction level to be more than 3. The correlations among the variables provided initial support for three proposed hypotheses, only health care was not significantly correlated with the role of Islamic microfinance.

Tabel II
Mean, Standard Deviation, and Correlation

No	Variable	Mean	S.D	1	2	3	4
1	Role of IMF	4.4	.38	1			
2	Education	4.5	.46	.366**	1		
3	Health Care	4.2	.37	.179	.259*	1	

4	Income	4.2	.39	.500**	.283*	.254*	1
5	Business Progress	4.2	.36	.473**	.239*	.245*	.520**

** . Correlation is significant at the 0.01 level (2-tailed).

* . Correlation is significant at the 0.05 level (2-tailed).

To address the purpose of the study, the proposed hypotheses were tested using regression analyses. The result of regression analyses are summarized in Table III below:

Table III
The result of regression analysis: Role of Islamic Microfinance of Poverty Alleviation variables

Variables	Independent Variable Role of Islamic Microfinance (IMF)		
	R ²	F change	B
Income	.250	24.70**	.500**
Education	.134	11.4**	0.366**
Health Care	.032	2.44	0.179
Business Progress	.223	21.29**	.473**

Note: * $p < 0.01$, ** $p < 0.05$

To test the first hypothesis, the study regressed role of Islamic microfinance and income. The relationship between role of Islamic microfinance and income is highly significant, as indicated in the table III ($R^2 = 0.25$, $p < 0.01$). The null hypothesis is therefore rejected. Role of Islamic microfinance scores explained about 25% of variance ($F = 24.70$, $p < 0.01$) in income. The second hypothesis was also supported, as indicated by $R^2 = 0.134$, $p < 0.01$ (see table III), therefore null hypothesis is rejected. The third hypothesis is not supported; the role of Islamic microfinance on health care is not significant. The null hypothesis is therefore accepted. For the last hypothesis, the study regressed role of Islamic microfinance and business progress. The result shows that Islamic microfinance has a significant role on business progress ($R^2 = 0.223$, $p < 0.01$). Therefore, the null hypothesis is rejected.

DISCUSSION, IMPLICATION AND LIMITATION

The results of the study demonstrated that role of BMT has strong

relationship with income, education, and business progress. However, role of BMT shows no significant effect on health care.

For the first, second and fourth hypothesis testing, the results indicate that the relationships between the Islamic microfinance to income, education and business progress are positive and significant. These are in line with the prior research (Shirazi and Khan, 2009; Durrani, et al. 2011; Gebru and Paul, 2011; Okpara, 2010; Kessy and Urio, 2006), which demonstrated the positive role of microfinance on to income, education and business progress. The result suggested that the Islamic microfinance plays important role on improving income of house hold, as well as improves access to children's education and also supports in improving business for poor people. The findings are in line with the previous studies conducted by Akhter, Akhtar, and Jaffri (2009). They found that interest free loans could be used as a powerful tool against poverty. The study, however, recommends that integrating Islamic Microfinance with NGOs, Zakah, Awqaf and Takaful, along with professional training and capacity building Institutions.

Interestingly, the third hypothesis, however, is not supported since the result of the study indicated that the role of Islamic microfinance on health care is not significant. This finding was supported by Tiruneh (2006) who reached similar finding. This result indicated that Islamic microfinance has no direct impact on health care. This situation could be attributed to one of these reasons: firstly, Central Java Authority gives insurance for the poor (Asuransi kesehatan Masyarakat Miskin/Poor Health Insurance), so, they do not need money to visit the doctor or hospital. Secondly, traditionally, the poor people do not go to hospital or doctor for the medical treatment rather they used alternative traditional medicine. Therefore, they do not need much money and that could be the reason why Islamic microfinance have no effect on poor health care in Central Java, Indonesia.

The finding of this study has some important implications. It offers some interesting guidelines for policy makers in Islamic microfinance. Firstly, Islamic microfinance has significant contribution on poverty alleviation especially its impact on income, education and business progress; so, Muslim society should support these institutions. Additionally, Indonesian government should support the Islamic microfinance by proving additional fund to expand the role of Islamic microfinance on poverty reduction. Finally, the government should provide training and development on Islamic microfinance. The ability of Islamic microfinance staffs to manage their organization will significantly improve the role of Islamic microfinance on poverty reduction.

Finally, the contribution of this study should be viewed in light of some limitations. First, the design for this study was cross-sectional, not longitudinal. Cross-sectional data are not adequate to make inferences of causality or reverse causality among the investigated variables. Thus, a longitudinal research design would provide additional and stronger support for the effects tested in this study. Second, the generalizability of the findings of the present study might be questionable due to the nature of the sample. Third, another shortcoming of this study is: the limited numbers of variables, therefore, the next study should incorporate some variables which measure poverty precisely.

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